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**LYING IN BUSINESS
INSIGHTS FROM HANNAH ARENDT'S 'LYING IN POLITICS'**

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Lying in Business

Insights from Hannah Arendt's 'Lying in Politics'

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Abstract

The famous political philosopher Hannah Arendt develops several arguments why truthfulness cannot be counted among the political virtues. This article shows that similar arguments apply to lying in business. Based on Hannah Arendt's theory, we distinguish five reasons why lying is a structural temptation in business: business is about action to change the world and therefore businessmen need the capacity to deny current reality; commerce requires successful image-making and liars have the advantage to come up with plausible stories; business communication is more often about opinions than about facts, giving leeway to ignore uncomfortable signals; business increasingly makes use of plans and models, but these techniques foster inflexibility in acknowledging the real facts; businessmen fall easily prey to self-deception, because one needs to act as if the vision already materializes. The theory is illustrated by a case study of Landis that grew from a relative insignificant into a large organization within a short period of time, but ended with outright lies and bankruptcy.

JEL codes

D89, M14, M41

Keywords

Lying, deceit in business, Hannah Arendt, image-making, self-deception, accounting fraud, politics and business, Landis

1 Introduction

One of the positive side effects of the credit crisis is that the halting of credit also made it more difficult to finance businesses that were built on deceit. The most shocking case appeared when Bernard Madoff confessed on 11 December 2008 that he made \$50bn disappear, obviously the biggest case in the history of lying in business. Many were duped and faced bankruptcy, investor lawsuits and shame. One, apparently unable to live with the knowledge that he pushed \$1.4bn belonging to his social and business acquaintances into Madoff, has killed himself.¹

Mr. Madoff's case doesn't stand on its own. There is a history of examples in which company officials and managers have made statements which they knew were corresponding to no reality at all (Rezaee, 2005). The names of the companies that were built almost entirely on fantasy, lie and cheat may still ring a bell with many of us. Some of those businesses were seemingly among the biggest and best and their managers were considered respected entrepreneurs at the time. What Enron, WorldCom, Parmalat, Tyco International and HealthSouth have in common is that they once belonged to the premier league of multi-billion dollar companies that were all listed on a high-profile stock exchange. But also for companies that have not experienced bankruptcy, there are indications of conscious manipulation of financial data coined as 'creative accounting' (Jameson, 1988; Leung and Cooper, 1995). Even Royal Dutch/Shell, one of the financially conservative enterprises, admitted in 2004 that it had overstated its oil reserves by 24% and had to pay fines totaling \$151 m to US and UK regulators (Grant and Visconte, 2006).

In literature as well as in public debate, the diagnosis of the lack of trustworthiness of corporations has often focused on individual moral deficiencies or institutional deficiencies. Some view the combination of personal greed and moral laxity (of, for example, Dennis Kolowski at Tyco or Andrew Fastow at Enron or the Tanzis at Parmalat) as a main cause of deceit (Dallas, 2004). Others have argued, however, that scandals are not mainly due to greed, opportunism, irresponsibility or arrogance among key executives, but point as well to the presence of systemic factors. Often mentioned examples of these systemic influences are the role of corporate governance (Agrawal and Chadha 2005), weakness of accepted accounting principles and lack of auditor oversight (Coffee, 2004), inappropriate executive compensation systems (Erickson, Hanlon and Maydew, 2006; Efendi, Srivastava and Swanson, 2007; Johnson, Ryan and Tian, 2008), badly founded corporate strategies (Grant and Visconti, 2006), or the cultural dominance of monetary success and the resulting tendency for social norms to lose their regulatory force (Choo and Tan, 2007).

In this article we search for philosophical reasons for the intimate relationship between lying and business beyond the obvious reasons of personal moral laxity or institutional deficiencies. In order to explore this research question, we will be using two papers from Hannah Arendt, *Lying in Politics* (Arendt, 1969) and *Truth and Politics* (Arendt, 1968). The advantage of using Arendt for this purpose is that her philosophy is significantly grounded in real-life experiences and not the product of theoretical philosophy developed in

the absence of context. Her philosophy of lying presupposes an inescapable organizational and institutional milieu that may breed personal and institutional failures and is therefore not separated but rather closely linked to the institutional analysis referred to above. Both of her papers cover the subject of lying in a political context and develop arguments why politicians are tempted to lie in order to realize their political goals. Despite the fact that serious differences exist between politics and business, we show that similar arguments apply to the business context that explain why businessmen are structurally exposed to the temptation to lie.

The contents of this article are as follows. First, we shortly discuss the definition of lying. In the next five sections, we distill five claims of Arendt about lying in politics and show how each of them can also explain the structural temptation of lying in business. In section 8 we illustrate our findings by a case study of one company that had a vision of becoming a large international company but ended with outright lies and bankruptcy. Section 9 summarizes the main findings and contributions of the paper.

2 Lying, deceit and deceitfulness

According to Sissela Bok a lie can be defined as follows: ‘A lie is a statement, believed by the liar to be false, made to another person with the intention that the person be deceived by the statement’ (Bok, 1989: 13). Another definition that demonstrates a great deal of overlap is from Bernard Williams. He takes a lie to be ‘an assertion, the content of which the speaker believes to be false, which is made with the intention to deceive the hearer with regard to that content’ (Williams, 2002: 96).

These definitions can be broken down in several component parts (Mahon, 2008). In order to establish a lie: 1) it is required that a person makes a statement and, 2) that the person making the statement believes that statement to be false and, 3) that the believed false statement is made to another person and, 4) that it is the intention of the person making the statement that it is judged to be true by the other person.² Each of these requirements allow for further specific interpretations. For example, whereas the first requirement stresses that lying assumes that the liar makes a statement, also signs and expressions that are common in a particular context can count as a statement. Even silence can be used as a means of communication with the intention to deceive, because silence often carries a particular meaning. The second requirement implies that a statement that was incorrectly believed by the liar to be false but is in fact true still can be qualified as a lie. Because the condition that a statement is believed to be false is fulfilled even in the case that the liar was erroneously believing that the statement was wrong. On the other hand, communicating falsehoods or inaccuracies, not knowing that one does, should not be referred to as lying. The third requirement obviously does not exclude generic statements that were conceived for a wider audience, or electronic mails or advertisement, which can also potentially qualify as lying. Finally, and most importantly, in order to lie there must be the intention to deceive the

addressee. This means that it is not necessary that the intention to deceive is successful. Lying is not a success verb, it is the intention that is decisive.

