



Journal of  
Case Research  
and Inquiry

Case, Notes and Articles

A publication of the Western  
Casewriters Association

Vol. 5  
December 2019

# *Journal of Case Research and Inquiry*

A publication of the Western Casewriters Association  
Published online at [www.jcri.org](http://www.jcri.org)

**ISSN 2377-7389 (online)**

The cases, notes, and articles included herein, and their respective accompanying instructors' manuals, were anonymously peer reviewed and accepted by the *Journal of Case Research and Inquiry*, Vol. 5, 2019.

Individual cases, notes, and articles in this volume are copyrighted by their authors. The authors and the *Journal of Case Research and Inquiry* grant state and nonprofit institutions the right to access and reproduce this manuscript for educational purposes. For all other purposes, all rights are reserved to the authors.

For membership in the Western Casewriters Association, visit [www.westerncasewriters.org](http://www.westerncasewriters.org)

#### Editors

Stephen J.J. McGuire, California State University, Los Angeles  
and  
Deborah Walker, Fort Lewis College

#### Guest Editors – Special Issue with Short Cases from Developing Countries

Julia Ivy, Northeastern University  
and  
Monika L. Hudson, University of San Francisco

#### *Journal of Case Research and Inquiry*

California State University, Los Angeles  
5151 State University Drive, STF 709  
Los Angeles, CA 90032 U.S.A.

Please send all Inquiries and Submissions to:

[editor@jcri.org](mailto:editor@jcri.org)

Qualified instructors will be provided with peer-reviewed instructor's manuals for each case. To request an instructor's manual, please complete the request form at [www.jcri.org](http://www.jcri.org), or write to one of the editors of the journal.



## **Western Casewriters Association**

The Western Casewriters Association (WCA) is the Western regional association of business casewriters. Its purpose is to train, develop and support business case writing for research and pedagogical purposes. WCA organizes an annual conference for experienced and new case-writers and academics using cases for teaching, and publishes the *Journal of Case Research and Inquiry*. [www.westerncasewriters.org](http://www.westerncasewriters.org)

### ***JCRI Editorial Board Members and Reviewers***

**Jyoti Bachani**, Saint Mary's College of California, [jb19@stmarys-ca.edu](mailto:jb19@stmarys-ca.edu)

**Mark A. Clark**, American University, [mark.clark@american.edu](mailto:mark.clark@american.edu)

**Ellen A. Drost**, California State University, Los Angeles, [edrost@exchange.calstatela.edu](mailto:edrost@exchange.calstatela.edu)

**Michael Germano**, California State University, Los Angeles, [mgerman@calstatela.edu](mailto:mgerman@calstatela.edu)

**Issam Ghazzawi**, University of La Verne, [ighazzawi@laverne.edu](mailto:ighazzawi@laverne.edu)

**Linda K. Gibson**, Pacific Lutheran University, [gibsonlk@plu.edu](mailto:gibsonlk@plu.edu)

**Armand Gilinsky**, Sonoma State University, [armand.gilinsky@sonoma.edu](mailto:armand.gilinsky@sonoma.edu)

**Leslie Goldgehn**, University of San Francisco, [goldgehn@usfca.edu](mailto:goldgehn@usfca.edu)

**Duane Helleloid**, University of North Dakota, [duane.helleloid@und.edu](mailto:duane.helleloid@und.edu)

**Anne T. Lawrence**, San José State University, [anne.lawrence@sjsu.edu](mailto:anne.lawrence@sjsu.edu)

**Teresa Martinelli**, University of La Verne, [tmartinelli-lee@laverne.edu](mailto:tmartinelli-lee@laverne.edu)

**Steve McGuire**, California State University, Los Angeles, [steve@mcguire.net](mailto:steve@mcguire.net)

**Vijaya Narapareddy**, University of Denver, [vnarapar@du.edu](mailto:vnarapar@du.edu)

**Nina O'Brien**, California State University, Los Angeles, [nobrien@calstatela.edu](mailto:nobrien@calstatela.edu)

**Marie Palladini**, California State University, Dominguez Hills, [mpalladini@csudh.edu](mailto:mpalladini@csudh.edu)

**Keith Sakuda**, University of Hawaii, [ksakuda@hawaii.edu](mailto:ksakuda@hawaii.edu)

**Jeff Shay**, Washington and Lee University, [shayj@wlu.edu](mailto:shayj@wlu.edu)

**James Spee**, University of Redlands, [james.spee@redlands.edu](mailto:james.spee@redlands.edu)

**Michael Valdez**, Fort Lewis College, [mevaldez@fortlewis.edu](mailto:mevaldez@fortlewis.edu)

**Deborah Walker**, Fort Lewis College, [walker\\_d@fortlewis.edu](mailto:walker_d@fortlewis.edu)

**George L. Whaley**, San José State University, [george.whaley@sjsu.edu](mailto:george.whaley@sjsu.edu)

**Yang Zhang**, University of Texas at El Paso, [yzhang9@miners.utep.edu](mailto:yzhang9@miners.utep.edu)

### ***JCRI Webmaster***

**Ludwig Slusky**, California State University, Los Angeles, [lslusky@calstatela.edu](mailto:lslusky@calstatela.edu)

## JCRI Editorial Policy

### ***Aim and goals***

The *Journal of Case Research and Inquiry* (JCRI) is a publication of the Western Casewriters Association ([www.westerncasewriters.org](http://www.westerncasewriters.org)). The *Journal of Case Research and Inquiry* publishes peer-reviewed teaching case studies (cases) prepared from primary and secondary research, as well as pedagogical notes and scholarly articles concerned with case research and teaching with cases. The journal publishes one issue per year, and if submissions so merit, may publish additional issues with editorial board approval. Cases, notes, and articles published in the journal are available online, full text, and free of charge at [www.jcri.org](http://www.jcri.org).

### ***Scope***

The journal publishes cases that address significant contemporary and perennial issues faced by organizations and managers in the areas of business and public administration, nonprofit management, social entrepreneurship, and public policy. All cases are necessarily accompanied by instructor manuals (IMs) that are not published but may be provided to the instructors upon request. All cases and IMs are double blind peer-reviewed by at least two reviewers. Cases may be derived from primary field research, secondary research, or a combination of both. JCRI does not accept fictional cases, nor cases, notes, or articles previously published elsewhere. Case authors are required to obtain release forms, when necessary, from the organizations studied.

Pedagogical notes that accompany a given case may also be published; notes may be summaries of industry characteristics and trends, or theoretical or legal analyses useful in the understanding of a case. All notes are blind peer-reviewed by at least two reviewers.

Finally, the journal publishes scholarly articles addressing significant issues related to case research, case writing, and teaching with cases. All articles are blind peer-reviewed by at least two reviewers.

### ***JCRI open source availability policy***

Cases, notes, and articles are available online at [www.jcri.org](http://www.jcri.org) at no cost to instructors and students at state and nonprofit educational institutions, who shall be granted the right to reproduce them for educational purposes. The journal shall encourage instructors to include in their course syllabi links to the JCRI website so that students can easily access cases, notes, and articles. For reproductions for commercial purposes in textbooks or elsewhere, authors shall retain all rights.

### ***Submission of manuscripts***

Authors should submit manuscripts electronically to [editor@jcri.org](mailto:editor@jcri.org). All submissions must follow the JCRI submission guidelines available in detail at [www.jcri.org](http://www.jcri.org). The minimum requirements for submission shall be:

When submitting manuscripts, authors should submit two WORD files, attached to a single email to [editor@jcri.org](mailto:editor@jcri.org). Each file sent to the journal should be saved with a name that clearly identifies the manuscript short title, type of manuscript, and date. At no place in any document except the Submission Form should authors be identified.

The first WORD file should contain the SUBMISSION FORM and the CASE SYNOPSIS (for cases) or ABSTRACT (for notes or articles). (See submission guidelines). This document contains the information required for contacting the author(s). It is used only by the editor and authorship is not revealed to reviewers. Please do not send PDF files to the journal.

The second WORD file should contain the CASE and INSTRUCTOR'S MANUAL (IM) for cases, or the NOTE or ARTICLE. (See submission guidelines).

In all documents submitted, use a size 12 Calibri font, 1 ½ spaced for text. Use a size 10 Calibri font, single spaced, for Exhibits, Tables, Appendices, Footnotes, Endnotes, Financial Statements, and References. Leave a one-inch margin on the top, bottom, and sides of all pages. Align text with the left except for major titles, and do not "justify" the text. Number (starting with 1) all pages of each document. Do not submit more than two files. Include any charts, graphs, figures, images, or photographs in the manuscript in the approximate place where it should be included. While IMs, notes, and articles may be written in the present tense, by convention all cases should be written in the past tense (e.g., "In 2019, Widgets-R-Us was the global leader in widget manufacturing.")

JCRI is an online publication. Case authors are encouraged to include photos, maps, links to websites, embedded videos and other features that take advantage of the internet.

#### ***Review policy***

At the editor's discretion, a submission to the journal may be rejected without a full review, particularly if the manuscript does not align well with the aim and scope of the journal.

Otherwise, all submissions shall be blind peer reviewed by at least two qualified reviewers. Authors shall receive the two reviewer's comments, together with a decision (reject, revise and re-submit, accept) by the editor. Unless approved by the editorial board, no cases or papers shall be invited and none published without undergoing the peer review process.

#### ***WCA Membership requirement for authors***

There shall be no fees to publish in the journal, however the policy of the journal is that at least one author must be a WCA member for the year in which the case is published. To join WCA, please visit [www.westerncasewriters.org](http://www.westerncasewriters.org)

#### ***WCA conference cases***

Authors of cases presented at the WCA conference will be invited and encouraged to submit their work to the journal. However, all submissions (whether presented at a NACRA, WCA, or other conference) will undergo the peer review process. No paper - even a WCA award-winning case - shall be guaranteed publication in the journal.

#### ***Content of the journal***

Published manuscripts may include CASE STUDIES, NOTES, and ARTICLES, which will be duly identified in different parts of the journal

- ***Case studies*** - The main part of the journal shall contain peer reviewed teaching case studies (cases) by authors who conducted primary research, secondary research, or a combination of both. Cases shall be about real organizations or managers facing issues in business administration, public administration, nonprofit management, or social entrepreneurship.

Cases must be submitted together with complete instructor manuals (IMs). IMs shall not be published in the journal, but shall be peer reviewed together with the case.

- **Notes and exercises** - A second part of the journal shall contain peer reviewed Notes, which can be summaries of literature, theory, or industry descriptions designed to be assigned to students together with cases. Peer reviewed Exercises may be short case-like assignments that provide less context about the organization and its environment than do cases studies but permit some of the learning associated with the case method.
- **Articles** - A third part of the journal may contain peer reviewed scholarly articles that address issues related to case research, teaching with cases, publishing case studies, and other topics related to case research.

### ***Release forms***

The journal shall require signed release forms from organizations, which must be collected by case authors for any case to be published that was carried out using primary research. The journal shall not publish a case based on primary research without a signed release form.

### ***Ownership and distribution of Instructor Manuals***

Instructor manuals (IMs) shall be archived by the journal for a period of at least three years after publication of a given case. IMs will only be provided to educators who so request them when such instructors are formally affiliated with a College or University.

No fees shall be charged to instructors who receive IMs, nor is membership in the WCA required to receive an IM. Educators seeking an IM should complete a request form on the JCRI website. IMs will then be sent by the journal editor to the requesting instructor with a cc to the case author, who may wish to know who is using his or her case and for what purpose. After the three-year period, inquiries for IMs should be made directly to the case author.



## JCRI Publication Ethics Policy

Approved by the JCRI Editorial Board, March 9, 2017

1. **Board Accountability.** The JCRI Editorial Board shall be responsible for establishing and updating, as needed, the Publication Ethics Policy of the *Journal of Case Research and Inquiry*.
2. **Editor Responsibilities.** The JCRI Editor shall be responsible for the content of the cases, notes, articles, and letters published in the journal. In consultation with the Editorial Board, the Editor shall endeavor to ensure that the content of the journal meets the standards of quality expected by the Western Casewriters Association (WCA) through the application of the blind peer-review process. The Editor shall also be responsible for ensuring that any non-peer reviewed content of the journal is clearly identifiable.
3. **Records.** The JCRI Editor shall keep accurate records of submissions to the journal, reviews, revisions, acceptances, and all other pertinent information to be able to inform the Editorial Board and WCA members of the status of the journal. The Editor shall also maintain a list of qualified reviewers for the journal that is updated based on reviewers' performance (availability, quality of review, and timeliness).
4. **Continuous improvement.** The Editor shall strive for continuous improvement of the quality of the journal and the quality of the published cases, notes and articles in each issue. The Editor shall seek the advice and input of Editorial Board and WCA members on ways to improve the quality, appeal, and usefulness of the journal.
5. **Retractions and Corrections.** The JCRI Editor shall be responsible for the publication of retractions, corrections, or clarification as needed, and shall keep the Editorial Board aware of any issues that might necessitate a retraction, correction, clarification or apology.
6. **Volunteer Basis.** The JCRI Editor, Editorial Board members, and reviewers shall carry out their duties on a volunteer basis, and under no circumstances accept any payment for such duties. Under no circumstances shall potential authors be required to make any payments to the JCRI or its Editor, Editorial Board, or reviewers, nor shall any such payment be accepted.
7. **Quality of the Review Process.** The Editor, in consultation with Editorial Board, shall review and as needed update the journal's editorial policy and guidelines for reviewers in order to ensure that thorough and timely reviews are prepared. The Editor shall also endeavor to ensure that the reviewers selected are qualified to review the submissions sent to them. The Editor shall apply the same review policies, procedures, and standards to submissions by WCA members, JCRI Editorial Board members, and non-WCA members. In addition, the JCRI Editor shall encourage reviewers to comment on the originality of submissions and be attentive to redundant publications or plagiarism. JCRI shall not accept fictional cases, nor cases, notes, or articles previously published elsewhere.

8. **Decisions and Appeals.** Decisions to accept or reject cases, notes, and articles shall be based on each paper's importance, originality, clarity, and pedagogical relevance as well as adherence to the submission requirements provided at [www.jcri.org](http://www.jcri.org). Editorial decisions shall not be affected by the origins of the manuscript, including the institutional affiliation, nationality, ethnicity, political beliefs, race, gender, religion, or sexual orientation of authors. Authors whose submissions to JCRI have been rejected may appeal to the President of the Western Casewriters Association at [www.westerncasewriters.org](http://www.westerncasewriters.org).
9. **Support of the Scholarly Process.** As appropriate, the Editor shall provide information to authors, reviewers, and institutions in order to support recognition of scholarly contributions.
10. **Support for author rights.** As per JCRI editorial policy, authors shall maintain full ownership and copyright for all papers published in the journal, with all the associated rights and obligations.
11. **Case Release Permissions.** Authors of cases shall be required to reveal the sources of information (primary, secondary or both) and to obtain release forms, when necessary, from the organizations studied, prior to publication of cases. In particular, release forms shall be required when primary data have been used as source of information.





## **Table of Contents with Case Synopses**

**WESTERN CASEWRITERS ASSOCIATION**, p. 2

**JCRI EDITORIAL POLICY**, p. 3

**JCRI PUBLICATION ETHICS POLICY**, p. 6

**LETTER FROM THE EDITORS**, p. 14

**SPECIAL ISSUE GUEST EDITORS**, p. 15

### **Case Research – Special Issue Short Cases from Developing Countries**

**LOAIZA FAMILY VALUES**, p. 17

By Monika L. Hudson, Maria Del Pilar Gomez Vallejo and George L. Whaley

This descriptive short case focuses on the entrepreneurial career of Omar Loaiza, the retired owner of the Loaiza Family Holding Company. Omar presented his story in a university entrepreneurship class, discussing the cultural values that guided him and his family as they established various rural Colombian financial and transit companies. Omar described his ability to recast business obstacles as opportunities as he continued to move forward. Students are asked to critically appraise the personal characteristics required for entrepreneurial success and evaluate the impact of environmental circumstances on entrepreneurial behavior and development.

*Key words: Entrepreneurship, family business, Columbia, family values*

**KOREAN BOX: POPULARIZING KOREAN COSMETICS IN CHILE**, p. 24

By Chahhat Lakhwani, Shreshthi Mehta and Julia Ivy

Jorge Morales had been running a profitable premium cosmetic retailer called Makeup Box in Chile. He decided to open a new store called Korean Box, which would sell only a limited selection of high-end Korean beauty products. Morales was unsure how this new store should be positioned within a highly competitive beauty industry in Chile. Korean functional cosmetics, although highly effective, were not popular in Chile. Morales was concerned that customers might equate the high quality, premium products with lower quality, cheaply sold Chinese products. Morales needed to make a strategic decision whether to stick with a focused differentiation strategy and demonstrate the effectiveness of Korean functional cosmetics so that customers would pay a premium for them, or extend the product line and adopt a broad-market differentiation strategy.

*Key words: Entrepreneurship, cosmetics, Makeup Box, Chile, Korean cosmetics, retail, strategy*

**LIGHT UP THE WORLD: RIGHT PERSON? RIGHT PLACE? RIGHT TIME?** p. 36

By Sandra Malach and Robert Malach

Dave Irvine-Halliday, an electrical engineering professor from the University of Calgary, Canada, spent his 1997 sabbatical in Nepal where he completed a project at the Institute of Engineering, Tribhuvan University, Kathmandu, Nepal. He then embarked on a trek around the Annapurna Circuit, a popular trekking route in Nepal. During his trek, it became obvious to him that most rural villages lacked adequate lighting. He thought about the children's ability to read in their homes and schools. Dave concluded that there had to be some way to bring light to the villagers.

Upon returning to the University of Calgary, he plunged into what was referred to as *"a wee personally funded project"* which had little, if anything, to do with his 'real' research. Toward the end of 1998, this project resulted in a prototype lighting system for the third world. In 1999, Dave and his wife Jenny took the prototype system to Nepal to determine whether Dave had developed a feasible, technological solution to the global third world lighting problem. The local response was overwhelmingly positive. Dave and Jenny were 'blown away' by the villagers' excitement over the system.

Dave now had to decide whether to bring this technology to those living at the bottom of the pyramid. Should he start a social venture to light up the world? Was he the right person, in the right place, at the right time?

*Key words: Entrepreneur, social entrepreneur, Nepal, lighting, social entrepreneurship*

**SOFTWARE TEAM SIX: ORGANIZING FOR SOCIOCRACY**, p. 49

By Iva Petkova, Jenia Kojuharova, Stefan Ivanov and Stoicho Gotzev

Software Team Six (ST6) was a start-up software development consulting firm providing expert hands-on engineering and consulting services for a niche segment of the IT market in Bulgaria. ST6 was created by Kiril Gantchev, Ivo Bratoev, and Stefan Dobrev, all three having previous experience in software engineering within corporations. The trio adopted a flat organizational structure that consisted of circles instead of departments. Each Circle had its own domain, which included setting policies and practices and maintaining open documentation so everybody in the company could remain informed about what was happening in the circle. Any employee could join (or leave) any circle at any time, and all participants in the circle had equal decision-making power. This concept was called sociocracy.

At the first annual meeting, the team members were about to review the progress they had made so far, the successes they had had, and any actions needed to continue being successful. How had they done so far? Were they on the right path? Was the current structure sustainable in the future as the company grew and more employees were hired?

*Key words: Sociocracy, entrepreneurship, small business, Bulgaria, software*

***SWEET SUCCESS OR HEADACHE?*** p. 75

By Monika L. Hudson and Frank Ohara

This short case describes issues leading up to a decision for a relatively new Colombian business owner - should she continue to go it alone with just family support and a bank loan, or should she accept an equity cash infusion along with associated conditions? Students are asked to put themselves in the position of the business owner as she reviews the course of action she needs to take.

*Key words: Entrepreneur, bank loan, small business, family business, equity, Colombia*

***FONSELP: CREATING SHARED VALUE TO MAKE THE WORLD A BETTER PLACE***, p. 82

By Jacob A. Massoud and Vafa Saboori-Deilami

In April 2018, Matías Laurenz launched the Argentine social impact startup, Fonselp. Fonselp was a digital platform that connected nonprofit organizations with companies in Argentina and Latin America, enabling them to receive donations of almost anything. Matías hoped to target small and medium businesses using a freemium revenue model. The hope was that some companies would upgrade to a subscription service to track their corporate social responsibility (CSR) performance, such as volunteer hours, and generate CSR reports. At the time of launch, Fonselp was a first mover in Latin America; however, several established competitors existed in developed countries, such as the United States. As a startup in an unstable economic climate, Fonselp faced a number of challenges while Matías attempted to scale his business. After receiving a proposal from a consultant to help Fonselp boost its revenues, Matías had to consider his strategy moving forward. Should he accept the consultant's proposal, seek out investors or alternative startup financing, or modify his revenue model?

*Key words: Argentina, business model, social impact startup, business strategy, social entrepreneurship*

## Case Research

### ***PFADT RACE ENGINEERING: SUPPLY CHAIN ISSUES IMPACT THE VALUE CHAIN***, p. 95

By Richard T. Herko

Entrepreneurs face difficult decisions regarding the geographic placement of their new business. Should they place themselves physically close to their key suppliers or key customers? What happens when these are both geographically dispersed? Even in a just-in-time/internet-of-things economy, some bulky materials still need to travel the old fashioned way on boats, trains and trucks. Choosing to locate close to customers requires longer lead times for entrepreneurs and forces them to incur costs that may not be supported by shallow niches. The case describes Pfadt Race Engineering's options for growth and the different consequences on the firm's value chain.

*Key words: Entrepreneurship, engineering, supply chain, value chain, global business*

### ***RESUSCITATING 1-800-AUTOPSY: A LIFESPAN OF A DEATH CARE ENTERPRISE***, p. 110

By Stephen J.J. McGuire and Andre S. Avramchuk

A private-autopsy industry pioneer, Vidal Herrera of Los Angeles enjoyed high-profile media attention and the publicity that few entrepreneurs ever achieved. He sought to fill the market segment left by hospitals and coroners reducing the numbers of performed autopsies due to budget cuts and technology enhancements. Vidal knew that people needed closure by confirming their loved one's true cause of death.

Since the 1988 opening of his Autopsy / Post Services, Inc., also branded as 1-800-Autopsy, the for-profit, 24-hour mobile enterprise and its charismatic leader had been featured in press, onscreen, and online. From the award-winning CNN news, Dateline TV, and Prime Video to *The Economist* and *The Wall Street Journal* reports, the interest in his services seemed to be strong and broad over the years. Herrera earned a runner up status for a Marketer of the Year with *Inc.* magazine and, with advice from a business consultancy, tried to franchise his unique concept. Despite constant publicity, decades of reputable experience, Herrera's enterprise had yet to blossom to its envisioned potential. His attempts to sell a franchise had, as yet, no serious takers. What should he do to become a successful franchisor, and what else should the company do to grow its business?

*Key words: Autopsy, entrepreneurship, entrepreneur, franchise, franchising, medical malpractice*

**WAS THE KRAFT HEINZ MERGER A TAXABLE ACQUISITION OR A TAX-FREE REORGANIZATION?**

p. 137

By Gretchen Lawrie

In 2015, H.J. Heinz Holding Corporation (Heinz Holding) acquired Kraft Foods Group, Inc. (Kraft) for over \$52 billion. Together, the companies became the Kraft Heinz Company, the third largest food and beverage company in North America and the fifth largest in the world with a projected combined revenue of \$28 billion. The merger was carried out with a subsidiary of Heinz Holding first merging with and into Kraft, with Kraft surviving, which, in a second transaction, merged with and into another Heinz Holding subsidiary, with this subsidiary surviving as a wholly owned subsidiary of Heinz Holding. As part of the merger, Heinz Holding issued approximately 593 million new shares of its common stock valued at \$42.5 billion to Kraft shareholders in exchange for their Kraft stock. Also, Kraft shareholders received a special cash dividend of approximately \$10 billion. Following the merger, Kraft shareholders owned 49 percent and together, Heinz Holding's pre-Merger shareholders, Berkshire Hathaway, Inc. and 3G Capital, Inc., owned 51 percent of Heinz Holding, which was renamed the Kraft Heinz Company. The focus of this case study is on the U.S. tax and non-tax consequences of the merger for the Kraft, Heinz Holding, and their shareholders.

*Key words: Tax, mergers, Kraft Heinz Company, taxable stock and asset acquisitions, tax-deferred stock and asset acquisitions, tax-free reorganizations, tax planning*

**WAS THE ACQUISITION OF H.J. HEINZ COMPANY BY BERKSHIRE HATHAWAY & 3G CAPITAL A TAXABLE TRANSACTION?** p. 154

By Gretchen Lawrie

In 2013, the ketchup company known for the slogan "57 Varieties," the H.J. Heinz Company (Heinz) was a publicly traded Delaware company, headquartered in Pittsburgh, Pennsylvania. It manufactured ketchup, sauces, soups, beans, and pasta under various brand names, including Heinz, T.G.I. Friday's snacks, Plasmon infant nutrition, Lea & Perrins Worcestershire sauce, and Classico pasta sauce. Its profit in 2012 was over \$900 million on revenues of over \$11 billion and employed more than 30,000 people. In 2013, Heinz was acquired for over \$28 billion by an investment consortium comprised of Berkshire Hathaway, Inc. (Berkshire) and the global investment firm, 3G Capital Partners Ltd. (3G Capital) (Heinz Merger or Merger). After the Merger, Heinz became a subsidiary of a newly created company controlled by Berkshire and 3G Capital, the H.J. Heinz Holding Corporation (Heinz Holding). What were the U.S. tax and non-tax consequences of the Merger for Heinz, Heinz Holding, and their shareholders?

*Key words: Tax, acquisitions, Heinz, Berkshire Hathaway, 3G Capital, taxable stock and asset acquisitions*

**STRATEGY AND LEADERSHIP AT THE WINDOW SPECIALIST: CAN A TECH CEO DRAMATICALLY GROW A CONSTRUCTION FIRM?** p. 170

By George L. Whaley, Connie Allsopp and Keith C. Perry

The case focuses on the CEO's evolving leadership style at a 40-year-old construction firm, The Windows Specialists (TWS). CEO Keith Perry took over the company in 2014 and reincorporated it as a benefit corporation. Although the financial picture of TWS had improved each year since Perry took over, a series of events in May 2017 created strategic, leadership, and financial challenges. The firm's 2017 sales figures from January to May were low. Perry then received a letter stating that his contractor's license had been revoked. Although it turned out this was due to a typo, it could bankrupt the company if not addressed immediately. Perry wondered what strategic actions and leadership style changes would allow him to grow TWS and address internal and external challenges. Readers are asked to focus on strategy and leadership concepts and to make growth and sustainability recommendations for TWS.

*Key words: Construction, windows, benefit corporation, strategy, leadership, entrepreneurship*

**CIRQUE DU SOLEIL: INNOVATION IS MORE A CULTURAL MATTER THAN A PROCESS**, p. 201

By Issam Ghazzawi

Cirque du Soleil (French for Circus of the Sun) had evolved as one of the most famous live spectacles, as well as one of the most successful stories in the history of the entertainment industry. While Cirque du Soleil's various performances had transformed over the years, its traditional elements of imagination, artistic entertainment, spectacle, theatrical storytelling, visual extravaganza, and incredible physical skill had remained at the core of this entertainment giant.

With an estimated \$845 million in revenue in 2014, Cirque du Soleil expanded rapidly through the 1990s and 2000s, going from one show to 19 shows that were presented simultaneously in over 200 cities on five continents throughout the world. The company's various shows attracted close to 90 million spectators. The organizational culture, according to Cirque producers, was accepting of people and open to doing things in different ways. The working environment was good-natured, with a considerable freedom given to employees and artistic directors. The behavioral norms and values resulted in affirmation of family, or at the very least community. In addition to its world-renowned productions, Cirque had extended its creative approach to a variety of entertainment forms, including: multimedia productions, immersive experiences, theme parks, and special events.

In 2015, ninety percent of Cirque was acquired. The company's president and CEO, Daniel Lammare, and its founder and artistic director, Guy Laliberté, were revisiting the challenge of balancing the needs to maintain high creative standards while expanding to a larger audience and meeting its new partners' expectations of increased returns. Could the company remain loyal to its original values?

*Key words: Cirque Du Soleil, organizational culture, creativity, innovation, culture change, human-computer interaction (HCI), acquisition and culture, performing arts industry.*

## Letter from the Editors

This is the fifth issue of the *Journal of Case Research and Inquiry*. So far, **JCRI** has published 40 peer-reviewed teaching case studies prepared from primary and secondary research. Each case has been thoroughly peer-reviewed and is accompanied by a peer-reviewed instructor's manual that is available to qualified instructors upon request. The cases published in **JCRI** address diverse issues in business and society. They include studies of for-profit, nonprofit, and governmental organizations in several countries around the world. Instructors will find cases that focus on everything from entrepreneurship and small business management to decisions made in multi-national organizations. The journal has also published five peer-reviewed scholarly articles or notes concerned with case research and teaching with cases. Cases, notes, exercises, and articles published in the journal are available online, full text, and free of charge at [www.jcri.org](http://www.jcri.org). The editors are available to write to authors' tenure and promotion committees, upon request.

In the volume, we publish twelve new cases. Six correspond to the special issue with short cases in developing countries, and six are regular-length, detailed cases. Topics include ethics, tax law, entrepreneurship, social entrepreneurship, leadership, strategy, franchising, international business, and more. JCRI cases are ready for use in the classroom, and all have peer-reviewed instructor manuals to assist with their classroom use.

**JCRI** is the publication of the Western Casewriters Association (WCA). On the WCA website, <http://www.westerncasewriters.org/>, authors will find a call for cases for the next WCA conference to be held on March 9, 2020 in Hawaii. The WCA annual conference is a unique opportunity to engage with other casewriters in a small group format to exchange feedback and polish-up a case, learn about teaching with cases, and enjoy presentations from leading case authors and case educators. The WCA is held in association with the annual meeting of the Western Academy of Management.

We are grateful to our authors for their submission and especially grateful to our reviewers for their detailed, insightful comments on the case submissions this year. We look forward to receiving well-written cases, notes, and articles in 2020 and urge you to consider the journal for your case research.

Thank you,

Steve McGuire and Deborah Walker  
Editors, *Journal of Case Research and Inquiry*

## *Special Issue Guest Editors*

In this volume, the Special Guest Editors were Dr. Monika Hudson of the University of San Francisco and Dr. Julia Ivy of Northeastern University. The special issue includes six short cases from around the world: Argentina, Bulgaria, Chile, Nepal, and two from Colombia. All the cases are short, classroom ready, peer-reviewed, with an accompanying peer reviewed Instructor's Manual. The topics covered in the short cases were entrepreneurship and social entrepreneurship, small business and family business, in both low tech and high tech industries.

Sometimes a short case is the best choice. Students typically prefer them over long cases, and if engaging enough, students will actually read them.

Julia Ivy mentors her students as they craft consulting case studies – the case as a method of diagnosis and recommendations for action to companies and entrepreneurs. She is the author of the recent book *Crafting Your Edge for Today's Job Market: Using the BE-EDGE Method for Consulting Cases and Capstone Projects* (Emerald Group Publisher).

In 2018, Monika Hudson completed (with Tracy Cuoto of LeMoyne College) the IgnitED/Global Jesuit Case Series workshop in Cali, Colombia, which allowed her to generate two Colombian-based teaching cases among the ones contained in this issue. These instructional tools illustrate critical issues related to leveraging valuation as an element of business expansion decisions and more critically examining the individual leadership characteristics of entrepreneurs.

JCRI has always welcomed cases from around the world, and shall continue to endorse innovative approaches to case research and teaching with cases. We are grateful to Julia Ivy and Monika Hudson for their contributions to this special issue.



***Special Issue:***  
***Short Cases from Developing Countries***



## **LOAIZA FAMILY VALUES**

**MONIKA L. HUDSON**

University of San Francisco

**MARIA DEL PILAR GOMEZ VALLEJO**

Pontificia Javeriana University

**GEORGE L. WHALEY**

San José State University

Although he had several weeks to prepare before coming, Omar Loaiza was visibly nervous as he scanned the students' expectant faces in the introductory entrepreneurship class. The retired owner of the Loaiza Family Holding Company, Omar wondered how he could help the students understand what it was that had allowed him to overcome many of the obstacles he had experienced in his life. Should he begin by talking about working in the family's leather factory? Or with the theft of money that led to the creation of the Society of Friends cooperative? Omar worried there was no way he could properly convey whether his personal attributes, ingrained habit of viewing problems as opportunities, or his Colombian values were what had led him and his family to move forward under challenging circumstances to create the Loaiza Family Holding Company. He decided that, after sharing some of his life story, he would ask the students to assess the relative importance of these factors to his family's success.

### **A Rural Colombian Upbringing and Family Values**

Omar Loaiza, the oldest of nine children, was born in 1953 in rural Sonsón Antioquia, Colombia. His father initially ran a small candy factory out of the family's home but subsequently moved everyone to Madrid Cundinamarca, a little town 21 kilometers from Bogotá, Colombia, where

---

The authors developed the case for class discussion rather than to illustrate either effective or ineffective handling of the situation. The case and its accompanying instructor's manual were anonymously peer reviewed and accepted by the *Journal of Case Research and Inquiry*, Vol. 5, 2019, a publication of the Western Casewriters Association. The authors and the *Journal of Case Research and Inquiry* grant state and nonprofit institutions the right to access and reproduce this manuscript for educational purposes. For all other purposes, all rights are reserved to the authors. Copyright © 2019 by Monika L. Hudson, Maria Del Pilar Gomez Vallejo, and George L. Whaley. Contact: Monika L. Hudson, University of San Francisco, 2130 Fulton Street, San Francisco, CA 94117, [mhudson@usfca.edu](mailto:mhudson@usfca.edu)

he thought there might be more business opportunities (see Exhibit 1 for a map of Sonsón Antioquia, Colombia). Here, Omar's father established a leather goods factory, consisting of a sewing machine and 5-6 employees producing suitcases and briefcases. All of the family's children – no matter how young – helped with production. If the children's hands were too small for other tasks, they were given glue sticks to attach hardware to the leather materials.

### Exhibit 1. Map of Sonsón Antioquia, Colombia

Source: Wikipedia



As part of the class discussion, Omar talked about how the children sacrificed play to work in the factory. He indicated that learning how to defer gratification at such tender ages helped the family develop a strong work ethic, an interest in learning new things, and financial discipline, with a strong emphasis on working together. He pointed out that he and his younger brother Mario emerged as the family's business leaders, leveraging different skills. Mario had an engineering degree, liked to "think outside the box," and stressed risk-taking, problem-solving, and sharing. As the older brother, Omar indicated that he was the one with planning and implementing skills. He said he felt his self-direction and achievement orientation complimented his brother's creativity and openness to change and, as a result, he became the

family's key business decision-maker. Finally, Omar noted that the social commitment of the entire family assured that they reinvested in their community as their ventures grew.

As students questioned Omar about how he guided the various ventures to success during his formal career (as outlined in Exhibit 2), he reiterated that he felt moving forward was always a necessity, not a choice, and he knew he could always count on his family.

### Exhibit 2. Loaiza Family Key Events Timeline

Source: Authors' notes

Year	Key Company Events
1953	Omar Loaiza was born in Sonsón Antioquia, Colombia, the oldest of nine brothers and sisters.
1972	The Society of Friends was formed, using savings from the Loaiza family's manufacturing venture as well as savings from other community members, after the family's original savings were stolen.
1975	Madrid Transport Society Juan XXIII SOTRAM S.A was formed by Omar and his family together with fellow community car owners to provide public transportation in the rural areas where they lived.
1983	Industrial Division Ayicar S.A. was founded to manufacture the first bus to supplement the transportation services provided by the Madrid Transport Society Juan XXIII SOTRAM S.A.
2006	Fuel Service Station Sotram S.A. was established as a service station to supply fuel to the Transport Society's vehicles.
2006	The Intermunicipal Transport Terminal was created and used to purchase a parking lot to centralize Industrial Division Ayicar bus storage; purchase financing was provided by traditional bank loans.

### A Favorite Story

Omar decided to share one story from his experiences to demonstrate how he and his family began their transportation services in response to both a family and community need. He noted that *The Society of Friends* saving cooperative had hired a bus to take people to a party in the town of Madrid, about three hours from where they lived. They left their village early in the morning and arrived around 10:00 a.m. to help prepare for the event. However, at about 2:00 p.m., the bus driver told them: "*Listen, I'm leaving, because I have to be in Bogotá at 6:00*

*p.m. and I need to take you back and then get there."* Omar's dad got visibly upset and said: *"This is wrong, but we have to leave because otherwise we do not have any way to go home."*

As they returned to Sonsón Antioquia, the savings cooperative members decided, *"We must buy a van."* Omar replied: *"A bus, not a van. We're going to buy a bus."*

When they got back, cooperative members realized they actually did not have enough money to purchase a bus. However, after some thought and many conversations, Omar, his family and their friends decided that the best way to respond to this problem was to invite owners of private cars, that in many cases were old and dilapidated, to be part of a transit association. The new firm, which became SOTRAM, S.A., began transporting villagers to surrounding areas. Mario and Omar met with the owners of the vehicles (which were also called *"pirate"* cars) and said: *"Let's work together. You have cars, we also have some, then you can rent or lend us yours, whatever you want."* Omar pointed out that the creative characteristics his family and neighbors displayed in forming the transit operation was just one example of how the collective managed to *"turn lemons into lemonade."*

### **Formation of the Loaiza Family Holding Company**

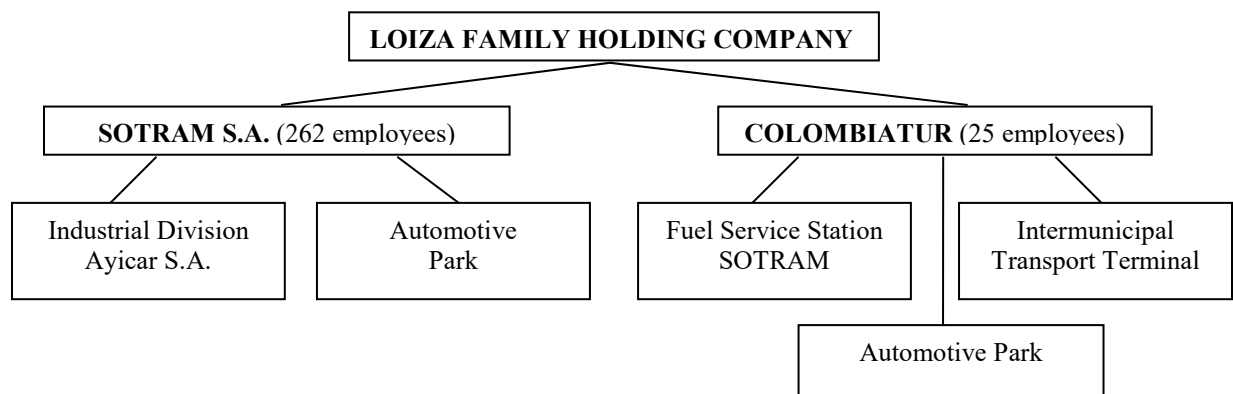
As their empire began, the family invested their leather factory earnings into *The Society of Friends* savings cooperative, which was formed after the family's savings had been stolen from a previous financial cooperative. Omar's father served as the family's investment adviser and their mother was the new cooperative's treasurer and secretary.

The various Loaiza businesses were created as the company continued to grow or when specific family members saw key community needs that were not being met. The resulting enterprises usually began informally, and business plans were not developed until there was a need for expansion financing, as was typical in this region of Colombia.

The *Society of Friends* savings cooperative ultimately became SOTRAM, S.A. From 1972 to 2006, the family used funds from SOTRAM for the subsequent development of a bus factory, two fuel service stations, a municipal and inter-municipal bus terminal, and a regional transportation business. Over the years, Omar reorganized each business unit into a consolidated holding company (see Exhibit 3).

### Exhibit 3. Relationship Among Loaiza Family Ventures

Source: Authors' notes



When the Bus Factory was developed in 1983, Omar inserted a new firm, Industrial División Ayicar inside SOTRAM, S.A, alongside the Automotive Park venture. When the Fuel Service Station SOTRAM was created in 2006, a new Automotive Park and the Intermunicipal Transport Terminal was developed, and all three ventures were organized inside a company that was renamed Colombiatur.

#### Exhibit 4. Omar Loaiza

Source: Omar Loaiza, A link to photos of SOTRAM can be found at [SOTRAM, SA](#).



### Conclusion

Students learned even though Omar and his family did not have well-developed business plans prior to moving forward with their enterprises, they never gave up! In his presentation, Omar discussed family values and behaviors from across his entire career that he felt helped turn what might have been problems into opportunities, resulting in the businesses shown in Exhibit 3.

In the end, he asked the students if they thought his personality, style and business behaviors matched those of successful entrepreneurs and entrepreneurial concepts they had learned in class. Specifically, he wondered aloud, was it something special about him, his family or the Colombian culture that made their ventures successful or could anyone do what he and his family had done?



#### **Monika L. Hudson**

is Associate Professor at the University of San Francisco and teaches entrepreneurship, organizational behavior and public administration. She directs USF's Gellert Family Business Center, which supports family firms in the SF Bay Area. Dr. Hudson's research interests include entrepreneurship, family-owned enterprises, identity and behavior and the strategic implementation of the same. Dr. Hudson received her undergraduate degrees from Northwestern University; her M.B.A. from USF; her doctor of management from Case Western Reserve University, Ohio; and her doctor of education from USF. A 2017-18 Fulbright Scholar, she conducts research in Colombia and other South American countries.



#### **Maria Del Pilar Gomez Vallejo**

is Assistant Professor at the Javeriana Cali University in Colombia and teaches entrepreneurship and entrepreneurial mindset. She led a joint Javeriana/Fordham University fair trade project that focused on Colombian artisans making handcrafts for sale in the U.S. Her research interests include entrepreneurship as well as entrepreneurial education, motivation, and skills development on both the graduate and undergraduate levels. Professor Gomez received her undergraduate degree in business administration from San Buenaventura University and her Master degree in education/human development from the same university. Her textbook, *La Mentalidad Emprendedora* (2018) is used in 14-16 undergraduate courses each semester at Javeriana University.



#### **George L. Whaley**

is Emeritus Professor of Human Resource Management at San José State University. Over the past twenty years, he has authored numerous case studies of companies in the high technology and biotechnology industries. Professor Whaley holds a B.S. in Engineering Mathematics and a M.B.A. from the University of Arizona and Ph.D. in Organizational Behavior from the University of Colorado. He has forty years of combined management, consulting and teaching experience, and serves on the editorial board of several academic journals. His research focuses on Strategic Human Resource Management, Sustainability, Leadership, Diversity and Entrepreneurship, and he teaches Organizational Behavior, Human Resource Management and Organizational Change.





## ***KOREAN BOX: POPULARIZING KOREAN COSMETICS IN CHILE***

**CHAHHAT LAKHWANI**

**SHRESHTHI MEHTA**

**JULIA IVY**

Northeastern University

In February 2018, Jorge Morales reviewed his business strategy. He owned Makeup Box, a store that sold beauty products from global suppliers in Chile. Morales was planning to set up a new store called Korean Box. Unlike Makeup Box, Korean Box would only deal in high-end functional cosmetics sourced from suppliers in South Korea. Functional cosmetics were proven to be more effective than general cosmetics. Hence, they were more expensive.

Functional cosmetics from South Korea were in high demand in Europe and North America but were not as popular in Chile. Morales was excited about introducing trendy Korean cosmetics to the beauty conscious Chilean population. At the same time he was anxious that the people would not purchase unrecognized but expensive Korean brands.

What could Morales do to portray the effectiveness of Korean functional cosmetics and make his business successful?

## A New Business Idea

Morales had studied business in the USA. After graduation, he established Health Foods in 2014 - a store that sold healthy food products in Chile. Happy with the success of Health Foods and having gained expertise in managing retail operations, Morales established Makeup Box in Iquique in April 2017.

While on a vacation in Spain, Morales noticed that the Korean wave (*hallyu*) had accounted for the global popularity of South Korea's culture, entertainment and music in Europe and other parts of the world. Even he was fond of Korean movies, songs and dance moves like the *Gangnam* style. Morales observed that these movies portrayed the beauty of the contemporary lives of people in South Korea, which thereby increased the popularity of Korean cosmetics in Europe and America.

Korean functional cosmetics were not widely seen in Chile. Having knowledge of the cosmetic industry, Morales felt that it was an opportunity that he could explore further. He conducted a feasibility study to determine if he could sell Korean cosmetics in Chile.

## Korean Functional Cosmetics

Korean beauty rituals and traditions were influenced by practices of the past. Korean women gave skincare and grooming a lot of importance since the earliest recorded times. Self-care manuals, makeup tools and other artefacts were present even during the 13<sup>th</sup> century in the ancient times of the Joseon dynasty (Arthur 2016). Ingredients such as yuja, bamboo and snail gel were used to manufacture Korean cosmetics. These materials were integral to the culture of South Korea, hence not found in traditional American or European cosmetics.

During his research, Morales noticed that cosmetics in South Korea were divided into two categories: general cosmetics and functional cosmetics. Functional cosmetics aided in the brightening of the skin or removing wrinkles. The focus was on making the skin or body beautiful naturally. In contrast, a general cosmetic product like lipstick would make the skin look beautiful only as long as the product was applied.

As per the South Korean Cosmetics Act, for functional cosmetics, both manufacturers and importers were required to undergo an evaluation on the safety and efficacy of cosmetics. Manufacturers of general cosmetics were subject to lesser sanctions (Reach 24H Consulting Group).

Due to the high costs associated with research and other regulations, functional cosmetics were more expensive (Shin & Park 2018). But the claims regarding the anti-aging properties of functional cosmetics guaranteed results making it a highly valued item.

### Social Trends Related to Beauty in Latin America

While setting up Makeup Box, Morales knew that the average Chilean citizen spent about USD \$168 annually on health and beauty products. According to *El Mercurio* (a Chilean newspaper), this was about 30% higher than that spent by the average Latin American consumer. Additional research revealed that the annual spending on health and beauty products by each person in Chile was expected to continue to grow by 2020 (Euromonitor).

Brazil was the fourth biggest market for beauty products in the world, after the United States, China, and Japan (Euromonitor). Although Americans and Europeans spent more on beauty products, the Latin American nations of Brazil, Argentina and Chile stood out among emerging markets as spenders on beauty.

South American nations regularly featured in the leading list of popular plastic surgery procedures. People were known to equate beauty with wealth. It was a cultural norm that physical beauty would reap social and economic rewards in the form of jobs or partners that valued appearance (Shilling 2003).

Latinos were very conscious of their physical appearance – which provided a great opportunity for cosmetic companies (de Casanova 2018). Morales thought that a cosmetic product with anti-aging properties had the ability to thrive in the Chilean market. He was excited and he started conducting research on how the cosmetics would be imported from South Korea.

### Selling Korean Beauty Products in Chile

In addition to obtaining approvals from the Korean government to import cosmetics, Morales also had to register the cosmetic products with the government of Chile. It cost USD \$1,000 to register a single product and required extensive paperwork. It was both a cumbersome and an expensive process. Morales was aware that many beauty stores in Chile were selling products illegally, without registering. By doing so, the distributors made high profits. Nonetheless, he felt that it was necessary to register the products he imported in order to minimize business risk. He would also be able to market the Korean cosmetics openly, reaching more people and encouraging them to make purchases. If the right marketing strategies were deployed, then Morales could generate more profits in the long run. This would be appropriate for the growth of his company.

Morales traveled to South Korea to attend trade shows and develop contracts. He noticed that most of the Korean suppliers had an agreement with a distributor, whereby the distributor would agree to a given sales target. If the sales target was not achieved, the distributor could lose sole distributorship rights or business with the supplier. On the other hand, some suppliers

preferred to work with several distributors. This helped the suppliers in selling products via more channels.

