A Culture of Greed at Chesapeake Energy

Mr. Jimmy Goodrich
Bachelor of Applied Science, Bismarck State College (Energy Management)
Master's of Science, University of Colorado - Denver (Global Energy Management)

Mr. Nwandu Uche Ejiasa
B.S. International Business, University of Colorado at Denver
Master's of Science, University of Colorado, Denver (Global Energy Management)

Mr. Trevor Penner
B.S. Geology, Missouri State
Master's of Science, University of Colorado, Denver (Global Energy Management)

Mr. Joe S Suglia
B.S. Geography - Ohio University
Master's of Science, University of Colorado, Denver (Global Energy Management)

Mr. David Zamarripa
Bachelor of Arts, University of Oklahoma (Sociology)
Master's of Science, University of Colorado, Denver (Global Energy Management)

Dr. Andrew Bertsch
(Corresponding Author)
DBA
Minot State University

Abstract
Together, the founders of Chesapeake Energy Corporation – CEO Aubrey McClendon and President Tom Ward – built the company through hard work and vision. Their initial style of 'growth through the drill bit' identified an industry niche in unconventional methods for extracting gas. In our case study, we reflect on McClendon's style of leadership and his decisions even as Chesapeake's Board of Directors was trying to reign in his drive to grow via leveraging and acquisition. Unfortunately, McClendon took the company into a tailspin with enormous debt before the Board could act and remove him as CEO. At the time of this writing, Chesapeake still has their head above water as their new CEO attempts to change the financial status of the company. The future does not look bright as employees and shareholders are fleeing. The financial woes brought on by McClendon via an unchecked and unsustainable leveraging position is likely too much to bear.

INTRODUCTION

Corporate greed has become all too prevalent in today's business world. In response to detrimental actions caused by corporate greed, the Sarbanes-Oxley Act of 2002 was enacted by the U.S. Congress to protect investors from the possibility of fraudulent accounting activities (Donaldson, 2003). One specific element of Sarbanes-Oxley was to ensure firms adopted ethical codes of conduct. In many cases such as for publically traded companies, firms must be transparent in their disclosure of their codes of ethics (Martin & Cullen, 2006). In our review of Chesapeake, we cover the life and actions of Chesapeake Energy's former CEO Aubrey McClendon and President Tom L. Ward to explore whether their actions as leaders of Chesapeake were morally and ethically structured in building the company's success, or perhaps there were other motives (e.g., personal financial gain). Was senior management of Chesapeake just another corporate entity to fit the greed model of so many companies before them? Was Aubrey McClendon, the pioneering wildcatter, an ethical and moral leader of the company, or was his aggressive growth (through the drill bit model) all for self-fulfillment and egocentricity?

These are the questions that will guide our review of McClendon and Chesapeake. We shall explore the past of both McClendon and Ward in an attempt to connect how their decisions were detrimental to Chesapeake's future. We will explore how strategic decisions (or perhaps personal outcomes) played a role in McClendon's business decisions. Although the outcome for Chesapeake was the same as other doomed companies (for example, Prenatt, Ondracek, Saeed, & Bertsch (2015)), we suggest that Chesapeake's poor decisions were due to greed and ethics violations rather than missed opportunities. Furthermore, we will delve into Chesapeake's fall from grace and review ethical or moral issues that exacerbated the issues. Finally, we will suggest how to attract new investors and current leadership's role in guiding Chesapeake's future. Our methodology is similar to previous historical accounts of other leaders and leadership decisions (see, for example, Ferrell, Ondracek, Saeed, & Bertsch (2016); Hardy, Ondracek, & Bertsch (2015))

2. PROFILE OF FOUNDING MEMBERS

Over the past twenty years, the increasing incidences of corporate greed have greatly impacted the lives and financial positions of millions of people. With this in mind, we will first look back on the lives' of Chesapeake's founders: CEO Aubrey McClendon and President Tom Ward. We explore their past to lay the foundation of how they contributed to Chesapeake's performance and ultimate demise. Their backgrounds and decisions may have adversely affected the ethical and moral decisions which directly contributed to Chesapeake Energy's initial accomplishments and longer term failure.

2.1 Aubrey Mcclendon

Aubrey McClendon was born July 14, 1959 in Oklahoma City, Oklahoma to Joe and Carole McClendon (Aubrey McClendon (a), 2016). McClendon is the great-nephew of Robert S. Kerr, former governor of Oklahoma and U.S. senator. McClendon's family has historical ties to the energy industry as well as lucrative connections to wealth. Prior to Kerr (McClendon's great-uncle) becoming involved in politics, Kerr and his brother-in-law – James Anderson – formed Anderson & Kerr Drilling Company (Gerkin, 2012). After Anderson retired, Dean McGee, a former chief geologist for Phillips Petroleum, joined the firm and they changed its name to Kerr-McGee Oil Industries (Vandewater, 1999). Kerr-McGee has its own rich history of financial wealth, corruption, and multiple spinoffs that moves beyond the scope of this study. McClendon's father also worked for Kerr-McGee for thirty-five years on the refining side of the industry (Robinson, 2002). McClendon had been raised in an energy industry family and was surrounded by energy leaders his entire life.

McClendon was raised near Oklahoma City, graduated co-valedictorian of his high school class, and later went on to graduate from Duke University with a B.A. in History and a Minor in Accounting (Aubrey McClendon (a), 2016). He met his wife Katie at Duke and married her in St. Joseph, Michigan in 1981. The couple had three children and lived in Oklahoma City. Katie McClendon (officially Kathleen Upton Byrns McClendon) is the granddaughter of Frederic S. Upton, a co-founder of Whirlpool

Corporation and cousin of U.S. Representative Fred Upton of Michigan (Aubrey McClendon (b), 2016). Aubrey McClendon's first job out of college was as an accountant but he later started working as a Landman at Jaytex Oil and Gas, which was founded by his uncle Aubrey M. Kerr, Jr. (Aubrey McClendon (a), 2016). Working as a Landman is how McClendon first met Tom Ward.

