

The dark side of organizations – the story of financial predation and inadequate regulations

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ABSTRACT

Numerous examples of financial fraud have emerged in the last twenty years in North America, Europe and East Asia, to name only a few geographical areas. The people at the helm of Enron, Worldcom, Bre-X and key figures such as Bernard Madoff and Sergei Aleynikov have in common that they have been at the heart of scandals that have shaken the markets, and most particularly, the confidence and trust the average investor has in the corporate system (see McKechnie and Howell, 1998).

We argue that there is an inherent drive for predation in any business venture; namely, predatory behaviors are inevitable, being a dramatic expression of human aggressive tendencies (McEllistrem, 2003). In the context of corporate fraud, we outline key characteristics that the main actors share and that disclose their dark predatory side. Not recognizing these key characteristics is opening the door to future examples of massive financial frauds that will further erode the average investor's confidence in the financial system. Hence, our research points to possible additional legislation that could be implemented to prevent further financial predatory behaviors and ensure that the market is fair towards financial agents and their clients so as to permit economic sustainability.

Key Words: Predatory marketing, financial predation, fraud, vulnerability, Mesly model.

INTRODUCTION

This paper discusses the concept of predation which is thought to affect all aspects of an organization, including its economic, marketing, legal, ethical and of course financial activities. Predation is a way of depicting organizations' behaviors in sharp contrast to the so-called pyramid of corporate social responsibility (Carroll, 1991).

Identifying financial predatory behaviors serves a role similar to that of a registry of sex offenders as found in Canada. It protects citizens while ensuring that civil rights and liberties are preserved for all.

However, not all financial experts are predators. For predation to take place there needs to be among other requirements a predator and a prey (a victim). In the examples that we are providing, the predators are invariably multi-million, if not multi-billion dollar companies, and preys are the average investor or financial institutions that represent a group of average investors. It seems reasonable to investigate unfair power relationships where one acts as a predator against the other, the prey: indeed, as pointed out by Courpasson (2000), domination permeates organizations and every sphere of human social action.

We will first discuss the concept of predation as it exists at the interpersonal level, since it is through interpersonal interactions that an individual decides to trust an investor with his money for which he has worked hard and often for many years. We present the Mesly model developed in this interpersonal context as well as the initial research done in the context of financial transactions (Mesly, 2010).

Next, we give a few examples of major company frauds that have caught the public's attention to exemplify the fact that predation, as defined by the Mesly model, exists as well at the corporate level. In other words, we point to the dark side of organizations and highlight their "insincerity" (Debeljak, Krkac, and Banks, 2011).

In the third section, we pinpoint key characteristics that seem to be common among corporate bandits and relate them to the Mesly model.

We conclude by showing that our analysis could lead the way to the creation of tougher laws that take into account not only the overall act of fraud, but also its intrinsic predatory mechanisms: punishment would be attributed based on the number and gravity of steps taken in the act of predation, thus forming a stronger deterrent for corporate thieves. The current legal system (at least in North America) seems to be short of a scale devising predatory behaviors into levels of harm, each of which having its own punishment. In proposing such a scale, we hope that we will participate in discouraging potential bandits from destroying lives and ruining organizations, keeping in mind this paper is essentially theoretical.

WHAT IS FINANCIAL PREDATION?

The economic, sales and marketing literature is relatively poor on the concept of predation. The concept of marketing predation has been recognized in the state of Maine

which attempted to pass an act on it in 2009 – The Act to prevent predatory marketing practices against minors¹.

Early at the dawn of last century, Thorsten Veblen introduced the concept of economic predation. Predation was first legally recognized in the United States with the Sherman Anti-Trust Act on July 2, 1890 (completed by the Clayton Antitrust Act of 1914 and the Sarbanes-Oxley Act of 2002) which prohibits monopolies and collusion. In Canada, the Consumer Protection Act is one example of a legal safeguard against economic and marketing predators. In general, economic competition must be based on quality of products and business sense, and should be based on a fair usage of the four marketing P's 1) products (innovation, design, information); 2) place (distribution channels controls); 3) promotion (an enterprise cannot promote its products in a way that damages its competitors or that upsets the market, by advertising a product it does currently does not have, as an example); and 4) price (dumping, certain types of price wars, etc. are to be avoided).

The term predation or financial predation is seldom used in marketing but some similar terminology is found in contexts other than ethology. Early in the 1900's, Freud introduces the concept of a death drive, and later Jung, also a psychiatrist, elaborated on a quasi primal social unconscious (1964); Morgan and Hunt (1994) use the term predation once – a rare example in the marketing literature. Researchers have however acknowledged a tendency towards opportunism (Williamson, 1975) and a dark side to human behavior (Grayson and Ambler, 1999). Addis and Holbrook (2001) refer to the dark side of consumption, Michon and Chebat (2008) to the consumer dark box, and Zaltman (2004) discusses how a car salesperson is often perceived as a predator. In essence, the notion of predatory behavior is not estranged to the Western culture, nor is it totally exempt from business scientific literature or from business terminology (e.g. sharks, bull and bear markets).

However, despite the fact that numerous examples point out to the devastating effect of financial predation on millions of citizens (see Hellwig 2009 and Rajan, 2010), including recently in 2008 with what was dubbed as predatory mortgages, very little research has been done on the subject, especially with respect to the relationship between the people at the core of such schemes: predators and preys.

It thus seems appropriate to introduce it in the present article and to try bringing a definition that will allow us to better understand how organizations develop a dark side of their own. Organizations are, after all, run by individuals, some of whom have incentives (such as bonuses) to maximize profits regardless of the impact of their actions on others.

Predation between a seller and a buyer

Following on a sales situation put forward by Zaltman (2004) whereby a salesperson could be perceived as a predator, we can elaborate and propose that both sellers and buyers experience some unease towards each other: “is the sales person honest or is he trying to sell me a lemon (a question somehow asked by 2001 Nobel Memorial Prize in

¹ http://www.mainelegislature.org/legis/bills/bills_124th/chappdfs/PUBLIC230.pdf.

