Case Study: When the Golden Rule Yields No Gold[1]

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ABSTRACT: Zach Jordan (a real person but not his real name), the owner of a small business in Connecticut, may not be able to compete any longer in the spring manufacturing industry. Overseas competition has put him at a significant cost disadvantage, and the losses continue to mount year after year. At the same time, he's deeply committed to care for his handful of employees — people who are dependent on him and who he considers "family." Now at a crossroads, he faces an apparent dilemma: (1) gamble $200,000 on rent to extend the jobs of his employee family or (2) liquidate the business while it's still worth something, sending his employees to the unemployment line during a bad economy. There may be other, more attractive options and identifying them and selecting from among them is largely what this case is about. Framed from a Christian worldview, the case comes down to this: In an intensely competitive environment, how can we faithfully serve employee needs while effectively stewarding the business?

THE CASE

Zach Jordan sat at his desk seeking the high road. It had been his approach from day one. Now, though, on day 10,001, that road was obscure. Or perhaps this time there were two or three high roads.

Metaphors aside, this much was apparent: If he sold his ailing company, several people — good people whom he had embraced as family over the years — would lose their jobs in a bad economy. But if he didn't sell and if business didn't improve, he could lose hundreds of thousands of dollars in rent.

He looked at the pictures adorning the walls, pictures of his three girls, pictures of his employees, a photo of him doing his magic act (Zach's favorite hobby) for mesmerized school children. Zach had a zest for life and an authentic love for everyone around him.

Throughout his career, his priorities made that abundantly clear. Zach had often worked from home during his 30s and 40s, sacrificing business growth so that he could help raise his girls. He had adopted a "Golden Rule" approach to management, paternalistically caring for his employees' needs, maintaining integrity in every deal, insisting on quality, respect, and timely delivery for every customer, treating all of his stakeholders as he would want to be treated.

The fruit of that management style was a fiercely loyal workforce — hardly any turnover in twenty years of business — as well as an equally loyal customer base. One of Zach's eleven employees summed it up well: "Zach's the glue that holds everything together around here. And he's a great boss, too. He treats us better than anyone's ever treated us in our other jobs. I'll give you an example: In good times and in bad, he's always given a big Christmas bonus. One time he even had to borrow the money to do it!"

There was financial fruit as well — lots of profit, at least through the first ten years. His New England Spring Company (NES) in Connecticut earned a great return throughout the 1980s. But international competition and a sputtering economy began to take their toll, and in the 1990s, many of Zach's customers began to import their springs, primarily from manufacturers in Asia whose costs were a fraction of Zach's. Profit evaporated and eventually turned to losses. The past five years had been particularly difficult, almost all of which culminated in red ink (see Exhibit 1 for NES financial information).

As he wiped some dust from the photo of the NES family celebrating an employee's birthday (Zach commemorated every employee birthday with a card and a $30 check), in walked his two invited guests for the day. Steve, his accountant and longtime friend, and Charles, a professor (now emeritus), from Zach's business school days. This was a bittersweet occasion. Zach embraced each but then had to share with the professor his reason for the invitation: He needed advice about whether to sell his beloved company.

Zach closed the door. "Thanks so much for coming, you guys. I really appreciate your willingness to give me some candid advice."

His expression turned somber, as did his tone. Zach looked squarely at the septuagenarian professor and repented: "Charles, this place is bleeding, and it has been for years. I'm seriously thinking about getting out rather than signing off on another two-year, $200,000 lease for the building. Steve tells me I can get at least $750,000 for the customers, the inventory, the receivables, and the equipment, but the problem is this: with my financials, nobody is going to buy the business itself. So if I sell, it has to be by parceling it off. But then NES won't exist anymore and my people would lose their jobs. And in this economy, they're not going to find jobs anytime soon, certainly not much beyond minimum wage. I could take a chance and try to keep it afloat, but I'm on the verge of losing my biggest account to India – twenty percent of my business! If that happens, I probably couldn't survive more than two months, and the selling price of the business would drop a whole lot more. But even if I keep this account, there's no guarantee that things are going to turn around. I just can't compete with Asia's dollar-an-hour labor."

That was a lot of information in sixty seconds, but Charles zeroed in on what he considered a critical issue. "What's the chance of losing that account?"