2.2 Tom L. Ward

Tom Ward was born and raised in the remote western Oklahoman town of Seiling. He played high school football and never really considered college until his future wife had informed him that she was attending the University of Oklahoma, so he followed her (Sasser, 2012). During his senior year in high school, Ward worked with his uncle in the oil fields making it an easy decision for him to pursue an energy-related degree while in college (Sasser, 2012). Ward graduated from the University of Oklahoma with a Bachelor of Business Administration in Petroleum Land Management in 1981 and started working as a private Landman in the Wenoka area (western Oklahoma) securing mineral leases (Oklahoma Hall of Fame, 2012). Ward first met McClendon in 1983 having similar careers in the oil and gas sector. In Ward's interview with Oklahoma Magazine, he reminisced about what led to their partnership, "(w)e were the only two, post-Penn Square Bank, who were aggressively buying leases and wells, so in short order we were partnering…. From 1983 to 1989 we dug a ton of wells" (Sasser, 2012, p. 1). As Ward pointed out in his interview, McClendon and he were aggressive from the start. Ward and McClendon's unchecked aggressive approach carried both men throughout their business ventures.

In 1989, Ward co-founded Chesapeake Energy with McClendon, and the years that followed are legendary in energy folklore. Chesapeake grew to be an 'energy giant,' propelling both men to the forefront of the industry and also propelling Ward to a position that seemed quite removed from his hometown (Sasser, 2012).

3. HISTORY OF CHESAPEAKE ENERGY

McClendon and Ward formally incorporated Chesapeake Energy in 1989. The name of the company came from McClendon's love for the Chesapeake Bay; however, the company was physically located in Oklahoma City, the heart of oil country (Li & Molina, 2014). Prior to the formal incorporation, McClendon and Ward worked as Landmen chasing mineral leases in the oil-price-bust of the 1980s (Robinson, 2002). As McClendon stated in an interview with Robinson (2002):

"About six months after I started out, I ran into a fellow named Tom Ward, who was doing more or less the same thing as I was. Both of us had no money but a lot of aggression, so one of us would invariably beat the other to a lease - and we would beat each other's brains out (financially) competing for it." (Page 1)

One day they came to the conclusion that instead of working against each other they should join forces and form a natural Gas Exploration and Production Company to collaborate ideas and integrate emerging technologies (Robinson, 2002). In 1989, McClendon and Ward began with just ten employees and a $50,000 initial investment Chesapeake specialized in the development of natural gas resources by committing new technology in horizontal drilling to find unconventional reserves (Li & Molina, 2014). With this new technique and drive for growth through the drill bit, this young company built significant positions in the Golden Trend and Sholem Alechem fields of south central Oklahoma and in the Giddings field along the Gulf Coast (Blauvelt, Jason; Lambert, James; Upadrashta, Prabhava, 2012).

As natural gas prices started to rise significantly in the early 2000s, Chesapeake began to focus more of its work on the unconventional reservoirs such as shale, carbonates, and tight sandstones (Li & Molina, 2014). As the company started to develop in these unconventional areas they began to define a niche in the industry. Deposits that had once been considered too costly to recover or unreachable altogether were now recoverable due to Chesapeake's contined push for growth through the drill and implementing advanced technology. McClendon and Ward forged on, leading Chesapeake through significant growth and hefty revenue, which in turn, led to boosting the wealth of McClendon and Ward (Robinson, 2002). However, Chesapeake also chose to grow using debt leveraging and this philosophy led to significant increased debt load. In 2006, Ward resigned from Chesapeake to pursue other interests, which included advocating for neglected children and various other business ventures (Adams, 2006).

Due to a confluence of technological innovation and market readiness, Chesapeake announced production in the Haynesville Shale in East Texas and northwestern Louisiana in 2008 (Li & Molina, 2014). Once again, this announcement solidified Chesapeake's role as an energy industry leader. Technological innovations allowed Chesapeake to discover new geologic formations that competitors failed to initially realize or simply believed were unrecoverable.

From 2009-2012, Chesapeake Energy continued their path of aggressive growth and spending. However, this all came to an end in 2013 when McClendon was forced into retirement (Driver & Grow, 2012). With a new CEO and direction, the company has attempted to make a complete one-hundred and eighty degree turnaround in hopes of refocusing their business strategy towards paying down debt and becoming financially disciplined (Sanati, 2012). The aggressive growth strategy that had been in full-force since 1989 was no longer sustainable (Sanati, 2012).

4. FOUNDING VISION – DID IT CHANGE OVER TIME?

Since Chesapeake's inception in 1989, the business strategy and vision had been focused on growth through the drill bit to build and develop the largest onshore natural gas resources. Additionally, Chesapeake's focus included high quality acquisitions, focusing on low cost, and increasing return on capital by hedging (Sanati, 2012). The initial business strategy propelled the company into greatly expanding its reserves and production through acquisition and development of large blocks of acreage (Robinson, 2002). Chesapeake Energy continued on this path of aggressive growth by utilizing its advanced technological expertise in the drilling of vertical and horizontal wells to further exploit areas of proven hydrocarbon production. Chesapeake teamed with major oil companies and well-capitalized independents to develop its existing inventory of more than 150 proved and probable drilling locations (Chesapeake Energy Corporation, 1993). The idea was to utilize their strength in geological and engineering processes to deliver higher financial results (Robinson, 2002). McClendon (and Ward up until his retirement in 2006) were on a profit driven path to boost financial success of the company through acquisition (e.g., leveraging) and implementing advanced technology (Sanati, 2012).