Economic Sciences winner Akerlof in his paper *The Market for Lemons*)? Has the sales person (for example, a financial broker) developed a strategy to catch me by surprise, leaving me with no practical recourse to defend myself should I get trapped?" Or in a car showroom: "is this buyer only here to kick tires, to try our new Porsche with no real intention or actual mean of buying it? Am I losing a future sale to a real buyer by dealing with the current client who doesn't have the profile of a wealthy individual?"

By putting up defences, both sellers and buyers try to limit their losses, a behavior reminiscent of military tactics (Wolfson and Shabahang, 1991), yet they run the risk of limiting their interaction. In their search for solutions to their own needs, they thus somewhat alter the course of the transaction which could run otherwise rather smoothly. Making sure buyers and sellers don't get trapped into a negative scheme is a legitimate concern. The fact that market agents perceive predation, whether it is real or only imagined, has a dual function: first, it helps them – sellers or buyers, to avoid wasting their valuable time and resources; yet, on the other hand, it limits their capacity to reach a mutually-beneficial transaction that is at its full potential. In other words, by putting up defences, sometimes unnecessarily, market agents restrain their capacity to collect valuable information while electing to focus on limited critical elements. By protecting their negotiation positions, they feel they are less vulnerable (Pietrzak, Downey and Ayduk, 2005).

It is important to note that both sellers and buyers adapt to each others (Brennan, Turnbull and Wilson, 2003) and experience some level of vulnerability. Of course, a buyer feels he can be the victim of a conspicuous seller because of an asymmetry of information that puts him at a disadvantage (the seller knows the car is a lemon). But a seller is also aware that an unhappy buyer can complain formally or informally, file a lawsuit, go to his employer, boycott the products (Cissé-Depardon and N'Goala, 2009), use social networks on Internet to bad mouth him, etc. Every seller knows he is vulnerable (Johnston and Marshall, 2006).

In summary, while predation involves a predator and a prey, in an interpersonal interaction between a seller and a buyer, both feel they are potential preys and both are concerned that they can suffer harm ("harmful action" in the words of Wangenheim and Bayón, 2007). In the organizational framework, a salesperson enjoys certain advantages (such as the firm's reputation) to position himself as a predator in a conniving way, a fact that the prey (the victim) discovers later on, always with an element of surprise – Madoff, for example, borrowed from his friend Carl Shapiro (50 years of friendship) US\$ 250 million in the ultimate days prior to his downfall (Sander, 2009).

The key differences between predation and opportunism as defined by Williamson (1975, 1983) is that predation is not bound by contracts; contracts replace trust as a binding mechanism between trading parties that remain transactional in nature (see Malhotra and Murnighan, 2002). In the case of predation, the bond is interpersonal and trust (often blind trust) is secured by the predator that will then use it against the victim, causing him a loss... by surprise.

A history of predation

Predation is not new to the corporate world and to humanity at large. Mercantilism, slavery (the first slavery code dates back 4000 years ago – the Hammurabi code in Babylonia), stings, sexual predation, free-riding, all have existed for hundreds of years, if not thousands of years in some form or the other. The American cinematographic industry is based on the dynamic between predators and preys as can be seen in movies such as “Jaws”, “Jason”, or roles such as “Hannibal”, etc. (see the works of Pierre Bourdieu on cultural violence). Popular psyche is often mesmerized by the capacity of a prey to turn around and to become a predator, with a new pursuit: that of destroying the original predator.

Thus, predation seems to be a cultural element that persists over time, across generations and within the structure of societies; therefore, of organizations.

Predation: a necessary evil?

With predatory behaviors causing an endless number of victims and a huge financial cost to societies that must try to regulate and punish corporate fraud, one can wonder what the use of predation is. In nature, predation is essential: a population of rabbits would explode without the presence of lynxes to control it (see Lorenz and Leyhausen, 1973).

Lewicki, McAllister and Bies (1998 p. 452) present the following argument: “Our analysis points to the centrality of distrust as a foundational requirement for effective organization.” Distrust would prevent such social phenomenon as groupthink which can have perverse effects. Medina et al. (2005) consider that conflict is inherent to any relation. In the same line of thoughts, Petty, Unnava and Strathman (1991) argue that weighting the pros and cons allows one to better protect oneself against unforeseen events. Williamson and Masten (1999) consider that contracts help reduce opportunism, especially in the case of mutual dependence.

In summary, conflicts are inevitable and can be measured (Reid et al. 2004). From a predatory perspective, conflicts usually arise when one thinks or believes the other one is there to cause him harm, by surprise. As mentioned earlier, the lack of literature on the phenomenon of predation forces us to propose a definition that includes trust, cooperation and a sense of win-win which when broken, lead to conflict and to more perceived predation. This point of view is the basis of the research presented below.

One can imagine that an average investor is not dependent upon a financial broker per se; neither the investor nor his broker, form a production line involving JIT efforts for example. Instead, the relationship is strategically based on trust, a sense of equilibrium, that is, an equal share of benefits and costs involved in dealing and negotiating (Lengnick-Hall and Wolff, 1999) and some level of cooperation. The broker gives some advice to the buyer, does him some favours, and in turn the buyer provides the seller with its investor’s profile, his ambitions, etc. According to Porter (1991, p. 97), “[...] the task of strategy is to maintain a dynamic, not a static balance”; that is, buyer and seller maintain a dynamic relationship whereby each one needs to observe the other to ensure he does not suffer any losses and that he, in the context of predation, doesn’t get caught by surprise.

