## — CHAPTER 2 —

## "I WILL SURVIVE"

"Did you think I'd crumble?
Did you think I'd lay down and die?
Oh no, not I
I will survive."

**—GLORIA GAYNOR, "I WILL SURVIVE"**

Coming off the success of Netscape, Marc knew all the top venture capitalists in Silicon Valley, so we needed no introductions. Unfortunately for us, Kleiner Perkins, the firm that backed Netscape, had already funded a potentially competitive company. We spoke to all the other top-tier firms and decided to go with Andy Rachleff of Benchmark Capital.

If I had to describe Andy with one word, it would be *gentleman*. Smart, refined, and gracious, Andy was a brilliant abstract thinker who could encapsulate complex strategies into pithy sentences with ease. Benchmark would invest $15 million at a pre-money valuation (the value of the company before the cash goes into the company treasury) of $45 million. In addition, Marc would invest $6 million, bringing the total value of the company including its cash to $66 million, and would serve as our "full-time chairman of the board." Tim Howes would be our chief technology officer. I would be CEO. Loudcloud was two months old.

The valuation and the size of the funding were signs of the times and created an imperative to get big and capture the market before similarly well-funded competitors could. Andy said to me, "Ben, think about how you might run the business if capital were free."

Two months later, we would raise an additional $45 million from Morgan Stanley in debt with no covenants and no payments for three years, so Andy's question was more reality-based than you might think. Nonetheless, "What would you do if capital were free?" is a dangerous question to ask an entrepreneur. It's kind of like asking a fat person, "What would you do if ice cream had the exact same nutritional value as broccoli?" The thinking this question leads to can be extremely dangerous.

Naturally, I took the advice and ran with it. We quickly built out our cloud infrastructure and began signing up customers at a rapid rate. Within seven months of founding, we'd already booked $10 million in contracts. Loudcloud was taking off, but we were in a race against time and the competition. This meant hiring the best people and fielding the broadest cloud service, and that meant spending money—lots of it.

Our ninth hire was a recruiter, and we hired a human resources person when we had a dozen employees. We were hiring thirty employees a month and snagging many of the Valley's smartest people. One of our new recruits had quit his job at AOL to spend two months mountain climbing, but instead he joined us; another forfeited millions to join Loudcloud when he resigned from another company on the day of its IPO. Six months in, we had nearly two hundred employees.

Silicon Valley was on fire, and Loudcloud was billed in a *Wired* cover story as "Marc Andreessen's second coming." We traded our first office—where you'd blow a circuit if you ran the microwave and coffeemaker at the same time—for a fifteen-thousand-square-foot warehouse in Sunnyvale, which was too small for us by the time we moved in.

We spent $5 million to move into a new three-story stucco building with jade-colored tiles we called "the Taj" (as in the Taj Mahal). It was also too small to keep pace with our hiring frenzy, and people were sitting in the hallways. We rented a third parking lot down the street and ran shuttle vans to the office. (The neighbors hated us.) The kitchen was stocked like Costco, and when we fired the snack contractor for making our fridge look like the one in Philip Roth's *Goodbye, Columbus*, he asked for equity.

This was the time.

In the next quarter, we booked $27 million worth of new contracts, and we were less than nine months old. It seemed like we were building the greatest business of all time. Then came the great dot-com crash. The

NASDAQ peaked at 5,048.62 on March 10, 2000—more than double its value from the year before—and then fell by 10 percent ten days later. A *Barron's* cover story titled "Burning Up" predicted what was to come. By April, after the government declared Microsoft a monopoly, the index plummeted even further. Startups lost massive value, investors lost massive wealth, and dot-coms, once heralded as the harbinger of a new economy, went out of business almost overnight and became known as dot-bombs. The NASDAQ eventually fell below 1,200, an 80 percent drop from its peak.

We thought our business might have been the fastest growing of all time at that point. That was the good news. The bad news was that we needed to raise even more money in this disastrous climate; nearly all of the $66 million in equity and debt we had raised had already been deployed in our quest to build the number-one cloud service and to support our now fast-growing set of customers.

The dot-com crash had spooked investors, so raising money wasn't going to be easy, especially since most of our customers were dot-com startups. This became quite clear when we pitched the deal to the Japanese firm Softbank Capital. My friend and Loudcloud board member Bill Campbell knew the Softbank people well and offered to get some "back-channel" information following the pitch. When my assistant told me that Bill was on the line, I quickly answered the phone. I was eager to hear where we stood.

I asked, "Bill, what did they say?" Bill replied in his raspy, coach's voice, "Ben, well, honestly, they thought you were smoking crack." With nearly three hundred employees and very little cash left, I felt like I was going to die. It was the first time I'd felt that way as CEO of Loudcloud, but not nearly the last.

During this time I learned the most important rule of raising money privately: Look for a market of one. You only need one investor to say yes, so it's best to ignore the other thirty who say "no." We eventually found investors for a series C round (meaning our third round of funding) at an amazing $700 million pre-money valuation and raised $120 million. The sales forecast for the quarter came in at $100 million, and things seemed like they might be okay. I felt confident that our sales forecasts would hold up given that previous forecasts had underestimated actual performance. And perhaps, I speculated, we could seamlessly migrate our customer base away from dot-com bombs to more stable, traditional customers such as Nike, our largest customer at the time.

And then the wheels came off.

We finished the third quarter of 2000 with $37 million in bookings—not the $100 million that we had forecast. The dot-com implosion turned out to be far more catastrophic than we had predicted.

## EUPHORIA AND TERROR

I needed to raise money yet again. Only this time the environment was even worse. In the fourth quarter of 2000, I met with every possible funding source, including Prince Al-Waleed bin Talal of Saudi Arabia, but nobody was willing to invest money at any valuation. We'd gone from being the hottest startup in Silicon Valley to unfundable in six months. With 477 employees and a business that resembled a ticking time bomb, I searched for answers.

Thinking about what might happen if we ran completely out of money—laying off all the employees that I'd so carefully selected and hired, losing all my investors' money, jeopardizing all the customers who trusted us with their business—made it difficult to concentrate on the possibilities. Marc Andreessen attempted to cheer me up with a not-so-funny-at-the-time joke:

Marc: "Do you know the best thing about startups?"

Ben: "What?"

Marc: "You only ever experience two emotions: euphoria and terror. And I find that lack of sleep enhances them both."

With the clock ticking, one unattractive but intriguing option emerged: We could go public. In an oddity of the times, the private funding market shut down for companies with our profile, but the window on the public market remained just slightly open. This may sound like a crazy anomaly and it was, but private funds had become completely cynical while the public markets were only 80 percent of the way there.

With no other options available, I needed to propose to the board that we go public. In order to prepare, I made a list of the pros and cons of an IPO.

I knew that Bill Campbell would be the critical person I'd need to persuade one way or another. Bill was the only one of our board members who had been a public company CEO. He knew the pros and cons better than anyone else. More important, everybody always seemed to defer to Bill in these kinds of sticky situations, because Bill had a special quality about him.

At the time, Bill was in his sixties, with gray hair and a gruff voice, yet he had the energy of a twenty-year-old. He began his career as a college football coach and did not enter the business world until he was forty. Despite the late start, Bill eventually became the chairman and CEO of Intuit. Following that, he became a legend in high tech, mentoring great CEOs such as Steve Jobs of Apple, Jeff Bezos of Amazon, and Eric Schmidt of Google.

Bill is extremely smart, super-charismatic, and elite operationally, but the key to his success goes beyond those attributes. In any situation—whether it's the board of Apple, where he's served for over a decade; the Columbia University Board of Trustees, where he is chairman; or the girls' football team that he coaches—Bill is inevitably everybody's favorite person.

People offer many complex reasons for why Bill rates so highly. In my experience it's pretty simple. No matter who you are, you need two kinds of friends in your life. The first kind is one you can call when something good happens, and you need someone who will be excited for you. Not a fake excitement veiling envy, but a real excitement. You need someone who will actually be more excited for you than he would be if it had happened to him. The second kind of friend is somebody you can call when things go horribly wrong—when your life is on the line and you only have one phone call. Who is it going to be? Bill Campbell is both of those friends.

I presented my thinking as follows: "We have not been able to find any investors in the private markets. Our choices are to either keep working on private funding or start preparing to go public. While our prospects for raising money privately seem quite difficult, going public has a large number of issues:

- "Our sales processes are not robust and it's difficult to forecast in any environment.
- "We are not in any environment; we are in a rapidly declining environment and it's not clear where the bottom is.

- “Our customers are going bankrupt at an alarming and unpredictable rate.
- “We are losing money and will be losing money for quite some time.
- “We are not operationally sound.
- “In general, we are not ready to be public.”

The board listened carefully. Their expressions showed deep concern with the issues I’d raised and an awkwardly long silence ensued. As expected, Bill broke the dead air.

“Ben, it’s not the money.”

I felt a strange sense of relief. Maybe we didn’t have to go public. Maybe I’d overestimated our cash problems. Perhaps there was another way.

Then Bill spoke again, “It’s the *fucking* money.”

Okay, I guess we’re going public.

In addition to the issues I had outlined for the board, our business was complex and hard for investors to understand. We typically signed customers to two-year contracts, and then recognized the revenue monthly. This model is now common, but it was quite unusual then. Given the fast growth in our bookings, revenue lagged behind new bookings by quite a bit. As a result, our S-1 (our registration with the SEC) stated that we had $1.94 million in trailing six months revenue, and we forecast $75 million for the following year—an incredibly steep revenue ramp. Since earnings are driven by revenue and not bookings, we had gigantic losses. In addition, the stock option rules at the time made it seem like our losses were about four times as large as they actually were. These factors led to extremely negative press heading into the IPO.

A scathing story in *Red Herring*, for instance, noted that our list of customers was “quite thin” and that we were too reliant on dot-coms. It quoted a Yankee Group analyst positing that we had “lost something like $1 million dollars per employee over the last 12 months,” and conjecturing that the way we did it was by having a bonfire in the parking lot and getting everyone busy burning dollar bills. *BusinessWeek* took us apart in an article that declared us “the IPO from hell.” A *Wall Street Journal* cover piece quoted a money manager’s reaction to our offering as “Wow, they were desperate.” One financier—who actually invested in the offering—called it “the best option among a particularly ugly set of options.”

Despite the horrifying press, we prepared to hit the road. Benchmarking ourselves against comparable companies, we settled on the price of the offering at $10 per share after an upcoming reverse split, which would value the company at just under $700 million—less than the valuation from the previous private round of financing, but much better than bankruptcy.

It was not at all clear that we would be successful with the offering. The stock market was crashing, and the public market investors we visited were visibly distressed.

At the end of the preparation process and after the banks had signed off, our director of finance, Scott Kupor, received a call from our banker at Morgan Stanley.

Banker: “Scott, did you know that $27.6 million of your cash is restricted and tied up in real estate commitments?”

Scott: “Yes, of course.”

Banker: “So, you have just over three weeks’ worth of cash before you go bankrupt?”

Scott: “Yes.”

Scott then relayed the conversation to me, saying, “Can you believe they underwrote the deal and didn’t notice that the cash was restricted until now? We gave them all the documents.”

Right before we were to leave for the IPO road show, I called an all-company meeting to share two pieces of news: First, we were going public, or at least we were going to try to go public. Second, the company had fallen so far in value that we would have to reverse split the stock two for one.

I thought the first part would go okay, but I was worried about how the second piece of news would be received. We had to reverse split the stock to get the price per share high enough to go public. In theory, a reverse split shouldn’t matter at all. Each employee owned a certain percentage of the company. The company had a total number of shares of stock. Multiply the total number of shares by the percentage, and you get the employees’ share number. Cut the number of shares in half and, while employees would have half the number of shares, they’d still own the exact same percentage of the company. Nothing changed.

Oh, but it did. As we grew from zero to six hundred employees in less than eighteen months, the stage was set for hyperbole and momentum. Some overly excited managers oversold the dream. They spoke only in terms of shares rather than in percentages and spun stories of a potential $100 per share stock price. Employees then calculated their fantasy price per share and figured out how much money they would make. I was aware that this was going on, but I never thought we would reverse split the stock, so I never worried about it. Like many other things that I screwed up during that period, I should have worried.