### The Chilean Economy

President-elect Sebastian Piñera took office in March 2018. It was perceived as unlikely that the President's policies would negatively affect the economy of Chile. Most expected a business-friendly environment for foreign imports and the continuation of a longstanding trade agreement between Chile and South Korea.

Chile and South Korea had a free trade agreement since 2004 and an additional supplementary trade agreement was signed in 2014. Tariffs on product imports were low. Morales was hopeful that the Chilean government would not impose additional tariffs on foreign imports to boost domestic businesses.

At the end of 2017, the unemployment rate in Chile stood at 6.8% and Consumer Confidence has reached its highest level since 2014 (Trading Economics 2018). Furthermore, Chileans saw their disposable income increase in 2016. The Consumer Purchasing Index had been increasing steadily since 2014. Since the increases in disposable income would be able to keep pace with the rising prices of commodities, Morales inferred that spending on cosmetics would only increase further.

### Perception of Korean Cosmetics

Morales continued his research. He observed that when products manufactured in developed countries were compared with similar products from emerging economies, consumers rated products manufactured in economically developed countries to be of higher quality. This demonstrated that the country of origin directly influenced a consumer's perception of product quality and purchase intention (Adina, Gabriela & Roxana-Denisa 2014). Following the Korean War in 1953, South Korea remained one of the poorest nations in the world. But, as of 2016, it had met the developed country criteria (Santacreu & Zhu 2018). The export-oriented policies of the country had contributed to its success.

Morales observed that South Korea had very recently become a developed country and the demand for K-beauty products was still growing in Chile. Hence, he was afraid that South Korean products would be perceived to be of inferior quality like those from other Asian countries. Morales wondered what product positioning strategies could be used to engage customers.

### Growth in the Popularity of K-beauty

As per Korean Customs, Korean cosmetics exports to China had reached USD \$151 million in January 2018. This number was up by USD \$81 million as compared to January 2017. This showed that despite the geopolitical tensions between China and South Korea, Korean cosmetics were a huge hit in China. The Chinese believed that Korean beauty products offered value for money.

KOTRA (Korea Trade-Investment Promotion Agency) reported that Korean cosmetic sales in South America rose to USD\$8.35 million in 2016 from USD\$997,000 in 2008. Morales noticed

that despite the overall sluggish demand in South America, an opportunity existed to sell functional cosmetics that could reap benefits for his company. He wondered what factors made Korean cosmetics popular amongst other nations.

Morales referred to a study of repurchase intentions of Korean beauty products among Taiwanese consumers. He saw that when the Korean cosmetic product was perceived of as good value for money it became popular. Consumers tended to share their opinions amongst their friends and this was more effective than commercial advertising (Moslehpour, Wong, Pham & Aulia 2017).

Morales reviewed another study that examined the brand loyalty of Korean cosmetics among Thai consumers (Taghipour & Loh 2017). As per this study, product packaging influenced buying intentions. While brand equity and customer satisfaction increased customer loyalty.

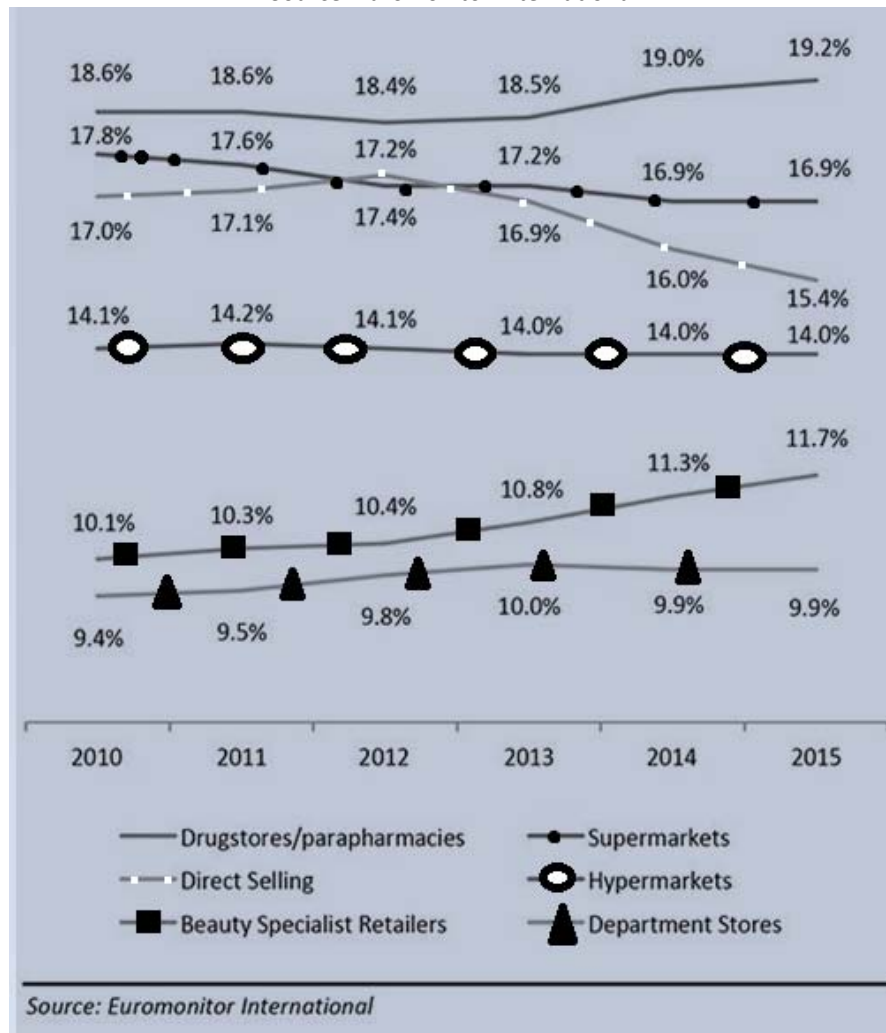
In Europe, Morales had observed that the retailers would demonstrate ways to use the functional cosmetics. A 10-step beauty routine was used to portray the effectiveness of different products. The retailers encouraged the customers to follow the beauty routine to make recurring purchases. But this approach was time consuming and expensive. Morales would not be able to build a customer base instantly by deploying this tactic.

### **The Cosmetic Industry in Chile**

A majority of Chileans made their beauty purchases at drugstores and pharmacies (Euromonitor). However, the trend was slowly changing and Morales noticed that specialized cosmetic stores were gaining popularity. In Chile, the cosmetics industry that was in the late stages of growth and competition was imminent. The distribution of products is shown in Exhibit 1.

**Exhibit 1. Distribution of Beauty and Personal Care Products as a Percentage of Market Share, 2010 – 2015**

Source: Euromonitor International



Morales observed that there were other stores that sold functional Korean cosmetics in Chile, like Republic of Beauty, Arumi Korean Cosmetics, Skin79 and Facerie. These businesses had many physical stores and ecommerce websites. Some of them had also formed alliances with spas and beauty clinics. The products sold by each of these companies were either substitutes or were in direct competition with Korean Box. See Exhibit 2 to view a summary about competition. Morales know that he had to develop a plan to reach potential customers. Ecommerce in the Chilean cosmetic industry was still developing. The younger generations (below 35 years of age) were more open to online shopping.



**Exhibit 2: Industry Competitors Table**

Source: Data compiled by authors

Competitor Name	Republic of Beauty	Arumi Korean	Facerie	Skin79	Korean Box	Pharmacies
<b>What They Offer</b>	<ul style="list-style-type: none"> <li>- Wide variety of cosmetic products</li> <li>- Includes makeup and skin care items</li> <li>- Also sells Korean cosmetics.</li> </ul>	<ul style="list-style-type: none"> <li>- Korean cosmetics and skin care.</li> </ul>	<ul style="list-style-type: none"> <li>- Korean cosmetics and skin care products</li> </ul>	<ul style="list-style-type: none"> <li>- Korean skincare products</li> </ul>	<ul style="list-style-type: none"> <li>- Korean cosmetics, skin care products and make-up</li> </ul>	<ul style="list-style-type: none"> <li>- Inferior quality skincare and makeup products</li> </ul>
<b>Target Market</b>	<ul style="list-style-type: none"> <li>- Young adult men and women.</li> <li>- Middle to higher income.</li> <li>- Mainly targets Chileans.</li> </ul>	<ul style="list-style-type: none"> <li>- Adult women</li> <li>- High income</li> </ul>	<ul style="list-style-type: none"> <li>- Adult women</li> <li>- High income</li> </ul>	<ul style="list-style-type: none"> <li>- Mostly sells directly to clinics</li> <li>- Higher income individuals that might buy from them online</li> </ul>	<ul style="list-style-type: none"> <li>- All women and men</li> <li>- Middle to higher income</li> </ul>	<ul style="list-style-type: none"> <li>- Adult men and women</li> <li>- Middle income</li> </ul>
<b>Competitive Advantage</b>	<ul style="list-style-type: none"> <li>- Developed e-commerce site</li> <li>- Largest share of the market with 25 stores in Chile.</li> </ul>	<ul style="list-style-type: none"> <li>- A Korean company with established presence in the Korean market.</li> <li>- Majority sales from ecommerce website.</li> </ul>	<ul style="list-style-type: none"> <li>- Only an e-commerce site.</li> <li>- Benefits from less overhead than those with brick and mortar stores.</li> </ul>	<ul style="list-style-type: none"> <li>- Has direct and exclusive relationships with the clinics</li> <li>- Ecommerce site.</li> </ul>	<ul style="list-style-type: none"> <li>- Has e-commerce as well as a store.</li> <li>- Has exclusivity with few brands</li> </ul>	<ul style="list-style-type: none"> <li>- Customers prefer to make purchases at drug stores and pharmacies.</li> </ul>
<b>Average Price Comparison of a Facial Cleanser</b>	USD\$ 20	USD\$ 20	USD\$ 20	USD\$ 40 - 100	USD\$ 20	USD\$ 5

### Strategy for Korean Box

Morales wondered what he could do to make Korean Box successful. How could he portray the effectiveness functional cosmetics and engage new customers? What could Morales do to remain competitive in business?

Several possibilities crossed his mind. The product was a success in other countries. But Morales knew he had to draft a thoughtful strategy to make Korean Box successful with the specifics of the Chilean market. Both financial and human resources were involved. What could Morales do to build an effective marketing strategy?

**Chahhat Lakhwani**

is a graduate in Business Management from Northeastern University and also did her Master in Hotel Development at Glion Institute of Higher Education. She has experience in Asset Management and is currently working in Capital Markets and Valuation at Cushman & Wakefield.

**Shreshthi Mehta**

has authored case studies in Strategy, Marketing and Human Resource Management. Shreshthi is a M.B.A. graduate with a flair for writing. She has worked as a consultant with many companies and managed complex HR projects.

**Julia Ivy**

holds a Ph.D. in Psychology and a Ph.D. in Management (Strategy, Entrepreneurship, and Innovation). Dr. Ivy is an Executive Professor of strategy and international business at Northeastern University. She mentors her students in their efforts of career crafting and boutique employability through conducting consulting cases for industry and organization of their choice. Her areas of research interest include a personal strategy for multidimensional job candidates. She is author of the book *Crafting Your Edge for Today's Job Market: Using the BE-EDGE Method for Consulting Cases and Capstone Projects* (Emerald Group Publisher).



## References

- Adina, C., Gabriela, C., & Roxana-Denisa, S. (2015). Country-of-origin effects on perceived brand positioning. *Procedia Economics and Finance*, 23, 422-427.
- Arthur, G. (2016). The key ingredients of South Korea's skincare success. BBC News. Retrieved from: <https://www.bbc.com/news/business-35408764>
- de Casanova, E. M. (2018). Beauty Ideology in Latin America. *dObra [s]: revista da Associação Brasileira de Estudos de Pesquisas em Moda*, 11(23), 10-21.
- Moslehpour, M., Wong, W. K., Pham, K. V. & Aulia, C. K. (2017). Repurchase intention of Korean beauty products among Taiwanese consumers. *Asia Pacific Journal of Marketing and Logistics*, 29(3), 569-588.
- Reach 24H Consulting Group (n.d.). South Korea Cosmetics Regulation. Retrieved from: <https://cosmetic.chemlinked.com/countrypage/south-korea-cosmetics-regulation>
- Santacreu, M. A. & Zhu, H. (2018). How Did South Korea's Economy Develop So Quickly? Federal Reserve Bank of St. Louis. Retrieved from: <https://www.stlouisfed.org/on-the-economy/2018/march/how-south-korea-economy-develop-quickly>
- Shilling, C. (2003). *The body and social theory* (2nd ed.). Thousand Oaks, CA: Sage.
- Shin, K. O. & Park, H. S. (2019). Antiaging Cosmeceuticals in Korea and Open Innovation in the Era of the 4th Industrial Revolution: From Research to Business. *Sustainability*, 11(3), 898-906.
- Taghipour, A. & Loh, A. (2017). Influences on brand loyalty among Thai female cosmetic consumers. *International Journal of Social Sciences*, 3(2) 1947-1969.
- Trading Economics (2018). Chile Unemployment Rate. Trading Economics. Retrieved from: <https://tradingeconomics.com/chile/unemployment-rate>

## ***LIGHT UP THE WORLD RIGHT PERSON? RIGHT PLACE? RIGHT TIME?***

**SANDRA MALACH**

**ROBERT MALACH**

Haskayne School of Business  
University of Calgary

Dave Irvine-Halliday was an engineering professor at the University of Calgary, Alberta, Canada (see Exhibit 1). He spent his 1997 sabbatical in Nepal where he completed a project at the Institute of Engineering, Tribhuvan University, Kathmandu, Nepal. Then he embarked on a trek around the Annapurna Circuit, a popular trekking route in Nepal. During his trek, it became obvious to him that most rural villages lacked adequate lighting. He thought about the children's ability to read in their homes and schools. Dave concluded that there had to be some way to bring light to the villagers.

Upon returning to the University of Calgary, he plunged into what was referred to as "*a wee personally funded project*" which had little, if anything, to do with his 'real' research (Irvine-Halliday, Craine, Upadhyaya & Irvine-Halliday 2000). Toward the end of 1998, this project resulted in a prototype lighting system for the third world. In 1999, Dave and his wife Jenny took the prototype system to Nepal to determine whether Dave had developed a feasible, technological solution to the global third world lighting problem. The local response was overwhelmingly positive. Dave and Jenny were just 'blown away' by the villagers' excitement over the system.

Dave now had to decide whether to bring this technology to those living at the bottom of the pyramid. Should he start a social venture to light up the world? Was he the right person, in the right place, at the right time?

---

The authors developed the case for class discussion rather than to illustrate either effective or ineffective handling of the situation. The case and its accompanying instructor's manual were anonymously peer reviewed and accepted by the *Journal of Case Research and Inquiry, Vol. 5, 2019*, a publication of the Western Casewriters Association. The authors and the *Journal of Case Research and Inquiry* grant state and nonprofit institutions the right to access and reproduce this manuscript for educational purposes. For all other purposes, all rights are reserved to the authors. Copyright © 2019 by Sandra Malach and Robert Malach. Contact: Sandra Malach, University of Calgary, 2500 University Dr. NW, Calgary, AB T2N 1N4, [sandra.malach@haskayne.ucalgary.ca](mailto:sandra.malach@haskayne.ucalgary.ca)

**Exhibit1. The Entrepreneur: Dave Irvine–Halliday**

Source: Irvine-Halliday 2008



Dave Irvine-Halliday was born on May 29, 1942 in Perth, Scotland. He spent his childhood in Dundee, Scotland. His father was a machine man who operated lathes and drillers and his mother worked in a jute factory as a seamstress. His extended family members were workers at mills, shipyards and the local council. None were entrepreneurs or had a University education. He was poor, but not dirt poor. There was always food on the table and he never froze. He had one pair of shoes and, as a kid when he ripped the sole off playing soccer, he had to tie a string around it. The family didn't have a radio until Dave was in his teens – never mind a TV. However, Dave was educated and felt lucky that he was educated without paying a penny.

After completing high school in Dundee, he studied telecommunication engineering at the Abertay University. When he started University, he felt inferior to the other students and so he *“worked his backside off”* because he couldn't afford to fail. As the years went by, he realized he wasn't the cleverest nor the dumbest student. After completing master and doctorate degrees at the University of Aberdeen, he was ready to take a job in Switzerland. When he learned that immigration would not allow his wife, Jenny, and their 18-month-old daughter, Rachel, to join him for a year, he devised a unique solution. During his stay at a Swiss hostel, he had met some people from Edmonton. *“You fancy going to Canada?”* he asked Jenny. After a moment of silence, she agreed (Venter 2005).

Dave's start in Canada was difficult. The family lived in Ottawa for 3 months before Dave secured employment as an electrical engineer with Bell Northern Research. Four years later he moved to Edmonton to take a position with Alberta Government Telephones (now TELUS). At Alberta Government Telephones, Dave was first exposed to fiber optics. In 1980, the family moved to Scotland and then Australia, where Dave began his academic career at Victoria University of Technology in Melbourne. In 1983, he returned to Alberta when he was hired by the Faculty of Engineering at the University of Calgary. His specialty was fiber optics. Dave had two grown children, a married daughter living in Vancouver and a son who was working on developmental projects around the world. His wife Jenny was a midwife by profession but had spent most of her time pursuing a variety of arts including weaving, spinning, and design. She was an entrepreneur, running a satisfying but financially unsuccessful clothing design business for 4-5 years.

Dave was fortunate as he always had a lot of physical energy. With a chuckle, he described himself as a recovering mountaineer and a mountain runner. As a student, he had been a Scottish champion cyclist who rode 400 miles per week. Mountaineering was close to his heart. As a young man, he climbed Ben Nevis, Britain's highest mountain, where he broke his leg, and Chamonix, where he broke his neck (Venter 2005). Calgary, Canada was only one hour from the Rocky Mountains – a great place to live for a mountaineer. He also traveled abroad trekking in Nepal and to Everest base camp.

Now, in his 60's he still had the capacity to work 18-hour days. When working on something he was passionate about, he never got tired. For example, the other night he talked on his cell phone until after midnight and when the battery ran out he called the party back on the land line to finish the call. He then did some e-mails and got up the next morning at 6 a.m. feeling refreshed. He didn't think he could work the same number of hours at a normal job (for which he lacked passion) but said that he felt blessed as being a professor gave him an amazing

amount of flexibility. He modestly said, *“I don’t want to suggest that I’m a superman or anything like that but it’s just a fact.”*

Dave had always been a spiritual person who had a lot of empathy for those living in poverty. He attributed this to his upbringing in Scotland where he believed it was just a natural inclination to try and help people. Throughout his married life, his family always sponsored children from World Vision and other organizations. In this way, he’d always shown his concern for the developing world. In his 20’s he started to think about things and made up his own mind. He wasn’t concerned if others agreed with him, thinking, *“that’s just too bad; I’m doing the best I can. I trust my own counsel.”*

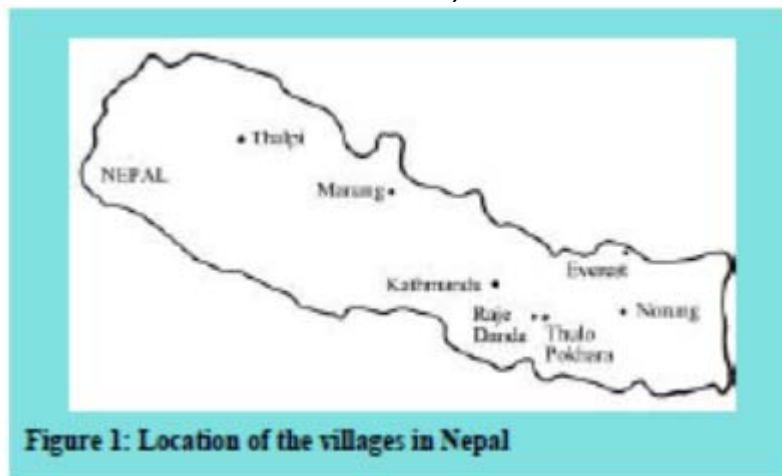
### The Opportunity to Light up the World

Dave Irvine-Halliday was an engineering professor at the University of Calgary and spent his 1997 sabbatical in Nepal. Nepal was a third-world country located in the Himalayan Mountains bordered by India and China. Dave completed a project at the Institute of Engineering, Tribhuvan University, Katmandu, Nepal. He then embarked on a multi-day trek around the popular, mountainous Annapurna Circuit with his trekking guide, Babu Ram Rimal (Munday 2004).



**Exhibit 2. Villages in Nepal**

Source: Irvine-Halliday et al. 2000



They spent one of the nights in the remote village of Manang and visited Babu's relatives (see Exhibit 2). Dave was introduced to a friendly couple who extended their hospitality to Dave and Babu by inviting them inside their stone and mud hut for tea. A wood fire that filled the air with smoke was used to heat the water. The home had no chimney as the Nepalese believed that the smoke from the cooking fire protected the wooden ceilings from insect attack (Irvine-Halliday et al. 2000). As Dave was sitting in this little home having a cup of tea with the old woman, he realized that he couldn't see the couple sitting in 5-6 feet in front of him until the embers would crumble in the little, tiny fire. Then he caught a brief glimpse of them.

On the trek a few days' later, Dave spotted a small, stone schoolhouse. His curiosity caused him to peek in the window. He was struck by how dark it was inside. In quick succession, two thoughts occurred to him— How do the kids see to read and write? Was there anything I could do?

Dave couldn't stop thinking about the lack of light in these villages that were off the power grid. The current light source was kerosene which was expensive, dangerous and provided poor quality light. The cost of operating a simple kerosene wick oil lamp was over 600% of that of a

lamp (as illustrated in Appendices A and B). Kerosene was also dangerous; it caused fires and burns, particularly to children, lung and eye disease and poisoning (Mills 2012). Dave compared the light of a simple wick kerosene lantern to that emitted by a birthday candle. A kerosene lantern provided only 1% to 10% of recommended lighting in industrialized countries (Mills 2005).

Dave thought that he could possibly come up with a novel solution to the problem. After all, he had a background in lighting and electronics. His knowledge of lighting included both traditional light sources, such as incandescent and fluorescent as well as modern sources, such as diodes and fiber optics. He understood traditional electrical grids as well as batteries and emerging solar technology. As a researcher in the field, Dave knew that a feasible solution had not been developed for poor people living in third world countries because over 2 billion people still didn't have a safe and affordable light source.

Upon his return to the University of Calgary, Dave set to work in his lab developing a lighting system for the third world. It had to be: simple, reliable and economic (Irvine-Halliday 2000). He tried to make white light with colored diodes. The results were disappointing – after 20 minutes you could barely see the light, much less read by it. However, he continued to work and developed a generator operated by pedals where power was generated when a person pedaled as if on a bicycle. The light source problem persisted until one day late in 1998 Dave conducted an internet search for “illumination products” and much to his wondering eyes did appear the words “White LED” on the web page of Nichia, a Japanese company (Munday 2004). He immediately called the company and explained that he was working on a project for the developing world and requested samples. Within a week, Dave received a shipment of a couple of dozen white LED diodes. Immediately, Dave, and his technician, John Shelley, took the samples to the lab. They connected the diodes to a power supply, placed a typed sheet of paper beside the diode, turned off the lights and turned on the diodes. Standing in front of the lighted

table, Dave exclaimed, “*Good God, John! A child could read by the light of a single diode!*” That was a defining moment (Irvine-Halliday 2007).

Dave worked excitedly to design the first lighting system. The technicians in the Department of Engineering developed the circuit layout and circuit boards. Some of the designs were a long strip of about 8 diodes, others were square, and others were round. Different configurations were developed to determine which would most effectively light space. Now that he had connected the lights to the pedal generated lighting system more questions gnawed within Dave. Would it work in Nepal? Would the villagers accept it?

Dave knew that he had to return to Nepal in 1999 – an expensive trip. He put it to his wife, Jenny, this way:

*“Look, we’re going there. We would have to pay for it ourselves because we couldn’t get anyone to give us money to try this thing out. But there was a real chance that the people in the villages wouldn’t like this. Just because we thought it’s a great system doesn’t mean they would think so. We had to make sure that we didn’t set ourselves up for failure. If it was obvious that it was not good enough or the villagers didn’t see its purpose, we had to accept that possibility. We’d have to be prepared to just come home and set up a little business. That plan was to start to make headlamps for mountaineers and other things.”*(Irvine-Halliday 2007).

In May 1999, Dave and Jenny returned to Nepal to ascertain how the lighting system would work and see if it would be accepted by the villagers. One evening, at the beginning of their trip, they were having supper in a powerless guesthouse with a local villager. In this mountainous village, the sun had set, and a kerosene lantern was the sole source of light. Unbeknownst to the villager, Dave had strung a LED light system over the table and connected it to a charged battery. He asked his host to turn off the kerosene lantern. Then Dave switched on the LED lights. There were smiles all around the table. After enjoying their dinner, the villagers asked if they could keep the light (Munday 2004). Dave and Jenny demonstrated the light to many villagers in many villages – the response was overwhelming. The people pleaded

with them to leave the lamp – just one lamp. They hated kerosene – it was smelly, it was expensive, and it was dangerous. Dave and Jenny were blown away by the success of the lighting system.

Within a week or so of going to their first village, Dave noticed that people used flashlights powered by D-cell batteries and incandescent bulbs. He decided to conduct an experiment. He bought some flashlights, took out the incandescent bulbs and replaced them with LED's. In the experiment one flashlight had an incandescent bulb and another had LEDs. He turned off the light in the hotel and turned on the flashlights. No light meter was required to clearly see that better light was emitted from the LED flashlight. Also, the battery life would be increased by at least seven times in the LED flashlight. The bulbs would not break if the flashlight were dropped. Dave realized that a huge environmental impact could be made just by replacing the bulb (Irvine-Halliday et al. 2000).

The 1999 Nepal trip gave Dave evidence that his technology worked and that it was overwhelmingly accepted by the villagers. It also dawned on him and his wife that this project was bigger than anything they had ever imagined – it was much bigger than Nepal. Dave was still thinking of the technical things – developing and improving this system so the kids could read at night and so that they could do homework after working in the fields. Nokia was at the time the sole manufacturer of white LEDs, so it would be the sole supplier. How would the system's power be generated? The prototype utilized mechanical power but with the rapid gains being made in solar technology could the sun be a viable power source? Would each individual lighting system have its own generating source, or would there be a central village charging station? Dave also thought about the distribution and maintenance of the systems. Would the systems be assembled centrally or at the village? He was considering that some locations could only be accessed via trekking or narrow, dirt roads. Did installation and maintenance create a small business opportunity for a villager? How would they be trained? Most of these locations were not connected to the internet. Dave also considered some

business questions. What were the system component and manufacturing costs? Would they differ if Dave started a non-profit versus a for profit social venture? Should the systems be donated to the villagers or should they be purchased? What was the price? How would the villagers pay?

It was a gradual realization – *“my God, this is just huge!”* Dave and Jenny had to decide whether Dave should dedicate his life to bringing light to those living at the bottom of the pyramid. What should Dave do? Was he the right person? At the right time? In the right place?



**Sandra Malach**

is an instructor in the Entrepreneurship and Innovation area at the Haskayne School of Business, University of Calgary.



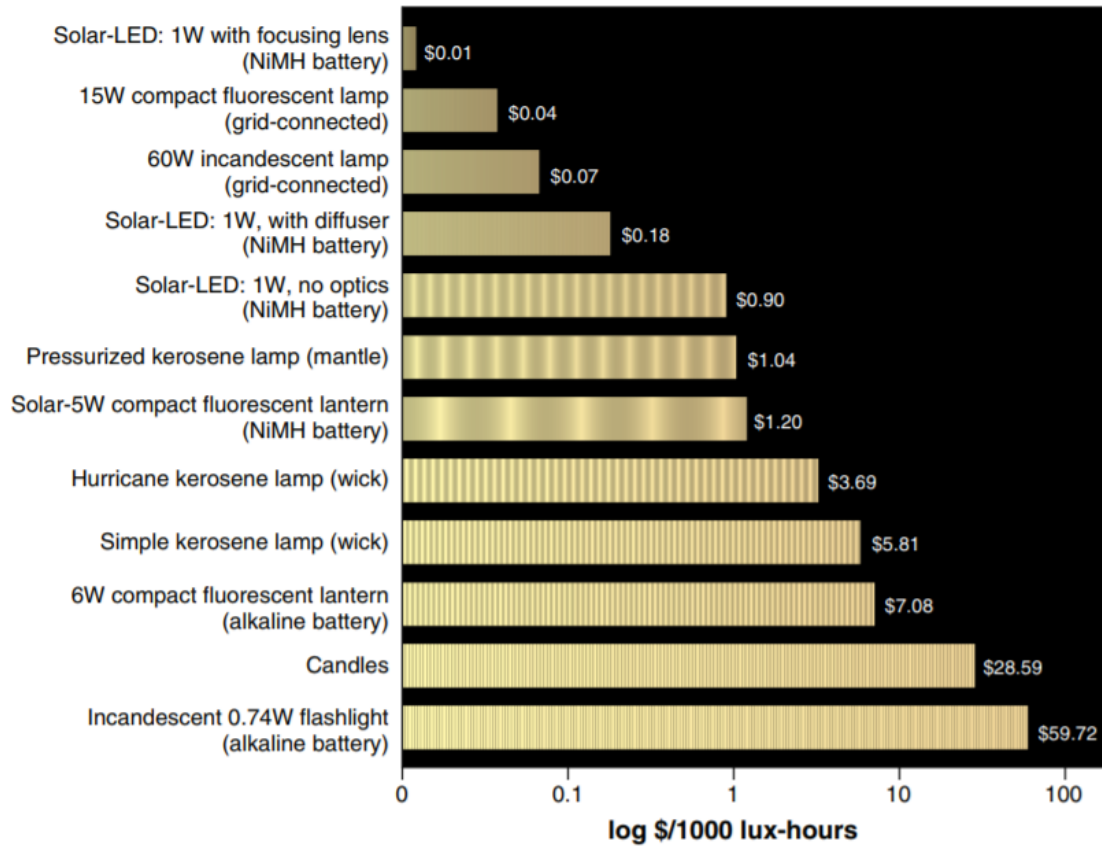
**Robert Malach**

is a Law Instructor in the Business and Environment area at Haskayne School of Business, University of Calgary.



**Appendix A**  
**Total Cost of Illumination Services**

Source: Mills 2012



**Total cost of illumination services.** Costs include equipment purchase price amortized over 3 years, fuel, electricity, wicks, mantles, replacement lamps, and batteries. Performance characteristics of light sources vary; values shown reflect common equipment configurations (see table S3) and include dirt depreciation factors for fuel lanterns and standard service depreciation factors for electric light per Illuminating Engineering Society of North America. Assumptions are 4 hours/day operation over a 1-year period in each case, \$0.1/kWh electricity price, \$0.5/liter fuel price. NiMH, nickel metal hydride. (Range of market prices for kerosene shown in table S5.) We estimate an average of 11 liters (1) of lighting fuel per household per month; observed values vary from 2 to 20 liters (table S4).

## Appendix B White Led Lighting and Power Information

*Source: Irvine-Halliday et al. 2000*

### Comparison Between an Incandescent Bulb and a WLED Lamp

Lamp Type	Input Voltage	Input Power	Cost (CS)	Relative Heat Output	Ruggedness	MTBF (Hrs)	Luminous Efficacy	Improvement Potential
Incandescent	110 V AC	25 W	1	Very high	Very low	1,000	10-20 lm/W	Very low
12 WLED	12 V DC	1 W	20	Extremely low	Extremely high	100,000	15-20 lm/W	Extremely high

### Typical WLED Home Lamp Assemblies & Power Requirements

Fixture	Type	Application	Power
Flexible Table Lamps	3 WLED	Reading	0.22 W
Fixed type, box shaped	2 WLED	Torch	0.15 W
Ceiling Light	6 WLED	Main Room	0.43 W
Ceiling Light	9 WLED	Main Room	0.65 W

### Approximate Calculations for Different Battery Costs in Nepali Rupees

Type of Lights	# of households	# of lamps per household	Power required per household	Cost of power for all households (NRs)	Battery Cost per household (NRs)
Bulbs	100	3	105 W	1,102,500	-
AC Compact Fluorescent	100	3	39 W	409,500	-
DC Fluorescent	100	3	27 W	283,500	4,821
DC WLED's	100	3	3 W	31,500	536



## References

- Irvine-Halliday, D. (2007, May). Light Up The World. (S. Malach and P. Robinson, Interviewers)
- Irvine-Halliday, D. (2008), Light Up the World Foundation. Rotary District Conference 2008. Retrieved from <https://portal.clubrunner.ca/50012/sitepage/dave-irvine-halliday-light-up-the-world>.
- Irvine-Halliday, D., Craine, S., Upadhyaya, M.R., Irvine-Halliday, G. (Fall, 2000). Light Up The World - Nepal Light Project and Everest. IEEE Review, 36, 14-18.
- Light Up the World Foundation. (2019, March 5). LUTW Homepage. Retrieved from www.lutw.org: <http://lutw.org/>
- Light Up the World Foundation. (n.d.). Light Up the World Foundation. Retrieved from YouTube: <https://www.youtube.com/watch?v=eAoOQLytCc&gl=CA>
- Mills, E. (2012). Lumina Project Technical Report #10. USA: Lawrence Berkeley National Laboratory, University of California.
- Mills, E. (2005, May 27). The Specter of Fuel-Based Lighting. Science, 308, pp. 1263-1264.
- Munday, B. (2004, July). Giving Light, Spreading Hope. Reader's Digest, pp. 68-71.
- Venter, A. (2005, November). Shine A Light. On Campus Weekly.
- Visionary Lighting & Energy India. (2019 March 12). VLE Homepage. Retrieved from <http://www.vleindia.com/about.php?id=MQ==>

## **SOFTWARE TEAM SIX: ORGANIZING FOR SOCIOCRACY**

**IVA PETKOVA  
JENIA KOJUCHAROVA  
STEFAN IVANOV  
STOICHO GOTZEV**

American University in Bulgaria

Kiril Gantchev, Ivailo (Ivo) Bratoev and Stefan Dobrev, the three co-founders of Software Team Six (ST6), reviewed the agenda for the upcoming meeting. It had been a year since the opening of the software design start-up firm that offered top level engineering consulting services. In the meeting, the first annual report was going to be presented to the small team.

The past year the team had focused on developing ST6's mission of resolving challenging technical problems with a global impact. The team had begun operating in a new type of structure in which all team members had an equal say in the company's decision-making process. At the first annual meeting, the team members were about to review the progress they had made so far, the successes they had had, and any actions needed to continue being successful. How had they achieved so far? Were they on the right path? Was the current structure sustainable in the future? What further actions could they take to make their vision a possibility?

## The Organization

Software Team Six (ST6) based in Sofia, Bulgaria, was a start-up software development and consulting firm which provided React, React Native, and GraphQL software services. The firm focused on a niche segment within the software services industry and its main goal was to provide expert hands-on engineering and consulting services.

### **Background**

Kiril and Ivo grew up in the small neighborhood of Stara Zagora, Bulgaria and went to primary school together. Stefan grew up in Kazanlak, Bulgaria. Kiril went to live in the United States in 1998, while Stefan and Ivo remained in Bulgaria, where they distinguished themselves in math and science competitions. Ivo and Stefan went to Sofia University's Faculty of Math and Informatics (FMI), where they met, worked on projects together, and sold their first startup idea to Telerik - a Bulgarian company which sold *"user interface components, content management solutions and Microsoft developer tools that allowed programmers to build their own applications"* (Dzhambazova 2012).

After Telerik acquired the startup, Stefan and Ivo assumed various engineering and then leadership roles within the company. Eventually, Stefan became the Director of Engineers, while Ivo was the Senior Team Lead and Senior Software Manager for a couple of teams. They had a reputation as among the top engineers in Telerik. In the meantime, Kiril had built his career with several large software companies in the United States and then worked as a Senior Software Engineer/Tech Lead at AdGooroo – *"a leading provider of internet marketing competitive intelligence, keyword research, and other keyword tools"* (AdGooroo 2004). Kiril moved back to Bulgaria in 2012 to become an entrepreneur. The paths of the three software engineers crossed again several times in 2013 and 2014 when Ivo and Stefan contributed to Kiril's start-ups.

### ***Timeline of Events***

The three men founded ST6 in 2017. Ivo and Stefan had left Telerik shortly after the December 2014 acquisition of Telerik by Progress Software - a leading platform for developing and deploying mission-critical, cognitive-first business applications for competitive advantage. Kiril had just closed his latest two start-ups, BitLendingClub - a marketplace that used block chain technology, and Loanbase - a company leveraging block chain technology in order to provide small business loans in emerging markets (Crunchbase 2014). The three of them got together in January, 2017 and decided they wanted to create another product-oriented startup. At first, they worked on a mobile application for whiskey enthusiasts, which they initially experimented with over Facebook. They saw that the idea wouldn't generate a profit early enough to warrant a further investment, and therefore decided to use their software and engineering skills to quickly earn revenue and build a team of talented individuals. Thus, ST6 began. As Stefan and Ivo had numerous connections with very talented engineers from their time at Telerik, they decided to begin recruiting through their network first.

In May 2017, the trio initially worked on a project for Hobsons – a company that enabled educators to improve college and career planning, admissions and enrollment management, student success and advising (Hobsons Education Advances 2018). ST6 helped Hobsons deliver on a major milestone for July 2017 and was able to do so successfully with only two team members on the project. During this time, ST6 had earned quite a bit of trust within Hobsons, and in December 2017, ST6 ended up championing an effort to transition Hobsons from a cumbersome and slow development structure to a single code repository structure. *“This was a major technical project that was generally never given to outside contractors and was handled by internal architects. However, our team managed to convince the VP of Engineering that this was an excellent decision, and it paid off!”* enthusiastically explained Kiril. By this time, the trio had hired four new members (software craftsmen and women); all were ready to continue their contributions to Hobsons’ success. The team managed to deliver the finished product during

the Christmas holidays when most of Hobsons' team members were out, therefore there was minimal impact and downtime.

In March 2018, ST6 began a project with Isobar – a global agency that delivered digital transformation, solved complex business challenges through digital marketing, ecosystems and products, driving digital strength and brand loyalty (Isobar-Global 2018). Isobar had recently signed a contract with one of the largest sports brands in the world and was supposed to take over work from another consulting company. *“However, the existing team at Isobar didn't have any experience with the technology stack used by the other company, and they were struggling to get their work approved for merging the codebase of the sports company,”* explained Kiril. Within two weeks, the ST6 team helped Isobar up to speed and Isobar's team was able to successfully pass the code reviews.

Almost a year after its foundation, the small software startup demonstrated a very promising balance sheet and P&L with a revenue of 200,000 BGN and a profit of 39,000 BGN (see Appendix A).

### ***Background on the Industry***

The Bulgarian IT sector had experienced a 17% average growth rate since 2007, and had become an increasingly important part of the country's economy and overall intellectual growth (Questers 2018). Leading multinational firms such as HP, VMware, and SAP were important players in the Bulgarian market. On the other hand, Bulgarian companies were competitive in the global market. The main problem that the Bulgarian industry faced was a lack of qualified individuals, which limited the growth potential of the firms in the IT sector.

### ST6's Unique Organizational Structure

The ST6 team members decided that in order to promote collaboration, innovation, and transparency throughout the company, they wanted a flat organizational structure. The structure that was implemented consisted of circles instead of departments. There were four main circles: Organizational, Operations, Office, and Consulting. The Consulting circle had two sub-circles: Sales and Hires (see Appendix B). Each circle met on a weekly or bi-weekly basis to discuss necessary and upcoming tasks, events, projects, etc. Any employee at ST6 could join any circle at any point in time, for as long as s/he wished and provide feedback or advice. Employees did not have to stay in only one circle. If they chose a given circle, they didn't have to remain a permanent member of that circle. Employees could participate in as many circle meetings as they wished. Kiril explained:

*“Each Circle within the company has its own domain, which includes setting policies, practices and maintaining open documentation so everybody can stay up to speed on what is happening in each circle. If a person wants to have input on a particular area of the company, he or she can join that circle and participate in it.”*

If any employee would like to be informed at any given point about any of the other circles, he or she could also read the meeting minutes from each meeting, which were available to everyone via Google Docs.

The Organization Circle set the goals on the company level, where a large portion of the whole team was part of the circle. Each adjacent circle within the organization then set its goals in order to achieve the company-level goals. All of these goals were documented in Google Docs and shared within the entire company. Employees could inform themselves on what had been agreed at the Organizational level at any given point (see Appendices C and D).

This novel form of organization was first suggested by one of the co-founders, Stefan Dobrev. When Stefan was Director of Engineers at Telerik, he had conducted his own research on how

to best organize his own team. That was when he came across a new concept, and applied the concept as much as he could to his then Telerik team. Years after, as a co-founder of ST6, he brought experience with the concept. Stefan worked with the rest of the team at ST6 to apply the organizational structure there. Since everyone had full control over all decisions, all had the opportunity to fully implement the concept into the organizational structure early-on. The concept was called sociocracy.

## Sociocracy

### *The Origin of the Idea of Sociocracy*

The origins of sociocracy can be traced back to the mid-nineteenth century when the French philosopher Auguste Comte developed the discipline of studying people in social groups, which he referred to as sociology. The root word for both sociology and sociocracy was the Latin word *socius*, which meant associates or companions. The suffix *ology* meant the “*study of*” as in archeology, psychology, etc. The suffix *ocracy* meant “*to govern,*” in other words, “*governance by associates/companions*” (Villines 2017). Within a context of political revolutions in which monarchies and aristocracies were stripped of power, Comte searched for a rationale for government. “*Governance on the basis of inherited rights, personal wealth, religious dictates, and military power had all proven corruptible and not in the interests of the people*” (Sociocracy for All).

Comte developed a philosophy of “*Positivism.*” In positivism, knowledge was built from what is acknowledged of the natural world and could be proven - not what a monarch or the church decreed. Comte believed that a society directed by scientists would come up with the best social and economic policies by using scientific methods.

## ***Sociocracy for Business***

The Dutch electrical engineer Gerard Endenburg was eager to find a method to implement sociocracy in a competitive, results-oriented corporation. He was frustrated, as an engineer, because he could design successful mechanical and electric systems, but when it came to managing people, it seemed impossible to produce results that satisfied all stakeholder groups: investors, managers, and workers. From his experience in a “Children Community Workshop,” Endenburg knew that in order to create a highly productive organization, everybody’s needs should be considered.

*“By the early 1980s, Endenburg had developed a method that produced a harmonious, self-regulating, and highly successful business. Remarkably, it could be used to govern any kind of organization effectively” (Villines 2017).*

Endenburg dedicated a few years and developed the Sociocratic Circle-Organization Method (SCM) (See Appendix E). He based it on his now famous three principles (Rau 2017) (see Appendix F):

- Consent decision-making for policy decisions, including electing people to roles and responsibilities;
- Circle meetings in which working groups meet as equals to make policy decisions;
- Double linking of circles to form a circular hierarchy that functioned as a feedback structure.

In their 2004 book *We the People*, John Buck and Sharon Villines made Sociocracy accessible to the English-speaking world. Since its publication, *We the People* became the standard reference on Sociocratic principles and practices, its history, and its theoretical base.

## ***Organizations Using Sociocracy***

There was no official list of organizations that applied sociocracy in their governance process.

*“Sociocracy is used in national and international associations, building and manufacturing companies, health care services, public school systems, villages, private schools, Buddhist monasteries, software companies, residential*



*communities, colleges, a wholesale florist company, veterinary offices, and consulting firms. They are spread over North and South America, all the countries of Europe, Scandinavia, Australia, New Zealand, and developing in Africa and Asia” (Villines 2017).*

### Evolution of Personnel at ST6

Being a start-up in its early stage, ST6 had an informal hiring process. Given the specificity of the sociocracy-based organizational structure, it was important to have a good cultural fit among team members. ST6's core values revolved around passion, perfection, teamwork, integrity and openness. The team looked for new hires who would fit well with the company's values and way of working. With that in mind, the founders and the rest of the team would meet with candidates several times before making an offer. Most recruits were people team members had already worked with elsewhere, but ST6 intended to extend its network of contacts and introduce a more structured hiring processes over time.

In addition to giving their team members the opportunity to participate in the decision-making process, the founders tried to motivate them by organizing weekly lunches, and monthly and quarterly team-building events. The team was equipped with the best office equipment including 4K dual-monitor set-ups, high-end keyboards, and elevating desks. Office perks such as a game room, foosball table, and TVs were made available also.

ST6 aimed to be in the top 5% of companies in Bulgaria in terms of compensation. In addition, all team members were given an equity share in the company. As a result, the company did not have any employee turnover as of August, 2018. Additionally, to ensure employee satisfaction was ongoing, the company sent weekly surveys to the employees and the results revealed overall satisfaction with the organization and with the current structure (see Appendix G).

## Conclusion

Kiril, Ivo, and Stefan concluded the meeting with the rest of the team after discussing their progress and development within the last year. They had also discussed some potential challenges they might face in the future. Should the team members put additional efforts into developing their current organizational structure as the company grew and added more and more employees? For how long could ST6 remain a Sociocratic organization?



**Iva Petkova** is a Bulgarian-born Compliance Professional in the Financial Services Industry. She graduated Lake Forest College in Lake Forest, IL, USA, with a double major in Business Administration and Spanish, and a minor in International Relations. After 7 years in Corporate America, she moved to Bulgaria to pursue her EMBA at AUBG.



**Jenia Kojuharova** is a Managing Director at Media Matters International Ltd., an outsourcing specialist for the media measurement, evaluation and communications research industry. She holds a Masters in Finance from the University of Paris 1 Pantheon-Sorbonne and an EMBA from the American University in Bulgaria.



**Stefan Ivanov** is an experienced professional in the pharmaceutical industry business, specializing in operational and organizational excellence and change management. He holds an EMBA from American University in Bulgaria.

**Stoicho Kirilov Gotzev** has a Bachelor degree in Accounting and Control, a Master degree in Finance management and in 2019 successfully completed the EMBA program in AUBG. He is finance professional, working as a Finance Manager in an international mining company.



**Appendix A**  
**Software Team Six: Balance Sheet & Income statement**

*Source: Software Team Six*

<b>BALANCE SHEET</b>	<b>As at 31 December</b>	
	<b>2017</b>	<b>2016</b>
<b>Current assets</b>		
Trade receivables	33	-
Other receivables and other current assets	7	-
Cash and cash equivalents	3	-
<b>Total current assets</b>	<b>43</b>	-
<b>Non-current assets</b>		
Plant and equipment	6	-
<b>Total non-current assets</b>	<b>6</b>	-
<b>TOTAL ASSETS</b>	<b>49</b>	-
<b>Current liabilities</b>		
Trade payables	5	-
Tax liabilities	5	-
<b>Total current liabilities</b>	<b>10</b>	-
<b>Shareholders' equity</b>		
Share capital	5	-
Net earnings	34	-
<b>Total shareholder's equity</b>	<b>39</b>	-
<b>TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY</b>	<b>49</b>	-
<b>INCOME STATEMENT</b>	<b>2017</b>	<b>2016</b>
Sales	242	-
Materials	(6)	-
Outside services expenses	(10)	-
Labour expenses	(179)	-
Other income / (expenses, net)	(2)	-
<b>Operating profit</b>	<b>45</b>	-
Foreign exchange (losses) / gains, net	2	-
<b>Profit before tax</b>	<b>43</b>	-
Corporate income tax	4	-
<b>Profit for the year</b>	<b>39</b>	-

(All amounts in '000 BGN)

**Appendix B**  
**Software Team Six – Organizational Structure**  
*Source: Authors' notes*

<b>Kiril Gantchev</b> Co-founder	<b>Ivaylo Bratoev</b> Co-Founder	<b>Stefan Dobrev</b> Co-Founder
<b>Kristina Koeva</b> Software Craftswoman	<b>Nikolay Valchev</b> Software Craftsman	<b>Ivan Spasov</b> Software Craftsman
<b>Steliyan Stoyanov</b> Software Craftsman	<b>Dimitar Tsonev</b> Software Craftsman	<b>Vladimir Zagorski</b> Software Craftsman

## Appendix C

### Software Team Six – Sociocracy Structure

*Source: Software Team Six*

*Organization Circle*

*Operations Circle*

*Office*

*Consulting*

*Consulting -> Sales*

*Consulting -> Hires*

#### **Organization Circle**

##### 1. Domain

- Company structure and common practices
- Business strategy
- Business vision
- Company culture
- Salaries
- Accountabilities
- Make company-wide decisions transparently with input from everyone.
- Make sure the company and everyone in it acts according to our values.

