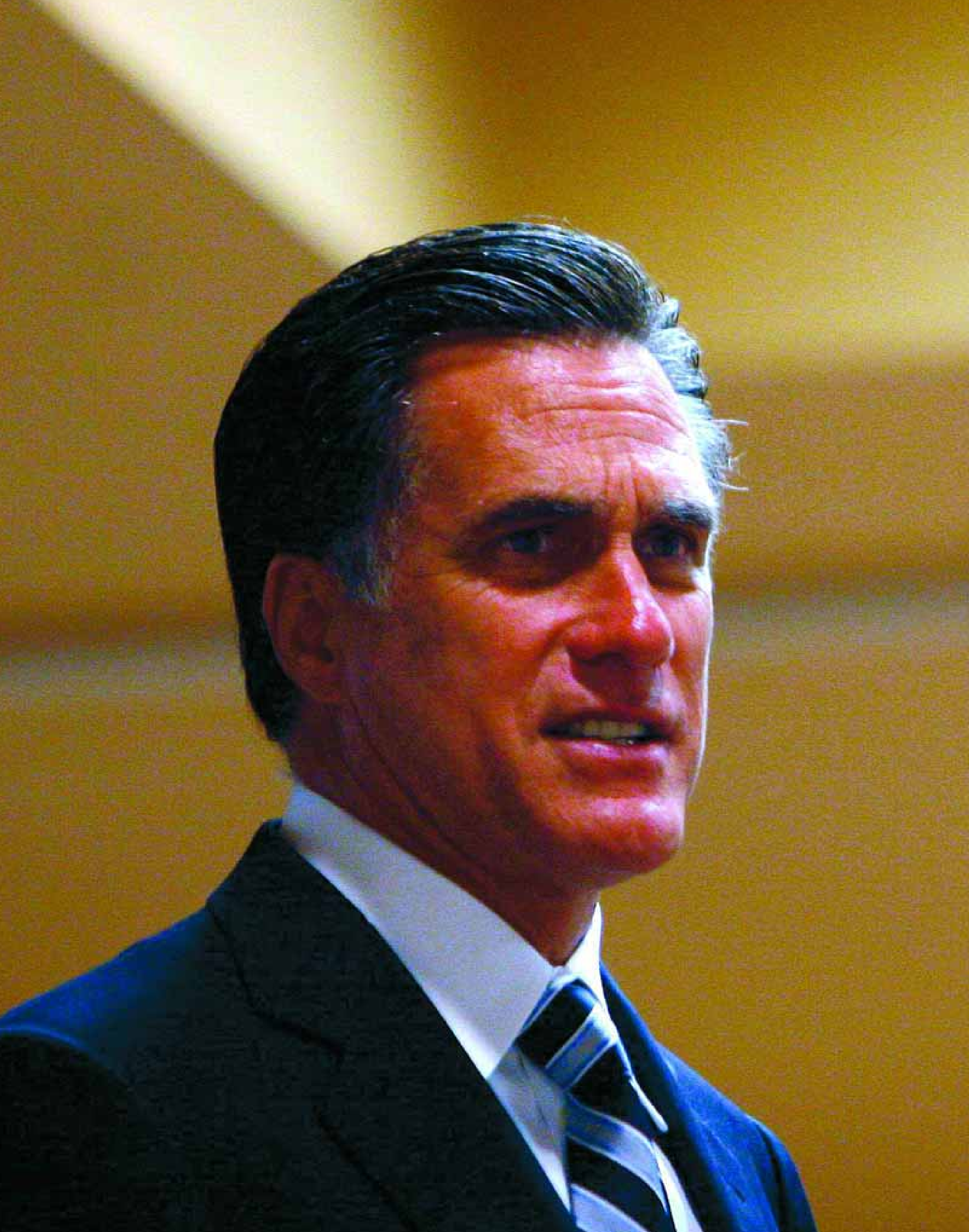


The house that Mitt built

Mitt Romney, the talented and charismatic former head of Bain Capital, is running for president of the United States. Those who worked with him during his private-sector years in the 1980s and 1990s describe a consulting superstar who succeeded in private equity while presiding, pater familias*-like, over a team of notably aggressive and ambitious investment professionals.* David Snow *examines Romney's legacy at Bain Capital and the leadership characteristics of a man who may be the next American president.*

In 1990, when a Goldman Sachs investment banker told Mitt Romney to "shut up", the preternaturally calm co-founder of Bain Capital momentarily lost his cool.

