

# Corporate management and the revolution of the Machiavelli-method

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*Until the 19. century the economy was built on the small and traditionally organized enterprises. In early of the 20. century gradually the companies become the most important factors of the economy). Based on the organizational and technological innovations the whole system of business – the ownership control and management of the organizations – fundamentally changed. From the 1930' the owners gradually withdraw from day to day activities of the business, and hand over the responsibilities of the corporate control to the management. However from the 1960' – as a result of the growing dissatisfaction with the performance of the management – the stockholders started a struggle for regain the power on the company. In the 1990' gradually formed the complex system of the corporate governance. It consists of the institutions of the shared power, balanced system of rights and responsibilities, and motivation simulating the owner's interest.*

*However the events of the 21. century – the collapses of the companies (ENRON, Parmalat) and the crise of the world economy – proved, that the well organized institutional check and balances, and existing system of ownership control necessary but not sufficient to guarantee the appropriate development of the companies. Moreover even the latest modifications in the company laws - SOX and the Say-on-Pay – aren't enough. The author analyse the problem why the institutional control is insufficient. The paper argue, that within the companies, as a result of the „natural” process of selection of management, a special type – so called High Mach – personality fill most of the posts of the managerial jobs. This type of the personality - from viewpoint of the management - is very efficient on the one side, however at the same time is very unstable. The control of this type of managers the companies needed – beside of the institutional control – a well organized motivational system, a well-considered decision-making process, socially responsible corporate culture, effective business ethics, and a selection process based on this conditions.*

*Keywords: corporate governance, market for corporate control, corporate disaster, „High Mach” personality, „High Narc” personality*

## 1. Introduction

Till the end of the 19<sup>th</sup> century the economy was built on small businesses that were tradition-based and tradition-oriented. At the beginning of the 20<sup>th</sup> century large companies gradually became dominant and the scientific analysis or the standardization of the production process started to begin. In these years standards of workshop oriented organizations (Taylor) are formed, just as well as the standards of professional organizations (M. Weber), standards of organizational management (Fayol) and also the standards of organizational forms and management (Sloan). Due to the adaptation of these innovations the capitalist economy and several companies started to develop dynamically. The average growth rate – despite the world crisis – exceeded that of each epoch of world history. The national income of those countries which were involved in world economics grew dynamically. Inequality of GDP/person, that can be experienced even today, mainly appeared in the 20<sup>th</sup> century and depends on different growth rate of the countries (Maddison 2008). Technical innovations changed the economy and the society fundamentally. More consecutive innovation waves went through the economy, creating life-cycles of new industries while leaving those of the old ones behind. The consumption compared to the previous centuries widened enormously.

This success was significantly due to the enterprises and their management. One sign of it is that the size of enterprises also grew. In view of the above effects – and about the presence of the intense competition – the practice of management became more and more important. The management’s job was to internally integrate the organization and provide the effective operation.

## **2. The evolution of the institution (-system) of corporate management**

During the 20<sup>th</sup> century, the management of business enterprises changed basically. In the early 20<sup>th</sup> century, the powerful owner-managers (now: Chief Executive Officers), who had huge ownership share(s), played the main role. However, in the first decades of 20<sup>th</sup> century the average size of the enterprises grew rapidly, while at the same time the complexity also grew. The companies satisfied more, sometimes even distinct consumers groups by producing diverse product portfolio for each group. It was possible with the help of “non-compatible” technologies and those generating units which were found in more and more countries. At the same time one problem occurred (that did not exist in the past): the owners became separated and got farther from those who worked in the manufacturing and service sectors.

From the 1930’s the owners gradually handed over not only the operational leadership, but also the management roles to the managers. In 1932 two researchers (*Berle–Means* 1932) determined this tendency as a general rule. The main line of their study is: ownership and leadership should be separated from each other. Owners should only focus on controlling; plus on selection and motivation of the appropriate management. However, the operation of the organization and the operational decisions – which require more specialized expertise – should be in the managers’ hands. In order to effectively enforce the interest, a so-called “checks and balances” system was created between the institutional controlling and the power counterweight.