This also explains why lying is very hard to detect and why liars can often get away with lying so easily. Intent must be formed before the act, and it must unite with the act: 'actus non facit reum nisi mens sit rea', which means that the act does not make a person guilty unless the mind is guilty too. Thus, in order to demonstrate that somebody is lying, we have to be able to establish that the liar has the intention to deceive the addressee about the content of the statement made, as well as the intention to deceive the addressee about the liar's beliefs and the intention to deceive the addressee about the sincerity of the liar. Since an intention is a mental state, it can however not objectively be explored.³ Rather, the intention has to be reconstructed from identifiable signs and behavior. In such a reduction there is always a chance that something is misinterpreted, overlooked or even missed. When a contextually relevant intention corresponds with an act that falls within the definition of lying and, when on top of that, a reasonable and direct enough link can be established between the act and the intention (mens rea and actus reus), then a court may be able to determine that there is sufficient proof that somebody is lying. But, even then, before lying becomes relevant from a point of view of criminal law, it is furthermore necessary that the person lying can be said to have understood and wanted the offence committed. This makes it a daunting challenge to sufficiently prove that somebody was lying, even if it appears to be obvious to an outsider.

According to Rappaport (2008), a lie is often associated with deceit, but deceit is more general both in occurrence and in scope. The term 'deceit' implies an intention to mislead to the disadvantage of those who are misled, particularly vis-à-vis those misleading them. 'Lie' also entails intention, but the defining intention of the lie is related to the signal transmitted, whereas the defining intention of deceit is concerned with the effect upon, or more specifically, the response of, the receiver (Rappaport, 2008: 11). From this insight we can conclude that deceit can be achieved through lying and that most lies cause deceit, but that this is not necessarily and in every instance the case. If, for instance, telling the truth aggravates a particular situation as in certain medical situations, it can be ethically defended not to tell the truth and to consequently lie about a particular situation. This so called white lie is a lie according to Sissela Bok's definition, but it is not deceitful as the intention to mislead is not to the disadvantage of the misled (Bok, 1989: 58).

Furthermore, important for our purpose is the notion that intention to deceive may not be enough to establish deceitfulness. There are situations in which we explicitly or tacitly accept to be deceived. In games and in play we expect and accept to be lead down a 'wrong' track by an intentionally misleading opponent. This is obviously not deceitful. What deceit presupposes is the existence of a relationship of trust which deceit then violates whereas no relationship of trustfulness prevailed at the time of the act (Rappaport, 2008). Hence, the quintessential element is the abuse of this relationship of trust between individuals or groups. It is particularly in those cases that lies become unethical and damaging to society at large.⁴

3 Action and mental freedom

Hannah Arendt's essay 'Lying in politics' is a response to the Pentagon Papers about America's role in Vietnam. The basic issue that these papers raise is deception. According to Hannah Arendt truthfulness has never been counted among the political virtues, and lies have always been regarded as justifiable tools in political dealing (Arendt, 1968: 223; 1969: 4). In this and the next four sections we want to bring forward several arguments substantiating why Hannah Arendt thinks that truth is not a virtue in politics and show why Arendt's analysis of the reasons for lying in politics is also relevant for business.

A first argument why according to Arendt truthfulness has never been counted among the political virtues follows from the notion that politics is all about action. This is expressed by the following citations:

"A characteristic of human action is that it always begins something new, and this does not mean that it is ever permitted to start *ab ovo*, to create *ex nihilo*. In order to make room for one's own action, something that was there before must be removed or destroyed, and things as they were before are changed. Such change would be impossible if we could not mentally remove ourselves from where we physically are located and imagine that things might as well be different from what they actually are. In other words, the deliberate denial of factual truth – the ability to lie – and the capacity to change facts – the ability to act – are interconnected; they owe their existence to the same source: imagination." (Arendt, 1969: 5)

"He (the Liar) is an actor by nature; he says what is not so because he wants things to be different from what they are – that is, he wants to change the world." (Arendt, 1968: 246)

No matter what the reasons may be, politicians have a desire to change the world. We cannot create something new out of nothing and therefore we have to procure the space we need to make manifest our ideas. Politics derives from a vision that the world can be different from what it is now. Having a vision is something that enables political leaders to guide people into uncharted territory. To be able to remove oneself from today's reality, not accepting the world as it is, requires imagination. This means that in order to realize our dreams something else has to give way. Without the mental freedom to deny or affirm existence, no action would be possible. Deliberate falsehoods are also attempts to remove oneself from today's reality. The deliberate denial of truth – the ability to lie – and the capacity to act are thus interconnected. Also the liar is a man of action who wants to change the world and in order to achieve that, he says what is not so.⁵

Action is not only the very stuff politics are made of, but also of business. There is no doubt that businessmen and politicians share the affinity with action. Just as politicians, businessmen have a capacity to see a future state of things which don't exist (yet). Businesses are based on ideas that were once rooted in people's heads who made them manifest by coming into action. Just like politicians, businessmen thus have a desire to change the world. Yesterday's ideas lie at the core of today's business world because some people decided not to stick with the world as it was. They took action and went off to create what they could see for themselves. This is what innovation is all about. A new product or solution is imagination coming into action.