##### 2. Members

- Kiril
- Stefan
- Ivo
- Ivan
- Krisi

##### 3. Recurrent Meetings

- Sync every 2 weeks.

##### 4. Roles

- Champion - Stefan
- Secretary - Krisi

##### 5. Kanban board: <https://trello.com/b/dZN93HIA/org>

#### **Operations Circle**

##### 1. Domain

- Financials
- Legal
- Accounting
- Billing
- GApps
- AWS Accounts
- GDPR

##### 2. Members

- Ivo
- Kiril

##### 3. Recurrent Meetings

- Monthly company-wide sync.

##### 4. Roles

**Appendix C cont.**  
**Software Team Six – Sociocracy Structure**

**Office**

1. Domain
  - Office and everything office related.
  - Company events.
2. Accountabilities
  - A nice and productive office environment.
  - Organize team events once per month.
  - Organize team buildings once per 3 months.
3. Members
  - Steliyan
  - Vladi
  - Krisi
  - Niki

**Consulting**

1. Domain
  - ST6 software consulting.
  - Technology focus.
  - Who works on what project.
2. Accountabilities
  - Share experience and technical knowledge.
  - Grow the skills of the team.
  - Keep high utilization.
  - Deliver more than expected.
3. Recurrent Meetings
  - Weekly Monday Sync - sync how all the projects are going.
4. Members
  - All
5. Roles:
  - Champion - Ivan
  - Secretary - Tsonev

**Consulting -> Sales**

1. Domain:
  - Sales process - utilization
  - Website
  - Social media
  - Marketing
  - Account managing
2. Members:
  - Kiril
  - Ivo
  - Stefan
  - Vladi

**Appendix C cont.**  
**Software Team Six – Sociocracy Structure**

**Consulting -> Hires**

1. Domain:
  - Identify potential hires
  - “Interview” process
  - Employer marketing/branding (recruiting)
2. Accountabilities
  - Grow the team
3. Members:
  - Stefan
  - Ivan
  - Niki
  - Krisi
  - Dimitar
  - Kiril
4. Recurrent Meetings
  - Once a month

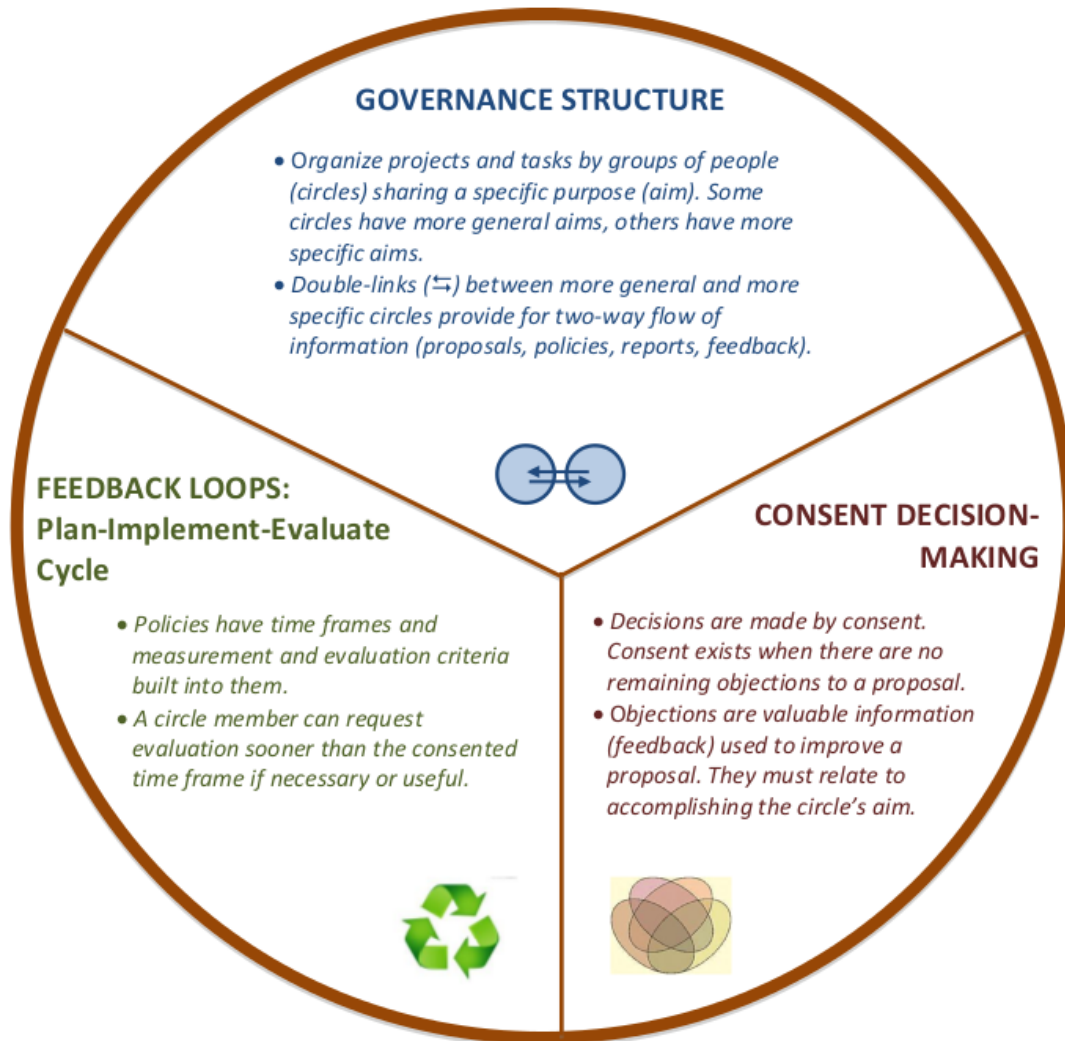


**Appendix D**  
**Software Team Six – Circle Responsibility Matrix**  
*Source: Authors' notes*

Sociocracy at ST6			
Scope of responsibilities			
Circle	Domain (area of responsibilities)		Synchronization meetings
Organization	Company structure, Strategy, Vision, Culture, Rewards, Accountabilities, Values		Every 2 weeks
Operations	Financials, Legal, Accounting, Billing, Data Privacy		Monthly
Office	Work-space related, Event planning		On-Demand
Consulting	Sales	Sales, Website maintenance, Social media, Marketing, Account Management	Weekly
	Hires	Recruitment process	Monthly

### Appendix E The Sociocratic Circle-Organization Method

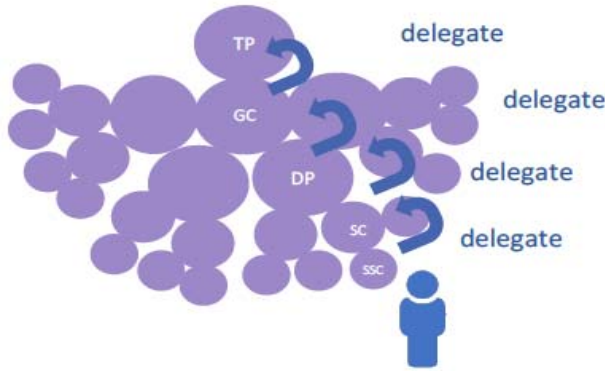
Source: *The Sociocracy Consulting Group, 2016*



2016 The Sociocracy Consulting Group LLC

**Appendix F**  
**Circles: The “Socios” in Sociocracy**  
*Source: The Sociocracy Consulting Group, 2016*

Decision-making circles:

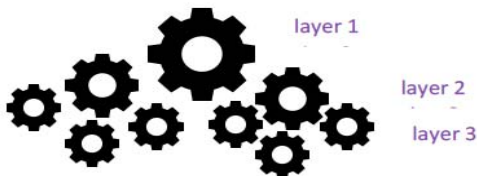


The double link is more than just being heard on board level. With consent as the decision-making method, workers cannot be ignored. Looking at how the management level is made up from workers, sociocracy is more than giving workers a voice in the management. The workers *are* the management.

Circle meetings:

a. Nested circles and domains

We want to create a system of circles where all circles are connected with each other. Although there can be varieties of patterns (see [below](#)), the most used is one of layers/layers:



The domains for these circles are nested, i.e. a subcircle is responsible for one part of the domain of its mother circle. In the diagram below, domains are color-coded. The mother circle is responsible for a large domain and passes two domains on to sub-circles.



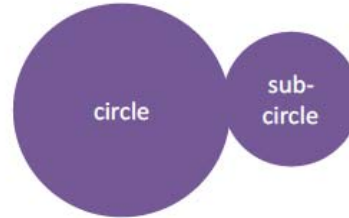
Free to share for non-commercial use. See more free content, videos and sociocracy classes on <http://www.sociocracyforall.org/>



Appendix F cont.  
Circles: The “Socios” in Sociocracy



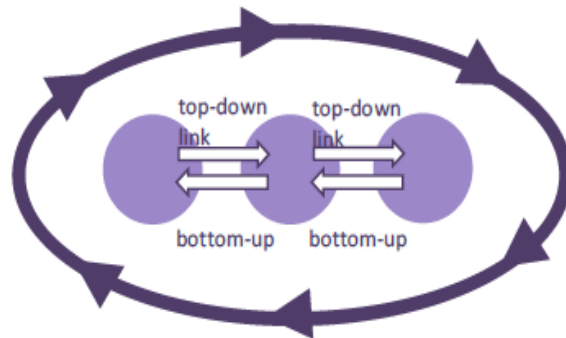
Content role within a circle  
(policy made in circle only)



Circle + sub-circle  
(both circle and sub-circle make their own policy)

Double-linking:

- When wrestling with terminology around power and hierarchy in sociocracy, we often use the term *circular hierarchy*. What is meant by that is that each circle has a top-down and a bottom up relationship at the same time (see *double linking* below), which leads to circular hierarchy:



Circular hierarchy

**Appendix G**  
**Software Team Six – Weekly Survey Results**

Source: Software Team Six

**I am happy at work.**

Strongly Agree

60% (3)

Agree

40% (2)

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

5

**For the most part, my job takes advantages of my strengths.**

Strongly Agree

0%

Agree

33% (1)

Neutral

67% (2)

Disagree

0%

Strongly Disagree

0%

Total votes

3

**Appendix G, cont.**  
**Software Team Six – Weekly Survey Results**

**My coworkers value my opinion.**

Strongly Agree

 100% (2)

Agree

0%

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

2

**I am an important member of this team**

Strongly Agree

 67% (2)

Agree

 33% (1)

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

3

**Appendix G, cont.**  
**Software Team Six – Weekly Survey Results**

**I am an important member of this team**

Strongly Agree

 67% (2)

Agree

 33% (1)

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

3

**I feel I make an impact in the company.**

Strongly Agree

 33% (1)

Agree

 67% (2)

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

3

**Appendix G, cont.**  
**Software Team Six – Weekly Survey Results**

**For the most part, my job takes advantages of my strengths.**

Strongly Agree

0%

Agree

100% (6)

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

6

**I can express my opinion freely.**

Strongly Agree

0%

Agree

80% (4)

Neutral

20% (1)

Disagree

0%

Strongly Disagree

0%

Total votes

5



**Appendix G, cont.**  
**Software Team Six – Weekly Survey Results**

**My coworkers respect my opinion.**

Strongly Agree

33% (2)

Agree

67% (4)

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

6

**We all pursue a common goal.**

Strongly Agree

67% (4)

Agree

33% (2)

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

6

**Appendix G, cont.**  
**Software Team Six – Weekly Survey Results**

**I would recommend this company to friends & family as a great place to work.**

Strongly Agree

 100% (4)

Agree

0%

Neutral

0%

Disagree

0%

Strongly Disagree

0%

Total votes

4

## References

- AdGooroo. (2004). Retrieved from Crunchbase: <https://www.crunchbase.com/organization/adgooroo#section-overview>
- Crunchbase. (2014). Retrieved from Crunchbase: <https://www.crunchbase.com/>
- Dzhambazova, B. (2012, October 30). Bulgarian Company Homes In on Technological Niche. Retrieved from The New York Times: <https://www.nytimes.com/2012/10/31/business/global/bulgarian-company-homes-in-on-technological-niche.html>
- Bulgarian Company Homes In on Technological <https://www.nytimes.com/2012/10/31/business/global/bulgarian-company-homes-in-on-technological-niche.html? r=0>
- Hobsons - Education Advances. (2018). Retrieved from Hobsons: <https://www.hobsons.com/>
- Isobar - Global. (2018). Retrieved from Isobar: <https://www.isobar.com/global/en/>
- Questers. (2018). IT Industry Report. Sofia: Questers.
- Rau, J. (2017). Circles: The "socios" in sociocracy the teams of people who work together to get something done. Empowered Learning Circles for Sociocracy, 18.
- Sociocracy. (2016). Retrieved from The Sociocracy Consulting Group: <http://sociocracyconsulting.com/about/sociocracy/>
- Sociocracy for All. (n.d.). Retrieved from sociocracyforall.org: <http://www.sociocracyforall.org/>
- Villines, S. (2017, November 29). Sociocracy's Achilles Heel. Retrieved from Sociocracy.info: <http://www.sociocracy.info/>

## ***SWEET SUCCESS OR HEADACHE?***

**MONIKA L. HUDSON**

**FRANK OHARA**

University of San Francisco

It had been a difficult three and a half years, but Maria could see light at the end of the tunnel. Micariño's pastries were now sold at almost 30 retail locations throughout Cali, Colombia and its catering services accounted for one-third of the firm's 2017 revenues. Maria and her family wanted to construct a new, larger kitchen so they could double their baked goods output. A USD \$1 million equity investment would easily allow them to achieve that goal. There was just one catch: while the new investor wanted to be a "silent" partner in exchange for her 20% share, she did not like the company's name and had brought in a marketing consultant to develop a new one. Further, the investor wanted to begin franchising the re-named Micariño's baked goods out of Miami. Maria wondered – should she continue to independently own her growing but still small family business in Colombia or should she become part of a U.S.-based franchise?

### **The Spur**

Maria and her then husband had two children and a relatively comfortable life in Cali, Colombia. Their large, ranch-style home had an expansive kitchen and a three-car garage. While Maria did not work outside of the home, she spent much of her time baking various Colombian sweets and meringues, which she often distributed to neighbors and friends. About four years ago, Maria's husband indicated he was filing for a divorce and had plans to remarry. Stunned, Maria wondered what she was going to do: she did not have an external job

and her daughter, Ana Maria, was in her final 18 months of college with her son, Eduardo, only two years away from starting the same. Desperate, Maria began to bake and think.

### Next Steps

During a family discussion about the divorce, Ana Maria offered to ask if the university would let Maria sell her baked goods on campus. Ana Maria said the school had recently initiated a project to allow non-student vendors on campus and they were looking for applicants. The two women filled out the required forms and were given a booth, space and permission to sell from 2:00 p.m. until 6:00 p.m. daily.

Maria now had a new schedule: she would rise at 4:30 a.m. and begin to bake. On days when she did not have classes, Ana Maria would work with her mother from 7:00 a.m. until about 11:30 a.m., when the two of them would begin to load items into their cars. Depending upon the day, Maria, Ana Maria and Eduardo would staff the university vendor booth on a rotating basis. They began to use the name Micariño to typify that they were selling mostly sweet items.

Fortunately, sales were immediately strong and within two months, Maria was able to offer two students part-time employment on the days when Ana Maria and Eduardo had classes and could not join her at the university booth. Maria also began handing out flyers promoting other Micariño items including birthday cakes and special occasion sweets. Eduardo helped Maria create an elementary website and several promotional brochures featuring their offerings. As a unit, the family developed a basic marketing plan and all three family members asked university students to distribute their flyers and promote Micariño on their social media platforms. As its first year of operations ended, Micariño had achieved the equivalent of \$90,000 USD in gross receipts, just from campus food sales and through four Cali retail bakery outlets.

Consultants from the university's business incubator advised Maria that the company might be able to significantly increase its second-year sales if she added a breakfast catering line and hired sufficient preparation staff. Maria immediately created three relatively simple breakfast menus and worked with the university employment office to identify some students willing to regularly work a 6:00 a.m. to 2:00 p.m. shift out of her home kitchen, with the last three hours devoted to prepping for the next day's baking and breakfast orders.

### Accelerated Growth

By the end of their third year, Micariño had more than tripled its first year's sales. Ana Maria had taken a semester's leave of absence during this period to assist her mother with the catering services. Both women were spending 40-60 hours per week producing the various products as well as promoting the firm at networking events at the university's business incubator, catering events for the local Chamber of Commerce and supporting customers' birthdays, anniversaries and parties. Their cakes, meringues and pastries were particularly sought after and Micariño was now known for being able to take any photograph and reproduce it on a pastry, delighting their growing numbers of customers.

Maria continuously set 15% of the firm's annual revenues aside in a working capital reserve. She had also managed to save enough for the third year of Eduardo's university tuition and Micariño now had three full-time employees. With the assistance of the university's incubator consultants, Maria was very proud to have generated integrated 2017 financial statements and, with Eduardo's help, she had gone through the process of projecting the company's profitability for the next three years as detailed in Exhibit 1.

Maria was aware the family's kitchen was no longer adequate for the growing small business. She contacted a local architect about a potential redesign of the family's garage into an

expanded kitchen that could provide the required additional storage, refrigeration and preparation space to allow Micariño to continue to scale. The architect estimated renovation costs at \$400,000 USD. Maria's bank had offered her a 10-year loan at 12% annualized interest.

### An Investment

The university incubator program had been seeking angel investors for Micariño, but until she received the Miami call, Maria was not certain if she should concentrate on saving for Eduardo's tuition or use company cash flow to cover the required kitchen improvements. A \$1 million USD equity investment would allow her to relax: she could use a portion of her draw to cover Eduardo's tuition, maintain the company's existing reserves, and handle the garage/kitchen conversion as well as expenses for additional production staff. Why Maria might even be able to enjoy a short Cartagena vacation!

As she reviewed her options, Maria was clear it came down to obtaining a bank loan or accepting the equity investment. After reviewing her financials and company ratios as well as the valuation projections developed by the university's incubator consultants (detailed in Exhibit 1, 2 and 3), Maria felt confident that she could earn the money needed to repay the loan per the bank's terms. In contrast, Maria worried that she knew nothing about the topic of franchising, although the staff at the university's incubator had assured her that she could learn. At this point, all she basically understood was that she would need to give up the family-selected company name and 20% control of the firm. Was this why Maria was so conflicted about accepting the \$1 million USD equity investment?

**Exhibit 1. Financial Statements**

Source: Authors' notes

MICARINO					MICARINO		MICARINO	
PROFIT/LOSS STATEMENT					CASHFLOW STATEMENT		BALANCE SHEET	
	2017	2018	2019	2020	December 31st 2017		December 31st 2017	
<b>SALES</b>	<b>298,000.00</b>	<b>312,900.00</b>	<b>333,645.13</b>	<b>357,600.00</b>	<b>BEGINNING CASH FLOW</b>	<b>120,000.00</b>	<b>ASSETS</b>	
<i>YoY % Growth</i>		5.00%	6.63%	7.18%	<b>CASH INFLOW</b>		Cash	0.00
<b>COGS</b>	<b>(59,000.00)</b>	<b>(61,950.00)</b>	<b>(66,057.26)</b>	<b>(70,800.00)</b>			Inventory	7,900.00
<b>GROSS PROFIT</b>	<b>239,000.00</b>	<b>250,950.00</b>	<b>267,587.87</b>	<b>286,800.00</b>			Advertising	7,500.00
Selling Exp.	(19,000.00)	(19,950.00)	(21,272.68)	(22,800.00)	From 2017 Sales	298,000.00	Computer/Web Design	7,800.00
Admin. Payroll	(25,000.00)	(26,250.00)	(27,990.36)	(30,000.00)	From Owner	35,000.00	Gross Leasehold	210,000.00
<b>TOTAL EXPENSES</b>	<b>(44,000.00)</b>	<b>(46,200.00)</b>	<b>(49,263.04)</b>	<b>(52,800.00)</b>	<b>TOTAL CASH INFLOW</b>	<b>333,000.00</b>	- Accumulated Depreciation	(70,000.00)
<b>EBITDA</b>	<b>195,000.00</b>	<b>204,750.00</b>	<b>218,324.83</b>	<b>234,000.00</b>	<b>CASH OUTFLOW</b>		Net Leasehold	140,000.00
Taxes	(27,300.00)	(27,300.00)	(27,300.00)	(27,300.00)	Computer/Web Design	(7,800.00)	Gross Equipment/Furnishing	32,000.00
Draw	(65,000.00)	(65,000.00)	(65,000.00)	(65,000.00)	Leasehold Improvements	(210,000.00)	- Accumulated Depreciation	(16,000.00)
<b>NET PROFIT</b>	<b>102,700.00</b>	<b>112,450.00</b>	<b>126,024.83</b>	<b>141,700.00</b>	Equipment/Furnishing	(32,000.00)	Net Equipment/Furnishing	16,000.00
					Advertising	(7,500.00)	<b>TOTAL ASSETS</b>	<b>179,200.00</b>
					Inventory	(66,900.00)	<b>LIABILITIES</b>	
					Payroll	(25,000.00)	Loan Principal	0.00
					Other Expenses	(11,500.00)	<b>TOTAL LIABILITIES</b>	<b>0.00</b>
					Taxes	(27,300.00)	<b>EQUITY</b>	
					Draw	(65,000.00)	Capital	35,000.00
					<b>TOTAL CASH OUTFLOW</b>	<b>(453,000.00)</b>	Current Earnings	195,000.00
					<b>NET CASH FLOW</b>	<b>(120,000.00)</b>	Retained Earnings	41,500.00
					<b>CUMULATIVE CASH</b>	<b>0.00</b>	LESS: Taxes	(27,300.00)
							LESS: Draw	(65,000.00)
							<b>TOTAL EQUITY</b>	<b>179,200.00</b>
							<b>LIABILITIES + EQUITY</b>	<b>179,200.00</b>



**Exhibit 2. Financial Ratios***Source: Bizstats.com*

<b>Financial Ratios</b>		
	<b>Micarino Ratios (2017)</b>	<b>Industry Ratios (Bakeries 2012)</b>
<b>Profit Margin (%)</b>	0.34	N/A
<b>Return on Sales (%)</b>	0.65	4.02
<b>Return on Assets (%)</b>	0.57	5.14
<b>Quick Ratio</b>	N/A	0.72
<b>Current Ratio</b>	N/A	1.17
<b>Liability/Equity</b>	N/A	1.33
<b>Inventory Turnover</b>	37.72	19.32

**Exhibit 3. Earnings Valuations (in USD)***Source: Authors' notes*

<b>EARNINGS VALUATION</b>		
<b>2017</b>		
<b>Multiple</b>	<b>Net Income</b>	<b>Valuation</b>
30.00	102,700.00	3,081,000.00
20.00	102,700.00	2,054,000.00
10.00	102,700.00	1,027,000.00
<b>2018</b>		
<b>Multiple</b>	<b>Net Income</b>	<b>Valuation</b>
30.00	112,450.00	3,373,500.00
20.00	112,450.00	2,249,000.00
10.00	112,450.00	1,124,500.00
<b>2019</b>		
<b>Multiple</b>	<b>Net Income</b>	<b>Valuation</b>
30.00	126,024.83	3,780,745.00
20.00	126,024.83	2,520,496.67
10.00	126,024.83	1,260,248.33
<b>2020</b>		
<b>Multiple</b>	<b>Net Income</b>	<b>Valuation</b>
30.00	141,700.00	4,251,000.00
20.00	141,700.00	2,834,000.00
10.00	141,700.00	1,417,000.00

**Monika L. Hudson**

is Associate Professor at the University of San Francisco and teaches entrepreneurship, organizational behavior and public administration. She directs USF's Gellert Family Business Center, which supports family firms in the SF Bay Area. Dr. Hudson's research interests include entrepreneurship, family-owned enterprises, identity and behavior and the strategic implementation of the same. Dr. Hudson received her undergraduate degrees from Northwestern University; her M.B.A. from USF; her doctor of management from Case Western Reserve University, Ohio; and her doctor of education from USF. A 2017-18 Fulbright Scholar, she conducts research in Colombia and other South American countries.

**Frank Ohara**

Frank H. Ohara is a Professor and Chair of the Department of Finance at the School of Management, University of San Francisco. He received his B.S. from Cornell University, and J.D from Santa Clara University. His wide-ranging research publications include the *Journal of Empirical Finance*, *Thunderbird International Business Review*, and *The CASE Journal*.

## ***FONSELP: CREATING SHARED VALUE TO MAKE THE WORLD A BETTER PLACE***

**JACOB A. MASSOUD**  
**VAFA SABOORI-DEILAMI**  
Barowsky School of Business  
Dominican University of California

Matías Laurenz, founder of the Argentine social impact startup, Fonselp, sat down at his office desk in Buenos Aires and opened his laptop. He had just finished pitching his digital platform to the Sales Director of SAP Argentina with the hopes of adding another user. His company was gaining traction. Fonselp had just recently surpassed 1,200 registered users, 800 of whom were active. However, Matías knew he needed to exponentially increase that number within the next year. He estimated he would run out of funds by the end of 2019.

Matías logged in to his email. He still had not responded to the proposal he had recently received from a consultant known for helping B2B startups scale their businesses. He contemplated whether to pursue this option or other ideas. He opened the email message and stared at it.

### **Background**

#### ***Fonselp's Early History***

Fonselp was officially launched in April 2018 as a digital platform that served as a business solution by connecting nonprofit organizations with companies in Argentina and Latin America. Essentially, Fonselp set out to answer the question, “*How do we help companies to help?*”

(Fonselp.com n.d.). The founder recognized an important problem related to corporate social responsibility (CSR) in Argentina and Latin America:

*"With medium and small companies the biggest obstacles to get involved and donate have been the time to carry out the task and the resources associated with providing the aid. Fonselp eliminates obstacles by saving time, preserving the privacy of the donor and nonprofit, and allowing them to connect and identify opportunities without costs" (Fonselp.com n.d.).*

The Fonselp digital platform enabled companies to donate almost anything of value to nonprofits: used furniture, computers, equipment, mobile phones, use of office space or event halls, educational workshops, professional services, etc. (Fonselp.com n.d.).

Matías had obtained his MBA from IAE Business School - Universidad Austral. He was one of the individuals responsible for establishing Idealist.org in Latin America, which sought to connect people for volunteering opportunities with organizations in need. Through these experiences, Matías discovered that business leaders were becoming frustrated by their inability to have a simple and reliable tool to facilitate positive change in society (Fonselp.com n.d.).

Matías was no stranger to entrepreneurship. Previously, he had founded CentralPos in 2012. CentralPos was established to develop web tools which allowed organizations to automate and manage their credit card transactions in a simple, secure way (Centralpos.com n.d.). He later sold that company and invested the proceeds into his new startup.

Fonselp was incorporated in the United States. This increased the probability of access to capital from U.S. based angel investors and venture capital firms, and enhanced the company's potential as a future acquisition target. The decision also positioned the company for possible future expansion into North America.

### ***Innovative Solution for Nonprofit Sector***

It was estimated that 800,000 nonprofits existed in Latin America, of which 10,000 were registered in Argentina. Another 90,000 informal nonprofits had a presence too. In comparison, over six million companies operated in Latin America (Economist Intelligence Unit n.d.). In addition to the unstable economic environment in Argentina (see Exhibit 1), the nonprofit sector faced several challenges. A lack of support from individual donors, the private sector, and government was a major issue. Jaskyte and De Riobó (2004) argued that an innovative solution should be employed to facilitate collaboration within and across sectors to enhance societal well-being.

Matías illustrated how Fonselp could promote such nonprofit sector innovation:

*“Not all donations need to be physical goods. You should be innovative. You can donate your time. If you are an expert on AIDS... You can teach the ABCs of AIDS prevention to the schools kids. I am dreaming about a day when nonprofits transfer parts of the knowledge that they possess to other nonprofits. I want to create the platform and the vehicle for this knowledge transfer.”*

### ***Target Market Evolves***

To generate awareness, Matías utilized social media such as LinkedIn, Twitter, and Facebook. He also experimented with Facebook ad campaigns to determine the costs of acquiring customers. Nonetheless, Fonselp limited its online marketing expenditures. Matías stated, *“I can put \$20,000 in marketing online, but I think it's not intelligent...I think you're wasting money... I have to divide myself in percentages: Some days selling, some days in meetings with programmers, and some days just thinking about 2019.”*

Fonselp also gained credibility with the business community after being featured on *La Nación* TV (Torres 2018).

Matías hoped to capitalize on growing interest in CSR and the lack of tools available in Latin America for corporate giving and CSR reporting. Matías explained Fonselp's focused differentiation strategy, *“We are different, but we are more or less the same idea. I think we*

*have an opportunity with the small and medium companies. U.S. competitors go for the big companies.”*

Success resulted from persistent emails, phone calls, and finally pitching the Fonselp digital platform in face-to-face meetings. Consequently, the Argentine technology company, Globant, adopted the platform and identified four nonprofits to donate its used furniture. However, the number of recipient candidates far exceeded the furniture available for donation (Fonselp.com n.d.).

Thus, there was a problem: a shortage of private sector donors and an overabundance of nonprofits in need. A company might list two computers, *“But it's two computers...then 110 nonprofits apply for those two computers.”* Matías commented, *“...imagine a situation where you bring 1,000 people to a restaurant and you only have 20 tables...the idea is the same, that I need to have more companies posting offerings.”*

### ***Fonselp Adapts to Marketplace***

Subsequently, Matías reconsidered ways to create greater shared value. Fonselp began registering nonprofits throughout Latin America. Then, Fonselp formed an agreement with Banco Santander, which adopted the platform to connect in a seamless way their 9,000+ employees with impact projects designated by the BSR area of the bank. Finally, to enhance the user experience, Fonselp began revamping the website and had a mobile App under development.<sup>1</sup>

Fonselp added the following features to version 2.0 of its digital platform:

- Companies could communicate with each other to foster matching donations, etc.
- Individuals could register in order to volunteer and track their hours, and
- Nonprofits could post donations to share resources and expertise.

---

<sup>1</sup> A new marketing landing page was available at <https://app.fonselp.com/sumarse>.

Matías also realized human resources (HR) had larger budgets than CSR at most businesses.

This led to a shift in tactics:

*“Instead of speaking to CSR departments, where maybe in Argentina there are only 200, we began speaking to HR departments. With HR, you're talking to maybe 10,000 or 20,000 or 50,000 managers...And we've adapted our message to say that by doing the volunteer work, you're boosting employee morale, reducing turnover, creating a better work environment, etc. That definitely fits in HR.”*

### **Competition Poses Threat**

Several formidable U.S. based competitors existed at the time of launch. All had established a digital media presence with blogs, Twitter, Facebook, and LinkedIn. Their websites emphasized the simplicity of the platform interface and user experience, time savings in coordinating volunteer efforts, donations, and CSR reporting, and organizational benefits of implementing CSR. The largest competitors had a strong presence with Fortune 500 companies in North America and other global markets. They included Benevity, YourCause, and Causecast.

Additionally, a recently defunct Latin American competitor had been charging \$1,000 per month to large multinationals, such as Nestlé. However, it likely failed because of the time and work required to use the platform's dashboard and enter data.

### **Fonselp's Freemium Revenue Model**

Fonselp adopted a freemium revenue model, something common among web-based services. Typically, this model offered basic services with options to upgrade to premium services (Neck, Neck & Murray 2018). Fonselp's revenue model was based on the assumption that some companies would pay a \$25/month subscription fee to track CSR performance and generate reports (see Exhibit 2). Matías was also aware that Software-as-a-Service (SaaS) business models like Fonselp were expected to have costs of goods sold equal to 10-20% of total revenue (Valchev 2016).

Matías was committed to the idea that nonprofits should not pay to receive donations. The initial fee for nonprofits was set at \$0. Other relevant alternatives originally under consideration had included an advertising revenue model (e.g. Google AdSense), a subscription revenue model, an intermediation revenue model (e.g. commission per transaction like eBay), or some combination thereof. Regardless, Matías wanted Fonselp to succeed because of the potential social impact: *“The main point is that the site is not going to fail. I will never unplug this site.”*

More recently, Matías had been approached by a consultant offering to boost Fonselp’s revenues. The terms were as follows: The consultant proposed a fixed fee of \$1,000/month, plus 50% of revenue, plus 10% equity. Although the proposal seemed one-sided, Matías was intrigued, and believed he could negotiate better terms.

### ***Startup Financing Strategy***

Like many entrepreneurs, Matías adopted a bootstrapping approach. He used proceeds from the sale of CentralPos as seed money. He spent approximately \$15,000 in the first year to get Fonselp up and running, and had another \$70,000 deposited to cover Fonselp’s operating expenses through 2019. Matías had in place a small team of investors and programmers. Fonselp’s 2017 Profit & Loss Statement showed net income of -\$15,367.91 (see Exhibit 3). Despite losses, Matías remained confident, “I can maintain the investment for four years basically, because everything on the site is automated.” Nevertheless, he recognized that an angel investor or partner who could invest another \$50,000 or more in capital might improve the platform’s functionality, and establish its financial viability.



### Fonselp Looking Ahead

Matías leaned back and smiled. He was happy with the progress so far. Fonselp was solving problems for businesses, nonprofits, and society, and simultaneously creating greater shared value. Nonetheless, Matías recognized important decisions needed to be made soon:

- How could he ensure Fonselp continued to exist beyond 2019?
- Should he seek investors or alternative startup financing?
- Should he accept the proposal from the B2B consultant?
- Would it make sense to change the Fonselp revenue model?

*As an entrepreneur, Matías had ambitions as well as fears about being a first mover. He thought to himself, “Clearly when you are an entrepreneur it is not a sprint. It’s a marathon. You have to conserve your energy and that’s what I’m doing right now. I’m building up momentum.”*

Matías then proceeded to type his reply to the consultant.

**Jacob A. Massoud**

is Associate Professor of Strategic Management in the Barowsky School of Business at Dominican University of California. He joined Dominican University of California in 2011 and teaches courses in management, including entrepreneurship, strategic management, and global consulting. His general research interests focus on social responsibility, environmental management, and broader issues of sustainability in organizations. Jacob also has a keen interest in Latin America. He speaks Spanish, and more recently learned Portuguese. Prior to entering academia, he worked professionally as the environmental director for a federally recognized American Indian tribe in El Paso, TX.

**Vafa Saboori**

is Assistant Professor of Management and Director of the MBA programs in Barowsky School of Business at Dominican University of California. He holds a Ph.D. in Manufacturing and Technology Management from the University of Toledo. He holds an MBA with a specialization in Strategic Management, and a BS in Mechanical Engineering. He was honored to receive The Barowsky School of Business Outstanding Teaching Award for the academic year 2015-2016, and Outstanding Researcher of the Year Award for the academic year 2017-2018. His main streams of research include healthcare operations and supply chain management, technological innovation, and corporate social responsibility.



**Exhibit 1. Indicators of Macroeconomic and Social Conditions in Argentina**

Source: Adapted from the Economist Intelligence Unit, World Bank Data Portal, Trading Economics, and UN Human Development Report


	2015	2016	2017	2018
<b>Exchange Rate</b>				
Argentine pesos (ARS) per US dollar	14.76	14.76	16.92	29.06
<b>Interest Rates</b>				
Lending interest rate (Average %)	24.90	31.20	26.60	45.20
<b>Inflation</b>				
Consumer prices (End Period, % Change)	26.90	41.00	24.80	44.60
GDP deflator (Index Points)	866.20	1101.00	1347.80	1887.00
<b>Unemployment</b>				
Recorded unemployment (Average %)	6.50	8.50	8.40	9.60
<b>Wages and labor costs</b>				
Monthly minimum wages (ARS)	4716.00	6060.00	8061.00	9500.00
<b>Poverty</b>				
People living below national poverty line (%)	30.00	30.30	25.70	32.20
<b>Inequality</b>				
Inequality in income (% Difference)	27.40	26.50	25.80	-
Country income inequality (Gini Index)	-	42.4	-	-
Inequality in life expectancy (%)	10.00	9.50	9.50	-
Human Development Index (HDI)	0.82	0.82	0.83	-

Exhibit 2. Fonselp Freemium Revenue Model

Source: Fonselp.com

### Prices

---




**STARTER**

I am a recurrent donor or just today I want to collaborate with the community.

**\$ 0** / month

free of charge

Check in




**PRO**

I need a tool to inform me of the contribution that my company makes to society.

**\$ 25** / month

usd

Check in



**IMPACT**

I have a great team of volunteers + staff and the excel is NOT the solution.

**CONTACT US FOR MORE INFORMATION.**

Contact

### Functions

---

	STARTER	PRO	IMPACT
Profiles of Donors and Org beneficiaries	✓	✓	✓
Create offers of donations, volunteer opportunities, pro bono, training and purchases of impact towards the social sector	✓	✓	✓
Tracking of donations to beneficiary organizations	✗	✓	✓
Tracking internal company donations	✗	✓	✓
Reports and data export	LIMITED	✓	✓
Budgeting	✗	✓	✓
Users	Max. 10	Max. twenty	UNLIMITED
Support	email	mail + chat	request

Note. Webpage translated to English by Google Chrome.

**Exhibit 3. Fonselp Profit & Loss Statement***Source: Fonselp (2018)*

January - December 2017

	TOTAL
Income	
<b>Total Income</b>	
Cost of Goods Sold	
Subcontractors - COS	3,180.25
<b>Total Cost of Goods Sold</b>	<b>\$3,180.25</b>
<b>GROSS PROFIT</b>	<b>\$ -3,180.25</b>
Expenses	
Accounting & Consulting	4,000.63
Accounting system	440.00
Advertising/Promotional	2,220.83
Bank Charges	250.73
Computer & Internet expenses	145.00
Legal & Professional Fees	280.00
Office Expenses	72.00
Promotional	135.62
Taxes & Licenses	300.00
Web Development	4,342.85
<b>Total Expenses</b>	<b>\$12,187.66</b>
<b>NET OPERATING INCOME</b>	<b>\$ -15,367.91</b>
<b>NET INCOME</b>	<b>\$ -15,367.91</b>

*Note.* Matías Laurenz invoiced work hours to Fonselp as Consulting at \$3,000/month beginning April 2018. He held a salaried job outside the company during most of 2017.

## References

- CentralPos. (n.d.). Retrieved November 4, 2018, from <https://centralpos.com/>.
- Economist Intelligence Unit. (n.d.). Retrieved November 10, 2018, from <http://country.eiu.com/argentina#>.
- Fonselp. (2018). Fonselp Profit and Loss Statement [Company report]. Argentina: Matías Laurenz.
- Fonselp. (n.d.). Retrieved November 4, 2018, from <https://fonselp.com/>.
- Jaskyte, K., & De Riobó, M. S. R. (2004). Characteristics of innovative nonprofit organizations in Argentina. *Voluntas: International Journal of Voluntary and Nonprofit Organizations*, 15(1), 71-79.
- Neck, H.M., Neck, C.P., & Murray, E. L. (2018). "Chapter 10: Creating Revenue Models." In *Entrepreneurship: The Practice and Mindset*. Los Angeles, CA: Sage.
- Torres, A. (9 August, 2018). "Entrevista completa a Matías Laurenz." *La Nación TV*. Buenos Aires, Argentina. Retrieved November 4, 2018 from <https://lnmas.lanacion.com.ar/program/video/78e6cbda-2873-42bc-ad90-5c98571d9417>.
- Trading Economics (n.d.). Retrieved November 10, 2018, from <https://tradingeconomics.com/argentina/indicators>.
- UN Human Development Report. (n.d.). Retrieved November 10, 2018, from <http://www.hdr.undp.org/en/data>.
- Valchev, K. (2016). "Cost of Goods Sold (COGS) for a Software-as-a-Service (SAAS) Business." Openview Labs. Retrieved November 10, 2018 from <https://labs.openviewpartners.com/cost-of-goods-sold-cogs-for-software-as-a-service-saas-business/#.W-eAmnpKiqB>.
- World Bank Data Portal. (n.d.). Retrieved November 10, 2018, from <https://data.worldbank.org/country/argentina?view=chart>.

## *Case Studies*



## ***PFADT RACE ENGINEERING: SUPPLY CHAIN ISSUES IMPACT THE VALUE CHAIN***

**RICHARD T. HERKO**  
Pepperdine University

Delivering on their promise to provide the most technologically advanced after-market suspension systems for the Chevrolet Corvette, Pfadt Race Engineering experienced explosive growth. Nonetheless, founders Robbin Sowinski and her husband Aaron Pfadt discovered that rapid growth had a downside. Robbin sat in their Salt Lake City, Utah office and stared at the four clocks that symbolized both the potential and the biggest potential obstacle to Pfadt's continued success. The clocks were set to local time as well as the correct time for their most-important European suppliers and the location of two key employees, currently off-site. The latest indicators signaled only minor positive changes in the economy. Was the slowing growth in sales a symptom of economic slowdown, or further evidence that the company would need to accelerate its move into other performance car products? Would Pfadt need to change its mix of suppliers to gain more flexibility?

Additional products or adding to the automobiles that Pfadt would build for would complicate operations. Already factor complicating operations was the long boat-to-train connection to Belgium for their two most critical imports: steel and precision machined parts. Costs were high, lead times were long, and delays that rippled to customer back orders were bedeviling the owners. Could Robbin and Aaron make things less complicated? Could they accept cheaper, rawer inputs and shorten delivery times?



## Industry Background

Pfadt Race Engineering operated in the \$10 billion U.S. Automobile Steering and Suspension Industry (Danova 2012). The industry included an extremely diverse group of companies making and selling shock absorbers, steering columns, steering gears, gear boxes and related parts. Although many industry players sold primarily to original equipment manufacturers (OEMs) or the major automotive companies, Pfadt was part of the “*aftermarket*,” with revenue also generated from professional racing teams. Aftermarket companies manufactured or re-manufactured part and add-ons for automobiles. Firms not associated with the major car OEMs added or modified automobiles or automotive systems. The entire industry was complementary to the automotive industry.

The market consisted of car enthusiasts who upgraded the performance of their vehicles through the installation of non-standard equipment. The industry was tracked by the Specialty Equipment Marketing Association that subdivided it into three product categories (Appearance and Accessory, Racing and Performance and Wheels, Tires and Suspension) and monitored nine sub-niches within these product segments (Knapp 2011). Pfadt chose not to participate in the entire market and focused on a few sub-niches although the industry was in a state of flux with growing numbers of domestic, U.S.-built trucks and automobiles by international firms (see Exhibits 1, 2 and 3).

While larger competitors manufactured parts for several different automobiles, Pfadt focused on two General Motors vehicles, the Corvette and the Camaro, which shared some common characteristics including passionate devotees who raced and showed off their vehicles. There were more than 1.5 million Chevrolet Corvettes on the road, having been in production since 1953. One of the most famous cars in the world, the Corvette had survived its seventh major re-design, or generation, including the 1963-67 Stingray version (2<sup>nd</sup> Generation, or “C2”) which was named the “Coolest Car of all Time” by Automobile Magazine in 2008. Estimates put the number of Camaros, which entered production in 1966, at approximately 900,000. The Camaro

had seen four re-designs in which the fifth generation was largely a re-creation of the most popular version. Pfadt produced primarily products for 1996 and newer models of the Corvette and 2010 and newer models of the Camaro.

Pfadt kept an extensive line of stock keeping units (SKUs) for both the Corvette and the Camaro, including both individual components and multiple part kits to account for the range of products under these two banners (Exhibits 4, 5, 6, and 7). In part because the true needs of its customers were unclear, Pfadt had relationships with many installers and received reports from them about which parts and kits were the most popular. That was only part of the market - many of Pfadt's customers were part of the do-it-yourself crowd. A few even had private mechanics.

The issues facing automotive aftermarket firms were nearly universal:

*"...We've identified the 90 core product/market and geographic segments, my marketing people tell me they can't develop the necessary facts to develop winning strategies because the data just aren't available..."* (Garda 1981: 18).

There were many classic and performance cars in the marketplace (Exhibit 3), but the Corvette held a special place in the hearts of so many owners, including Robbin. Robbin's family owned a succession of the cars throughout the years; her Dad drove a white 1973 Stingray. With a large and active base of collectors and racers, the Corvette was perfect for aftermarket parts. The Camaro was a good complement given its reputation among the Corvette audience. Other brands also lent themselves to the aftermarket. Dodge and Ford cars were actively collected and raced throughout the United States, but they were very different than the twin muscle cars that formed the basis for Pfadt's business model.

### Upstream Geography

Western Europe (England, France, Germany, Belgium, and Italy) was home to many of the automotive industries biggest names. Many key car components came from European companies. In addition to high-end electronic components such as Blaupunkt, Europe also supplied the auto industry and the aftermarket companies with inputs such as high-grade stainless steel and machine-crafted precision parts. ArcelorMittal, the world's largest steel manufacturer, was headquartered in Luxembourg, and its spin-off stainless steel manufacturing division, Aperam, S.A., had its main facilities in France, Belgium and Brazil. With fewer domestic sources for U.S. auto industry companies, the European companies were becoming the main source of stainless steel.

The issue for firms in the Western United States like Pfadt was that countries like Belgium were thousands of miles and several time zones away. Coordination with suppliers at this distance was problematic. Big bulky steel shipments traveled to the coast and then by boat across the Atlantic, up the Saint Lawrence Seaway to the Great Lakes, and then across the country to Salt Lake City (Exhibit 8). Salt Lake City was much less convenient than traditional regions such as the Upper Midwest (stretching from Detroit, MI through Toledo, OH and Youngstown, OH) or Southern states such as Tennessee.

While Chinese, Indian, Eastern European and Brazilian steel manufacturers were also a possibility, their lack of a premium reputation added to the language, cultural, temporal and transportation difficulties they presented. Pfadt's exacting specifications were the main reason for purchasing specialty steel from Belgium rather than from U.S. suppliers. The company experimented with purchasing steel from China but after an entire shipment proved unusable, the experiment ended.

Likewise, the calipers and other specialty-machined parts were Belgian in origin. Difficult to replicate locally, prices for these parts were largely the cost of the steel plus the cost of labor.

Labor costs varied widely by nation (Exhibit 9). Pfadt rejected buying from U.S. firms due to the high cost, but quality became an issue as well. The company had experimented with several suppliers from the U.S., South Korea, and later China, but encountered high reject rates. U.S. firms delivered parts that required scrap or re-work at 10% higher rates than the Belgian supplier. Chinese and South Korean firms delivered parts that required scrap or re-work at 30% higher rates. Pfadt looked into opportunities to source from Germany, Italy and several Eastern European nations. Finding others in the industry who had experience with suppliers from these nations was difficult, particularly from Poland and the Czech Republic where costs would have been significantly lower. Pfadt also had on-going discussions with the manufacturer of machine parts from Brazil but could never come to terms on quality.

Pfadt paid on time, was willing to wait on backlogs, and sent engineers to Belgium several times a year to discuss ways to make the partnership better. As quickly as it was growing, Pfadt was a tiny customer for the large multi-national steel supplier. Both steel and machined-parts manufacturers supplied a wide-range of industries. Customers outnumbered suppliers, and many of the customers were much larger than Pfadt.

### Downstream Geography

Western Europe had long had a racing culture that rivaled the circuits in the United States. Western Europe's emphasis was on European cars to the point of near exclusivity. Enthusiasts upgraded and raced BMWs, Fiats, Porsches and other European brands in a crowded marketplace. Some teams raced Chevrolet products as well. The vehicles were heavily modified for the highest levels for races such as the World Touring Car Championship in Germany, France, Hungary, Russia, Portugal, Slovakia, the Czech Republic, as well as the non-European countries of Argentina, Qatar, Morocco, China, Japan and Thailand. The Championship no longer traveled to the United States for a race ([www.fiawtcc.com](http://www.fiawtcc.com)).