Without some antennas that are up to detect if there is a potential predator in front of him, the buyer is likely to fall easily into the broker's paws, whether these paws are candid mistakes (a bad judgment on the tendency of the market) or a lure to catch the victim and suck his money out. Cases like Earl Jones, who used his brother's money for his own benefits for years in a Ponzi scheme lead us to believe that these anti-predators antennas are essential, precisely because predation is a natural force of human (and animal) behavior.

THE MESLY MODEL

Mesly (2010) developed a model based on the works of Anderson & Narus (1990) and Mayer, Davis, and Schoorman (1995), which in its fundamental form, is presented as follows (See Figure 1 in Appendix).

We now endeavour to review this model by looking at each construct and each link between the constructs. Perceived predation refers to the fact that sellers and buyers try to detect whether the other party of the interactional dyad has a hidden agenda (Palmer, Lindgreen and Vanhamme, 2005). Is the seller trying to lock the buyer into a deal which would be costly to get out of? He is acting as a free rider? On this point, Campbell and Kirmani (2000) make the convincing argument that the seller is perceived as the one having an ulterior persuasion motive.

This fear of the other (in the case of the seller) affects directly the construct of trust. This is because the fear is based on one's own sense of vulnerability. Trust has been defined as the willingness to make oneself's vulnerable with the hope that the other party will behave to meet his moral and ethical obligations (see Bell, Oppenheimer and Bastien, 2002 and Bendor and Swistak, 2001). Thus, it is fair to say that perceived predation affects first and foremost the level of trust one grants the other.

Numerous studies have found a strong link between trust and cooperation (most particularly Anderson and Narus, 1990; Morgan and Hunt, 1994). In their meta-analysis, Palmatier et al. (2006), conclude that 90 % of the studies made on trust and cooperation confirm an intense link between the two constructs. Hence, the Mesly model takes into account the fact that at some point during the interaction between a seller and a buyer, trust and cooperation work hand in hand: "I trust the other, which leads him and me to operate, and the more cooperation there is the more trusty we both become towards each other."

The Mesly model includes the equilibrium construct as a partial mediating variable between trust and cooperation (see Mesly, 2010 for several researches corroborating this argument). That is, sellers and buyers will trust each other and operate with each other; if there are some feelings of equal treatment, of win-win, the more the better. One can build the relationship without committing to such win-win situation but favours the presence of some sense of reciprocity and equity (see Gneezy, 2005).

All in all, trust, cooperation and equilibrium participate in the formation of a certain relationship atmosphere (see Grönroos, 1994, 1996, 2004), which can be positive (if there is little perceived predation), negative (if there is a certain amount of perceived predation, whether this reflects the reality or whether it is merely the perception of the beholder that prevails), or even destructive (as in the case of violence). Jap, Manolis and Weitz consider (1999) that a mediocre relationship is emblematic of conflict, which can be manifested by

hostility, frustration, anger, verbal disagreement or interference, leading to disengagement and lack of trust.

Of course, the more trust one devotes to the other, the more vulnerable one becomes, as others get to know each other in their strengths and weaknesses. It can be seen that the predator is the one with a hidden agenda, who goes undetected, who builds on blind trust and who creates a pleasant interactional atmosphere, with the selfish hidden goal of benefiting from the prey's vulnerabilities.

In summary, perceived predation is the fact that one market agent (or both agents) of the dyad believes that the other has malicious intentions of benefiting from his naive stance. It necessarily takes five conditions to claim that there is emergence of predation: 1) a predator, 2) a prey, 3) a tool or weapon (for example asymmetric information), 4) a loss, and 5) an element of surprise (Mesly, 2010, 2010a).

The Mesly model in the organizational setting

While the Mesly model has originally been developed and tested at the interpersonal level (where the bond to the individual is stronger than to the organization; see Brooks and Rose, 2008), it does not preclude us from arguing that it can be equally valid in organizational settings. In fact, Coviello and Brodie (2001) and Addis and Holbrook (2001) argue that the conclusions reached in B2B settings could well apply to interpersonal interactions.

In the case of organizations, it remains to be seen whether they have a dark side, which we will endeavour to exemplify further below. However, it can be noted that the theory of predation as explained in this paper is currently being used in a legal case against Amway, with independent entrepreneurs (IE) having commenced legal action against Amway Canada on the basis that they were victimized by the company's multi-level marketing scheme (Canadian Federal Court- Trial Division, file No.: T-1754-09).

Using the Mesly model, we can hypothesize that organizations will try to go undetected as far as their Machiavellian intentions are concerned, that they will attempt to instil trust on the part of the general population, and especially on the part of the average investor, that they will show some level of cooperation in meeting directly or indirectly government regulations, and that they will position themselves on the market as winners, those who promote a positive atmosphere driven by return on investments or possibilities of earning substantial profits. Some financial organizations, it is alleged, may have a hidden agenda by which they would benefit by abusing the naive investors while attempting to dupe regulatory agencies.

In the case discussed below, a potential home buyer is so certain that her real estate agent is trying to take advantage of her that she has the transaction to buy the house of her dreams cancelled using false excuses.

A RELATION TURNED SOUR

During the years 2008 and 2009, several researches were conducted on the theme of predation based of semi-structured interviews (Mesly 2010). Two related sectors were of interest: the banking sector with the financing of mortgages to would-be home owners, and

the real estate sector. Both activities entail large investments that affect clients for years, the purchase of a home being one of the largest expense an individual does during a lifetime.

Several market agents (mortgage brokers, real estate agents – one of which being a top 10 in Canada) and their customers were met individually to discuss their relationships with their business contacts. Meeting both sides of a business dyad is common practice in research and recommended for this kind of investigation (see Ellram and Hendrick, 1995), given in particular that people are not likely to fill up a quantitative questionnaire that addresses predation directly. Wieseke et al. mention (2008, p.324): “Also commonly found is the “key informant” approach, where dyads with one subject on each level are taken into account [...] Therefore, obtaining data from multiple informants has been recommended as superior to such an approach.”