My wife, Felicia, came to the all-company meeting as she always did. This time her parents were in town, so they came, too. The meeting did not go well. People did not realize how close to the edge we were, so the news of the IPO didn't make anyone happy. The news of the reverse split made them even less happy—in fact, it infuriated them. I had literally cut their fantasy number in half, and they were not pleased about it. Nobody said harsh things directly to me. My in-laws, however, heard everything. And, as my father-in-law put it, "it wasn't nothin' nice."

My mother-in-law, Loretta, asked my wife, "Why does everybody hate Ben so much?" Felicia, who is normally the most electric, outgoing person in any room, was just recovering from hernia surgery so she wasn't her normal bubbly self. She was discouraged. My in-laws were depressed. The employees were pissed. I had no idea if I'd be able to raise the money. What a way to start a road show, an event that's usually the cause of a bit more fanfare.

The road show was brutal. The stock market crashed daily, and technology stocks were to blame. Investors looked like they'd come out of torture chambers when we arrived. One mutual fund manager looked right at Marc and me and asked, "Why are you here? Do you have any idea what's going on in the world?" I thought that there was no way we'd be able to raise the money. We were going to go bankrupt for sure. I did not sleep more than two hours total during that entire three-week trip.

Three days into the tour, I received a call from my father-in-law. John Wiley had been through a lot in his seventy-one years. As a boy, his father was murdered in Texas. In order to survive, he and his mother moved in with an unkind man and his nine children. There, John was abused, made to stay in the barn with the animals, while the other children ate his dinner.

Eventually, John and his mother left that cruelty by walking for three days down a dirt road, carrying everything they owned. John would recall that journey in great detail his entire life. As a young man, before finishing his high school education, he left home to fight in the Korean War so that he could support his mother. As a young father of five, he took every job imaginable to support his family, including unloading banana boats and working to build the Alaskan pipeline. He tragically saw two of his children die before he reached the age of sixty. He had a hard life and was used to bad news.

John Wiley did not call me for casual reasons. If he called, it was serious, possibly even deadly serious.

Ben: “Hello.”

John: “Ben, the office said not to bother you, but I just want to let you know that Felicia stopped breathing, but she is not going to die.”

Ben: “Not going to die? What?!?! What happened?”

I could not believe it. I had been so focused on work that I had lost focus of the only thing that really mattered to me. Once again, I neglected to worry about the one thing that I should have worried about.

Ben: “What happened?”

John: “They gave her some medicine and she had an allergic reaction and she stopped breathing, but she’s okay now.”

Ben: “When?”

John: “Yesterday.”

Ben: “What? Why didn’t you tell me?”

John: “I knew that you were busy and that you were really in trouble at work because of that meeting that I went to.”

Ben: “Should I come home?”

John: “Oh no. We’ll take care of her. You just take care of what you need to do.”

I was completely stunned. I started sweating so hard that I had to change my clothes right after the call. I had no idea what to do. If I returned home, the company would surely go bankrupt. If I stayed . . . how could I stay? I called back and had him put Felicia on the phone.

Ben: “If you need me, I will come home.”

Felicia: “No. Get the IPO done. There is no tomorrow for you and the company. I’ll be fine.”

I stumbled through the rest of the road show completely discombobulated. One day I wore a mismatching suit jacket and suit pants, which Marc pointed out to me midway through the meeting. I had no idea where I was half the time. During the three weeks we were on the road, comparable companies in our market lost half of their value, which meant that our $10 share price was roughly double the current benchmark. The bankers recommended that we lower the price of the offering to $6 a share in order to reflect this new reality, but they gave us no assurance that the deal would actually get done. Then, the day before the offering, Yahoo, the lighthouse company of the Internet boom, announced Tim Koogle, its CEO, was stepping down. We had hit the nadir of the dot-com crash.

The Loudcloud offering finally sold at $6 a share, and we raised $162.5 million, but there was no celebration and no party. Neither Goldman Sachs nor Morgan Stanley—the two banks that took us public—even offered us the traditional closing dinner. It may have been the least celebratory IPO in history. But Felicia was feeling better, and we had pulled it off. In a brief moment of lightheartedness on the plane ride home, I turned to Scott Kupor, my director of finance, and said, “We did it!” He replied, “Yeah, but we’re still fucked.”

Years later, in 2012, after Yahoo fired its CEO, Scott Thompson, Felicia mused, “Should they bring back Koogle?” I replied, “Tim Koogle? How do you even know who Tim Koogle is?” She then relived the conversation we’d had eleven years earlier. It went something like this:

Ben: “We’re fucked.”

Felicia: “What do you mean? What happened?”

Ben: “Yahoo fired Koogle. It’s over. The whole thing is over.”

Felicia: “Who is Koogle?”

Ben: “He was the CEO of Yahoo. We’re fucked. I’m going to have to shut the company down.”

Felicia: “Are you sure?”

Ben: “Didn’t you hear me? They fired Koogle. We’re fucked.”

She had never seen me that depressed before, and she never forgot it. For most CEOs, the night before their public offering is a highlight. For me, it was a highlight of depression.

## IF YOU ARE GOING TO EAT SHIT, DON’T NIBBLE

During the road show, as a way to break the tension, Marc would say, “Remember, Ben, things are always darkest before they go completely black.” He was joking, but as we entered our first quarter as a public company, those words seemed prescient. Customers continued to churn, the macroeconomic environment worsened, and our sales prospects declined. As we got closer to our first earnings call with investors, I conducted a thorough review to make sure that we were still on track to meet our guidance.

The good news was that we would meet our forecast for the quarter. The bad news: There was very little chance that we would meet our forecast for the year. Typically, investors expect that companies will refrain from going public if they can’t hit at least their first year’s forecast. These were exceptional times, but resetting guidance on your very first earnings call was still a very bad thing to do.

As we discussed where to reset guidance to investors, we were faced with a tough choice: Should we try to minimize the initial damage by taking down the number as little as possible or should we minimize the risk of another reset? If we reduced the number by a lot, the stock might fall apart. On the other hand, if we didn’t lower it enough, we might have to reset again, which would cost us all the credibility we had left. My controller, Dave Conte, raised his hand with what would be the definitive advice: “No matter what we say, we’re going to get killed. As soon as we reset guidance, we’ll have no credibility with investors, so we might as well take all the pain now, because nobody will believe any positivity in the forecast anyway. If you are going to eat shit, don’t nibble.” So we reset guidance for the year, slashing our original forecast of $75 million in projected revenue to $55 million.

Resetting revenue guidance also meant resetting expense guidance, and that meant laying people off. We’d been the darling of the startup world, and now I had to send home 15 percent of our employees. It was the clearest indication yet that I was failing. Failing my investors, failing my employees, and failing myself.

Following the reset, Goldman Sachs and Morgan Stanley—the investment banks that had taken us public—both dropped research coverage, meaning their analysts would no longer follow the company’s progress on behalf of their clients. This was a huge slap in the face and a massive reneging of the promises they made when they were pitching us, but times were tough all around, and we had no recourse. With a vote of no confidence from our banks and a lowered revenue forecast, the stock price plummeted from $6 a share to $2.

Despite the mammoth negative momentum, we soldiered on, and were putting together a fairly strong quarter in the third quarter of 2001. Then, on September 11, terrorists hijacked four jetliners, flying two into the World Trade Center and another into the Pentagon, and in the end throwing the whole world into chaos. It turned out that our largest deal that quarter was with the British government. It represented one-third of our bookings, and we would miss the quarter's targets badly without it. Our champion on the deal called to inform us that Prime Minister Tony Blair had redirected the funds for our deal to the war chest—literally. By some miracle our sales director convinced one of Tony Blair's staffers to get the money back, so we got the deal and made the quarter.

Nonetheless, the close call was a sign to me that the entire operation was far too fragile. I got another sign when our largest competitor, Exodus, filed for bankruptcy on September 26. It was a truly incredible bankruptcy in that the company had been valued at $50 billion a little more than a year earlier. It was also remarkable because Exodus had raised $800 million on a "fully funded plan" just nine months earlier. An Exodus executive later joked to me: "When we drove off the cliff, we left no skid marks." If Exodus could lose $50 billion in market capitalization and $800 million in cash that fast, I needed a backup plan.

In my first attempt at a "Plan B," we evaluated acquiring Data Return, a company like ours that focused more on Windows applications than Unix applications as we did. We studied the deal for weeks, modeling what the two companies might look like together, figuring out product offerings and cost synergies. My CFO at the time was extremely excited about the deal since it would make use of his favorite skill set—cost cutting.

Toward the end of the process, I took a two-day vacation to Ashland, Oregon. Almost as soon as I arrived, I received an urgent call from John O'Farrell, who was in charge of corporate and business development.

John: "Ben, sorry to disturb you on vacation, but we just had a meeting on the Data Return deal and I don't think that we should do it."

Ben: "Why not?"

John: “Quite frankly, our business is in trouble and their business is in trouble and putting them together will just be double trouble.”

Ben: “I was thinking the exact same thing.”

In fact, looking at Data Return’s business made it crystal clear to me that Loudcloud would probably not end well. Some things are much easier to see in others than in yourself. Looking at Data Return, I could see Loudcloud’s future, and it was not pretty. I had a great deal of trouble sleeping as I thought about our fate. I tried to make myself feel better by asking, “What’s the worst thing that could happen?” The answer always came back the same: “We’ll go bankrupt, I’ll lose everybody’s money including my mother’s, I’ll have to lay off all the people who have been working so hard in a very bad economy, all of the customers who trusted me will be screwed, and my reputation will be ruined.” Funny, asking that question never made me feel any better.

Then one day I asked myself a different question: “What would I do if we went bankrupt?” The answer that I came up with surprised me: “I’d buy our software, Opsware, which runs in Loudcloud, out of bankruptcy and start a software company.” Opsware was the software that we’d written to automate all the tasks of running the cloud: provisioning servers and networking equipment, deploying applications, recovering the environment in case of disaster, and so forth. Then I asked myself another question: “Is there a way to do that without going bankrupt?”

I ran through different scenarios in my mind where we might move into the software business and exit the cloud business. In each scenario, step one was separating Opsware from Loudcloud. Opsware had been written to run only in Loudcloud and had many constraints that prevented it from being a product that would work in any environment. I asked my cofounder and CTO Tim Howes how long it would take to separate Opsware from Loudcloud. He said about nine months, which would prove to be quite optimistic. I immediately assigned a team of ten engineers to start the process in a project we called Oxide.

At this point, our business was still a cloud business, and I gave no indication to the rest of the staff that I might have other ideas. Doing so would have instantly doomed the only business we were in, as everyone would want to work on the future and not the past. I said that Oxide was simply another product line. This statement deeply worried two of my employees who had graduated from Stanford Business School. They scheduled an appointment and presented me with a slide deck detailing why my decision to start Oxide was quixotic, misguided, and downright stupid. They argued that it would steal precious resources from our core business while pursuing a product that would surely fail. I let them present all forty-five slides without my asking them a single question. When they finished I said, "Did I ask for this presentation?" Those were the first words I spoke as I made the transition from a peacetime CEO to a wartime CEO.

By virtue of my position and the fact that we were a public company, nobody besides me had the complete picture. I knew we were in deep, deep trouble. Nobody besides me could get us out of the trouble, and I was through listening to advice about what we should do from people who did not understand all the pieces. I wanted all the data and information I could get, but I didn't need any recommendations about the future direction of the company. This was wartime. The company would live or die by the quality of my decisions, and there was no way to hedge or soften the responsibility. If everybody I had hired—and who gave their lives to the company—could be sent home with little to show for it, then there were no excuses that would help. There would be no: "It was a horrible economic environment"; "I got bad advice"; "Things changed so quickly." The only choices were survival or total destruction. Yes, most things could still be delegated and most managers would be empowered to make decisions in their areas of expertise, but the fundamental question of whether—and *how*—Loudcloud could survive was mine and mine alone to answer.