As evidenced by their inclusion in the most prominent races, after-market performance enhancements were becoming big business in Asia and the Middle East. As wealth and car-ownership proliferated in these two regions, private and semi-professional racing increased. American muscle cars like the Corvette and Camaro were welcome along with top-of-the-market European cars. Smaller Japanese and Korean cars, often dismissed by enthusiasts, were a growing part of the after-market in Asia and were seen as fun, colorful alternatives to the muscular Americans and the stately Europeans.

Pfadt's reputation within the industry was sterling. It had clients from among the big NASCAR and Formula One teams, which helped attract amateurs. Pfadt engineers worked with teams on integrating parts, testing performance parameters, and pit rows. Formula One raced every other weekend in cities around the globe. Formula One circled the globe from Australia to Asia and Europe before hitting North America, South America and back to Asia. Typical race cities could be as large and metropolitan as Abu Dhabi and Mexico City or as out-of-the-way as Baku, Azerbaijan, or Silverstone, England.

The NASCAR schedule, in contrast, stayed entirely in the United States; it offered races almost every weekend from February to November. The schedule took the race teams to 22 different states mostly in the American South, but stretching from Southern California to New Hampshire.

The logistical and staffing commitment for Pfadt was daunting. Even though visibility with the racing teams at the highest-end of the market had created credibility with buyers (both end-users and installers), it came at a high cost to Pfadt.

Although NASCAR and open-wheel racing dominated the coverage on the major media outlets, hundreds of amateur and semi-professional racers jumped onto their motorcycles or into their modified personal autos every Friday night or weekend day. About 17% of the U.S. population participated in racing at some level (Amari 2012). These people wanted the latest innovations

in engine power and handling. Pfadt attracted a following among amateur racers whose day jobs included Olympic athletes, rock musicians, and movie stars. These clients were perfect for Pfadt as they were more concerned with performance and appearance than cost. The Western U.S. was a hotbed of driving enthusiasts year-round thanks to the climate, and hobbyists were able to locate and restore older models that had been protected from rust-inducing road salts.

The Western U.S. was a big place. Driving enthusiasts enjoyed long stretches of open roads with high speed limits (75 miles per hour in some states) and massive open spaces such as salt flats and old runways. Drivers faced little in the way of on-coming traffic or speed restrictions. Population centers were widely scattered with the exception of a few major metropolitan areas, primarily Los Angeles and its satellite of affluent communities stretching along the coast.

Only a percentage of Pfadt racing customers were able to use Pfadt's products right out of the box because most products required complicated additions or alterations to the key systems in expensive automobiles. While the movie stars and musicians could afford the Pfadt team engineers for custom installations, more than half of Pfadt's customers ordered parts that were shipped to an automotive body shop.

Pfadt used various marketing channels (see Exhibit 10), including the internet, catalogs and trade magazines, and shows with independent shops. While racing was an important proving ground and marketing tool, most of Pfadt's products were installed on '*daily-driver*' cars. These vehicles were owned by enthusiasts who liked to make performance modifications, but still drove the vehicle to work or out to dinner. Online marketing had grown in importance, so Pfadt hired a person to handle direct online sales and customer service.

The period of 2009 to 2011 was great for the company and for racing in general. New teams were formed and the biggest dilemma Pfadt faced during this period was keeping dealers happy. Individual novice customers took advantage of volume discounts to purchase Pfadt parts for resale or drop ship at dealer locations. These customers found Pfadt through the on-

line marketplace and after reading about the company in magazines dedicated to the automotive market. Being out-of-stock was a problem as the company moved backwards in the supply chain and came into competition for raw materials with international firms ten- and hundred-times its size. Transportation costs rose as Pfadt turned to European suppliers of high-grade components.

The decision to focus on the top of the market and high performance equipment led to a secondary revenue stream: the team consulted with racing teams, including on race day. Being credited by teams who had won at Daytona Racetrack opened doors. It is not unusual to find Aaron or one of the engineers on pit road or back in the garage offering tweaks and testing the parameters of Pfadt's products. Races were held around the country and in Europe which generated a lot of travel and down time for the staff. The business was lucrative both from the professional teams willing to pay for incremental advantages in power, torque or handling and the pro-am racers paying top dollar for Pfadt engineers to join their entourages.

As the brand had established cachet in racing, merchandising deals were pitched to Robbin as well. Although she thought them premature, t-shirts and toy cars emblazoned with Pfadt Race Engineering could be in the offing.

The first few months of each calendar year had typically been slow with U.S. customers from the East, Midwest and even the South focused more on digging snow out of the driveway than the toys parked in the garage. For the past several years, the slow months had allowed Pfadt to resolve back inventory issues and build inventory reserves. But sales did not accelerate over the summer months as they had done in past years and Pfadt's owners grew worried. Word of mouth was still unanimously positive, but the rate of sales growth declined. There was more traffic on Pfadt's websites from potential customers cajoling, pleading, demanding Pfadt parts for their Ford Mustangs and Dodge Chargers. The discussion boards filled with talk of European cars and the Japanese racers. Any change to servicing customers, or seeking new ones, would ripple through the organization all the way back to the decisions about inputs and staffing.



**Richard Herko**

is an Assistant Professor of Strategy at Pepperdine University, where he has taught since 2012. He teaches Strategy, Competitive Intelligence and an Integration simulation. He has more than 20 journal articles and conference papers and has been quoted by *Forbes* and NPR. He has a Ph.D. and M.B.A. from The University of Pittsburgh; a B.S. from Penn State U. and fourteen years of experience in the corporate world. He served with distinction in the United States Army and now resides in Thousand Oaks, CA with his wife, their daughter and her two cats.





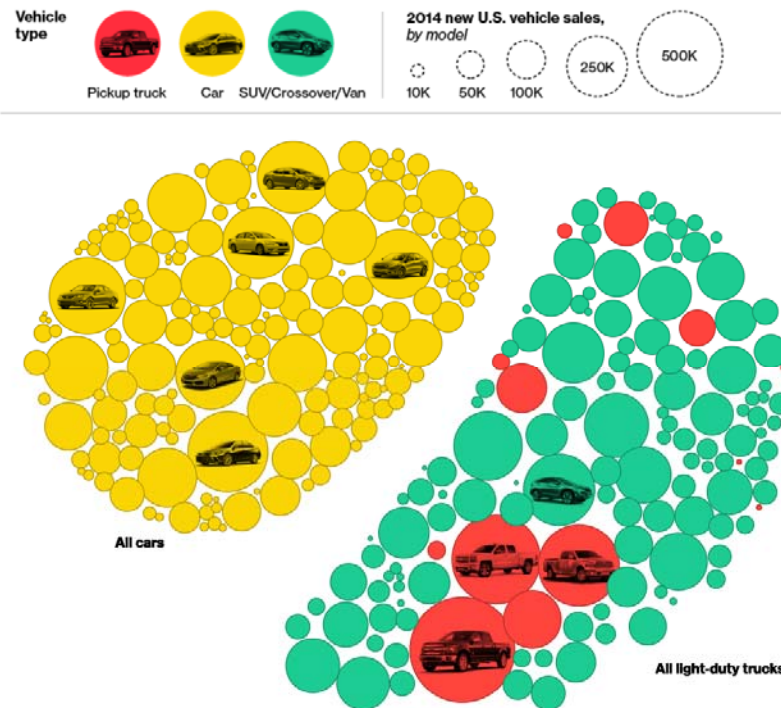
**Exhibit 1. SEMA Sector Matrix (Pfadt Race Engineering Products Indicated with X)**

Source: Automobile Magazine, 2008

	Appearance and Accessory	Racing and Performance	Wheels, Tires and Suspension
Light Truck			
Off Road			
Racing		X	X
Compact Performance			
Street Performance		X	X
Restyling			
Restoration		X	X
Custom		X	X
Other			

**Exhibit 2. New Automobile Sales Moving Towards Trucks**

Source: [www.bloomberg.com/graphics/2015-auto-sales/](http://www.bloomberg.com/graphics/2015-auto-sales/)



**Big vehicles are booming and cars aren't keeping up.**  
 Sales of light trucks grew five times faster than cars last year, increasing 10 percent compared to 1.8 percent for cars.

Since the end of the recession, sales of cars and trucks had been neck and neck: Americans bought about 39,000 more trucks than cars in 2013. But in 2014, light trucks dramatically pulled away, outselling cars by 685,000 vehicles. Sales of midsize cars, which include the typical family sedan, actually shrank 0.5 percent.

**Exhibit 3. Comparative U.S. Registrations***Source: Knapp, 2011*

<b>Registration Data for Popular Street-Performance Vehicles</b>					
	<b>1960s</b>	<b>1970s</b>	<b>1980s</b>	<b>1990s</b>	<b>2000s</b>
<b>BMW M3</b>	-	-	1,711	28,826	46,559
<b>BMW M5</b>	-	-	757	972	12,435
<b>Cadillac CTS V</b>	-	-	-	-	9,455
<b>Chevy Camaro</b>	72,406	19,309	155,304	373,981	94,024*
<b>Chevy Chevelle</b>	35,391	48,828	-	-	-
<b>Chevy Corvette</b>	21,816	114,573	146,437	167,799	286,558
<b>Chevy Nova</b>	10,811	51,707	-	-	-
<b>Dodge Challenger</b>	-	9,242	-	-	31,021
<b>Dodge Charger</b>	6,045	8,979	-	-	379,058
<b>Ford Mustang</b>	67,397	42,708	174,311	729,683	1,245,479
<b>Ford Torino</b>	-	3,029	-	-	-
<b>Infiniti G37</b>	-	-	-	-	45,614
<b>Lexus IS 200/300/350</b>	-	-	-	-	253,195
<b>Plymouth Barracuda</b>	-	7,493	-	-	-
<b>Plymouth Roadrunner</b>	4819	4785	-	-	-

**Exhibit 4. Pfadt Product Line***Source: Westcoastcorvettes.com***Coils & Shocks**

Pfadt Race Engineering designs, tests and builds coil overs and shock absorbers specifically for the Corvette, offering easy to adjust damping, ride-height flexibility, and superior quality. Our coil over and shock absorber products give your Corvette the handling performance of the super car that it is.

**Swaybars**

Professional level sway bars from Pfadt Race Engineering offer the ultimate in balance and roll-stiffness. Our lightweight, adjustable, three piece sway bars are the absolute leading the in the high-end performance market. Your Corvette will respond to turns with precision and comfort.

**Engine / Transmission Mounts**

An excellent solution for high horsepower or high-performance Corvettes, Pfadts Race Engineering's Engine and Transmission mounts reduce the massive power train shake that's common in the C5 and C6 Corvette. Put more power to the ground with our purpose built powertrain mounts.

**Silicone Radiator Hoses**

Silicone hoses from Pfadt Race Engineering withstand temperature and deterioration better than the stock rubber for a worry-free engine bay. Stainless clamps included.








**Control Arm Bushings**

Installing the Pfadt Race Engineering polyurethane control arm bushings & sleeves adds poise and responsiveness to your corvette.

[Home](#) → Pfadt Race Engineering

**Exhibit 5. A Selection of Pfadt Products**


Source: Westcoastcorvettes.com

 <p><b>Corvette Coilovers - Drag Racing FeatherLight Generation Coilovers - Pfadt Racing : 1997-2013 C5, C6 &amp; Z06</b> \$2,489.95 <a href="#">Add to Cart</a></p>	 <p><b>Corvette Rear Drag Racing Sway Bar - Pfadt Racing : 1997-2013 C5, C6 &amp; Z06</b> \$849.95 <a href="#">Add to Cart</a></p>	 <p><b>Corvette Drag Race Spherical Bearings - Pfadt Racing : 1997-2013 C5, C6, Z06</b> \$1,274.95 <a href="#">Details</a></p>	 <p><b>Corvette Racing Clutch Kit - Pfadt Racing : 2005-2013 C6 &amp; Z06</b> \$2,699.95 <a href="#">Add to Cart</a></p>
 <p><b>Corvette - Pfadt Tri-Y Header Package : 2005-2008 C6 Z51 - LS2 LS3</b> Regular Price: \$2,100.00 <b>On Sale For: \$1,890.95</b> <a href="#">Details</a></p>	 <p><b>Corvette Spherical Control Arm Bearings - Pfadt Racing : 2006-2013 Z06</b> \$1,890.95 <a href="#">Add to Cart</a></p>	 <p><b>Corvette Spherical Control Arm Bearings - Pfadt Racing : 1997-2004 C5 &amp; Z06</b> \$1,890.95 <a href="#">Add to Cart</a></p>	

**Exhibit 6: Ordering Pfadt products**

Source: Westcoastcorvettes.com


**Corvette Coilovers - Drag Racing FeatherLight Generation Coilovers - Pfadt Racing : 1997-2013 C5, C6 & Z06**

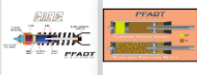


SKU: 3310  
**Manufacturer Part Number:** 1110245  
**Availability:** Usually Ships In 3-5 Days  
**\$2,489.95**

[Add to Cart](#) [Add to Wishlist](#)

**FREE Shipping!**  
 Email this product to a friend  
 Request more product info





[View Larger Image](#)

**Exhibit 7. A Video on Pfadt Racing Products**

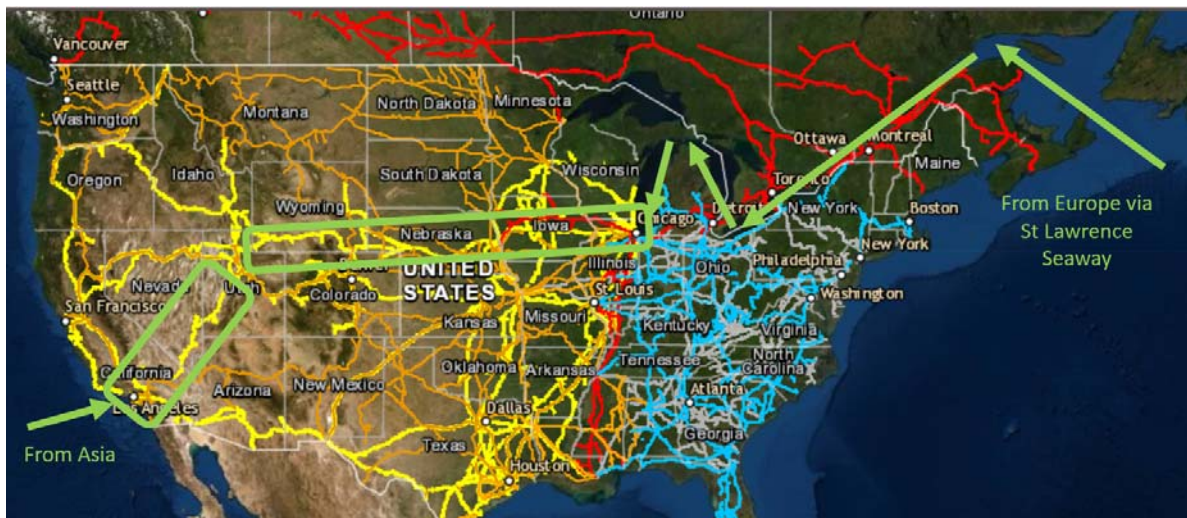
Source: [https://youtu.be/az\\_lof7\\_LEc](https://youtu.be/az_lof7_LEc)

**BOA MOUNT, THE NEW STANDARD IN CORVETTE SHOCK UPPER MOUNTING:** An idea taken directly from its much more expensive bigger brother, the Feather Light Generation DA; the new BOA mount is a no-compromises solution to Corvette shock upper mounts. Our mount is a zero-maintenance, completely sealed design that allows the FULL articulation required for the Corvette suspension. A common problem in coilover mounting for the Corvette is how to effectively mount the upper shock to the chassis without losing much shock travel and articulation. Common solutions are a clevis design that severely limits shock travel and will effect ride quality, and a "pin top" design that relies on compliance in consumable rubber bushings to deflect and bind the shock, creating an unsealed mount needing eventual replacement. The BOA MOUNT suffers none of these shortcomings as it is a solid mount similar to a control arm ball joint (quiet, durable, maintenance free), that is locked in place and then articulates with the suspension utilizing a low friction internal monoball that is sealed from the exterior elements. On top of all of this, the installation procedure could not be any easier. A simple easy to torque washer and nut retain the whole assembly. If your coilover doesn't have the BOA mount, be aware of the potential future problems. Take a look at the video to see the new BOA MOUNT in action!



**Exhibit 8. U.S. Railway System and the Sea/Rail Pathways to Salt Lake City, Utah from Europe and Asia**

Source: [Acwr.com](http://Acwr.com)



**Exhibit 9. Hourly Compensation Costs in Manufacturing, as Percent of U.S. Costs (U.S. = 100), for Selected Countries Engaged in this Industry**

Source: Conference-board.org

Belgium	47.26
Germany	43.18
Italy	32.49
South Korea	22.98
Slovakia	11.57
Czech Republic	10.71
China	9.82
Poland	8.53
Brazil	7.98

**Exhibit 10. Market Channels**

Source: Knapp, 2011

Retail Channel	Purchase Most Parts	Find Information*
Internet-Retail Store Website	24%	37%
Catalog Mail Order	21%	47%
Internet-Manufacturer’s Website	15%	61%
Internet-Auction Website (i.e. eBay...)	11%	25%
Custom Shop/Installer	8%	20%
Chain Auto Parts Store	5%	18%
Independent Parts Store/Installer	5%	17%
Internet-Classifieds	4%	19%
Car/Truck Show	3%	36%
Magazine Mail Order	2%	45%
Retail Department Store	1%	5%
Vehicle Dealership	1%	11%
Newspaper Classifieds	0%	4%

## References

- Amari, R. 2012. *IBISWorld Industry Report 71121b Racing and Individual Sports in the U.S.* IBISWorld, Inc.  
[www.arcelormittal.com](http://www.arcelormittal.com)
- Automobile Magazine*. 2008. Features: 100 Coolest Cars.  
[www.automobilemag.com/features/0410\\_coolest\\_cars/](http://www.automobilemag.com/features/0410_coolest_cars/)  
[www.bloomberg.com/graphics/2015-auto-sales/](http://www.bloomberg.com/graphics/2015-auto-sales/)  
[www.conference-board.org/ilcprogram/index.cfm?id=38269](http://www.conference-board.org/ilcprogram/index.cfm?id=38269)
- Danova, A. 2012. *IBISWorld Industry Report 33633 Automobile Steering & Suspension Manufacturing in the U.S.* IBISWorld, Inc.  
[www.fiawtcc.com](http://www.fiawtcc.com)  
[www.formula1.com](http://www.formula1.com)
- Freight rail map of class and carriers in North America  
<http://www.acwr.com/economic-development/rail-maps/class-i-freight-carriers>
- Garda, R. A. 1981. "A Strategic Approach to Market Segmentation," *McKinsey Quarterly*, 3: 16-29.
- Knapp, G. 2011. *2011 SEMA Annual Market Study*.  
[www.nascar.com/en\\_us/sprint-cup-series/schedule.html](http://www.nascar.com/en_us/sprint-cup-series/schedule.html)

## **RESUSCITATING 1-800-AUTOPSY: A LIFESPAN OF A DEATH CARE ENTERPRISE**

**STEPHEN J.J. MCGUIRE  
ANDRE S. AVRAMCHUK**  
California State University, Los Angeles

*Mortuis praesidium et vocem dare necessee est* – the deceased must be protected and given a voice. With these Latin words, Vidal Herrera defined his company’s mission and his personal vocation. Since 1974, Herrera had been involved in giving a voice to the deceased – discovering why and how their lives had ended. Since 1988, his private, mobile thanatology service had been available to families, and often the families’ lawyers, who wanted their loved ones to be given a voice just one more time. Herrera’s business journey, however, was complex.

Death has always been inevitable, but the concept of an on-call, 24-hour per day mobile autopsy service was inconceivable before 1988. Autopsy / Post Services, Inc., which did business under the trade name 1-800-Autopsy, was a thanatology specialty service company. Thanatology was the medical and legal study of death and the conditions affecting cadavers. Autopsy was widely perceived as the gold standard for determining how and why a person died. The need for autopsies had been recognized internationally in professional healthcare and forensic circles and beyond. Herrera was in his entrepreneurial “element” catering to that need. He also wondered whether he made all the right decisions along the way.

The dramatic growth in demand for private autopsies in the U.S. led to Herrera to announce in 1998 that franchises were available for 1-800-Autopsy. *“We plan to establish franchised 1-800-AUTOPSY locations in specific major cities throughout the United States ... over the next several years. Though it may sound callous, death is truly recession-resistant and the need for our*

---

The authors developed the case for class discussion rather than to illustrate either effective or ineffective handling of the situation. The case and its accompanying instructor’s manual were anonymously peer reviewed and accepted by the *Journal of Case Research and Inquiry, Vol. 5, 2019*, a publication of the Western Casewriters Association. The authors and the *Journal of Case Research and Inquiry* grant state and nonprofit institutions the right to access and reproduce this manuscript for educational purposes. For all other purposes, all rights are reserved to the authors. Copyright © 2019 by Stephen McGuire and Andre S. Avramchuk. Contact: Stephen McGuire California State University, Los Angeles, 5151 State University Dr., Los Angeles, CA 90032 [smcguir@exchange.calstatela.edu](mailto:smcguir@exchange.calstatela.edu)

*unique services will only increase...*"<sup>1</sup> As of 2019, no franchise had been established. Should Herrera abandon the idea of franchising? If so, what should he do to grow the business?

### The Rise and Decline of the American Autopsy

An autopsy is "*an invasive examination of a deceased to determine a cause and manner of death.*"<sup>2</sup> The word was derived from the Greek *autopsia*, meaning "*seeing for oneself.*"<sup>3</sup> Autopsies were performed by pathologists, specialized medical doctors who wrote and signed an autopsy report stating the cause of death and other findings. A forensic pathologist was a medical doctor who had completed 4 years of medical school plus 4 or 5 years residency in anatomic pathology. Autopsies were performed in hospitals (the "morgue"), in government laboratories under the supervision of a state, county, or city coroner, in funeral homes, and increasingly in private laboratories. Typically, the pathologist was assisted by laboratory helpers (called "dieners"), specialized autopsy technicians, and forensic photographers or videographers.

Most autopsies were performed within 48 hours of death, upon the request of the deceased's doctor or hospital, the coroner, or the deceased's immediate family. There were three main types of autopsies: complete (in which all body cavities are examined, including the head), limited (all body cavities except the head), and selective (only specific organs).<sup>4</sup> Greek physicians had employed the practice as early as 500 B.C. In 350 B.C., Egyptians used autopsies to teach anatomy and physiology, apparently sometimes on live criminals as well as corpses. In America, autopsies dated to the 1600s; an early case recorded an attempt to determine if an 8-year old girl had died of witchcraft or natural causes. A popular practice was also the autopsy of brains of deceased criminals in an attempt to discover the reasons behind their criminal behavior. In Germany in 1906, the neurologist Alois Alzheimer performed an autopsy to identify the cause of death of a woman who had suffered from confusion and memory loss. A



century later, it was still the case that Alzheimer's disease could only be definitively diagnosed by means of an autopsy.<sup>5</sup>

In 1945 in the United States, half of all deaths routinely led to an autopsy. Records showed that in 1961, 41% of deaths were followed by an autopsy. By 2019, the rate had fallen to below 5%.<sup>6</sup> In 1995, the National Center for Health Statistics, faced with budget cuts, stopped collecting autopsy statistics and compiling reports.<sup>7</sup> The best available data suggested that half of U.S. hospitals conducted autopsies on 8.5% or fewer of all deaths,<sup>8</sup> and less than 6% of non-forensic deaths.<sup>9</sup> "Many hospitals have autopsy rates at or near zero percent despite many deaths," wrote Dr. George Lundberg, a pathologist and former editor of *The Journal of the American Medical Association*.<sup>10</sup>

Why such a decline? The primary cause appeared to be financial. Hospitals generally did not charge families for autopsies and were typically not reimbursed from insurance companies, HMOs, or Medicare. On average, an autopsy cost a hospital between \$2,000 and \$4,000.<sup>11</sup> Clearly, it provided no health benefit to a patient. The autopsy was therefore a service that needed to be available but lost money for the hospital.<sup>12</sup>

Improvements in medical care and shorter in-hospital stays also led to a significant decrease in the number of patients who died in America's hospitals; more died at home, in a nursing home, or in a hospice. Moreover, some physicians believed that technological advances had made the autopsy obsolete. Tools such as computed tomography (CT scans) and magnetic resonance imaging (MRI) were routinely used in diagnostics. Medical schools had also de-emphasized the importance of autopsies. According to the National Center for Health Statistics:

*"Many medical students ... graduate with no training in autopsy procedures, no instruction on how to request permission for an autopsy, and no opportunity to view an autopsy in process or the inside of a cadaver."*<sup>13</sup>

Although the autopsy provided valuable information about the actual cause of death, in a world of escalating costs of malpractice insurance, no news was good news – at least to the doctors

and hospital who had treated the deceased. Dr. Lundberg remarked: *“Doctors, once so eager to perform autopsies that they stole bodies, have simply stopped asking.”*<sup>14</sup>

Finally, a change in hospital accreditation standards contributed to the decline of autopsies in the U.S. hospitals. The major accrediting body, the Joint Commission on Accreditation of Health Care Organizations, formerly required hospitals to perform autopsies on 20% of all patients who died in the hospital. This rate was later reduced to 15% and then abolished altogether. A Joint Commission spokesperson remarked that the organization encouraged hospitals to perform autopsies as necessary, but was focused on *“performance and not percentages.”*<sup>15</sup>

Whatever the arguments against the need for regular autopsies, research systematically revealed that autopsies detected information that had escaped the notice of physicians while the patient was alive, even with CT scans or MRIs. One specialist remarked that doctors had been *“lulled into a false sense of security”* by the advanced diagnostic tools they had at their disposal.<sup>16</sup>

A study in the *Journal of the American Medical Association* reported that doctors overlooked or wrongly diagnosed cancer in about half their patients.<sup>17</sup> A study by the Agency for Healthcare Research and Quality (AHRQ) found that the chance that autopsy would reveal a misdiagnosis (e.g., cause of death) was 10.5%. Alarming, the probability of the autopsy detecting a *major error* in a given case was 25%.<sup>18</sup> The AHRQ study suggested that medical malpractice was a major cause of *“unsuspected complications of care”*<sup>19</sup> that were only later revealed in the autopsies. A review of autopsy studies reported an even grimmer picture: in about a third of the misdiagnoses detected by autopsies, the patient would have been expected to live if proper treatment had been administered.<sup>20</sup>

Vidal Herrera had created an industry by launching the first private, for-profit, mobile thanatology service. The entrepreneurial opportunity, however, was generated by the

dramatic decline in the autopsy services provided by hospitals and government coroners' offices over the last several decades.

### Murder and Death in the U.S.A

About every 37 minutes, someone, somewhere, was murdered in the U.S.A. In 2018, an estimated 16,214 murders and non-negligent manslaughters occurred in America's large cities, of which over 1,700 were in California and more than 250 in the City of Los Angeles.<sup>21</sup>

The primary purpose of an autopsy was to determine the cause and manner of death. Forensic autopsies were typically required in every case of suspected homicide, and full or limited autopsies were requested when there was the suspicion that medical errors had caused or contributed to the death.

According to a study by Johns Hopkins, more than 250,000 people died each year in the U.S. due to preventable medical errors, America's third-leading cause of death.<sup>22</sup> On average, 12,414 medical malpractice claims were filed in the U.S. for the decade 2009 to 2018.<sup>23</sup> A trend indicated a gradual but steady decline in the number of medical malpractice lawsuits filed in U.S. courts, yet with increasingly large monetary awards to successful plaintiffs, often over one million dollars. The number of cases settled out of court was unknown, but certainly dwarfed the number actually brought to a jury. The stakes were obviously high for those who requested autopsy services.

Paradoxically, while autopsy rates had steadily declined in America, the public's awareness of autopsies and forensic techniques had dramatically increased. Popular television shows such as *CSI*, *Law and Order*, *Crossing Jordan*, *Hawaii Five-O*, *House*, and others regularly featured autopsies – more often than not showing how forensic technicians solved mysteries that

baffled the police. The cable television network HBO, for example, generated a devoted viewership to its series *Autopsy*, which followed step-by-step a forensic pathologist at work.

### The Man Called “El Muerte”

The Spanish name Vidal was derived from the Latin *vitale*, meaning “of life, vital.”<sup>24</sup> Ironically, Vidal had long been called by the nickname “*El Muerte*” (the dead one). One of seven boys, Herrera was raised alternatively by foster parents and his single mother in the Echo Park barrio of Los Angeles. As a teenager, he volunteered at the L.A. County Coroner’s Office and was later hired as a diener. He sought this macabre career for reasons that might appeal to any teenager – a friend told him that the employees in the Coroner’s Office got paid fairly well, didn’t work too hard, and had lots of “down time” between autopsies. Herrera figured such a job would allow him to study. “*Just think about it,*” he said, “*Nobody bothers you.*” Herrera attended vocational classes, and worked his way up from orderly to morgue attendant to autopsy technician, then forensic photographer, and finally forensic investigator for the Coroner.<sup>25</sup> In these roles, he participated in several cases that caught the attention of the media, including the autopsy of David Janssen (actor in “*The Fugitive*” television series), the drowning death of O.J. Simpson’s daughter, and the investigation of the victims of the “Hillside Strangler.” The “Hillside Strangler” was later discovered to be a team of cousins, Angelo Buono and Kenneth Bianchi, two psychopaths who tortured and murdered girls in Los Angeles in 1977. As a forensic investigator, Herrera was credited for finding the fingerprint that led to the conviction of serial killer Richard Ramirez, the “Night Stalker” who terrorized Los Angeles in the early 1980s. From these experiences, he learned firsthand the power of media exposure to shape public awareness and interest. Later when building his brand, he would make full use of the press and television to generate interest in his services.

Always fascinated by death, over the years “*El Muerte*” accumulated a large, macabre collection of artifacts related to death, spiced with items that clearly demonstrated his dark sense of

humor. He collected antique autopsy tools, movie posters (showing death or gruesome scenes), caskets of all shapes and sizes, finger bone pens and artery pens, plaster skulls and full skeletons, and many other objects. Mostly, the objects told the history of autopsy or poked fun at death.

Herrera worked for more than 10 years at the Los Angeles County Coroner's Office, until the day in 1984 when he lifted the corpse of a 5 foot 2 inch, 285 pound female. The result: three ruptured discs in his back, chronic pain, and confinement to a wheel chair.

After the accident, Herrera was unemployed and largely unemployable for 4 years. His back problem made him unable to remain standing for more than 15 minutes at a time. The painkillers he took led to an addiction. He ran out of money. He knew, however, that he could beat the addiction and overcome the disability if only given a chance: a decent job and a reason to stay off the pills. Desperate for work of any sort, he submitted nearly 2,000 job applications in the four-year period, all of which were rejected.

When he received the phone call from the Veterans Administration West Los Angeles Medical Center (VA) in 1988, Herrera knew he had nothing to lose. After all, he had even been rejected for the job of burger flipper at McDonald's and Jack-in-the-Box. The VA was looking for a part-time autopsy technician to work with first-year pathology residents. When asked if he knew of a competent technician, Dr. "Lucky" Lachmann of the Los Angeles County Coroner's Office remembered Vidal Herrera.

To get to the VA, without a car, leaning on a cane, and with only coins in his pocket, Herrera recalls taking three buses, and arriving exhausted – but on time for the job interview. The interview turned out to be a hands-on work session, in which he prepared the autopsy room and proceeded to train first-year pathology residents in autopsy techniques. He would be paid on a per-case basis, and would also get the opportunity to assist at autopsies outside the VA for additional fees. Herrera would soon transform this opportunity into a business.

Upon completion of his first day of work, the exhausted Herrera cleaned and sanitized the autopsy room. Without the energy to brave the L.A. metro bus system to get home, he crawled up on the autopsy table and slept in the very place where he had shown the young doctors how to dissect a cadaver. He slept, and for the first time in 4 years woke up as a man with a job and the motivation to make the most of the opportunity.

In order to assist at autopsies as a freelancer, Herrera needed the tools of the trade and a means of transportation. He borrowed the tools (scalpel, bone saw, rib cutter, skull chisel, etc.) from a doctor friend. After three cases, he was able to purchase his own set of tools and a car. Herrera recalls the joy of buying an ugly 1974 lime green Honda at the yard sale of a couple getting divorced. Little did he know at the time that he would soon be cruising the freeways of L.A. driving something much more noticeable.

In 1988, he founded Autopsy / Post Services, Inc. Herrera recalls being impressed by an article in *Forbes* about the power of 800 numbers. He remarked, *"When you watch TV, have you ever seen 1-800-DOCTOR, 1-800-LAWYER, 1-800-DENTIST? I thought, why not 1-800-AUTOPSY?"* He got the phone number he wanted and was soon conducting business under the trade name 1-800-Autopsy.

### The Private Autopsy Industry

Due to the decline in hospital-performed autopsies, families began to seek the services of external, private autopsy agencies to determine the cause of death of a loved one in the hope of getting some sense of closure. Families were often motivated by a nagging sense that the hospital or doctors did something wrong that led to the death. One report put it succinctly: *"Most for-profit autopsies have one thing in common: the family suspects something."*<sup>26</sup>

Individual pathologists and autopsy technicians, as well as firms, entered the private autopsy industry in increasing numbers in the early 1990s. While data on the size and growth of the private industry were unavailable, Herrera estimated that demand for private autopsies grew at around 10% to 15% per year. Frank Sebastian of Northwest Autopsy Services in Washington remarked, *“It’s a growth industry. We’ve seen a doubling or more of business a year. We’re filling in where the public agencies and hospitals are leaving off.”*<sup>27</sup> In 2000, Private Autopsy Services, Inc. in Oklahoma City cut the ribbon on a new \$250,000 laboratory facility.<sup>28</sup>

Pathology Support Services of Sacramento and Los Angeles ran radio advertisements to drum up business, asking, *“Do you have any questions about a loved one’s death?”*<sup>29</sup> (A list of some of the private autopsy firms that competed with 1-800-Autopsy is provided in Exhibit 2.)

Private autopsy firms, including 1-800-Autopsy, voluntarily followed the standards and protocols established by coroners and hospital pathologists, but the industry was largely unregulated. Some government and hospital pathologists had doubts about the quality of the work done by private autopsy firms. Dr. Henry Schneiderman, Chief Physician at Hebrew Home & Hospital, remarked, *“The quality of autopsies done by hospitals is very high. There is no indication that these for-profit autopsy firms are anywhere near close to that.”*<sup>30</sup> Dr. Margaret Hastings of the Institute of Medicine in Chicago also expressed concern over the quality of work carried out by the unregulated, private industry: there remained the risk that autopsies would be performed by those who *“may not have the requisite skills and may be going into it for the money.”*<sup>31</sup> The National Center for Health Statistics noted:

*“Organized, commercial autopsy service enterprises are relatively new and growing in number. How they perform and interface with medical professional guidelines and standards, facility inspections, and accreditation and certification procedures remains to be seen.”*<sup>32</sup>

**Exhibit 2. Private Autopsy Services (Sample List)**

**American Autopsy Service** in San Francisco, CA specialized in seeking answers to neurological disorders by procuring tissue samples, specifically of brain and spinal cords. It was founded by a licensed embalmer with 14 years of experience in the funeral services industry.<sup>33</sup>

**Autopsy & Forensic Service**, Chandler, AZ.

**Autopsy Pathology Division** of the Johns Hopkins Medical Laboratories in Maryland provided full private autopsy services to local, national, and international customers. The division claimed to have performed over 50,000 autopsies.

**Autopsy Pathology Services** in San Diego, CA provided private autopsy and toxicology analyses since 1997 to customers in California, Arizona, and Nevada.

**Autopsy Services LLC**, Cockeysville, MD.

**Autopsy/Diener & Removal Services LLC**, Pemberton, NJ.

**Chicago Area Autopsy Service** was founded by a diener in 1991 in Chicago. Like 1-800-Autopsy, it contracted with pathologists on a per-case basis to provide private autopsy services.

**Dieners Autopsy Services, Inc.**, Upper Marlboro, MD.

**Forensic Pathology Services** in Austin, Texas was owned and operated by a forensic pathologist and former medical examiner. It offered private postmortem examinations and expert witness services in cases of medical malpractice, negligence and wrongful death trials.

**John T. Cooper, Forensic Pathologist** provided private autopsy services and consultations in forensic pathology in Texas and nationwide.

**Northwest Autopsy Services** was a division of Emphasis Technography, Ltd., which had facilities in Tacoma, WA, Sacramento, CA, and Los Angeles. Northwest employed a board certified forensic pathologist and a private investigator; it provided autopsy services, medico-legal services, forensic consultations, and forensic technician services to families and professionals (attorneys, physicians, pathologists, coroners, hospitals and funeral homes), in the state of Washington.

**Pathology Support Services, Inc.** began providing private autopsy services in 1984, and by 2006 had offices in Los Angeles, Sacramento, Miami, Orlando, Nevada, and Texas. It claimed over 45,000 medical/legal and clinical autopsies, before it closed its doors to new cases upon the doctor's death.<sup>34</sup>

**Pacific Autopsy Services Medical**, Concord, CA.

**Pensacola Pathologists**, Fort Walton Beach, FL.

**Private Autopsy Service, LLC** in Oklahoma City was established by a board certified forensic pathologist, and provided a wide range of services similar to those provided by 1-800-Autopsy, including death investigation and expert witness testimony.

**Southeastern Autopsy Services**, Birmingham, AL.

**Tampa Pathology Laboratory** provided private autopsy services to augment the laboratory work it sold to hospitals and clinics in Florida.



## Business Strategy

From the start of Autopsy / Post Services, Inc., Vidal Herrera competed on the basis of service. The company promised customers that it would take calls immediately and provide service whenever possible within 4 to 8 hours, every day of the week, 24 hours a day. Moreover, the 1-800-Autopsy van, materials, supplies, and personnel could be quickly transported to the venue chosen for the autopsy: hospitals, morgues, laboratories, mortuaries, or funeral homes. The company promised answers: closure for the families, or perhaps evidence for a lawsuit. *"We find answers when people die unnecessarily,"* Herrera remarked. *"We are the last venue of truth for families."*<sup>35</sup>

The business was run out of Herrera's home in La Crescenta, CA. Herrera organized the cases and managed the schedule and personnel. His wife Vicki, who had never attended an autopsy and had no intention of doing so, took care of most of the administrative tasks. For a long time, autopsies were not done on company premises. 1-800-Autopsy owned a laboratory /office building in East Los Angeles, which had been converted into a thanatology museum, and was available for rent. The company used a fully functioning laboratory accredited by the College of American Pathologists.

When he founded the company, Herrera sought a prestigious address; the firm's mailing address was a rented mailbox in Brentwood, near Beverley Hills, UCLA, and the offices of many top lawyers. *"They call them 'suites' in Brentwood,"* Herrera remarked. *"It's amazing what a change in your ZIP code can do for you. Instant credibility."*<sup>36</sup> In addition to the Herrera couple, the firm employed 2 full-time autopsy technicians and 1 part-time autopsy technician; all other personnel were contracted as needed and paid on a per-case basis. About 90% of the autopsies performed were on bodies from the Los Angeles area; the remainder was flown in from other states or foreign countries, and occasionally Herrera and his team would be required to travel out of state in service.

## Services and Products

Since Vidal Herrera was not a doctor, he did not perform autopsies himself. Instead, he selected from a list of several board certified pathologists who were available on a fee-per-case basis. In effect, for its core service, 1-800-Autopsy functioned as a subcontractor to pathologists. Herrera provided the pathologist with the contact, tools, and technical and administrative support. The pathologist billed the customer directly and paid up to 50% of the fee to 1-800-Autopsy for the referral and support. The pathologist prepared and signed the official autopsy report, and as necessary (for additional fees) testified in the courtroom.

The company's price for a private autopsy ranged from \$2,000 to up to \$20,000 depending on the services provided, typically between \$2,800 and \$3,200. Specialized services such as forensic photography increased the price, and fees were higher for out of state services or when bodies needed to be transported from other states or foreign countries. A competitor, Northwest Autopsy Services, reported that its price for a complete autopsy ranged from \$2,200 to \$3,500, depending on the location.<sup>37</sup> One pathologist charged \$375 per hour, but noted that *"hourly fees have been largely replaced with a flat fee-for-service."*<sup>38</sup>

In addition to medical or forensic autopsies, the company provided a full range of thanatology services, including forensic photography and videography. 1-800-Autopsy also retrieved tissue and organs for several medical schools and research institutes, and provided support autopsy (diener) services to Los Angeles hospitals that were frequently understaffed.

Exhumation and disinterment autopsy services required the digging up a buried cadaver in order to perform an autopsy. According to Herrera, this service was difficult to perform, but highly profitable. *"It's the most time-consuming job. It's like reconstructing a crime scene. We have to photograph the gravesite, the tomb, the casket, and the body."*<sup>39</sup> Toxicology and serology analyses were performed to detect the presence or absence of drugs or chemical substances in the body of the deceased. In some cases, analyses were made to detect the

presence of asbestos or other carcinogens for the purpose of obtaining evidence in civil lawsuits. Post-mortem diagnoses were made to detect neurological diseases, HIV and AIDS, and others.

Sperm and DNA procurement were other services provided. Post-mortem DNA was collected for analysis, typically to establish paternity. In one case, Herrera collected sperm from the body of a man for the purpose of impregnating his fiancée. Because semen only remained viable in the body for 36 hours after death, being on call 24 hours per day made all the difference. At 10:30 p.m., Herrera removed the man's sexual organs and delivered them to a sperm bank in plenty of time to extract semen.

Expert services were also provided by Herrera and his pathologists to families and their lawyers in medical malpractice or wrongful death cases. Herrera obtained written endorsements from a number of prominent lawyers, including the late Johnny Cochrane (of O.J. Simpson trial fame), Carl Douglas, and Milton Grimes (who represented Rodney King), which he proudly posted on [www.1800autopsy.com](http://www.1800autopsy.com). (See Appendix A.)

Other services varied from medical appliance recycling (for example, retrieving pacemakers) to reviewing autopsy report and medical records to packing and storing cadavers to post-traumatic clean-up services (also called *“crime-scene mop-ups”*).

A small line of business that may have struck competitors as bizarre was the company's online gift shop, which Herrera called his *“Casket of Goodies.”* The 1-800-Autopsy website offered such products as skull caps and T-shirts with the company's logo, coffin cases, and items that indicated Herrera's dark sense of humor: brain gelatin molds, artery pens, skeletons (*“perfect for home, school, or office”*), and black coffin gift boxes. His CoffinCouches.com augments that with sales of furniture built with recycled coffins.

Finally, 1-800-Autopsy sold services to the Los Angeles entertainment industry. A former autopsy facility in East Los Angeles site had been transformed into a “fully dressed set,” which was rented to production companies for around \$5,000 per day. The set had been used for several movies and television series such as *Dragnet*, *Crossing Jordan*, *CSI: Miami*, *CSI: New York*, and *NCIS*. Herrera also rented morgue props to moviemakers through his *MorguePropRentals.com* and occasionally served as a consultant to scriptwriters and directors.

### Creating a Brand

Herrera cruised around Los Angeles in his mobile autopsy unit, a white van with 1-800-Autopsy prominently written on its side panels, hood, and back doors. On the driver’s door was Herrera’s nickname, “*El Muerte*.” The van’s vanity license plate was YSPOTUA, or autopsy spelled backwards. The van was fully equipped with mobile telecommunications equipment, as well as surgical instruments and attire, photography equipment, and storage and packaging containers. It was a moving advertisement; while it generated some complaints, it kept his brand in the public eye (see Exhibit 1).

#### **Exhibit 1. Vidal Herrera and the 1-800-Autopsy Van**

Source: [www.1800autopsy.com](http://www.1800autopsy.com)



Eager for the spotlight, Herrera took advantage of every available opportunity to generate interest in and news about his firm. He took advantage of opportunities for free visibility on the small screen. His business and his unique personal style were featured in over 75 newspaper and magazine articles, including the newspapers *Los Angeles Times*, *Wall Street Journal*, *New York Times*, *USA Today*, and magazines such as *Inc.*, *Entrepreneur*, *Playboy*, and *The Economist*. Some of the articles were short, others were detailed, and all of them served to increase interest in, and awareness about, his services.

His skills as a marketer did not go unnoticed; he was a runner up for *Inc.* magazine's 1997 "Marketing Masters" award.<sup>40</sup> He was invited to lecture at business schools in Los Angeles. Herrera and the company were featured on more than 20 television broadcasts, such as CNN, NBC's *Dateline*, ABC's *60 Minutes*, NBC's *Today Show*, and WB's *Making It*. Herrera remarked that every time he appeared on TV, volume peaked to such an extent that he could barely handle all the requests he got.

In 2002, Story House Productions, Inc. began following Herrera around with a camera for a series of shows for Court TV.<sup>41</sup> In 2006, documentary filmmakers associated with HBO were in the process of gathering footage for a documentary. In 2013, the *Entrepreneur* magazine profiled his unique franchise. A 2015 YouTube video showcasing Vidal and his team had over 1.5 million views (<https://www.youtube.com/watch?v=xPPq5-9k6B4>). Prime Video even offered the documentary 1-800-Autopsy starring Vidal Herrera (<https://www.amazon.com/1-800-Autopsy-Vidal-Herrera/dp/B071DNMQ1H>).

Over many years there had been a great deal of interest in the company and the entrepreneur, and many opportunities had become available to build and expand the company.

## Challenges and Opportunities

Given the decrease in hospital and state autopsies, the inevitability of death, and the high financial stakes of medical malpractice lawsuits, it was obvious that private autopsy was a growth industry. Several opportunities presented themselves to Vidal Herrera: the potential for evolutionary growth in core services, diversification of services, sale of the business, and franchising or licensing the brand to others.

Herrera had received tentative offers to sell the firm outright. The numbers thrown around in these discussions ranged from \$10 million to \$24 million, but Herrera had little interest in selling and no interest at all in getting out of the business.

Because of the many requests he received from out-of-state and even out of the country, Herrera sought a way to capture the demand outside of his core Los Angeles geography. In 1997, he first announced his intention to sell 1-800-Autopsy franchises. Articles subsequently appeared in magazines and newspapers, such as *Entrepreneur*, *Wall Street Journal*, and several California newspapers announcing the availability of a 1-800-Autopsy franchise: *"The world's first private autopsy franchise is now available."*<sup>42</sup>

In 1998, the company rented a booth at the Death Care World Expo convention, attended by funeral directors and others involved with thanatology. Herrera announced that he would offer the following services to his franchisees: *"...thorough initial and ongoing training, materials, techniques, and guidance, and methods for operating the business. An operations manual [...with] specifications, standards, checklists, and procedures to follow for nearly every conceivable [situation]."* He remarked that his booth at the convention was visited by potential franchisees from around the world, including *"Japanese businessmen interested in purchasing 11 of his franchises,"* and a group from China that expressed interest in *"approximately 20 franchises."*<sup>43</sup>

A few months earlier, a local newspaper reported that 1-800-Autopsy wanted to open “72 franchises in the United States and 16 in other countries.”<sup>44</sup> Herrera placed advertisements in business magazines nationwide, offering franchises in 24 locations.<sup>45</sup> He offered the franchise for \$30,000, not including the \$45,000 or so needed to purchase equipment.<sup>46</sup> In December 2002, the *Startup Journal* (*The Wall Street Journal*’s online center for entrepreneurs) named 1-800-Autopsy “the most unusual franchise we’ve encountered recently.” The journal reported that franchises were available for \$92,000, which would include “training, equipment and the lease of a specially equipped van with a big 1-800-Autopsy logo on each side.”<sup>47</sup>

In May 2006, he was quoted in the press as saying, “I’ve been in this business 32 years, and in the past six years we’ve seen a steady increase. That’s why we finally decided we’re going to franchise.”<sup>48</sup> He suggested that 1-800-Autopsy could expand via franchises to Orlando, then possibly New York, Chicago, Houston, Denver, Seattle and San Francisco.<sup>49</sup>

Although he made full use of the press to get out his message and his franchise offer, the 1-800-Autopsy franchise was a tough business undertaking. Not everyone was convinced that the concept would travel well. Jane Weber of Northwest Autopsy Services stated that she had heard about 1-800-Autopsy, but was unsure that the concept would catch on outside of its home market. “People used to chuckle about it. It is like, ‘Anything goes in L.A.’ That wouldn’t work so much in the northwest. It’s more conservative here.”<sup>50</sup>

Herrera considered that one of the difficulties that potential franchisees had with 1-800-Autopsy’s model was its 24-hour on-call approach; many pathologists were unwilling to be on call during odd hours. “There are no appointments for death,” he remarked. “When death happens, we need to respond regardless of the time of day or night.” The target franchisee was not, in any case, a pathologist. Herrera believed that the concept worked best when an autopsy technician organized the services and contracted pathologists on a case-by-case basis. In Orlando, a potential franchisee was a funeral director.