Adhering to a strong ethical doctrine ought not to compromise profit margins (Saeed & Ahmed, 2001). The business strategy continued to focus on growth as the company expanded its reach and increased its debt (Sanati, 2012). McClendon was committed to looking for ways to grow and build his personal and Chesapeake's portfolio of wealth by securing and commercializing new unconventional liquid-rich plays. Chesapeake was very proud of its innovative and aggressive implementation of business strategy and it showed with lavish spending and continued growth (Chesapeake Energy Corporation, 2013). This core business strategy all ended when the board forced the retirement of McClendon in 2013. In 2012, breaches of fiduciary duties and corporate waste were reported. In addition to other factors, these breaches led to McClendon's forced retirement. Chesapeake's Board of Directors quickly set the new business strategy for the company by focusing on financial discipline and efficient growth from captured resources in hopes to increase profitability (Chesapeake Energy Corporation, 2014). The days of lavish spending and exponential growth were coming to an end.

As Chesapeake moved forward, putting the McClendon era behind them and paying for the debt load which burdened the company, Chesapeake's new business strategy focused on maximizing liquidity, improving margins, and improving value in existing plays (Chesapeake Energy, 2015). This was a very different strategy than what the company was originally founded on.

5. CHESAPEAKE'S RISE TO PROMINENCE

A quote from Walt Disney's feature film *Remember the Titans* illustrates a key concept of leadership and the true nature of the relationship between a leader and those that he or she leads: "Attitudes reflect(s) leadership" (Howard, 2000). This simple three-word quote is illustrative of how the culture of an organization gravitates toward the behaviors and values of its leaders. From the inception phase to ascendance, and ascendance to downfall, the culture, norms, and behaviors of a company will often mirror the aspirations of leadership. We will explore in more detail the decisions that led up to the 'unsustainable tipping point' in Chesapeake's history previously outlined.

5.1 A Closer Look

"Swift as the wind. Quiet as the forest. Conquer like the fire. Steady as the mountain" (Sun Tzu, 500 B.C.). Chesapeake's rise to prominence is not unlike this quote by Sun Tzu in the Art of War. Their dominance was as swift as the wind and advanced rapidly like a spreading fire. Their rise was, in large part, due to an insatiable appetite to devour competitors via mergers and acquisitions. Let us further explore this period of significant yet unsustainable growth.

5.1.1 Phoenix Rising (Acquisitions And Growth)

In 1997, on one of Chesapeake Energy's most significant moves was the acquisitions of Kansas based Hugoton Energy for $275 million in stock and the assumption of $105 million in debt (The New York Times (NYT), 1997). According to the NYT article, both Boards of Directors' of Hugoton and Chesapeake unanimously approved the transaction (The New York Times (NYT), 1997). The following year (in 1998) Chesapeake acquired portions of Occidental Petroleum Corporation for $105 million (The New York Times, 1998). This 'growth through acquisition' (and leveraging) continued in 2000 with Gothic Energy for $28 million and the assumption of $316 million in debt (The New York Times, 2000). This only a partial list with Chesapeake either acquiring companies for money and large assumptions of debt, acquiring stock in competitors, or acquiring gas key (strategic gas reserves from landowners). Many of the companies that Chesapeake acquired were heavily leveraged and themselves in unsustainable debt positions. Although Chesapeake was able to acquire many companies at favorable market rates, many of those acquisitions included the assumption of significant debt. This pattern of rapid acquisitions laid the groundwork over that fateful decade (1999-2009) that dramatically increased the size of Chesapeake (in both market share and total leverage). McClendon was able to convince himself and the board of directors that the rapid growth promised a bright future.

5.1.2 Let The Good Times Roll

In July of 2003, Chesapeake energy released second quarter earnings and the results left both internal and external stakeholders cheering. The New York Times (2003) reported that net income for Chesapeake had more than tripled in 2003's second quarter; profits increased to $82.2 million, or 31 cents a share (after payment of preferred dividends) compared to $25 million, or 13 cents a share a year earlier. Revenue had more than doubled to $429.6 million. Gas output in the same quarter rose 55 percent, to 67.3 billion cubic feet. Gas and oil production increased to the equivalent of 258 billion to 262 billion cubic feet (The New York Times, 2003).

In 2005, the Oklahoman News (*NewsOK*) printed an article praising McClendon for his maverick ways and hard to argue results. McClendon earned a whopping $10.6 million dollars in salary, bonuses, and stock gains (McCoy, 2005). At 44, McClendon was the youngest CEO in Forbes Top 40 ranking of Most Effective Bosses (McCoy, 2005). Praises of McClendon's drive and vigor from other industry CEOs are peppered throughout various news outlets and highlights of his extreme lack of risk aversion were also mentioned (McCoy, 2005).

5.1.3 The Ruler Archetype

Golden (2016) explores 12 common archetypes based on the work of Carl Jung. Many of the dark sides of these archetypes are illustrated in McClendon's behaviors. We suggest that the Ruler is the one archetype that mirrors McClendon the most during this point in time. Golden explores Jung's definition of the Ruler archetype as an individual who does not believe power is everything, but it is the only thing. The core desire of the Ruler is complete control and an overarching goal is to be successful and prosperous at all costs (Golden, 2016). This appears to be congruent with McClendon's behaviors and apparent desire. Helman (2011) explores the two sides of McClendon and highlights a very specific instance when Helman first meets McClendon. Helman recounts this meeting by describing how

McClendon is pensive about which wine they should drink. Helman points out how McClendon is not shy about spending money and highlights his unabashed desire for the finer things in life (Helman, 2011).