A grid was prepared to direct the conversation towards the concepts of trust, cooperation and win-win. The term “predation” was never mentioned by us in order to avoid creating a negative atmosphere during interviews. The market agents were chosen randomly, having manifested their interest in participating in the research following pre-screening telephone calls in the Eastern Townships (Canada) region. The main researcher received an ethic certificate from the Université de Sherbrooke, Canada.

In the case of the mortgage broker, the relationships with the clients that were met by us were harmonious, as were the relationships between the performing real estate agent (top 10) and her clients. However, in the case of one real estate agent working for another real estate company, one particular relationship with a client turned sour. That particular real estate agent refused to meet us and did not disclose her problems to her employer. The employer was met and was under the impression that all of his six real estate agents were performing well, bringing with him one of his clients as a proof of his assertion (a client which turned out to be a friend of many years).

The unsatisfied customer was reluctant to speak to us at first. In fact, in a sample of 250 clients from various sectors of activity met during that two-year research, only a handful of those who were disgruntled accepted to talk. It is possible that it brought them bad memories, changed their mood or else that they felt afraid of possible retaliation from other market agents. In the case of the unsatisfied customer, the entire relationship with the real estate agent was found to be painful.

After several discussions lasting approximately 45 minutes each, the unsatisfied customer accepted to confide in us more specifically. She explained that she had bought a house (“the house of my dreams”) but became so insecure and disgruntled with the real estate agent that she called her bank manager and asked him to pretend she did not have enough credit to buy the coveted home (which was untrue). The transaction was thus nullified.

Preliminary results

Asked about her change of heart, the unsatisfied customer explained that it was solely due to the attitude of the real estate agent towards her during the visit of the house and after the offer was made, and not by anything related to the house itself (for example, finding out that it required repairs).

The main argument expressed by the unsatisfied customer was that the real estate showed a different aspect of herself when they visited the dream home. Realizing she was keenly interested in the home, the agent wanted to speed up the purchase process so as “to collect her real estate commission as soon as possible.” It became clear that the real estate had operated a behavioral shift: she had decided to place her interest first, ahead of that of her client. To the latter, this realization came as somewhat of a “bad surprise” (a term also found in the literature – see Vanhamme, 2008, p. 4).

This preliminary research pointed towards the Mesly model, showing how perceived predation could and would either break or seriously deteriorate elements of trust and cooperation between two mutually-dependent market agents (agent and buyer). It also showed how a market agent participated in creating a negative image for the real estate company she worked for. Dark sides of organizations are the makings of the very people that work in them.

The next section delves into some recent examples of corporate fraud as a way of exemplifying further how financial predation takes place between sellers and buyers. It relies heavily on legal documents retrieved from different Court cases.

OTHER EXAMPLES OF THE DARK SIDES OF ORGANIZATIONS

The cases of Bre-X (Indonesia - Canada, 1989-2002), Barings (Singapore, 1995); Enviromondial (Québec, Canada 2000); Norbourg (Québec, Canada 2005 – see Munger, 2007, Laprade, 2009); Aleynikov-Goldman Sachs (New York, 2007 - onwards) can be used to exemplify how predatory behaviors come about. Predatory behaviors appear over the years, across continents, in different cultural contexts and have produced various kinds of victims (elderly, young, executives, governments, etc.).

Bre-X (1989-2002): a case of deceit

Montréal-born David Walsh founded Bre-X in 1989 and declared personal bankruptcy in 1992, avoiding the payment of C\$40,000 in debts. In 1993, he managed to buy the so-called Busang site in Indonesia; his Philippine mine manager believed at the time that the site contained 2 million ounces of gold. These estimations kept rising over the years, going from 2 to 30 (in 1995), to 60 (in 1996), and to 70 million ounces at the beginning of 1997, pushing Bre-X’s market value to a whopping 6 billion dollars.

Companies fought to become partners with Bre-X, including Barrick Gold (US\$1.2 billion in revenues in 1997) and Freeport-McMoRan Copper & Gold (US\$2.2 billion in 2003).

However, early in 1997, Freeport found out, after technical analyses were performed, that the core Busan samples had been salted with gold (a process called supergene gold). This turned into the largest scandal in Canadian history and the largest mining fraud of all time. Billions of dollars were lost. Walsh had stacked away US\$25 million prior to the announcement, and his associate, John Felderhof, US\$84 million. Among the victims were the Ontario Municipal Employees Retirement Board (loss of US\$45 million) and numerous small investors.

Everyone was caught by surprise, including Walsh and Federholf who claimed to have been victims themselves. Why were mining samples not subject to more scrutiny over the four-year period that the entire episode lasted? It is a question worth asking. This case demonstrates that by not having the “necessary antennas” up and active, investors found themselves in financial trouble after years of hopes for substantial profits.

Barings (1995): a case of blind trust

On February 23, 1995, Barings head office in London, UK realized that its Singapore employee and trading star, Nicholas Leeson, had generated US\$ 1.3 billion in losses, twice the amount available to the bank. The fallout cost it an additional US\$ 100 million.

Nicholas Leeson occupied both front and back desks at Barings' Singapore office, allowing him to hide his deals performed on the derivative markets. His notorious 88888 account (8 was chosen because it is a lucky number in China) was originally opened to hide a mistake made by one of the Singapore employees. It became a shelter to hide a mounting debt as Leeson's bets on the derivatives and Nikkei index markets turned out to be vastly erroneous.

Barings, England's oldest bank and which had HM the Queen as client, was forced into bankruptcy. Was there anyone at Barings' UK head office willing to question (not having trust in) a 28-year old who had not completed his math courses but who was handling hundreds of millions of dollars in market transactions? History shows that the answer is “no”.

Enviromondial (2000): from green to red

Another exemplifying case concerns the energy supply sector in Québec, Canada. Québec had been planning ahead with the development of its energy sources, which had changed over time, as shown in Table 1, with a declining emphasis on petroleum (Appendix).