In spite of the conventions, press releases, advertisements, television appearances, and Herrera's many discussions with potential franchisees, by 2019 he had no franchise locations open for business. He remarked that a couple of franchisees tried but never got off the ground for various reasons, including unscrupulous business practices. He was unsure what more he needed to do to move the franchising project forward. One idea was to provide a business opportunity to returning and disabled war veterans by training them for free and waiving the usual start-up franchise fees. He remained optimistic about his company's prospects, his chosen vocation, and his life: *"This job has made me value life more, because I look at death from a different perspective. I look at how the dead can help the living."* He still did not have any shortage of local orders, and his business remained comfortably profitable. By helping the veterans in a tangible way, Herrera once again hoped to spread his message and build his business. He just wanted to know how.





**Steve McGuire**

is Professor of Management in the College of Business and Economics at California State University, Los Angeles.



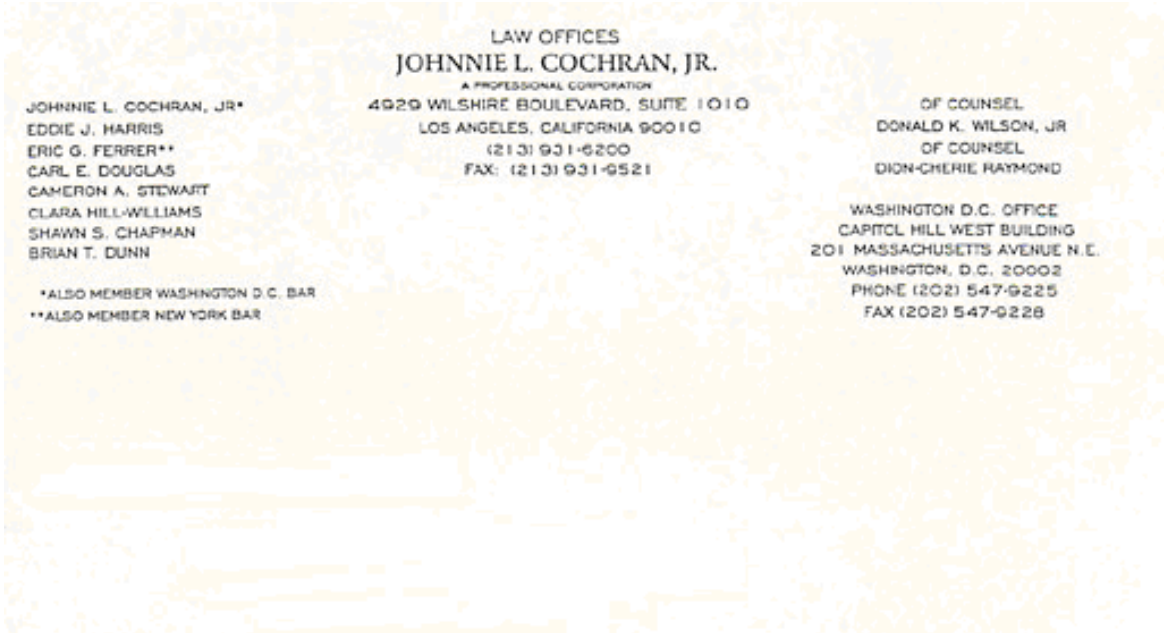
**Andre S. Avramchuk**

is Associate Professor of Management and Coordinator of the Healthcare Management program in the College of Business and Economics at California State University, Los Angeles.



Appendix A  
Letters of Endorsement from Los Angeles Lawyers

Source: [www.1800autopsy.com](http://www.1800autopsy.com)



JOHNNIE L. COCHRAN, JR.\*  
EDDIE J. HARRIS  
ERIC G. FERRER\*\*  
CARL E. DOUGLAS  
CAMERON A. STEWART  
CLARA HILL-WILLIAMS  
SHAWN S. CHAPMAN  
BRIAN T. DUNN

LAW OFFICES  
JOHNNIE L. COCHRAN, JR.  
A PROFESSIONAL CORPORATION  
4929 WILSHIRE BOULEVARD, SUITE 1010  
LOS ANGELES, CALIFORNIA 90010  
(213) 931-6200  
FAX: (213) 931-9521

OF COUNSEL  
DONALD K. WILSON, JR.  
OF COUNSEL  
DION-CHERIE RAYMOND

WASHINGTON D.C. OFFICE  
CAPITOL HILL WEST BUILDING  
201 MASSACHUSETTS AVENUE N.E.  
WASHINGTON, D.C. 20002  
PHONE (202) 547-9225  
FAX (202) 547-9228

\*ALSO MEMBER WASHINGTON D.C. BAR  
\*\*ALSO MEMBER NEW YORK BAR

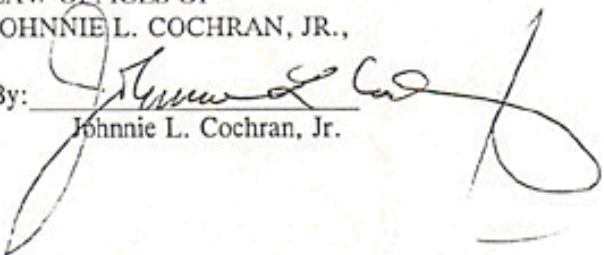
To whom it may concern:

I am writing to express my highest approval and recommendation for the services provided by Autopsy Post Services, and Videll Herrera, with whom I have worked on several cases. Throughout my dealings with Autopsy Post Services, I have found its staff to be knowledgeable, efficient, and courteous. Without fail, the autopsies and reports conducted by their independent pathologists, have been extremely well prepared and thorough, and have been highly effective in serving my clients' interests throughout the litigation process.

Do not hesitate to contact me or one of my attorneys if you would like to discuss some of the cases that we have prepared together.

Sincerely,

LAW OFFICES OF  
JOHNNIE L. COCHRAN, JR.,

By:   
Johnnie L. Cochran, Jr.

BTD dkd.apa.twc

Appendix A, cont.  
Letters of Endorsement from Los Angeles Lawyers

*law offices of Milton C. Grimes*

---

3774 WEST 54TH STREET  
LOS ANGELES, CA 90043

Phone (323) 295-3023  
Fax (323) 295-3708

RE: 1-800-autopsy

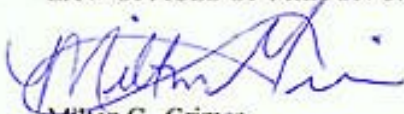
To Whom It May Concern:

In 1997, a young widow, mother of 4 small children, came to my office seeking justice when her husband was killed by police during a pursuit for suspicion of misdemeanor activity. We first contacted 1-800-autopsy when we were informed the County Coroner determined the cause of the young man's death to be heroine toxicity, yet his head and body were covered with bruises and abrasions. The medical professionals provided to our clients by 1-800-autopsy were nationally and internationally recognized as foremost experts in their specified fields. The independent autopsy revealed broken jaws, broken neck, and signs of possible strangulation and post mortem/post restraint boot imprints. The independent toxicology evaluation showed the levels of opiates were not sufficient to cause death. The medical science proved to be the greatest leverage for this family's financial recovery from such a life shattering experience.

Since then, we have continued to refer others to 1-800-autopsy as well as use them on other matters when the medical science provided by coroners are questionable and become an issue. We highly recommend 1-800-autopsy and their affiliated professionals.

Sincerely,

LAW OFFICES OF MILTON C. GRIMES



Milton C. Grimes  
Attorney at Law

MCG:te

Appendix A, cont.  
Letters of Endorsement from Los Angeles Lawyers

LAW OFFICES OF  
**CARL E. DOUGLAS**  
315 SOUTH BEVERLY DRIVE  
SUITE 305  
BEVERLY HILLS, CALIFORNIA 90212-4309  
(310) 277-9595  
FACSIMILE (310) 277-0177

Vidal Herrera  
Autopsy Post Services  
2222 Foothill Blvd., Suite E580  
La Canada, California 91011

Dear Mr. Herrera:

This letter is written to commend most highly, the services of Autopsy Post Services. As a civil lawyer who handles a range of wrongful death cases, I have found the services rendered by Autopsy Post Services to be critical to the outcome in several of my cases.

Autopsy Post Services is most often called upon to perform a needed service at a time of great personal stress and urgency for family members of a decedent and under strict guidelines and time constraints set by counsel. They are well accustomed to these situations and handle them in a professional and compassionate manner. I have found their staff to be attentive and responsive to my needs and concerns, as well as experienced, in anticipating what is required.

In many cases, only the decedent can truly tell us what happened, and how and why he or she died. Autopsy Post Services has successfully assisted me in telling that story, without which, the outcome of these cases, would surely have been different.

Very truly yours,

LAW OFFICES OF  
CARL E. DOUGLAS



Carl E. Douglas

CED:jb

**Appendix B**  
**Selected Items from the 1-800-Autopsy Online Gift Catalog**



**Skull Cap - Item#: 106**

Close fitting stretch black knit hat with roll-up cuff emblazoned with our 1800AUTOPSY on front and on the back www.1800autopsy.com.

**Price: \$ 18.00**

Quantity:



**Woman's Tank - 1-800-AUTOPSY - Item#: 102**

Black with 2 color 1-800-AUTOPSY on the anterior. 100% pre-shrunk cotton. Sizes S, M, L, XL

Please Choose

**Price: \$ 17.00**

Quantity:



**Coffin Case - Item#: 129**

Each sturdy 10" x 5" x 3 1/4" purse has a soft faux velvet interior to help your valuables rest peacefully and a removable adjustable nylon strap that will slip comfortably over your shoulder. There's even a little oval mirror on the inside. The corners are protected by metal fittings and are held closed by a sturdy latch.

**Price: \$ 28.00**

Quantity:

## Appendix B cont.

## Selected Items from the 1-800-Autopsy Online Gift Catalog

**Phrenology Head - Item#: 132**

Used in the nineteenth century to map out a persons mental characteristics just like the gypsies utilize palm reading techniques. This unique updated modern version can be used a bookend, conversation piece, etc. The revised regions of the mind are on a 7" x 3 1/2" x 3" off-white ceramic head. 46 different sayings in all.

**Price: \$ 20.00**

Quantity:


**Brain Gelatin Mold - Item#: 122**

Fill the plastic mold with a gelatin mix and a few hours later, out pops a life-size anatomically correct brain. Yes, perhaps we have sick minds to think that anyone with brains would want to eat them. Recipe included. 8.5" x 9.5" x 3.5"

**Price: \$ 11.95**

Quantity:


**Box O'Bones - Item#: 118**

Sixteen pieces snap together to form a 12" skeleton that glows in the dark. Comes apart easily and fits back into the box. Comes with a loop at the top of its head for hanging.

**Price: \$ 3.50**

Quantity:

Appendix B cont.  
Selected Items from the 1-800-Autopsy Online Gift Catalog



**Petite Pete Skeleton** - Item#: 128

This elementary-level model is flexibly wired to allow movement and positioning of the arms and legs. Perfect for home, school or office. Black plastic stand included. 8" tall.

**Price: \$ 8.95**

Quantity:



**Classic Coffin Boxes** - Item#: 131

Classic black coffin gift boxes made of heavyweight cardboard.

Quantity:



**Artery Pens** - Item#: 112

The artery pen is so comfortable to hold and compares a healthy cholesterol-free artery alongside a diseased artery, showing the harmful effects of a high fat diet. (Set of 2)

**Price: \$ 3.95**

Quantity:

## Endnotes

- 
- <sup>1</sup> Herrera, Vidal (1999). "1-800-Autopsy Provides Unique Services," *Arizona Society of Pathologists*, Dec.
- <sup>2</sup> 1-800-Autopsy promotional brochure.
- <sup>3</sup> Deathonline, [www.deathonline.net](http://www.deathonline.net). Accessed June 10, 2006.
- <sup>4</sup> Deathonline, op. cit.
- <sup>5</sup> Freedman, Danny (2006). "A Dying Art," *GW Magazine*, Summer.
- <sup>6</sup> Medscape. <https://emedicine.medscape.com/article/1705948-overview>. Accessed December 20, 2019. Also see National Center for Health Statistics (2001). "The Autopsy, Medicine, and Mortality Statistics," *Vitality and Health Statistics*, Series 3, no. 32, National Center for Health Statistics, Department of Health and Human Services. Washington, DC: U.S. Government Printing Office.
- <sup>7</sup> "National Autopsy Data Dropped From the National Center for Health Statistics Database," *The Journal of the American Medical Association*, 280(10). Extract printed on [jama.ama-assn.org/cgi/content/extract/280/10/886](http://ama-assn.org/cgi/content/extract/280/10/886). Accessed June 10, 2006.
- <sup>8</sup> National Center for Health Statistics (2001), op. cit.
- <sup>9</sup> Agency for Healthcare Research and Quality (2002). "Autopsy as an Outcome and Performance Measure. Summary, Evidence Report/Technology Assessment: Number 58." AHRQ Publication No. 03-E001. Rockville, MD: Agency for Healthcare Research and Quality.
- <sup>10</sup> American Cancer Society (1998). "Examining Autopsies: Many Cancers Missed in Original Diagnosis Are Found in Autopsies," Article date: November 6, 1998, [www.cancer.org](http://www.cancer.org). Accessed June 9, 2006.
- <sup>11</sup> American Cancer Society (1998), op. cit.
- <sup>12</sup> National Center for Health Statistics (2001), op. cit., p. 30.
- <sup>13</sup> National Center for Health Statistics (2001), op. cit., p. 30.
- <sup>14</sup> American Cancer Society (1998), op. cit.
- <sup>15</sup> Mead, Alyson (1998). "Day of the Dead," *In These Times*, April 19.
- <sup>16</sup> American Cancer Society (1998), op. cit.
- <sup>17</sup> American Cancer Society (1998), op. cit.
- <sup>18</sup> Agency for Healthcare Research and Quality (2002), op. cit.
- <sup>19</sup> Agency for Healthcare Research and Quality (2002), op. cit.
- <sup>20</sup> Anguelov, Zlatko (2001). "The Decline of the Autopsy," *Currents*, 2(3), University of Iowa Hospital and Clinics, [www.uihealthcare.com/news/currents/vol2issue3/6autopsy.html](http://www.uihealthcare.com/news/currents/vol2issue3/6autopsy.html). Accessed June 10, 2006.
- <sup>21</sup> Statista.com. <https://www.statista.com/statistics/195331/number-of-murders-in-the-us-by-state/> Accessed December 12, 2019.
- <sup>22</sup> CNBC.com, <https://www.cnbc.com/2018/02/22/medical-errors-third-leading-cause-of-death-in-america.html> Accessed December 20, 2019.
- <sup>23</sup> Rosenbaum and Associates, <https://www.rosenbaumfirm.com/medical-malpractice-statistics.html>. Accessed December 20, 2019.
- <sup>24</sup> "Behind the Name," <http://www.behindthename.com/name/vidal> Accessed January 8, 2015.
- <sup>25</sup> Anonymous (1999). "People are Dying to Work for Him," *Detour*, December 1.
- <sup>26</sup> Smock, John Marx (1997). "Traveling Autopsies Find Growth Market," *Health Care Weekly Review*, Aug. 27.
- <sup>27</sup> Dotinga, Randy (2000). "Entrepreneurs of Death: The Autopsy Business Is a Growth Industry," *APB News.com*, [www.randydotinga.com/autopsy.html](http://www.randydotinga.com/autopsy.html). Accessed June 10, 2006.
- <sup>28</sup> Dotinga, Randy (2000), op. cit.
- <sup>29</sup> Jaffe, Greg (1997). "Need An Autopsy? You Might Give Vidal Herrera a Ring," *Wall Street Journal*, July 1.
- <sup>30</sup> Jaffe, Greg (1997), op. cit.
- <sup>31</sup> Anonymous (1999). "Breathing New Life into Autopsies," *American Medical News*, March 9.
- <sup>32</sup> National Center for Health Statistics (2001), op. cit.
- <sup>33</sup> American Autopsy, [www.americanautopsy.com](http://www.americanautopsy.com). Accessed June 9, 2006.
- <sup>34</sup> Pathology Support Services, Inc., [www.pssautopsy.com](http://www.pssautopsy.com). Accessed January 10, 2015.
- <sup>35</sup> Dotinga, Randy (2000), op. cit.



- <sup>36</sup> Terry, Don (1998). "Autopsy Technician Turns Adversity and an 800 Number into Success," *New York Times*, April 20.
- <sup>37</sup> Northwest Autopsy Services, <http://www.emphasis-technography.com/nas/page3.htm>. Accessed January 8, 2015.
- <sup>38</sup> John T. Cooper Forensic Pathologist Consulting Services, [www.doccooper.com](http://www.doccooper.com) Accessed June 8, 2006.
- <sup>39</sup> Medina, Hildy (1998). "Autopsies for All Occasions," *Los Angeles Business Journal*, March 8.
- <sup>40</sup> Anonymous (1997). "1997 Marketing Masters Awards," *Inc.*, December 1.
- <sup>41</sup> Anonymous (2002). "February 2002 Production New," *iCOM*, [www.icommag.com/february2002/production-news.html](http://www.icommag.com/february2002/production-news.html). Accessed June 10, 2006.
- <sup>42</sup> Anonymous (1998). "A/PS, Inc. (1-800-AUTOPSY) Launches Autopsy Franchise," *YB News*, Sept. 1.
- <sup>43</sup> Anonymous (1998). "California Thanatologist Expands Autopsy Business Worldwide," *Death Advisor*, Feb. 1.
- <sup>44</sup> Morris, Joan (1997). "'Cadaver King' Has Turned Death into the Good L.A. Life," *Central Contra Costa Sunday Times*, Nov. 16.
- <sup>45</sup> Mead, Alyson (1998), op. cit.
- <sup>46</sup> Adamson, Deborah (1998). "Autopsies on Wheels" *Daily News*, April 3,
- <sup>47</sup> Bennett, Jule (2002). "Even Fringe Franchises Can Find a Following," *Startup Journal – The Wall Street Journal Center for Entrepreneurs*, Dec. 18, [www.startupjournal.com](http://www.startupjournal.com). Accessed June 10, 2006.
- <sup>48</sup> Fin 24 (2006). "Dial-an-autopsy," published May 25, [www.fin24.co.za/articles/business](http://www.fin24.co.za/articles/business). Accessed June 10, 2006.
- <sup>49</sup> Fin 24 (2006), op. cit.
- <sup>50</sup> Terry, Don (1998), op. cit.

## **WAS THE KRAFT HEINZ MERGER A TAXABLE ACQUISITION OR A TAX-FREE REORGANIZATION?**

**GRETCHEN LAWRIE**

California State University, Los Angeles

In 2015, H.J. Heinz Holding Corporation (Heinz Holding) acquired Kraft Foods Group, Inc. (Kraft) for over \$52 billion. Together, the companies became the Kraft Heinz Company, the third largest food and beverage company in North America and the fifth largest in the world with an estimated combined revenue of \$28 billion (Kraft Heinz Merger or Merger).<sup>1</sup>

At the time of the Merger, Kraft was a publicly traded Virginia corporation, headquartered in Northfield, Illinois and one of the largest consumer packaged food and beverage companies in North America with 22,000 employees in the United States and Canada and revenues in 2014 of \$18.2 billion. In the U.S. and Canada, it manufactured and marketed cheese, meats, coffee, packaged dinners, snack nuts, and other grocery products under various brand names, such as Kraft, Capri Sun, Jell-O, Velveeta, and Kool-Aid.<sup>2</sup>

Heinz Holding was a privately held Delaware company, headquartered in Pittsburgh, Pennsylvania owned by the multi-business conglomerate, Berkshire Hathaway, Inc. (Berkshire) and the global investment firm, 3G Capital, Inc. (3G Capital). It manufactured and marketed to over 200 countries ketchup, sauces, soups, beans, and pasta under various brand names, including Heinz, Weight Watchers Smart Ones, T.G.I. Friday's snacks, and Plasmon infant nutrition.<sup>3</sup> What were the U.S. tax and non-tax consequences of the Merger for Kraft, Heinz Holding, and their shareholders?

---

The author developed the case for class discussion rather than to illustrate either effective or ineffective handling of the situation. The case and its accompanying instructor's manual were anonymously peer reviewed and accepted by the *Journal of Case Research and Inquiry, Vol. 5, 2019*, a publication of the Western Casewriters Association. The author and the *Journal of Case Research and Inquiry* grant state and nonprofit institutions the right to access and reproduce this manuscript for educational purposes. For all other purposes, all rights are reserved to the author. Copyright © 2019 by Gretchen R. Lawrie. Contact: Gretchen R. Lawrie, California State University, Los Angeles 5151 State University Dr. Los Angeles, CA 90032, [glawrie@calstatela.edu](mailto:glawrie@calstatela.edu)

## The Companies

### ***Kraft Foods Group, Inc.***

In 1903, James L. Kraft started a wholesale cheese-distribution business in Chicago and incorporated the business in 1909 as the J.L. Kraft Bros. & Company. It opened its first cheese factory in 1914. In 1915, it began manufacturing pasteurized processed cheese and sold six million pounds of it to the U.S. Army during World War I. It went public in 1924.

### ***H.J. Heinz Holding Corporation***

In 1869, Henry J. Heinz and L. Clarence Noble formed a partnership, the Heinz Noble & Company, and began selling horseradish, vinegar, and pickles. After the partnership went bankrupt in 1875, Henry Heinz, his brother John Heinz, and his cousin Frederick Heinz formed another partnership, F & J Heinz, and began manufacturing and selling ketchup, pickles, and other condiments. In 1888, Henry Heinz bought out his brother and cousin and renamed the company H.J. Heinz Company (Heinz), which made its first public offering in 1946. In 2013, Heinz Holding acquired Heinz for over \$28 billion with Heinz's shareholders receiving \$72.50 in cash for each share of their Heinz common stock. After the acquisition, Heinz Holding became a privately held company.<sup>4</sup>

At the time of the merger of Kraft and Heinz Holding, 3G Capital owned 425 million shares or 46 percent of Heinz Holding's common stock and Berkshire also owned 425 million shares of Heinz Holding's common stock. Combined with warrants giving Berkshire the right to acquire 46 million additional shares of Heinz Holding's common stock, Berkshire controlled 51 percent of Heinz Holding's common stock.<sup>5</sup>

## Reasons for the Merger

When the Merger was announced in March 2015, Kraft's chief executive officer (CEO) and chairman of its board of directors, John Cahill, stated that the combination of Kraft and Heinz

Holding offered “...significant cash value to our shareholders and the opportunity to be investors in a company very well positioned for growth, especially outside the United States, as we bring Kraft’s iconic brands to international markets.”<sup>6</sup> About the Merger, Alexandre Behring, the chairman of Heinz Holding’s board of directors and the managing partner of 3G Capital commented that: “[b]y bringing together these two iconic companies through this transaction, we are creating a strong platform for U.S. and international growth.”<sup>7</sup>

According to Kraft’s board of directors, factors that weighed positively in favor of Kraft’s board voting in favor of the Merger were:

*“the synergies and other benefits to the combined company...including an enhanced competitive and financial position, increased diversity and depth in its product line and geographic areas... and the potential to realize... an estimated \$1.5 billion in annual cost savings from the increased scale of new organization, the sharing of best practices and cost reductions by the end of 2017.”<sup>8</sup>*

At a March 2015 presentation to investors, several reasons for the Merger were discussed including that it would create “a global powerhouse in food and beverage,” substantially improve the scale of both companies in “key North American retail and food service markets,” and allow for “potential brand expansion opportunities.”<sup>9</sup>

### Merger Timeline

At a meeting on January 25, 2015, Heinz Holding’s chairman, Mr. Behring, spoke to Kraft’s CEO, Mr. Cahill, about Heinz Holding being interested in merging with Kraft. After the meeting, both companies reviewed certain non-public information about their respective businesses. On January 29, 2015, Mr. Behring informed Kraft that Heinz Holding intended to present a formal merger proposal to Kraft.<sup>10</sup>

On February 8, 2015, Heinz Holding submitted to Kraft a formal proposal for the two companies to merge with Heinz Holding shareholders owning 53 percent and Kraft shareholders owning 47

percent of the combined company's stock and Kraft shareholders receiving a \$12.50 per share special cash dividend. After reviewing the proposal, on February 9, 2015, Kraft's board of directors decided that Heinz Holding's proposal undervalued Kraft, but agreed to continue merger discussions with Heinz Holding. On February 24, 2015, Heinz Holding proposed increasing the Kraft shareholders' interest in the combined company to 48 percent and increasing the special dividend to \$15 per share. On March 3, 2015, Kraft told Heinz that it was *"strategically interested in a potential transaction with Heinz Holding, but that the economic terms proposed by Heinz were inadequate."*<sup>11</sup>

On March 6, 2015, Mr. Behring told Mr. Cahill that Heinz Holding would increase the Kraft shareholders' ownership interest to 49 percent and increase the special dividend to \$16.50 per share for a total dividend of \$10 billion, but that this was Heinz Holding's best and final offer. On March 24, 2015, Kraft's board of directors concluded that Heinz Holding's revised offer was fair to and in the best interests of Kraft and its shareholders, and therefore it unanimously voted to approve the Merger and Merger Agreement and to recommend that Kraft's shareholders vote in favor of the Merger. Later that day, Kraft and Heinz Holding executed the Merger Agreement.<sup>12</sup>

On the following day, it was announced that Heinz Holding would be acquiring Kraft for approximately \$50 billion with Kraft shareholders owning 49 percent and Heinz Holding's shareholders, Berkshire and 3G Capital, together owning 51 percent of Heinz Holding, which was to be renamed the Kraft Heinz Company. Also, as part of the Merger, Kraft shareholders would receive a special cash dividend of \$16.50 per share of their Kraft common stock for an aggregate \$10 billion dividend and would exchange their Kraft shares for Heinz Holding common stock valued at approximately \$40 billion.<sup>13</sup>

In response to the Merger announcement, Kraft's CEO, Mr. Cahill stated that Kraft looked *"... forward to uniting with Heinz [Holding] in what will be an exciting chapter ahead."*<sup>14</sup> Heinz Holding's CEO, Mr. Hess stated,

*"We are thrilled about the unique opportunities this merger will create for our consumers worldwide, as well as our employees and business partners. Together, Heinz and Kraft will be able to achieve rapid expansion while delivering the quality, brands and products that our consumers love."<sup>15</sup>*

Additionally, Berkshire's chairman and CEO, Warren Buffett stated,

*"I am delighted to play a part in bringing these two winning companies and their iconic brands together... I'm excited by the opportunities for what this new combined organization will achieve."<sup>16</sup>*

On July 1, 2015, Kraft's shareholders voted to approve the Merger with more than 98 percent of votes cast in favor of the Merger, which was more than 69 percent of all of Kraft's outstanding shares.<sup>17</sup> About Kraft shareholders' vote, Heinz Holding's chairman, Mr. Behring stated that: *"Today's approval [by Kraft shareholders] to create the Kraft Heinz Company will unite two powerful businesses, deliver incredible shareholder value, and provide a platform for growth both domestically and internationally."<sup>18</sup>* Kraft chairman and CEO, Mr. Cahill stated that: *"This truly is a historic moment for our two companies as we combine to become a global food and beverage leader with an unparalleled portfolio of great brands."<sup>19</sup>*

### Merger Transactions

To carry out the Merger transactions, in 2015 Kite Merger Sub Corp (Kite Corp) was incorporated in Virginia as a wholly owned subsidiary of Heinz Holding, and Kite Merger Sub LLC (KM LLC) was formed in Delaware as a wholly owned subsidiary of Heinz Holding.

On June 22, 2015, Kraft declared a special cash dividend in the amount of \$16.50 per share of Kraft common stock payable to Kraft's shareholders.

On July 1, 2015, Berkshire acquired 262.9 million shares of newly issued Heinz Holding common stock for \$5.26 billion and 3G Capital acquired 237.1 million shares of newly issued Heinz

Holding stock for \$4.74 billion, for an aggregate purchase price of \$10 billion, which was used to finance the \$10 billion special dividend paid to Kraft's shareholders.

On July 2, 2015, Heinz Holding issued approximately 593 million new shares of its common stock valued at \$42.5 billion to Kraft shareholders in exchange for their shares of Kraft stock. Also, on the same day, two merger transactions occurred. In the first merger transaction, Kraft merged with and into Kite Corp, with Kraft, not Kite Corp, surviving (Merger Transaction 1). In the second transaction, Kraft merged with and into KM LLC, with KM LLC, not Kraft, surviving as a direct wholly owned subsidiary of Heinz Holding (Merger Transaction 2).<sup>20</sup>

### Post-Merger

Upon completion of the Merger, Heinz Holding had paid \$52.9 billion to acquire Kraft, of which \$42.5 billion was the total value of the Heinz Holding common stock Kraft shareholders received in exchange for their Kraft stock, \$9.8 billion was the special cash dividend Kraft shareholders received, and \$0.6 billion was the value of equity that had been issued to replace incentive service awards Kraft had awarded employees prior to the Merger. Kraft shareholders owned 49 percent, Berkshire owned approximately 26.8 percent and 3G Capital owned approximately 24.2 percent of Heinz Holding, which was renamed the Kraft Heinz Company.<sup>21</sup>

Kraft's common stock ceased to be publicly traded and was delisted from the NASDAQ. On July 6, 2015, Kraft Heinz Company's common stock began trading under the symbol "KHC" on the NASDAQ at the opening price of \$71 per share. Kraft Heinz Company's board was made up of 11 directors, with Kraft appointing five of the directors and Berkshire and 3G Capital each appointing three of the directors. Mr. Behring became the chairman of Kraft Heinz Company, Mr. Hees the CEO, and Mr. Cahill the vice chairman.<sup>22</sup>



**Gretchen Lawrie**

is Assistant Professor of Accounting at the College of Business and Economics in California State University, Los Angeles.





## Appendix A U.S. Tax Law Concepts

Source: Author's notes

### Overview

For U.S. tax purposes, the acquisition of a corporation's (Target) stock and/or assets by another corporation (Acquirer) may be treated as a taxable acquisition or a tax-deferred acquisition, commonly referred to as a tax-free acquisitive reorganization under Internal Revenue Code (IRC) § 368(a). Broadly, the term taxable acquisition means that Target is taxable upon the sale of its assets to Acquirer and Target's shareholders are taxable upon the sale of their stock to Acquirer. Whereas in a tax-free acquisitive reorganization, any taxes due on gains realized by Target, Target shareholders, or Acquirer are deferred until a subsequent event occurs, such as Target shareholders selling their Acquirer stock for cash after a tax-free reorganization.

### Taxable Stock and Asset Acquisitions

In a taxable stock acquisition, Acquirer pays cash and/or notes for Target shareholders' stock, who will recognize gain or loss equal to the difference between the amount they received for their stock and the basis of their stock (Amount received for Target stock - Target stock's basis = Target shareholders' gain or loss).<sup>23</sup> Target becomes a subsidiary of Acquirer or liquidates. Acquirer takes a cost basis in the stock it acquired from Target shareholders and the basis of Target's assets remains the same.<sup>24</sup>

In a taxable asset acquisition, Target transfers all or substantially all of its assets to Acquirer for cash and/or notes. Neither Acquirer or Target shareholders will recognize gains or losses, but Target will recognize gains or losses equal to the difference between its assets' fair market value (FMV) and the amount Acquirer paid for Target's assets and the amount of Target's liabilities Acquirer assumed (Target assets' FMV - amount Acquirer paid for Target assets - amount of liabilities assumed by Acquirer = Target's gain or loss).<sup>25</sup> Acquirer takes a cost basis in Target's assets.

### Tax-Free Reorganizations

IRC § 368 provides for several different corporate tax-free acquisitive reorganizations, in which Acquirer uses its stock with either none or a limited amount of cash and other property (together referred to as boot) to acquire Target's stock and/or assets. To be treated as a tax-free acquisitive reorganization, certain statutory and non-statutory requirements must be met.

## Appendix A, cont.

### Statutory Requirements for Tax-Free Acquisitive Reorganizations

One type of acquisitive reorganization is an IRC § 368(a) (1) (A) or Type A merger or consolidation. In a Type A merger, Target's assets and liabilities are transferred to Acquirer with Target shareholders receiving Acquirer stock or a combination of stock and a limited amount of boot and Target dissolves by operation of state law. In a Type A consolidation, both Target's and Acquirer's assets and liabilities are transferred to a newly created corporation with both corporations dissolving and their shareholders becoming shareholders in the new corporation.<sup>26</sup> If Target merges into a wholly owned subsidiary of Acquirer that is a disregarded entity, such as a limited liability company (LLC), and Target ceases to exist, the transaction qualifies a Type A merger or consolidation, because Acquirer is treated as owning its disregarded entity's assets, including Target's assets that were transferred to the subsidiary.<sup>27</sup>

In a IRC § 368(a)(1)(B) or Type B stock-for-stock reorganization, Acquirer acquires all or part of Target's stock solely in exchange for Acquirer's voting stock. Immediately after the acquisition, Acquirer must control Target, meaning that Acquirer (or its subsidiary) owns at least 80 percent of the total combined voting power of Target's stock and at least 80 percent of the number of shares in each class of Target's nonvoting stock. Target may continue as a subsidiary of Acquirer or be liquidated. If in the reorganization, Acquirer does not acquire 100 percent of Target's stock, Target shareholders will become shareholders of Acquirer.<sup>28</sup>

In a IRC § 368(a)(1)(C) or Type C stock-for-assets reorganization, Acquirer acquires substantially all of Target's assets in return for consideration consisting solely of Acquirer's voting stock or a combination of Acquirer's voting stock and up to 20 percent of boot. Then, Target liquidates by exchanging Acquirer's stock for Target shareholders' stock and distributing boot and any other remaining Target assets to Target shareholders. After the reorganization, Target ceases to exist, Target shareholders become Acquirer shareholders, and Acquirer owns Target's assets. Generally, substantially all means that the transferred assets represented at least 90 percent of the FMV of Target's net assets (i.e., assets less liabilities) and at least 70 percent of the FMV of Target's gross assets.<sup>29</sup>

In a IRC § 368(a)(2)(D) forward triangular merger, Target merges with and into Acquirer's wholly owned Subsidiary, with Subsidiary, not Target, surviving the merger. Specifically, Subsidiary transfers Acquirer's stock, cash, and other property (boot) to Target in return for substantially all of Target's assets, which Target distributes to its shareholders in cancellation of their Target stock. After the merger, Subsidiary holds both its and Target's assets, Target ceases to exist, and Target shareholders hold only Acquirer stock.

In a IRC § 368(a)(2)(E) reverse triangular merger, Target merges with and into Acquirer's wholly owned subsidiary, with Target, not Subsidiary, surviving the merger. The steps are the same as in a forward triangular merger, except Target shareholders' stock is not cancelled, but is distributed to Acquirer. After the merger, Target holds both its and Subsidiary's assets, Subsidiary ceases to exist, Acquirer holds Target stock, and Target shareholders hold only Acquirer stock.

The acquisition of a corporation's assets and/or stock can consist of two or more transactions, which, under the step transaction doctrine, may be treated for federal tax purposes as separate, independent transactions or combined together and treated as one transaction. For example, in Revenue Ruling 2001-46, 2001-2 CB 321, the Internal Revenue Service (IRS) applied the step transaction doctrine and ruled that if, under an integrated plan, a newly formed, wholly owned subsidiary of an acquiring corporation merges into a target corporation, as part of a reverse triangular merger, followed by the merger of the target corporation into the acquiring corporation, the transaction is a single statutory merger that qualifies as a tax-free Type A merger. If after a reverse triangular merger, Target merges into an LLC of Acquirer, rather than directly into Acquirer, the transaction may also be treated as a single Type A reorganization. Both of these transactions and other transactions that consist of two mergers are commonly referred to as double merger reorganizations.

## Appendix A, cont.

### Non-Statutory Requirements for Tax-Free Acquisitive Reorganizations

Besides meeting statutory requirements, a tax-free reorganization must also meet the following non-statutory requirements: 1) plan of reorganization; 2) business purpose; 3) continuity of business enterprise (COBE); and 4) continuity of interest (COI). A tax-free reorganization must be carried out pursuant to a plan of reorganization adopted by each party to the reorganization, but it does not have to be in a particular form or in writing. Other than avoiding federal income taxes, a reorganization must have a valid business purpose, such as expanding product lines, reducing administrative and other costs, or avoiding state and local taxes.<sup>30</sup> To meet the COBE requirement, Acquirer must either continue at least one significant line of Target's historical business or use a significant portion of Target's historic business assets in a business.<sup>31</sup>

For COI, Target shareholders must have a substantial equity interest in Acquirer after the reorganization, meaning that a substantial part of the value of the Target's stock must be exchanged for Acquirer's stock, which is measured by the percentage of Acquirer's stock that was used as consideration in the reorganization.<sup>32</sup> For the IRS, the COI requirement is met if, in the aggregate, Target shareholders receive and hold Acquirer stock that equals at least 40 percent of Target's outstanding stock.<sup>33</sup> However, some courts have accepted a lower percentages, such as the United States Supreme Court, which held that a target corporation's shareholders receiving 38 percent of an acquiring corporation's nonvoting preferred stock was sufficient for COI.<sup>34</sup>

### Target Shareholders' Tax Consequences

In a tax-free reorganization, Target shareholders may have a realized gain if the FMV of Acquirer's stock plus the amount of boot (cash and FMV of property) they received in the reorganization exceeds their Target stock basis (FMV of Acquirer's stock + cash + FMV of other property - Target stock basis = Target shareholders' realized gain or loss). However, they will only recognize (pay tax) on a portion of their realized gain, which is referred to as a recognized gain. The amount of their recognized gain is equal to the lesser of the boot they received or their realized gain.<sup>35</sup> For example, if Target shareholders' realized gain is \$500 and they received \$100 of boot, their recognized gain is \$100, because the \$100 of boot is less than the \$500 of realized gain.

Target shareholders' basis in their Acquirer stock equals their Target stock basis plus any recognized gain minus the amount of boot received and minus the amount of liabilities assumed by Acquirer as part of the reorganization (Target stock basis + recognized gain - boot - assumed liabilities = Target shareholders' basis in Acquirer stock). If Target shareholders held their Target stock as a capital asset, their holding period in their Target stock is tacked on to their holding period in their Acquirer stock.<sup>36</sup> Their basis in boot received from Acquirer is its FMV on the date of the exchange and the holding period for the boot begins on the date of the exchange.<sup>37</sup>

### Target's Tax Consequences

In an acquisitive reorganization, Target will not recognize gain or loss on exchanging property for Acquirer's stock, nor on distributing Acquirer's stock to Target shareholders. Target will also not recognize gain or loss on boot received as part of the reorganization, if it distributes the boot to its shareholders. But, Target will recognize gain, not loss, if it distributes to its shareholders assets that were not transferred to Acquirer (i.e., retained assets), calculated as if Target had sold the distributed property for its FMV.<sup>38</sup>

## Appendix A, cont.

### Acquirer's Tax Consequences

If Acquirer exchanges solely its stock for Target's stock and assets, Acquirer will not recognize gain or loss. However, if Acquirer also transfers other property (non-cash boot) as part of the reorganization, it will recognize gain or loss equal to the FMV of the property minus its basis.<sup>39</sup>

Acquirer's basis in Target's transferred assets equals Target's basis in those assets plus any gain recognized by Target (Target assets' basis + Target's recognized gain = Acquirer's basis in Target assets). Target's holding period in its transferred assets is tacked on to Acquirer's holding period in those assets. Acquirer's basis in Target stock it receives from Target shareholders equals their basis in their Target stock plus any gain recognized by them (Target shareholders' basis in Target stock + Target shareholders' recognized gain = Acquirer's basis in Target shareholders' Target stock). Target shareholders' holding period in their transferred Target stock is tacked on to Acquirer's holding period in those shares.<sup>40</sup>

### Tax Consequences in Forward and Reverse Subsidiary Mergers

In a forward triangular merger, Acquirer and Subsidiary will not recognize gain or loss on the use of Acquirer's stock to carry out the merger, except to the extent the Subsidiary uses Acquirer stock in the merger that it did not receive from Acquirer under the reorganization plan.<sup>41</sup> Acquirer's basis in its Subsidiary stock after the forward triangular merger equals Acquirer's basis in its Subsidiary stock plus the basis of Target's assets (Acquirer's basis in Subsidiary stock + basis of Target's assets = Acquirer's basis in Subsidiary stock).<sup>42</sup> After the merger, Subsidiary has Target's assets and its basis in Target's assets is the same as Target's basis. And, Target's holding period is tacked on to Subsidiary's holding period in those assets.

In a reverse triangular merger, Acquirer and Subsidiary do not recognize gain or loss. When Subsidiary merges into Target, its assets and their historic bases transfer to Target. After the reverse triangular merger, Acquirer's basis in Target stock equals Acquirer's basis in its Subsidiary stock plus the basis of Target's assets (Acquirer's basis in Subsidiary stock + basis of Target's assets = Acquirer's basis in Target stock).

### Tax Consequences for Acquirer's Shareholders

If Acquirer's shareholders do not participate in a tax-free reorganization involving the Acquirer, generally there is no reorganization-related tax consequences for Acquirer's shareholders. Generally, Acquirer shareholders would not realize and/or recognize gain or loss and their basis and holding period in their pre-reorganization Acquirer stock would be the same after the reorganization.

**Appendix A, cont.**

**Advantages and Disadvantages of Taxable Acquisitions and Tax-Free Acquisitive Reorganizations**

One advantage of taxable stock acquisitions is that there is only one level of tax because only Target shareholders realize taxable gain in the transaction. Two disadvantages are that all of Target's assets and liabilities are transferred in the transaction and the basis of Target's assets is not stepped up. Some of advantages of taxable asset acquisitions are that Acquirer can select specific Target's assets and liabilities, the basis of Target's assets is stepped up to the purchase price, and Target shareholders do not realize gain or loss, but Target will pay tax on any gain from selling its assets to Acquirer.

Some advantages of Type A reorganizations are that up to 60 percent of the consideration can be boot and Acquirer does not have to acquire substantially all of Target's assets. Two disadvantages are that by operation of law, Acquirer must assume all of Target's liabilities and some states require that both Acquirer's and Target's shareholders approve the reorganization. Although in Type B reorganizations, Target's liabilities can remain in a subsidiary and there is no substantially all requirement, the only allowable consideration is Acquirer's voting stock. Some of the advantages of Type C reorganizations are that Target's liabilities can remain in a subsidiary and up to 20 percent of the consideration can be boot. Also, even though Acquirer must acquire substantially all of Target's assets, Acquirer can select specific Target assets.

Although in both types of triangular mergers substantially all of Target's assets must be acquired, Target's liabilities can remain in the surviving entity (either Acquirer's Subsidiary or Target), and Acquirer's shareholders do not have to approve the merger. Even though boot can be used in both types of triangular mergers, the amount of boot in a forward triangular merger can be up to 50 percent, but only up to 20 percent in a reverse triangular merger.

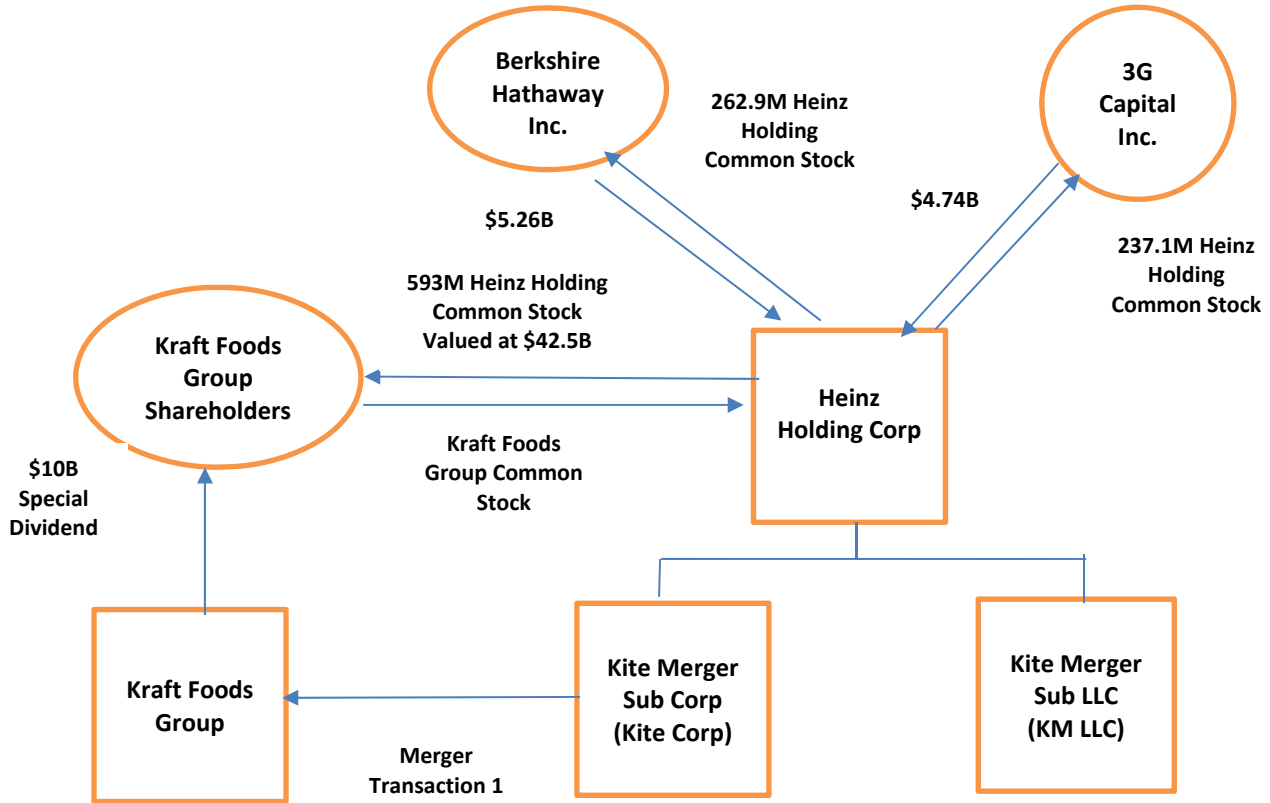
## Appendix B Merger Timeline

*Source: Author's notes*

DATE	EVENT
1/25/2015	At a meeting, Heinz Holding chairman Alexandre Behring spoke to Kraft CEO John Cahill about Heinz Holding being interested in merging with Kraft.
1/29/2015	Mr. Behring informed Kraft that Heinz Holding intended on presenting a formal merger proposal to Kraft.
2/8/2015	Heinz Holding submitted to Kraft a formal proposal for the two companies to merge with Heinz Holding shareholders owning 53% and Kraft shareholders owning 47% of the combined company's stock and Kraft shareholders receiving a \$12.50 per share special cash dividend.
2/9/2015	Kraft's board of directors informed Heinz Holding that its proposal undervalued Kraft but would continue to discuss merging with Heinz Holding.
2/24/2015	Heinz Holding proposed increasing the Kraft shareholders' interest in the combined company to 48% and increasing the special dividend to \$15 per share.
3/6/2015	Mr. Behring told Mr. Cahill that Heinz would increase the Kraft shareholders' ownership interest to 49 percent and increase the special dividend to \$16.50 per share.
3/24/2015	Kraft's board of directors unanimously voted to approve the merger of Kraft and Heinz Holding (Kraft Heinz Merger or Merger) and to recommend that Kraft's shareholders vote in favor of the Merger.
3/24/2015	Kraft and Heinz Holding executed the Merger Agreement.
3/25/2015	The Merger was publicly announced.
6/22/2015	Kraft declared a special cash dividend in the amount of \$16.50 per share of Kraft common stock payable to Kraft's shareholders.
7/1/2015	Kraft's shareholders voted to approve the Merger.
7/1/2015	Berkshire acquired 262.9 million shares and 3G Capital acquired 237.1 million shares of newly issued Heinz Holding common stock for a combined purchase price of \$10 billion.
7/2/2015	In exchange for their Kraft shares, Heinz Holding issued over 593 million shares of its common stock valued at \$42.5 billion to Kraft shareholders.
7/2/2015	In Merger Transaction 1, Kraft merged with and into Kite Merger Sub Corp (Kite Corp) with Kraft, not Kite Corp, surviving. Then in Merger Transaction 2, Kraft merged with and into Kite Merger Sub LLC (KM LLC), with KM LLC, not Kraft, surviving as a subsidiary of Heinz Holding.