4 Successful image making

“Since the liar is free to fashion his “facts” to fit the profit and pleasure, or even the mere expectations, of his audience, the chances are that he will be more persuasive than the truth teller. Indeed, he will usually have plausibility on his side; his exposition will sound more logical, as it were, since the element of unexpectedness – one of the outstanding characteristics of all events – has mercifully disappeared. ” (Arendt, 1968: 247)

“It is equally true in image-making of all sorts, in which again, every known and established fact can be denied or neglected if it is likely to hurt the image; for an image, unlike an old-fashioned portrait, is supposed not to flatter reality but to offer a full-fledged substitute for it. And this substitute, because of modern techniques and the mass media, is, of course, much more in the public eye than the original ever was.” (Arendt, 1968: 248)

In order to be successful, the politicians must convince the audience of their vision.⁶ According to Arendt, half of politics is image-making and the other half the art of making peoples believe in the imagery (Arendt, 1969: 8). They view their audience from a public-relations perspective. In order to convince the public, it is important to create an image that is coherent and consistent. Here, the liar is at an advantage as he can fashion the facts to tailor them to suit the ‘reality’ that he sees before his eyes. He will sound more plausible and logical as the element of unexpectedness has disappeared. Not bothered by having to communicate unwelcome facts, the liar has the ability to sweet talk to every audience while adjusting his pitch to what people want to hear. He has prepared his story for public consumption to making it credible.

Hence, truthfulness is not so much a political virtue because it makes it harder to convince the audience and therefore to prepare the way to change. Only if the policy of image-making does not succeed, the politician may fall back to another strategy to gain

support, that is by using carrot and stick. As substitutes for more violent means, lies can therefore be considered as relatively harmless tools in the arsenal of political action.

Also with respect to image-making, there is a striking parallel between politics and business. In the modern business environment huge amounts of money are invested in image-making. Madoff could do what he has done because he managed to create an image of reliability and trustworthiness. It was done with extreme care. How a company appears in the public eye is of the greatest importance. More than ever, companies represent how we should live and to which group we belong. Something as simple as a soft drink has become an icon personifying a particular lifestyle. Those images are carefully crafted and unwelcome facts that have the potential to distort this manufactured image are met with hostility. Substantial marketing and advertising budgets are deployed to maintain an image intact because there is a lot at stake.⁷ People often buy a dream rather than a product (Waide, 2007).

In this process, dangers because of the manipulation of facts constantly arise. Schoderbek and Deshpande (1996) estimate that impression management (measured by the so-called impression management scale) is significantly correlated to unethical conduct (measured by the Ruch and Newstrom ethics scale) as well as to over claiming (measured by the so-called over claiming scale). An illustrative example is the image that Philip Morris Inc wanted to portray through its brand Marlboro (Colby, 2008). The cowboy riding his horse was an image of freedom and the good life. Despite the fact that for a long time they have stopped using that image, it still is with us. A reality that has a counter side to it, though. Instead of selling a perceived happy lifestyle, Philip Morris sells cigarettes that were known to cause deadly diseases. Seen from this perspective, the 'good' life as presented by Marlboro is anything but the good life, but exactly the opposite. What is interesting is that despite the fact that both Philip Morris and their customers are aware of the negative effects of smoking, these facts remain underexposed as they are hostile to the image.

Also communication on corporate social responsibility is part of the company's impression management (Hooghiemstra, 2000). Companies engage in corporate social reporting to affect public's perceptions of the company, using it as an instrument for controlling public relations (Owen et al, 2000). As management is willing to report good news, but reluctant to disclose bad news, social and environmental disclosures run the risk to be to a large extent self-laudatory (Hooghiemstra, 2000). In a study of Australian companies which were known to have breached various environmental protection laws, Deegan and Rankin (1996) show, for example, that the disclosure of positive information greatly outweigh the negative disclosure. The mean amount of negative disclosures was only 5.5 words. Only 10% of the companies made a reference to the breach of environmental law. Interestingly, the sample of prosecuted firms significantly disclosed more (positive) environmental information than firms that were not prosecuted. Firms apparently tried to deflect attention from the proven misconduct towards their positive environmental policies. Also Wiseman (1982) finds for US companies in the steel, oil and pulp sectors that there appears to be no relationship between the environmental performance disclosed in annual

reports and their actual environmental performance. Berthelot et al (2003) refer to various other researches that show that voluntary environmental disclosure is not a reliable indicator of a firm's environmental performance. According to Gray (2001) social reports are incomplete to such an extent that one must conclude that they are either a waste of time and money or even a deliberate attempt to mislead society as to the quality of CSR of the reporting companies. He concludes that voluntary reporting practices will not advance accountability, because providing complete information is not in the organization's interest. Hess and Dunfee (2007) argue that if it is not possible to know whether a company is telling the truth or just engages in cheap talk, stakeholders will turn away from this information, resulting in what they call a 'babbling equilibrium'. In this situation, a firm can adopt the appearance of a CSR program, without actually taking care to prevent wrongdoing. They attempt to change perceptions without changing facts (Hess, 2007).

5 Truth and opinion

"The trouble is that factual truth, like all other truth, peremptorily claims to be acknowledged and precludes debate, and debate constitutes the very essence of political life." (Arendt, 1969: 237)

"Factual truth is no more self-evident than opinion, and this may be among the reasons that opinion holders find it relatively easy to discredit factual truth as just another opinion." (Arendt, 1969: 239)

A third reason for the conflict between politics and truth is that politics is about debate. Unwelcome factual truths are therefore often transformed into opinions that can be debated. Factual truth differs from opinion in the degree of claimed validity. Because facts are beyond dispute, they carry an element of coercion that opinions lack. From a political point of view, truth may therefore be seen as despotic. Unwelcome opinions can be rejected or compromised upon, but unwelcome facts possess a stubbornness that can only be removed by outright lies. Of course, facts and opinions belong to the same realm, as facts inform opinions. Opinions that differ widely may still be legitimate, but only as long as they respect factual truth. Hence, although politicians have a right to interpret the facts in accordance to their own vision, they are not allowed to change the facts themselves.

The reason why politicians may find it relatively easy to discredit factual truth as just another opinion is that contingent facts are not compellingly true.⁸ They could always have been otherwise. Facts need testimony to be remembered and trustworthy witnesses. But eyewitnesses are notoriously unreliable and facts recorded by documents can be suspected as forgeries. There are many known examples in history in which facts have been deliberately misrepresented or lied away. Facts that are ignored or deliberately lied away or that are otherwise transitioned out of the world may disappear forever, because their content often defies verification. The chances that an element of factual truth survives the deliberate attack

from powers that want to make such facts disappear are not seriously high. Because of this contingent character, factual truth is always very vulnerable.