Stevens Demers illegally sold shares in his company claiming to be able to supply green energy based on a new patented technology. While he had been found guilty of illegal trades on a few occasions over the years, that didn't stop him from continuing to sell shares, since the punishments received (measured in the thousands of dollars only) were not a strong enough deterrent. He collected millions of dollars from naive investors who believed in green technologies. His behavior appears to be typical of antisocial individuals: “Low fear of punishment and physiological underactivity may predispose them to seek out stimulation or take risks and may explain poor (social) conditioning and socialization.” (Van Goozen et al., 2000, p. 1444-1445).

In the end, the green project turned into red ink: hundreds of hopeful investors lost (were robbed of) their life savings. This case shows that poor deterrents invite those people committing fraud to continue their activities.

Norboung (2005): When luck is on one's side

After completing his studies at the Université de Sherbrooke in Canada, Vincent Lacroix worked for the powerful Caisse de dépôt et placement du Québec (CDPQ), worth over C\$140 billion.

In the mid-1990s, he obtained from Desjardins (another mighty financial group) the rights to manage an investment fund through his newly-created company, Norboung.

He used money entrusted into his care to live a lavish lifestyle, buying properties (for example, the Auberge l'Étoile-sur-le-Lac worth C\$2.6M) and flying abroad to fancy resorts. In the end, in just a few years, 9200 investors were duped and more than C\$130 million disappeared. Vincent Lacroix, it is believed, stacked away C\$35 million in two foreign banks: one in the Cayman Islands and one in the Bahamas.

According to Judge Claude Leblond from the Quebec Court who headed the case against Lacroix²: “These were premeditated and deliberate actions that can be divided into four sections: (i) the creation of the Groupe Norboung and the acquisitions of various companies, (ii) the falsification and transmission of erroneous documents to investors and regulatory authorities, (iii), the manipulation of over 10000 banking transactions between his various companies in order to blur the flow of money, and (iv) the use of this money for his own (selfish) advantage.”

This assessment by judge Leblond seems right to the point.

Aleynikov vs. Goldman Sachs (2007): Who exactly was the predator?

Aleynikov transferred 32 of 1,024 MG (i.e. 3 %) of an old computer software program belonging to his employer, Goldman Sachs, after work hours on June 1st, 4th and 5th, 2009 (June 5th being his last day of employment).

Goldman Sachs acquired the software in 1999 when it bought Hull Trading Company for US\$500 million. The program enabled the company to make ultra-rapid transactions and to deal with large volumes of trades before other brokers had time to react to changes in the market.

However, a few questions were raised following a lawsuit launched by Goldman Sachs against Aleynikov. He was known as a computer genius. Why would he contend himself with 32 MG of information that came from a software program dating back to 1999? Why did Goldman Sachs not install a firewall against Aleynikov, knowing as they did a month earlier that he was going to join a potential competitor?

Aleynikov claimed he downloaded the 32 MG by mistake. Is this credible? Or was he set up to download this information so that he could then be sued, thus limiting his ability to find employment elsewhere in the future? These questions arose as Goldman Sachs found itself the target of numerous accusations: in July 2009, the Rolling Stone magazine published an article by Matt Taibbi³ arguing that Goldman Sachs had been

² Source: Lacroix c. Autorités des marchés financiers, 2008 QCCS 2998 (CanLII); Date: 2008-07-08
Dossier: 500-36-004600-089 ; Références parallèles: [2008] R.J.Q. 1884 • 59 C.R. (6e) 61
URL: <http://www.canlii.org/fr/qc/qccs/doc/2008/2008qccs2998/2008qccs2998.html> ; free translation.

³ Taibbi, M. (2009). La grande machine à faire des bulles. *Rolling Stone*, July 13, 2009.

manoeuvring the markets to benefit from both its ups and downs for years. On April 16, 2010, the U.S. Securities and Exchange Commission (SEC) accused Goldman Sachs of fraud for its implication in the 2008 subprime loans and mortgages collapse.

This case shows that facts and events must be regarded from different angles to determine the extent of possible predation.

Summary of corporate predation

As can be seen from the above examples of corporate fraud, each reveals at least one fact of predation as defined in this paper. The surprise element (which was noted by the unsatisfied client in the aborted real estate transaction) is obvious in the Bre-X case; blind trust seems to explain the fall of Barings; the abuse of an individual's vulnerability is exemplified by the Enviromondial case, in that the investors dreaming of green energy were easily lured by Stevens Demers' sales pitch; the losses to the investors in the Norbourg case were front page news; the entire act of predation itself (setting a trap with the objective of destroying the other party) seems obvious in the case of Goldman Sachs vs. Aleynikov.

Therefore, it seems fair to suggest that the definition of predation as developed in the context of interpersonal dyads (Mesly, 2010a) also applies to the corporate world. Organizations do indeed have a dark side: at times, they plan a series of strategic actions to their own benefit and which cost their victims dearly, catching them by surprise, making use of blind trust to secure the relationship and then exploiting their prey's vulnerabilities.

RESULTS: SOME COMMON CHARACTERISTICS FOUND IN THE CASES OF CORPORATE PREDATION

The above-mentioned cases, as well as others such as the Bernard Madoff's case, have some common characteristics that can help researchers and governments better understand the dark side of organizations, that is, their inner predatory nature (forthcoming, Mesly, January 2012). These characteristics are as follows: 1) an opportunity to commit a predatory act; 2) withdrawal (or else defection) of some key players at some point along the predatory path; 3) a lucky star ; (4) the use of complexity to baffle the prey or regulatory bodies; 5) a privileged social network; 6) blind trust; 7) the presence of ghost accounts and partners; 8) tied hands; and finally 9) an appetite for financial gain, regardless of the costs sustained by the victims⁴.

