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Restoration of the Sea Star

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Soon after the country finally decided to abolish the centrally planned economy and move toward a market economy, the ship-building industry, the pride of the country's post-war growth, faced serious challenges. The markets in other transitional economies were lost, at least for the foreseeable future. The high cost of production and the low quality of their ships made it nearly impossible to enter the markets of developed countries. In the middle of this crisis, the top management of the shipyard decided to take advantage of their country's privatization program. The opportunity was unique, with very little personal capital they were able to take control of the company. The fact that the workers also acquired part of the shares did not bother the top managers. The control package was in the hands of the top managers and it was very easy to "manipulate" the minority share-holders – including the employees.

But soon the good feelings that came with owning the company were over. It took less than a year before they sold everything of the company that could be sold. The profit did not come from selling any new ships but exclusively from selling huge inventories of raw material that accumulated during the previous regime. For months, the employees received a small fraction of the salaries that they use to receive before privatization. The top managers also became more and more nervous because they could not see any way of improving the company's situation. Overwhelmed with their short term interest, they never made any serious effort to restructure the company. A few offers that they received from several foreign strategic investors were immediately turned down. Nothing could convince them that they should give up control of the company to foreigners. They had managed the company for so many years that they knew every single detail of its operations. How could foreigners successfully run a company that they did not know well, in a country they did not completely understand. Equity investment was out of the question as long as the investors wanted to have control over the company. On the other hand, no foreign investor was interested in providing loans. Management was also unable to get any new loans from domestic banks. The overall situation of the company was becoming worse with each passing day.

Vladimir, the company's top manager and main shareholder, although a born optimist, became more and more insecure. He desperately waited for the day when the situation would finally turn around. One afternoon, as he stood by the windows of his office, the telephone rang. He was not sure how much time went by before he picked up. He was looking out the window overseeing not only the shipyard but also a good part of the city. It was one of those miserable autumn days when the clouds were low and the rain fell hard and he could barely see the top of the big cranes that had not been used in months. He wondered if the visibility was so poor because of the rain or due to the

nearby heating station, which provided hot water for the entire city. Environmental protection was not high on the company's list of priorities. The city government also did not care much about pollution. In fact, not much had changed from the days of the centrally planned economy when very little attention was given to environmental protection. With so many companies on the brink of bankruptcy and poorly enforced environmental regulations, Vladimir wondered whether the pollution was even worse than before.

The telephone call brought him back to reality. It was Peter, one of the company representatives from one of the Western countries. With an excited voice, Peter told him the big news, something they were waiting for many years to hear. There was a real possibility for the company to get a good job.

It was not about building a new ship, but about restoring an old ocean liner. A few months ago, a group of investors in one western country decided to reactivate an old cruiser, "Sea Star". The world economy was doing well. People were more and more attracted to cruises. The capacity of the liners was not sufficient to meet new demands. Building a new liner would take too long and they did not want to lose the opportunity presented by increased demand. Finally, Sea Star, once a luxurious ocean liner, had a long tradition and was well known in the tourism trade. Its brand name could easily attract more passengers than a new one. The only serious problem was that most of the insulation of Sea Star was made with asbestos. At the time it was built, asbestos was considered to be an excellent material. Only much later was it found to be very dangerous.¹

This fact surfaced much later because asbestos producing companies did their best not to inform the public of the danger. Once this became known, at least in the Western countries, governments attempted to eliminate the problem. In several cases, the companies were seriously punished for non-ethical behavior. A case in point was the Manville Corporation in the USA. For over forty years, the company (i.e., its top executives) hid the information about the implications of asbestos insulation. Subsequent court decisions seriously punished the company for violating corporate ethics.² The case also contributed considerably to the nation-wide campaign to eliminate the use of asbestos.

Therefore, it was necessary to first strip the ship of its asbestos lining. Only then would the actual restoration begin. Eliminating the asbestos was a very expensive activity. Foreign companies were much more aware that asbestos inhalation was killing people. If U.S. standards for asbestos removal were applied, the estimated cost for this job would be over \$150 million. And this was exactly what several Western companies

¹ Asbestos inhalation is a cause of asbestosis, a debilitating lung disease, as well as lung cancer and mesothelioma, an invariably fatal lung disease.

² "...a California court found that Manville hid the asbestos danger from employees rather than looking for safer ways to handle it.... A New Jersey court was even more blunt: it found that Manville made a conscious, cold-blooded business decision to take no proactive or remedial actions, in flagrant disregard of the rights of others." As a consequence, 80 percent of the company's equity was required to be given to a trust representing the people who had sued or planned to sue the company. See Saul W. Gellerman. "Why 'Good' Managers Make Bad Ethical Choices." Harvard Business Review. April-July 1986, pp. 85-90.

based their fees on to complete the job. Once Peter learned about this, he saw a real business opportunity. He knew that his company could easily do the job much cheaper and still make a large profit.

Vladimir told Peter to immediately send the bidding documents. Once the documents were received, the top managers held a meeting. Everyone was very anxious that their shipyard had a unique opportunity to obtain a highly profitable job from a Western client. There was no uncertainty with this job. If they got the contract, in less than a year they would complete the removal of the asbestos and the money would be waiting for them in a foreign bank. These were serious clients. They would pay, unlike their unreliable domestic clients.

The shipyard managers were surprised that there was not much explanation in the bidding documents about the danger of working with asbestos. Some of the managers argued that the lack of explanation about the deadly consequences of asbestos inhalation was due to the fact that this was well known in the West. Other managers said that, after all, asbestos is not necessarily as dangerous as was reported in the foreign press. Furthermore, the regulations in their own country were not as strict as in Western countries.