In addition to Chesapeake's sizeable growth and favorable market share, McClendon was simultaneously lining his pockets (Sanati, 2012). Record dividends were being paid by Chesapeake; and the 12,000 employees and external stockholders of the company were being rewarded for putting their faith in McClendon (Sanati, 2012). We wonder whether anyone, in such moments of great prosperity, ever thought that perhaps they were flying too close to the sun?

5.1.4 Flying Too Close To The Sun?

The year 2009 proved to be pivotal for Chesapeake, and ultimately, McClendon. This was the year that the Board of Chesapeake Energy compensated McClendon with a $75 million bonus despite the decline of Chesapeake's stock (Morgenson, 2009). This specific example highlights the Board's continued support of McClendon and Chesapeake's prominence. McClendon was credited with orchestrating major acquisitions, out-of-this-world mergers, and triple digit profitable growth. This recognition is exactly what McClendon was about: larger, bigger than life transactions. At Chesapeake's apex, McClendon held $2 billion worth of stock; yet, as Chesapeake began to decline, McClendon sold 94% of his shares (Morgenson, 2009). Despite this being against his original contract of employment, McClendon was rewarded with a new deal and compensated with that $75 million bonus. McClendon had cemented his legacy as an individual who could get things done.

Staying true to form, Chesapeake announced plans for a $345 million initial public offering (IPO) in 2010 (DealBook, 2010). In the nine months ending September 30, 2010 Chesapeake Midstream lost $17.4 million, compared to a profit of $165.9 million in the first nine months of 2008 (DealBook, 2010). Chesapeake was hopeful the IPO would help to pay off debt and raise capital (DealBook, 2010). With past record gains that Chesapeake recorded, it seemed unthinkable that Chesapeake would be forced to raise capital to pay down debt (Ailworth, 2015). Chesapeake was beginning to see a shift as debt was starting to be a limiting and unsustainable factor in their business operations.

6. FALL FROM GRACE

Valuating a commodity driven business typically trends with the price of that commodity at a given period of time. Over time, Chesapeake Energy managed to find a way to circumvent that common logic as we have shown over the years since its inception. This trend continued up to the 2010 IPO filings. While the company has had large decreases in its valuation due to falling commodity prices in natural gas, other problems within Chesapeake's corporate governance has exasperated the effect. Actual acts of corruption exist across a rather broad range; however, there are key elements that are common across the entire range including short cuts to gain market share and outcomes that undermine stakeholder welfare (Saeed & Ahmed, 2001). In recent years, Chesapeake Energy has suffered demise due to its bullish and relentless leadership stemming from one McClendon. Although McClendon has been off the board since 2013 due to shareholder revolt, his practices still affect Chesapeake to this day and their impending doom as a public entity (Gustin, 2012).

6.1 Land Grabbing

One of the most notorious traits of McClendon and his leadership team was to conduct what critics considered land grabbing; a business model which includes acquiring as much land as possible despite cash limitations (Horn, 2013). Regardless of any common business sense, McClendon utilized this business model to grow the company. Under McClendon's direction, the money to be made was not selling natural gas as a commodity; but rather, the buying and selling of leases containing the gas (Goodell, 2012). After Chesapeake acquired a tract of land, they would then drill for gas. If and after gas was proven in the tract, they then sold the leases to operators interested in acquiring producing leases. McClendon used this logic beginning with the inception of Chesapeake in 1989. With his background as a Landman, McClendon used his insight for this type of strategy in purchasing and trading oil leases, which became the business strategy at Chesapeake.

McClendon began this blitzkrieg of land grabbing early on in his career and continued up until his departure from Chesapeake. In 2008, at the petroleum price peak, McClendon was making deals priced up to $30 thousand per acre in the Haynesville shale formation (Goodell, 2012). Such transactions proved near disastrous in 2008 as natural gas prices slumped and over-leveraged assets resulted directly from overpriced leases. In turn, this caused a drop in Chesapeake's value by 80 percent (Helman, 2011). Despite this slump, McClendon managed help Chesapeake stay afloat. While shareholders may have praised McClendon for Chesapeake's 2009 rebound, it was not before his unethical practices made him famous. McClendon was able to rebound Chesapeake's margin calls by raising funds from the questionable Founder Well Participation Program (FWPP) (Driver & Grow, 2012). Despite McClendon's highly aggressive techniques, he was always able to secure leverage to make the next acquisition.

By 2012, Chesapeake had acquired over 15 million acres of land containing natural gas (Polluter Watch, 2012). According to Driver, et.al (2012), Chesapeake had spent $31.2 billion to acquire drilling rights on unproven U.S. land over the course of a 15-year period. This dwarfed the acquisitions of Exxon – a company whose revenue was 35 times larger than Chesapeake's – and who only spent $27 billion over the same 15-year period (Driver, Grow, & Schneyer, Reuters, 2012). We suggest this is illustrative of Chesapeake's hunger for land acquisitions no matter the market cost or the cost passed to shareholders.

The old saying 'buy low and sell high' did not seem to be a philosophy that McClendon or Chesapeake subscribed to. Instead, McClendon and company seemed to live by the adage: 'buy high or low as long as were buying'. Leveraging production costs is not unusual in the oil and gas industry and is a commonly used business practice. However, Chesapeake's leverage ratios were much higher than their domestic and international competitors (Chesapeake Energy Corporation, 2014). These higher than normal leverage ratios illustrate the amount of money needed to perform large-scale lease acquisitions orchestrated by McClendon; yet, Chesapeake did not have enough cash flow to support such tactics.