However, as a result of these some typical contradictions arose. Both the employees and the representative leaders could practice the opportunist behavior easily (instead of furthering the interest of the organization and that of the owners, their own goals and interests followed). (*Cordes et al* 2010, p. 2.). While seeking for solution the institutional model of corporate governance refined continuously. After the 1970’s crisis the owners have gradually realized that they barely have control options. For that very reason they took the field for winning back the legal leadership. The scientific footprint of this struggle is a study from 1976, which proved that managers basically do not further the owners’ interests (*Jensen–Meckling* 1976). The authors proved – in the article that turned classic – management, who runs and actuates a company, takes less care about raising the value of capital; and tends to follow their own (financial) aims. After the disputes came to an end the corporate senior management – partly because of discretion, partly because of the opportunism – accepted the critique: on the one hand they committed themselves to maximize shareholder’s value, on the other hand they decisively focused on the enforcement the interest of the ownerships.

This way, till the early 1990’s, the system of Corporate Governance developed entirely (*Mallin* 2004). The institutionalized distribution of power developed gradually; the role of corporate decision-making strengthened, a stock-option based incentive scheme was developed which simulated the proprietary interest. Partly due to these changes the 1990’s brought some incredibly fast development. The Dow-Jones index quintupled and the riskier stock of start-up companies – NASDAQ – was able to produce major growth. This confirmed the view – which may prove illusionary in retrospect – that the managers can create and suitably operate the adequate institution of responsible governance within the enterprise; this way not only the corporate disasters can be avoided, but also the enforcement of proprietary interest can be ensured. However, series of catastrophes that occurred since 2000 – first the

collapse of NASDAC and NYSE, then the bankruptcy of numerous wonder enterprises (eg. ENRON, Parmalat etc.) – queried all these hopes. Why did thus the crisis come about?

### 3. The leader individual: “High Mach”

The book of “The Peter Principle” was published at the end of the 1960’s, which explicated a modish idea in an easy to understand form: after a certain time in each organization everybody reaches his own level of competence (*Lawrence–Hull* 1969). The authors of books made their point around the statement that in an organization, sooner or later, each position will be filled with incompetents. They presumed to discover the reason of the phenomenon in the “normally” prevailing practice of the selection – which emphasizes the disciplined and reluctance-free execution. Further examinations did not confirm the emergence of the Peter Principle; however, they pointed out a similar, but an inconvenient, with far more serious consequent factors: the Machiavelli Principle.

The Machiavelli Principle states that sooner or later the top positions in an organization will be filled by so-called “High Mach” individuals. The concept of High Mach refers to N. Machiavelli, Italian scientist. On the turn of 16th century in his book, *Principle*, he described those practical counsels with which a leader can acquire and retain authority (*Machiavelli* 1987). Though he did not mention the motto that is now engaged by his name – that the end justifies the means – but he drew attention to the simple fact that “if you want to reach the aim, you will ask for the means, too”. However, the fact is that – despite the sanctified principles of his era – he served with very rational counsels to the lords and the statesmen.

According to the literature and political science the Machiavelli Principle – in any organization, as we are approaching the top of the hierarchy, the positions will be stuffed with “High Mach” type leaders – has been present for a long while in the society. However, its significance has multiplied in the 20<sup>th</sup> century, when big organizations gathered ground in the fields of society, politics and especially economics. In these establishments the work is mainly done by trustees (persons who are entrusted by the proprietor). From the interest of the proprietors’/investors’ point of view this situation basically leads to two main motivation problems:

1. the proprietors “file out” (of) the organization and entrust others, not only with the completion of production but also with the leadership. Whilst they should face the problem that the trustees will follow their own interest, not the proprietors. So they behave in an opportunist – following self-interest – way (*Cordes et al* 2011).
2. One – in many cases basically – determining aspect of the trustees’ behavior is to advance in hierarchy. However, the selection model applied by the organization decisively favors the “high Mach” personality-type, which – as we will see – is liable to execute even the acts that are not justifiable by moral principles; which evokes the disapproval of the proprietary and the society.

Treating others like a tool, having hard and risky jobs done by others and partner manipulating – sometimes even immoral – behavior are typical of a “High Mach” personality. “High Mach” persuades others to sacrifice their freedom and life, to carry out dirty and dangerous tasks, he tends to apply without any hesitation the most efficient – morally not supported – tools that are necessary to achieve the aims; though he himself only supports the objects of the organization if they are in accordance with his own ones. At first sight this personality does not seem very favorable, indeed, the majority of sociologists and writers talk about it in a negative way.

