

# Cognitive Errors and Group Decisionmaking

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## Who are these people?



- On the left: Cynthia Cooper (WorldCom).
- In the middle: Colleen Rowley (FBI).
- On the right: Sherron Watkins (Enron).

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## Scandals aren't anything new.

- BCCI.
- S&L crisis.
- Enron (and WorldCom, Tyco, Global Crossing, Parmalat, etc.).
- The subprime crisis.
- Bernie Madoff.
- Every other corporate scandal.

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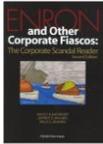
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## Law, by itself, can't regulate behavior.

- Goal of our first Enron book: explain, understand, learn.
- Goal of our second Enron book: why can't we learn?



March 19, 2009  
REUTERS/Mario Anzuoni



[http://en.wikipedia.org/wiki/Bernard\\_Madoff](http://en.wikipedia.org/wiki/Bernard_Madoff)



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## Smart people ran Enron (and they run other scandal-plagued companies).

- Smart people; dumb actions.
- Tougher rules don't work.
- What might work?
- Can you help your organizations not to make dumb decisions?

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## What can we learn from Enron & other, more recent, corporate scandals?

- RULE #1: Never underestimate human cognitive errors.
  - The individual.
  - The situation.

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What can we learn from Enron & other, more recent, corporate scandals?

- All other rules flow from Rule #1:
  - Checks and balances & human cognition.
    - “Rules on paper”: not enough.

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Hard-wired cognitive errors.

- Mix of psychological and sociological errors.
  - Cognitive dissonance error.
  - Diffusion of authority error.
  - Social pressure error.
  - Anchoring error.
- You combine these four and you get “the person and the situation” examples.

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Cognitive dissonance.



“I am a good person.”



“I am doing a bad thing.”



“There’s a good reason I’m doing this.”

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When it comes to cognitive dissonance,  
there are no lobsters, only frogs.



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### Other personal and group cognitive errors:

- Diffusion of authority and the bystander effect.
  - “Someone else will do it”—the Kitty Genovese story.
  - (A new book argues that fewer people were witnesses—maybe just 6—but that still implicates the error.)



Photo available at [http://en.wikipedia.org/wiki/Murder\\_of\\_Kitty\\_Genovese](http://en.wikipedia.org/wiki/Murder_of_Kitty_Genovese).

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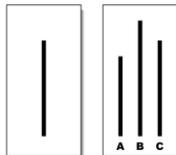
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### Other personal and group cognitive errors:

- Social pressure.
  - Solomon Asch's “lines” experiment.



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### Anchoring error.

- “Anchoring” involves “the common human tendency to rely too heavily, or ‘anchor,’ on one trait or piece of information when making decisions.”\*
- Best article describing anchoring: Amos Tversky & Daniel Kahneman, *Judgment under Uncertainty: Heuristics and Biases*, available at [www.hss.caltech.edu/~camerer/Ec101/JudgementUncertainty.pdf](http://www.hss.caltech.edu/~camerer/Ec101/JudgementUncertainty.pdf).

\* Quote & description available at [www.sciencedaily.com/articles/a/anchoring.htm](http://www.sciencedaily.com/articles/a/anchoring.htm).




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### Anchoring in action:

- [Try this one yourself.](#)
- (No calling out if you’ve seen it before!)




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### How cognitive errors can affect your behavior.

- Talking yourself into believing that something you did was OK, even when it wasn’t OK.
- Assuming that, if you discover a problem, everyone else knows it, too, so you don’t have to act on your discovery.
- Letting “everyone else does it” determine whether you do it, too.
- Focusing on one factor and ignoring all others.




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### Given our cognitive predilections, what can we do?

- We need to be conscious of the fact that humans can find themselves doing dumb things.
- We also need to think about the ways that our organizations can help us do, or hinder us from doing, what we should be doing.




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### Enron's incentives and culture.

- Incentives.
  - Paper profits = bonuses.
  - Bad news = banishment.
  - Individuals > teams.
- Organizational culture matters.
  - Valhalla.




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### Enron wasn't an anomaly.

- WorldCom.
- HealthSouth—Aaron Beam, former HealthSouth CFO:
 

“So when we had trouble hitting Wall Street expectations, [Scrushy] encouraged us to cook the books. I was intimidated by [Scrushy]. . . . I was afraid to stand up to him.”\*

\* John L. Smith, HealthSouth co-founder knows how greed grows on you, Las Vegas Review-Journal, May 19, 2010, at B1.




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Having a gate isn't the same as  
having one that works.



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A culture's myths predict future  
behavior.

- Stories of bravery and cowardice.
  - Celebrating “successes”?
  - Punishing “failures”?
  - “False positives”?

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Your own organizations.

- Bending the rules for “top performers”?
- What gets rewarded?
  - Enron's code of ethics: “RICE.”



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### Can we even fix the problem?

- Increased punishment alone won't work.
  - Smart people and risk of sanctions.
  - General counsel as influencers of corporate culture.\*

\* Colin Marks & Nancy B. Rapoport, Corporate Ethical Responsibility and the Lawyer's Role in a Contemporary Democracy, 77 FORDHAM L. REV. 1269 (2009), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1376475](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1376475).




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### The Rapoport “designated nay-sayer” proposal.

- Build in a structure of “questioning”
- Force ways to slow down decisions, except in emergencies.
- Rotate role to avoid stigma.
- Double-check “results” that agree with hypotheses.
- Reward critical thinking and false positives.




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### Hard life of a nay-sayer.

- Ostracism.
- Social pressure.
- Active resistance.




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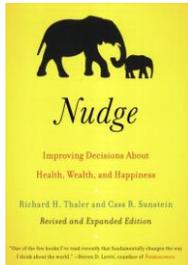
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In addition, think about “small changes”:



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### Options for nudging behavior

- Default rules (opt-in or opt-out?)
  - Possible application: timesheet entries
- Other incentives (e.g., changing compensation structure)
  - Possible application: cross-selling; mentoring junior staffers
- Checklists
  - Possible applications: conflicts checks, staffing decisions

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### Mentoring associates:

- Mentoring vs. sponsoring
- Again, if there are no tangible rewards for mentoring/sponsoring, then most of the more senior lawyers will gravitate toward that which is rewarded (fees).
- Greenberg Traurig’s “residency” program—lower first-year salary traded for increased training from the firm (but there’s still a risk of not being “retained” after the residency ends).

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## Some barriers to change

- Don't discount the "perceived losses" problem.
- Smart people will find workarounds to any changes that a firm imposes.
- Few firms want to be the "first" to make big changes.
  - *But see* Duane Morris as an example.

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