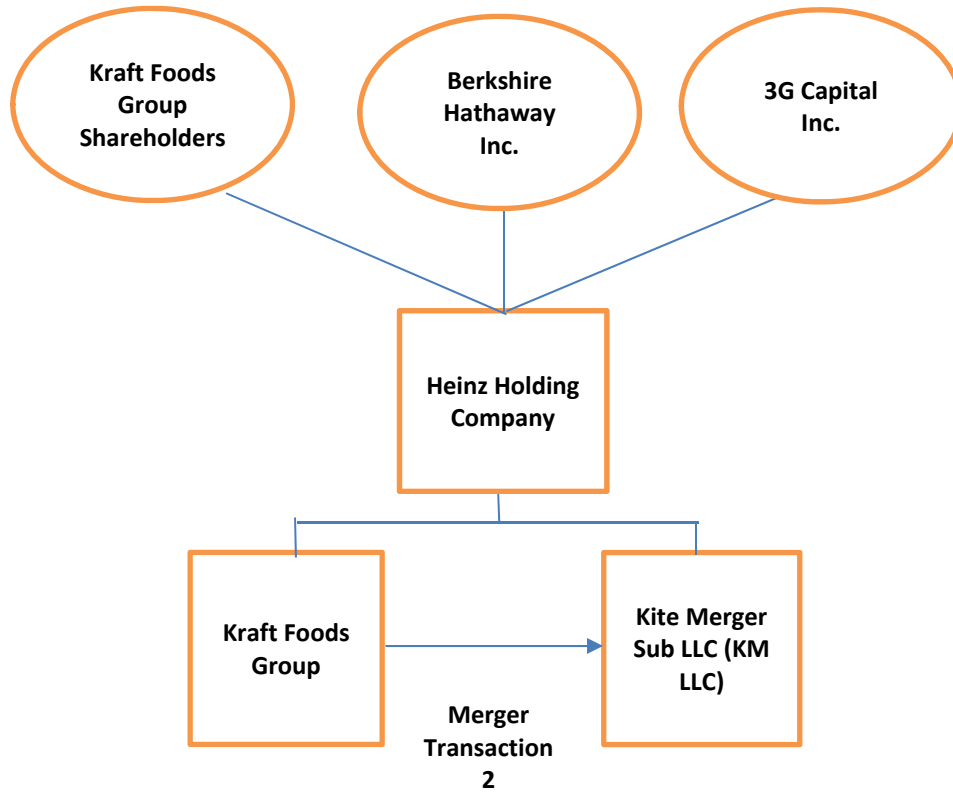
### Appendix C Merger Transaction 1

Source: Author's notes



**Appendix D**  
**Merger Transaction 2**

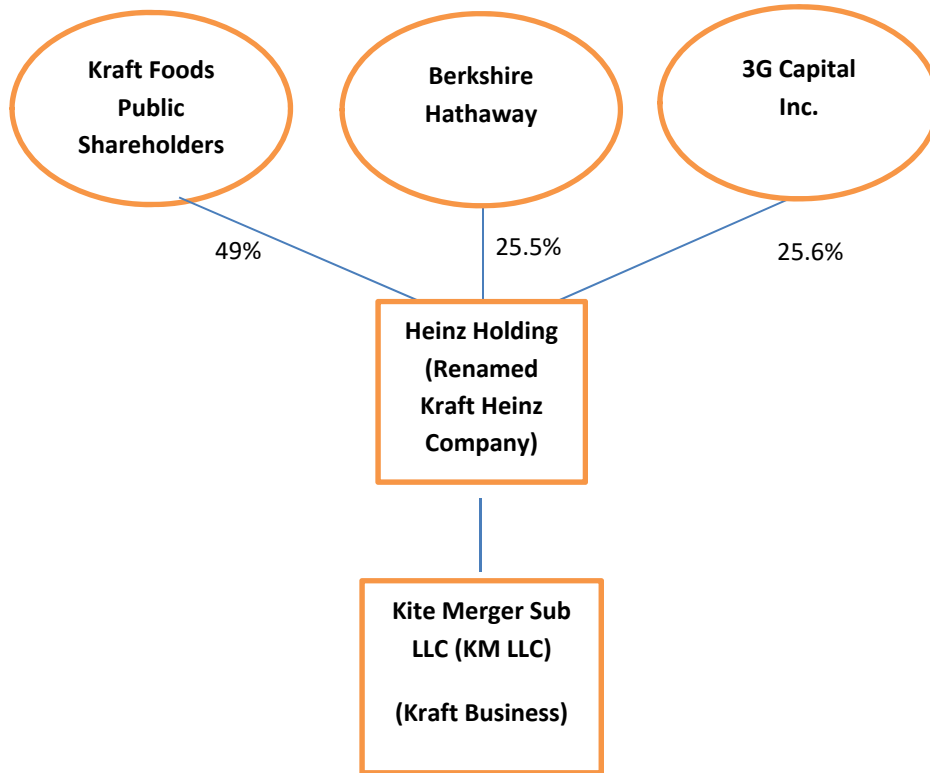
*Source: Author's notes*





**Appendix E  
Post- Merger**

Source: Author's notes



## Endnotes

- <sup>1</sup> Kraft Foods Group, Inc. H.J. Heinz Company and Kraft Foods Group Sign Definitive Merger Agreement To Form The Kraft Heinz Company, Press Release (March 25, 2015) (Kraft Press Release (March 25, 2015)).
- <sup>2</sup> Kraft Foods Group, Inc. United States Securities and Exchange Commission Form S-4 Registration Statement, Proxy Statement and Prospectus (June 2, 2015) (Kraft Proxy); Kraft Press Release (March 25, 2015).
- <sup>3</sup> *Id.*
- <sup>4</sup> Kraft Proxy; H.J. Heinz Company, United States Securities and Exchange Commission Form 10-K: Annual report for transition period from April 29, 2013 to December 29, 2013 (March 2014).
- <sup>5</sup> Kraft Proxy.
- <sup>6</sup> Kraft Press Release (March 25, 2015).
- <sup>7</sup> *Id.*
- <sup>8</sup> Kraft Proxy, p. 61.
- <sup>9</sup> Kraft Foods Group, Inc. and H.J. Heinz Holding Corporation, Creating a Global Food & Beverage Leader, Investor Presentation (March 25, 2015).
- <sup>10</sup> Kraft Proxy.
- <sup>11</sup> Kraft Proxy, p. 58.
- <sup>12</sup> Kraft Proxy; Kraft Press Release (March 25, 2015).
- <sup>13</sup> *Id.*
- <sup>14</sup> Kraft Press Release (March 25, 2015).
- <sup>15</sup> *Id.*
- <sup>16</sup> *Id.*
- <sup>17</sup> Kraft Press Release (June 9, 2015).
- <sup>18</sup> *Id.*
- <sup>19</sup> *Id.*
- <sup>20</sup> Kraft Heinz Company, United States Securities and Exchange Commission Form 10-K: Annual report for fiscal year ending on January 3, 2016 (March 2016) (Kraft Heinz Company Form 10-K (2016)); Berkshire Hathaway Inc., United States Securities and Exchange Commission Form 10-K: Annual report for fiscal year ending on December 31, 2015 (February 2016). (BHC Form 10-K 2016).
- <sup>21</sup> Following the Merger, the total amount of Kraft Heinz Company's outstanding common stock was approximately 1.2 trillion shares (Kraft Heinz Company Form 10-K (2016)). BHC Form 10-K (2016)
- <sup>22</sup> Kraft Proxy; Kraft Press Release (March 25, 2015); Kraft Heinz Company Form 10-K (2016).
- <sup>23</sup> 26 USC § 61(a)(3).
- <sup>24</sup> 26 USC § 1012.
- <sup>25</sup> 26 USC §§ 61(a)(3) and 1001.
- <sup>26</sup> Treas. Reg. § 1.368-2(b)(1)(ii).
- <sup>27</sup> Treas. Reg. § 1.368-2(b)(1)(iii) Ex. 2.
- <sup>28</sup> 26 USC § 368(c); Treas. Reg. § 1.368-2(c).
- <sup>29</sup> Rev. Proc. 77-37, 1977-2 C.B. 568.
- <sup>30</sup> Treas. Reg. §§ 1.368-1(c), 1.368-2(g), and 1.368-3(a).
- <sup>31</sup> Treas. Reg. § 1.368-1(d).
- <sup>32</sup> Treas. Reg. § 1.368-1(e).
- <sup>33</sup> Treas. Reg. § 1.368-1(e)(2)(v) Ex 1.
- <sup>34</sup> *John A. Nelson Co. v. Helvering*, 296 US 374 (1935).
- <sup>35</sup> 26 USC §§ 354 and 356.
- <sup>36</sup> 26 USC § 1223(1).
- <sup>37</sup> 26 USC §§ 358 and 1223(1).
- <sup>38</sup> 26 USC §§ 361 and 1032.
- <sup>39</sup> 26 USC §§ 361, 1001 and 1032; Rev. Rul. 72-327, 1972- CB 197.
- <sup>40</sup> 26 USC §§ 362, 1223(1) and 1223(2).
- <sup>41</sup> Treas. Reg. § 1.1032-2.
- <sup>42</sup> Treas. Reg. § 1.358-6.

## ***WAS THE ACQUISITION OF H.J. HEINZ COMPANY BY BERKSHIRE HATHAWAY & 3G CAPITAL A TAXABLE TRANSACTION?***

**GRETCHEN LAWRIE**

California State University, Los Angeles

In 2013, the ketchup company known for the slogan “57 Varieties,” the H.J. Heinz Company (Heinz), was a publicly traded Delaware company headquartered in Pittsburgh, Pennsylvania. It manufactured ketchup, sauces, soups, beans, and pasta under various brand names, including Heinz, T.G.I. Friday’s snacks, Plasmon infant nutrition, Lea & Perrins Worcestershire sauce, and Classico pasta sauce. Its profit in 2012 was over \$900 million on revenues of over \$11 billion and it employed more than 30,000 people.<sup>1</sup>

In 2013, Heinz was acquired for over \$28 billion by an investment consortium comprised of Berkshire Hathaway, Inc. (Berkshire) and the global investment firm, 3G Capital Partners Ltd. (3G Capital) (Heinz Merger or Merger). After the Merger, Heinz became a subsidiary of a newly created company controlled by Berkshire and 3G Capital, the H.J. Heinz Holding Corporation (Heinz Holding).<sup>2</sup>

What were the U.S. tax and non-tax consequences of the Merger for Heinz, Heinz Holding, and their shareholders?

---

The author developed the case for class discussion rather than to illustrate either effective or ineffective handling of the situation. The case and its accompanying instructor’s manual were anonymously peer reviewed and accepted by the *Journal of Case Research and Inquiry, Vol. 5, 2019*, a publication of the Western Casewriters Association. The author and the *Journal of Case Research and Inquiry* grant state and nonprofit institutions the right to access and reproduce this manuscript for educational purposes. For all other purposes, all rights are reserved to the author. Copyright © 2019 by Gretchen R. Lawrie. Contact: Gretchen R. Lawrie, California State University, Los Angeles 5151 State University Dr. Los Angeles, CA 90032, [glawrie@calstatela.edu](mailto:glawrie@calstatela.edu)

## Companies

### ***H.J. Heinz Company***

In 1869, Henry J. Heinz and L. Clarence Noble formed the partnership, Heinz Noble & Company, and began selling horseradish, vinegar, and pickles. After the company went bankrupt in 1875, Henry Heinz, his brother, John Heinz and their cousin, Frederick Heinz founded the partnership of F & J Heinz and began manufacturing and selling ketchup, pickles, and other condiments. In 1896, Heinz began using the slogan, “57 Varieties.”

In 1888, Henry Heinz bought out his brother and cousin and renamed the company H.J. Heinz Company (Heinz), which was incorporated in 1900. In 1946, Heinz made its first public offering at \$25 per share on the New York Stock Exchange (NYSE) under the symbol “HNZ”.

Heinz was known for supporting various charitable and philanthropic causes in Pittsburgh and other communities. For example, in 1951, the H.J. Heinz Company Foundation (Heinz Foundation) was founded and funded by Heinz to promote the health and nutritional needs of children and families with priority given to programs and organizations in communities where Heinz operated. In 2010 and 2011, the Heinz Foundation contributed \$12.8 million to various Pittsburgh charities including the Greater Pittsburgh Community Food Bank, the Extra Mile Education Foundation, and Brother’s Brother Foundation.<sup>3</sup>

### ***Berkshire Hathaway Inc.***

In 1839, Oliver Chance founded the textile manufacturing company, Valley Falls Company, which in 1929 merged with Berkshire Cotton Manufacturing Company and was renamed Berkshire Fine Spinning Associates. In 1955, Berkshire Fine Spinning merged with Hathaway Manufacturing Company becoming Berkshire Hathaway Inc. (Berkshire).

At the time of the Heinz Merger, Berkshire was a publicly traded, conglomerate holding company headquartered in Omaha, Nebraska and was engaged in various business activities,

including property and casualty insurance and reinsurance, utilities and energy, freight rail transportation, finance, manufacturing, and retailing.<sup>4</sup> In 2013, Berkshire's earnings were approximately \$18 billion on total revenue of over \$182 billion.

Berkshire's well known chief executive officer (CEO) and chairman, Warren E. Buffett, began buying in 1962 stock in Berkshire and eventually acquired enough stock to take control of Berkshire.

### ***3G Capital Partners Ltd***

In 2004, Alex Behring, Jorge Paulo Lemann, Carlos Alberto Sicupira, Marcel Herrman Telles, and Roberto Thompson Motta founded the private investment firm, 3G Capital. 3G Capital had acquired and invested in numerous companies, such as Burger King in 2010 for \$3.3 billion.<sup>5</sup> 3G Capital was known implementing zero-based budgeting for the companies it had acquired.<sup>6</sup>

### **Merger Timeline**

In early December 2012, Jorge Paulo Lemann, partner and co-founder of 3G Capital, met with Berkshire's CEO and chairman, Warren Buffett, and proposed that 3G Capital and Berkshire jointly acquire Heinz. Following the meeting, Mr. Buffett informed Mr. Lemann that Berkshire was interested in acquiring Heinz and would be willing to provide equity financing for a potential acquisition.

On December 13, 2012, the chairman, president, and CEO of Heinz, William R. Johnson, was asked by representatives of 3G Capital's financial advisor, Lazard Freres & Co., LLC, to meet with 3G Capital in order to "*share their views on the food and beverage industry.*"<sup>7</sup> At a dinner meeting on December 18, 2012, Mr. Johnson discussed with Mr. Lemann and the managing partner of 3G Capital, Alexandre Behring, the food and beverage industry, potential industry

consolidation, and their respective businesses. They agreed to meet in 2013 to continue their discussion.

At a meeting on January 10, 2013, Mr. Behring told Mr. Johnson that, together with Berkshire, 3G Capital (the Acquirers) was interested in discussing the potential acquisition of Heinz and intended on making a proposal to acquire Heinz. Mr. Johnson stated that Heinz was not for sale, but that he would inform Heinz's board of directors of their discussion and would present any acquisition proposal to the board.

On January 14, 2013, Berkshire and 3G Capital delivered a joint letter to Mr. Johnson proposing to acquire all of Heinz's outstanding shares of common stock for \$70 in cash per share. After Heinz's board of directors deliberated about the Acquirers' proposal, on January 16, 2013, Mr. Johnson contacted Mr. Behring and told him that Heinz was considering the proposal, but that Heinz had made no decision about the proposal or whether to authorize further discussions.

On January 21, 2013, Heinz's board directed Mr. Johnson to inform the Acquirers that it was unlikely to authorize further merger discussions unless the Acquirers improved the financial terms of their proposal. On January 24, 2013, the Acquirers' increased their offer to \$72.50 in cash per share of Heinz common stock, which was a premium of 19.6 percent on Heinz's closing share price on that day of \$60.64. At its January 30, 2013 meeting, Heinz' board *"unanimously concluded that the [Acquirers'] revised proposal represented an attractive opportunity compared to other available alternatives (including remaining a standalone company) and that it would be in the best interest of Heinz shareholders and other constituencies to continue discussions with [Acquirers]"* and authorized further discussions with Acquirers.<sup>8</sup>

After several weeks of further negotiations, on February 13, 2013, Heinz's board of directors voted unanimously to approve the Merger and to recommend that Heinz shareholders vote to approve the Merger.<sup>9</sup>

Several factors Heinz's board of directors considered potentially positive about the Merger were:

1. the \$72.50 per share offer exceeded Heinz's likely value as a standalone company;
2. it was unlikely that other buyers would be willing to acquire Heinz at a price in excess of the \$72.50 per share offer, even if Heinz conducted an auction process or solicited other alternative acquisition proposals;
3. the Merger consideration was solely cash;
4. Heinz's headquarters would remain in Pittsburgh;
5. Heinz's heritage and the name H.J. Heinz Company would be preserved;
- and
6. Heinz's support for charitable and philanthropic causes in Pittsburgh and other communities would continue.<sup>10</sup>

Several potentially negative factors of the Merger that the board considered were that:

1. Heinz would no longer exist as an independent, public company;
2. Heinz's shareholders would not be able to participate in any value creation that Heinz could generate in the future and/or in any future appreciation in the value of Heinz;
3. Heinz had not solicited proposals from other potential buyers;
- and
4. The Merger consideration would be taxable to Heinz's shareholders.

On February 13, 2013, Heinz entered into a definitive merger agreement to be acquired by Berkshire and 3G Capital with each Heinz shareholder receiving \$72.50 per share or a total of \$23 billion. With Berkshire and 3G Capital also agreeing to assume Heinz's outstanding debt, the Merger was valued at \$28 billion. Berkshire and 3G Capital agreed to maintain Heinz's headquarters in Pittsburgh, preserve Heinz's heritage, support Heinz's philanthropic and charitable causes in Pittsburgh, and honor Heinz's obligations under the naming rights and promotion agreement relating to Heinz Field, a professional baseball stadium located in Pittsburgh.<sup>11</sup>

In response to the public announcement of the Merger on February 14, 2013, Heinz CEO, Mr. Johnson stated that: "[t]he Heinz brand is one of the most respected brands in the global food industry and this historic transaction provides tremendous value to Heinz shareholders" and that Heinz looked "... forward to partnering with Berkshire Hathaway and 3G Capital ... in what will be an exciting new chapter in the history of Heinz."<sup>12</sup> Berkshire CEO, Mr. Buffet stated that

Berkshire was “very pleased to be a part of this partnership” and that Heinz had “... strong, sustainable growth potential based on [its] high quality standards, continuous innovation, excellent management and great tasting products.”<sup>13</sup>

Concerning the Merger, 3G Capital partner Mr. Behring stated that 3G Capital had “... great respect for the Heinz brands and the strong business that management and its employees operate around the world” and recognized “Heinz’s value and heritage.”<sup>14</sup> He also stated that the Merger would provide “...tremendous value to Heinz shareholders” and that as a private company, Heinz would “...have an opportunity to drive further growth and advance [its] commitment to providing consumers across the globe with great tasting, nutritious and wholesome products.”<sup>15</sup>

At a special shareholders meeting held on April 30, 2013, Heinz shareholders voted to approve the Merger with approximately 95 percent of the votes cast voting in favor of the Merger, which represented approximately 60 percent of Heinz’s total outstanding common stock.<sup>16</sup>

To carry out the Merger, several entities were formed including Hawk Acquisition Holding Corp (Hawk Holding) and its wholly owned subsidiaries: 1) Hawk Acquisition Sub, Inc. (HA Subsidiary); 2) Hawk Acquisition Intermediate Corporation I (HA I); and 3) Hawk Acquisition Intermediate Corporation II (HA II). As part of the Merger, Berkshire and 3G Capital each purchased for \$4.12 billion 425 million shares of Hawk Holding’s common stock. Berkshire also purchased shares of Hawk Holding’s 9 percent preferred stock for \$8 billion and warrants to purchase approximately 46 million additional shares Hawk Holding common stock.

On June 7, 2013, Heinz merged with and into HA Subsidiary, with Heinz surviving as an indirect, wholly-owned subsidiary of Hawk Holding Corporation, which was renamed the H.J. Heinz Holding Corporation (Heinz Holding).<sup>17</sup> Heinz’s shareholders received \$72.50 in cash for each share of their Heinz common stock. With the assumption of Heinz’s outstanding debt, the total Merger consideration was approximately \$28.75 billion.<sup>18</sup>



In response to the June 7, 2013 announcement that the Merger had been completed, the new CEO of Heinz, 3G Capital partner Bernardo Hees stated that he looked “... *forward to building upon Heinz’s incredible platform and delivering world-class products for all of our consumers around the world, while maintaining... [Heinz’s] unwavering commitment to quality, safety and superior customer service.*”<sup>19</sup> Former Heinz CEO Mr. Johnson became a part-time advisor to Mr. Hess on certain specific industry and strategic non-operating matters.<sup>20</sup>

After the Merger, Heinz’s common stock ceased to be publicly traded and was delisted from the NYSE.



**Gretchen Lawrie**

is Assistant Professor of Accounting at the College of Business and Economics in California State University, Los Angeles.



## Appendix A U.S. Tax Law Concepts

Source: Author's notes

### Overview

For U.S. federal tax purposes, the acquisition of a corporation's (Target) stock and/or assets by another corporation (Acquirer) may be treated as a taxable acquisition or a tax-deferred acquisition, commonly referred to as a tax-free acquisitive reorganization under Internal Revenue Code (IRC) § 368(a). The term taxable acquisition means that Target is taxable upon the gain realized on sale of its assets to Acquirer and that Target's shareholders are taxable upon the gain realized on the sale of their stock to Acquirer. Whereas in a tax-free acquisitive reorganization, taxes due on gains realized by Target, Target shareholders, and/or Acquirer are deferred until a subsequent event, such as Target shareholders selling their Acquirer stock for cash after a reorganization.

### Taxable Stock and Asset Acquisitions

#### **Types of Taxable Stock and Asset Acquisitions**

There are several different types of taxable acquisitions including: 1) direct stock sales; 2) direct asset sales; 3) cash mergers; 4) forward subsidiary cash mergers; 5) reverse subsidiary cash mergers; 6) direct stock sales with an election under IRC § 338; and 7) direct stock sales with an election IRC § 338(h)(10).

In a direct taxable stock acquisition, Acquirer's pays cash and/or notes for Target shareholders' stock with Target becoming a subsidiary of Acquirer or being liquidated. In a direct taxable asset sale, Target sells substantially all of its assets to Acquirer for cash, notes, property, and/or the assumption of Target's indebtedness. After the transaction, Target may continue to exist or liquidate and distribute the sale proceeds and any assets it retained to its shareholders.

In a taxable cash merger, Target merges directly into Acquirer in a transaction carried out pursuant to state law with Target's shareholders receiving cash and/or notes for their stock. Instead of merging directly into Acquirer, in a taxable forward subsidiary cash merger, Target merges, pursuant to state law, with and into Acquirer's wholly owned subsidiary, with Subsidiary, not Target surviving the merger. In a taxable reverse subsidiary cash merger, Target and Acquirer's Subsidiary merge, but Target, not Subsidiary, survives the merger.

In a stock sale with a Section 338 election, Acquirer purchases 80 percent or more of Target's stock within a 12 month period and then elects to have the transaction treated for federal tax purposes as if Target had sold its assets in a taxable transaction to a hypothetical new corporation for their fair market value (FMV). In a stock sale with a Section 338(h)(10) election, Acquirer purchases 80 percent or more of Target's stock from Target's parent corporation or from shareholders of a Target that is an S corporation and then elects to have the transaction treated for federal tax purposes as a sale of Target's assets, rather than as a sale of Target's stock.

## Appendix A, cont.

### Tax Consequences of Taxable Stock and Asset Acquisitions

In direct stock sales, reverse subsidiary cash mergers, direct asset sales without liquidation of Target, and direct stock sales with a Section 338(h)(10) election, Target shareholders are taxed on the sale of their Target stock (Cash received for Target stock – Target shareholders' basis in Target stock = Target shareholders' gain or loss). In cash mergers, forward subsidiary cash mergers, and direct asset sales followed by liquidation of Target, Target shareholders are taxed on the liquidation or deemed liquidation of Target and Target is taxed on the sale or deemed sale of its assets (Cash received for Target's assets – Target's basis in assets = Target's gain or loss). In direct stock sales with a Section 338 election, shareholders are taxed on the sale of their Target stock and Target is taxed on the deemed sale of its assets. In direct stock sales and reverse subsidiary cash mergers, Acquirer takes a FMV basis in Target stock acquired from Target's shareholders and takes a carryover basis in Target's assets. Whereas, in direct asset sales, cash mergers, forward subsidiary cash mergers, direct stock sales with a Section 338 or Section 338(h)(10) elections, the basis of Target's assets are adjusted to FMV.

### Tax-Free Reorganizations

#### Statutory Requirements for Tax-Free Acquisitive Reorganizations

IRC § 368 provides for several different corporate tax-free acquisitive reorganizations, in which Acquirer uses its stock with either none or a limited amount of cash and other property (together referred to as boot) to acquire Target's stock and/or assets. In a IRC § 368(a)(1)(A) or Type A merger, Target's assets and liabilities are transferred to Acquirer with Target shareholders receiving Acquirer stock or a combination of stock and a limited amount of boot and Target dissolves by operation of state law.

In a IRC § 368(a)(1)(B) or Type B stock-for-stock reorganization, Acquirer acquires a controlling interest in Target's stock from Target shareholders solely in exchange for all or part of Acquirer's voting stock. A controlling interest means that immediately after the reorganization, Acquirer (or its subsidiary) owns at least 80 percent of the total combined voting power of all of Target's voting stock and at least 80 percent of the total number of shares of each other class of Target's stock.

In a IRC § 368(a)(1)(C) or Type C stock-for-assets reorganization, Acquirer acquires substantially all of Target's assets in return for consideration consisting solely of Acquirer's voting stock or a combination of Acquirer's voting stock and up to 20 percent of boot. Then, Target liquidates by exchanging Acquirer's stock for Target shareholders' stock and distributing boot and any other remaining Target assets to Target shareholders.

In a IRC § 368(a)(2)(D) forward triangular merger, Target merges with and into Acquirer's wholly owned Subsidiary, with Subsidiary, not Target, surviving the merger. In an IRC § 368(a)(2)(E) reverse triangular merger, Target merges with and into Acquirer's wholly owned subsidiary, with Target, not Subsidiary, surviving the merger.

## Appendix A., cont.

### Non-Statutory Requirements for Tax-Free Acquisitive Reorganizations

Besides meeting the specific requirements of IRC § 368, A tax-free reorganization must also meet the following non-statutory requirements: 1) plan of reorganization; 2) business purpose; 3) continuity of business enterprise (COBE); and 4) continuity of interest (COI). A tax-free reorganization must be carried out pursuant to a plan of reorganization adopted by each party to the reorganization, but it does not have to be in a particular form or in writing. Other than avoiding federal income taxes, a reorganization must have a valid business purpose, such as expanding product lines, reducing administrative and other costs, or avoiding state and local taxes.<sup>21</sup>

To meet the COBE requirement, Acquirer must either continue at least one significant line of Target's historical business or use a significant portion of Target's historic business assets in a business.<sup>22</sup> For COI, Target shareholders must have a substantial equity interest in Acquirer after the reorganization, meaning that a substantial part of the value of the Target's stock must be exchanged for Acquirer's stock, which is measured by the percentage of Acquirer's stock that was used as consideration in the reorganization.<sup>23</sup>

### Tax Consequences

#### Target Shareholders' Tax Consequences

In a tax-free reorganization, Target shareholders may have a realized gain if the FMV of Acquirer's stock plus the amount of boot (cash and FMV of property) they received in the reorganization exceeds their Target stock basis (FMV of Acquirer's stock + cash + FMV of other property - Target stock basis = Target shareholders' realized gain or loss). However, they will only recognize (or pay tax) on a portion of their realized gain, which is referred to as a recognized gain. The amount of their recognized gain is equal to the lesser of the boot they received or their realized gain.<sup>24</sup> For example, if Target shareholders' realized gain is \$500 and they received \$100 of boot, their recognized gain is \$100, because the \$100 of boot is less than the \$500 of realized gain.

Target shareholders' basis in their Acquirer stock equals their Target stock basis plus any recognized gain minus the amount of boot received and minus the amount of liabilities assumed by Acquirer as part of the reorganization (Target stock basis + recognized gain - boot - assumed liabilities = Target shareholders' basis in Acquirer stock). If Target shareholders held their Target stock as a capital asset, their holding period in their Target stock is tacked on to their holding period in their Acquirer stock.<sup>25</sup> Their basis in boot received from Acquirer is its FMV on the date of the exchange and the holding period for the boot begins on the date of the exchange.<sup>26</sup>

#### Target's Tax Consequences

In an acquisitive reorganization, Target will not recognize gain or loss on exchanging property for Acquirer's stock, nor on distributing Acquirer's stock to its shareholders. Target will also not recognize gain or loss on boot received as part of the reorganization, if it distributes the boot to its shareholders. But Target will recognize gain, not loss, if it distributes to its shareholders assets that were not transferred to Acquirer (i.e., retained assets), calculated as if Target had sold the distributed property for its FMV.<sup>27</sup>

## Appendix A., cont.

### Acquirer's Tax Consequences

If Acquirer exchanges solely its stock for Target's stock and assets, Acquirer will not recognize gain or loss. However, if Acquirer also transfers other property (non-cash boot) as part of the reorganization, it will recognize gain or loss equal to the FMV of the property minus its basis.<sup>28</sup>

Acquirer's basis in Target's transferred assets equals Target's basis in those assets plus any gain recognized by Target (Target assets' basis + Target's recognized gain = Acquirer's basis in Target assets). Target's holding period in its transferred assets is tacked on to Acquirer's holding period. Acquirer's basis in Target stock it receives from Target shareholders equals their basis in their Target stock plus any gain recognized by them (Target shareholders' basis in Target stock + Target shareholders' recognized gain = Acquirer's basis in Target shareholders' Target stock). Target shareholders' holding period in their transferred Target stock is tacked on to Acquirer's holding period in those shares.<sup>29</sup>

### Tax Consequences for Acquirer's Shareholders

If Acquirer's shareholders do not participate in a tax-free reorganization involving the Acquirer, generally there is no reorganization-related tax consequences for Acquirer's shareholders. Generally, Acquirer shareholders would not realize and/or recognize gain or loss and their basis and holding period in their pre-reorganization Acquirer stock would be the same after the reorganization.

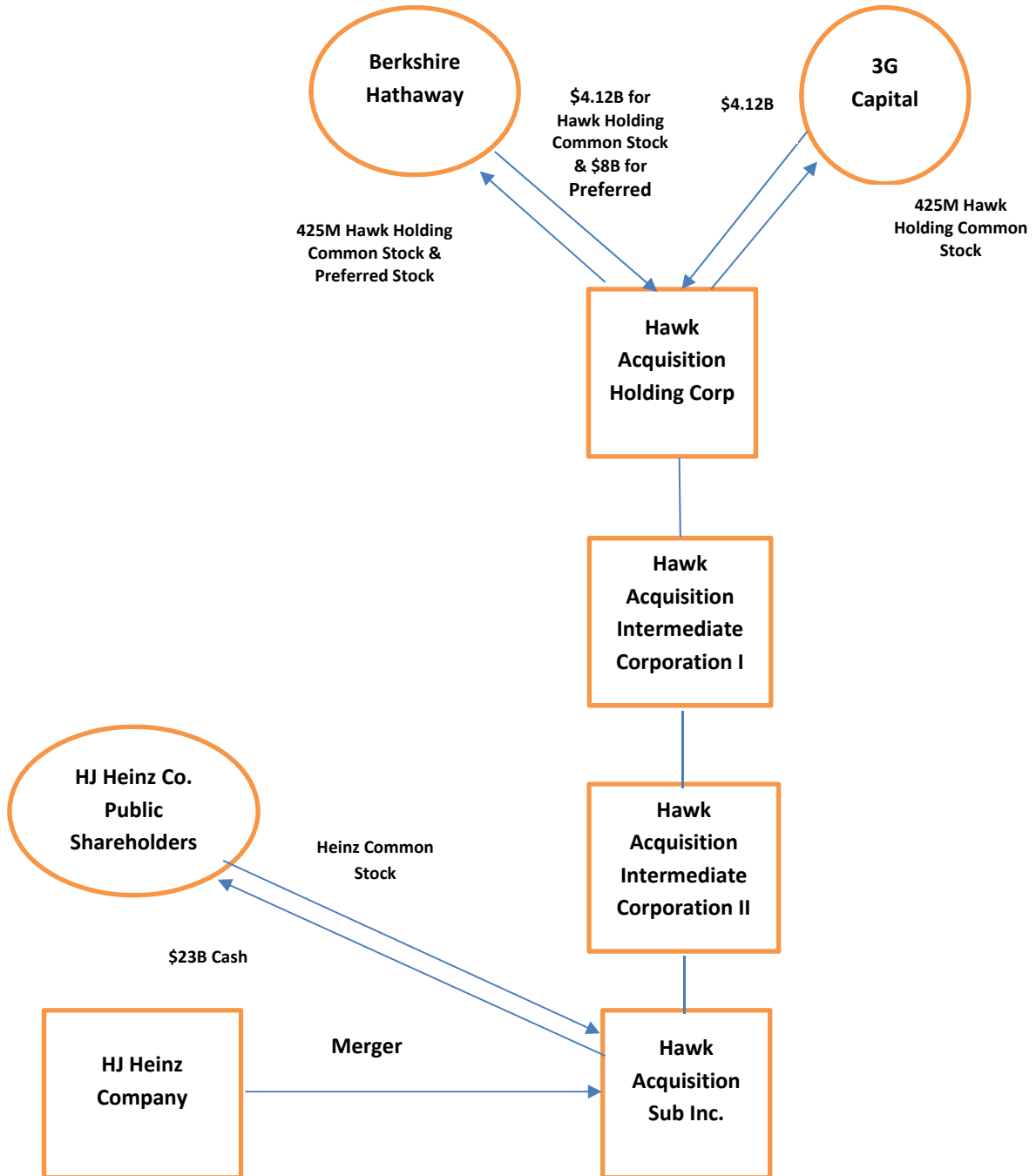
## Appendix B Merger Timeline

*Source: Author's notes*

DATE	EVENT
December 2012	Jorge Paulo Lemann, partner and co-founder of 3G Capital, met with Berkshire's CEO and chairman, Warren Buffett, and proposed that 3G Capital and Berkshire jointly acquire Heinz.
December 2012	Mr. Buffett informed Mr. Lemann that Berkshire was interested in acquiring Heinz and would be willing to provide equity financing for a potential acquisition.
12/13/2012	William R. Johnson, chairman, president and CEO of Heinz, asked to meet with 3G Capital in order to discuss the food and beverage industry.
12/18/2012	At a meeting, Mr. Johnson discussed with Mr. Lemann and the managing partner of 3G Capital, Alexandre Behring, the food and beverage industry, potential industry consolidation, and their respective businesses and agreed to meet in 2013 to continue their discussion.
1/10/2013	At a meeting, Mr. Behring told Mr. Johnson that Berkshire and 3G Capital (Acquirers) were interested in discussing the potential acquisition of Heinz and intended on making a proposal to acquire Heinz. Mr. Johnson stated that Heinz was not for sale, but that he would inform Heinz's board of directors of their discussion and would present any acquisition proposal to the board.
1/14/2013	Berkshire and 3G Capital delivered a joint letter to Mr. Johnson proposing to acquire all of Heinz's outstanding shares of common stock for \$70 in cash per share.
1/16/2013	After Heinz's board of directors deliberated about the Acquirers' proposal, Mr. Johnson contacted Mr. Behring and told him that Heinz was considering the proposal, but that Heinz had made no decision about the proposal or whether to authorize further discussions.
1/21/2013	Heinz's board directed Mr. Johnson to inform the Acquirers that it was unlikely to authorize further merger discussions unless the Acquirers improved the financial terms of their proposal.
1/24/2013	The Acquirers' increased their offer to \$72.50 in cash per share of Heinz common stock.
2/13/2013	Heinz's board of directors voted unanimously to approve the Merger and to recommend that Heinz shareholders vote to approve the Merger.
2/13/2013	Heinz, Berkshire, and 3G Capital entered into a merger agreement with each Heinz shareholder receiving \$72.50 per share or a total of \$23 billion. With Berkshire and 3G Capital agreeing to assume all of Heinz's outstanding debt, the Merger was valued at \$28 billion.
4/30/2013	At a special shareholders meeting, Heinz shareholders voted to approve the Merger.
Spring 2013	To carry out the Merger, Hawk Acquisition Holding Corp (Hawk Holding) and its wholly owned subsidiaries: 1) Hawk Acquisition Sub Inc. (HA Subsidiary); 2) Hawk Acquisition Intermediate Corporation I (HA I); and 3) Hawk Acquisition Intermediate Corporation II (HA II), were formed.
Spring 2013	Berkshire and 3G Capital each purchased for \$4.12 billion 425 million shares of Hawk Holding's common stock. Berkshire purchased shares of Hawk Holding's 9 percent preferred stock for \$8 billion and warrants to purchase approximately 46 million additional shares Hawk Holding common stock.
6/7/2013	Heinz merged with and into HA Subsidiary, with Heinz surviving as an indirect, wholly-owned subsidiary of Hawk Holding Corporation, which was renamed the H.J. Heinz Holding Corporation (Heinz Holding).
6/7/2013	Heinz's shareholders received \$72.50 in cash for each share of their Heinz common stock.

**Appendix C  
Merger Transaction**

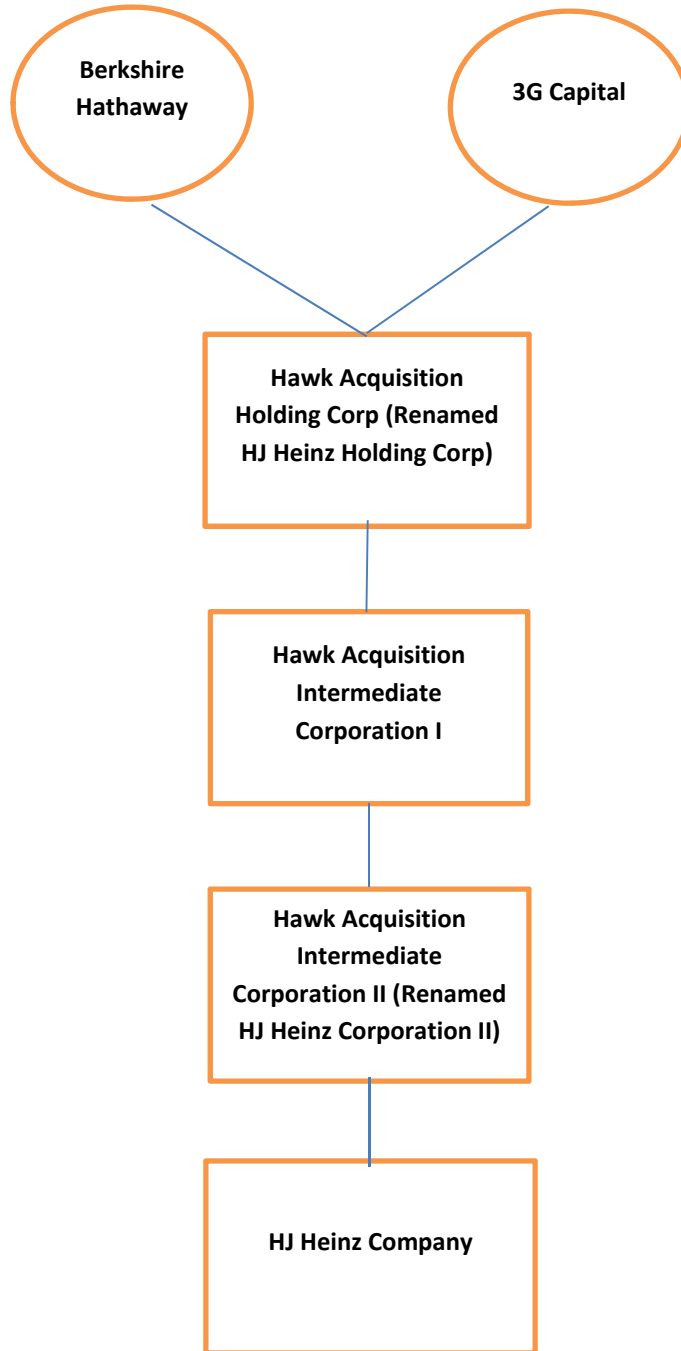
Source: Author's notes and H.J. Heinz Holding Corporation SEC Form S-4 (April 10, 2015)





**Appendix D  
Post-Merger**

Source: Author's notes and H.J. Heinz Holding Corporation SEC Form S-4 (April 10, 2015)



## Endnotes

- <sup>1</sup> H.J. Heinz Company Schedule 14A Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934 (March 27, 2013) (Heinz Proxy); H.J. Heinz Company, United States Securities and Exchange Commission Form 10-K: Annual report for transition period from April 29, 2013 to December 29, 2013 (March 2014).
- <sup>2</sup> Heinz Proxy; Berkshire and 3G Capital in a \$23 billion Deal for Heinz, Michael J. de la Merced and Andrew Ross Sorkin, NY Times (February 14, 2013); Berkshire Hathaway to swallow Heinz, Mateusz Perkowski, East Oregonian (February 21, 2013).
- <sup>3</sup> Heinz philanthropy won't change, despite new ownership, Thomas Olson, Tribune-Review (February 16, 2013).
- <sup>4</sup> Heinz Proxy.
- <sup>5</sup> *Id.*
- <sup>6</sup> Developed in the 1960s, zero-based budgeting is an accounting practice that requires starting a budget each year at a zero, rather than using the prior year's budget as the starting point (Shook the Food Business by Snagging Burger King, Kraft and Heinz. Now 3G is Reeling, Annie Gasparro and Vipal Monga, Shook the Food, Wall Street Journal (February 22, 2019)).
- <sup>7</sup> Heinz Proxy, p. 35.
- <sup>8</sup> Heinz Proxy, p. 38.
- <sup>9</sup> *Id.*
- <sup>10</sup> Heinz Proxy.
- <sup>11</sup> The Merger Agreement was amended on March 4, 2013 (Heinz Proxy). H.J. Heinz Company Enters Into Agreement to Be Acquired by Berkshire Hathaway and 3G Capital, H.J. Heinz Company Press Release (February 14, 2013).
- <sup>12</sup> H.J. Heinz Company Enters Into Agreement to Be Acquired by Berkshire Hathaway and 3G Capital, H.J. Heinz Company Press Release (February 14, 2013).
- <sup>13</sup> *Id.*
- <sup>14</sup> *Id.*
- <sup>15</sup> *Id.*
- <sup>16</sup> On the record date of March 18, 2013 for the special meeting, 203,258,999 of the 321,187,333 shares of Heinz common stock entitled to vote voted, with 192,117,965 shares voting for the Merger, 8,477,373 shares voting against, and 1,817,551 shares abstaining. (H.J. Heinz Company Shareholders Overwhelmingly Approve Acquisition by Berkshire Hathaway and 3G Capital, H.J. Heinz Company Press Release (April 30, 2013)).
- <sup>17</sup> Heinz Proxy. HA Subsidiary was a subsidiary of HA I, which was a subsidiary of HA II, which was a subsidiary of Hawk Holding (See Appendix C).
- <sup>18</sup> Heinz Proxy; H.J. Heinz Company Form 10-Q for period ended October 27, 2013 (December 11, 2013).
- <sup>19</sup> Berkshire Hathaway and 3G Capital Complete Acquisition of H.J. Heinz Company, H.J. Heinz Company Press Release (June 7, 2013).
- <sup>20</sup> *Id.*
- <sup>21</sup> Treas. Reg. §§ 1.368-1(c), 1.368-2(g), and 1.368-3(a).
- <sup>22</sup> Treas. Reg. § 1.368-1(d).
- <sup>23</sup> Treas. Reg. § 1.368-1(e).
- <sup>24</sup> 26 USC §§ 354 and 356.
- <sup>25</sup> 26 USC § 1223(1).
- <sup>26</sup> 26 USC §§ 358 and 1223(1).
- <sup>27</sup> 26 USC §§ 361 and 1032.
- <sup>28</sup> 26 USC §§ 361, 1001 and 1032; Rev. Rul. 72-327, 1972- CB 197.
- <sup>29</sup> 26 USC §§ 362, 1223(1) and 1223(2).

## **STRATEGY AND LEADERSHIP AT THE WINDOW SPECIALIST: CAN A TECH CEO DRAMATICALLY GROW A CONSTRUCTION FIRM?**

**GEORGE L. WHALEY**

San José State University

**CONNIE ALLSOPP**

The World's Registrar

**KEITH C. PERRY**

San José State University

Keith Perry, CEO of The Window Specialist (TWS), woke up at 3:00 a.m. in self-doubt. Perry was an experienced executive, teacher, engineer, and entrepreneur from the high-tech industry who had purchased a low-tech 40-year-old window replacement firm in 2014 (see Appendix A) and managed it as a start-up operation. TWS' business model provided in-home estimates, materials, labor and after sales service for best-in-class offerings to customers of all income levels. Perry believed that his business and academic experience, along with his leadership abilities, made the difference in achieving TWS' strategic and financial goals. He also wanted to help society. He immediately reincorporated TWS as a benefit corporation that embraced goals beyond its financial growth. The overall status of TWS improved each year, however in 2017, a series of events had created strategic, leadership, and financial challenges that came to a head in May.

Payroll had understandably tripled to support TWS's 500% growth by year end 2016. TWS was forced to move in January 2017 when its landlord gave notice that the warehouse was going to

be razed to build condos. TWS was forced to move outside of its primary Oakland, California market for the first time, paid 400% more for a new lease, and incurred additional travel costs on virtually every job. Another issue was TWS' low year-to-date 2017 sales figures (see Appendix B) which correlated with the Federal Reserve Bank's May 5<sup>th</sup> report on the economy that noted the pace of real consumer spending in first quarter had slowed significantly (U.S. Economy 2017). Perry wondered if he was overreacting. After all, this 40-year-old company had weathered the recession of 2008, the Bay Area's dot-com bust, and many other business cycles.