Borrowing from the science of criminology, we propose that these characteristics be grouped into three clusters: the opportunity (characteristics #1, #3, and #5); the tool (#4, #6, and #7) and the motive (the gain, #9). We suggest adding "obstacle" as another cluster defining organizational predation as it constitutes a challenge that energizes the predator (#2, #8). These findings are summarized in Table 2 and could constitute a possible scale to determine the extent of punishment (Appendix).

The following sub-sections discuss each of these characteristics using the examples discussed earlier, as well as other examples taken from the history of corporate fraud.

⁴ Further research (Mesly, 2012) point to 12 characteristics in total.

The opportunity

The opportunity to commit the act of predation is composed of three characteristics: 1) the opportunity itself; 2) the lucky star; and 3) a privileged social network.

As regards Leeson's case (Barings), the 88888 account was originally created to cover some "minor" losses resulting from a colleague's trading activity. As it was left undetected, it became the opportunity for Leeson to hide his own wrong-doings. Similarly, Lacroix, of Norbourg, has argued that he initially created false documents in order to hide a loss of C\$300,000 which he claimed he intended to promptly pay back. Mr. Iguchi, who was working at Daiwa during the 1990s, endeavoured to hide a US\$50M mistake which over the course of the years led to losses reaching a billion dollars. Like Leeson, he occupied both front and back offices, which allowed him to cover his tracks. The dual office was his window of opportunity.

A lucky star has shone on many financial actors: Lacroix received one million dollars from the Québec government as a start-up fund, followed by a lucrative contract from Desjardins, with his credibility backed by very few credentials. Aleynikov ended up with a dreamed well-paid job; Goldman Sachs was rescued from bankruptcy by the US government while its competitors were not (example: Lehman Brothers); Demers obtained the right to a green patent developed by the prestigious Polytechnique school in Montréal.

The likelihood for success of these financiers' on-going endeavours was limited, but somehow, things turned out to their advantage, giving them a sense of power and invincibility, a trait that may be necessary for predators to act.

All of the people and companies that were engaged in some form of fraud developed a social network that protected them, at least for some time.

Many of the professionals who worked at Enron were in fact former employees of Arthur Andersen's. Thus, Andersen's experts were placed in the difficult (if not conflicting) role of evaluating former colleagues. Kenneth Lay (founder and president of Enron) was known to be a friend of the Bush family.

Goldman Sachs has been tapping into the top financial positions in the USA for years: Robert Rubin (26 years with Goldman Sachs, whose company, Citigroup he managed, received US\$300 billion from the Paulson plan). As it turned out, Henry Paulson was himself was a former president and director of Goldman Sachs and former Treasury Secretary for the USA. Goldman Sachs also attracts high profile individuals: Otmar Issing, who was chief economist at the European Central Bank; Ed Liddy (who arranged for AIG to receive US\$13 billion in the Paulson rescue plan, dollars which were in fact due to Goldman Sachs).

Bernard Madoff is a case in point: he was on numerous committees and boards: the National Association of Securities Dealers (NASD), NASDAQ; the Securities Industry Association; Yeshiva University, to name a few. He was also a member of the New York City Center and of two prestigious golf courses (Glen Oaks New York and Palm Beach Florida). His niece is married to Eric Swanson, former associate director for conformity at SEC.

We do not claim any or all of these people or companies are predators; we outline the fact that some have been found guilty of or are currently under investigation for fraud

and recognize the mere fact that they all exhibit a substantial network that helps them navigating the financial world in a well-protected manner.

The tool (weapon)

The tools used by economic predators seem to fall into three categories: 1) the use of complexity to baffle investors and investigators; 2) the recourse to blind trust granted by consumers and legal authorities; and 3) the use of ghost accounts and partners.

There were an overwhelming number of procedures for the people at Barings' head office, who could not, by Leeson's own account, understand his sophisticated transactions. Similarly, there was a labyrinth of companies at Norbourg; 30000 transactions were performed by Iguchi (Daiwa); 3000 Special Purpose Entities (or SPEs) were created at Enron. It took more than 600 people and 18 months to try to identify and correct accounting irregularities found at the once all-powerful computer network giant Nortel in 2002-2003.

Complexity is used by financial predators to blur the vision of those who are invited to trust them or are supposed to scrutinize them – i.e., investors and regulators. Through such complexity, people are baffled, confused, or give up searching further into the (cruel) reality.

Madoff is again a perfect example of this characteristic. Investors would hand over a million dollars (the entry fee) without raising an eyebrow. His friend of 50 years, Carl Shapiro, lent him US\$250 million just days before the magnitude of Madoff's financial abuse was revealed to the public.

Even clear warning signs have been insufficient to shed light on the dark side of organizations and some of the individuals involved in them. An article in Barron's (2001) seriously questioned Madoff's pretensions⁵ as far as investments and profits were concerned. This was followed by an infamous letter written by Harry Markopoulos (2005) which contained no less than 29 precise, well-articulated questions about Madoff's methods. Markopoulos convincingly showed that by all accounts, Madoff's numbers did not add up. Similarly, the Québec Finance et Investissement journal published in June 2004 a document that outlined the incongruities contained in the Norbourg operations⁶; yet, it took years before Lacroix was caught. On August 18, 2000, Enron was qualified by Andersen as "maximum risk", yet Andersen did not respond as it should have had. Mr. Threlkeld raised a flag concerning Yasuo Hamanaka, the copper guru of the 1990s, who hid from his employer Sumitomo some US\$2.6 billion in losses over ten years. Charles Grose rang the warning bell against Richard Pascuzzi, who managed to darken the up-to-then impeccable name of the Prudential (the Bache scandal, in the 1990s).

The ability of predators to lead their victims blindfolded into their dark room, where they empty their pockets without feelings of guilt or remorse appears to be an ingredient of their modus operandi.