"Probably about 50/50 next year," Zach replied. "Maybe even 60/40. India's come out with a stainless steel spring that weighs fifty percent more than ours — much better quality — for the same price, and my customer is genuinely considering making the switch."

"And can you get back the lease money if the business fails?"

"No. I'm on the hook for that regardless," Zach sighed.

"I've told you this before, pal," his accountant gently offered. "You've gotta get out. Either that or cut your seven-figure salary."

Zach smiled at the welcome levity — and the irony. Two years ago he had cut his own pay to $31,000, less than what some of his employees were earning.

"Funny you should mention that," Zach returned with a grin. "The SEC is stopping by this afternoon. I thought I'd give 'em your card."

"Remind me, my friend," Charles interjected with a chuckle, "what your product line looks like. And tell me how you've been pursuing new business lately."

"We manufacture and sell several types of springs," Zach began, "everything from specialty stainless steel springs to springs for navy jets and helicopters to common springs you'd find in a hardware store. And over the years, I've tried to grow the business through a combination of in-house sales reps and advertising in the standard industry newspapers, both in print and on the web. Quite frankly, though, it's been years since either approach has paid off, so I've recently dropped them. Bids are so tight that a sales rep's five percent commission required me to bid at my cost to remain competitive. I was taking jobs just to cover overhead! And the hundred grand I dropped in advertising over the past decade has returned almost no business. So basically, I'm left with no sales force and essentially no advertising."

"Sounds like you could use some fresh ideas," the professor observed thoughtfully. He was often brilliant, Zach thought, but now he was simply stating the obvious.

"That would be nice." Zach was eager for a few hot tips from the good doctor, but he knew those were probably a few days off. "And there might actually be some new business out there. But my 'fresh idea' file is freshly depleted. I've also thought about re-tooling as an option — you know, create other products that might have a niche — but I'd need about a quarter-million for equipment, even used equipment, and I have no customer list for whatever that new product would be."

"Let me give the marketing piece some thought," Charles replied with characteristic circumspection. "But in the meantime, tell me just how bad things are financially. Do you have some income statements handy?"

Zach buzzed his secretary. "Mandy, can you please bring me the binder of financials?" Mandy, as always, responded promptly, smiling at the gentlemen on her way out. As she closed the door, Zach shared with his guests that Mandy, his secretary for twenty years, was recently

Exhibit 1: Financial Information

New England Spring Company
Income Statements ($ in thousands)

		Year Ended December 31,			
	2012	2011	2010	2009	2008
Sales	$ 1,211	$ 1,282	$1,256	$1,294	$1,308
Cost of Sales					
Materials	403	396	375	349	353
Production wages	390	375	362	395	399
Overhead & other	51	135	65	49	84
Total Cost of Sales	844	906	802	793	836
Gross Margin	367	376	454	501	472
Operating Expenses					
Rent	100	100	100	100	100
Executive & admin salaries	66	98	145	152	168
Employee benefits	63	59	52	49	44
Office & supplies	32	42	38	42	31
Utilities & phone	52	57	54	51	49
Depreciation	46	46	46	58	61
Other & miscellaneous	22	18	26	47	26
Total Operating Expenses	381	420	461	499	479
NET INCOME (LOSS)	$ (14)	$ (44)	$ (7)	$ 2	$ (7)

New England Spring Company
Balance Sheets ($ in thousands)

			Year Ended December 31,		
Assets	2012	2011	2010	2009	2008
Current assets					
Cash	$ 98	$ 142	$ 121	$ 92	$ 119
Accounts receivable	22	19	27	38	41
Inventories	98	106	89	95	42
Other	3	6	4	9	12
Total current assets	221	273	241	234	214
Fixed assets (net of depreciation)	382	416	462	508	566
TOTAL ASSETS	$ 603	$ 689	$ 703	$ 742	$ 780
Liabilities & Equity					
Current liabilities	$ 284	$ 356	$ 326	$ 294	$ 314
Long-term debt	-	-	-	64	84
Common stock	300	300	300	300	300
Retained earnings	19	33	77	84	82
TOTAL LIABILITIES & EQUITY	$ 603	$ 689	$ 703	$ 742	$ 780

widowed, having psychological problems from the loss and in critical need of the health insurance benefits he provides. "My other office gal," he explained, shaking his head, "has a disabled husband and is the sole support for a family of five. And the guy who runs the plant has four kids, two of them getting ready for college. If he lost his job at age fifty, I don't know what he'd do."