The question is whether the scientific research confirm the existence of Machiavelli Principle or not. The auto-selection and the existence of a leader personality became the

subject of the examination only in the 20<sup>th</sup> century. The first studies were related to motivation within the company. McClelland continued his first – the so called TAT-based – researches at the end of 1940's. Within the confines of the above mentioned he diagnosed that in the world of work people are basically motivated by these three factors: performance, relationship and power (*McClelland* 1961). From the beginning it was obvious that in some proportion all three factors can be caught in act in everyone; but they do not distribute equally. Further examinations – which applied the so-called Mach-test – have really shown that a typical distribution can be experienced among the people with different positions and different tasks. Engineers are mainly motivated by performance; employees who directly serve consumers are relationship-driven, whilst in the leader positions we can usually meet with power-oriented ones (*Harrell–Stahl* 1981). That is to say people in leader positions are more typical of a “High Mach” personality according to the Mach-scale than workers from other positions (*Vugt–Cremer* 1999).

#### **4. Why will the “High Mach” (HM) be selected?**

Becoming a leader turned into a planned and conscious process in the 20<sup>th</sup> century, when organizations began to grow. From this time career has been basically determined by the internal logic of the organizations. From our point of view there are 4 basic reasons why “High Mach” (HM) personalities will (in almost each and every organization in the modern societies) be necessarily selected – concerning companies especially from an extremely competitive area – and why they get along easier in the hierarchy:

1. Though the selection principles of organizations do not directly focus on selecting these personalities, but indirectly the HMs favor them. Organizations are fond of the, problem-solving oriented, career ambitious individuals who are hungry for success. Therefore, their selection parameters prefer the dynamic, power- and money-oriented people who seek for solutions and for excuses. They like to employ those who are capable of giving instructions (orders) and are ready to execute those; who do not hesitate but are ready to take actions.
2. The one who does the selection is mainly the HM, as well. They know what can be expected from each person, and also know who is the one being able to execute the instructions without any hesitation. They also know how these individuals can be motivated, how they should be handled. Work is easier with an HM than with a LW, however, it is clear for him: it is not wise to set the HM free but he has to keep an eye on him.
3. People who apply for a leader position are usually HMs, as well. The reason of it is the following: they generally know – especially if they have spent some years in the world of work – with what kind of tasks should the leader cope with, what kind of problems can occur around the bureau. They consider how much they would like to face with these problems day by day. For an “Average-Mach” this kind of work is accompanied by a significant role-conflict and a higher stress-level which he dislikes.
4. Stepping up in the corporate hierarchy from one level to another is basically determined by two factors: the success showed on the present level and the predicted performance on the new, higher level. Success in the management areas is generally helped by an HM personality. (See competence-management!) As someone gets higher and higher in the hierarchy, the real professional problems will be fewer and there will be more in connection with human- and corporate relationships (*Bartol–Martin* 1991, p. 25.). Nevertheless, the HM rather tends to help the success of handling these problems than to hold it back.

In view of the above mentioned factors the leader positions of the organizations – not only in the economy but also in politics and in the area of non-profit companies – are usually filled by “High Mach” personalities.

#### *4.1. Is “High Mach” a curse or a gift?*

We have seen that in the world of business the HM personalities – who are usually considered as negative figures – will be almost naturally selected. According to the above it seems that the people of everyday life and the writers, researchers all agree that the HMs are not only unpleasant but they also affect internal life of the organizations unfavorably and even harmfully. But why is it this way? Let us just think of the fact that in almost every organization and in each society such situations occur repeatedly – like crisis and corporate catastrophes – when it is needed to make decisions quickly, even if they are against someone’s interest, but they serve the interest of the society. Even these days circumstances can predict such cases when danger and risk are lurking at a group of people, and it depends on the top managers’ decision how many of them will survive. In these situations dilly-dallying and uncertainty can be followed by consequences of the management principle being seemingly justifiable, which can be characterized mainly with one of the characters’ saying from the book titled *Foundation of Salvor Hardin* – I. Asimov: “Never let your morality hinder the right action.”

