

To: Berkshire Hathaway Managers (“The All-Stars”)

From: Warren E. Buffett

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The five most dangerous words in business may be “Everybody else is doing it.” A lot of banks and insurance companies have suffered earnings disasters after relying on that rationale.

Even worse have been the consequences from using that phrase to justify the morality of proposed actions. More than 100 companies so far have been drawn into the stock option backdating scandal and the number is sure to go higher. My guess is that a great many of the people involved would not have behaved in the manner they did except for the fact that they felt others were doing so as well. The same goes for all of the accounting gimmicks to manipulate earnings – and deceive investors – that has taken place in recent years.

You would have been happy to have as an executor of your will or your son-in-law most of the people who engaged in these ill-conceived activities. But somewhere along the line they picked up the notion – perhaps suggested to them by their auditor or consultant – that a number of well-respected managers were engaging in such practices and therefore it must be OK to do so. It’s a seductive argument.

But it couldn’t be more wrong. In fact, every time you hear the phrase “Everybody else is doing it” it should raise a huge red flag. Why would somebody offer such a rationale for an act if there were a good reason available? Clearly the advocate harbors at least a small doubt about the act if he utilizes this verbal crutch.

So, at Berkshire, let’s start with what is legal, but always go on to what we would feel comfortable about being printed on the front page of our local paper, and never proceed forward simply on the basis of the fact that other people are doing it.

A final note: Somebody is doing something today at Berkshire that you and I would be unhappy about if we knew of it. That’s inevitable: We now employ well over 200,000 people and the chances of that number getting through the day without any bad behavior occurring is nil. But we can have a huge effect in minimizing such activities by jumping on anything immediately when there is the slightest odor of impropriety. Your attitude on such matters, expressed by behavior as well as words, will be the most important factor in how the culture of your business develops. And culture, more than rule books, determines how an organization behaves.

Thanks for your help on this. Berkshire’s reputation is in your hands.