Economic and marketing predators use organizations in ways that serve their secret interests. Leeson had a refuge account. Lacroix had a secret office in La Prairie, south of Montréal, and was using an obscure external accounting firm composed of a single individual, as did Madoff who relied for his entire \$50 billion business on an accounting

⁵ <http://online.barrons.com/article/SB989019667829349012.html>

⁶ <http://www.finance-investissement.com/nouvelles/le-myst-re-norbourg/a/3804>

firm composed of two low-profile individuals. Ghosts are everywhere in the organizational dark world. Joseph Jett's accounting books did not tell the whole truth, which led to a black hole of US\$210 million in the kingdom of GE, whose CEO was none other than Jack Welsh, named CEO of the 20th century.

The motive

Motive is perhaps the most obvious element of predatory behavior. Whether for the purpose of power or self-esteem, in the end, it all comes down to dollars and cents, with expectations of earning more money either immediately or in the near future.

The obstacles

As previously mentioned, in traditional criminology, once a body has been discovered, one looks for the opportunity, the weapon(s), and the motive. Once these three elements are identified, accusations can be made that will hold reasonable weight in a court of law.

In the case of organizations and the people that are ultimately responsible for their demise, it is appropriate to add obstacles as an element of predation. Based on a review of corporate fraud, predators seem to face two obstacles that invigorate them and give them a boost in their drive toward success: the withdrawal of key players and tied hands.

Vincent Lacroix saw two of his original partners leave him (Mario Lavallée and Jean Bourgeois); on June 21, 2005, his closest associate and partner in crime, Mr. Asselin, changed sides and began cooperating with the legal authorities. Stevens Demers became the sole proprietor of his "green company" after the four other founders left. The Goldmans broke away from the Sachs at the turn of the 20th century. Arthur Andersen and Andersen Consulting resulted from fission within the Andersen Company. All indications are that Madoff's two sons were the ones who denounced their father Bernard to the police.

Obstacles help the predator become wiser, more alert, and quicker to respond to threats. Hence, they are part of the predation experience.

Predators and their prey are locked into what initially appears to be a mutually beneficial relationship, and from which they have a hard time extricating themselves due to psychological or financial exit costs. There is a strong sense of interdependency (Palmatier et al., 2006, p. 140; Svensson, 2004; Mohr and Spekman, 1994) in business relationships. Many of Norbourg's victims had been warned of the danger of investing in the company but could not find it in themselves to pay the mere C\$300 to get out. Had Andersen resigned its contract with Enron, this would have led to Enron's demise, as it would have signalled to everyone that there were unsolvable problems at the company.

It thus appears that predators and preys work hand in hand to construct a sombre scenario that leads to the downfall of one and the "extinction" of the other, by way of life investment losses. This rather resembles a Darwinian scenario (see Eyuboglu and Buja, 2007), with the predator falling at times, but not necessarily every time.

Legal implications

Of course, a predator that uses the organization to commit fraudulent acts will do everything in his power to reduce the amount of predation perceived by the buyer and regulatory authorities. His deck of trick cards includes, for example, the use of blind trust and of ghost accounts. Once perceived predation is at its minimum, the relationship between seller and buyers can proceed in an atmosphere of positive interaction; hence the predatory terrain is set and will be fertile until such time as it is discovered and appropriately punished.

The following two conditions need to be fully exercised in order to prevent a financial predator from abusing his targeted preys: (1) identification; and (2) appropriate punishment. Weak deterrents are not enough of a punishment for the predator, who is by nature oblivious to others' suffering.

Our analysis points to ways of accomplishing this task of stopping financial predators. By following the clues any predator leaves in his tracks (such as tied hands and the defection of key players), legal authorities will be better able to prevent predatory actions or catch the culprits before they cause excessive harm⁷. By being able to lay charges on every count of misconduct present in the nine characteristics identified that form part of the predatory *modus operandi*, legal authorities would deter potential partners-in-predation (read “-in-crime”). We contend that financial predators cannot act alone: someone, somewhere always knows something, if only via the social networks used by financial predators, which are often considerable in size and breadth. Financial predation is always part of an ecosystem that supports it.

If it could be proven, for example, that key players defect from the predator's organization because they realize they are part of a predatory scheme (implying opportunity, weapon, motive and of course obstacles), then these players should be held accountable should they not disclose what they have uncovered and realized. This would serve as a safeguard for them as well as for future victims: would-be partners would be reluctant to work with a potential predator knowing they could be held accountable even after they quit the predatory scheme, and this could de facto limit the number of victims down the road.

The Mesly model as applied to the dark side of organizations requires further analyses and research. However, based on the limited cases presented here, we feel it would be worth giving some thought to the idea of 1) unveiling the existence of a dynamic perceived predation in organizations that contributes to their dark side, and 2) finding ways of identifying and punishing financial predators much faster than is currently being done, given the legal tools currently available.

This article is exploratory in nature. However, we believe it provides enough compelling evidence to suggest that more steps need to be taken in order to prevent, control and punish predators, would-be predators, and their associates. Put more directly: governments and regulatory authorities should develop better mechanisms to protect average investors by better understanding the phenomenon of perceived and actual financial predation.

⁷ Our research shows, for example, that the *Autorité des Marchés financiers* (the equivalent of the SEC in Québec, Canada) has only pinpointed six of the 12 subterfuges financial predators use to commit their predatory acts (see Mesly, 2012).

CONCLUSION

In this article, we looked at the dark side of organizations from the point of view of predation. Predation exists in the human world just as it does in the animal kingdom for the purpose of allowing the best predators to take advantage of their preys. In human predation, the core of the action is focused around the motive of personal financial gain, with a series of at least nine landmark activities inherent to the predatory path. In particular, financial predators use information in such a way as to cover their tracks, confuse their victims as well as regulatory authorities, promote blind trust and build a social network that protects them.