The management had no intention of sharing the information about the dangers of inhaling asbestos with the employees. “Why should we do this?” argued the managers. “We will do everything that is required by the country’s existing laws and regulations. You know, the Americans are always pushing things to the very limit. With so many lawyers around, they have no choice but to overstate the facts and to search for any opportunity to make money from innocent companies. Our regulations have been in place for so many years and no one has really complained. And we have used asbestos for many years. Our employees are experienced people.” When one young manager, Marko, noticed that there was no change made in the country’s law when the asbestos problem received so much attention in the Western countries, the reaction from the rest of the group was united. This was not the company’s problem, but a problem of the law.

Marko was not sure whether he should push his arguments further. Everyone was so excited about the potential deal and, at the same time, aware that the decision should be made as soon as possible that they were not ready to listen to Marko. For a moment, Marko thought intensively while listening to his colleagues. He thought about to what extent the discussion to compete for the job was within reasonable ethical and legal limits. Everyone agreed that the deal was in the company’s best interest and therefore, each individual, including Marko, was expected to support the activity. The decision was supposed to be made by a small group of people – real friends who knew each other for many years, and there was no chance that someone out of this group would ever learn how the decision was made. In other words, everyone should feel safe. In the worst case scenario, even if something went wrong, the individuals would be protected because the deal was in the company’s best interest.

As he thought about the potential contract, Marko was interrupted by a heated debate on whether domestic regulations should be changed in order to meet international environmental and safety standards. Marko’s suggestion to consult medical doctors was

also disregarded on the grounds that there was nothing new about asbestos. The fact that the ship was from a foreign country did not make any difference. “The asbestos is the same in our country or abroad,” argued one of the managers. “We have no desire to lose this unique business opportunity,” argued Alexander. “If we follow all of the American regulations, we will never make any money from this deal. And we are not in the business of changing country regulations.”

This might require months to change. “Our parliament is in continuous opposition with the Government and the last issue they want to deal with is environmental protection and the improvement of working conditions,” argued another manager. “Even if we manage to bring the issue to the parliament, which is not in the company’s best interest, we will have serious problems in implementing the new regulations in practice. With a lack of experience in improving the safety of the workplace, it will be very complicated for our company to change the established working procedures. And we are under tremendous time pressure. We have no time to look for safer ways to handle the asbestos problem. We should simply hide the findings made in foreign countries regarding asbestos danger from our employees. Finally, there is no difference between the domestic asbestos and the American asbestos. The employees have never complained about working with asbestos.”

The ethical dilemma was in front of the managers. Or was there a dilemma? The interest of the company was the most important issue. The destiny of thousands of families depended on the survival of the company, which was the major employer in the city. Marko’s dilemma was that the potential deal seemed to be in accord with the country’s laws, and therefore, it was logical that the company expected his loyalty. The fact that the company had no code of conduct or any “official ethical standards” made it difficult for Marko to argue against internal standards and procedures. At the same time, it was difficult for him to draw a clear line between what was the law and what was justifiable from the standards of the broader society. How far is too far and when does our “legal” activity become immoral? Is this deal against common morality and society itself? The main challenge for him was how to apply the general question of human judgement and human behavior in a real life situation. To what extent were these activities “really” illegal or immoral? Although it was in the best interest of the company, should he take advantage of the fact that it would never be discovered?

The managers decided to solve the problem in a way that seemed to be both most profitable and the least troublesome for the company. In order to eliminate the possibility of losing the bidding, they decided to go with a lower bid (\$1.4 million) and not to disclose information that could hurt the deal and make employees less enthusiastic, and at the same time, more demanding about fulfilling the job.

When the foreign investors received the bid they could not believe it. It was nearly one hundred times lower than any other bid. The sense of surprise was soon replaced with joy. They never dreamed of having such a huge savings. This would allow them to make the Sea Star even more luxurious, and that meant making the ship even more attractive for top of the line tourists.

Their main concern was whether the bidding company that submitted the lowest bid could do the job of removing the asbestos. Soon they concluded that this should not be a problem. The employees were highly skilled. They had built many ships, and for them, removing asbestos, which was not a sophisticated job, was easy.

The investors did not spend much time discussing why the bid was so low. They knew that the salaries in the company were much lower than in similar companies in Western countries. Still, it was obvious that lower salaries could not explain such a low bid. Although it was apparent that the low bid must be related to lower safety measures, no one wanted to open the issue. Finally, this was not their problem. Everyone knew that many of the safety regulations in transitional economies were much lower than in Western countries, but that was not the investor's problem. This was the responsibility of the bidding company and they should address and solve this problem.

Even when the issue of the extremely low bid came to the table, the discussion focused on the issue of "cultural relativism" and that "no culture's ethics are better than any other's." Therefore, they cannot insist on implementing their own standards in other countries. If the people of the country are happy with their legislations, then it is not a problem for the investors. The management of the shipyard knew much more about what is socially acceptable and what is in accordance with the country's laws. One of the investors even recommended to his colleagues, "When in Rome, do as the Romans do."

When someone mentioned that the shipyard may be taking full advantage of the fact that the country was unable to effectively enforce the existing laws, which were also out-of-date regarding asbestos, the other colleagues disagreed. The course of the discussion was not changed even when one of the investors insisted that although the country has the right to establish its own health and safety regulations, the investors are responsible for the well-being of the workers working on the Sea Star.

After a short discussion, the contract was given to the lowest bidder.

It is still unclear whether the managers of the shipyard were fully aware of the consequences of their decision. To what extent could the short-term profit undermine the very existence of the company in the future? They did not spend too much time establishing a proper balance between pursuing their company's best interest (being the owners of the company, the real question is to what extent was this about the top managers' best interest) and the bounds of what society will tolerate – not only now, but also in the very near future?

Have the foreign investors found themselves in a similar situation – an ethical dilemma – as the shipyard's management? Or do they have completely different responsibilities?