We muddled through the fourth quarter of 2001 and beat our target for the year, delivering $57 million in revenue against our $55 million forecast. Not a great win, but very few companies met expectations that year, so I took it as a small victory. The stock price slowly rose to $4 a share, and it looked as though we might be able to make the cloud business work.

In order to do so, we needed more cash. We carefully analyzed our financial plan and decided that we needed another $50 million to get to cash flow breakeven—the point at which we would no longer need to raise money. Given our momentum in the market, raising money was now barely possible and the only way to do it was in the form of a seldom-used construct called a private investment in public equity (PIPE). We worked with Morgan Stanley to line up investors with the goal of raising $50 million.

It was Monday morning, and we were all set to hit the road on Tuesday to raise the PIPE when I got the call. “Ben, the CEO of Atriax is on the phone; shall I put him through?” Atriax, an online foreign currency exchange backed by Citibank and Deutsche Bank, was our largest customer. Atriax paid us more than $1 million per month and had a two-year guaranteed contract. I was in the middle of a meeting with Deb Casados, my vice president of human resources, but I said, “Put him through.” He then informed me that Atriax was bankrupt and could not pay any of the $25 million he owed us. It was like the world stopped spinning. I sat there in a daze until I heard Deb’s voice saying, “Ben, Ben, Ben, do you want to have this meeting later?” I said, “Yep.” I walked slowly over to my CFO’s office to assess the damage. It was worse than I thought.

Given the materiality of losing the contract, we could not raise money without first disclosing that we’d lost our largest customer and $25 million out of our financial plan. We put the PIPE road show on hold and then issued a press release. The stock immediately fell by 50 percent, and with a rapidly declining market cap of $160 million, we could no longer raise $50 million in a PIPE. The plan that was $50 million short of breakeven was now, with the loss of Atriax, $75 million short of breakeven with no way to close the gap. Loudcloud was doomed. I had to deploy Oxide.

The situation was complex, because 440 of our 450 employees worked in the cloud business, which represented all of our customers and generated 100 percent of our revenue. I could not tell the employees or even my executive team that I was considering abandoning the cloud business, because our stock price would have collapsed to nothing, killing any hope of selling the company and avoiding bankruptcy.

The one person I needed and could trust was John O’Farrell. John ran business and corporate development, but more than that he was the greatest big-deal person I had ever known. To illustrate my point, let’s say you were a religious man. We’re speaking in the hypothetical now. And let’s say you had reached your end of days and you faced your maker for final judgment. Let’s further suppose that as your fate was to be decided for all eternity, you were granted a single person to negotiate on your behalf. Whom would you choose? Well, if it were me, I’d take that Irish brother, John O’Farrell.

I told John that he and I needed to execute a contingency plan, and we needed to get started immediately. This would be a two-person project to start, and we needed everyone else focused on the task at hand—reducing Loudcloud's cash burn. Next I called Bill Campbell to explain why I thought we needed to exit the cloud business.

Bill understood what a crisis looked like since he'd been CEO of GO Corporation in the early 1990s. Essentially GO had attempted to build an iPhone-like device in 1992 and ended up being one of the largest venture capital losses in history. I took Bill through my logic: The only way out of the cloud business without going bankrupt was through higher sales, because even if we laid off 100 percent of the employees, the infrastructure costs would still kill us without a sharper sales ramp. I further explained that the dwindling cash balance decreased customer confidence, which in turn hurt sales, which in turn caused the cash balance to decline further. He simply said "spiral." And I knew that he understood.

John and I mapped out the ecosystem to figure out which companies might be interested in acquiring the Loudcloud business. Unfortunately, many of the prospective buyers were in dire straits themselves. Giant telecoms Qwest and WorldCom were embroiled in accounting fraud cases, and Exodus had already gone bankrupt. We decided to focus on the three most likely buyers: IBM, Cable & Wireless, and EDS.

IBM's hosting business, led by the congenial Jim Corgel, immediately took a strong interest. Jim valued the Loudcloud brand and our reputation for technological superiority. EDS, on the other hand, showed no interest. This worried me intensely as I studied all the public filings from both companies; it was clear to me that EDS needed Loudcloud far more than IBM did. Needs always trump wants in mergers and acquisitions. John said to me, "Ben, I think we need to walk away from EDS, so that we can focus on the higher-probability targets." I asked him to draw the EDS organizational chart one more time to see if we could find someone influential at EDS whom we hadn't yet approached. When he did, I asked, "Who is Jeff Kelly?" John paused, then said, "You know, we haven't gotten to Jeff, but he may be able to make this decision."

Sure enough, Jeff was interested. Now with two potential bidders, we put things in motion. John and I worked hard to create urgency with both IBM and EDS, because time was against us. We hosted both companies in our facilities, sometimes with them passing each other in the hallway as part of John's well-orchestrated sales technique. The final step was to set the timeline for the endgame. John and I debated the best way to do this as the deadlines that we planned to set were clearly artificial. I suggested that we stop by Los Angeles on our way to Plano, Texas, home of EDS, to get some advice from Michael Ovitz.

Michael was on Loudcloud's board, but more important, he had formerly been known by many observers as the Most Powerful Man in Hollywood. When he was twenty-eight years old, he started a talent agency, Creative Artists Agency (CAA), which grew to dominate the entertainment industry. CAA's rise made Michael so influential that he could routinely structure deals that had never been done before.

When we arrived in his offices, the place buzzed with activity. Michael seemed to be engaged in a dozen different activities, but finally came out to meet with John and me. We explained the situation: We were racing against time and had two bidders, but no specific incentive to coax them toward the end of the process. Michael paused, thought for a moment, and then delivered his advice:

"Gentlemen, I've done many deals in my lifetime and through that process, I've developed a methodology, a way of doing things, a philosophy if you will. Within that philosophy, I have certain beliefs. I believe in artificial deadlines. I believe in playing one against the other. I believe in doing everything and anything short of illegal or immoral to get the damned deal done."

Michael had a way of making things extremely clear.

We thanked him and headed to the airport. We called both EDS and IBM to let them know that we would complete the process over the next eight weeks and sell the Loudcloud business to someone. If they wanted to play, they had to move on that schedule or withdraw immediately. The Michael Ovitz artificial deadline was in full effect. We knew that we might have to go past it, but Michael gave us confidence that going past the deadline was a better move than not having one.

After seven weeks, we came to an agreement with EDS. They would buy Loudcloud for $63.5 million in cash and assume its associated liabilities and cash burn. We would retain the intellectual property, Opsware, and become a software company. EDS would then license our software to run both Loudcloud and the larger EDS for $20 million per year. I thought it was a great deal for both EDS and us. It was certainly far better than bankruptcy. I felt 150 pounds lighter. I could take a deep breath for the first time in eighteen months. Still, it wouldn’t be easy. Selling Loudcloud meant selling about 150 employees to EDS and laying off another 140.

I called Bill Campbell to tell him the good news: The deal was signed and we would be announcing it in New York on Monday. He replied, “Too bad you can’t go to New York and be part of the announcement; you’ll have to send Marc.” I said, “What do you mean?” He said, “You need to stay home and make sure everybody knows where they stand. You can’t wait a day. In fact, you can’t wait a minute. They need to know whether they are working for you, EDS, or looking for a fucking job.” Damn. He was right. I sent Marc to New York and prepared to let people know where they stood. That small piece of advice from Bill proved to be the foundation we needed to rebuild the company. If we hadn’t treated the people who were leaving fairly, the people who stayed would never have trusted me again. Only a CEO who had been through some awful, horrible, devastating circumstances would know to give that advice at that time.

## — CHAPTER 3 —

# THIS TIME WITH FEELING

"I move onward, the only direction
Can't be scared to fail in search of perfection."

**—JAY Z, "ON TO THE NEXT ONE"**

Once the EDS sale was completed, I felt like the company was in good shape, but my shareholders did not agree. I had sold all of my customers, all of my revenue, and the business they understood. Every large shareholder bailed out, and the stock price fell to $0.35 per share, which represented about half of the cash we had in the bank. I realized that nobody besides me knew how bad things had become and nobody besides me believed in the future, so I decided to take the employees off-site and resell them on the opportunity.

I rented forty rooms in a low-end motel in Santa Cruz and took our remaining eighty employees there for one night of drinking and one day of explaining the Opsware opportunity. At the end of the day, I tried to be as honest as humanly possible.

"You have now heard everything that I know and think about the opportunity in front of us. Wall Street does not believe Opsware is a good idea, but I do. I can understand if you don't. Since this is a brand-new company and a brand-new challenge, I am issuing everyone new stock grants today. All that I ask is that if you have decided to quit that you quit today. I won't walk you out the door—I'll help you find a job. But, we need to know where we stand. We need to know who is with us and whom we can count on. We cannot afford to slowly bleed out. You owe it to your teammates to be honest. Let us know where you stand."

That day two employees quit. Of the other seventy-eight, all but two stayed through the sale to Hewlett-Packard five years later.

After the off-site gathering, the first thing I had to do was increase the stock price. The NASDAQ had sent me a curt letter stating that if we failed to get our stock price over a dollar, they would “delist” us from the exchange and send us to the purgatory known as penny stocks. The board debated the best way to do this—reverse-split the stock, a stock buyback, or other options—but I felt we just needed to tell our story. The story was simple. We had a great team, $60 million in the bank, a $20 million a year contract with EDS, and some serious intellectual property. Unless I was the worst CEO of all time, we should be worth more than $30 million. The story took hold, and the stock climbed above $1 a share.

Next, I had to ship a product. Opsware had been built to run Loudcloud and Loudcloud only. It was not yet ready for the world. In fact, parts of the code were hardwired to physical machines in our building. Beyond that, the user interface was far from ready for prime time. The component that managed the network was called the Jive and featured a purple pimp hat on the front page. Project Oxide gave us a running start, but our engineers were nervous. They brought me a long list of features that they felt we needed to complete prior to entering the market. They pointed to competitors with more finished products.

As I listened to their lengthy objections, it became clear to me that the features the engineers wanted to add all came from Loudcloud requirements. As painful as it might be, I knew that we had to get into the broader market in order to understand it well enough to build the right product. Paradoxically, the only way to do that was to ship and try to sell the wrong product. We would fall on our faces, but we would learn fast and do what was needed to survive.

Finally, I had to rebuild the executive team. I had a CFO who didn’t know software accounting, a head of sales who had never sold software, and a head of marketing who did not know our market. Every one of them was great at their old jobs, but not qualified for their new jobs. It was miserable, but necessary, to see them all go.

The strategy and the team came together, and the business started working. We began signing customers at a consistent pace and our stock price rose from its $0.35 low to more than $7 a share. It felt like we were finally out of the woods.

Naturally I was wrong.

## SIXTY DAYS TO LIVE

A few quarters into Opsware, we received very bad news from our largest customer, EDS. "Largest customer" really understates it; EDS accounted for 90 percent of our revenue. And they were not happy. Their Opsware deployment had stalled out and not met its goals as they had run into multiple difficult technical issues. EDS wanted to cancel the deployment, end the contract, and get their money back. Giving EDS their money back would mean the end of Opsware. Getting into a big dispute with a customer that accounted for all but 10 percent of our revenue would also mean the end of Opsware. We were doomed again.

I called my top two lieutenants on the account in for a meeting.

Jason Rosenthal was the very first employee I had hired and the best manager in the company. A Stanford graduate with an impeccable memory and a genius mind for managing all the details of a complex project, Jason was in charge of the EDS deployment.

Anthony Wright grew up in the tough part of Pittsburgh, the son of legendary street fighter Joe Wright, and had earned a black belt in several martial arts himself. Self-made, super-determined, and unwilling to fail, Anthony had an uncanny ability to quickly gain deep insight into people's character and motivations—"able to charm dogs off a meat truck," is how another guy on the team described it. Anthony was the relationship manager for EDS.

I began with an assessment: What happened? It turned out, a lot of things. EDS's environment was insane and chaotic. They had inherited networks and infrastructure from every customer they'd ever signed and from every era in which they had signed them. They had data centers connected by 56-kilobit links at a time when no other customer connected at speeds even twenty times that slow. EDS ran versions of operating systems that were so old that they didn't support basic technologies like threads, which meant our software wouldn't run on them. And the people were not our people. We'd find them sleeping in the data center at two o’clock in the afternoon; they were not motivated and generally not very happy. Beyond that, our product was far from perfect and every one of the many bugs and shortcomings was a reason to stop the deployment.