Romney was at the time on a leave of absence from his private equity firm to rescue his former employer, consulting firm Bain & Co., which like many over-leveraged businesses then was teetering on the brink of bankruptcy. The turnaround gig was tough, but perfectly suited to Romney's virtuosity for analysis, mess-sorting and interpersonal refereeing.

Here was a top consulting business, known as a breeding ground for good ideas, now caught in a financial death spiral of its own making. Romney was attempting to play the many impatient constituents against each other until the spiraling was brought under control. But the Goldman banker in question was rather more explicit in expressing his impatience, telling Romney in a meeting that the only hope for Bain & Co.'s resuscitation was for it to first enter into bankruptcy protection. Romney, an ace communicator, began his rebuttal, but was abrasively cut short. "I thought that he would probably kill the guy," says a person who witnessed the confrontation. "That was probably the maddest I've ever seen Mitt."

While Romney was used to – even an instigator of – vigorous, needling debate, being told to shut up deeply offended him, not because it was directed at him, but because it was impolite. Romney, the devout Mormon who never swore, drank or missed Monday-night family gatherings, demanded aggressive analysis, aggressive dealmaking and aggressive peer review from his team. But he took exception when people responded to this distinctly Bain brand of competitive energy with something other than a veneer of good manners.

Mitt Romney and Bill Bain in 1990. Romney, a star consultant at Bain & Co., was chosen to spearhead the firm's foray into private equity.

Romney's nice-guy persona was backed up by the confidence of someone who succeeded at everything he did. The undisputed alpha dog at Bain Capital had no need to bark. Even years after his departure, it is notable that at a firm bursting with self-confidence and ambition, Romney is still viewed with something akin to awe. Says Josh Bekenstein, a Bain Capital managing director and one of the firm's first professionals: "The thing that one cannot overstate is how smart Mitt is. He's a very, very smart guy. We interact with a lot of smart people, but I never felt that I was in a room where there were people that were smarter than Mitt."

"Mitt was someone who was almost too good to be true," says Charles "Chip" Baird, the founder of Greenwich, Connecticut private equity firm North Castle Capital Partners and a consultant at Bain & Co. during Romney's years there. "He is so good at so many different things, and that's what drives some people bonkers."

The confidence that Romney inspired was such that his ownership of Bain Capital's management company was welcomed by the firm's other partners. Romney was widely seen as the "glue" to the firm he built. When, in 2001, he turned the firm over to its employees, there was some worry among limited partners that the exit of *pater familias* would bring disorder to the house of Bain.

MASSACHUSETTS AVENUE

Romney was wildly successful in private equity, but the private equity industry was not big enough for Romney's ambitions. After a stint overseeing the scandal-marred Salt Lake City Winter Olympics, Romney was elected governor of Massachusetts, becoming, against considerable odds, a Republican overseeing a traditional Democratic stronghold. He is now running for president of the United States of America. Romney must first defeat John McCain, Rudolph Giuliani and possibly Fred Thompson in rolling state Republican primary elections that begin in January. The winner of the Republican primaries will face the Democratic nominee in the 2008 US presidential elections.

Romney is viewed as more socially conservative than McCain and Giuliani – a potential advantage for securing the Republican nomination, until one factors in his religion, which is a minus for many of the same socially conservative voters. Romney also has a potential liability in the form of his career in private equity, due not to any particular decisions he made at Bain Capital, but because of the generally low opinion many voters have of buyout firms. Romney lost a 1994 bid for Ted Kennedy's Senate seat in part because of negative publicity he received from union bosses, who claimed that Bain Capital had fired workers at a tyre-making portfolio company.