The question is whether the research underpins that “High Mach” is a completely negative personality. The question is right because several situations occur in the society and a personality which functions efficiently in one situation might be unsatisfying in another one. In the past years a special analyzing system has been extended, the so-called trolleyology. (*Thomson 1976*). This model tries to explore the personal attitude in the ethically susceptible situations. The basic situation of trolleyology is the following: 5 people are working in front of a runaway bogie, rolling down the railway and they can not take off. We stand in front of the wheel and turn the shift gear on a free rail, but there is a man standing whom we might hit this way. What should we choose? Save those 5 people at a price of scarifying one? Situations like this can occur even in our society: in case of a corporate bankruptcy we have to decide on dismissals, during a social disaster whom to help and whom not to, or when we have not got enough resources we have to make decisions.

It is easy to see it is not only a disadvantage but a significant opportunity if the decision maker is not hesitating in situations like this, but – in a utilitarian manner – ‘he searches for the good for more people instead of only one’. It means that refusing “High Machs” – which usually relates to personal antipathy – cannot be justified in all cases. However, the “trolleyologic” researches unearthed more thought-provoking outcomes, as well. A new research has shown that 90% of the people refuse in the “trolleyology” tests to kill someone unknown just to save five more unknown ones. The scientists examined the psychological “profile” of the other 10% “hotshots”. They are diagnosed as follows: (1) they have a high “High Mach” point; (2) basically they approach decisions in a utilitarian manner with other words in a purpose-oriented way, (3) they do not assign high value to life. Above all – assigned by the researchers – we have to be aware and treat them carefully (*Bartels–Pizarro 2011*).

Another research also gives valuable information about “High Mach” personalities. Researchers have found a strong correlation between utilitarian values – which play an important role of managing the organization – and the set of a “High Mach” personality. They have found that the High power, which is typical of a “High Mach” personality, is liable to prefer the aim- and tool-rational deliberation by solving social problems. Contrary to this the Low power personality tends to put ethical deliberations forward (*Lammers–Stapel 2009*).

In a new research, executed this year, 213 people were put into low and high status and in power oriented situations. Some were chiefs (high status) and some were employees (low status). Some were put into powerful positions above others so they could divide money among them. Main observation is: people who originally had low status, but now they stepped – even if just temporarily – into a high status, tended to ‘take advantage of’ others (on), so as to humble and humiliate them, especially those with high status/low power situations. According to their phrasing low status/high power situation brings “little Hitlers” forth (*Fast et al 2011.*)

These researches impulse us to be cautious by hiring employees/leaders with such personality characteristics. On the whole we can draw a lesson that “High Mach” is an indispensable, useful, efficient, but a risk and danger hider personality. It executes orders without thinking and in order to execute a command, it is liable to violate moral principles, cultural traditions and the drawn rules of decisions. It can count but does not feel! It has arithmetic but no ethics. It knows what is more or what is less, but does not know what good or bad is. This type of personality is indispensable in some situations – in the case of a war or a catastrophe – on the other hand, it can generate in peaceful times. It is wise to employ him only carefully, watchfully and under hard control.

## **5. Root case of crisis**

Analyzing causes of corporate “rampages” – which by the way can be caught red-handed at the breakdowns of political parties’, as well – the most results refer to the following:

- Success and failure does not depend on one single person, but rather on the institution.
- Success and failure are made not by separate people, but are “made” by “cooperating” groups.
- The prime root cause of failures is: an institution under a responsible governance working inappropriately (the appropriate board of trustees, the board of supervision and the general manager).

Studies and experience refer to the case when even corporate and institutional separation of powers is not enough to prevent from corporate “rampages”. Like a good engineered truck, a safe and well serviced brake system even with a well-qualified, proficient driver is not sufficient to avoid road accidents. It is not sufficient even if the road on which the truck is driven is usually safe. If the driver is drunk, or if he does not drive the truck according to the weather conditions, he can bring about an accident. If he turns in an unforeseeable bend mindlessly, because he is in a hurry, the tragedy is set up, as well. Experience of the 21st century – enterprise bankruptcies (ENRON) and the global economic crisis – show: institutional separation of power is needed (just as the safe brake-system is also needed), but is not sufficient. Even “retailoring” the law (SOX law or the Say-on-Pay, ect.) proved to be slight at keeping business enterprises on a sufficient growth route.