I took a long pause, rubbed my head, and then began to give instructions. I chose my words carefully:

“I appreciate the difficulties and more than that, I thank you deeply for the effort. However, I do not think that I’ve made myself clear on the situation that we’re in. This is not a scenario where an excuse will do. This is a must win. If EDS drops us, we’re fucked and it’s over. The IPO, avoiding the Loudcloud bankruptcy, all the layoffs and pain will have been for nothing—because we’re dead. So, our only option is to win. We cannot lose this one.

“Jason, the whole company is at your command. Whatever you need, I will make sure you get it. Anthony, Jason is going to work to deliver all the value that EDS expects, but he will fail. He will fail to deliver one hundred percent of expectations, so you are now in charge of finding out what they don’t expect, but want. You are in charge of finding the exciting value. When you do, we will deliver it.”

Jason and Anthony then headed to Plano, Texas, to meet with their counterparts at EDS.

They didn’t know who was making decisions, but after a bunch of meetings and dead ends, they found their way to the office of a person I will call Frank Johnson (not his real name)—a big guy who grew up in the oil fields of Oklahoma, graduated from West Point, and now was in charge of anyone who touched any servers at EDS. Anthony and Jason touted the Opsware technology and potential cost savings.

After listening for a bit, Frank pushed back his chair, stood up, and shouted, “You fucking want to know what I think about Opsware? I think it’s the biggest goddamn piece of shit! All I hear about all day is how much this product fucking sucks. I’m going to do everything I can to get you guys thrown out of here.”

Frank revealed his plan to remove all of our software immediately, demanding all funds to be returned. He was dead serious.

Anthony remained calm, looked him in the eye, and said, “Frank, I will do exactly as you say. I’ve heard you loud and clear. This is a terrible moment for you and for us. Allow me to use your phone, and I will call Ben

Horowitz and give him your instructions. But before I do, can I ask you one thing? If my company made the commitment to fix these issues, how much time would you give us to do that?"

He responded, "Sixty days." Anthony told him the clock had just started ticking and left his office immediately. It was good news: We had exactly sixty days to fix all the problems and make the deployment work. If we did not, we were done. We had sixty days to live.

An early lesson I learned in my career was that whenever a large organization attempts to do anything, it always comes down to a single person who can delay the entire project. An engineer might get stuck waiting for a decision or a manager may think she doesn't have authority to make a critical purchase. These small, seemingly minor hesitations can cause fatal delays. I could not afford any hesitation, so I scheduled a daily meeting with Anthony, Jason, and the team—though they were now based in Plano. The purpose was to remove all roadblocks. If anyone was stuck on anything for any reason, it could not last more than twenty-four hours—the time between meetings.

Meanwhile, Anthony worked furiously to find the exciting value we could offer EDS. We started with little things that did not change our fate, but revealed important clues. We flew our main EDS executive, Frank, out to meet with our top engineers and architects. In booking the trip, Anthony reported that Frank requested the longest layover possible in the connecting airport. I thought that I misheard him. "What, he wants a long layover?"

Anthony: "Yep."

Ben: "Why would anybody want a long layover in an airport?"

Anthony: "Apparently, he likes to hang out in the airport bar between flights."

Ben: "Why does he like to do that?"

Anthony: "I asked him the same question. Frank said: 'Because I hate my job and I hate my family.' "

Wow. I had no idea who I was dealing with until that point. Understanding how differently Frank viewed the world than the people at Opsware helped clarify my thoughts. Frank expected to get screwed by us. It's what always happened to him in his job and presumably in his personal life. We needed something dramatic to break his psychology. We needed to be associated with the airport bar, not with his job or his family.

At the same time, Jason marched the team through the deployment with unrelenting precision. A month into the plan, the Southwest Airlines crew that worked the San Jose–Dallas flight knew Jason and his team by name. They made steady progress, but it wasn't going to be enough. We would not get EDS fully deployed in sixty days—so now we really needed Anthony to deliver exciting value.

As I sat in my office hoping for a breakthrough, my cell phone rang. It was Anthony.

Anthony: "Ben, I think I've got it."

Ben: "Got what?"

Anthony: "The exciting value is Tangram."

Ben: "What?"

Anthony: "Tangram. EDS uses a product from a company called Tangram that inventories their hardware and software. Frank absolutely loves it, but the purchasing guys are going to force him to switch to an equivalent Computer Associates product, because it's free as part of EDS's settlement with CA. Frank hates the CA product. Frank is getting screwed again."

Ben: "So what can we do?"

Anthony: "If Tangram can come free with Opsware, then Frank will love us."

Ben: "That sounds economically impossible. If we buy the licenses from Tangram and give them to EDS, that will be a colossal expense. We'll never be able to describe it to Wall Street."

Anthony: "You asked me what EDS really wanted. They really want Tangram."

Ben: "Got it."

I had never heard of Tangram, so I quickly looked them up. They were a small company in Cary, North Carolina, but they traded on the NASDAQ market. I looked up their market capitalization. This couldn't be right. Tangram Enterprise Solutions, according to Yahoo Finance, was worth only $6 million. I had never heard of a public company being that cheap.

I immediately called my head of business development, John O'Farrell, and told him that I wanted to buy Tangram, and I needed the entire process to be extremely quick—as in, I wanted the Tangram acquisition done before our sixty-day window with EDS closed.

Tangram was run by Norm Phelps, an interim CEO, which was a great sign that they'd be willing to sell the company, because most boards would much rather sell a company than roll the dice by hiring a new CEO. John got in touch with Tangram and they were immediately interested, so we assembled a team to conduct due diligence while we negotiated a merger agreement in parallel. At the end of due diligence, I brought my team back together. They promptly and unanimously agreed that buying Tangram would be a bad idea: The technology would be difficult to integrate and not that valuable. The company was in North Carolina. It was fifteen years old and the technology was old, too. The finance team thought the acquisition was a money loser. I listened, and then I told them all that I didn't care about any of that. We were going to buy Tangram. The team seemed shocked, but did not argue with me.

John and I negotiated a deal to buy Tangram for $10 million in cash and stock. We signed the deal prior to the end of the sixty-day plan. I called Frank from EDS to tell him that once the transaction closed, we would include all Tangram software for free as part of his Opsware contract. Frank was ecstatic. Now that we had solved Frank's Tangram problem, he viewed the work that Jason's team completed in a totally different light. At the end of the sixty days, Frank gathered our team and made the following speech:

"I've given the speech that I gave to you guys at the beginning of this process to at least a dozen other vendors. They all promised things, but none ever delivered. You guys really delivered and I am shocked. You are the best vendor that I have and I am happy to be working with you."

We'd done it. We saved the account and saved the company. What a relief! But we still had the small matter of the company that we'd just purchased and its fifty-seven employees. Some decisions were simple—we didn't need nine out of the ten salespeople, because they weren't selling anything. Some were more complex: Should we keep the North Carolina location? In the end, we decided to keep it and locate customer support there. It turned out that when you accounted for turnover rates and the cost of recruiting and training, Cary, North Carolina, engineers were cheaper to hire than Bangalore, India, engineers. As the years went by, Tangram proved to be a highly profitable acquisition—well beyond the critical role it played in saving the EDS account.

During acquisition talks, both sides had agreed that Tangram's CFO, John Nelli, would not become part of Opsware. But during the time between signing and close, John began to get severe headaches. His doctors discovered that he had brain cancer. Because he would not be an Opsware employee and it was a preexisting condition, he would not be eligible for health insurance under our plan. The cost of the treatment without health insurance would likely bankrupt his family. I asked my head of HR what it would cost to keep him on the payroll long enough to qualify for COBRA and what COBRA would cost. It wasn't cheap—about $200,000. This was a significant amount of money for a company in our situation. On top of that, we barely knew John and technically we didn't "owe" him anything. This wasn't our problem. We were fighting for our lives.

We were fighting for our lives, but he was about to lose his. I decided to pay for his health costs and find the money elsewhere in the budget. I never expected to hear anything else about that decision, but fifteen months later I received a handwritten letter from John's wife letting me know that John had died. She wrote that she was absolutely shocked that I would help a total stranger and his family and that I had saved her from total despair. She went on for several paragraphs saying that she didn't know why I did it, but it enabled her to continue living and she was eternally grateful.

I guess I did it because I knew what desperation felt like.

## SURVIVAL OF THE FITTEST

Almost as soon as the EDS crisis was resolved, I got news that three new clients we had expected to sign were now fading away. An excellent new competitor, BladeLogic, had arisen and was beating us in key accounts. We lost several deals to them and missed our quarterly numbers as a result. The stock price dropped back down to $2.90.

Here we go again.

With a losing product, a dwindling stock price, and a tired team, I knew we were in trouble. To make matters worse, Marc, who had been working exclusively with me on Loudcloud and Opsware as "full-time chairman of the board," had decided to found another company, Ning. The success or failure of Opsware was really up to the team and me at this point, but the timing sucked. Not only was the company circling the drain, but our most visible spokesman was going to work on something else. Damn. After all that we had been through, how could I ask the team to charge up yet another impossible mountain? How could I muster the strength to do it myself?

I felt like I had no more stories, no more speeches, and no more "rah-rah" in me. I decided to level with the team and see what happened. I called an all engineering meeting and gave the following speech:

"I have some bad news. We are getting our asses kicked by BladeLogic and it's a product problem. If this continues, I am going to have to sell the company for cheap. There is no way for us to survive if we don't have the winning product. So, I am going to need every one of you to do something. I need you to go home tonight and have a serious conversation with your wife, husband, significant other, or whoever cares most about you and tell them, 'Ben needs me for the next six months.' I need you to come in early and stay late. I will buy you dinner, and I will stay here with you. Make no mistake, we have one bullet left in the gun and we must hit the target."

At the time, I felt horrible asking the team to make yet another big sacrifice. Amazingly, I found out while writing this book that I probably should have felt good about it. Here's what Ted Crossman, one of my best engineers, said about that time and the launch of the aptly named Darwin Project many years later:

> *Of all the times I think of at Loudcloud and Opsware, the Darwin Project was the most fun and the most hard. I worked seven days a week 8 a.m.–10 p.m. for six months straight. It was full on. Once a week I had a date night with my wife where I gave her my undivided attention from 6 p.m. until midnight. And the next day, even if it was Saturday, I'd be back in the office at 8 a.m. and stay through dinner. I would come home between 10–11 p.m. Every night. And it wasn't just me. It was everybody in the office.*
>
> *The technical things asked of us were great. We had to brainstorm how to do things and translate those things into an actual product.*
>
> *It was hard, but fun. I don't remember losing anyone during that time. It was like, "Hey, we gotta get this done, or we will not be here, we'll have to get another job." It was a tight-knit group of people. A lot of the really junior people really stepped up. It was a great growing*

> *experience for them to be thrown into the middle of the ocean and told, "Okay, swim."*
>
> *Six months later we suddenly started winning proofs of concepts we hadn't before. Ben did a great job, he'd give us feedback, and pat people on the back when we were done.*

Eight years later, when I read what Ted had written, I cried. I cried because I didn't know. I thought I did, but I really didn't. I thought that I was asking too much of everybody. I thought that after barely surviving Loudcloud, nobody was ready for another do-or-die mission. I wish I knew then what I know now.

After the speech came the hard work of defining the product. The product plan was weighed down with hundreds of requirements from our existing customers. The product management team had an allergic reaction to prioritizing potentially good features above features that might hypothetically beat BladeLogic. They would say, "How can we walk away from requirements that we *know* to be true to pursue something that we *think* will help?"

It turns out that is exactly what product strategy is all about—figuring out the right product is the innovator's job, not the customer's job. The customer only knows what she thinks she wants based on her experience with the current product. The innovator can take into account everything that's possible, but often must go against what she *knows* to be true. As a result, innovation requires a combination of knowledge, skill, and courage. Sometimes only the founder has the courage to ignore the data; we were running out of time, so I had to step in:

"I don't care about any of the existing requirements; I need you to reinvent the product and we need to win." Nine months later, when we released our new product we could now win any deal. Armed with the new product, Mark Cranney, head of sales, went to war.