Not surprisingly, there is no mention of the terms "buyout" or even "private equity" on the official Mitt Romney campaign web site. Bain Capital, one reads near the end of Romney's bio, is "one of the nation's most successful venture capital and investment companies". Romney's decision to downplay his years at Bain Capital in favour of more recent accomplishments is politically astute, but it does obscure the fact that his success at Bain Capital was the platform that allowed him to enter politics. It was the first time that Romney was able to build and control his own organisation. It created for Romney a degree of public recognition, not to mention vast personal wealth (Romney is entitled to receive distributions from Bain Capital entities until February 2009). Romney's years at Bain Capital also allowed him to build out a network of wealthy and connected admirers, especially on Wall Street, who are now among the strongest supporters of his pro-business agenda.

Of course, public office was not an unexpected goal for Romney – politics was after all the family business. He is the son of George Romney, the former governor of Michigan and himself a former Republican White House hopeful (the senior Romney lost to Richard Nixon in the 1968 Republican primaries after voicing skepticism about the war in Vietnam).

George Romney first built his private-sector career during the 1940s and 1950s in the automobile industry. Mitt Romney entered the business world through the hot industry of the late 1970s – business consulting. After graduating with a joint degree from

Harvard's business and law schools, Romney was hired at Boston Consulting Group. But just three years later, in 1978, he joined a firm co-founded by Bill Bain and several other Boston Consulting defectors.

At the time, Bain & Co was encountering explosive growth and attracting the best and brightest from MBA programmes, remembers North Castle's Baird.

Romney was quickly promoted to the equivalent of a partner at Bain & Co. and became the youngest of seven senior professionals at the firm. "Certainly, he was a star," says Baird. "He was someone that clients liked and was someone that people liked to work for."

Romney had all the ingredients necessary for achievement in the business of selling business advice. "A huge part of the consulting business is trust," adds Baird. "Mitt is someone who is and comes across as an ingenuous, personable, straight shooter. Second, consultants are paid to solve business problems, and Mitt is enormously capable as an analyst, as a manager of an analytical process, as a synthesizer of options and solutions, and then as a communicator of what can be often quite obtuse, arcane types of analyses, put in a language that a general manager in a plastics company can understand."

In addition to consulting across a range of industries, including hospitals, textiles and publishing, Romney took up the role of human capital acquirer for Bain & Co. "We were hiring huge numbers of people," says Baird. "From 1978 to 1989 we went from 40 to 1,400 people, and for a big chunk of that time, Mitt was responsible for hiring."

Romney became an assiduous evaluator and manager of people, and the role allowed him to hone a talent for building an organisation that achieved, as distinct from building a personal support system. He grew into "someone who was not wildly involved in the details," says Baird. "He would help the manager in the process outline, but not get involved in the day to day analytical exercise, necessarily."

"Mitt jumped off the merry-go-round to do something which I'd say at that point was a question."

Not that Romney was incapable of marshalling the details when called upon. Baird remembers a particular consulting assignment that Bain & Co was bidding on, where it became apparent that the firm was on track to lose. Romney personally stepped in at the last minute. "Mitt stayed up all night and wrote the whole proposal," says Baird. "He literally wrote every word. [It became] the biggest single piece of work that Bain had ever won in a competitive process."

PRINCIPAL TRANSITION

By 1984, with the consulting business still highly lucrative, the senior partners of Bain & Co. took notice of a small but growing cluster of groups that would eventually come to be known as private equity firms. According to Bekenstein, a client posed a question: "You guys do such a great job giving strategic advice to clients, why don't you try to invest in companies and participate in the equity appreciation of those companies?"

