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Ethical Dilemmas in Corporate Restructuring[1]
Part A

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Markov was pleasantly surprised when only a week after returning from four months of training abroad, the Deputy Mayor called and asked for a meeting. The Deputy Mayor was very interested to learn what kind of training Markov had attended, and how relevant it was for his company. Markov explained that the training was focused primarily on the fundamentals of a market economy, and covered a broad range of macro and micro issues. With some excitement, he began talking about private sector development and the way corporations operate in a market economy. The Deputy Mayor listened very carefully, but did not show any reaction. This made it difficult for Markov to "tune" his presentation, and he did not know how much excitement and emotion he should demonstrate as he talked about the privatization of state owned companies. While he was thinking about how to proceed, he was interrupted by the Deputy Mayor: "Markov, we have decided to offer you a new job. You have spent the past 10 years, in fact for your entire professional carrier, with Green Apple, our leading food processing company. You know that with the transition to a market economy Green Apple has started to experience serious problems, including competition from imports and several new private start-ups. Mr. Petkov, your current boss, has successfully run the company for the last three decades, but the times have changed, and besides, he is about to retire. With your knowledge of the market economy, and your experience with Green Apple, we believe that you are our best choice for a new general manager."

Markov was in shock. While he was honored by the offer, he was not sure how successfully he could run Green Apple. This was one of the biggest companies in the city, as well as the major employer. He was intimidated by the responsibilities of this assignment, but before he had time to express his doubts, the Deputy Mayer stood up to congratulate him on his new job, telling Markov that he would have the full support of the city administration. And that was it. Next Monday, Markov was sitting in his new office grappling with the financial situation of Green Apple. It did not take long before he realized that the company was in big trouble. The debt to local banks was huge and there was no possibility of this being repaired soon. Inventories were full and sales were slow. The competition from imports and several local private competitors was severe. He spent the next several weeks trying to figure out how to turn the company around. He found himself in a position of trying to implement what he had learned during his training abroad. The privatization and finance experts had lectured about the importance of

[1] Djordjija Petkoski, of the World Bank Institute, prepared this case as a basis for class discussion, rather than as a means for illustrating either effective or ineffective handling of a management dilemma. Part C of this study contains short descriptions of two real-life examples published by L.S. Paine, "Managing for Organizational Integrity," in Harvard Business Review, March-April, 1994.

stopping the financial bleeding of a company, spinning off the social assets, and privatization. He did remember the long debate on whether the company should first be restructured and then privatized, or immediately privatized. But he could not recall whether there was any consensus on this. What he knew was that Green Apple desperately needed cash. He wanted to find out which of the business units was most profitable and then focus on increasing sales. He knew that it would take time before any substantial increases in revenues could occur. This is why he also wanted to know whether he could sell some of the social assets and thereby immediately generate cash and avoid potential bankruptcy. Markov knew that the city administration could not afford to immediately close Green Apple, but he was also aware that there was no chance of getting any additional loans from the essentially bankrupt local banks.

His advisers came up with two solutions. First, to sell the company recreation facilities at the lake, and second, to increase apple juice sales through more aggressive marketing. Both options were so appealing and so easy to implement that Markov asked his secretary to arrange for a dinner with the management team where he would explain the “new corporate restructuring strategy.” Everybody got so exited with the good news that the dinner lasted until the small hours of the morning.

The Apple Juice

Markov first focused on the apple juice business, the most profitable business of Green Apple. After looking at the financial data, he realized that the main gains were coming from the low price of high quality apple juice concentrate, which they were buying through a small private company, QuickEx. He immediately called the managers of the juice business unit to discuss the possibility of increasing sales of apple juice. He took the opportunity to tell them that he had learned quite a lot about marketing and that, in this particular case, they should focus on pursuing an aggressive marketing campaign. “We have an excellent product – 100% pure apple juice. It is not enough that this is clearly written on the label. Our marketing campaign should emphasize the purity of our product, and drive out the more expensive and lower quality imported products. The quality of our juice is what really matters. Thanks to the transition to a market economy, the population is becoming increasingly aware of the importance of the nutritional value of food. We should be able to benefit from this trend.”

