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What Can We Learn from the Downfall of Theranos?

The health company's plummet carries valuable lessons for Silicon Valley.

December 17, 2018 | by Sachin Waikar

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Theranos founder Elizabeth Holmes epitomized Steve Jobs, which attracted Silicon Valley investors who didn't look too closely at the health company's claims, says John Carreyrou, the Wall Street Journal reporter who investigated Theranos. | Reuters/Brendan McDermid

One of the most epic failures in corporate governance in the annals of American capitalism.

That's how [John Carreyrou](#) described the high-profile plummet of health technology business Theranos from heralded Silicon Valley unicorn to disgraced cautionary tale, with founder Elizabeth Holmes and President and COO Ramesh "Sunny" Balwani facing multiple current fraud charges. Carreyrou, a Pulitzer Prize-winning *Wall Street Journal* reporter, chronicled the downfall of Theranos in his book [Bad Blood](#).

Carreyrou recently visited Stanford Graduate School of Business as part of a program organized by the school's [Corporations and Society Initiative](#). He spoke before an audience in conversation with [Michael Callahan](#), executive director of the [Rock Center](#) for Corporate Governance, which cosponsored the event.

The Theranos story was supposed to have a very different ending. In 2003, 19-year-old Elizabeth Holmes dropped out of Stanford University to start the company, which promised something revolutionary: accurate diagnoses of health conditions using a single drop of blood. Holmes's passion for the venture and Steve Jobs-like image (black turtlenecks and all) gained her the support of luminaries like Oracle founder Larry Ellison and former Secretary of State Henry Kissinger.

But the suspect science behind Theranos and its paranoid, secretive culture of leadership eventually caught up to the business, leading to criminal charges.

Professor [Anat Admati](#), faculty director of the Corporations and Society Initiative, noted in [her introduction](#) for the event that "Theranos raises

Stanford community by shedding light on what happened and what the audience can learn from this story.

Here are the main takeaways from Carreyrou's discussion of the scandal.

Dark Side of the Valley

"The culture of Silicon Valley created the conditions for someone like Holmes to come along, to thrive," Carreyrou said.

For example, the valley is replete with mantras like "fake it until you make it" and "fail fast." As Carreyrou noted, "Holmes' grave error was to channel this culture, especially the fake-it-until-you-make-it part." Applying such maxims to a medical product with life-and-death implications was a key driver of the Theranos downfall. The technology simply couldn't deliver as promised.

The gender factor also played a role, as Carreyrou highlighted in his book: "There was a yearning to see a female entrepreneur break out and succeed on the scale that all these men have: Mark Zuckerberg, Larry Page and Sergey Brin, Steve Jobs, and Bill Gates before them." As a young, conventionally attractive woman, he adds, Holmes was also able to charm many of the older men who eventually backed her.

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— John Carreyrou

Carreyrou's outside perspective helped him break the story. The reporter entered Silicon Valley not as a tech businessperson or even a tech reporter but as a health care reporter pursuing a tip. "The reporters who had interviewed Elizabeth Holmes over the previous two years accepted the way she framed herself as heir to the throne of Steve Jobs," he said. "I came at it from the medical perspective with my East Coast skepticism."

No Checks, No Balances

The Theranos board and federal regulators provided insufficient oversight, Carreyrou noted.

Theranos board that Holmes had exaggerated revenue projections, the board considered replacing her with an experienced executive. “They decided the company needed to be led by an adult,” Carreyrou said. But Holmes talked her way out of the decision and prevented subsequent intervention by multiplying the voting rights of her shares to give her 99% of total voting rights.

The board was a who’s who of big names — including Kissinger and current Secretary of Defense Jim Mattis — that boosted Theranos’s reputation and Holmes’s credibility, but was a “make-believe” board, Carreyrou said, due to Holmes’s voting control. “This board took her at her word,” he added.

Theranos also exploited a regulatory loophole: Laboratory-developed tests like those the business offered didn’t (and still don’t) fall under the exclusive purview of the Food and Drug Administration or other health care-focused agencies. No one was truly policing the business’s processes or offerings. Of course, Theranos was actively deceiving regulators, too. “I’m not sure what law you could pass that would catch someone intent on lying,” Carreyrou said.

From Confidence to Confidence Games

“Elizabeth Holmes is not Bernie Madoff,” Carreyrou said. “I’m pretty certain she didn’t drop out of Stanford premeditating a long con.” He pointed out how much entrepreneurs have to believe in their product, even if no one else does, especially to recruit investors.

“But there’s a line between that and hyping so much you cross over into outright lies,” Carreyrou said — such as when Holmes misrepresented the sources of finger-stick tests, most of which were done on Siemens machines rather than her company’s. Those tests — and Walgreens’ adoption of Theranos technology in its stores — led to \$750 million in new funding.

“The gap between what she claimed and what she had really achieved became a massive fraud,” Carreyrou said.

Culture at the Core

Would-be whistleblowers were threatened with lawsuits. Criticism of leadership or practices was unwelcome. Those who pushed “were usually either fired or marginalized to the extent that they had to leave — they had an expression, which was to ‘disappear’ someone,” Carreyrou said. “The paranoia went into overdrive.”

He added, “If the culture had been more wholesome, then maybe Theranos would have actually made some headway toward achieving Holmes’s vision.”

A Dangerous Formula

At the time of this writing, Holmes and Balwani were facing fraud charges, including making false representations to investors, doctors, and patients. “I think the public health component of the criminal charges is going to resonate,” Carreyrou said. “It wasn’t just billionaires who were misled and bamboozled.”

Perhaps the biggest takeaway from the Theranos story is the expansion of Silicon Valley from its traditional roots to a much broader range of offerings. “It’s getting into new industries, getting into self-driving cars, getting into medicine,” Carreyrou said. “When you enter industries where lives are in the balance, you can’t really just iterate and debug as you’re going. You have to get your product working first.”

Combine that reality with the “myth of the brilliant Silicon Valley start-up founder who sees around corners and can never be wrong,” as Carreyrou described it, and you have a very dangerous set of circumstances — the kind that yield a business story that starts with sky-high valuations and ends in criminal charges.

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