We have suggested that financial predators are much like common criminals, in that they exploit an opportunity, have a motive and use certain tools (weapons). We have added “obstacles” as another pillar of their operational system: indeed, financial predators enjoy obstacles and are invigorated by them. Obstacles represent challenges that prove them right and fortify their predatory ability. People admire how business people face adversity and are even more inclined to trust them and give them their money once they are known to be successful.

Predators are part of organizations, whether public ones (e.g. Dunn at Nortel) or their own (Madoff). As such, organizations have a dark side that can no longer be ignored. It is up to each organization to decide whether it wants to live as an honest corporate citizen and enforce good corporate governance or else if it wants to use its prestige to defraud society at large. On January 18, 2005, journalist Holly Shaw published an article in the Canadian-based National Post conveying the perception that some corporate suppliers had of their client Shoppers Drug Mart, a multi-billion dollar pharmacy chain active in Canada: “[...] Shoppers Drug Mart Corp. has taken the unprecedented step of charging key suppliers a fee for doing business with the retailer, a move that has some of the vendors crying foul. A surprise bill from Shoppers to its entire private label product suppliers went out last month, asking them to remit a “preferred vendor” charge equivalent to 20% of their business with the retailer in November and December. “They said “either you pay it or you're out [as a supplier] – there was no discussion,” said an industry source who referred to the missive as a “shakedown.” Another supplier who refused to pay the clawback had all of his products shipped back to him....” Upon checking the members of the board of directors at the time, one could see that there was one board member closely associated with the Canadian Coalition for Good Governance as well as a former Canadian provincial prime minister.

While SDM’s share price went up and the then CEO left the company with C\$ 24 million in his pocket, the questions could be raised based upon what we have learned of predation in this article: 1) was there a loss on one side that unilaterally benefited the another party? 2) Was there an element of surprise? 3) Was the new policy meticulously planned with the tool being the preferred vendor charge?

Actual research is needed to test the above-described hypotheses relating to the concept of predation. Initial data collection through a two-year research, court documents and general news seems to point towards specific components of financial predation.

As a society, we are far from having unveiled the multiple facets of predation. Yet, this paper has tried to make a compelling case about the fact that corporations have a dark

side and that this dark side must be under scrutiny at all times in order to protect our economic system as a whole, including large and small companies, governments and individuals. By better understanding predatory behavior (and how perceived predation affects trust and cooperation), we hope that companies and government alike will be better equipped to strengthen their drive towards sound corporate social responsibility. This will not happen however without tough laws specifically aimed at catching and discouraging financial predators.

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APPENDIX

Figure 1 – The Mesly model

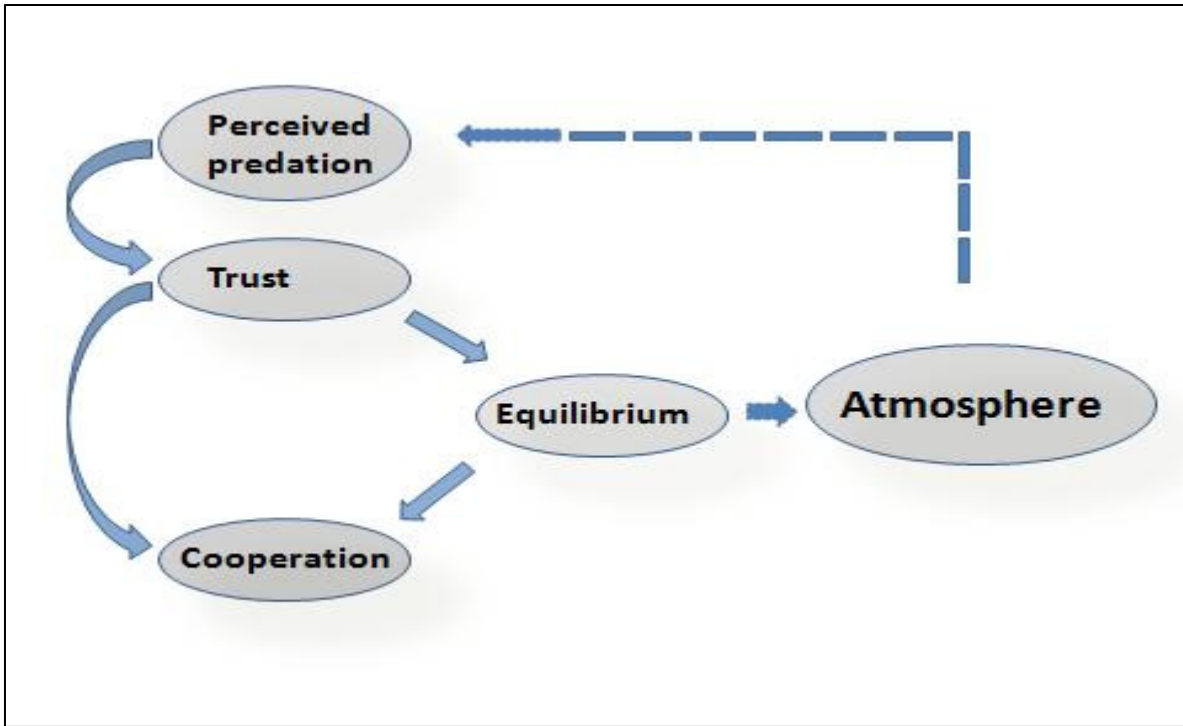


Table 1- Energy sources in Québec since 1960

Source	Year 1960	1980	2000
	<i>In %</i>		
Biomass	--	7	10
Coal	11	0	0
Electricity	18	30	38
Natural gas	4	9	13
Petroleum	67	53	38
TOTAL	100	99	99

Table 2 - Key characteristics of corporate predation

Main groups of characteristics	Individual characteristics
Opportunity	Opportunity to commit the act of predation
	Lucky star
	Privileged social network
Tool (weapon)	Complexity
	Blind trust
	Ghost accounts and partners
Motive	Personal financial gain
Obstacle	Key players' withdrawals
	Tied hands



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