The professor nodded; the accountant flipped pages in the binder. "It's not terrible," Steve said as he opened the books for Charles, "but it's not sustainable either. We've been losing money for years. Costs are inching up, mostly because of health care, workers' comp, and raw material prices. Salaries are exactly at market — anywhere from $10 to $26 an hour. But we've cut everything else to the bare bones. And as far as sales goes, we've been flat for a long time, and we have no expectation for new sources of revenue."

Charles adjusted his glasses as he reviewed the statements. His grimace told Zach that there was no quick fix forthcoming.

"I'm telling ya, Zach, cut and run," Steve recommended, preempting the professor's analysis. "I know you care about these people, but they're big boys and girls now. They can take care of themselves. Believe me, they'll be fine."

Zach didn't know whether to be irritated at or grateful for the counsel. Maybe Steve's was the only rational response, but Steve was also ignoring the fact that Zach didn't want to sell out his employees. Irritation trumped gratitude for the moment.

"Would you be 'fine' if your income were cut in half and if you lost your health insurance?" Zach retorted softly but firmly. "Would your family be 'fine'? I know you're looking out for me, Steve, but I simply can't operate that way."

"All right," his accountant back-peddled with a shrug. "So spend $175,000 to give them six months' severance. And spend another twenty-five grand to maintain their health benefits. Will that help you to sleep at night?"

Zach pondered the idea, but it seemed a bit excessive. "I'm getting too old for this kind of stress," he said leaning back in his chair and rubbing his eyes. "I'm 62 now Charles, which I know sounds like a spring chicken to you. But the spring business is taking all the spring out of this spring chicken."

Deep down, Zach desperately wanted his company to bounce back. But that seemed unlikely without some bold new strategy. And he wasn't sure he had either the energy to pursue it or the gumption to roll the dice on another $200,000 lease. "Cut and run" seemed like a logical course of action, but what about his people? This "Golden Rule" spring manufacturer recoiled at the thought of repaying their loyalty with a trip to the unemployment line.

SUGGESTED TEACHING APPROACHES AND DISCUSSION QUESTIONS

For What Course and at What Level?

The case is not complicated to understand and requires only modest prerequisite business knowledge to address intelligently; however, because of the strategy issues involved, it may best fit upper-level undergraduate and introductory graduate courses in management, marketing, entrepreneurship, and business ethics, among others.

The lead author has used the case primarily with second-year, undergraduate business students as well as for a case competition among MBA and EMBA students, with the actual protagonist ("Zach") offering prize money for the best ideas. So it's a reasonably versatile case. It can encourage students at several levels to think strategically about a turnaround situation, while never losing sight of what's entailed by a "Christian worldview."

Teaching Plan

Group work (10 minutes)

There are many ways to teach this case. The method typically used by the lead author is to have students talk through their proposed solutions (in groups of four to six) for 10 minutes before having a plenary, instructor-led discussion. The group work gives the students some practice presenting their ideas before being tapped to share their ideas with the entire class. It enables brainstorming and instills some confidence in the students, often leading to more and richer participation later in the class period.

Initial Ideas (10 Minutes)

For the plenary discussion, this is a good case for facilitator to take a Socratic approach, beginning with a broad question and later funneling down to related but more specific questions. Posing the case question to one of the mid-level students works well to get things started ("mid-level" since a top student may solve the whole thing from the outset, precluding the opportunity for other students to wrestle and to discover). "What should Zach do?" is the opener. "Roll the dice on another 200,000 bucks or wave the white flag?"

This framing allows the facilitator to get some initial solutions on the board without being too intimidating. After all, each of the students was asked to prepare this very case question. Inviting a few more students to respond to and build on the first student's ideas will develop these ideas further, giving the facilitator more to work with (and keeping the class on its toes, if the facilitator is cold calling).

After about ten minutes, the discussion may profitably be organized and clarified. One approach is to organize the ideas thus far into those that point toward selling the business and those that point toward developing a turnaround strategy (the facilitator should probably do this inconspicuously when chronicling the ideas on the board. Scribe the ideas on separate boards as students offer them, but do not yet label the boards as "sell it" or "keep it"). It may even be worthwhile at this point to take an informal poll once the two sets of ideas are formally labeled. That permits the facilitator to see where the class stands and it creates some public commitment, which often encourages further participation.