Also in business unwelcome facts can be easily ignored because business communication is often about opinions. In the stock market, a business is valued by its future potential of making profits, which depends on market expectations. Companies therefore have a major interest in communicating positive expectations in annual reports on the realization of business plans. This kind of statements does, however, not have the status of factual truth. To verify whether a fact is true, we have to check its occurrence and this can only be done with respect to the past. But such markers are absent when talking about the future. Any statement about a future event therefore reflects an opinion that only grows gradually into falsity or truth because of the elapse of time. This gives leeway for ignoring signals that contrast the expectations.

Grant and Visconti (2006) show for 12 case studies of US and European companies involved in major accounting scandals that the background of the accounting fraud is a strategic misfit based on overambitious growth targets, multiple acquisitions and excessive debt financing. For businessmen who are in charge of realizing a future goal, admitting failure when things go wrong is indeed never easy. The alternative – to change the image of the future and admit failure – may be too difficult and too costly. It is easier to continue along the same track ignoring the signals. As long as there is time, there is the thought of a possibility to catch up and use the elapse of time in combination with targeted action to cover up. However, once allowing deviations between the reality actually perceived and the communicated ‘facts’, there is hardly an avenue that leads back to reality. The problem is that lies often start small and then grow bigger. The incentives to lie the second time will be greater once one has started lying, because lying seldom cures the underlying reasons that caused the failures. When the problem that prompted the first lie reappears, the risk of having past untruths exposed is a powerful incentive to lie again (Fleming and Zyglidopoulos, 2008).

Obviously, it very difficult to say when lying starts if businesses communicate unrealistic opinions about the expected performance in future. If predictions do not materialize, is it because they have been deceptively communicated like that, or is failure the result of unforeseen circumstances? Hence it is hard, if not impossible, to judge the extent to which people are lying when they make statements about the future. Without doubt some statements are likelier than others, but there are no clear indicators telling us when we have entered the world of error or fantasy or deliberate falsehood. A goal may seem impossible from the start, but only the elapse of time will tell the real tale. How big must the deviation from an original prediction be before we can consider it a moral duty to inform stakeholders? Is it 5 percent or 10 or 50? There are no clear answers and this provides opportunities for companies to communicate predictions that they know themselves to be unrealistic.

6 The use of models

“They were eager to discover laws by which to explain and predict political historical facts as though they were necessary, and thus as reliable , as the physicists once believed natural phenomena to be.” (Arendt, 1968: 11)

“Insofar as they have the appetite for action and are also in love with theories..., they will be tempted to fit their reality ... into their theory, thereby mentally getting rid of its disconcerting contingency.” (Arendt, 1968: 12)

The fourth argument that we derive from Hannah Arendt’s analysis does not pertain to the politicians in the first place, but rather to those who inform politicians with political analysis. Arendt refers to this group as the higher ranks of the civilian services. According to Arendt, these people can be characterized as problem-solvers with great self confidence who rarely doubt their ability to prevail and are accustomed to winning. They are different from the ordinary image makers, in the sense that they are intelligent and in love with abstract theory and models.

But the use of sophisticated modeling techniques in the preparation of policy runs the danger that politicians put an unrealistic faith in models and theory. Although models help us understand complex aspects of reality, they may also foster blindness for aspects that are not in the model (Brümmer, 1993). Politicians tend to forget that any model that their advisors are using is a representation of reality, and never more than that. At the same time, insofar as politicians have the appetite for action, their advisors will hardly have the time to wait until the theories and hypothetical explanations are verified or denied by facts. Instead they will be tempted to adjust facts to make them fit their theory.

Because of too much confidence in ‘theory’ and ‘models’ of their advisors, the risk increases that politicians lose connection with reality and that they enter into a defactualized world. In the words of Hannah Arendt (1969: 20): ‘the bureaucratic model had completely displaced reality: the hard and stubborn facts, which so many intelligence analysts were paid so much to collect, were ignored’.

Like in politics, also in the business world there is an increasing pervasiveness of the use of theories and methodologies. In 2004, 78 of the top 100 universities in the US offered courses on business planning, typically in the area of entrepreneurship or small business management (Honig, 2004). It is obviously important for business leaders to use methods for planning purposes. Usually a planning department is responsible for putting together multi-year business plans. Those plans are used by management to pro-actively align resources in order to realize envisaged targets. Guiding an organization into a particular direction becomes much easier if management has a sense of direction. However, the research on how business plans affect profitability has yielded mixed results. Some of these studies found a positive relationship between planning and profitability, growth and performance. For example, in an

empirical research on 223 new ventures in Sweden, Delmar and Share (2003) find that business planning is an important precursor to action in new ventures. By helping firm founders to make decisions, to balance resource supply and demand, and to turn abstract goals into concrete operational steps, business planning reduces the likelihood of venture disbanding and accelerates product development and venture organizing activity. But other studies found a negative, or lack of relationship, between business plans and profitability (Honig, 2004).

One of the reasons for the negative impact of business plans on performance is that planning is constraining creative responses to environmental changes (Mintzberg, 1987). Regularly business plans receive a certain degree of authority that gets elevated to a level similar to a 'truth'. The fascination with such imaginary goals is surprising and typically suits problem-solvers and business-planners who are trained in translating factual content into a language of numbers and scenarios. However, no matter the level of theory that is applied, every plan suffers from the same defect, they remain what they are: plans. To a smaller or larger degree no complex business plan ever gets fully realized, but the desire to perform according to plan remains a strong motivator. Predictability, although counter natural, is something that is highly praised by business executives and rewarded by shareholders (Blake et al, 2000). No doubt it is vital to have plans and ideas about where we want to go, but we should not lose sight of the fact that there is nothing permanent about such plans. No matter how hard we try, as long as plans have not reached the status of fact, they remain an intelligent guess about what the future might look like.⁹

Again, there is an evident link with lying. Although the motive is different, just like image making, business planning may lead to a more or less conscious neglect of stubborn facts, just because they do not fit the assumptions on which the business plan is based. If a manager has put his entire weight behind a plan, and the assumptions turn out to be incorrect, an easy way to save face for those who have developed the plan is to ignore these signals and to change 'reality'.