However, stepping into the 21<sup>th</sup> century another contradiction joined the above mentioned ones. In politics, but especially in business, as well, one more – earlier less conspicuous – factor affects the selection. An article draws attention to the appearance of the so-called narcissistic personality (*Neicka 2011*). As in politics, – where it leads to problems, as well – in the governance of enterprises and non-profit organizations, where the decision making also passes by directly or indirectly by election, the so-called celebrity CEOs get into a leader role.

Narcissistic personality has specific characteristics: high self-evaluation (‘God knows everything, He knows everything better’), overconfidence, lack of self-criticism and realistic

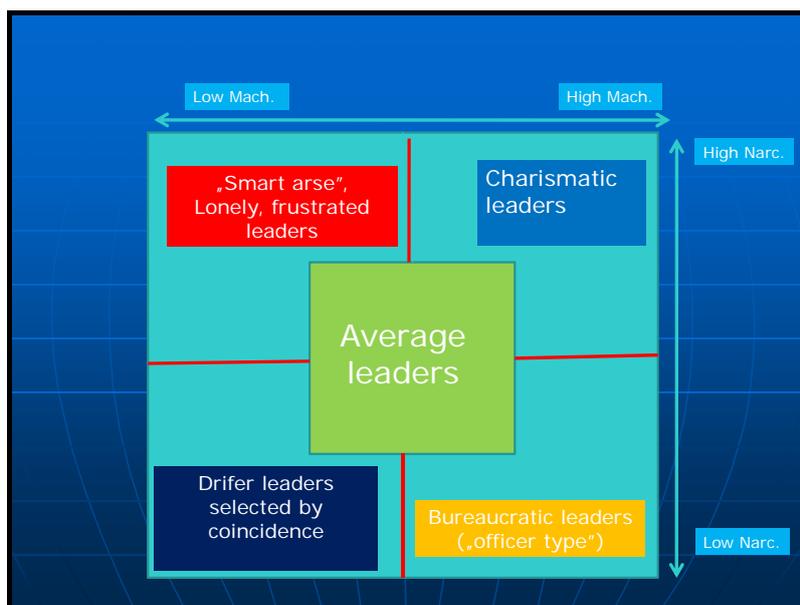
self-assessment, narcissism. From the synergy of them an unusual – adored and likely to be followed by an average person – individual “arose”. This person has a clear and seductive vision, though sometimes seceded from reality. He is shiny, begrudged and desired to be followed at the same time, but is not helpful at all. He is dumbfoundingly appealing, but self-interested beyond measure. He has excessive self-confidence, but always blames others for mistakes; defeats are always someone’s faults. He is deaf at critics, he declines it in the organizations and moreover, he bans open colloquy. He tends to follow only his own logic and intuition. In spite of his paradox features an average outsider determines the following important management qualities: self-confidence, excellence in leadership, ability to convince others, authority. Studies have shown that occasionally it is really true, but it is more often that even the opposite comes true. Researchers have found that while the narcissistic leader is busy with his own excellence, just his above mentioned features hinder the organization to practice the method of collective decision-making.

Eventually based on these two factors – the High Mach and the High Narc – evolve the degree of leader charisma in the selectors and the electors, which becomes a determinative selection factor by “rewriting” almost every other professional practice and experience. (see Figure 1).

## **6. Conclusion**

The experience of the last decade implies that not only in politics, but even in business “celebrity CEO” is spreading. They are the ones who are formed to “band names” with corporate expenditures and with the help of the media, and their value becomes an important part of the value of the company. However, likewise in politics, in business being a “celebrity” is also dangerous. The end source of success and failure: appropriate institutions, clear rules of decision-making, responsibility stimulating culture and the effective and accepted ethics in the society. Just like in management – as we have pointed out – by necessity the so-called High-Mach and lately the “High Narc.” personality is selected, to “have a hold” on this personality beside the institutional separation of power, mature incentive system, appropriate operational method and an organizational culture which is considering the interest of the society, and effectively operating ethics is also necessary. The complexity of organizations has reached a level when it is no longer important who the leader is, but what the content of governance is. Furthermore, we have to move forward from here: the institution of responsible governance which is “holding in check” the charismatic individual is not enough; building around, effective culture, adequate ethics and deliberate decision-making system is essential.

Figure 1. Leader types



Source: own construction

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