Romney, along with another top producer within the consulting firm named Coleman Andrews, stepped forward to lead Bain & Co.'s expedition into private investments. The two were selected for the job because of "a combination of them being incredibly talented, and in the course of their careers they had expressed interest in something more entrepreneurial than being consultants," says Geoffrey Rehnert, a co-chief executive officer of Boston-based private equity firm Audax Group, and a co-founder of Bain Capital.

Romney and Andrews suggested, and the rest of the partners agreed, that Bain Capital would seek to apply Bain & Co-style strategic consulting advice to the companies in which it would invest.

The firm would "try a different strategy than most buyout firms were pursuing at the time," says Bekenstein. "We wanted to look for buyouts that might be complex and have operational opportunities, and for venture capital deals that weren't just about technology."

In retrospect, Romney's move into the private equity business seems like a no-brainer, given the eventual success of Bain Capital. But at the time, Bain & Co., with roughly 600 consultants worldwide, was "about as successful an organization as you can imagine," notes Baird. "It was growing at crazy rates, everybody was getting promoted and getting paid more. Mitt jumped off the merry-go-round to do something which I'd say at that point was a question."

To round out the initial Bain Capital team, Romney hired Bekenstein, while Andrews, who was then based in California, hired Rehnert, who had just joined the consulting firm out of Stanford Law School. "I was fortunate," says Rehnert.

The first Bain Capital fund, called simply Bain Capital Fund, was a friends and family affair. At a Bain & Co. partners meeting in 1984, a piece of paper was passed around the table upon which the partners wrote the amounts of their respective commitments. This added up to $12 million. Romney and Andrews didn't think it was enough, and so the two set out to meet with people in the Bain network for additional commitments. By the end of the year, Bain Capital held a final close on $37 million and a new private equity franchise was born.

The deal between Bain Capital and the partners of Bain & Co. gave the consulting firm fifty percent of the carried interest as well as an interest in the general partnership of the firm. For technical reasons, Romney's and Andrews' salaries were initially paid by Bain & Co.

Bain Capital declined to give details on its evolving ownership structure.

Coleman Andrews left Bain Capital in 1986 to pursue his interests in the airline industry. He was replaced by Robert White, another Bain & Co. consultant.

White, Bekenstein, Rehnert and Romney became the four general partners of Bain Capital, with Romney, aged 38, a good decade older than his three partners. Although all partners were involved in all aspects of the firm, a pattern emerged whereby "Mitt was clearly the adult. He was the guy who flew out to meet with the CEO to negotiate the transaction" while the others focused more on financial models and deal terms, says Rehnert.

"Mitt's got a commanding presence when he comes into a room," adds Rehnert. "People notice him. He's charismatic and energetic."

The young firm had two early, audacious successes. And while Romney will likely not use the phrase "leveraged buyouts" during his presidential campaign, Bain Capital's first two homeruns were highly leveraged, classic mid-1980s LBOs. The first was Calumet Coach Company, a provider of mobile medical-imaging units. The deal, sourced by Rehnert in 1986, involved an equity cheque of $1 million and $10 million in debt. Twenty-seven months later Bain Capital exited the deal with a 35-times multiple on its investment. It was the firm's first leveraged buyout.

Next came Accuride, a division of tyre giant Firestone that was spun-out by Bain Capital near the end of 1986. The deal was referred by Bain & Co., a pleasing validation of hoped-for synergies between the two firms. Bain Capital invested $2.6 million in equity and structured the deal with 40-to-1 leverage. Fifteen months later the company was sold and Bain Capital realised 24 times its investment. Calumet Coach and Accuride alone would return three times the value of the first Bain Capital fund.

"The culture at Bain has never, ever been, 'Let's just do this the easy way.'"

All involved were pleased with the results, and the next Bain Capital fund received commitments from three insurance companies and the Bessemer Trust Company, in addition to enriched friends and family.

BATTLESHIP BAIN

The stage was set for Bain Capital to grow beyond its pass-the-hat origins, and at this point Romney's most valuable skill sets kicked in. Rehnert argues that the press coverage focused on Romney's dealmaking during those years misses the essence of his success with Bain Capital, which was as a builder of an organisation.