Perry was also distracted by an urgent letter from the Contractors State License Board (see Appendix C) stating that his contractor's license had been revoked. He realized the sole issue was that the company name was singular in the letter and plural on the Secretary of State's listing. Although Perry viewed the licensing issue as a bureaucratic detail, he shook his head in amazement that something so minor could put his entire company in jeopardy. Perry tossed and turned in bed for another hour before leaving early to reduce his 2-hour commute to the office.

It was May 2017 as Perry wondered aloud on what was important rather than just urgent:  
*"What strategies and leadership approaches should I adopt to address the current challenges for growth and sustainability to take TWS to the next level?"*

### **The Change in TWS Ownership, Leadership, and Management Backgrounds**

TWS had only four people on its management team during its entire 40 years of existence. One was a very successful salesperson who was let go during the 2008 great recession and eventually became a competitor. A brief background on each of the other three follows.

### ***Tom From***

Tom From, the founder and owner of TWS until 2014, learned about the window replacement business from his grandfather who owned a construction company. He obtained a business degree and branched out on his own in 1977.

From practiced a participatory leadership style with office staff and installers through many economic cycles. After 35 years of doing the same thing, from started thinking of retiring from the window industry to focus his energies on refurbishing houses with his wife who was a realtor. By 2014, he decided to sell the firm to his colleague and cycling buddy, Keith Perry, who had different business, educational, and leadership orientations.

### ***Keith Perry***

Keith Perry was a leader in the high-tech industry prior to purchasing the 40-year-old low-tech window replacement construction firm. After working 8 years at the largest software and management consulting firms in Canada, Perry joined a Fortune 500 high-tech firm, Amdahl Corporation, and eventually relocated to California. Perry held increasingly responsible roles in pre-sales engineering, product management, sales, and marketing during his 12 years at Amdahl.

He then became senior vice president of sales and marketing for two technology firms and focused on strategy development which drove revenue and profit at each firm. He won Deloitte's Fast 50 award for growth at one, and increased revenue and profit at the other over 400% in just his first year. During this time, Perry discovered that leadership was necessary to drive strategic change. His interest in leadership motivated Perry to move into the venture capital (VC) industry; he accepted a position as president and COO of a portfolio company at a VC. This piqued Perry's interest in entrepreneurship and he decided to launch his own firm. He co-founded a phone company in 2003 and advanced its business model several times while learning new markets until its customer base spanned 40+ states. While running his phone

company, Perry decided to return to university to study the relationship between leadership, technology, and change.

He pursued a master degree in software engineering as well as an MBA as the best way to formally study the relationship between leadership, technology, and change. After graduating from San José State University's dual-degree program with a 3.9 GPA, Perry was asked to teach a few courses. He also continued to expand his phone business and found that he enjoyed the balance between theory and practice. His teaching responsibilities grew and he eventually taught strategy courses at San José State's College of Business and software engineering courses in the College of Engineering while helping the associate dean of engineering plan curricula.

In 2014, Perry purchased TWS and became its full-time CEO after reducing his teaching load to three engineering courses. One was mobile software while the other two focused on developing engineering solutions that helped improve the community. Perry continued to also "give back" to the community by serving as a keynote speaker on entrepreneurship for international audiences and speaking about innovative engineering topics on TV.

### ***Jim Ford***

After completing high school, Jim Ford and his family moved from Canada to the Bay Area where they established Ford Custom Lumber (FCL). FCL re-cut lumber to other dimensions not usually processed by a primary sawmill for wood fences, and improved low grade lumber to higher grades by removing imperfections when re-cutting. At the age of 21, Ford obtained his contractor's license, and the company expanded to sell decks, fences, and gazebos. As profitable new market trends emerged, FCL started selling par-courses (i.e., outdoor exercise stations) and spas. Over time, his father's health deteriorated and markets changed so FCL closed in 2002. Ford then came to work for TWS.

Ford started out as the service manager and rose through the ranks to become From's right hand man. When Perry came into the picture in 2014, he asked Ford to reconsider From's previous offer of handing ownership to Ford in appreciation of his many years of loyal service. Ford once again politely declined but continued to be an outstanding colleague. As general manager, Ford handled the day-to-day running of TWS as if it were his own company. Perry enjoyed his old-school management style, as well as his highly ethical approach to running the company.

### **TWS Company Background**

From started the company under his own name as a sole proprietorship in 1977. His business model targeted residential and apartment owners in San Francisco and on the "East Bay" who had single-pane windows and/or windows with aluminum frames. He sold primarily vinyl windows as well as aluminum clad wood windows and hand-crafted windows. He expanded his product line by also selling and installing vinyl siding on older homes and over time, changed the legal structure to an S-Corporation and created a more formal name, The Exterior Specialist. Vinyl siding waned over time so From went back to just windows and changed the name to The Window Specialist in 1999. From's most successful financial years followed the dot-com bust of 2000. He and his sales person focused on replacing windows in San Francisco apartments with vinyl windows before permit requirements were tightened to only allow wood windows when they were visible from the street. His sales person left during the great recession of 2008 and sales continued to stagnate until Perry took over ownership in 2014. Perry implemented a strategic plan to gain an edge in an increasingly competitive market by expanding TWS' product offerings to include luxury homes and by winning large contracts.

### ***Organization Vision, Mission, and Core Values***

After Perry re-incorporated TWS as a for-profit benefit corporation to align the legal entity with his philanthropic passion to give back to the community, he did not make any internal changes

for the balance of 2014. He realized from one of his business school models that the company’s initial phase of growth through creativity had waned over the decades and recognized the company was in a growth crisis. Customers continued to call looking for missing quotes and Perry and Ford scrambled to maximize installations using antiquated white boards. In year 2, Perry started a new phase that focused growth through direction, trust, and leadership. While his direction included improving the sales process through technology and implementing Google calendar on a large TV screen for installations, he also provided higher level direction by hiring an old friend as a marketing consultant. Together with Ford, they created the company’s vision based on Perry’s evolving strategic plan that focused on technology. The mission statement and core values incorporated Perry’s philanthropic passion (see Exhibit 1) and by 2017, evidence of these qualities showed in the ways that TWS did business.

**Exhibit 1. Vision, Mission, and Core Values**

*Source: Company Records, 2017*

---

Vision	Simplify the window replacement industry globally
Mission	Boutique best-of-breed construction window selection and installation for all income levels while providing additional services for those less fortunate
Core Values	Demonstrate expertise taking a consultative approach to customer needs  Be a learning organization with more skills than the competition  Deliver WOW (extraordinary factors) through customer service  Deal ethically in all relationships

---

Perry and Ford had strategically focused TWS to be responsive, dependable, and experienced in order to implement this new higher-level direction. Their primary involvement was estimating expertise which set the stage for high-quality product delivery and service excellence. One strategy Perry implemented was the Department of Energy’s Property-Assessed Clean Energy (PACE) program, which gave homeowners an affordable way to finance new windows. Customer feedback included “trustworthy” and “honesty,” and one reviewer even



acknowledged, “Now I can do small payments while I enjoy these fabulous new energy efficient windows.”

**Organizational Culture**

This family-style approach included a flat organizational structure with an engaged CEO. Staff members who aligned with Perry’s ethical goals remained while others departed or were asked to leave. The team members listed below were committed to providing clients with the highest levels of customer service as noted in reviews on Yelp (2017) and the company’s website.

**Exhibit 2. TWS Organization Structure**

*Source: interview with CEO, 2017*

CEO				
Full-time salesperson	Part-time salesperson	General manager  2 Two installation teams 1 One custom hand-crafted wood installation team	Office manager	Bookkeeper

**TWS Leadership Changes and Challenges**

Perry recalled from his graduate studies that leadership was an important component of strategic management.

**Employee Task Coordination**

Perry had learned in graduate studies that his time assigning and following up on tasks could be optimized according to his employees’ skill sets and commitment. He optimized his time by delegating tasks to Ford, who did not need direction or support. When there was a 49ers game that Ford wanted to attend in the afternoon, he let Perry know. Ford put in extra hours regularly and was TWS’ most valuable player, so Perry started to pay for his season tickets.

The bookkeeper exemplified a second approach. Perry provided a high level of support, but she required low direction as she had worked there for seven years and knew her job intimately. She had been full time, but eventually had accepted another job close to her home and kept on doing TWS' books part time for several years. After months of unacceptable work with no improvement since Perry had come on board, the bookkeeper disclosed that she was having difficulty juggling the two jobs as her mother was dying. They mutually agreed to part ways and Perry hired a senior accountant part time who had been recommended by TWS's CPA.

The new salesperson had questionable commitment and needed direction to do his job. He would disappear during workdays and not be available by phone. Once, he asked for Thursday and Friday off to take his girlfriend camping when he had a quote due the same Friday that would have provided him with tens of thousands of dollars in commission. The salesperson went around Perry's back repeatedly ordering windows that regularly had incorrect measurements. His disappearances and apparent inability to learn continued until Perry terminated his job after 9 months due to a breach in confidentiality. It took a full year before his mistakes no longer affected TWS' bottom line. Perry realized that he had spent far too much time supporting this person and the bookkeeper at the expense of the company.

Daniel Cavenecia was a lead installer who exemplified the fourth approach to task coordination. Perry and Ford both recognized that he was highly motivated but could still learn more. Ford, as his line manager, provided significant direction daily while Perry found courses for him. Both recognized that Cavenecia was highly committed and spent little time worrying about supportive behaviors.

The following provides a timeline of events (see Appendix A) that occurred during each year of Perry's ownership.

### ***Year 1: March 2014-February 2015***

In March 2014, Perry and From shook hands based on From's latest exit plan offer to Perry who was his only alternative to shutting down the business entirely:

*“Buy [TWS] for no money down, and if you don’t make money, you don’t owe me a thing. If you make a good profit, pay me 10% of it.”*

Perry recognized that From’s weaknesses were Perry’s strengths and vice versa. However, From’s strengths were already embedded in the team - many customers thought he was a co-owner. From had given Perry his approval to make any changes to the company that he wanted, but Perry maintained the company’s operations out of respect for the current staff and their expertise as he learned the business himself. Perry’s initial actions appeared to be a hands-off, low-task, and low-relationship approach. Some were confused about Perry’s hands-off leadership approach and his willingness to share important company decisions with Ford. Perry came to the office daily to learn from Ford, even though he did not yet have legal ownership.

Ford’s approach to daily company operations was tried and true, so Perry used his entire first year to learn what worked before introducing major changes. For instance, Ford used notebooks to track all customer visits, measurements, and quotes. Perry used the same paper-and-pencil system as Ford; however, after decades of using a laptop, Perry eventually went back to using it while Ford continued using notebooks without change. Both continued to receive and make calls using the company’s entry level Radio Shack phones, faxing window orders to suppliers, and writing on white boards to schedule installations.

Perry believed change was required in numerous areas, but he held back from taking action. Examples included: using Google calendar to schedule customer visits; using laptops to take measurements and develop quotes; implementing a sophisticated phone system similar to what his previous company sold; processing vendors’ orders using their software; and replacing the company’s 15-year-old website. Although Perry recognized this was a pattern of not taking action where changes would improve the company, he acknowledged to Ford, *“We are barely able to process our leads, anyway, so losing a few along the way isn’t the key to growing the*

*company.*” Unacceptable levels of not following up on existing leads, not ordering windows on signed contracts, and other process issues were hurting the company’s reputation (Yelp, 2017). Perry knew that growth through process improvement and building trust with staff was going to depend on his leadership. He had studied leadership during his graduate program and viewed himself as either a servant or a transformational style leader. However, interviews with colleagues revealed that his leadership style had evolved to a more consultative style. (See Appendix E).

### **Year 2: March 2015-February 2016**

Perry carefully made incremental procedural changes to the company’s infrastructure throughout the second year of ownership (see Appendix D). It took approximately 4 months of conversion before the white calendar board was replaced by a large TV screen that displayed all installations on a Google calendar. Perry’s old phone company now ran TWS’ phones in the cloud. Telemarketing calls dropped and extensions simultaneously rang through to individuals’ cell phones subsequently improving sales. The phone system included an integrated eFax system that e-mailed faxes to Ford and Perry. The number of faxes also became much smaller as Perry adopted vendors’ online ordering systems while Ford continued without change. Perry scanned checks for deposit which saved him 30-minute trips to the bank. However, the TWS website remained unchanged.

More importantly, Perry tried to implement a new style of leadership during this second year because he felt that this would best advance TWS toward the benefit corporation goal. Perry focused year 2 on valuing and developing people, building a sense of community with employees, displaying authenticity, and sharing leadership responsibilities.

### **Value People**

Perry felt that his best approach to making the company successful was to serve the needs of his staff. For instance, as new office staff were hired, Perry bought each employee a new

laptop, a protocol that was the norm in his prior tech industry yet almost unheard of in the construction industry. This change was now a 100% cost to Perry as the sole owner of TWS.

### **Develop People**

Perry developed and hired three local people with questionable work and non-work personal backgrounds. For the most part, these decisions turned out to be win-win situations for TWS and the people involved.

### **Build Community**

A community relationship unfolded with the employees collaborating on various aspects of their jobs. Perry and Ford created a rhythm of working together on commercial proposals with Ford measuring every window and Perry capturing the details on his laptop. Customers were impressed with the company's attention to detail and TWS won more business as a result, even with higher prices.

### **Display Authenticity**

Perry made sure that he was accountable to others and remained open to feedback. He would specifically ask crews after an installation which windows did not fit well so that he could improve his measuring capabilities. He learned from them and continued to learn from Ford who advised him on all major and/or minor decisions of the window business. Perry wanted to ensure that he displayed integrity and developed a sense of trust with the TWS team.

### **Displaying and Sharing Leadership**

Perry worked closely with Ford as they developed a shared vision. Ford had suffered a stroke shortly after Perry had purchased the company. After a month of convalescence with full pay, Ford assumed day-to-day leadership more than ever before as Perry shifted his attention to new business plan initiatives such as selling Fleetwood's (2017) architectural aluminum products to luxury homeowners. Ford showed himself to be dependable and trustworthy.

Whenever Perry could praise employees, he would highlight the successes of individual staff members and thank them for their efforts. Perry's challenge with this servant leadership style was its time commitment to serve his staff well in small and large ways while he balanced his teaching duties at the university. Eighty-hour weeks remained the norm, and 100-hour weeks occurred frequently with this leadership approach. Perry realized that this style of leadership was not sustainable, given the growing time commitment required to obtain the growth he envisioned at TWS.

### ***Year 3: March 2016-May 2017***

Perry returned to his academic roots to search for another leadership approach that he could use that supported his core values and were in alignment with the company's benefit corporation designation. Perry valued an article that he had read on compassionate leadership and decided to emulate these actions in Year 3 (Grant 2008). He found that because he was moved by the needs of others and their emotions, he should focus on being as selfless as possible and model being a shining light to others. Perry worked to transition seamlessly to this new leadership style that had three tenets: be moved by others' needs and emotions, be selfless, and become a shining light for others. These were all consistent with his core values and a benefit corporation.

## **Evolving Leadership**

### ***Moved by Others Needs and Emotions***

Perry's first month of compassionate leadership led him to take leadership action in several ways. First, he first arranged a trip home to Peru for Cavenecia, his lead installer, to see his family. Cavenecia appreciated this time away and upon his return, Perry noticed an increased sense of dedication and loyalty.

Martin was a part-time employee who had worked for TWS for more than a year, so it was time for Perry to fulfill his promise of dramatically increasing Martin's income. Perry and Ford obtained contracts in September 2016 to replace 409 windows and 38 patio doors at three apartment blocks, so they promoted Martin to the position of crew chief, which was at the same level as Anthony Gonzales, the company's longest serving lead installer and Cavenecia who had trained him. Martin was delighted with the increase in pay. These newfound skills, coupled with advertising on his truck for his home repair business, saw his income increase so much that he stated he had never made so much money in his life.

The third leadership action was with the full-time salesperson. He convinced Perry that his position as a property manager was sales and asked for a commissioned based structure that would pay him at the same level as sales positions generally do as he felt he was significantly underpaid. Perry hired this salesperson on a salaried 6-month training program to learn TWS practices before switching him to 100% commissioned sales. The salesperson could see significant financial opportunities from the way that TWS did business, but unfortunately didn't have the skills, motivation, interest to learn, nor acceptable ethics and as mentioned above, was fired after 9 months.

### ***Selfless Leadership***

Perry understood that it usually took a couple of years to launch any startup, so he was comfortable not drawing a salary during his first 2 years of ownership of TWS. The company experienced tremendous growth, but the third year also passed without salary because of some unforeseen costs and lower 2017 revenue. For instance, Perry had to replace Cavenecia's personal truck when it failed inspection and Cavenecia didn't have the money to replace it. Perry bought a new Ford with an aluminum body which was more environmentally friendly because of its light weight.

And then TWS' landlord decided to raze the building. Realtors noted vacancy rates were at 1%, with nothing in Oakland that fit TWS's needs. Perry and Ford ultimately chose a property in San

Leandro that cost 400% more and completed the move by January 1<sup>st</sup>, 2017. On a positive note, several incorrectly measured windows had accumulated in the old warehouse over the last decade and as Cavenecia was involved in helping a village in Mexico, they agreed that Perry would donate these windows and Cavenecia would arrange delivery.

Another 2016 highlight was NBC's coverage of Perry and his engineering students unveiling a year-long community service project for a course that he had been asked to lead at San José State. Perry had purchased a shipping container which his students had converted to a trailer with portable showers and laundry facilities for the homeless. The TV crew came by on the last day of class to video Perry's engineering students working on it (see EPICS 2016).

Coincidentally, Oakland's Fox TV affiliate contacted TWS a couple of months later asking for technical assistance; another company was selling Fox one type of glass and installing a less energy efficient version. Perry drove several hundred miles to borrow a glass tester from his manufacturer and verified that the investigative unit's source was correct. The Fox station was delighted with Perry's credentials as a professor and ran two episodes featuring him. San Francisco had surpassed Silicon Valley for startups and social media had made customers much more sophisticated, so Perry discussed details at a detailed, technical level. During the process, Perry asked personnel at the TV station why they had called TWS. They told him that they had contacted the Better Business Bureau and then had checked other sources that confirmed that TWS was an ethical company. A station executive mentioned later that one of the episodes was the most popular one they had run that year.

### ***Be a Shining Light to Others***

When Verizon announced its purchase of Yahoo!, ABC's news team contacted San José State's School of Global Innovation and Leadership for someone to discuss the CEO's failure to turn the company around. Perry hadn't taught in that school for a few years, but the school still provided ABC with his name. During the taping, Perry expressed his admiration for Marisa Mayer and highlighted the challenges of creative entrepreneurship within Fortune 500s. Perry had co-authored a case study on this topic and had many examples of how difficult Mayer's job



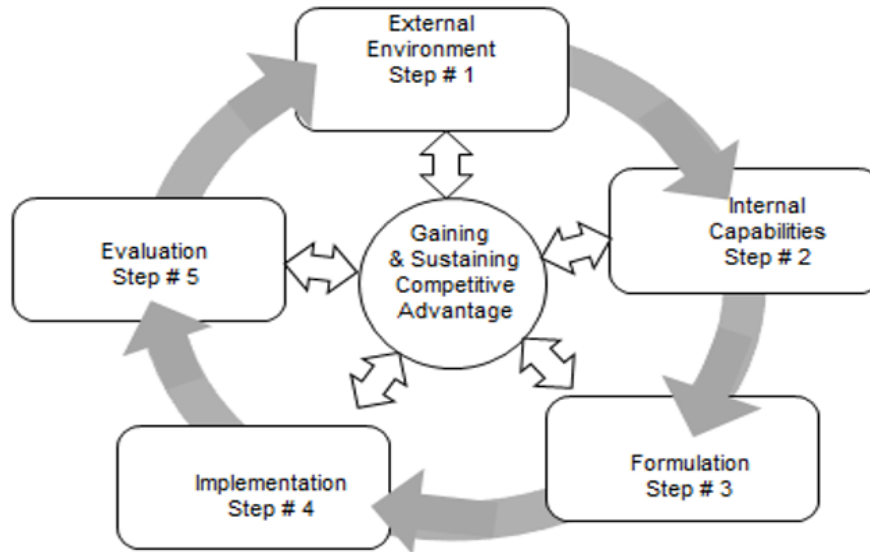
was. His comments did not endear him to the news team who were looking for controversy. He didn't make it home that evening in time for even the late evening news which was just as well as ABC had accidentally put someone else's name under his face followed by "Industry Analyst." Perry's wife and friends had fun calling him that name for months.

Perry had been a regular keynote speaker on entrepreneurship in Silicon Valley over the years. In 2016, Perry's four TV appearances and eight speaking engagements were in addition to lesser known efforts such as his donation of windows to the village in Mexico. He also supported Rebuilding Together San Francisco (equivalent to Habitat for Humanity focused on remodeling rather than building new homes) and low-income neighbors who received cash for recycling the aluminum from windows that TWS had replaced. He focused on compassion that was not based on passionate or parental love, but rather on the love that he hoped brought a sense of community. Unfortunately, there were occasions where he was perceived as soft such as not firing his salesperson earlier, and he struggled to balance the for-profit company aspects with his leadership style focused on humility, love, altruism, forgiveness, kindness, and compassion.

### Strategic View of TWS Business Model

#### ***Strategic Framework***

Perry stated, *"I believe nothing beats a good theory tested by practice."* To that end, he incorporated many successful theories from his graduate school studies into his practice to manage and lead TWS. Perry recalled a step-by-step strategic model (see Exhibit 3) that he had used in his strategy management classes that started with the external and internal environments and ended with the implementation and evaluation of strategic formulation models.

**Exhibit 3. Generic Strategic Framework***Source: Adapted from author's notes, 2017***External Factors**

Perry recalled research indicating that approximately 20% of a company's profitability was attributed to the industry it competed in and 36% of the variance in profitability was attributed to the firm's internal resources (McGahan 1999; McGahan & Porter 2005). He also remembered several strategic formulation tools that included PESTLE, Porter's Five Forces, and SWOT to help gain a competitive advantage for his company (Porter, 2008) and applied a SWOT analysis with Ford on the day he took ownership of the company which looked at both external forces and internal capabilities. He decided to focus on the external forces that influenced the performance of companies (Barney 2010; David 2009; Rothaermel 2015; Wheelen & Hunger 2006). Perry knew that external factors such as the economy had a dramatic effect on his business. Low interest rates helped the housing market and Bay Area IPOs repeatedly created instant millionaires who drove housing up further which was a benefit to TWS's industry. Perry also regretfully noted that one of his installers had lost his business and another had lost his house in the 2008 great recession. He thought about competition amongst contractors; competition from suppliers; the power of customers negotiating lower prices, how easy it is to enter this market and become a competitor, lawsuits that affected the industry and TWS' brand; and Workers' Compensation issues. He couldn't fathom a substitute for windows which

have been around for thousands of years, but thought a complement to them would be to sell doors although he now knew that selling and installing doors was a very different business than the window industry.

He was mindful that TWS faced several other external issues in addition to these industry threats. He was reminded of the \$9,965 he spent on legal fees (see Appendix B) to buy only the assets of the company so that he wouldn't be burdened with any historical liabilities. The Secretary of State found a company with a similar name and blocked his use of TWS (an asset he had just purchased) until the other firm wrote a letter 6 months later saying it was dissolving that company. Perry purchased an interim website, [www.windowsspecialists.com](http://www.windowsspecialists.com), and it took three submissions before the Secretary of State accepted this plural version. Then the Contractors State License Board revoked his license – forcing Perry to regroup. In fact, regulations had become so complicated that one of TWS' property managers required the company to subscribe to Compliance Depot which monitored over 40 TWS items. Perry had adopted quoting software provided at no charge from manufacturers, however some still used 30-year-old technology that was cumbersome. Newer cloud-based versions added network delays which slowed quoting by 400%.

Access to financial capital could be another external issue along with insurance claims and government policies. Lower federal tax rate changes had a positive impact on TWS as did the current political climate at all levels of government. President Trump's dissatisfaction on trade with other countries could lead to increased prices of oil (used in vinyl), wood and/or aluminum that could increase the cost of windows.

California's focus on the environment was an opportunity for TWS. Local Tesla sales were the highest in the nation and solar panel sales remained strong even though the Return on Investment (ROI) could be 20 years or more. Similarly, the ROI for windows from reduced PG&E bills was 15-25 years, yet purchasers often stated their primary reason for replacing them was

their increased energy efficiency. This was completely out of step with businesses who regularly demanded 3-5 year ROIs for investments.

In 2014, Perry and Ford had identified opportunities during their SWOT analysis such as Yelp, which produced half of their leads from mobile phones; a fragmented market; and resources/consultants. Perry concluded that the numerous external forces reinforced his belief that residential remodeling was a very competitive industry that pushed him to compete on price to sell windows while his focus was to differentiate TWS.

### **Internal Factors**

Because research had indicated that a larger percent of the variance in profitability was typically attributed to internal rather than external resources, Perry said, *“I need to place more emphasis on building a strong team, developing a collaborative company culture and improving people’s skills.”* When Perry taught his management courses at university, he emphasized internal-focused strategic models such as value chain analysis, VRIO, and SWOT to evaluate sustainable competitive advantage (Barney 2010; David 2009; Rothaermel 2015). He decided to evaluate these strategic management theories in his company, such as VRIO (Value, Rarity, Imitability, and Organization), and the strengths and weaknesses of the SWOT model to determine the internal components in need of his attention (Barney 2010; David 2009; Rothaermel 2015).

In 2014, Perry and Ford had identified the company’s major strengths: concerned, energetic staff with people skills; depth of experience on subject matter expertise; technology skills; strong local market and supplier relations; broad range of products; long list of long-term relationships with a diverse group of customers; and low overhead costs. Among the company’s major weaknesses were the following: estimation delays; bad Yelp reviews from customers complaining about these delays; a poor physical office environment; staffing below critical mass; incorrect measurements of windows; poor process from finding a new client to installing windows; transition time and effort for Perry such as obtaining his contractor’s

license; Perry's lack of knowledge; and finally, installers not formally trained. Perry and Ford addressed many of these weaknesses by 2017.

Perry and Ford also concluded that some of TWS's internal strengths could also be considered weaknesses. For example, windows were donated to a worthy charitable cause which aligned with the company's benefit corporation guidelines, however these were the results of mis-measured windows which cost the company dearly. Internal financial indicators showed a dramatic increase in sales and revenue until 2016, but in May 2017, sales were in a slump even following tax season which was unusual. (See Appendix B). Although issues felt insurmountable in May 2017, Perry resolved, that *"If I serve my team with good leadership, we will make it."* Leadership had become an important part of the strategic direction.

### ***Differentiation***

Perry held a strategic planning meeting with Ford and they decided that TWS needed to look for less price-sensitive products and services to differentiate TWS from the competition. He stated, *"I do not care whether it is external or internal; we need something new to change the ball game."* Perry and Ford explored several options in an effort to change the competitive marketplace: product and market specialization such as the preservation of historical buildings; large contract opportunities; expanding their Fleetwood sales, and improving their philanthropic network. One in particular caught Perry's attention which was to lead the industry with new technology and services that addressed pain points such as their issue submitting timely quotes.

Perry had submitted a patent application in 2015 that he had developed with three former engineering students. The basis for this idea was to measure windows from photos by using open computer vision software. Perry had believed that this innovation could open a new market by optimizing the window ordering process by allowing potential customers not skilled in window measuring to forward photos without TWS having to drive to their home. This made sense environmentally.

However, Perry had now familiarized himself with the details of the window replacement industry and realized that taking photos was best suited for selling a small number of windows which was an unprofitable portion of the business. Perry also realized that providing window quotes over the Internet would likely result in a competitive bidding process to the lowest price as Expedia and other consolidators had proven. This lowest price approach was not a valuable business model to him. Over time, he realized that another option could be the development of a software application to optimize the quoting process. Perry wondered how he could employ more recent development approaches such as applying human centered design to his business. He counted that it took approximately 25 keystrokes to enter one window quote and contemplated how he could make this process simpler. Perhaps TWS had potential to incorporate Perry's expertise from teaching mobile development to leverage this as a stand-alone service. Perry realized that to make that dramatic a change, he would need to adopt a more demonstrable leadership model.

### **Financial Performance Indicators and Challenges**

Appendix B provides income statements, balance sheets from 2014 to 2017, and more details about the estimation approaches taken (see Exhibit 4) for key metrics and ratios.

Perry knew from his graduate studies that when financial performance was inconsistent, firms often used traditional and integrative financial techniques to interpret their strategic financial performance (Barney 2010; Wheelen & Hunger 2006). As TWS was managed as a startup firm, short-term profits were not essential; however, some short-term indicators gave management cause for concern (see Appendix B). Perry was aware that traditional integrative financial tools such as the Dupont formula and Altman Z statistic existed to provide a more complete financial picture of solvency by combining traditional ratios in formulary and multivariate statistical formats (Altman 2013; Barney 2010; Wheelen & Hunger 2006).

**Exhibit 4. Key Financial Indicators***Source: Company records, 2017*

(\$ Values)	2014 *	2015	2016	2017 *
Current assets	35,766	104,906	443,159	1,431,614
Current liabilities	75,219	223,920	271,849	1,019,119
Working capital	(39,453)	(119,014)	171,310	412,495
Total assets	123,638	192,878	501,800	1,492,232
Total liabilities	175,219	323,920	371,849	1,119,244
Revenue	261,154	634,961	1,544,672	903,437
Profit/(loss)	(51,5910)	(79,461)	260,781	243,027
Cash and cash equivalents	37,780	88,7752	459,233	1,423,572
Current ratio (absolute)	.5	.5	1.6	1.4
Book value of equity	(51,581)	(131,042)	129,951	372,988

\* Estimates. See Appendix B, Annual Financial Statements for details.

TWS was a benefit corporation with societal goals that went beyond traditional financial goals, so Perry acknowledged that traditional and integrative financial indicators of corporate performance were only the starting point to demonstrate the firm's performance and strategic evaluation. Perry also knew from his graduate studies that nonfinancial indicators were available to reflect the interests of companies and multiple stakeholders. These interests often were reflected in balanced scorecard (BSC) approaches that had gained widespread business interest (David 2009; Kaplan & Norton 1996; Rothaermel 2015; Wheelen & Hunger 2006). Perry remembered that Kaplan and Norton's (1996) BSC approach comprised financial as well as nonfinancial indicators such as customer, internal business perspectives, innovation and learning components, improved strategic planning and evaluation, and leadership. The TWS benefit corporation caused led Perry to think about the triple bottom line of people, planet, and profit as another BSC approach to include the ethical component of TWS (Elkington 2018;

Honeyman 2014; Triple Bottom-line-the Ethical Measure of Business, 2019). Perry was concerned whether his small firm had the resources at this stage to develop these more complex strategic evaluations.

### Decision Focus for the Strategic Direction of TWS

In the three years since Perry first acquired TWS, numerous changes and challenges had happened. (See Appendix A). Perry reincorporated TWS as a benefit corporation and slowly implemented a new business model that focused more on differentiation, innovations in the provision of estimates, and service, and less on a low-cost, low-price strategy. He also changed his leadership style. The financial status of TWS had improved each year since 2014 (see Appendix B), but with the drop in the first part of 2017 caused proactive CEO Perry to wonder, *“What did I learn from past situations that I can continue to use in our 40-year-old startup?”* Two issues in May 2017 led to an important personal and professional crossroads for Perry as well as his company. The company’s sales figures in 2017 were down and rent had increased 400%. In addition, receipt of an urgent letter stating that his contractor’s license was revoked because of a bureaucratic technicality was a total surprise (see Appendix C). Could Perry continue to rely on past strategic models and managerial actions to improve the current downward trend and what role could leadership play? More importantly, what future strategic management and leadership actions could CEO Perry take to address the major internal and external challenges facing TWS?





#### **George L. Whaley**

is Emeritus Professor of Human Resource Management at San José State University. Over the past twenty years, he has authored numerous case studies of companies in the high technology and biotechnology industries. Professor Whaley holds a B.S. in Engineering Mathematics and a M.B.A. from the University of Arizona and Ph.D. in Organizational Behavior from the University of Colorado. He has forty years of combined management, consulting and teaching experience, and serves on the editorial board of several academic journals. His research focuses on Strategic Human Resource Management, Sustainability, Leadership, Diversity and Entrepreneurship, and he teaches Organizational Behavior, Human Resource Management and Organizational Change.



#### **Connie D.M. Allsopp**

is a business and education consultant in private practice, the founder of **The World's Registrar** for online training, and a former supervisor and instructor at the University of Victoria, B.C. Canada. Dr. Allsopp holds a B.Ed. in Literacy and Inclusive Education, an M.Ed. in Administration, and a Ph.D. in Leadership Education from the University of Manitoba, along with a Post Doc. in Program Education from the University of Victoria. She has twenty plus years of teaching, consulting and school leadership at all levels while concurrently working as an entrepreneur in product sales and online marketing. Additionally, she serves on the review board of the *Journal of School Leadership*, and has authored several teacher instructor manuals for Scholastic. She has given S.T.E.M. education talks in China, served on a medical team in Dominican Republic, and constructed a public school in Baja, Mexico. Recently, she launched a not-for-profit dental clinic for children and youth, and now works in a family style dental clinic. Her research focus has been on leadership education, knowledge mobilization, entrepreneurship, strategy, project management, and program evaluation.



#### **Keith C. Perry**

is Director of Engineering Programs in Community Service (EPICS) for the College of Engineering and Industry Professor for the Department of Computer Engineering at San José State University (SJSU). He has also taught for the School of Management and the School of Global Innovation and Leadership in SJSU's College of Business. Recently, he taught for the Biological Sciences Department in the College of Science and for the College of Professional and Global Education at SJSU. He holds a B.S. in Computer Science (Honors) from the University of Manitoba, Canada as well as an M.B.A. and a Master in Software Engineering from SJSU. His forty years of industry experience spans executive positions at numerous technology companies including a technology global Fortune 500, as CEO in multiple startups, and as partner at a venture capitalist. He currently is CEO and owner of The Window Specialist, BK Sales and Services, and a technology startup. He is a frequent keynote speaker to international audiences on entrepreneurship in Silicon Valley and session chair at international IEEE conferences. His research and publications focus on strategy, entrepreneurship, leadership, mobile cloud, and the environment.



## Appendix A

### Company Milestones: Key Events that Shaped the Window Specialist

Source: Authors' notes, 2017

- 1979** Tom From started his own window business after starting in construction after obtaining a degree in business. His grandfather had owned a construction company before him.
- 2008** Perry joined San Francisco's Executives Association and met From, a long-term member.
- 2009** Perry was nominated President of the "Execs" by acclamation as they trusted and respected him.
- 2013** He transformed this 95 year-old non-profit by increasing their awareness of the importance of tasks, focusing on the group rather than personal interests, and activating their higher order needs. His treasurer was outstanding and followed him as president.
- 2014:**
- **Mar 31.** From shook Perry's hand to sell the company to him at 10% of the profits over a 5 year period. Perry started coming to work daily shadowing Jim Ford, the general manager.
  - **May 15.** Perry incorporated Keith C. Perry Holdings as a benefit corporation.
  - **Aug 11.** The assets of The Window Specialist were purchased by Perry's holding company. He met with Ford and they did a SWOT analysis.
  - **Dec.** Perry made his first major changes on the 1-year anniversary from commencing the process to purchase The Window Specialist.
- 2015:**
- **Mar.** The company changed the status of the subcontractors, who had been doing all the installations, to employees of the company. The company also hired a marketing consultant to start the process of rebranding the Company and narrow their focus to best-of-breed solutions.
  - **July.** A previous employee came back part-time and subsequently left his full-time job. The company created a new web site and started using Gmail as its email server.
  - **Oct.** The Company purchased the domain name windowspecialists.com then proceeded to change the company name and email domain to reflect this change.
- 2016:**
- **May.** The company added back one of its historical core strengths of replacing windows for entire apartment blocks while continuing to expand its focus on luxury home owners. TWS finalized their new logo as the next step in rebranding the company.
  - **Oct.** Perry began evolving his duties from COO to CEO. The company also added Milgard to their product line following the old adage, "if you can't beat them, join them."
  - **Dec.** TWS given 30-day notice to move as their landlord would raze the building.
- 2017:**
- **May.** Perry noticed sales remained low and he received notice that his contractor license had been cancelled.

**Appendix B**  
**Annual Financial Statements**

*Source: Company records, 2017*

The following unaudited statements in U.S. dollars are from the company's records. Year 2014 in Exhibit 6, Profit and Loss Statements, includes estimates from January 1<sup>st</sup> until Perry took over on August 11 as well as results from the time Perry took ownership. As the 2014 information in Figure 4, Balance Sheet Statements ending December 31 requires profitability as of Dec. 31<sup>st</sup>, Earnings Before Interest, Tax, Depreciation and Amortization (EBITDA) is broken down by owner, and Perry's portion is reflected in the 2014 Balance Sheet. As the case ends in May 2017, an estimate for the entire year is provided in both Exhibit 6 and 7. The reason for these estimates is to enable year-over-year comparisons. While 5 years is a normal timeframe to compare results, the timing of the acquisition and decision point does not allow for this type of assessment.

**Exhibit 5. Profit & Loss Statements (unaudited)**

	2014 *	2015	2016	2017 *
Revenue	261,154	634,961	1,544,672	903,437
Cost of Goods Sold	149,515	489,878	1,126,449	418,578
Gross Profit	111,639	145,083	418,223	484,859
Operating Expenses				
Startup Expenses	9,965			
Payroll Related	109,116	76,946	87,545	128,919
Office Rent & Expenses	19,970	35,449	22,752	42,069
Travel & Entertainment	39,788	43,799	12,207	7,395
Technology	224	3,210	8,176	10,014
Marketing and Sales	12,462	32,183	21,775	47,103
Total Operating Expenses	198,652	224,544	157,422	241,833
Profit EBITDA ***/(Loss)				
Perry	(51,591)	(79,461)	260,781	243,027
Previous Owner	(35,422)			
Combined	(87,014)			

\* Estimate

**Appendix B cont.**  
**Annual Financial Statements**

**Exhibit 6. Balance Sheet Statements ending Dec 31st (unaudited)**

	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017 *</b>
<b>Current Assets</b>				
Cash	596	29,204	361,403	1,404,101
Accounts Receivable	1,244	57,260	95,814	17,454
Prepaid Expenses	33,926	273		
Inventory		18,169	(69,358)	(39,400)
Other Current Assets			55,300	49,459
<b>Total Current Assets</b>	<b>35,766</b>	<b>104,906</b>	<b>443,159</b>	<b>1,431,614</b>
<b>Fixed Assets</b>				
Total Intangible Assets	85,566	85,566	58,369	47,566
Total Tangible Fixed Assets	2,306	42,406	273	13,052
<b>Total Fixed Assets</b>	<b>87,872</b>	<b>87,972</b>	<b>58,642</b>	<b>60,618</b>
<b>Total Assets</b>	<b>123,638</b>	<b>192,878</b>	<b>501,800</b>	<b>1,492,232</b>
<b>Current Liabilities</b>				
Accounts Payable	3,326	46,514	56,394	99,790
Credit Cards & Line of Credit	6,959	59,714	94,230	386,247
Deposits on Jobs	0	18,113	6,000	146,007
Due to K. Perry	32,788	99,288	97,926	95,351
Truck Loan			(9,000)	(9,000)
Payroll Liabilities	32,146	351	26,299	300,723
<b>Total Current Liabilities</b>	<b>75,219</b>	<b>223,920</b>	<b>271,849</b>	<b>1,019,119</b>
Long Term Liabilities	100,000	100,000	100,000	100,125
<b>Total Liabilities</b>	<b>175,219</b>	<b>323,920</b>	<b>371,849</b>	<b>1,119,244</b>
<b>Equity</b>				
Retained Earnings		(51,591)	(130,830)	129,951
Net Income	(51,591)	(79,460)	260,781	243,027
<b>Total Equity</b>	<b>(51,591)</b>	<b>(131,051)</b>	<b>129,951</b>	<b>372,978</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>123,628</b>	<b>192,868</b>	<b>501,800</b>	<b>1,492,222</b>

\* Estimate

Appendix C. Letter from Contractors State License Board

Source: Company records, 2017



**CONTRACTORS STATE LICENSE BOARD**  
9821 Business Park Drive, Sacramento, California 95827  
Mailing Address: P.O. Box 26000, Sacramento, CA 95826  
800.321.CSLB (2752) | [www.cslb.ca.gov](http://www.cslb.ca.gov) | [CheckTheLicenseFirst.com](http://CheckTheLicenseFirst.com)

STATE OF CALIFORNIA  
Governor Edmund G. Brown Jr.

THE WINDOW SPECIALIST  
DBA TWS WHOLESALE  
14733 CATALINA ST  
SAN LEANDRO, CA 94577

**DATE:** 05/15/2017  
**LICENSE:** 1002989

**NOTICE OF LICENSE SUSPENSION**

**Appendix D. Interviews with CEO**

Source: Authors' notes, 2017

Interview data was collected from Perry, staff surveys, and company data. It serves to illustrate Perry's decisions and the impact they had on staff, customers and suppliers during his ownership.

**Exhibit 7. Interview with Perry**

Year	Decisions	Impact for Staff, Clients & Suppliers
2014 March- Start Up	<ul style="list-style-type: none"> <li>-TWS sold after 37 years in business</li> <li>-No \$ down</li> <li>-10% of above average profits for 1<sup>st</sup>- 5 years go to Tom From</li> <li>-Transfer complete to KCP on Aug 11, 2014</li> </ul>	<ul style="list-style-type: none"> <li>-Retained Jim Ford which provided a smoother transition</li> <li>- Re-offered TWS to Jim Ford before purchasing it</li> <li>-Ownership shift to Perry</li> <li>-2014 Protecting new company from pre-2014 liability claims</li> <li>- Honoring pre 2014 warranty claims</li> <li>-Incorporating as a benefit corporation</li> <li>- Perry opted for no salary</li> </ul>
2014 March- Year 1	<ul style="list-style-type: none"> <li>-Tracking Daily Operations</li> <li>-Internal changes</li> </ul>	<ul style="list-style-type: none"> <li>-Shadowed Ford to learn what works or doesn't work</li> <li>-No changes made on white board calendaring, landline phones, or fax machine</li> <li>-Didn't change company website</li> </ul>
2015 March- Year 2	<ul style="list-style-type: none"> <li>-Valuing People &amp; Staff Survey</li> <li>-Developing people</li> <li>-Building community</li> <li>-Displaying authenticity</li> <li>-Providing leadership and highlighting staff</li> <li>-Ordering system updated to online for vendor</li> <li>-Building a sales force to scale contracts</li> </ul>	<ul style="list-style-type: none"> <li>-Set financial goals</li> <li>-Acted on staff's feedback</li> <li>-Developed staff and use of technology such as google calendars</li> <li>-Changed contractors to employees</li> <li>-Improved turnaround and accuracy of orders with an online system</li> <li>-Obtained larger contracts to increase profit margins with a "scale, scale, scale" mantra</li> <li>-Helped Cavenecia increase productivity so he could earn more</li> <li>-Used cloud-based phone system</li> <li>-Developed stronger relationships with suppliers, and capitalized on their strengths</li> <li>-Praised employees for individual successes</li> </ul>
2016 March- Year 3	<ul style="list-style-type: none"> <li>-Moved as landlord raised rent thus cost went up by 400%</li> <li>-Be a shining light for others</li> <li>-Focus on needs &amp; emotions of others</li> <li>-Selfless leadership consideration</li> </ul>	<ul style="list-style-type: none"> <li>-Improved ethical leadership</li> <li>-Built a sense of community</li> <li>-Helped TV station uncover fraud</li> <li>-Flew Cavenecia to Peru for a family visit</li> <li>-Promoted Martin to crew chief</li> <li>-Hired a salesperson and invested 9 months of training</li> <li>-Bought a pick-up truck for Cavenecia when his broke down</li> <li>-Donated windows to Mexico &amp; created showers for homeless</li> </ul>
2017 March- May 1 <sup>st</sup> Year 4	<ul style="list-style-type: none"> <li>-Ruminate on growth options</li> <li>-Concern for bankruptcy</li> <li>-Desire for turnaround</li> <li>-Questions for Leadership styles &amp; Entrepreneurship models</li> </ul>	<ul style="list-style-type: none"> <li>-Managed time by reducing his teaching</li> <li>-Determine how to grow TWS</li> <li>-Determine what leadership style to use next</li> <li>-Determine what needs attention going forward</li> </ul>

**Appendix E. Survey Results**

Source: Company records, 2019

Below are the results of various perspectives on KCP’s leadership style by from salesperson, installer, and suppliers, specifically related to tasks completed and leadership.

**Exhibit 8. Perry’s Leadership Survey Results**

Employee	Task-People (T-P) Shared Leadership		Situational Leadership Category Scores			
	T	P	Primary Flexibility	Secondary Effectiveness		
Perry	10	14	S3	S4	20	52
Full time Salesperson	16	13	Not completed			
Installer	14	11	S3	S2	24	51
Supplier	17	11	S3	S1	22	56

Note:

The T score is similar to Theory X and P score is similar to Theory Y

S1 score is similar to Theory X and S3 is similar to Theory Y

The norm range for flexibility scores is 10-18 points with a mean of 14

The norm range for effectiveness scores is 41-51 points with a mean of 46

## References

- Altman, E. I. (2013). Predicting financial distress of companies: Revising the Z-Score and ZETA models. *Handbook of Research Methods and Applications in Empirical Finance*, 428.
- Barney, L. (2010). *Gaining and Sustaining Competitive Advantage* (4<sup>th</sup> Ed.) Upper Saddle River, NJ: Pearson Prentice Hall.
- David, F. R. (2009). *Strategic Management: Concepts and Cases*, (12<sup>th</sup> Ed.). Upper Saddle River, NJ: Pearson Prentice Hall.
- Dennis, R. S., & Bocarnea, M. (2005). Development of the servant leadership assessment instrument. *Leadership & Organization Development Journal*, 26(8), 600-615.
- Elkington, J. (2018, June 25). 25 years ago I coined the phrase “triple bottom line.” Here’s why it’s time to rethink it. *Harvard Business Review*. June 25, 2018. Retrieved from <https://hbr.org/2018/>
- EPICS. (2016). Retrieved from <http://sites.google.com/a/sjsu.edu/epics-sjsu/>
- Fleetwood. (2017). Retrieved from [www.1.fleetwoodusa.com](http://www.1.fleetwoodusa.com)
- Goldratt, E. M. (1990). *Theory of Constraints*. Great Barrington, MA: North River Press.
- Grant, K. (2008). Who are the lepers in our organizations? A case for compassionate leadership. *Business Renaissance Quarterly*, 3(2), 75.
- Honeyman, R. (2014). *The B Corp handbook*. San Francisco, CA: Berrett-Koehler Publisher, Inc.
- Hunter, J. (1998). *The servant*. New York, NY: Crown Business.
- Kaplan, R. S., & Norton, D. P. (1996). *Using the Balanced Scorecard as a strategic management system*. Boston, MA: Harvard Business School Press.
- May 25, 2016 interview, Channel 2 Fox TV. <http://www.ktvu.com/news/2-investigates/145006734-story>
- McGahan, A. M. (1999). Competition, strategy and business performance, *California Management Review*, 41(3), 74-101
- McGahan, A. M., & Porter, M. E. (2005). Comments on the industry, corporate and business segment effects and business performance: A non-parametric approach by Ruefli and Wiggins. *Strategic Management Journal*, 26: 873-880.
- Parolini, J., Patterson, K., & Winston, B. (2009). Distinguishing between transformational and servant leadership. *Leadership & Organization Development Journal*, 30(3), 274-291.
- Parris, D. L., & Peachey, J. W. (2013). A systematic literature review of servant leadership theory in Organizational contexts. *Journal of Business Ethics*, 113(3), 377-393.
- Porter, M. E. (2008, January). The five competitive forces that shape strategy. *Harvard Business Review*, January 2008.



Reed, L. L., Vidaver-Cohen, D., & Colwell, S. R. (2011). A new scale to measure executive servant leadership: Development, analysis, and implications for research. *Journal of Business Ethics, 101*(3), 415-434.