7 Self-deception

"The more successful a liar is, the more people he has convinced, the more likely it is that he will end by believing his own lies." (Arendt, 1968: 34)

"Only self-deception is likely to create a semblance of truthfulness, and in a debate about the facts the only persuasive factor that sometimes has a chance to prevail against pleasure, fear and profit is personal appearance." (Arendt, 1969: 250)

The fifth reason why truthfulness is not a political virtue we take from Hannah Arendt's analysis of the question how politicians can lie at such a grand scale. This explanation points at the interconnectedness of deception and self-deception. As discussed above, to change reality as it is, requires imagination. A common theme in success psychology is that to get to

the desired success, one has to be able to put oneself in the situation as if the goal had already been achieved. The danger associated with this kind of image-making and the consequent mass manipulation to make the audience believe the image is that it may easily evolve to self-deception. If others start seriously believing the truth of the image, the politician may also become more and more convinced of his vision. Successful politicians are thus susceptible to falling prey to self-deception.

This self-deception helps the liar to be much more trustworthy in the eyes of others. This may be a reason for political advisors not to inform their political bosses about disturbing facts.¹⁰ Because once one is convinced of certain facts, it is much easier to convince others of these facts. One is then acting from within the same boat as the victims and not from a cold distant place. Self-deception is often met with more permissiveness and tolerance than cold lying.

The importance of mental freedom, successful image making, opinions and the use of business plans in business makes businessmen also susceptible to self deception. In order to arrive at the different world that a businessman can see because of his visionary mind, he often lives and acts as if this new world already exists, deliberately deceiving his own mind as a consequence. The step from image-making to believing is a small one, and if the people who are creating those images are not careful, the image becomes a perceived reality in the minds of themselves.

Such self-deception is instrumental to what Tenbrunsel and Messick (2004) coin “ethical fading”, a process by which the moral colors of an ethical decision fade into bleached hues that are void of moral implications. Because self-deception allows the businessman to behave self-interestedly, while at the same time believing that he upholds his moral principles. This process is facilitated by various enablers, such as language euphemisms and routinization of decisions. For example, instead of illegal accounting practices managers talk about aggressive accounting. These terms may become so commonplace that managers do no longer see the questionable behavior that they represent. That also applies to decision making processes that become routine and therefore ordinary. A series of small steps away from ethical and acceptable practices, if sufficiently small, may therefore lead to an unconscious practice of lying.

Another mechanism that evokes self deception suggested by the analysis of Arendt is that it is in the business interest to inform top executives selectively. A example is provided by the construction fraud in the Netherlands (XXX). In 2001 a TV program by Zembla exposed a clearing system for construction companies that colluded in price offers for public works. In 1992, the European Commission prohibited the practice of pre-consulting and in 1998 the Dutch government implemented this EU regulation and forbade the practice of ex-ante consultations. But, as the TV program showed, the practice still continued in 2001. When the fraud unfolded, many construction companies were persecuted and fined. In response, many CEO’s of large Dutch construction companies complained that they had not known these practices. The reason might well be that the executives in charge of acquisition

policy deliberately did not inform their bosses, because it was neither in their own interest nor in the interest of the business doing so. Because a company is more successful in presenting an honest image if the CEO believes his company to be fully honest.

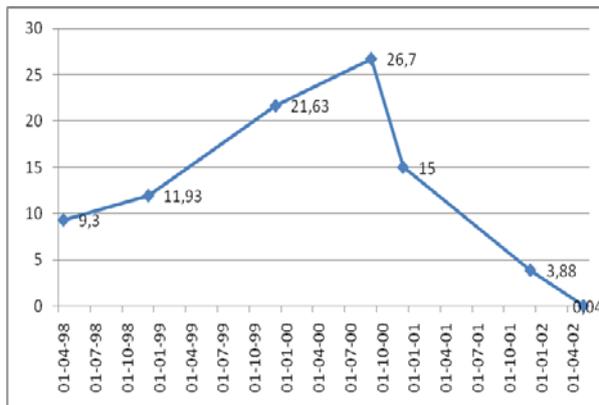
8 Landis, a case study in lying

As a case study we have chosen Landis. The Landis case is particular not because of its relative size. Though sizable in terms of absolute numbers there are more important bankruptcies that can be studied. What interests us in the Landis case is that it has several characteristics that makes trust in its future plans a crucial factor of success. Though Landis Group N.V. has been in existence since 1991, the listing on the Amsterdam Euronext exchange in 1998 marks a departure from Landis as a pure trading company. From 1998 onwards Landis is increasingly entering new business areas with which the management has had very little experience. As there was very limited history of the firm's performance in these new areas, the outside observer had few anchors to judge the extent to which information coming from the company is realistic or not. This provided the company management with a context in which they could operate relatively freely and created a setting in which the mechanisms that Arendt's theory of lying stress could easily show up.

Historical overview of Landis

Landis grew out of HCS Technology N.V. when it was made independent in 1991 as a result of a successful management buy-out. Its original focus was that of a supplier of information technology and more specifically of communication equipment. In order to reap the benefits of a growing market it reinvented itself from a local reseller into an international full-service distributor. The growth was made possible because of acquisitions that were facilitated by an IPO (initial public offering) that took place in 1998. Having floated the company on a stock exchange facilitated the access to capital which allowed Landis to take its expansion ideas even further. But in order to sustain expansion in a competitive market, Landis needed additional capital to support its growth. For that purpose it raised a loan of 175 million euro from a syndicate of nine banks. This transaction was completed during the third quarter of 2000. In March 2001 it raised another 45 million euro by means of a convertible loan which had to be renegotiated because of liquidity issues. A breach of trust with the banks combined with a shortage of cash as a result of negative cash flows on the side of Landis called for different solutions. When the banks cancelled the loan and Landis reported a loss of 52 million euro for the year 2001 on April 11 2002 the Board of Directors stepped down. The liquidation of Landis became unavoidable when a rescue plan presented by an entirely new Board of Directors was turned down on April 22 of the same year. Landis went bankrupt on July 8 2002. As a consequence 3000 employees lost their jobs and roughly 600 million euro could be considered lost during the process which lasted not much longer than 4 years.