Remembers Bekenstein: "He was a huge believer in finding the best people. That was always the most important thing."

A person who used to work closely with Bain Capital says the firm developed a reputation for hiring highly ambitious, intelligent, even "cocky", professionals, at least in the eyes of the limited partners and investment bankers who interfaced with them. The term "Battleship Bain" came to be used by some investment bankers, the person says (several Bain Capital professionals say they have never heard of this term). The person summarises the reputation of the firm's deal professionals under Mitt Romney as "not the Care Bears".

Bekenstein says Bain Capital's culture remains one of "ambitious people" in a very competitive market, but he adds that he is confident that Bain professionals are also perceived in the market to be "respectful". "There's no yelling and screaming at the firm," he says.

Romney, perhaps taking a cue from his legal training, encouraged a decision-making culture whereby the smart, aggressive Bain professionals would gather and intensely debate investment and strategic options. Romney often played the Socratic referee. His goal, says Bekenstein, was to arrive at consensus, but not without first going through a rigorous discussion.

Mike Goss, the current Bain Capital chief financial officer who joined the firm in its earliest years, says that all partners at the firm were expected to ask tough questions of each other, but no one was a more persistent questioner than Romney. Says Goss: "If you suddenly said that you weren't interested in doing the deal any more, Mitt would switch sides and ask you to explain why."

Adds Bekenstein: "If Mitt and other team members asked a bunch of tough questions, and the deal team said, okay, maybe we should pass on this deal, Mitt would be the first guy to say, 'Well wait a second, are you sure you want to kill the deal? Maybe we should evaluate it some more.'"

"The culture at Bain has never, ever been, 'Let's just do this the easy way,'" says Goss.

Still, says Rehnert, "Mitt was not a deal junkie. In the 1980s there were a lot of guys who negotiated because they loved the sport of negotiation. Over time there were plenty of deal junkies at Bain Capital. Mitt became a manager of deal junkies. He was smart enough to hire and train and develop them. It was during the course of the growth of Bain Capital that he really learned how to run an organisation."

Those on the other side of the table from Bain Capital pros during a transaction learned to expect the attack of the deal junkies. Romney encouraged a very aggressive approach to negotiations. "It's going over every term," says a person familiar with Bain's negotiating style. "If there are 20 cookies on the table, I'm going to explain why I deserve 16 and you deserve four. And if you only give me 15 cookies, I want the biggest ones."

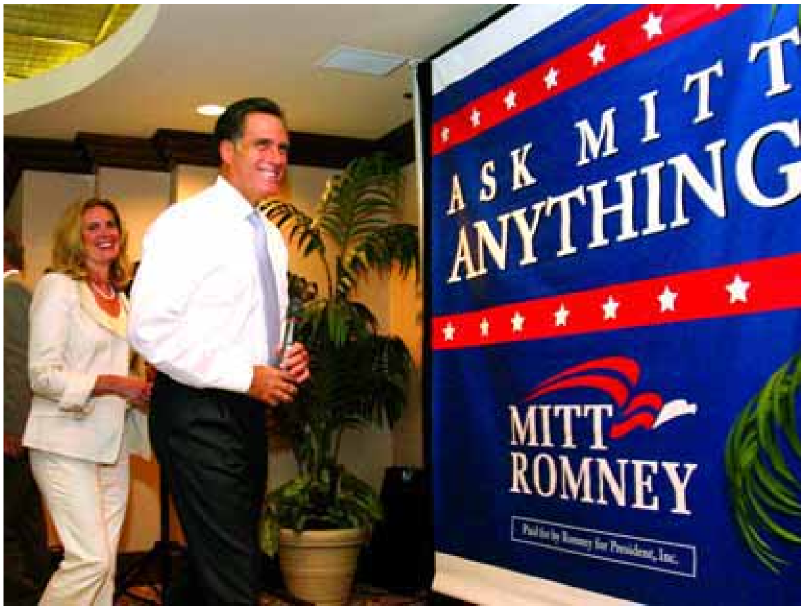
Under Romney, Bain Capital took the unorthodox step of moving from a 20 percent to a 30 percent carry. The firm remains one of the few large private equity firms to charge higher than a 20 percent carry. The change came in 1998 with Bain's sixth fund, just before Romney left to lead the Salt Lake Olympics. A source says the impetus to raise the carry came from Romney and Bekenstein, although Bekenstein says it was a collaborative decision among the firm's partners. He says Bain Capital had a very people-intensive style of investing, and the extra carry was conceived of mostly as a way to help pay this larger team.