By early 2016, Chesapeake was enduring the most turmoil it has experienced since inception. The company is taking a hit much greater than its near demise in 2008-2009. Since going from one of the biggest natural gas powerhouses, Chesapeake (2016) is currently valued as a virtual penny stock in the market with talks of bankruptcy (Google Finance, 2016). Even though McClendon was removed from the board in 2013, shareholder distrust, debt covenant fears, and a mounting gap between cash flow and future expenditures have pushed Chesapeake to the brink of bankruptcy. The market value of natural gas has dropped tremendously and aggressive land grabbing tactics, facilitated by McClendon, has increased Chesapeake's leverage ratios even higher to pay for past purchases and acquired leases. In addition to focusing solely on land trading for revenue, there was not a consistent form of operating cash flow to be received from drilling and development to pay for those covenants. Although this is not the first slump in Chesapeake's history, it may be the company's last.

7. LEADERSHIP AND THE LEGACY OF AN AGREEMENT

In 2008, Fortune Magazine (2008) regarded Chesapeake Energy as one of the 'Best Companies to Work for in America' and the Chesapeake had built a reputation as the one of the most aggressive energy companies in the industry. This designation by Fortune magazine continued through 2014 (Chesapeake Energy Corporation, 2014). Since its inception, Chesapeake's executive leadership fostered a culture of growth through acquisition. In 1999, Chesapeake Energy Corporation was valued at approximately $30 million; by 2008, the company value had ballooned to an estimated $15.6 billion (Chesapeake Energy Corporation, 2009). Using shrewd and aggressive trade practices, Chesapeake's leadership established one of the most successful companies in America.

At the height of the company's success, Chesapeake Energy entered into one of the most significant agreements in company history. In October of 2007, McClendon and Chesapeake drafted and signed an 'Amended and Restated Employment Agreement' which became effective in January of 2008 (Chesapeake Energy Corporation, 2007). Although McClendon founded the company and had been at the helm since the beginning, this employment agreement was not a mere extension of his previous contracts. This agreement included provisions that directly conflicted with the interests of the corporation and allowed McClendon to participate in corporate owned and operated oil and gas wells and to engage in other lavish personal activities at the expense of Chesapeake shareholders (Driver, Grow, & Schneyer, 2012).

The importance of well participation and the financial opportunities that come from such practice cannot be overstated when discussing the nature and culture of the oil and gas industry. Well participation is defined as financial participation in the direct costs of drilling a specific well or wells and is differentiated from owning an interest in an oil company stock or partnership (Mineral Web, 2016). Stated another way, this newly drafted and ratified provision allowed McClendon (individually), to become a silent partner in every well drilled by Chesapeake; thereby, diluting shareholder profits (Helman, 2011).

A closer examination of McClendon's previous (2003) employment agreement revealed two particular provisions of interest. One provision was intended to instill a sense of obligation to the company while another provision was to govern the executive's behavior with respect to personal trade practices in the oil and gas industry.

Within the 2003 employment agreement, Provision 2.3 ('Stock Investment') provided that the executive hold no less than 10,000 shares of the Company's stock at all times (Chesapeake Energy Corporation, 2003). This provision would be amended in the latter agreement to require that the executive hold an investment value greater than 500% (in company stock) of his compensation paid during a given calendar year (Chesapeake Energy Corporation, 2007). This provision was included to provide McClendon with a sense of obligation to the company to ensure that his personal financial situation would be directly impacted by the company's performance. Such provisions are meant to positively and substantially impact the CEO's diligence and discretion when making decisions. The purpose of this intent is paramount and will be explored further when discussing the issue of McClendon's personal financial activities. Emerging and modified ethical decision making (EDM) models are being reexamined in light of specific organizational decisions and case studies. For example, the sense making suggests important variables such as personal constraints and emotional regulation as a strategy (Thiel, Bagdasarov, Harkrider, Johnson, & Mumford, 2012) which were both likely lacking in Chesapeake's governance.

In addition to Provision 2.3 described above, Provision 3.0 ('Other Activities') of the 2003 agreement clearly requires that the CEO refrain from engaging in behaviors that may cause the CEO to have a conflict of interest in his/her relationship with the company. By signing the employment agreement and as clearly stated in Provision 3.0, McClendon agreed not to:

"(a) engage in other business activities independent of the Company which individually or in the aggregate require a substantial portion of the Executive's time; (b) except for passive investments which do not violate this Agreement, serve as a general partner, officer, employee, director or member of any corporation, partnership, company or firm; or (c) directly or indirectly invest, participate or engage in the Oil and Gas Business. For purposes of this Agreement the term 'Oil and Gas Business' means: (i) producing oil and gas; (ii) drilling, owning or operating an interest in oil and gas leases or wells; (iii) providing material or services to the Oil and Gas Business; (iv) refining, processing or marketing oil or gas; or (v) owning an interest in or assisting any corporation, partnership, company, entity or person in any of the foregoing." (page 2) (Chesapeake Energy Corporation, 2003).

These provisions described above – via the execution of the 2003 agreement – were fully enforced until the Restated and Amended Employment Agreement became effective January 1, 2008. The Restated and Amended Employment Agreement, the provisions contained therein, and the programs established thereby would shape the remaining years of Chesapeake and McClendon's relationship. The program established in that fateful employment agreement was branded as the Founder Well Participation Program (FWPP) (Chesapeake Energy Corporation, 2007). The FWPP allowed McClendon to enjoy the spoils of the company in a manner that was separate from, and in addition to, his lucrative executive employment contract. This significant and definitive agreement did have some restrictions though, as it required that the CEO participate in an 'all or nothing' manner. In other words, the CEO was not allowed to participate in some wells and pass on others.