After assembling a top-end sales force, he completely revamped the sales process and sent every salesperson through a rigorous and unforgiving training program. He demanded mastery. Any slip-up in technique, skill, or knowledge would be met with total intolerance from Mark.

We held a weekly forecast call where Mark reviewed every deal in front of the entire 150 person sales force. On one such call, a salesperson described an account that he'd forecast in detail: "I have buy-in from my champion, the vice president that he reports to, and the head of purchasing. My champion assures me that they'll be able to complete the deal by the end of the fiscal quarter."

Mark quickly replied, "Have you spoken to the vice president's peer in the networking group?"

Sales rep: "Um, no I haven't."

Mark: "Have you spoken to the vice president yourself?"

Sales rep: "No."

Mark: "Okay, listen carefully. Here's what I'd like you to do. First, reach up to your face and take off your rose-colored glasses. Then get a Q-tip and clean the wax out of your ears. Finally, take off your pink panties and call the fucking vice president right now, because you do not have a deal."

Mark was right. It turned out that we did not have a deal, as the vice president's peer in networking was blocking it. We eventually got a meeting with him and won the deal. More important, Mark set the tone: Sloppiness would not be tolerated.

Now that we'd improved our competitive position, we went on the offensive. In my weekly staff meeting, I inserted an agenda item titled "What Are We Not Doing?" Ordinarily in a staff meeting, you spend lots of time reviewing, evaluating, and improving all of the things that you do: build products, sell products, support customers, hire employees, and the like. Sometimes, however, the things you're not doing are the things you should actually be focused on.

In one such meeting, after asking the question, every person on my staff agreed: "We are not automating the network." Although the original version of Opsware that we used in Loudcloud automated our network, the software was not robust and, of course, featured the purple-pimp-hat user interface. As a result, when we switched over to being a software company, we narrowed our focus to server automation and never revisited the decision. This worked well for the first several years of Opsware, but now we had an opportunity to bring back our network automation product.

Unfortunately, the Jive was not a good code base and could not be turned into a commercial product. My choices were: (a) start a new project or (b) buy one of the four existing network automation companies. Early in my career as an engineer, I'd learned that all decisions were objective until the first line of code was written. After that, all decisions were emotional. In addition, I had John O'Farrell, the industry's greatest M&A negotiator, on my team so I decided to investigate the other companies before sizing the internal effort.

Surprisingly, among the four existing network automation players, the company that we thought had the best product architecture, Rendition Networks, had the lowest revenues. This made some of our businesspeople skeptical of our technical evaluation. However, if I'd learned anything it was that conventional wisdom had nothing to do with the truth and the efficient market hypothesis was deceptive. How else could one explain Opsware trading at half of the cash we had in the bank when we had a $20 million a year contract and fifty of the smartest engineers in the world? No, markets weren't "efficient" at finding the truth; they were just very efficient at converging on a conclusion—often the wrong conclusion.

After confirming that acquiring would be superior to building, we negotiated a deal to buy Rendition Networks for $33 million. Within three months of completing the acquisition, John negotiated a deal with Cisco Systems—the world's largest networking company—to resell our product. The deal included an agreement to prepay us $30 million for advanced licenses. As a result, the Cisco deal alone paid more than 90 percent of the acquisition costs.

Note to self: It's a good idea to ask, "What am I not doing?"

## THE ULTIMATE DECISION

As we fielded the broader product line, our momentum steadily grew. From the ashes, we'd built a software business that approached a $150 million revenue run rate. Along with our revenue, our stock price rose from its floor of $0.35 per share as well as we traded between $6 per share and $8 per share, sometimes trading at a market capitalization of more than $800 million.

Still, everything was not rosy. Every quarter was tough, and the competitive and the technology landscapes changed rapidly. A technology called virtualization was taking the market by storm and changing the way customers thought about automating their environments. In fact, it looked to me like virtualization might be the technological breakthrough that finally enabled the cloud computing business model to work. Beyond that, being a public company was still never going to get easy. At one point, a shareholder activist named Rachel Hyman decided that my ego was out of control, and she demanded that the board remove me and sell the company immediately. This was despite the fact that we were trading at $7 per share, which was ten times the original price of her shares.

Nonetheless, I was not looking for the exits. Whenever a potential acquirer approached us, I would always reply, “We are not for sale.” It was a great answer in that I wasn’t ready to sell and it conveyed that, but it also left the door open to a particularly aggressive buyer. “Not for sale” didn’t mean that we wouldn’t listen to offers—it just meant that we weren’t trying to sell the company. So, when EMC implied that it wanted to buy us, I thought nothing of it. We were trading at about $6.50 per share and I wasn’t planning to sell at anything close to that price. But this time the news of the offer leaked to the press and the stock shot up to $9.50 per share, changing the economic equation, especially since the stock was going up for all the wrong reasons.

Ironically, the higher the stock price went up, the more companies wanted to buy us. Over the course of the next month, eleven companies expressed interest. Given the uncertainty in the business and the implied earnings multiple, their interest was too much to ignore.

To get things started, John and I called Michael Ovitz to get some advice. We felt one of the potential bidders, Oracle, would be the least likely to bid high, because it was extremely disciplined in its financial analysis. We conveyed this to Michael and questioned whether we should pursue Oracle at all. His reply was priceless: “Well, boys, if you are going to have a dog race, then you are going to need a rabbit. And Oracle will be one hell of a rabbit.”

With that strategy in hand, we generated a broad set of bids, all between $10 and $11 per share, with the highest bids representing a 38 percent premium over the current stock price. Although this was considered a good premium, I did not feel right selling the company for $11 per share. The team had worked too hard, we’d accomplished too much, and we were too good a company. The risks of staying stand-alone were substantial, but I still wanted to bet on the team. I recommended to the board that we not sell.

The board was surprised, but supportive. Still, they had a fiduciary responsibility to shareholders to ask the tough questions. “If you’re unwilling to sell at eleven dollars per share, is there a price at which you would sell?” I had to think about that one. I had promised the team that if we got to be the number-one company in a big market, we would not sell. We were number one, but how big was the market? Did the team really want to continue or was it just me who wanted to continue? How could I know without panicking the company? And thus began a series of very long talks with myself.

It was an argument to the death, and it was me against me. On the one hand, I argued that virtualization created an explosion of virtual server instances, making what we did more essential than ever. In the next breath, I retorted that while that may have been true, the architectural changes would make our market position vulnerable. I battled myself for weeks before concluding that things were changing fast enough that we’d need to make major changes to our product architecture in order to stay on top. The key to answering the ultimate question was knowing the state of the team. Were they up for yet another giant challenge or were they at the end of a very long road? I decided to bring my direct reports into the loop and ask them what they thought. The answers came back clear: Everyone, with the exception of one person who felt that the opportunity in front of us was still quite large, opted for the sale. Now it was just a matter of price. But what price?

After a long discussion with John O’Farrell, I decided that the right price to sell the company would be $14 per share, or about $1.6 billion. I took that number back to the board. They thought the number was extremely high and that it was unlikely we’d be able to generate a bid at that level, but they were supportive nonetheless. I called back all the potential acquirers and let them know that we would only entertain bids of $14 or more. There were no takers.

More than a month passed without a word, and I figured the M&A talks had ended. I began refocusing on how to make the necessary changes to keep us competitive. And then I received a call from Bob Beauchamp, the CEO of BMC Software. He offered $13.25 per share. I held firm: “Bob, that’s great, but the number is fourteen dollars per share.” Bob said that he'd have to think about it. He called back two days later and offered $14 per share. Wow. The dog had caught the bus.

John and I immediately called back all the other suitors to let them know that we had an offer that we planned to take. Hewlett-Packard was still interested and offered $13.50 per share in an effort to make sure that I wasn't bluffing. I responded that as a public company CEO, I couldn't take a lower offer. HP eventually offered $14.25 or $1.65 billion in cash. We had a deal.

When it finally ended—the long road from Loudcloud to Opsware—I couldn't believe that I'd sold what it took eight years and all of my life force to build. How could I have done that? I was sick. I couldn't sleep, I had cold sweats, I threw up, and I cried. And then I realized that it was the smartest thing that I'd ever done in my career. We'd built something from nothing, saw it go back to nothing again, and then rebuilt it into a $1.65 billion franchise.

At that point, it felt like my business life was kind of over. I had hired all the best people that I knew or could find, and I had gone through every step from founding to going public to sale. I definitely did not feel like doing any of that again. But I had learned so much. It seemed like such a waste to do something completely different. And then I got an idea to build a new kind of venture capital firm.

We will explore this idea in chapter 9, but first, chapters 4 through 8 will take you through most everything I learned to this point plus a few new war stories from my experiences running Loudcloud and Opsware.

# — CHAPTER 4 —

# WHEN THINGS FALL APART

> “There are several different frameworks one could use to get a handle on the indeterminate vs. determinate question. The math version is calculus vs. statistics. In a determinate world, calculus dominates. You can calculate specific things precisely and deterministically. When you send a rocket to the moon, you have to calculate precisely where it is at all times. It’s not like some iterative startup where you launch the rocket and figure things out step by step. Do you make it to the moon? To Jupiter? Do you just get lost in space? There were lots of companies in the ’90s that had launch parties but no landing parties.
>
> “But the indeterminate future is somehow one in which probability and statistics are the dominant modality for making sense of the world. Bell curves and random walks define what the future is going to look like. The standard pedagogical argument is that high schools should get rid of calculus and replace it with statistics, which is really important and actually useful. There has been a powerful shift toward the idea that statistical ways of thinking are going to drive the future.”

**—PETER THIEL**

When I was attempting to sell the cloud computing services part of the Loudcloud business, I met with Bill Campbell to update him on where I was with the deal. The deal was critical, because without it, the company would almost certainly go bankrupt.

After I carefully briefed him on where we were with both interested parties, IBM and EDS, Bill paused for a moment. He looked me in the eyes and said, “Ben, you need to do something in addition to working on this deal. You need to do it alone with your general counsel. You need to prepare the company for bankruptcy." To an objective observer, this might sound like Bill was prudently advising me to build my contingency plan. But something in his voice and his eyes said something different. They said that he believed the contingency plan was going to be *the* plan.

The conversation brought to mind a story that a friend told me about his brother, a young doctor. A thirty-five-year-old man came to see my friend's brother. The man looked awful. His eyes were hollow and his skin was ashen. The young doctor knew something was wrong, but he could not figure out what, so he brought in an elder colleague to help with the diagnosis. The more experienced doctor examined the man and then sent him on his way. The old doctor then turned to the young doctor and said, "He's dead." The young doctor was flabbergasted: "What are you talking about? He just walked out of here alive!" The older doctor replied, "He doesn't know it yet, but he's dead. He's had a heart attack and when people that young have heart attacks their bodies are not yet pliable enough to recover. He won't recover. He's dead." Three weeks later the patient died.

I felt that Bill was telling me, although I was walking around trying to get the deal done, that I was already dead and that I did not know it. It was a very hard thing for him to say and only the best of friends will muster the courage to break news that horrible. It was an even harder thing for me to hear. He told me so that I could emotionally prepare myself and financially prepare the company for the inevitable funeral. The odds of landing a company-saving deal during the technology industry's nuclear winter were close to nil. Chances were, I was dead.

I never built that contingency plan. Through the seemingly impossible Loudcloud series C and IPO processes, I learned one important lesson: Startup CEOs should not play the odds. When you are building a company, you must believe there is an answer and you cannot pay attention to your odds of finding it. You just have to find it. It matters not whether your chances are nine in ten or one in a thousand; your task is the same.

In the end, I did find the answer, we completed the deal with EDS, and the company did not go bankrupt. I was not mad at Bill. To this day, I sincerely appreciate his telling me the truth about the odds. But I don't believe in statistics. I believe in calculus.