A few days later Markov was approached by Ms. Bisera, the chief of the company’s laboratory and research department. She explained to him that immediately after the contract was signed with QuickEx, there was a rumor that the “pure apple concentrate” was actually not that pure after all, and that it contained sugar water and some chemical additives. Although she was never officially asked to do so by management, she performed some laboratory testing. They did not have all of the necessary instruments to systematically perform this kind of work, but preliminary results suggested that there was some truth to the rumors. She had verbally informed the general manager, but no action was initiated. Moreover, she was explicitly told that they do not need any written report on this. After all, no one had asked her to “waste time on this kind of research.” Later she learned that the owner of QuickEx was the son of the City Mayer.

After hearing this, Markov decided not to call an official meeting, but to first have several informal discussions with members of the management team. The message he received was quite clear. There was an established practice in the company of not worrying much about customers, so long as their health was not in danger. In addition, there was nothing in the country's laws indicating how this should be handled, and no one could recall of any domestic company having to face legal charges because the declared nutritional content of their product was not 100% identical to the real content. The colleagues insisted that the main priorities for the company was to preserve the level of employment and increase the cash flow, and only later would they worry about whether the apple juice was 100% pure or not. Some of them reminded Markov not to forget who the owner of QuickEx was, and that it was very important for the company to preserve good relations with the City Administration.

Markov decided not to make any decisions for the time being on whether they should terminate the contract with QuickEx; change the label of the apple juice and disclose the real content; or simply eliminate the inventories, buy 100% pure juice concentrate from another importer and continue insisting on the 100% natural apple juice. He wanted to concentrate on a more immediate task – selling the recreation facilities.

The Recreation Facilities

Markov did remember the lecture from the World Bank expert, who insisted that one of the main tasks of any company in a transitional economy is to get rid of the social assets. "Manager should focus on managing the core business and not to waste time on managing hospitals, schools, restaurants, and recreation facilities."

The good news came within a week. He learned from the press that representatives from Global Travel, a large multinational travel company, would be visiting his country soon. Global Travel had already made several joint ventures in neighboring countries, and had expressed a strong interest in investing in his country as well. Markov immediately asked several members of the management team to join him for a visit to their recreation facilities. Although over the past twenty years, the lake had suffered serious environment degradation, it was still renowned for its beauty. Markov expected that Global Travel might be interested in buying their recreation facilities in order to expand their regional chain of hotels. In this way, foreign tourists could visit several countries in the region, adding to the diversity of their travel tours.

"We have good facilities to sell," insisted Markov. Reminded by his colleague Vladimir, the manager of the complex, that the facilities had been built thirty years before, and that very little new investment had occurred since then, Markov energetically reacted by stating that "we are not selling building, but fresh air and clean water. The only real problem I see, is how to evaluate this. We need to complete a comprehensive evaluation of our facilities, including the 'intangibles.' I have to look again at my notes on business evaluation. In the training program, we learned several methods on how to do this."

On the way back from the lake, the recreation facilities manager took the opportunity of speaking alone with Markov. "A long time ago," said Vladimir, "there was a rumor that a few years before the recreation facilities were built, the land was used to dump metal containers with chemical waste from the local pharmaceutical company. Perhaps these were just rumors. In the meantime, over the past thirty years no one has reported any health complaints. Even if it was true, the container was probably built of solid metal. At that time, no one really paid much attention to the costs of production. But who knows, if true, the waste might one day find its way to the lake."

Vladimir promised to conduct a small investigation without involving other people. He could not find any information in the corporate books, nor in the city archives. However, his neighbor, a retired employee from the pharmaceutical company, told him that he was personally involved in dumping the containers and that they were filled with highly toxic waste. "As far as the official books are concerned, we are OK," insisted Vladimir. "There is also nothing in the country's laws regarding the disclosure of hazardous substances on commercial property. The new environmental law has been in the parliament for the last three years, and still there is no chance that this law will be debated in the near future."

Markov's Dilemmas

In addition to the problems regarding the purity of the apple juice, Markov faced another dilemma. Should he disclose the "unofficial information" regarding the dumped hazardous waste with the Global Travel representatives, or should he simply point out what was written in the official documents? Global Travel was a big company and they could easily fix the problem once they bought the property. Any disclosure could easily postpone the negotiations with a real danger of completely loosing the chance. The lake was big enough and there were many other properties for sale.

Markov decide to take the binders containing the training material to his summer house for the weekend. He wanted to refresh his memory. So many important topics had been covered during the training course abroad that reading some of the material could be very useful. He would have two days to decide what to do with the apple juice and the recreation facilities.

What should Markov do?