Well participation can be costly, especially when one considers that Chesapeake Energy was heavily engaged in unconventional well development (fracturing, horizontal drilling, etc.). This type of well development is very expensive as evidenced by Chesapeake's 2008-reported acquisition, development, and exploration costs, which totaled approximately $8.5 billion in 2008 (Chesapeake Energy Corporation, 2009). By the terms spelled out in the FWPP, McClendon would be responsible for approximately $212 million to cover his proportional share of Chesapeake's 2008 development costs (assuming that all wells were grass roots wells). This extraordinary expense resulted in McClendon securing bank loans to finance these operating costs, which effectively created a conflict of interest as defined in the 2007 employment agreement. Joshua Fershee, associate professor of energy and corporate law at the University of North Dakota, said:

"If Mr. McClendon has $1 billion in debt through his own companies - companies operating in the same industry as Chesapeake - he has or could have a high degree of risk for conflicts of interest. As in, whose interest will he look out for, his own or Chesapeake's(?)" (Page 2) (Driver & Grow, 2012).

Another important clause required McClendon "to take all commercially reasonable action" (Page 2) to ensure that other owners and operators of the wells including Chesapeake "comply with…covenants and agreements" (Page 2) of the loans (Driver & Grow, 2012). Such clauses are common in energy finance deals; but it is rare for the CEO of a major energy company to be personally subject to such a provision involving the corporation that he/she runs. This setup yet another potential conflict as McClendon could have an incentive to influence Chesapeake to act in the interest of his (personal) lenders rather than Chesapeake's shareholders. (Driver & Grow, 2012).

Other modifications to the Amended and Restated Employment Agreement highlighted the CEO's growing sense of entitlement. A new provision in the employment agreement made effective January 1, 2008 cited security reasons to include the following provision:

"4.6 Travel. For safety, security and efficiency the Executive will utilize aircraft owned, leased or chartered by the Company for business and personal use and will not be required to reimburse the Company for any cost related to such use. The Executive will: (a) not owe any additional amounts to the Company under this paragraph for guests or family members traveling with the Executive; and (b) pay all personal income taxes accruing as a result of the personal use of the Company's aircraft by the Executive and the Executive's immediate family members under this paragraph" (Page 5) (Chesapeake Energy Corporation, 2008).

Yet another significant modification made to the employment agreement pertains to McClendon's annual salary. According to Chesapeake's records, McClendon's salary was $300,000 annually in 2003 (Chesapeake Energy Corporation, 2003). Four years later, the CEO's salary had increased 325% to $975,000 annually. Additionally, there were added bonuses deemed appropriate by the Compensation Committee of the Board of Directors (Chesapeake Energy Corporation, 2008).

An Oklahoma City reporter cited the following when discussing McClendon's behavior and use of company resources:

"According to internal documents reviewed by Reuters, the unit's accountants, engineers and supervisors handled about $3 million of personal work for McClendon in 2010 alone. Among other tasks, the unit's controller once helped coordinate the repair of a McClendon house that was damaged by hailstones. Fourteen miles south, at Will Rogers World Airport, Chesapeake leases a fleet of planes that shuttle executives to oil and gas fields and the McClendon family to holiday destinations. On one trip, the clan took flights to Amsterdam and Paris that cost $108,000; McClendon counted the trip as a business expense. In another case, Chesapeake logs show, nine female friends of McClendon's wife flew to Bermuda in 2010 without any McClendon (family members) aboard. The cost: $23,000" (Page 1) (Driver, Grow, & Shiffman, 2012).

All of these behaviors illustrate how success and opportunity can lead an individual toward self-centered decision making if he or she is not subject to an appropriate set of checks and balances. Unfortunately, the FWPP and other amendments to McClendon's Amended and Restated Employment Agreement of 2008 proved to be the platform and opportunity that allowed his ego to cloud his overall judgment and act in a self-serving manner.

Unfortunately, the Executive Staff and Board of Directors, which built Chesapeake Energy Corporation from a fledgling oil and gas company in 1989 into the industry titan they had become by 2008 will likely not be remembered for their accomplishments. They are the same Staff and Board who supported the personal aspirations of a single officer of the company rather than keeping the best interests of the corporation and stakeholders at the center of their decisions.

In May of 2012, Chesapeake Energy Corporation filed a report with the U.S. Securities and Exchange Commission (SEC), which read:

"Pursuant to a letter agreement, dated as of April 30, 2012 (the "Letter Agreement"), between the Board of Directors of Chesapeake Energy Corporation (the "Company") and Aubrey K. McClendon, Chairman and Chief Executive Officer of the Company, the Board and Mr. McClendon agreed to the early termination of the Chesapeake Founder Well Participation Program (the "FWPP") on June 30, 2014, 18 months before the end of its current term on December 31, 2015. The Letter Agreement provides that Mr. McClendon will not be entitled to compensation in respect of the early termination of the FWPP. In order to effectuate the early termination of the FWPP, the Letter Agreement provides for certain amendments to the FWPP. In addition, the Letter Agreement reflects the Board's determination that the positions of Chairman of the Board and Chief Executive Officer should be separated and Mr. McClendon's support for that approach. In connection with that separation, Mr. McClendon waived any rights he may have under specified provisions of the Third Amended and Restated Employment Agreement between Mr. McClendon and the Company, effective March 1, 2009 (the 'Employment Agreement'). Mr. McClendon also agreed to provide to the Board at any time during his employment with the Company and prior to a Change of Control (as defined in the Employment Agreement), to the extent reasonably available and reasonably requested in writing by either the Chairman or the Lead Director, certain information regarding his participation in the FWPP. The foregoing summary does not purport to be complete and is qualified in its entirety by reference to the specific language of the Letter Agreement, which is attached hereto as Exhibit 1.1, and the FWPP as amended and restated, which is attached hereto as Exhibit 1.2" (Page 1) (Chesapeake Energy Corporation, 2012).