**P**eople always ask me, “What’s the secret to being a successful CEO?” Sadly, there is no secret, but if there is one skill that stands out, it’s the ability to focus and make the best move when there are no good moves. It’s the moments where you feel most like hiding or dying that you can make the biggest difference as a CEO. In the rest of this chapter, I offer some lessons on how to make it through the struggle without quitting or throwing up too much.

While most management books focus on how to do things correctly, so you don’t screw up, these lessons provide insight into what you must do after you have screwed up. The good news is, I have plenty of experience at that and so does every other CEO.

I put this section first even though it deals with some serious endgame issues such as how to fire an executive and how to lay people off. In doing so, I follow the first principle of the Bushido—the way of the warrior: keep death in mind at all times. If a warrior keeps death in mind at all times and lives as though each day might be his last, he will conduct himself properly in all his actions. Similarly, if a CEO keeps the following lessons in mind, she will maintain the proper focus when hiring, training, and building her culture.

# THE STRUGGLE

Every entrepreneur starts her company with a clear vision for success. You will create an amazing environment and hire the smartest people to join you. Together you will build a beautiful product that delights customers and makes the world just a little bit better. It's going to be absolutely awesome.

Then, after working night and day to make your vision a reality, you wake up to find that things did not go as planned. Your company did not unfold like the Jack Dorsey keynote that you listened to when you started. Your product has issues that will be very hard to fix. The market isn't quite where it was supposed to be. Your employees are losing confidence and some of them have quit. Some of the ones who quit were quite smart and have the remaining ones wondering if staying makes sense. You are running low on cash and your venture capitalist tells you that it will be difficult to raise money given the impending European economic catastrophe. You lose a competitive battle. You lose a loyal customer. You lose a great employee. The walls start closing in. Where did you go wrong? Why didn't your company perform as envisioned? Are you good enough to do this? As your dreams turn into nightmares, you find yourself in *the Struggle*.

## ABOUT THE STRUGGLE

"Life is struggle."
**—KARL MARX**

The Struggle is when you wonder why you started the company in the first place.

The Struggle is when people ask you why you don't quit and you don't know the answer.

The Struggle is when your employees think you are lying and you think they may be right.

The Struggle is when food loses its taste.

The Struggle is when you don't believe you should be CEO of your company. The Struggle is when you know that you are in over your head and you know that you cannot be replaced. The Struggle is when everybody thinks you are an idiot, but nobody will fire you. The Struggle is where self-doubt becomes self-hatred.

The Struggle is when you are having a conversation with someone and you can't hear a word that they are saying because all you can hear is the Struggle.

The Struggle is when you want the pain to stop. The Struggle is unhappiness.

The Struggle is when you go on vacation to feel better and you feel worse.

The Struggle is when you are surrounded by people and you are all alone. The Struggle has no mercy.

The Struggle is the land of broken promises and crushed dreams. The Struggle is a cold sweat. The Struggle is where your guts boil so much that you feel like you are going to spit blood.

The Struggle is not failure, but it causes failure. Especially if you are weak. Always if you are weak.

Most people are not strong enough.

Every great entrepreneur from Steve Jobs to Mark Zuckerberg went through the Struggle and struggle they did, so you are not alone. But that does not mean that you will make it. You may not make it. That is why it is the Struggle.

The Struggle is where greatness comes from.

## SOME STUFF THAT MAY OR MAY NOT HELP

There is no answer to the Struggle, but here are some things that helped me:

- *Don't put it all on your shoulders.* It is easy to think that the things that bother you will upset your people more. That's not true. The opposite is true. Nobody takes the losses harder than the person most responsible. Nobody feels it more than you. You won't be able to share every burden, but share every burden that you can. Get the maximum number of brains on the problems even if the problems represent existential threats. When I ran Opsware and we were losing too many competitive deals, I called an all hands and told the whole company that we were getting our asses kicked, and if we didn't stop the bleeding, we were going to die. Nobody blinked. The team rallied, built a winning product, and saved my sorry ass.

- *This is not checkers; this is motherfuckin' chess.* Technology businesses tend to be extremely complex. The underlying technology moves, the competition moves, the market moves, the people move. As a result, like playing three-dimensional chess on *Star Trek*, there is always a move. You think you have no moves? How about taking your company public with $2 million in trailing revenue and 340 employees, with a plan to do $75 million in revenue the next year? I made that move. I made it in 2001, widely regarded as the worst time ever for a technology company to go public. I made it with six weeks of cash left. There is always a move.
- *Play long enough and you might get lucky.* In the technology game, tomorrow looks nothing like today. If you survive long enough to see tomorrow, it may bring you the answer that seems so impossible today.
- *Don't take it personally.* The predicament that you are in is probably all your fault. You hired the people. You made the decisions. But you knew the job was dangerous when you took it. Everybody makes mistakes. Every CEO makes thousands of mistakes. Evaluating yourself and giving yourself an F doesn't help.
- *Remember that this is what separates the women from the girls.* If you want to be great, this is the challenge. If you don't want to be great, then you never should have started a company.

## THE END

When you are in the Struggle, nothing is easy and nothing feels right. You have dropped into the abyss and you may never get out. In my own experience, but for some unexpected luck and help, I would have been lost.

So to all of you in it, may you find strength and may you find peace.

# CEOS SHOULD TELL IT LIKE IT IS

One of the most important management lessons for a founder/CEO is totally unintuitive. My single biggest personal improvement as CEO occurred on the day when I stopped being too positive.

As a young CEO, I felt the pressure—the pressure of employees depending on me, the pressure of not really knowing what I was doing, the pressure of being responsible for tens of millions of dollars of other people's money. As a consequence of this pressure, I took losses extremely hard. If we failed to win a customer or slipped a date or shipped a product that wasn't quite right, it weighed heavily on me. I thought that I would make the problem worse by transferring that burden to my employees. Instead, I thought I should project a positive, sunny demeanor and rally the unburdened troops to victory. I was completely wrong.

I realized my error during a conversation with my brother in-law, Cartheu. At the time, Cartheu worked for AT&T as a telephone lineman (he is one of those guys who climb the poles). I had just met a senior executive at AT&T, whom I'll call Fred, and I was excited to find out if Cartheu knew him. Cartheu said, "Yeah, I know Fred. He comes by about once a quarter to blow a little sunshine up my ass." At that moment, I knew that I'd been screwing up my company by being too positive.

In my mind, I was keeping everyone in high spirits by accentuating the positive and ignoring the negative. But my team knew that reality was more nuanced than I was describing it. And not only did they see for themselves the world wasn't as rosy as I was describing it; they still had to listen to me blowing sunshine up their butts at every company meeting.

How did I make such a mistake and why was it such a big mistake?

## THE POSITIVITY DELUSION

As the highest-ranking person in the company, I thought that I would be best able to handle bad news. The opposite was true: Nobody took bad news harder than I did. Engineers easily brushed off things that kept me awake all night. After all, I was the founding CEO. I was the one "married" to the company. If things went horribly wrong, they could walk away, but I could not. As a consequence, the employees handled losses much better.

Even more stupidly, I thought that it was my job and my job only to worry about the company's problems. Had I been thinking more clearly, I would have realized that it didn't make sense for me to be the only one to worry about, for example, the product not being quite right—because I wasn't writing the code that would fix it.

A much better idea would have been to give the problem to the people who could not only fix it, but who would also be personally excited and motivated to do so. Another example: If we lost a big prospect, the whole organization needed to understand why, so that we could together fix the things that were broken in our products, marketing, and sales process. If I insisted on keeping the setbacks to myself, there was no way to jump-start that process.

## WHY IT'S IMPERATIVE TO TELL IT LIKE IT IS

There are three key reasons why being transparent about your company's problems makes sense:

### 1. Trust.

Without trust, communication breaks. More specifically:

In any human interaction, the required amount of communication is inversely proportional to the level of trust.

Consider the following: If I trust you completely, then I require no explanation or communication of your actions whatsoever, because I know that whatever you are doing is in my best interests. On the other hand, if I don't trust you at all, then no amount of talking, explaining, or reasoning will have any effect on me, because I do not trust that you are telling me the truth.

In a company context, this is a critical point. As a company grows, communication becomes its biggest challenge. If the employees fundamentally trust the CEO, then communication will be vastly more efficient than if they don't. Telling things as they are is a critical part of building this trust. A CEO's ability to build this trust over time is often the difference between companies that execute well and companies that are chaotic.

**2. The more brains working on the hard problems, the better.**

In order to build a great technology company, you have to hire lots of incredibly smart people. It's a total waste to have lots of big brains but not let them work on your biggest problems. A brain, no matter how big, cannot solve a problem it doesn't know about. As the open-source community would explain it, "Given enough eyeballs, all bugs are shallow."

**3. A good culture is like the old RIP routing protocol: Bad news travels fast; good news travels slow.**

If you investigate companies that have failed, you will find that many employees knew about the fatal issues long before those issues killed the company. If the employees knew about the deadly problems, why didn't they say something? Too often the answer is that the company culture discouraged the spread of bad news, so the knowledge lay dormant until it was too late to act.

A healthy company culture encourages people to share bad news. A company that discusses its problems freely and openly can quickly solve them. A company that covers up its problems frustrates everyone involved. The resulting action item for CEOs: Build a culture that rewards—not punishes—people for getting problems into the open where they can be solved.

As a corollary, beware of management maxims that stop information from flowing freely in your company. For example, consider the old management standard: "Don't bring me a problem without bringing me a solution." What if the employee cannot solve an important problem? For example, what if an engineer identifies a serious flaw in the way the product is being marketed? Do you really want him to bury that information? Management truisms like these may be good for employees to aspire to in the abstract, but they can also be the enemy of free-flowing information—which may be critical for the health of the company.

## FINAL THOUGHT

If you run a company, you will experience overwhelming psychological pressure to be overly positive. Stand up to the pressure, face your fear, and tell it like it is.

# THE RIGHT WAY TO LAY PEOPLE OFF

Shortly after we sold Opsware to Hewlett-Packard, I had a conversation with the legendary venture capitalist Doug Leone of Sequoia Capital. He wanted me to recount the story of how we went from doomed in the eyes of the world to a $1.6 billion outcome with no recapitalization.

After I took him through the details—including several near bankruptcies, a stock price of $0.35 per share, unlimited bad press, and three separate layoffs where we lost a total of four hundred employees—he was most amazed by the layoffs. During more than twenty years in the venture capital business, he'd never seen a company recover from consecutive layoffs and achieve a billion-dollar-plus outcome. He confessed that he'd bet against that every time. Since my only experience was the great exception, I needed more information. I asked him why all the other startups failed. He replied that the layoffs inevitably broke the company's culture. After seeing their friends laid off, employees were no longer willing to make the requisite sacrifices needed to build a company. He said that although it was possible to survive an isolated layoff, it was hugely unlikely that a company would experience great success. Building a highly valuable business, he added, after three consecutive giant layoffs accompanied by horrible prominent press coverage (we got taken apart with cover stories in both the *Wall Street Journal* and *BusinessWeek*), was a complete violation of the laws of venture capital physics. He wanted to know how we did it. After thinking about this question, here's my answer.

In retrospect, we were able to keep cultural continuity and retain our best employees despite multiple massive layoffs because we laid people off the right way. This may sound nutty—how can you do something that's fundamentally wrong in "the right way"? Here's how.

## STEP 1: GET YOUR HEAD RIGHT

When a company fails to hit its financial plan so severely that it must fire the employees it went to great time and expense to hire, it weighs heavily on the chief executive. During the first layoff at our company, I remember being forwarded an email exchange among a group of employees. In the exchange, one of our smarter employees wrote, “Ben is either lying or stupid or both.” I remember reading that and thinking, “definitely stupid.” During a time like this, it is difficult to focus on the future, because the past overwhelms you—but that’s exactly what you must do.

### STEP 2: DON’T DELAY

Once you decide that you will have to lay people off, the time elapsed between making that decision and executing that decision should be as short as possible. If word leaks (which it will inevitably if you delay), then you will be faced with an additional set of issues. Employees will question managers and ask whether a layoff is coming. If the managers don’t know, they will look stupid. If the managers do know, they will either have to lie to their employees, contribute to the leak, or remain silent, which will create additional agitation. At Loudcloud/Opsware, we badly mismanaged this dynamic with our first round of layoffs, but sharply corrected things on the next two.