Figure 1 Landis share price



Source: Euronext

What went wrong?

One of the facts that contributed to the course of events as they took place is the way Landis financed its expansion. First, during and after the flotation of the Landis business it acquired around 440 million euro in cash mainly by issuing shares. Second, while listed, Landis acquired a large number of businesses by issuing stock. In order to sustain its growth it had to report positive results if the Landis management were to continue an expansion strategy of any kind. Management realized that a substantial decline in the Landis stock price would be an obstacle to growing the company by means of using its shares to acquire additional businesses. A declining share price was something that had to be avoided at all cost. As the financial position of Landis was extremely fragile, at least in retrospect, a difficult dance had to be performed in order to maintain a positive image.

This task was made even more difficult as market conditions started to change again. The year 2000 marked a turning point. In the IT sector spending was at an all time high and general consent had it that growth would continue. But it didn't. The NASDAQ stock exchange reached its all-time high on March 10th, 2000 at a level of 5132.52. Shortly after, the heavily technology dependent exchange would fall more than 62% in the following two years when the bottom dropped out of the so-called Internet bubble. Landis being in the center of the technology industry suffered as a result of the deteriorating market conditions.

As if the implosion of the technology industry was not enough, another important element negatively impacted Landis' chances to sustain its growth. Presumably driven by the almost unlimited possibilities of new technology, an initiative was launched at the end of the last century to offer more extensive mobile services. Licenses allowing telecom operators to utilize this so-called third-generation mobile services (UMTS or "3G") were auctioned at record amounts. But their roll-out - initially expected in 2002 - has been taking place more slowly than originally planned, and the great expectations associated with their introduction contrast starkly with the difficulties facing the sector. It was only in 2004, for instance, that KPN started offering UMTS services.

Could it be considered just a stroke of bad luck only that Landis had focused its entire business on two sectors of the technology market that were effectively shrinking, or has management been over-optimistic about market opportunities? Fact is that management had taken a bet and was late in acting when things turned against expectations.

A final explanation of what went wrong is the way in which Landis acquired target companies. Because of the growth-strategy management believed they had to adopt, Landis went through a whole series of acquisitions, some smaller, others bigger. From the company's records¹¹ it can be deduced that an amount in excess of 417 million euro has been charged to Landis' equity in the years between 1999 and 2001 because of takeovers. Without doubt the number of entities that had to be integrated was higher than 10. As a rule, the preparation before taking over the many companies as they did was insufficient. In most cases the obvious minimum requirements that one has to satisfy before paying sizeable amounts for an acquisition target were not met. There are hardly any records indicating that proper market research had been done for any of the companies that were acquired. Financial due diligence was mostly limited to a quick scan. Maybe Landis management was not concerned about the acquisition at all, since most of it was paid in Landis shares. Like no one else they had inside knowledge about the intrinsic value of their own shares. Maybe it is an indicator for the fact that the management could not be called naïve.

Landis as an illustration of the relevance of Arendt's theory

From the case study about Landis parallels can be drawn between the theory that we have derived from studying Hannah Arendt and the way lying played a role in the demise of Landis.

First, when we look at action and mental freedom it is clear that Landis was the brainchild of a group of entrepreneurs who could imagine a future. Looking at growing markets, the management team tried to envisage what they had to do to address those business opportunities. As a consequence they began to transform Landis into the company that in their eyes was required to achieve their objectives. The strategic objective was, as the Landis 2000 annual report points out, 'to become the leading value added networking distributor throughout Europe.' The flotation on the Amsterdam stock exchange was necessary to facilitate the planned growth. The mental capacity to imagine a future that others do not see, is also reflected by a response of Mr. Paul Kuiken in an interview by Computable on 6 September 2000, after Landis lost a distribution contract with an important supplier (Cisco Systems). Despite the fact market conditions were visibly deteriorating, in this interview Mr. Kuiken was confident that Landis could double its revenues in the second half of the year 2000 while increasing profits by 50%.

The second element we look at is image-making. Appearing to be consistently successful is an important element when you want to make a company grow. To the outside world they created an image of a successfully managed and fast growing small private company that managed to transform itself into an international market leader company and that was led by people who were in control of their destiny. In order to gain and maintain

credibility in the eyes of shareholders, investors and competitors, Landis had to be able to realize their plans. Unwelcome facts that could harm the image were therefore carefully lied away. This can be illustrated by a number of serious and demonstrable misrepresentations, such as:

1) An e-mail has been found that was submitted by Mrs. Bonnema, the Landis controller, in which she instructs a subordinate from the consolidation department to do exactly this: 'redo all calculations but ensure that the totals do match, adjust the rest. Come what may I must arrive at euro 0.26 a share and an EBIT of 45 million Dutch guilders'.

2) The profits that were recorded for 1999 were off by at least 7.4 million euro. Instead of the reported 9.9 million the more accurate number should have been 2.5 million.

3) The loan referred to earlier was granted under the condition that Landis informed the bank syndicate about its financial situation. In reality, Landis had issued compliance certificates that were incorrectly stating that Landis complied with the ratios agreed with banks. In actual fact, Landis had never complied with any of the ratios.¹²

4) Landis raised most of euro 440 million on the capital market in the years 1998 to 2001. It can be concluded that Landis raised most of its capital based on misleading and too positive figures, because the guarantee capital as at the end of 2000 was not euro 111.6 million, as presented by Landis in its annual accounts for 2000, but at the most euro 53.4 million and therefore less than half the presented amount. Landis' solvency as at the end of 2000, expressed as the guarantee capital in proportion to the balance sheet total, was therefore not the presented 28.2% but at the most 15.9%.¹³

5) Most acquisitions have been wrongly recorded. Goodwill has in several cases been used (4U Group and Dennis Bergström) to make the results look prettier as in fact they were.

