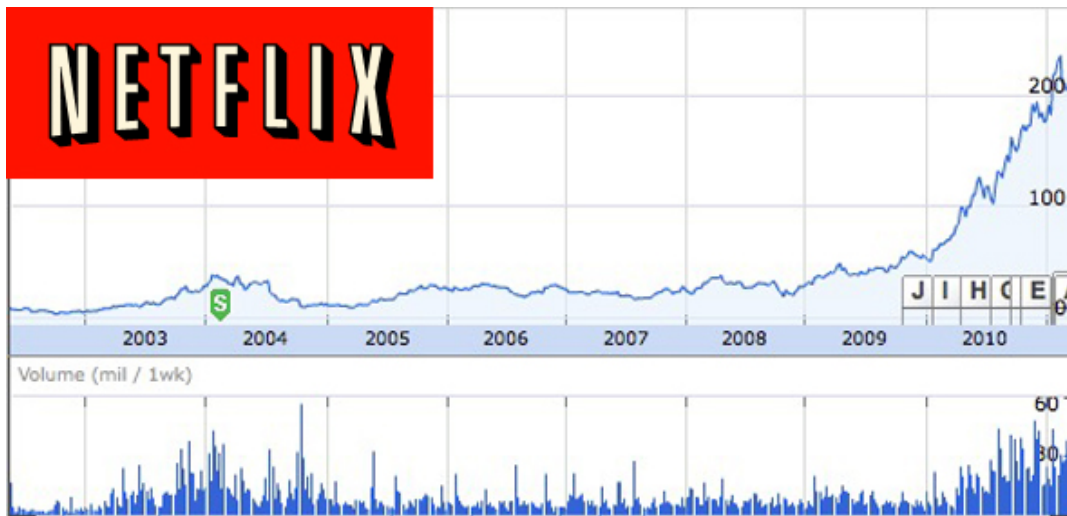


Leadership Lessons from Netflix

Written by Nick Sanders
Tuesday, 23 April 2013 00:00



Back in the 1990's the Defense Department wanted to be more like Silicon Valley. The Pentagon felt it was no longer the "leading edge" of technological innovation, despite the many hundreds of millions of dollars it continued to spend on contractor Independent Research and Development (IR&D) costs each year. It believed it was hamstrung by onerous MILSPEC requirements, by "non value-added" administrative controls—and by a prescriptive, bureaucratic, culture adverse to risk-taking. The period from 1992 to 2000 was largely defined by broad attempts to "reinvent" government in an effort to make it "work better and cost less"—and many of those reform initiatives were aimed at (*and embraced by*) those in the defense acquisition field.

Since then, not so much.

The Obama Administration's "acquisition reform" efforts (to the extent they qualify for that description) have seemed, by and large, to focus on undoing the acquisition reform efforts of the Clinton Administration. We have studied the contrasting efforts at acquisition reform, and concluded that Clinton-era reform efforts imbued Federal employees with enhanced discretion, but failed to impose commensurate levels of accountability. This failure led to well-documented abuses during the Bush Presidency; and ultimately it led to more prescriptive bureaucratic processes and controls imposed on acquisition professionals during the Obama Presidency. Failing to find accountability, the Obama Administration seemingly has chosen to limit discretion.

It's about culture, not processes. But culture has never been the strong suit of any large bureaucracy; it's far easier to focus on changing processes rather than changing culture.

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Moreover, growth seems to inevitably lead to imposition of additional processes: the larger and more complex the organization, the more it seemingly focuses on imposing control processes in order to assure its people are working toward strategic objectives. Attempts to streamline bureaucracy and reduce control process are themselves implemented via new, additional, processes. We've [discussed this phenomenon](#) with respect to the DOD's Better Buying Power initiative before. We quoted J. David Patterson, Director of the National Defense Business Institute at the University of Tennessee, who stated, "Suborning people to processes results in the least-productive bureaucratic behaviors." In other words, if you want change, you need to focus on people and culture, not processes.

Being ourselves implementers of process change and not cultural change, we've wondered about organizations that focus on process and ignore culture—especially those that contract with the Defense Department. We've noticed that the larger and more successful government contractors seem to mimic the Executive Branch's own organization and culture—and perhaps that's what makes them so successful.

But does it always have to be this way? Should we simply accept the onerous rules and regulations and business processes as a fact of life in the government contracting environment? Is it endemic only to the defense acquisition arena, a by-product of a multi-level hierarchy coupled with political pressure and the occasional newspaper headline? Or is it perhaps some immutable axiom of organizational behavior, a phase that all organizations grow into as they increase in size and complexity?

Is there a way out?

Well, we don't know the answers to all of our questions, but we do know that Netflix thinks it both understands the problem and has found a solution to it. And Netflix has documented its corporate analysis in a 126-page slideshow, which we provide below.