### STEP 3: BE CLEAR IN YOUR OWN MIND ABOUT WHY YOU ARE LAYING PEOPLE OFF

Going into a layoff, board members will sometimes try to make you feel better by putting a positive spin on things. They might say, “This gives us a great opportunity to deal with some performance issues and simplify the business.” That may be true, but do not let that cloud your thinking or your message to the company. You are laying people off because the company failed to hit its plan. If individual performance were the only issue, then you’d be taking a different measure. *Company* performance failed. This distinction is critical, because the message to the company and the laid-off individuals should not be “This is great, we are cleaning up performance.” The message must be “The company failed and in order to move forward, we will have to lose some excellent people.” Admitting to the failure may not seem like a big deal, but trust me, it is. “Trust me.” That’s what a CEO says every day to her employees. Trust me: This will be a good company. Trust me: This will be good for your career. Trust me: This will be good for your life. A layoff breaks that trust. In order to rebuild trust, you have to come clean.

## STEP 4: TRAIN YOUR MANAGERS

The most important step in the whole exercise is training the management team. If you send managers into this super-uncomfortable situation with no training, most of them will fail.

Training starts with a golden rule: *Managers must lay off their own people*. They cannot pass the task to HR or to a more sadistic peer. You cannot hire an outsourcing firm like the one in the movie *Up in the Air*. Every manager must lay off his own people.

Why so strict? Why can’t the more confrontational managers just handle this task for everyone? Because people won’t remember every day they worked for your company, but they will surely remember the day you laid them off. They will remember every last detail about that day and the details will matter greatly. The reputations of your company and your managers depend on you standing tall, facing the employees who trusted you and worked hard for you. If you hired me and I busted my ass working for you, I expect you to have the courage to lay me off yourself.

Once you make it clear that managers must lay off their own people, be sure to prepare them for the task:

**1.** They should explain briefly what happened and that it is a company rather than a personal failure.

**2.** They should be clear that the employee is impacted and that the decision is nonnegotiable.

**3.** They should be fully prepared with all of the details about the benefits and support the company plans to provide.

## STEP 5: ADDRESS THE ENTIRE COMPANY

Prior to executing the layoff, the CEO must address the company. The CEO must deliver the overall message that provides the proper context and air cover for the managers. If you do your job right, the managers will have a much easier time doing their jobs. Keep in mind what former Intuit CEO Bill Campbell told me—*The message is for the people who are staying*. The people who stay will care deeply about how you treat their colleagues. Many of the people whom you lay off will have closer relationships with the people who stay than you do, so treat them with the appropriate level of respect. Still, the company must move forward, so be careful not to apologize too much.

## STEP 6: BE VISIBLE, BE PRESENT

After you make the speech telling your company that you will be letting many of them go, you will not feel like hanging out and talking to people. You will probably feel like going to a bar and drinking a fifth of tequila. Do not do this. Be present. Be visible. Be engaging. People want to see you. They want to see whether you care. The people whom you laid off will want to know if they still have a relationship with you and the company. Talk to people. Help them carry their things to their cars. Let them know that you appreciate their efforts.

# PREPARING TO FIRE AN EXECUTIVE

When you recruit an executive, you paint a beautiful picture of her future in your company. You describe in great depth and in vibrant color how awesome it will be for her to accept your offer and how much better it will be than joining that other company. Then one day you realize you must fire her. Reconcile that, Ms. CEO.

It turns out that the actual act of firing an executive can be relatively easy compared with any other firing. Executives have experience being on the other side of the conversation and tend to be quite professional. Firing an executive correctly is a bit more complicated and extremely important. If you do not learn the right lessons, you will be doing it again soon.

Like so many things, the key to correctly firing an executive is preparation. Here is a four-step process that will treat the executive fairly and improve your company.

## STEP 1: ROOT CAUSE ANALYSIS

While it's possible to fire an executive for bad behavior, incompetence, or laziness, those cases are rare and relatively easy. Unfortunately, unless you have a horribly deficient hiring process, those are probably not the reasons why you got to this point. At this level, almost every company screens for the proper skill set, motivation, and track record. Yes, the reason that you have to fire your head of marketing is not because he sucks; it's because *you* suck.

In other words, the wrong way to view an executive firing is as an executive failure; the correct way to view an executive firing is as an interview/integration process system failure. Therefore, the first step to properly firing an executive is figuring out why you hired the wrong person for your company.

You may have blown it for a variety of reasons:

- *You did a poor job defining the position in the first place.* If you don't know what you want, you will be unlikely to get it. Far too often, CEOs hire executives based on an abstract notion of what they think and feel the executive should be like. This error often leads to the executive not bringing the key, necessary qualities to the table.
- *You hired for lack of weakness rather than for strengths.* This is especially common when you run a consensus-based hiring process. The group will often find the candidate's weaknesses, but they won't place a high enough value on the areas where you need the executive to be a world-class performer. As a result, you hire an executive with no sharp weaknesses, but who is mediocre where you need her to be great. If you don't have world-class strengths where you need them, you won't be a world-class company.
- *You hired for scale too soon.* The most consistently wrong advice that venture capitalists and executive recruiters give CEOs is to hire someone "bigger" than required. "Think about the next three to five years and how you will be a large company" is how the bad advice usually sounds. It's great to hire people who can run a large-scale organization if you have one. It's also great to hire people who know how to grow an organization very fast if you are ready to grow your organization very fast. However, if you do not or you are not, then you need someone who can do the job for the next eighteen months. If you hire someone who will be great *in* eighteen months but will be poor for the next eighteen months, the company will reject her before she ever gets a chance to show her stuff. Your other employees will wonder: Why did we give her all those stock options when she's not contributing anything? Those kinds of questions are impossible to recover from. It turns out that venture capitalists and executive recruiters are not stupid; they just learned the wrong lessons from previous failures. To learn the right lesson, see the *special case of scaling* and *the special case of fast growth* as explained below.
- *You hired for the generic position.* There is no such thing as a great CEO, a great head of marketing, or a great head of sales. There is only a great head of sales for your company for the next twelve to twenty-four months. That position is not the same as the same position at

Microsoft or Facebook. Don't look for the candidate out of central casting. This is not a movie.

- *The executive had the wrong kind of ambition.* In chapter 6, I will describe the difference between ambition for the company and ambition for oneself. If an executive has the wrong kind of ambition, then despite her skills, the company may reject her.
- *You failed to integrate the executive.* Bringing a new person into your company in an important role is difficult. Other employees will be quick to judge, her expectations may be different from yours, and the job may be largely undefined. Be sure to review and improve your integration plan after you fire an executive.

### The special case of scaling

A fairly common reason for firing an executive is that when the company quadruples in size, the executive no longer does the job effectively at the new size. The reason is that when a company multiplies in size, the management jobs become brand-new jobs. As a result, everybody needs to requalify for the new job, because the new job and the old job are not the same. Running a two-hundred-person global sales organization is not the same job as running a twenty-five-person local sales team. If you get lucky, the person you hired to run the twenty-five-person team will have learned how to run the two-hundred-person team. If not, you need to hire the right person for the new job. This is neither an executive failure nor a system failure; it is life in the big city. Do not attempt to avoid this phenomenon, as you will only make things worse.

### The special case of fast growth

If you build a great product and the market wants it, you will find yourself needing to grow your company extremely quickly. Nothing will ensure your success like hiring the right executive who has grown an organization like yours very quickly and successfully before. Note that this is not the same as inheriting a very large organization or working your way up to running a very large organization. Make sure you hire the right kind of fast-growth executive. Also, do not hire this person if you are not ready to give them lots of budget to grow their organization; expect them to do what they do.

The successful fast-growth executive is so important to building successful startups that recruiters and venture capitalists often advise CEOs to bring them in before the company is ready.

Once you identify the problem, then you create the basis for the next steps.

## STEP 2: INFORMING THE BOARD

Informing the board is tricky and many issues can further complicate the task:

- This is the fifth or sixth executive that you had to fire.
- This is the third executive that you fired in this role.
- The candidate was referred by a board member who recommended the executive as a superstar.

Realize that in any of these cases the board will be at least somewhat alarmed and there is nothing that you can do about that. But keep in mind that your choices are: (a) alarm the board or (b) enable an ineffective executive to remain in her position. While choice (a) is not great, it's a heck of a lot better than choice (b). Leaving a failing leader in place will cause an entire department in your company to slowly rot. Let that happen and the board will be more than alarmed.

You should have three goals with the board:

- *Get their support and understanding for the difficult task that you will execute.* You should start by making sure that they understand the root cause and your plan to remedy the situation. This will give them confidence in your ability to hire and manage outside executives in the future.
- *Get their input and approval for the separation package.* This will be critical for the next step. Executive packages are larger than regular severance packages and rightly so. It takes about ten times longer for an executive to find a new job than it does for an individual contributor.

- *Preserve the reputation of the fired executive.* The failure was very likely a team effort, and it's best to portray it that way. You don't make yourself look good by trashing someone who worked for you. A mature approach to this issue will help keep the board confident in your ability to be CEO. It's also the fair and decent thing to do.

Finally, firing an executive turns out to be a piece of news that's handled better with individual phone calls than in dramatic fashion during a board meeting. It takes a bit longer, but it's well worth the effort. Individual conversations will be particularly important if one of the board members introduced the executive to the company. Once everyone agrees individually, you can finalize the details in a board meeting or call.

## STEP 3: PREPARING FOR THE CONVERSATION

After you know what went wrong and have informed the board, you should tell the executive as quickly as possible. In preparation for that meeting, I recommend scripting or rehearsing what you plan to say so that you do not misspeak. The executive will remember the conversation for a very long time, so you need to get it right.

As part of your preparation, you should review any performance reviews or written performance conversations to understand any inconsistencies in your prior communication.

Three keys to getting it right:

**1.** *Be clear on the reasons.* You have thought about this long and hard; don't equivocate or sugarcoat it. You owe it to them to be clear about what you think happened.

**2.** *Use decisive language.* Do not leave the discussion open-ended. This is not a performance review; it's a firing. Use words and phrases like "I have decided" rather than "I think."

**3.** *Have the severance package approved and ready.* Once the executive hears the news, she will stop caring about the company and its issues; she will be highly focused on herself and her family. Be ready to provide specific details of the severance package.

Finally, the executive will be keenly interested in how the news will be communicated to the company and to the outside world. It is best to let her decide. Bill Campbell once gave me a critical bit of advice when I was preparing to fire an executive. He said, “Ben, you cannot let him keep his job, but you absolutely can let him keep his respect.”

## STEP 4: PREPARING THE COMPANY COMMUNICATION

After you have informed the executive, you must quickly update the company and your staff on the change. The correct order for informing the company is (1) the executive’s direct reports—because they will be most impacted; (2) the other members of your staff—because they will need to answer questions about it; and (3) the rest of the company. All of these communications should happen on the same day and preferably within a couple of hours. When disclosing the firing to the direct reports, make sure that you have a plan for whom they will report to in the meantime and what’s next (executive search, reorganization, internal promotion, or something else). Generally, it’s smart for the CEO to act in the executive role in the meanwhile. If you do act in the role, you must really act—staff meetings, one-on-ones, objective setting, etc. Doing so will provide excellent continuity for the team and greatly inform your thinking on whom to hire next.

As you did when you updated the board, keep the message positive and refrain from throwing the executive under the bus. The best employees in the organization will likely be the ones closest to the executive. If you trash her, you will put all her best employees on notice that they are next. Is that a message you want to send?

When you update the company, you might worry about employees misinterpreting the news and thinking the company is in trouble. Do not try to maneuver around such a reaction. When you expect your employees to act like adults, they generally do. If you treat them like children, then get ready for your company to turn into one big *Barney* episode.

## IN THE END

Every CEO likes to say she runs a great company. It’s hard to tell whether the claim is true until the company or the CEO has to do something really difficult. Firing an executive is a good test.

