

CROWN & MARKS EXECUTIVE SEARCH
The Americas • Europe/Middle East/Africa • Asia Pacific

THE INSIDER SUCCESSION TRAP

Adam Galinsky, Brian Gunia and Niro Sivanathan

New research reveals the danger in trying to fix failure with friends.

When bad decisions force business leaders to leave their jobs, organizations often rush to replace them with insiders, who are familiar with the original problem and the former leader. In times of turmoil, the choice seems natural and even obvious: Because insiders know the past, they should be less likely to repeat it. General Motors pointedly replaced [Rick Wagoner](#) as its chief executive officer with his protégé Fritz Henderson, a career GM employee. However, our research reveals that despite the natural inclination to opt for an insider with connections to the old boss, a failing leader is often better replaced with a completely unrelated outside party.

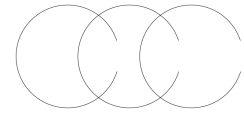
We conducted research that speaks to one of the most vexing problems that business leaders confront, a phenomenon called "escalation of commitment." Escalation occurs when a decision maker honors resources already invested in a particular course of action (what economists call "sunk costs") by allocating further resources to the same course of action--even though it is failing. In short, escalation of commitment essentially means throwing good money after bad.

Barry Staw, a psychologist at the [University of California](#) at Berkeley, has offered an elegant remedy to this ubiquitous quagmire: Have one individual make the initial investment decision, and have a different individual make the subsequent reinvestment decision. This partitioning of decision makers removes the initial individual's self-serving need to justify and defend previous investments, slackening the motivation to reinvest in failing courses of action.

Despite the simplicity of that remedy, our research, which will appear in an upcoming issue of *Journal of Experimental Social Psychology*, documents a systematic and destructive barrier: When new decision makers share a psychological connection with old decision makers, they tend to invest further in the failing programs of their predecessors, even to their own financial detriment. We have labelled this phenomenon "vicarious entrapment." The problem is that insiders are all but certain to share some connections with the leaders they replace. Escaping the clutches of past failure, we argue, depends not just on a physical separation, but also on a psychological separation of the two decision makers. In other words, insiders may be precisely the wrong people to fill a failed leader's shoes.

Our research looked at three separate organizational contexts: financial investments, personnel decisions and auctions. In each study, we constructed a situation in which a prior decision maker's choices had clearly gone awry. Our participants, acting as new, second decision makers, faced a choice between dedicating further resources to the failing course of action and dedicating the resources elsewhere. Their choice, we repeatedly found, depended on whether they shared a psychological connection with the prior decision maker.

Compared with the connections between lifelong colleagues like GM's Wagoner and Henderson, the connections in our studies were incredibly subtle. In one of our studies, new decision makers were simply told that they shared the same birthday month and school year as the previous decision maker. In other studies, we asked participants to try to empathize with their departed colleague. We compared these participants against those without a psychological connection, i.e., those with a different birthday, or baseline decision makers not asked to feel empathy. Even under these, the subtlest of conditions, psychologically connected decision makers made much greater investments in an old decision maker's losing decisions.



In one study, the participants learned that the prior decision maker had dug himself into an unwinnable auction. After taking over for this person, the only way participants could salvage the auction and prevent the bleeding of their own compensation was to stop bidding immediately. Those who ostensibly shared the same birthday lost a remarkable 285% more of their own money in the auction than those with a different birthday. In another study, the prior decision maker had invested research-and-development funds in one of two divisions, which had subsequently performed worse than the other. Participants asked to empathize with the original decision maker dedicated \$1.42 million, or 37%, more to the underperforming division than did baseline participants. Surprisingly, these effects held even when our participants faced a direct financial cost to themselves, and even among economics majors specifically trained in the irrationality of honoring sunk costs.

Our research offers a new twist in the debate about how to turn around failing enterprises, and it does so by building on decades of psychological evidence that suggests humans are social beings driven to find connections to others. Psychologists have long shown that people consistently seek out and share natural psychological connections, and once such connections form, people are more likely to cooperate and favor one another financially. Our research demonstrates that psychologically connected individuals are also more likely to perpetuate each other's failures, vicariously flushing away their own money and time.

For Fritz Henderson, who knew Rick Wagoner well and spent the early part of 2009 working around the clock with him to solve the company's problems, our research suggests that their tight connection alone could undermine Henderson's independence. It also implies that GM might have been better-served following **Ford Motor Company's** (F - news - people) lead: Ford appointed an outsider, Alan Mulally, from **Boeing** (BA - news - people), to turn around the company, with comparative success. Finally, it suggests that some members of the Obama administration may have understood this issue, at least intuitively, when they appointed a true outsider, former **AT&T** (T - news - people) executive Ed Whitacre, to chair GM's new board.

In general, our research implies that business organizations trying to shed failed legacies might want to follow Ford's example. Organizations hoping to escape past failures need to balance their preference for the familiarity and knowledge that an insider affords against the entrapment an insider may suffer. Although outsiders undoubtedly take longer to understand a problem, our research suggests that once they do, their psychological independence can limit their tendency to throw good money after bad.

Adam Galinsky is the Morris and Alice Kaplan Professor of Ethics and Decision in Management at Northwestern University's Kellogg School of Management. Brian Gunia is a doctoral candidate at Kellogg. Niro Sivanathan is an assistant professor of organizational behavior at [London Business School](#).