Digging Deeper (20 to 25 minutes)

The facilitator can then begin to explore with the "sell it" group what Zach should do for his now-jobless employees. It's usually a wise move to insist that the students respond in the first person rather than in the third — *what I would do if I were Zach*. In that way, they own the response and they must integrate their personal values (dealing with such issues in the third person seldom inspires this level of introspection). At this point the case is primarily an ethics and HRM case, but this is also an appropriate place to interpret the condensed financial statements in Exhibit 1. They paint a pretty grim picture and may seem to support this "sell-it" approach.

Here are some of the highlights:

- During the past five years, sales have remained steady between \$1.2 and \$1.3 million. Stagnant sales are often a sign of an unhealthy company.
- Gross margin as a percentage of sales is a significant and useful tool for evaluating a company's financial health. This represents the portion of each dollar of sales remaining after paying for the cost of manufacturing the springs. It is troubling that gross margin has declined from 36.1 percent (\$472/\$1,308) in 2008 to 30.3 percent (\$367/\$1,211) in 2012.
- In general, declining gross margins may be caused by declining sales prices, increasing costs, or a combination of the two. It is quite likely that both are factors here. Note that a significant part of the cost of sales consists of salaries and wages paid to production employees, which is a root of Zach Jordan's dilemma.
- Operating expenses have been cut from \$479,000 in 2008 to \$381,000 in 2012 to avoid major losses. But most of this comes from cutting the owner's salary.

This synopsis of the financials also provides a natural transition point for the discussion. The facilitator can now turn to the "keep it" group with a provocative devil's-advocate question like: *So, are you insane?* This is hopeless, isn't it? Why throw good money after bad, especially with your top customer about to bolt?

Many of these students usually step up to the implicit challenge (since a few minutes ago they put themselves on record as being part of the "keep it" group), and the class can become quite engaging, even animated. Facilitation is relatively easy at this point as the idea-generation process accelerates. However, a good facilitator will insist on *specificity* here, as well as a defense of the assumptions underlying each proposed solution.

At this point, it becomes more of a marketing and strategy case. Some typical student proposals, along with some proposed follow-up queries from the facilitator, are: tap into new revenue streams (Which ones? Do any viable options really exist?), outsource production/move the business (To where? And what about your employees?), invest in more advertising (though this hasn't really worked in the past), form a strategic partnership with a company that sells a complementary product (Such as?), hire a sales manager whose performance more than pays for himself (Not a bad idea, but where will you find the money?), insist on a more flexible lease (How will you persuade the landlord?), visit that major customer who's about to walk away and do whatever it takes to keep it (What can you offer that India cannot? Quality? On-time delivery?), cut a couple employees (Does that comport with your Christian values? And how does that help in the long run?).

Decision and Facilitator's Summary (10 to 15 minutes)

There is a plethora of alternatives for Zach, and fleshing them out is where much of the learning takes place in this case — provided the facilitator makes sense of it all. Creating a laundry list of options is obviously not the objective. Neglecting to sift the now-crowded blackboard will simply relativize the proposed solutions and possibly frustrate the students.

It's here that a good facilitator takes center stage for five to ten minutes to identify the most promising options (or, if there's time, to ask the students to do so — or if this is a longer class, to send the students back to their discussion groups with this task) and to communicate whatever major takeaways that he or she wants to emphasize.

This note is not intended to be prescriptive about what those are. Connecting the dots to what the students have learned thus far in the course and the curriculum is always a good idea. But one takeaway in a Christian college environment should probably be genuine faith integration. For example, the facilitator may want to raise the most basic of Christian worldview questions: "What do you think Jesus might do if he were in Zach's position?"

This is not intended as a "gotcha" question, simply a lucid, cut-to-the-chase framing of Christian-based decision-making. Such a question models for the students what we'd like them to ask habitually for themselves after graduation. The more clearly we can see Jesus's likely response, the more we may pattern our own response after His. Accordingly, this is a valuable place to linger and to land, gently inviting students to explain their Christology.

As is typical in a Christian business program, we are not necessarily looking for the "one right answer" to this question, but instead, cogent answers that flow from faithfully seeking God's will.

ENDNOTE

1 This case is based on a true story, but the company name and the character names have been changed.