# DEMOTING A LOYAL FRIEND

When I started Loudcloud, I hired the best people I knew—people whom I respected, trusted, and liked. Like me, many of them did not have deep experience in the jobs that I gave them, but they worked night and day to learn, and they made great contributions to the company. Nevertheless, the day came when I needed to hire someone else, someone with more experience, to run the function that I had previously entrusted to my loyal friend. Damn. How do you do that?

## SHOULD YOU DO IT AT ALL?

The first question that always comes to mind is "Do I really need to do this? Who could I possibly hire who will work this hard and bleed the company colors like this?" Sadly, if you're asking the question, you very likely already know the answer. If you need to build a worldwide sales organization, your buddy who did the first few deals is almost certainly not the best choice. As hard as it may be, you need to take a Confucian approach. You must consider first all of the other employees and second your friend. The good of the individual must be sacrificed for the good of the whole.

## HOW DO YOU BREAK THE NEWS?

Once you make the decision, breaking the news will not be easy. It's important to consider two deep emotions your friend will feel:

- **Embarrassment** Do not underestimate what a large factor this will be in his thinking. All of his friends, relatives, and colleagues know his current position. They know how hard he's worked and how much he's sacrificed for the company. How will he possibly explain to them that he will no longer be part of the executive team?

- **Betrayal** Your friend will undoubtedly feel something like this: I've been there from the beginning, I've worked side by side with you. How could you do this? It's not like you're perfect in your job, either. How can you be so comfortable selling me out?

Those are some powerful emotions, so get ready for an intense discussion. Ironically, the key to an emotional discussion is to take the emotion out of it. To do that, you must be very clear in your mind about what you've decided and what you want to do.

The most important thing to decide is that you really want to do this. If you walk into a demotion discussion with an open decision, you will walk out with a mess: a mess of a situation and a mess of a relationship. As part of the decision, you must get comfortable with the thought that the employee may quit the company. Given the intense emotions he will feel, there is no guarantee that he will want to stay. If you cannot afford to lose him, you cannot make this change.

Finally, you must decide the best role for him in your company. The obvious thing is to have him continue under his new boss, but this may not be the best thing for him, his boss, or his career. Your loyal employee will continue to have lots of knowledge about your company, competition, customers, and market that his new boss lacks. On the one hand, this can be a good thing—he can help get the new boss up to speed. On the other hand, when mixed with the intense emotions of embarrassment and betrayal, you might end up with a sabotage cocktail.

Another problem with this approach is that from a career path perspective there is no way to paint a picture of him reporting to his new boss as anything but a demotion. An alternative, if appropriate, would be to move him to another area of the company where his skills, talent, and knowledge will help. This kind of move will give him a chance to develop a new set of skills and help the company while he's doing it. For young employees, getting experience in different areas can be highly valuable.

Sadly, this option may not be a silver bullet. He might not want to work in another job; he might be hell-bent on keeping his current job, so prepare for that as well.

Once you've decided to hire someone above your friend and decided on the alternatives that you'd like to offer him, you can have the conversation.

Keep in mind that you cannot let him keep his old job, but you can be fair and you can be honest. Some keys to doing that:

- *Use appropriate language.* Make clear with your language that you've decided. As previously discussed, use phrases like "I have decided" rather than "I think" or "I'd like." By doing this, you will avoid putting the employee in the awkward position of wondering whether he should lobby for his old job. You can't tell him what he wants to hear, but you can be honest.
- *Admit reality.* If you are a founder-CEO like I was, it probably won't be lost on the employee that you are just as underskilled for your job as he is for his. Don't dodge this fact. In fact, admit that if you were a more experienced CEO, you might be able to develop him into the role, but two people who don't know what they are doing is a recipe for failure.
- *Acknowledge the contributions.* If you want him to stay in the company, you should say that and make it crystal clear that you want to help him develop his career and contribute to the company. Let him know that you appreciate what he's done and that your decision results from a forward-looking examination of what the company needs, not a review of his past performance. The best way to do this, if appropriate, is to couple the demotion with an *increase* in compensation. Doing so will let him know that he's both appreciated and valued going forward.

Through all of this, keep in mind that it is what it is and nothing you can say will change that or stop it from being deeply upsetting. Your goal should not be to take the sting out of it, but to be honest, clear, and effective. Your friend may not appreciate that in the moment, but he will appreciate it over time.

# LIES THAT LOSERS TELL

When a company starts to lose its major battles, the truth often becomes the first casualty. CEOs and employees work tirelessly to develop creative narratives that help them avoid dealing with the obvious facts. Despite their intense creativity, many companies often end up with the same false explanations.

**SOME FAMILIAR LIES**

"She left, but we were going to fire her, or give her a bad performance review." High-tech companies tend to track employee attrition in three categories:

**1.** People who quit

**2.** People who got fired

**3.** People who quit, but it's okay because the company didn't want them anyway

Fascinatingly, as companies begin to struggle, the third category always seems to grow much faster than the first. In addition, the sudden wave of "semi-performance-related attrition" usually happens in companies that claim to have a "super-high talent bar." How do all these superstar employees suddenly go from great to crap? How is it possible that when you lose a top-rated employee before you can say "unwanted attrition," the manager carefully explains how her performance fell off?

"We would have won, but the other guys gave the deal away." "The customer selected us technically and thinks we are the better company, but our competitor just gave the product away. We would never sell so cheaply as it would hurt our reputation." Anybody who has ever run an enterprise sales force has heard this lie before. You go into an account, you fight hard, and you lose. The sales rep, not wanting to shine the light on himself, blames the "used car dealer" rep from the other company. The CEO, not wanting to believe that she's losing product competitiveness, believes the rep. If you hear this lie, try to validate the claim with the actual customer. I'll bet you can't.

"Just because we missed the intermediate milestones doesn't mean we won't hit our product schedule." In engineering meetings where there is great pressure to ship on time—a customer commitment, a quarter that depends on it, or a competitive imperative—everybody hopes for good news. When the facts don't align with the good news, a clever manager will find the narrative to make everybody feel better—until the next meeting.

"We have a very high churn rate, but as soon as we turn on email marketing to our user base, people will come back." Yes, of course. The reason that people leave our service and don't come back is that we have not been sending them enough spam. That makes total sense to me, too.

Where do lies come from?

To answer that question, I thought back to a conversation I had years ago with the incomparable Andy Grove.

Back at the tail end of the Great Internet Bubble in 2001, as all the big technology companies began missing their quarters by giant amounts, I found myself wondering how none of them saw it coming. One would think that after the dot-com crash of April 2000, companies like Cisco, Siebel, and HP would realize that they would soon face a slowdown as many of their customers hit the wall. But despite perhaps the most massive and public early warning system ever, each CEO reiterated strong guidance right up to the point where they dramatically whiffed their quarters.

I asked Andy why these great CEOs would lie about their impending fate.

He said they were not lying to investors, but rather, they were lying to themselves.

Andy explained that humans, particularly those who build things, only listen to leading indicators of good news. For example, if a CEO hears that engagement for her application increased an incremental 25 percent beyond the normal growth rate one month, she will be off to the races hiring more engineers to keep up with the impending tidal wave of demand. On the other hand, if engagement decreases 25 percent, she will be equally intense and urgent in explaining it away: “The site was slow that month, there were four holidays, and we made a UI change that caused all the problems. For gosh sakes, let’s not panic!”

Both leading indicators may have been wrong, or both may have been right, but our hypothetical CEO—like almost every other CEO—only took action on the positive indicator and only looked for alternative explanations on the negative leading indicator.

If this advice sounds too familiar. and you find yourself wondering why your honest employees are lying to you, the answer is they are not. They are lying to themselves.

And if you believe them, you are lying to yourself.

# LEAD BULLETS

Early in my tenure at Netscape, when we realized that Microsoft's new Web server had every feature that ours had, but was also five times faster and was to be given away for free, I immediately went to work trying to pivot our server product line to something that we could sell for money. The late, great Mike Homer and I worked furiously on a set of partnerships and acquisitions that would broaden the product line and surround the Web server with enough functionality that we would be able to survive the attack.

I excitedly reviewed the plan with my engineering counterpart, Bill Turpin, who looked at me as though I were a little kid who had much to learn. Bill was a longtime veteran of battling Microsoft from his time at Borland and understood what I was trying to do, but he was not persuaded. He said, "Ben, those silver bullets that you and Mike are looking for are fine and good, but our Web server is five times slower. There is no silver bullet that's going to fix that. No, we are going to have to use a lot of lead bullets." Oh snap.

As a result of Bill's advice, we focused our engineering team on fixing the performance issues while working on the other things in the background. We eventually beat Microsoft's performance and grew the server line to become a $400 million business, and we would never have done it without those lead bullets.

I carried that lesson with me for many years. Six years later, when I was CEO of Opsware, our toughest competitor, BladeLogic, started to consistently beat us in large deals. We were a public company, and the losses were all too visible. To make matters worse, we needed to win those deals in order to beat Wall Street's projections, so the company felt tremendous pressure. Many of our smartest people came to me with ideas for avoiding the battle:

- “Let’s build a lightweight version of the product and go down-market.”
- “Let’s acquire a company with a simpler architecture.”
- “Let’s focus on service providers.”

All these approaches reinforced to me was that we weren’t facing a market problem. The customers were buying; they just weren’t buying *our* product. This was not a time to pivot. So I said the same thing to every one of them: “There are no silver bullets for this, only lead bullets.” They did not want to hear that, but it made things clear: We had to build a better product. There was no other way out. No window, no hole, no escape hatch, no back door. We had to go through the front door and deal with the big, ugly guy blocking it. Lead bullets.

After nine months of hard work on an extremely rugged product cycle, we regained our product lead and eventually built a company that was worth $1.6 billion. Without the lead bullets, I suspect we would have ended at about one-tenth that value.

There may be nothing scarier in business than facing an existential threat. So scary that many in the organization will do anything to avoid facing it. They will look for any alternative, any way out, any excuse not to live or die in a single battle. I see this often in startup pitches. The conversations go something like this:

Entrepreneur: “We have the best product in the market by far. All the customers love it and prefer it to competitor X.”

Me: “Why does competitor X have five times your revenue?”

Entrepreneur: “We are using partners and OEMs, because we can’t build a direct channel like competitor X.”

Me: “Why not? If you have the better product, why not knuckle up and go to war?”

Entrepreneur: “Ummm.”

Me: “Stop looking for the silver bullet.”

There comes a time in every company’s life where it must fight for its life. If you find yourself running when you should be fighting, you need to ask yourself, “If our company isn’t good enough to win, then do we need to exist at all?”

# NOBODY CARES

"Just win, baby."
**—AL DAVIS**

Back in those bad old days at Loudcloud, I often thought to myself: How could I have possibly prepared for this? How could I know that half our customers would go out of business? How could I know that it would become impossible to raise money in the private markets? How could I have figured out that there would be 221 IPOs in 2000 and 19 in 2001? Could anybody expect me to achieve a reasonable outcome given those circumstances?

As I was feeling sorry for myself, I randomly watched an interview with famous football coach Bill Parcells. He was telling the story of how he had a similar dilemma when he began his head coaching career. In his very first season, Parcells's team, the New York Giants, was hit with a rash of injuries. He worried incessantly about the impact of the injuries on his team's fortunes, as it is difficult enough to win with your best players, let alone a bunch of substitutes. When his friend and mentor, Raiders owner Al Davis, called Parcells to check in, Parcells relayed his injury issues.

Parcells: "Al, I am just not sure how we can win without so many of our best players. What should I do?"

Davis: "Bill, nobody cares, just coach your team."

That might be the best CEO advice ever. Because, you see, nobody cares. When things go wrong in your company, nobody cares. The media don't care, your investors don't care, your board doesn't care, your employees don't care, and even your mama doesn't care.

Nobody cares.

And they are right not to care. A great reason for failing won't preserve one dollar for your investors, won't save one employee's job, or get you one new customer. It especially won't make you feel one bit better when you shut down your company and declare bankruptcy.

All the mental energy you use to elaborate your misery would be far better used trying to find the one seemingly impossible way out of your current mess. Spend zero time on what you could have done, and devote all of your time on what you might do. Because in the end, nobody cares; just run your company.