A limited partner source says Bain Capital raised its carry because, frankly, it could – the firm's track record by 1998 was phenomenal, with an average return on each Bain deal of roughly 100 percent.

With returns like that, Rehnert says of the move to 30 percent carry, "It would almost be stupid not to charge premium carry."

While Bain Capital worked relentlessly to get the best terms for the firm, within the firm several current and former employees describe a general sense that compensation was remarkably fair under Romney. "Mitt was very generous with economics," says someone who worked for Romney. "People got paid what they deserved."

Romney created a system around



Mitt and wife Ann on the campaign trail

compensation at the firm, which involved extensive peer review, although Romney ultimately "controlled the money bag", as a Bain insider puts it. Several Bain insiders note that Romney structured a compensation methodology that most agreed was transparent. Goss says he remembers being hired by Romney, and asking about what it would take to become a partner at the firm. He was impressed when Romney, without promising anything, replied: "All I can tell you is that we will give you a piece of the pie if we believe that the pie will get bigger as a result of your having a piece."

Anyone who underperformed at Bain likely would not get a lecture directly from Romney. "He was good at creating an organisation where colleagues delivered the pressure and the bad news," says Rehnert. "Mitt would set the stage for the information to be received."

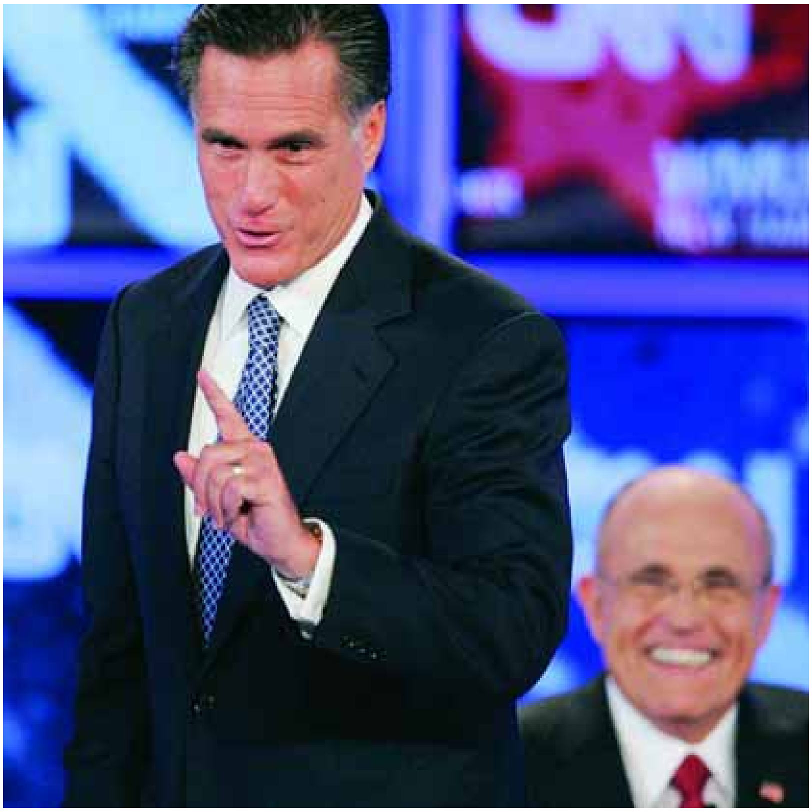
While Bain & Co. owned a stake in the early Bain Capital funds, the creation of Bain Capital Inc. in 1992 saw Romney become the 100 percent owner of the firm's management company, which technically gave him control of decision making at the firm. In practice, however, Romney broadly shared economics and kept in place a governance structure characterised by consensus-building among the many professionals. The other Bain Capital professionals saw Mitt's ownership not only as acceptable, but as a much simpler alternative to the many other potential structures, given the trust they placed in Romney. "People were willing to concede that," says Rehnert. "He had established enough credibility, enough trust, that it was better to have him be the sole decision maker rather than have a bunch of young guys beating each other up" in deciding on a shared ownership structure.