[Culture](#) from [Reed Hastings](#)

Now we know you. You are not going to click through 126 pages of somebody telling you about their corporate culture. You don't have the patience, and you don't think it applies to your organization in any case. And there's a real argument to be made that, no matter how innovative and cross-my-heart-true this cultural approach sounds, it simply could never be implemented in your organization. We get that. Which is why we are going to print selected quotes and paraphrases from the Netflix slideshow.

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Consider the following as statements of cultural philosophy, as statements of intent to create and foster a unique culture. Consider how you could, in a perfect world, unfettered by your HR policies and procedures, implement them within your organization. Consider the impact. Consider what it would be like to work in such a culture.

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Actual company values, as opposed to the *nice-sounding* values, are shown by who gets rewarded, promoted, or let go. *Actual*
company values are the *behaviors*
and *skills*
that are *valued*
in fellow employees. At Netflix, we value nine behaviors and skills: Judgment, Communication, Impact, Curiosity, Innovation, Courage, Passion, Honesty, and Selflessness.

-

We seek excellence. A great workplace created by *Stunning Colleagues*—people you can respect and learn from. We're like a *pro sports team*, not a kid's recreational team. We want stars at every position. Adequate performance gets a generous severance package.

-

Each Netflix manager uses the *Keeper's Test* to evaluate employees: Which of my people, if they told me they were leaving for a similar job at a peer company, would I fight hard to keep at Netflix? *The other people should get a generous severance now, so that we can open a slot to try to find a star for that role.* The more talent we have, the more we can accomplish. To that end, we assist each other all the time; we help each other to be great.

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We don't measure people by how many hours they work or how much they are in the office. We care about accomplishing great work. Sustained B-level performance, despite an "A for effort," generates a generous severance package, with respect. Sustained A-level performance, despite minimal effort, is rewarded with more responsibility and great pay.

-

We insist on high performance. In procedural work, the best are 2x better than average. But in creative/inventive work, the best are 10x better than average. There is a huge premium on creating effective teams of the best performers.

-

We are looking for responsible people who thrive on freedom, and who are worthy of freedom. Responsible people are self-motivating, self-aware, self-disciplined, self-improving, act like leaders, don't wait to be told what to do—and they pick up the trash on the floor. Great managers figure out how to get great outcomes from their people by setting the appropriate context, rather than trying to impose control. High performance people will do better work when they understand the context, the overall goals and strategies. When one of our talented people does something dumb, a great manager doesn't blame the employee; instead, the manager asks where s/he failed in setting the context.

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The Netflix model seeks to *increase* employee freedom as we grow, rather than to limit it. We do that by focusing on increasing *talent density* as we grow. Many companies impose process controls as they grow, in order to manage increasing complexity. That's fine: such companies may be market leaders, defined by their optimized processes that drive efficiency and permit few mistakes. But they are also defined by: minimal thinking required of their employees, a lack of curious innovators/mavericks, and a lack of flexibility. When the market shifts, those companies have trouble adapting to

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new conditions. But we seek to avoid that by-product of successful growth by adding more and more high performers, who have the self-discipline to thrive in an informal work environment. We increase talent density by: (1) paying top of market compensation, (2) giving our people an opportunity to make a big impact, and (3) continuing to demand high performance.

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We seek to have only outstanding employees. One outstanding employee gets more done and costs less than two “adequate” employees. We have three questions, or tests, to determine a person’s compensation: (1) What salary could this person get elsewhere? (2) How much would we have to pay for a replacement? (3) How much would we pay to keep this person if they received an offer from elsewhere? Our goal is to keep each employee at the top of the market for that person. We will pay an outstanding employee more than anybody else likely would; we will pay them as much as a replacement would cost; and we will pay them today as much as we would if they had a higher offer from elsewhere. These questions are asked of each employee every year.

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We do not have centrally administered “raise pools” or salary range percentiles. We don’t focus on internal parity or giving everybody the same flat raise; instead, we focus on what the employee is worth in the marketplace. Regardless of how well Netflix is doing, we will always pay our people top of market compensation. Think of a sports team: even if the team has a losing record, it is still paying its players the market rate.

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We do not rank our employees into “top 30%” or “bottom 10%” categories. We do not want our employees to feel competitive with each other. We want all our employees to be in the top 10% relative to the pool of global candidates. This approach fosters cooperation, which is what we want.

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Formalized employee development is rarely effective, and we don't do it. We don't have rotations, mentorships, etc. Instead, we develop people by surrounding them with stunning colleagues, and by giving them big challenges to work on. If we would promote somebody to prevent them from leaving, we will promote that person today.

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Bad processes are in place to prevent mistakes. Our model focuses on *rapid recovery* rather than error prevention. For example, we don't have a vacation policy. Further, our policy for expense reports, travel, acceptance of gifts, and entertainment consists of *five words*
: Act in Netflix' best interest. That's it.

Netflix is working hard to create its own organizational culture, and it says it understands why the culture it has created fosters accomplishments of its strategic vision and goals. Can you say the same about your organization and your culture?