McClendon was also expelled from Chesapeake Energy Corporation and would move on to form a new corporation. Nevertheless, it appears that Chesapeake's Board of Directors and shareholders have learned a costly, but valuable lesson: every single decision matters.

Subsequent company officers have also been barred from participating in oil and gas activities and it does not seem likely that anyone will challenge that logic in the wake of Chesapeake's fall from grace.

8. REBIRTH OF CHESAPEAKE ENERGY

Transitioning into 2016, Chesapeake is aligning their strategy to take into account gaps in technology. Chesapeake's strategy encompasses drilling longer multi-section laterals to drive down costs compared to traditional drilling of standard laterals (Seeking Alpha, 2016). Chesapeake's expectations per well are expected to reduce costs by 27%, or approximately $700,000 per well in many locations. Chesapeake's motivation of this strategy is to reduce their break-even point to $40 per barrel of oil and deploy this strategy to other plays (Chesapeake Energy, 2015). Below is an example of Chesapeake's projected reduced costs by utilizing this strategy in the Hayneville play to reduce drilling costs per foot. From the second quarter of 2014 through the third quarter of 2015, Chesapeake has reduced drilling cost per foot by $80. The significance of Chesapeake's strategy is to continue to push for their $40 per barrel threshold to increase profits.

These types of strategies are an integral segment of why new management is leading the way for the turn around to occur with Chesapeake. The new leadership understands that in order to be successful, they need to take advantage of technology and their skilled employees. Even though this rapid transformation process is taking place, the question remains if investors will chose Chesapeake Energy.

8.1 CEO Doug (Robert) Lawler

Doug Lawler has taken significant steps at the helm of Chesapeake in making decisions to alter past financial, operational, and cultural issues that have affected (and continue to effect) the company under the reign of McClendon. Stock price fluctuations of Chesapeake under Lawler's control began at $19.90 per share (June 17, 2013), peaked at $30 per share, and significantly declined to current levels of $1.50-$2.50 per share in 2016 (Google Finance, 2016). The reasons behind such a drop are not just attributed to the recent decline in oil and gas prices. As we have described above, there are deeper and engrained issues of uncertainty from investors (Assis & Linnane, 2016). McClendon's removal brought to light the borrowing of large sums of money from private-equity firms that had invested in the company to be used for personal use (Ailworth, 2015). Ailworth (2015) further reports that Chesapeake had issues with overspending that sent stock prices on a 'roller coaster' because of substantial leveraging that frightened investors and shareholders. McClendon loved the control he exerted on others; all the way down to selecting what kind of cheese the cafeteria could serve (Ailworth, 2015). This control had lingering effects on employees as the new CEO Lawler has been trying to transition a much greater level of transparency to all stakeholders of the company (Ailworth, 2015).

Continued inquisitions by Lawler of financial records disclosed many more issues that needed immediate attention. Extravagant costs associated with Chesapeake's name on the local sports arena, giving millions to charities, perks to employees, providing a community garden (and company beekeeper), access for employees and investors to have company paid Botox injections while enjoying tanning beds were immediately eliminated as unnecessary expenses (Ailworth, 2015). Lawler understood that many employees would view his tact as cheap or question his authority because they had always perceived these expenses as entitlements under McClendon's control (Ailworth, 2015). McClendon signed agreements with outside investors that committed Chesapeake to drill hundreds of wells in regions that showed little promise to be economically productive (Ailworth, 2015). The company was also responsible to transport required amounts of natural gas on agreed pipelines or face significant penalties. McClendon's commitments positioned Chesapeake's spending from 2010-2012 to be almost $30 billion more on drilling and leasing than it brought in from operations (Ailworth, 2015).

By 2015, Lawler made significant strides in eliminating unnecessary expenses by decreasing spending by more than half of 2012 numbers. Lawler has accomplished this by removing 67% of staff employees, decreasing drillable acreage by 5.5 million acres, resolving anti-trust allegations by the state of Michigan, along with two-thirds of the total lawsuits filed against Chesapeake over past business practices; again, all incurred under McClendon's control (Ailworth, 2015). The response from employees that are still employed by Chesapeake has been very positive as they appreciate their CEO and company as they are aggressively fighting to survive. This type of personal ownership from employees has triggered cost reduction measures to align with Lawler's own message. Employees strive to find higher efficiency to reduce costs in drilling processes while leadership continues to find ways to stay solvent. This two-way (e.g., Chesapeake's current leadership team and employees) initiative is currently keeping Chesapeake afloat; while any negative reaction from investors could cause the company to file for bankruptcy. If Chesapeake does survive, leadership should understand the impact that virtue has on organizational commitment (Neubert, Carlson, Kacmar, Roberts, & Chonko, 2009). The employees that remain at Chesapeake are very likely ready to help turn the corner and journey together with a virtuous and ethical leader.