Ironically, given his future in politics, Romney enforced a no-press policy throughout his firm, a policy which persists in a somewhat relaxed form to this day. The radio-silence helped build up an elite aura around Bain Capital, but by the time Romney left, there existed an antagonistic relationship between the firm and some members of the media. In 2000, this relationship was tidily summed up when, on the occasion of a very rare interview with a trade reporter, a Bain Capital senior partner began by saying: "You guys give us abysmal coverage."

Life and work at Bain Capital under Romney was not all grind. The head of the firm occasionally unleashed a wicked sense of humour against his colleagues. And though he never drank, Romney would join in any celebrations with the firm. People at Bain Capital also observed that Romney would religiously head home early each Monday for an evening with his family. "He was very committed to that. He'd just get up from his desk and go," says someone who worked with him at the time. "But he'd work his ass off the rest of the time."

ROMNEY TO THE RESCUE

As Bain Capital grew, it became apparent that Romney was restless for different challenges. In 1990, Romney agreed to return temporarily to Bain & Co. as CEO to help the damaged consulting firm through a painful restructuring. Rehnert says he considers this period to have highlighted Romney at his best. "In the end, everyone was better off if Bain & Co. survived," remembers Rehnert. "But if it was going to go bankrupt, any one of these parties would have been better off being the ones who pushed it into bankruptcy, because they would have gotten more out of the bankruptcy if they were the ones who asserted their claim first. So he had to have everyone sit still and convince them that they'd be better off sitting still. In the end, he was able to inspire enough trust and confidence in all of these warring factions that he was going to get the job done. Even though a lot of smart people thought it was hopeless, he wound up making it work."



Romney and political rival, former New York City mayor Rudolph Giuliani, share a stage during a recent candidates debate.

Not long after returning to Bain Capital following the restructuring of Bain & Co., Romney took a much larger lateral step away from the firm. In 1994, he campaigned for the Senate seat of Ted Kennedy. "He gave a little consideration as to what would happen if he got elected," says Rehnert. "There were some contingency plans made for governance and ownership in the event that he got elected."

Bekenstein credits the collaborative decision-making process encouraged by Romney for preparing the firm for a post-Mitt world. "When he ran for the Senate in 1994, he was gone for about nine months, and we continued to run the firm and make decisions as we had when Mitt was around," says Bekenstein.

Romney was not successful at winning Ted Kennedy's seat. In the wake of this defeat, however, he set his sights on bigger prizes, and sought to give himself greater visibility on a national stage. In 1999, with the 2002 Salt Lake Olympics approaching, Mitt made himself available to clean up yet another mess, this one related to a bribery scandal embroiling the Olympic committee. In 2001, to dispel any doubts as to his ongoing connection with Bain Capital, Romney said at a press conference that he had agreed to transfer his ownership of Bain Capital to his partners, and to do so "without financial consideration".

While indicating he would continue to be involved as a limited partner with Bain Capital, Romney said at the press conference: "I didn't want [Bain Capital managing directors] to wonder whether I [was] going to be coming back to take over again … I didn't want them to wonder whether … I was going to show up at the front door and say, 'O.K. everybody, move over one office, I'm here again.'"