Thirdly, like any company with a growth strategy, Landis was keen on communicating future expectations that would allow attracting the financial means to finance the growth of the company. Significant in this respect is that Landis still announced publicly, on 31 October 2001, that it expected a profit for 2001 of at least EUR 0.40 a share, which would work out to a profit of EUR 19 million. It is also significant that the second internal annual balance for 2001, dated around February 2002, did indeed show a profit of over EUR 19 million. More than a month later, Landis announced a loss of EUR 52 million for 2001. (Seventeenth report etc. 2007: 31). It is difficult to ascertain from the outside whether a company's board believed itself in its communicated (unrealistic) expectations or whether the predictions were deliberate deceptive. Nevertheless, in the case of Landis the evidence of deliberate manipulation of data presented above indicates that Landis maximally used the leeway that opinions about the future offer in order to wait for a (increasingly implausible) turn in the market that would make these expectations come true. This behaviour comes with the risk of ethical fading. If one can get away with small transgressions (a euphemism for the word lies), chances are that the next lie is going to be a bigger one: 'one lie perpetuates many more'.

The fourth element has to do with too much confidence in theory and planning. The growth strategy that Landis had developed was based on such a plan; a model of the real

world in which Landis was operating. In the 1999 annual report Landis states that it wanted to become a leading supplier in the internet and telecoms domain. To pursue such a strategy several events needed to subsequently happen in order to be able to compete. If then important assumptions like the uptake and wide availability of 3G UMTS networks prove themselves wrong, management has to act. When the market conditions started to work against Landis, the entire strategy should have changed as a result. None of that happened. To illustrate, as late as in 2000 Landis completed a sizable acquisition of a network services company (Detron) paying 255 million for the goodwill of the company alone.

Only the last element of Arendt's theory does not seem particularly relevant in the case of Landis, as Landis' manipulation of data described above indicates that the misleading communication by Landis did not result from self deception and an unconscious adaption of facts to the own vision. Neither do we have indications that there was a kind of role division in the sense that the top of Landis was deliberately badly informed by the lower management levels in order to make Landis' communication to its stakeholders more convincing. An indication is that the deliberate manipulation of financial data was ordered by the higher levels of management. As a rule, forecasts were discarded by the CEO Mr. Paul Kuiken, who insisted that divisional management had to work differently to obtain higher revenues and 'there were no formal budgets. Budgeting was a game of negotiations between Kuiken en his managers'.^{14 15}

Roland Berger Strategy Consultants, a consulting firm that has studied many bankruptcies including that of Landis, nicely summarizes the various elements that we discussed above when it states: 'Companies that end up in a crisis in the manner of Landis are often neither able nor willing to take appropriate measures with the necessary openness and determination. Instead, the management confines itself to denying the facts or it applies a considerable amount of energy to preventing the crisis from becoming known. By means of reporting measures, the balance sheet can for the time being still be 'brightened up'. The fact that a crisis exists is only acknowledged when the results dramatically come to light, liquidity problems and the shareholders' equity has been almost entirely used up. At that point, there is hardly any room left for taking appropriate measures and the company is consequently no longer able to come out of the crisis on its own'.¹⁶

9 Conclusion

Literature has developed several explanations for lying in business beyond the obvious and straightforward explanation of personal gain, such as the role of corporate governance, weakness of accepted accounting principles, inappropriate executive compensation systems, badly founded corporate strategies or the cultural dominance of monetary success and the resulting tendency for social norms to lose their regulatory force. This article searches for more fundamental philosophical reasons that may explain why lying and business are intimately related. For this purpose, we use Hannah Arendt analysis of lying in politics. The advantage of using Arendt for this purpose is that she is well aware of the significance of

organizational and institutional milieu on communication. Therefore her philosophy is closely linked to the type of institutional analysis that is common in business ethics literature.

Based on two essays of Arendt on lying, we distill five reasons for lying in politics that also apply to business: politics and business is about action to change the world and therefore politicians as well as businessmen need the capacity to deny current reality; politics and business requires successful image-making and liars have the advantage to come up with plausible stories; political and business communication is more often about opinions than about facts, giving leeway to ignore uncomfortable signals; political and business decision processes increasingly make use of plans and models, but these techniques foster inflexibility in acknowledging the real facts; politicians and businessmen fall easily prey to self-deception, because one need to act as if the vision already materializes.

Our application of Arendt's philosophy of lying to business adds several additional insights to existing business literature. First, by showing the relevance of her analysis of lying in politics for business, we have been able to make clear that lying is not specific to business and its focus on money making alone. It makes clear that lapses in business ethics are not primarily the result of businessmen choosing profit over what is right. Since similar mechanisms are at work in the context of politics, lying must result from more general characteristics of human psychology and behavior that are stimulated and developed both in the context of the policy making process and the practice of business. This indicates that the reasons for lying are not personal, but rather systemic in nature. That means that such unethical behavior are not characteristic of a special group of unethical people, the bad apples, but that all operating in a similar context may be seduced to deception (Bazerman and Banaji, 2004). Instead of businessmen and politicians being categorically dishonest, the reason that trustfulness is not likely to be a virtue in politics and business is that both groups operate in a context in which the chances to fall into the trap of lying are higher than anywhere else. The relatively boundless freedom that politicians and businessmen have to develop their vision brings certain risks. If, under given circumstance, they are not careful, chances are that they lose touch with reality.

Second, although existing business literature on lying has already paid much attention to the importance of successful image-making and the role of impression management as well as, to a lesser extent, the risks of using business plans and the dangers of self-deception, there has been no attention to the more philosophical explanations that Arendt provides for lying in politics, namely that business is about action and that action requires the ability to deny the present reality and the vulnerability of contingent facts.