9. FUTURE OF CHESAPEAKE ENERGY CORPORATION

Chesapeake Energy Corporation has positioned itself via revamped operations to survive through 2016 by suspending preferred dividend payouts, issuing second-lien notes, suspending common-dividend stock, stopping the payments of corporate bonuses, and continuing to reduce staffing levels to skeleton crews (Jakab, 2016). Chesapeake currently has $9.8 billion in debt, which is six times higher than their total market capitalization (Graul, 2016). As rumors spread through the industry that Chesapeake is restructuring their debt for a possible bankruptcy, the company continues to pay down debt. More specifically, a $500 million note that is due in mid-March has already been funded which instills confidence in investors (Graul, 2016). However, professionals in the energy industry understand that 'cash is king' and Chesapeake is not able to grow assets because of the current state of the market. Competitors are waiting. Why should these competitors purchase assets at a higher price when they could wait for Chesapeake to possibly liquidate their position? Unless there is a dramatic swing in the oil and gas markets, Chesapeake's future may conclude by the end of 2016 or early 2017. There is just too much commodity in the market (oversupply). Even though Chesapeake has realized past failures and has successfully mitigated those failures, this one may be insurmountable.

10. CLOSING CHAPTER ON AUBREY MCCLENDON

Majority shareholder and investor Carl Icahn led the shareholder revolt in 2013 to remove McClendon as CEO (Ailworth, Kendall, & Olson, 2016). Past issues surrounding Chesapeake's agreement with the Michigan Attorney General to resolve any anti-trust allegations under McClendon's control has led to further investigation of the U.S. Justice Department (Ailworth, Kendall, & Olson, 2016). On March 1, 2016, The Justice Department indicted McClendon on charges that he violated the Sherman Act for oil and gas leasing activity (Ailworth, Kendall, & Olson, 2016). If McClendon were to be found guilty of the pending charges, maximum penalties could include a fine of $1 million and 10 years in prison (Ailworth, Kendall, & Olson, 2016). Chesapeake will avoid any further investigation from the Justice Department and will not face any criminal prosecution or fines. Chesapeake has also acknowledged that they are taking appropriate steps to try and address any legacy issues while continuing to comply with all laws and regulations (Ailworth, Kendall, & Olson, 2016). There is an ongoing call for more diligence and policing by stakeholders and researchers (for example, see Martin & Cullen (2006)). Likewise, there are calls by researchers to investigate cultural manifestations (Bertsch, 2013) which, may serve a company like Chesapeake well as they continue their transition and attempt to survive.

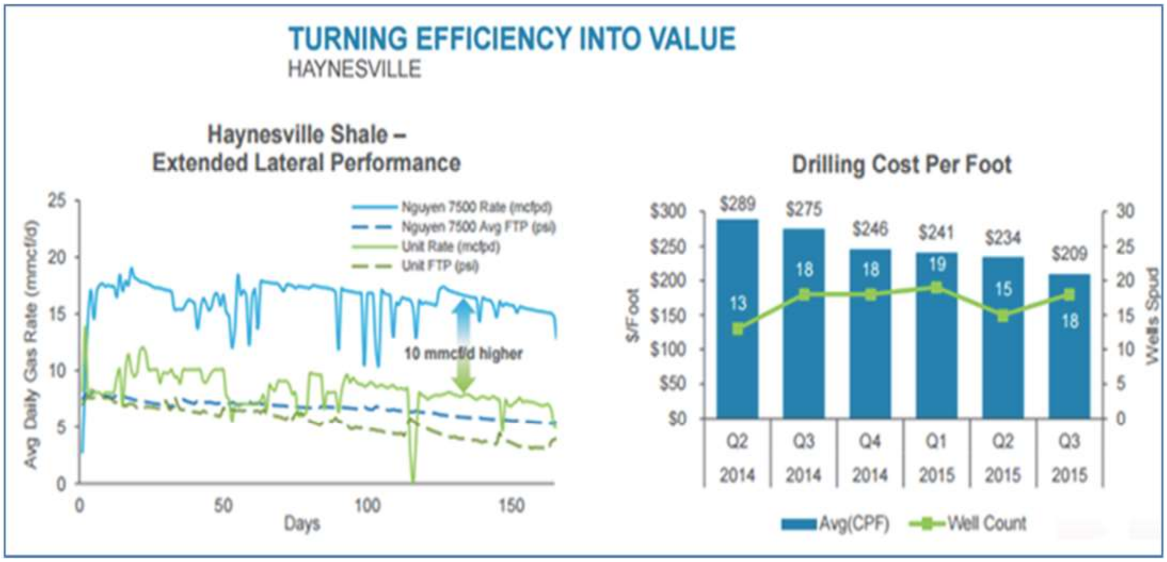
10.1 Addendum

Our study has introduced the rise of McClendon in the oil and gas industry, the start of Chesapeake Energy, surrounding issues that arose under his authority, and his dismissal from Chesapeake. However, we did not foresee the sudden death of McClendon that occurred one day after his indictment by a federal grand jury on charges of conspiring to rig the price of oil and gas leases (Ailworth, Olson, & Dezember, 2016). The late McClendon died in a single-vehicle crash when his car struck a concrete wall of an overpass at a speed well above the 40-mph limit (Ailworth, Olson, & Dezember, 2016). At age 56, McClendon leaves behind his wife, Katie, and three children (Ailworth, Olson, & Dezember, 2016). T. Boone Pickens, another energy pioneer, describes Aubrey McClendon from his past 25 years of knowing him:

"He was a major player in leading the stunning energy renaissance in America. He was charismatic and a true American entrepreneur. No individual is without flaws, but his impact on American energy will be long-lasting" (Ailworth, Olson, & Dezember, 2016) (page 1).

On March 3, 2016, the Justice Department dismissed the indictment against McClendon that will probably conclude any further probing into alleged 'bid-rigging' of oil and gas leases (Ailworth & Olson, 2016).

FIGURE 1: HAYNESVILLE PLAY (SOURCE: CHESAPEAKE ENERGY, 2015).



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