Last month, the Romney campaign filed a financial disclosure form that described Romney's separation from Bain Capital as such: "As part of his retirement from Bain Capital, he entered into a non-compete, non-hire agreement running through February 11, 2009 which provides him with a passive, declining profit share that is fixed by contract in certain Bain Capital entities, and the right to make passive investments in certain Bain Capital investments."

A source says this arrangement refers to Romney's share of the carried interest in Bain Capital entities. (It is unclear what is identified in a footnote to the Romney financial disclosure, which says that the "Ann D. Romney Blind Trust" has a right to receive profits until February 2009 from an entity called "Bain Capital").

The campaign announcement took pains to note that the former governor has since 2003 not had "any control over the assets acquired or disposed of".

Certainly, Romney has continued to benefit from his passive affiliation with Bain Capital. But he left money on the table. Allowing that, until fairly recently, the management company of a private equity firm was not deemed to be a thing of great value, had Romney retained ownership of Bain Capital until today, this asset could have been worth $10 billion or more, using the current (albeit fluctuating) valuations of Fortress and Blackstone as proxies. The Romney campaign has disclosed that the candidate's net worth is somewhere between $190 million and $250 million.

Romney's decision to transfer the firm's management company to its employees stands in contrast to the many other examples of founders now seeking to monetise their respective franchises. "Mitt could have kept that," says a former colleague. "Maybe he could have put it in a trust, but he chose the. . . approach to pass it on to the generation of people who are producing, and not the entrepreneurial 'I founded it and therefore I deserve $7 billion'" approach.

"He chose to go away with hundreds of millions of dollars," adds the former colleague. "Could he have had billions? Sure."

Although all at Bain Capital expected less involvement from Romney because of his leadership in the Olympics, his departure from the firm was not expected by all within the broader Bain network, according to a source in close contact with the firm at the time. While there was acknowledgement among LPs that the firm's partners would continue to build the firm, there was also some anxiety expressed that the "glue" of the firm, Romney, was no longer in place.

A person who attended Bain Capital's May 2000 annual general meeting describes a somewhat emotional gathering of LPs, Bain professionals and the next generation of leadership, at which senior partners spoke with pride about their 15 years together, and their determination to make the firm thrive going forward.

The firm has certainly thrived post-Mitt, growing to $50 billion under management across multiple asset classes. In private equity, the firm has among the largest platforms in the world. Bain is reportedly raising as much as $15 billion for its next fund. From a governance perspective, Romneyesque zeal for consensus-driven decision-making continues. The 51 managing directors delegate authority to numerous committees. No individual partner has stepped forward to replace Romney as the leader of Bain Capital.

Romney's final departure from the firm went smoothly. But his charismatic presence was evidently a harder thing to unwind. A person who frequently visited the Bain offices in Boston during the 2000 period noted that Romney's office remained fully furnished and untouched for months following his move to Salt Lake City. On the walls hung large individual portraits of his family members. Romney was no longer boss, but the challenge of boxing up and clearing out the founders' belongings was perhaps more complex than might have been the case at a firm with a different history. ■

ROMNEY TIMELINE

1971 Graduates from Brigham Young University as valedictorian.

1975 Graduates from Harvard University with joint graduate degrees in law and business.

Joins Boston Consulting Group.

1978 Joins Bain & Co.

1984 Co-founds Bain Capital with $37 million in capital commitments from Bain & Co. partners and people in the Bain network.

1990 Returns temporarily to turn around Bain & Co. as the consulting giant teeters on the brink of bankruptcy.

1994 Runs against longtime Massachusetts senator Ted Kennedy, a Democrat, but loses with 41 percent of the vote. Romney returns to Bain Capital.

1999 Leaves Bain Capital to manage the 2002 Salt Lake City Olympic Winter Games.

2001 Announces that he has transferred his ownership in the firm for no financial consideration.

2003 Sworn in as governor of Massachusetts with 50 percent of the vote, defeating Shannon O'Brien.

2007 Gubernatorial term ends and Romney files to run for the Republican nomination for president. Republican primary elections begin next January. The winner will run against the Democratic nominee for the White House.