The Psychologist-Manager Journal, 15: 142–147, 2012
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ISSN: 1088-7156 print / 1550-3461 online
DOI: 10.1080/10887156.2012.676886

Psychology Press
Taylor & Francis Group

Collecting Data for Decisions about Individual/Corporate Transitions: A Nine Factor Model

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Psychologist managers help clients obtain valid information so that they can make free choices. Choices about corporate and individual transitions are one of those critical decision areas where psychologists can add unique value by helping clients to arrive at decisions using a structured approach to decision making. Corporate and individual transition decisions include mergers, acquisitions, alliances, and new employment. In this article the author describes one structured framework for collecting valid information using nine business factors. Specific questions to ask and specific websites to visit are provided. Limitations of the framework are discussed.

Professional "transitions" refers to a category of decisions that involve aligning professional or corporate reputation with a new corporate entity. Examples of questions raised include:

- Should the company be acquired?
- Should the company form a strategic alliance?
- Should I join this company Board?
- Should I take a job with another company?
- Should we acquire this company?

When clients deal with such transition questions, our job as psychologist managers is to provide them with valid information so that free, informed choices can be made. Part of our value is helping to frame questions they need to ask themselves and others. Another value we bring is steering clients to useful sources of information that could help them make informed decisions.

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The purpose of the author in this article is to provide practicing psychologists with a 9 factor framework to help evaluate the worthiness of a particular professional transition. The 9 factors are the nature of corporate control systems, CEO personality, base for success, compensation system, legal structures, profit picture, consultant stability, law suit patterns, and vendor payment history.

1. CORPORATE CONTROL SYSTEMS

Like all of us, chief executive officers are human and can make errors of judgment that could become illegal or get too close to a legal gray area. A proper institutional checks & balances system to guard against out of control CEO decisions is an important first factor to consider. The place to focus attention is on the audit committee of the board of directors. A question one might ask others is, "Tell me about the people on the audit committee?"

Public companies are required to have independent board members on audit committees. But there is a loophole in the definition of "independent." One can meet the standards of business independence by having audit committee members with no business ties to the company. But it says nothing about social ties, such as neighbors, people who went to college with the CEO, fellow country club members, etc. Private companies can have audit committee members who are family members or employees.

Ideally you would want to hear words like "strong" to describe the committee. It would help if a retired partner of a well known CPA firm was on that committee. Another question to ask is, "Tell me about what board meetings are like?" I am always concerned when the response is, "Everybody gets along." Getting along is a great idea for couples on an ocean cruise. It is not necessarily an ideal culture for a board of directors. I prefer to hear phrases like "spirited debate."

One important component of a corporate control system is the general counsel. Ask, "Tell me about the general counsel?" Be wary if you hear words like "well liked." That is not the general counsel's job. You hope to hear words like "respected" and "integrity."

If you ask, "Describe the chief financial officer," you don't want to hear the phrase "nice person." You do want to hear words like "tough" "fair" "strategic."

2. CEO PERSONALITY

As psychologists, our first focus might be on personality but I have made it #2. A poor institutional system of checks and balances should be considered an amber light even if the CEO seems to have a wonderful personality.

Within the constellation of the "Big Five," I tend to look for signs of neuroticism. How can one use web based tools to identify potential trends toward emotional instability and poor impulse control? Try searching the name of the potential boss or the CEO on news.google.com. Are there stories in the press that might raise concern? If it is a public company, check out the CEO name by googling "investing businessweek (name of CEO)." This should provide a basic resume. Click on the picture of people to see the person's network of board members. Know any people in common you could contact? Is the person on Linkedin.com? Do you know people who might know the CEO?

If it is private company, consider purchasing a D&B credit report at www.dnb.com. Does the CEO have a history of sudden business reversals? How long is the average tenure? Short tenure with sudden business changes, even from bad to good, might not necessarily be good signs. There are ways to create short term shareholder value yet leave long term investors in the lurch.

"Accessories" is a term often used to describe nonessential wearing apparel. What are the accessories the CEO "wears" to present him/herself to others? For example, does the CEO's office look more like a den at home than a business office? Are the photos around the office mostly of the CEO with famous personalities? Does the CEO have the most prominent parking spot near the front door? These might be indicative but not conclusive signs of neuroticism. It suggests more reference checking need be done rather than conclusions be drawn.

3. BASE FOR SUCCESS

If a service company, who is the chief rainmaker and what percent of the total business does this person control? If a manufacturing company, what percent of the total business do the two most important customers account for? In a constantly changing business environment, a successful company with a narrow base for success cannot maintain this position for long.

It is a good sign if a company admits its base for success is narrow and is trying to broaden the product line, distribution system, or customer base. If a company's base for success is narrow but it thinks it is in great shape, that is a bad sign.