A third contribution of this paper is that Arendt's analysis of lying in politics deepens our insight into the interconnectedness of the various explanations of lying, as the five elements identified above are likely to enforce each other. In particular, since business is about changing the world, it requires a strong capacity to imagine future opportunities that are hidden to others. Furthermore, in order to gain the necessary support and financial means for their future ventures, it is inherent that managers must create an image that makes others trust their abilities to realize this future. This also necessitates that the businessman shows no

doubt and remains convinced of his or her dream, even if confronted with opposing facts and this may feed the inclination to self-deception. Because the support for the company's plans depends on its future potential, business communication is also necessarily more about opinions than about facts. But to present a coherent picture of future and to master the complex processes that make this future happen, the businessman also heavily depends on business plans that necessarily bypass other alternative opportunities and therefore help to stick at the dreams, even if these become less probable.

Our analysis therefore implies that lying and deception in business will be very persistent, as freedom to act, good image, communication of opinions, planning and self-deception are inherent to business and the ingrained mechanisms that lead to lying are hard to correct. Whatever the ethical views on lying and deception are, moral outrage will not make them go away. Moreover, because of the mental nature of lying, legal force can hardly get to grips with the phenomenon of lying and deception. Laws have been, and will continue to be, an ineffective means to increase the level of veracity of dealings of businessmen. That means that it will always be tempting for businessmen to make their way to successful business by lying and deception.

This does not mean that lying and the escalation of deception in an organization is inevitable. There are several moderators that can halt the deception from escalating in an organization. The first step to containing lying is to recognize this pervasiveness, for to deny the inherent tendencies to lying is to practice self-deception. We must be aware of the conditions that easily provide a stimulus to lying and be critical of our judgments and our motives driving our actions (Tenbrunsel and Messick, 2004). By confronting the tendency toward lying, we will be more likely to reduce its prevalence and prevent its escalation.

Furthermore, lying may not lead to further acts of deception if the organizational infrastructure makes detection probable or raises enough suspicion to deter further lying (Fleming and Zyglidopoulos, 2008). This depends on the alertness and receptivity of monitoring parties, the quality of the organization's control systems, ethical codes, but also on the presence of procedures that protect whistleblowers.

If all of these moderators fail to halt the escalation of deception, the increasing severity and pervasiveness of deception can transform it into an organization level phenomenon, at which point the only way to end it is organizational failure, as in the case of Madoff and Landis. As Fleming and Zyglidopoulos (2008) argue, when the organization has passed the tipping point in which more of the organization is deceptive than not, the further escalation of deception can kill what once were promising business organizations. As Arendt discusses, the contingent character of facts allows boundless possibilities for lying, but in the end this makes for self-defeat. If you have to remember one particular falsehood, then that may be possible with unwavering consistency. But if you have to adjust images and stories to ever-changing circumstances, chances are that you might get lost and confused. In the long run, manipulation of facts can therefore only be successful through radical destruction of the context. In Western society this is impossible, because of the role of the media providing access to material that politicians or businessmen eagerly try to hide. This means that in the

end the lies will always be discovered. Therefore, preventing or halting deception once it has occurred is over the long term a matter of organizational survival.

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¹ The Independent, Wednesday 31 December 2008

² Similar conditions are mentioned by Velasquez (1998) who distinguishes three conditions for deception: (1) the author must intend to have the audience believe something false; (2) the author must know it is false; (3) the author must knowingly do something that will lead the audience to believe the falsehood. These elements are also present in the definition of financial statement fraud by Rezaee (2005: 279): the deliberate attempt by corporations to deceive or mislead users of published financial statements, especially investors and creditors, by preparing and disseminating materially misstated financial statements.

³ For structural reasons, it will always be impossible to *prove*, in the strict sense, that someone has lied even if one can prove that he or she did not tell the truth. One will never be able to prove anything against the person who says, 'What I said is not true; I was wrong, to be sure, but I did not mean to deceive; I am in good faith' (Derrida, 2002: 34).

⁴ The element of trust is also central in the so-called broken trust theory of corporate fraud, see Choo and Tan, 2007). A tenet in this theory is that when executives commit fraud, they intentionally break the trust and betray shareholders.

⁵ A biological counterpart of what can be called 'unconscious' behavior can be found in many living species. Adaptation to the conditions of life, which Darwin's colleague Herbert Spencer considered basic to all ethical progress, can and does involve deception. That is a major theme of evolutionary studies today. Certain species flourishing now might be extinct if they had depended on truthfulness to increase and multiply (Campbell, 2001: 18).

⁶ Biological roots can also be found for image making. To flourish, living things must be able to make good use of the resources around them, and these resources include other organisms. If a creature cannot get what it wants from others by exercising force, it must do so by using guile. Some animals apply the so-called puppet master strategy of tinkering directly with another creature's brain (Smith, 2004: 30).

⁷ Typically, deception in advertising is achieved by omission rather than commission and by making statements that, though true when taken strictly literally, carry implications that are false (Barnes, 1994: 44).

⁸ This is different from rational of scientific truth that is based on the laws of science and that can therefore be reproduced.

⁹ One of the approaches to overcome the problem of inflexibility to unexpected changes in the environment is so-called contingency based business planning (Honig, 2004). This method provides tools that assist in the navigation and development of paths characterized by uncertainty and unpredictability.

¹⁰ According to Arendt, oddly enough, the President of the United States, allegedly the most powerful man of the most powerful country, is likely to be an ideal victim of complete manipulation: because of the immensity of his job he is surrounded with advisors who filter the information that reaches him.

¹¹ Obtained from published annual accounts years 1997 to 2000. 2001 from Landis' internally prepared statements

¹² Seventeenth report pursuant to section 73A of the bankruptcy act concerning the liquidation of Landis Group N.V.

¹³ Ibid.

¹⁴ It concerns a transcript from a discussion between an official committee of inquirers and Mrs. Jalili. Mrs. Jalili worked for Landis as an administrative clerk at the group administration department. She was interviewed as part of an official enquiry requested by the courts of Amsterdam. The inquiry was lead by mr. L.P. van den Blink and Prof. Dr. L. Traas and published on 5 may 2009, p. 171-172.

¹⁵ The COSO Report (Beasley et al, 1999) reveals that in the majority of financial fraud cases, the CEO and/or were associated with the financial fraud.

¹⁶ Freely translated from 'Stürmische Zeiten Meistern' by Roland Berger Strategy Consultants, 2003