4. COMPENSATION SYSTEM

Ask questions about how the CEO is paid. "How" the CEO is paid is more important than "how much" the CEO is paid. "How" the CEO is paid sends a signal

from the board regarding what is important. That signal moves down the corporate chain of command to influence corporate culture at all levels.

Pay particular attention to the elements that go into the bonus system and the stock option program. Does the bonus system create a dangerous short-term focus on quarterly or half-year results? The CEO may say that "people are our most important resource" but what percent of the bonus system is based on people factors and how are those factors measured? If no percent of bonus is based on some measure of human capital management, then that should be noted.

If venture capitalists or private equity firms are on the board, ask how much urgency there is for a "liquidity event," for example, to raise cash through an initial public offering or sell the company to a larger competitor?

5. LEGAL STRUCTURE

For a private company, examine the Dunn & Bradstreet credit report. If the company is public, look at the 10K. You can find the 10K by going to the Edgar database at www.sec.gov. Finance.yahoo.com is another excellent way to tap into the 10K reports. Look at the number of corporate entities that have been created by the target company.

Consult an attorney and ask if the legal structure is overly complex given its size and industry? For example, a company like General Electric would probably have hundreds of legal corporate entities. But that is not unusual, given this company's size and complexity. On the other hand, a $50 million producer of candy ought not to have fifteen legal entities under it. This is far too complex for its size and industry. It might be possible to hide shenanigans through untraceable patterns of intercompany borrowing. When looking at legal structure, simple is good.

6. PROFITS

A for-profit company wants to achieve Earnings before Income Taxes and Amortization (EBITA). A nonprofit wants to achieve Retained Earnings. Unusual profits relative to industry standards may indicate a well-run company—but may also point to accounting gimmicks, such as shifting expenses to next year. Go to your local commercial bank to browse through the RMA Directory. Published by the Risk Management Association (www.rmahq.org), the directory has summaries of 350,000 financial statements broken into standard industrial classification and sales size. Using it will allow you to make specific comparisons between your target company and a larger index based on sales volume and

industry sector. Some university libraries offer the RMA Directory online. It is called RMA E Statement Studies.

7. SHIFTING CONSULTANTS

Look for recent switching of consultants and other vendors as a diagnostic sign. There is always a learning curve when starting new institutional relationships. During that learning curve, mischief can be disguised. Examples would involve recent switching of banks, CPAs, or law firms. The question to ask would be, "How long has the company had its relationship with its present outside legal counsel, bank, and CPA firm?" Long term institutional relationships tend to be a positive sign.

8. LAWSUITS

Most attorneys subscribe to Lexis Online. Banks and CFOs often have access to D&B credit reports. Both services will show lawsuits filed and the reasons for the filings. One or two lawsuits should be no cause for alarm. You are seeking a pattern of law suits around related issues.

Look for the number of lawsuits initiated by the company against others. A corporate culture that values aggressive litigation against customers, competitors, and former employees might serve as a warning to you.

9. VENDOR PAYMENTS

The D&B credit report will show the relationship between the company's current ratio and the average days late on vendor payments. The current ratio is the relationship between corporate assets that can be converted into cash within 12 months or less divided by the amount of money owed over the next 12 months or less. A current ratio of .80 means that the entity has 80 cents available for every dollar it owes. A history of late payment with vendors may indicate a company in a difficult financial situation. On the other hand, a company with a current ratio of 1.2 has $1.20 for every dollar it owes. If this company also has a similar history of late payment with vendors, that might suggest a culture of not treating vendors well. Companies that do not treat vendors well often have a similar philosophy with other company stakeholders: employees, alliance partners, and even customers.

This relationship between current ratio and vendor payment should be reviewed by someone with an understanding of the company's business sector. There are strong industry norms that can temper conclusions drawn.

DISCUSSION AND LIMITATIONS

The nine factor professional transitions framework described in this article can also be used by psychologists in independent practice to evaluate how close they want to get to a potential institutional client opportunity. Risks for independent psychologists are less about reputation and but more about not getting paid or wasting valuable time with clients who do not want to change.

These nine factors were designed with a United States focus. The factors may or may not be appropriate outside the United States. The web tools presented will most likely not be appropriate outside the United States. Further research might focus on factors and web-based tools appropriate for other countries.

FOREWARNED IS FOREARMED

Much of our work as psychologist managers involves assisting clients in making personal and corporate transitions. These transitions might involve alliances, acquisitions, mergers, or new employment. Our value to clients is to steer them to a structure for obtaining valid information so they can make free and informed decisions. President Ronald Reagan often quoted a Russian proverb that makes sense for anyone thinking about such transitions: "Trust, but verify."