Rothaermel, F. T. (2015). *Strategic management concepts*. Chicago, IL: McGraw Hill.

Stone, G. A., Russell, R. F., & Patterson, K. (2004). Transformational versus servant leadership: A difference in leader focus. *Leadership & Organization Development Journal, 25*(4), 349-361.

Triple Bottomline- the Ethical Measure of Business. (2019). Retrieved from <https://arthamoney.com/people-planet-profit-triple-bottom-line-the-ethical-measure-of-businesses-53750035035f>

U.S. Economy (May, 2017). Federal Reserve Bank of New York, Research and Statistics Group, New York, NY

Wheelen, T., & Hunger, D. (2006). *Concepts in strategic management & business policy, 10th.* (10<sup>th</sup> Ed.). Upper Saddle River, NJ: Pearson Prentice Hall.

Yelp. (2017). Retrieved from [www.yelp.com](http://www.yelp.com)

## **CIRQUE DU SOLEIL: INNOVATION IS MORE CULTURE THAN PROCESS**

**ISSAM GHAZZAWI**  
University of La Verne

*“From their employees, artists, technicians, and managers around the world, great expectations, magnificent dreams, and creative products have emerged. They have learned to surrender to their senses, trust their instincts, take risks, and meet new challenges in an artistic and nurturing environment.”*

Guy Laliberté Founder and Past CEO, Cirque du Soleil<sup>1</sup>

Cirque du Soleil (French for Circus of the Sun) had evolved as one of the most famous live spectacles and success stories in the history of the entertainment industry. While Cirque du Soleil’s various performances had transformed over the years, its traditional elements of imagination, artistic entertainment, spectacle, theatrical storytelling, visual extravaganza, and incredible physical skill had remained at the core of this entertainment giant.

As Cirque turned thirty-six years old, most of its artists and employees had heard stories of its past. They learned about Guy Laliberté’s struggles with work as a youth and his supporting himself on unemployment insurance. They were told about Cirque’s beginning as a group of street performers in the picturesque village of *Fête Foraine de Baie-Saint-Paul* near the St. Lawrence River just outside of Quebec City, and very importantly its financial hardship at its beginning in the 1980s (DeLong & Vijayaraghavan 2002; Ghazzawi, Martinelli-Lee & Palladini 2014).

---

<sup>1</sup> A forward by Guy Laliberté for the book by Heward, L. & Bacon, J. (2006). *The Spark: Igniting the Creative Fire that Lives Within Us All*. Doubleday Canada.

A turning-point for the company happened in 1987, when it embarked on its first tour in the U.S. It started with an invitation to perform at the Los Angeles Arts Festival; Cirque took a big risk in going to Los Angeles as it only had enough money to travel one way and counted on its ability to raise funds to get back to Montreal. What happened in Los Angeles - positive media reviews and audience support - led Cirque to tour other cities in California. Its success in the U.S. helped solidify its reputation and prestige at home (Leslie & Rantisi 2011).

For over three decades, Cirque held shows around the globe. Customers lined up to buy its expensive tickets, and money was easily made. At the end of the day, the Cirque entertainment phenomenon had permanency. Together with its sustainable culture of innovation, strong communication, and ethical behavior in its worldwide operations, Cirque maintained relational trust among all stakeholders while living and functioning as one company (Ghazzawi, et al. 2014). With an estimated \$845 million in revenue in 2014 (CBC.CA 2015), Cirque du Soleil expanded rapidly through the 1990s and 2000s, going from one show to 19 shows simultaneously in over 200 cities on five continents around the world. The company's various shows attracted close to 90 million spectators (Cirque du Soleil-c).

Cirque's culture, according to one of Cirque producers, was *"very open and accepting of people and open to doing things in different ways. You can invite problems or you can offer solutions"* (Ricotta 2013). The working environment was good-natured, with considerable freedom given to employees and artistic directors. The behavioral norms and values resulted in affirmation of family, or at the very least community (Ghazzawi et al. 2014).

The company's continued success was driven by its continual innovation and creative culture. Cirque's creative process usually began when its president and CEO Daniel Lammare and Guy Laliberté, its founder and artistic director, defined the theme of the next show. The theme of any show started as a broad vision as opposed to a confined mandate, in order to give others the opportunity to contribute to the creative process. Cirque executives did not use traditional brainstorming techniques to arrive at the theme (Dan 2012). Cirque CEO's belief was that *"no-*

*idea-is-a-bad-idea;*” acquiescence and consensus were emphasized over debate and openness (Dan 2012).

*“Cirque’s culture of innovation and creativity encourages honesty and judgment when ideas are explored. Passionate, provocative dissent and disagreements are not only tolerated but cultivated, to spur the best ideas and, as importantly, to eliminate bad ones quickly. While a consensus seeking approach may lead to a few incremental innovations, he (Lammare) says, a bit of tension, even friction during creative ideation, is likely to lead to innovation breakthrough” (Dan 2012: Para. 3).*

See Exhibit 1 for selected images of Cirque shows.

### Exhibit 1. Selected Images from Cirque Du Soleil Shows

Source: <https://www.cirquedusoleil.com/press>



**Title:** Cadre from "O".

**Picture credit:** Tomasz Rossa

**Costume credit:** Dominique Lemieux.



**Title:** Hand Balancing from "Mystère"

**Picture credit:** Richard Termine

**Costume credit:** Dominique Lemieux

It was Cirque’s practice that once a theme had been selected, Lammare and Laliberté would step back and let the creative director take over and develop the concept over the 2-3 years that it took to put the show together (Dan 2012).

In addition to its world-renowned shows, Cirque had extended its creative approach to a variety of other entertainment forms, including multimedia productions, immersive experiences, theme parks, and special events. The company went beyond its creative activities by making a

positive impact on people, communities, and the planet - all through Cirque's valuable tools of creativity and art.

In 2015, ninety percent of Cirque was acquired. President and CEO Daniel Lammare and Founder and Artistic Director Guy Laliberté were revisiting the challenges of balancing the company's need to maintain high creative standards with an appeal to larger audiences, while meeting their new partners' financial expectations and remaining loyal to Cirque's values.

### The Creation of a Powerful Entertainment Company

Guy Laliberté left home at the young age of 14. He left behind a note to his anguished parents explaining the reasons for his bold act and quoting the philosopher Kahlil Gibran: "*Your children are not your children. They are the sons and daughters of life's call to life*" (in Denton, 1988: Para. 7). Guy described himself as a "*dreamer, fascinated by the cultures of the world.*" For him, the best way to see the world was to perform on the streets. He performed for a while as a musician, playing traditional Canadian music on an accordion while he told stories and collected money in a hat from passersby. Feeling confident in his street performance skills, Laliberté decided to travel to Europe when he was eighteen (Browse Biography 2011).

As he was attracted to the busker's<sup>2</sup> lifestyle from a young age, he travelled to Paris in 1978 and learned the art of fire-breathing. After coming back to Québec in 1979, he began stilt-walking alongside his friend Gilles Ste-Croix while the two were organizing activities for the Baie-Saint-Paul youth hostel in the Charlevoix region of Québec<sup>3</sup> (Zarov 2014). See Exhibit 2 for images of Charlevoix, Canada.

---

<sup>2</sup> Busking and street performing is the art of street theatre. It is a style of performance unlike any other. A musician playing in the open air - tap dancers hoofing on a side walk. Source: <http://www.buskercentral.com/defined.php>

<sup>3</sup> Charlevoix is a beautiful region of the province of Quebec, Canada. Famous for its idyllic topography of rolling hills and mountains along the St. Lawrence River, the region is very attractive to visitors because of its agricultural tourism and regional farm-to-table cuisine, arts and culture, and scenic driving routes (McLean 2019).

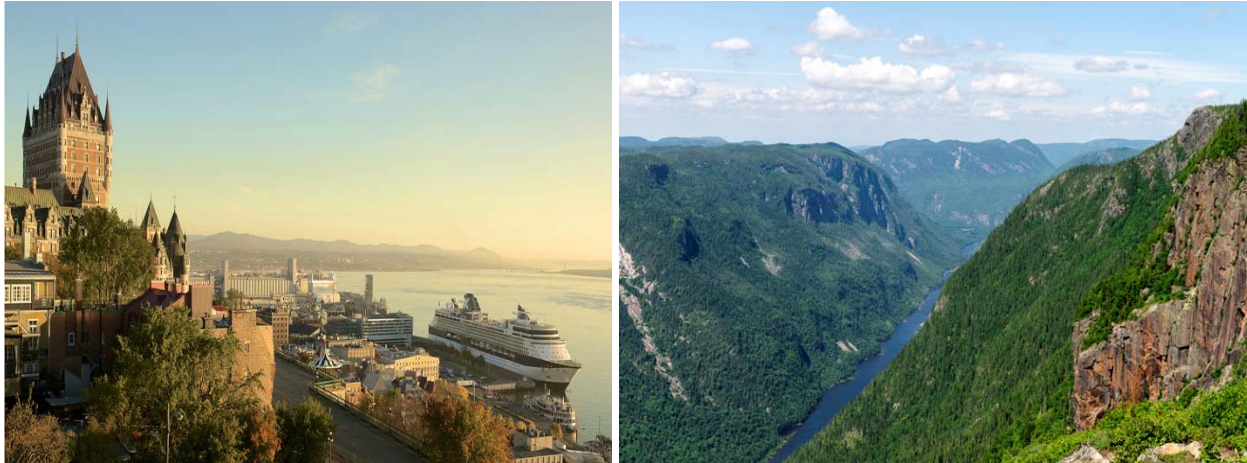
Guy did not have enough money to sustain his life in Europe, so eventually he returned to Quebec to accept a full-time job at a hydro-electric power plant. After three days, the plant workers went on strike and Guy was fired (Bass 2013).

In summer 1980, Laliberté joined Ste-Croix's stilt-walking theatre company *Les Échassiers de Baie-Saint-Paul* (The Stilt Walkers of Baie-Saint-Paul). The following year, Ste-Croix and Laliberté, along with stilt-walkers Serge Roy, Josée Bélanger and Carmen Ruest, founded the non-profit *Club des Talons Hauts* (High Heels Club) to promote stilt-walking events (Zarov 2014).

With financial help from the government of Québec, Laliberté founded Cirque du Soleil in 1984. The Cirque toured Québec, and its big top had a capacity of 800 seats (Zarov 2014). The tour performers and productions were such a success that the company began to generate demand outside of Canada.

### Exhibit 2. Images of Charlevoix, Canada

Source: <https://www.bing.com/images/>



In 1985, the tour included stops in Ottawa, Toronto and Niagara Falls. In 1986, Cirque produced a new show, *La Magie Continue* (“*We Reinvent the Circus*”), which toured Canada, the U.S. and Europe. When it finally closed in 1990, the big top's capacity was 2,500 seats. Two years later, the Cirque would be running simultaneous shows on three continents (Zarov 2014). According to Tony Ricotta, Laliberté had a dream to reinvent the circus to the level of an art form. This

dream was encapsulated in the company's mission statement: *"To invoke the imagination, provoke the senses, and evoke the emotions of people around the world"* (Ricotta 2013).

Laliberté's artistic innovation bridged the entertainment culture of the circus with the artistry of acrobatic performance. See Exhibit 3 for an image of Cirque's big top.

With the creation of Cirque du Soleil, the mischievous days of popcorn, peanuts, sawdust, spangles, and calliopes were gone! Cirque was a hybrid of acrobatics and dance performance (Berry et al. 2006). This venue was *"a multi-level production without the menagerie of exotic animals, yet was one that captured the magnificence of the human form, agility, and creativity"* (Ghazzawi et al. 2014: 26-27).

Cirque du Soleil Entertainment Group became a world leader in live entertainment with about 4,000 people, including about 1,300 artists from nearly 50 countries who entertained over 180 million spectators with shows in about 450 cities in 60 countries. With Cirque's 28 residential and touring performances around the globe, the company's revenue was estimated to be more than \$1 billion annually (Gittleson 2013).

### Exhibit 3. An Image of Cirque Du Soleil Big Top

Source: [http://www.flyingkite.com/galleries/Features/2013/Issue\\_126/totem\\_fp02.jpg](http://www.flyingkite.com/galleries/Features/2013/Issue_126/totem_fp02.jpg)



From 1984 until 1989, Cirque performed only one show at a time. Its productions were divided into shows designated as either resident or touring. Resident indicated one location only, whereas touring indicated visits among cities. See Appendix 1 for Cirque's comprehensive list of resident and touring shows, Appendix 2 for important dates, and Exhibit 4 for an image of a resident show "Mystère" and one from a touring show "Alegria."

With Cirque's worldwide popularity across the world, its success came with a few challenges and organizational disputes including "artistic rebellions" and partnership clashes (DeLong et al. 2002). In 1998, Laliberté bought out Gautier's share and retained full control of Cirque which was valued at \$800 million at the time. On March 1, 2006, Laliberté resigned and was succeeded by Daniel Lamarre. Lamarre, who joined the Cirque executive team in 2001, maintained the title of Founder and Guide (Ghazzawi et al. 2014).

In 2015, Cirque du Soleil was acquired for an estimated \$1.4 billion. The company's founder, Guy Laliberté, retained a ten percent stake in Cirque, and ninety percent were acquired by three parties: TPG Capital (Texas Pacific Group-an American investment company), Fosun International Limited, a Chinese international investment company, and Caisse de Dépôt et Placement du Québec (CDPQ)<sup>4</sup>, also referred to in English-language media as the Caisse (Palmeri 2015).

---

<sup>4</sup> Caisse is an institutional investor that manages several public and parapublic pension plans and insurance programs in Quebec, Canada (CBC.CA, 2015).



#### Exhibit 4: Selected Images from Cirque Resident "Mystère" and Touring "Alegria" Shows

Source: <https://www.cirquedusoleil.com/press>



**Title:** Spermato and Spermatines from "Mystère"  
**Picture credit:** Richard Termine  
**Costume credit:** Dominique Lemieux.



**Title:** Crossed Wheel from "Alegria".  
**Picture credit:** MA Lemire ©2019 Cirque  
**Costume credit:** Cirque du Soleil

In 2014, the year before the acquisition, Cirque brought in \$845 million in revenue. In the same year, all the shows on Broadway combined brought in \$1.37 billion (CBC.CA 2015). Recognized over the world, Cirque du Soleil had constantly sought to evoke imagination and provoke emotion.

### Competitive Landscape of the Performing Arts Industry

Companies in the performing arts industry primarily engaged in producing live presentations involving the performances of actors and actresses, singers, dancers, musical groups, artists, and other performers (BusinessDataCodes.com). The U.S. performing arts industry included more than 8,000 companies and employed more than 120,000 people. There were also a large number of self-employed artists (Pearson 2019). The performing arts industry earned about \$35 billion per year (Vault.com). Growth in revenue was 1.8 percent annually from 2011 through 2016, due to the sluggish economy and federal and state budget cuts. Local government support for the arts had dropped 18 percent, and state funding fell 27 percent.

The recession resulted in less disposable income, and less spending on arts and entertainment. However, the outlook for the industry was brighter through 2020, as the economy was getting stronger and spending on performing arts had improved (Vault.com).

Demand for performing arts was driven by personal income and leisure time. The profitability of individual performing arts companies was based on what audiences wanted to see. While

*“large companies have advantages in marketing, fundraising, and attracting star performers. Small companies can compete effectively by specializing in new, unique, or popular works. The U.S. industry is fragmented: the 50 largest companies account for less than 30% of revenue”* (Hoovers.com).

In addition to show admission fees, performing arts companies were motivated to obtain revenue from contract and residual fees, licensing agreements, royalty fees, and in some cases private contributions and government grants (Ghazzawi et al. 2014). Admissions accounted for 45% of industry revenue, contract fees 25%, and private contributions 15%. Other revenues included food, beverage and merchandise sales, facility rentals, membership dues, and fees for entertainer management, advertising, and endorsements (Hoovers.com).

### ***Cirque du Soleil’s Top Competitors***

As an entertainment powerhouse, Cirque’s competitors were all companies in the performing arts industry, including Dodger Properties, Feld Entertainment, Jujamcyn Theaters, Live Nation Entertainment, Nederlander Producing Company, Renaissance Entertainment, Shubert Organization, and TBA Globa. Its top direct competitors were Feld Entertainment and Live Nation Entertainment. See Exhibit 5 for Cirque Top Competitors.

**Exhibit 5. Cirque du Soleil Top Competitors***Source: Hoovers.com*

<b>Company's Name</b>	<b>Gross Revenue</b>	<b>Net Profit Margin</b>	<b>Net Operating Cash Flow</b>
*Cirque du Soleil	\$ 342.9	N.A.	N.A.
*Feld Entertainment	\$ 1,368	N.A.	N.A.
Live Nation Entertainment	\$10,787	(0.16 %)	\$941.59M

\* Figures in USD millions. Figures are estimated as these companies are privately held and do not publish financial information (CBC.CA 2015).

**Feld Entertainment**

With a focus on clowning, Feld Entertainment was one of the largest live entertainment producers in the world. The company entertained people in North America through its centerpiece, Ringling Bros. and Barnum & Bailey Circus, which visited about 120 cities annually. The Ringling Bros. and Barnum & Bailey Circus made its first performance in 1871. Feld Entertainment, through its partnership with Walt Disney, produced “*Disney on Ice*” shows, “*Treasure Trove*,” and “*It’s Disney Live!*”

**Live Nation Entertainment**

A U.S. global company founded in 2010 by the merger of Live Nation and Ticketmaster, Live Nation Entertainment was the world's largest ticket seller and promoter of live entertainment. Live Nation Entertainment operated more than 220 venues in North America and Europe (D&B Hoovers). Over 580 million people attended Live Nation events per year. Live Nation owned House of Blues venues through HOB Entertainment and dozens of prestigious concert halls. Additionally, the company owned a stake in more than 500 artists’ music, including albums, tours, and merchandise (Hoovers.com 2019-b). Live Nation had offices in 40 countries and performing venues in 11 (D&B Hoovers).

## Culture and Creativity at Cirque

Lynn Heward, Cirque's former president of creative content, credited the company's growth with its culture of innovation and creativity. In his own words,

*"Cirque du Soleil has been a world-renowned laboratory of creativity, enthraling audiences around the world by fusing dazzling acrobatics, staging and choreography, and music, along with beautiful costumes and technical effects to inspire and create magical, almost otherworldly theatrical experiences" (Heward & Bacon).*

This sentiment was resonated when Cirque founder Guy Laliberté provided a *forward* to a storybook about Cirque titled, *The Spark: Igniting the Creative Fire that Lives within Us All* by Heward and Bacon. Laliberté wrote:

*"Their stories - the people of Cirque du Soleil - are real. From their great expectations and "magnificent dreams," creative products have emerged. They have learned to surrender to their senses, trust their instincts, take risks, and meet new challenges in an artistic and nurturing environment. They work alone and they work together learning to connect with and touch people in new ways, endeavoring always to reinvent themselves. And they aspire to give back to the world in the endless continuum of change, exchange, and renewal; they are catalysts... From a tiny spark a great fire was kindled, and its flames warmed the world."*

New employees and artists were transmitted Cirque's underlying cultural values through stories. Some of the stories were about Guy Laliberté leaving home at the young age of 14. He quoted the philosopher Kahlil Gibran when he wrote a note to his family: *"Your children are not your children. They are the sons and daughters of life's call to life"* (Denton 1988). Employees were also told that Guy Laliberté was attracted to the busker's lifestyle from a young age; he started as a street performer.

The company's culture was open, nurturing, and accepting of people. It was open to doing things in different ways, and it encouraged people to take risks. This organizational culture accepted that *"there was no single formula for creative success - each of us must unlock the power of our imagination in our own way"* (Heward & Bacon). Artists remarked that what

ignited their creativity wasn't the pressure of deadlines but instead the exhilaration that came from risking it all. The culture changed the way they lived and worked as they felt creative and had the opportunity to tap into the powerful force that was Cirque (Heward & Bacon 2006).

### ***The Street: The Origin Cirque's Organizational Culture***

The culture at Cirque was rooted in its street performances. *"In the street you take a lot of risks, you never know how people will react"* (Leslie & Rantisi 2011: 1775). The founding father of Cirque had toured Europe, performing the arts of busking, fire-breathing, juggling, and stilt walking. The street was also the origin of the of the risk-taking entrepreneurial culture of the company (McGuire 2003). The ability to accept risk, uncertainty, inefficiency, and react to the needs of the audience helped Cirque to sustain a culture of continuous innovation and change. One creative director at Cirque asserted that his early experience working on the streets developed his communication skills needed to assemble a team of creative artists (Leslie & Rantisi 2011).

Street culture was well integrated in some of Cirque shows, for instance in the 1006 show *"Quidam."* Quidam meant *"a nameless passer-by, a solitary figure lingering on a street corner, a person rushing past and swallowed by the crowd."* It could have been anyone in the crowd, a member of the silent majority, or the one who cried out. The show as it was explained by the show director was for all the *"quidams"* whom this show allowed to speak - finally emerged from anonymity (Cirque Du Soleil-d).

Another show in the early nineties was *Saltimbanco*, Italian for *"jump on a bench."* The show explored *"the urban experience in all its myriad forms: the people who live there, their idiosyncrasies and likenesses, families and groups, the hustle and bustle of the street and the towering heights of skyscrapers"* (Yelp.com).

In sum, Cirque's company's culture was enriched with its humble beginning, street experiences, and street performing hippies who did not need more than their circus-like talents.

### ***Cirque Values, Dominant Culture and Subcultures***

Cirque had developed cultural values and norms that strongly emphasized the need for employees to be empowered, to experiment, and to take risks. While the varied productions, departments, and locations across the organization differed in some practices, they united along the organization norms and values. Ricotta (2013) recounted from Cirque's initial beginnings:

*“Those values [that] were created when we first began this company were such strong emotional values that they're almost impossible to erase and we wouldn't want to change them. ... there is no dipping in the values when you become part of the company. You just know that they are there and people make you fully aware. Further, they are not posted on the wall but somehow they get to you. At the heart of it all, Cirque sees itself as a global citizen. And it is doing its job for a purpose. I know it's going to sound trite, to make the world a better place, and we do that through entertainment.”*

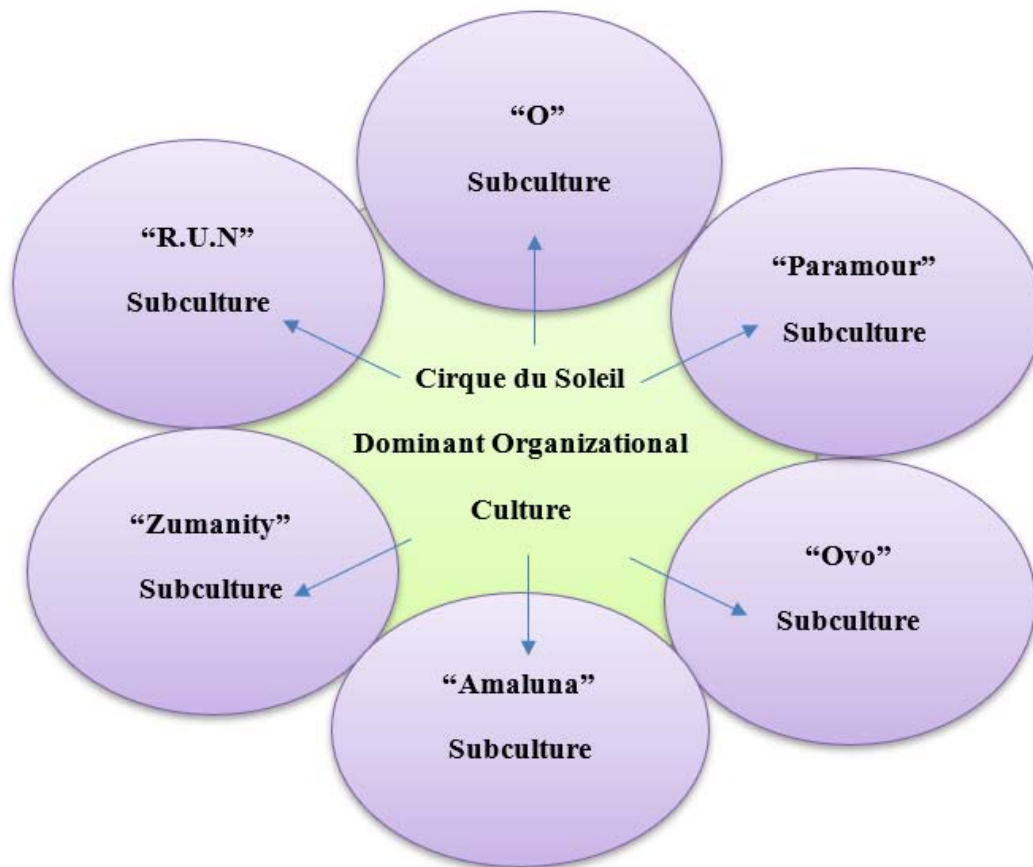
The key to the company's cultural success was that its employees and artists lived up to Cirque espoused values and practiced norms, the “*Cirque unwritten rules*” that successfully guided the way its people worked and treated each other. Laliberté's leadership philosophy was built on his knowledge and artistic experience. As a leader, Laliberté was both paternalistic and protective of his performers' creative outlets and comfort capacities (DeLong & Vijayaraghavan 2002; Ghazzawi et al. 2013). Cirque's philosophy was that if it could sustain the performers' “*happiness*” then the audience/spectator would no doubt experience an emotionally driven, memorable, glitzy performance. “*This invaginate blanket served to establish Cirque's organizational norms and values. Thus, protection of a disparate and diverse band of performers resulted in motivating performers to excel in a one-of-a-kind entertainment excellence*” (Ghazzawi et al. 2013: 41).

While the prescribed culture manifested the values and norms shared by Cirque's majority members, as a large company, Cirque had subcultures that were based on the characteristics of their own departments, shows, or geographical locations. See Exhibit 6 for an illustration of the organization's culture and sub-cultures as conceptualized by the author of this case.

Cirque was a company with a cause. Its people were “*citizens of the world;*” they lived and company values. They practiced it by showing joy, showing love, showing hardship, showing pain, and somehow getting people involved (Ghazzawi, et al. 2014).

### Exhibit 6. Organizational Culture and Subcultures\*

Source: Author’s notes



\* **Subcultures** exist within parts of the organization rather than entirely throughout them. The above illustration does not cover all of Cirque shows, locations, or departments; it is merely meant to illustrate subcultures.

### ***Empowerment and Collaboration: Micro-Management is Not an Option***

The working environment at Cirque was good-natured, with a substantial freedom given to artists and employees. According to Dan (2012), once a Cirque theme was decided upon, Lammare and Laliberté empowered the creative director of that particular show to take over

for the purpose of developing the concept over the 2-3 years that were needed to bring the show to life. Both corporate leaders reviewed progress every 6 months,

*“but in order to encourage collaboration they do not dictate changes, simply point out what doesn’t work, and leave it to the creative director and the troupe to come up with solutions. The pair’s focus is on quality control, and making sure that the product unfolds within the original vision that they created, without micro-managing the “line executives” who are responsible for putting the show together”* (In Dan 2012: Para. 3).

Empowerment at Cirque was relevant to establishing directions and boundaries as opposed to micro-managing people. The empowerment aspect of Cirque was described by a performer who suggested:

*“We don’t have a big history of circus. When you go to Europe, they have 250 years of family circus, of circus schools, of people, for us it’s all new, so everything is merging right now ... We can still do what we want with it because it’s only 25 years old”* (in Leslie & Rantisi 2011: 1776).

As opposed to calling all the shots, managers at Cirque granted employees the autonomy to take charge of what they did. According to Grabher (In Fuchs & Shapira 2005: 65):

*“Diversity allows evolution to follow... The proliferation of a broad spectrum of different organizational forms and diverse practices - as opposed to the diffusion of a single “best practice” - provides a richer “selection environment” for regions, firms and individual actors to co-evolve.”*

As empowerment was well connected to innovation, Cirque leadership cemented this belief when stating,

*“As with any artistic endeavor, inspiration plays a big part in the creative process, but Cirque’s approach to innovation, while intuitive, is guided by a deep commitment to R&D as the catalyst of the creative spark”* (In Dan 2012: Para. 5).

The outcomes of empowerment were satisfied artists and employees who were innovative, creative in what and how they performed, and who felt a sense of achievement.



### ***Embracing Creativity and Innovation through Partnership***

To keep its creative brand fresh, Cirque believed that it was critical to strive for collaboration beyond its yellow-and-blue striped tent (Dan 2012). An important aspect of Cirque's culture was its openness to the outside world, and willingness to cooperate and embrace others' ideas. According to Leslie and Rantisi (2011: 1777),

*"the presence of interrelated and complementary industries suggest the importance of 'path interdependence'—situations where the path-dependent trajectories of different industries are mutually reinforcing."*

Cirque searched for talent all over the globe, both online and with in-country trend-spotters (Dan 2012). The company utilized a global network of talent scouts to discover new performers, and it relied on research

*"... within its own extensive archives that contained thousands of books, videos, musical scores, and images to establish accuracy of details. Scores of researchers feed information of what's "cool" and unique that allows the creative directors to determine the relevancy and appeal of the new show" (Dan 2012: Para. 5).*

Stephan Haves, a Master Teacher and Cirque consultant asserted that,

*"Technology nearly surpassed the artistry with seamless hologram projections and lasers that it becomes so immersive for the public that it has become a new generation [of entertainment]. The technology is . . . exponentially more incredible, an indication that via technology the future of the circus will be to the point of intoxication."*

Marc Gagnon, head of Enterprise Architecture at Cirque, commented on this relationship when stated:

*"Creativity and innovation are in our DNA... It's what we've been doing for decades. Using technology as a tool for intentional and frequent innovation is at the core of our strategy to become the world leader in live entertainment" (Newswire Today 2018: Para. 3).*

See Exhibit 7 for images of Human-Computer Interaction (HCI).

**Exhibit 7. Images of Human-Computer Interaction (HCI)**

Source: <https://www.bing.com/images/>



Cirque created on-going strategic alliance with a few entities, including Disney, artists such as Madonna (for whom it helped produced 2012 Super Bowl show, see Exhibit 8), and James Cameron (with whom it collaborated on a 3D movie, see Exhibit 9). Additionally, the company collaborated closely with engineering and art departments in as many as 17 universities where it solicited ideas from students, many of which were eventually incorporated into its shows (Dan 2012).

Equally important to Cirque's was the role of the City of Montreal where the company's head office was located. Montreal was home to the National Theatre School, the O Vertigo dance company, the world-famous Jazz Festival, and vibrant other independent music, arts, and design companies. Additionally, Montreal was recognized as the center of Canada's fashion, visual arts and design. This center of arts, design, fashion, and music had created a basin for creators and "spill-across" effects that were important to Cirque's artistic development.

**Exhibit 8. Images of Madonna 2012 Super Bowl Show**

Source: <https://www.bing.com/images/>

***Creativity through Teamwork and Diversity***

Collaboration was a key to Cirque's culture of creativity. Teams and teamwork were the basin of creative work at Cirque, as entertainment productions were based on collaborative efforts. Artistic show had to be done by teams. According to Ricotta (2013), the greatest competitive advantage that the company had was the diversity of its teams. Tony Ricotta, a "Zarkana" company's manager, reiterated:

*"If everybody is from the same side of the river, you are only going to look at it one way and you can't appeal to everybody if you are only looking at it from a very narrow field of vision. So everything is made up of teams. Whether it's the production team, the operations team, and the artistic team, they all come from all over the place. So there is a varied perspective and that is what gives us a competitive advantage. When we started, it was very French Canadian... Now we have the ability to reach beyond our headquarters and bring in new creators from around the globe and give them an opportunity to create in a way that they never been able to before and do some amazing things."*

Each Cirque performance required a team of people with specialized/complimentary skills who worked together to perform a unique production. According to Ghazzawi et al. (2014: 42):

*“Each production began on a storyboard with narrative development leading to an accrument of design levels not limited to lighting and stage design, gymnastic choreographers, music writers and composers, engineers and set developers, structural erectors, among other design specialists. Once developed operations took on a level of functions including auxiliary services such as catering, communications, medical services, business operations, marketing and human relations.”*

### Exhibit 9. Images of James Cameron, Cirque du Soleil Production

Source: <https://www.bing.com/images/>



For Cirque, Teams were important for the very simple reason that no one person could keep all these talented balls in the air. Additionally, performances, creative shows, and theater productions in most cases required collaborative, team-based work (Ricotta 2013). Exhibit 10 provides images of teamwork during a Cirque production. Each team member had a role of what was expected from her/him to perform. Roles at Cirque had rights and responsibilities attached to them. Team members needed to interact with each other to perform their specific roles. Accordingly, team members acquired roles through role-making and through role-taking. According to Ghazzawi et al. (2014: 41):

*“Given the diversity of merging cultures, communications among recruits and personnel was indeed challenging but certainly not impossible. Add to the mix the complexities of living arrangements and the constant adaptation required on a daily basis, one could easily imagine the critical trust requirements needed when performing highflying stunts promulgated by precarious drops and turns.”*

Cirque performers had high group efficacy; members of the performing team had a shared belief that they were able to achieve their goals and objectives as a group, in other words, “perform well together.” Said efficacy developed over time as group members came to understand each other, how the group functioned, the tasks it needed to accomplish, and the group’s capabilities (George & Jones 2012).

### Exhibit 10. Selected Images of Teamwork Performances at Cirque

Source: <https://www.cirquedusoleil.com/press>



**Title:** Tabloid Junkie from Michael Jackson.  
**Picture credit:** Isaac Brekken/Getty Images.  
**Costume credit:** Zaldy Goco



**Title:** Counselor's Son and Spearmen from ONE KA  
**Picture credit:** Eric Jamison  
**Costume credit:** Marie Chantale Vaillancourt

Ricotta (2013) asserted that “the greatest competitive advantage that the company had was the diversity of its teams.” DeLong and Vijayaraghavan (2002) noted that the artists and performers originated from more than 40 countries and they spoke more than 25 different languages and dialects. Cirque was home to 4,000 employees, 500 of whom were performers who arrived from various destinations and from remote villages in Africa, China, and South America. The practice at Cirque was to allow at least two friends or family members to accompany a performer to help ease the challenges of changes in culture, language, customs, and environment (DeLong & Vijayaraghavan 2002; Ghazzawi et al. 2014).

Additionally, language (reading, speaking, and writing) courses and educational opportunities were provided for both performers and their accompanied family members. Celebrations of

cultural diversity were common at Cirque. Troupe parties were held with ethnic food and special events that reflected the company's diversity. Medical care, transportation assistance, food, social and psychological support, and living facilities were standard benefits for Cirque performers/artists.

### ***Cirque's Four Pillars of Corporate Social Responsibility "CSR"***

Cirque du Soleil established a philanthropic organization to help at-risk youth by discovering them, putting them on stage, and providing them an outlet so that they could be sheltered from life's challenges. Cirque was a company with a cause and Cirque people were "*citizens of the world.*" Cirque identified its four pillars as: "*Talent, Community, Procurement and Partnership, and Environment*" (Cirque du Soleil-d). (See Exhibit 11 for the author's conceptualized illustration of the four pillars.)

#### ***Talent***

For Cirque's "*Talent*" pillar, according to its own definition,

*"Our employees are the undeniable force on which our reputation is built. Their work environment has a great influence on their quality of life, their family life and their health. Hence, we make sure this environment is open, safe, creative and friendly"* (Cirque du Soleil-d).

Cirque emphasized employees' well-being and energy, health and safety, and access to the arts. Additionally, the company was passionate about creation. Cirque supported the local artistic community by purchasing exhibitions and shows tickets for its employees to enable them to discover new ideas. Cirque also organized the "PARADE" program, an annual exhibit to salute its employees' artistic talent. At the "PARADE," employees exhibited their artwork. The event took place at international headquarters and in a gallery in Las Vegas (Cirque du Soleil-d).

#### ***Community***

As for the "Community" pillar, the company communicated the following:

*“We strive to be a good neighbor at our offices and in the cities we visit by building relationships with communities through activities and programs that benefit at-risk youth. This cause is a natural fit for a company founded by street performers. We speak to youth in a language that is built into our DNA: art”* (Cirque du Soleil-e).

The company used art as an intervention tool to help its community. Cirque created two intervention programs for youth: *Cirque du Monde*, a program that promoted circus acts as a mean of intervention with at-risk youth, also known as the social circus; and “*Arts Nomades*,” a program that offered a pedagogical approach based on a partnership in a school setting. “*Arts Nomades*” featured a team of teaching artists working with teachers who wished to use the arts in support of academic concepts. Both programs “*used art to contribute to the personal and social development of the participants by fostering self-esteem, confidence, social skills, citizen development and creativity*” (Cirque du Soleil-e).

Cirque supported various community programs, namely “*Art Collection and Show Heritage*” and “*Montreal: City of Circus Arts*,” among others. The company encouraged its employees to participate in action-based initiatives and supported events that were meaningful to the local community. It supported the annual Run Away with Cirque du Soleil at the Springs Preserve and the 5K Run and 1-Mile Fun Walk where all proceeds supported educational and environmental programs (Cirque du Soleil-e).

### ***Procurement and Partnership***

In 2008, Cirque adopted a responsible procurement policy, with principles for environmental protection and work standards defined by the International Labor Organization. The company used responsible suppliers who shared Cirque’s Corporate Social Responsibility approach (Cirque du Soleil-f). The “*Procurement and Partnership*” Pillar was characterized as follows:

*“Cirque du Soleil has a social responsibility clause in its partnership agreements. This clause covers a set of social responsibility parameters, such as employee relations, responsible procurement, environmental protection and social and cultural action in the community”* (Cirque du Soleil-f).

## **Environment**

In 2006, Cirque adopted an environmental policy based on the following themes: *“water management, greenhouse gas (GHG) management, residential and hazardous waste management, and employee education and awareness building”* (Cirque du Soleil-g). To reduce its GHG emissions, Cirque connected its shows to cities' power grids whenever possible as opposed to using generators. Additionally, the company started using a light-colored canvas for its new Big Top instead of its traditional Big Top; the new canvas reflected the sun's rays, reducing air-conditioning needs (Cirque du Soleil-g).

The company became a member of the urban heating network that linked its international headquarters to the Biomont power plant in the Saint-Michel district of Montreal. The *“urban heating network transformed biogas from the landfill site of the Saint-Michel Environmental Complex into electricity. Controlled combustion of the biogas produces electricity”* (Cirque du Soleil-g). According to Cirque, the residual heat of the process was recovered, supplied the heating systems of its headquarters, and reduced its emissions by more than 1,200 tons a year (Cirque du Soleil-g).

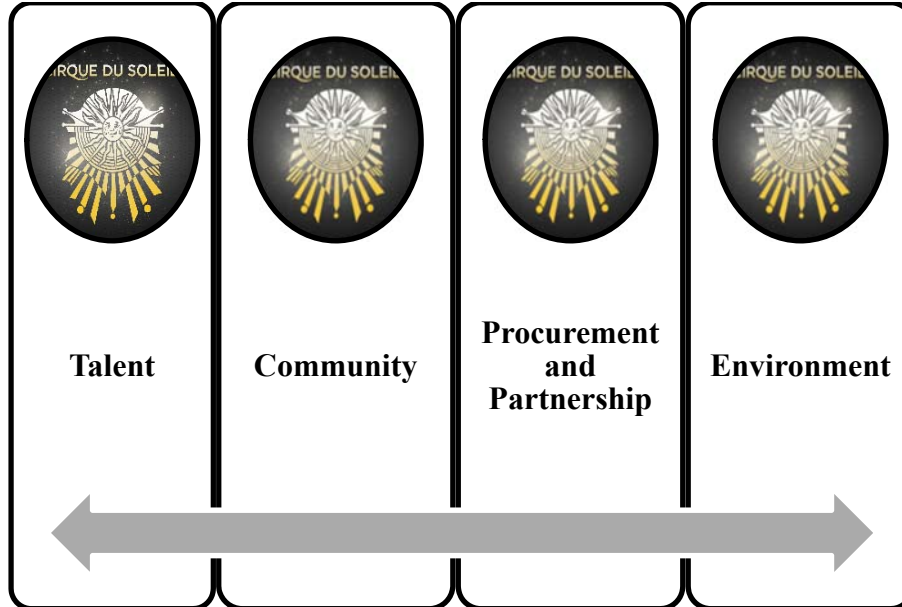
Other initiative including two-sided printing and elimination of disposable cups and dishes, reduction of water consumption, new methods and materials to increase the lifespan of costumes, and active recycling and compost (Cirque du Soleil-g).

Cirque international headquarters was certified “BOMA BEST®” Level 3. Said certification recognized the company’s environmental practices and its healthy workplace. BOMA BEST® covered six aspects: energy, water, waste reduction and sites, effluent emissions, the indoor environment, and the environmental management system (Cirque du Soleil-g).



### Exhibit 11. An Illustration of Cirque's Four Pillars "CSR"

Source: Conceptualized by the case author



### The Future of Culture and Creativity at Cirque

Laliberté's was a "talent harvester" and "cultivator of people" who was committed to developing his artists' and managers' talent while maintaining stewardship of their physical and emotional welfare. His vision for Cirque and its people "will be applied to future productions whereby he pursues and realizes ideals and creativity and hunts for the potential in individuals, while healing the very spirit of live performance" (Ghazzawi et al. 2014: 44).

Despite its historical growth and success, the company had been plagued by a series of failed shows and a decline in its profit. In 2010, Cirque cancelled *Banana Shpeel*'s scheduled run at the Golden Gate Theatre in San Francisco. After its troubled showing in New York City and Toronto, the show was dubbed as "one of the most frustrating failures in Cirque's history" by the *New York Times* (Arcand 2019). Entertainment critic Christopher Hoile wrote in his review of *Banana Shpeel*: "To remain creative, a company needs to experiment; this experiment just

*doesn't work out. It would be better for Cirque du Soleil to withdraw Banana Shpeel than flog it on tour and endanger its reputation"* (in Arcand 2019: Para. 5).

Adding to Cirque's trouble was the need to cancel five shows in 2011-12: Z and Zaya in Asia, *Saltimbanco* on Tour, Viva Elvis in Las Vegas, and Iris in California. Iris, presented at the Dolby Theater in Los Angeles, was put to rest in December 2012 due to a low audience attendance despite its positive critical reception (Baillargeon 2013). See Appendix 1 for Cirque shows. In 2012, the company announced a wave of layoffs at Montreal headquarters, including 30 head office positions (Baillargeon 2013). President Daniel Lamarre argued that said changes were necessary *"to support the sustainability"* of the company. To Lamarre, *"the situation did not seem catastrophic ... however, that after a decade of tremendous growth, global economic conditions were forcing a review of the business model"* (Baillargeon 2013, para. 6). According to Cousineau (2014):

*"Laliberté discreetly reclaimed half of the 20-per-cent stake in the Cirque du Soleil he had sold to Dubai investors in 2008 after the financial crisis in Dubai crushed their global real estate investments and turned this much publicized Cirque global expansion/partnership into a mirage. The failed expansion contributed to the Cirque's financial difficulties, which resulted in 400 layoffs in January, 2013. The financial difficulties were also felt in Las Vegas, where hotel groups gave into discounting, forcing their circus partner to follow suit, Mr. Laliberté said. The Cirque generates close to half of its \$850-million in annual revenue from its eight Vegas shows. The rising Canadian dollar, which swelled production costs, also hit the bottom line, shaving off at least \$50-million in profits per year."*

As ninety percent of Cirque du Soleil was acquired in 2015, some were questioning whether a traditional culture that valued social norms and stability would not work well with process-oriented and bottom-line requirements of the new owners. Accordingly, Daniel Lammare and Guy Laliberté were re-visiting the challenges that faced an organization during its growth cycle where Cirque culture needed to adapt to environmental changes. Cirque executives knew that the acquisition played a significant role in the survival and revitalization of the company. They for sure knew that the acquiring partners' expectations were to put in place organizational processes that would yield a reasonable return on their invested capital, gains in market share, and retention of key employees.

According to Leslie and Rantisi (2019: 264),

*“The intimate connections between performers and the audience that has also led to innovation have also been disrupted with the shift from big tops to arenas. The show creation process has become increasingly linear in a geographic and organizational sense, as aspects of creation are more tightly controlled...A standardization of work and rationalization of labor - as well as an increasingly closed script and regulated space-have created conditions whereby a growing number of young performers seek out employment at smaller, more innovative troupes... .”*

In moving forward, the big question before Cirque leadership was, how could Cirque proactively respond to the changes in its internal environment while maintaining its high creative standards, expand its appeal to a larger audience, meet its new partners' expectations, and remain loyal to its original values?



**Issam A. Ghazzawi**

is Professor of Management and the Sam Walton Fellow at the University of La Verne. Professor Ghazzawi offers courses in organizational design, organizational theory, organizational behavior, and management. He received his Ph.D. from the University of Pittsburgh; his Master in Labor and Human Resources (M.L.H.R.) from The Ohio State University; and his Master in Business Administration (MBA) from Sul Ross State University. He is a past president of the Western Casewriters Association.



## Appendix A Cirque du Soleil Shows

*Source: Wikipedia*

Venue	Premiere	Touring Vs. Resident	Style/Format	Status
Alegria	April 21, 1994	Touring show	* Grand Chapiteau (1994-1999, 2001-2009). Arena (2009-2013)	Retired
Alegría: In a New Light	April 18, 2019	Touring show	Grand Chapiteau	Active
Amaluna	April 19, 2012	Touring show	Grand Chapiteau	Active
Axel	April 4, 2019	Touring show	Arena	Active
Banana Shpeel	November 19, 2009	Touring show	Theatre	Retired
Bazaar	November 14, 2018	Touring show	Grand Chapiteau	Active
Corteo	April 21, 2005	Touring show	Grand Chapiteau Arena (since 2018)	Active
Criss Angel Believe	September 26, 2008	Luxor, Las Vegas	Resident (2008 — 2016)	Retired
Crystal	October 5, 2017	Touring show	Arena (since 2017)	Active
Delirium	January 26, 2006	Touring show	Arena (2006 — 2008)	Retired
Dralion	April 22, 1999	Touring show	Grand Chapiteau (1999- 2010) Arena (2010-2015)	Retired
Iris	September 25, 2011	Dolby Theatre, Los Angeles	Resident (2011- 2013)	Retired
Joyà	November 8, 2014	Riviera Maya, Mexico	Resident (since 2014)	Active
Kà	November 26, 2004	MGM Grand, Las Vegas	Resident (since 2004)	Active
Koozâ	April 19, 2007	Touring show	Grand Chapiteau (since 2007)	Active
Kurios: Cabinet of Curiosities	April 24, 2014	Touring show	Grand Chapiteau (since 2014)	Active
La Nouba	December 23, 1998	Disney Springs, Lake Buena Vista, Florida	Resident (1998 - 2017)	Retired
Luzia	April 21, 2016	Touring show	Grand Chapiteau	Active
Messi 10	October 10, 2019	Touring show	Arena (since 2019)	Active
Michael Jackson: One	May 23, 2013	Mandalay Bay Resort and Casino, Las Vegas	Resident (since 2013)	Active
Michael Jackson: The Immortal World Tour	October 2, 2011	Touring show	Arena (2011-2014)	Retired
Mystère	December 25, 1993	Treasure Island, Las Vegas	Resident (since 1993)	Active
Nouvelle Expérience	May 8, 1990	Touring show	Grand Chapiteau (1990-1993)	Retired

**Appendix A, cont.**  
**Cirque du Soleil Shows**

O	October 15, 1998	Bellagio, Las Vegas	Resident (since 1998)	Active
Ovo	April 23, 2009	Touring show	Grand Chapiteau (2009-2015) Arena (since 2016)	Active
Paramour	April 16, 2016	Hamburg, Germany	Theatre (2016- 2017, 2019 - present)	Active
Quidam	April 23, 1996	Touring show	Grand Chapiteau (1996-2010, 2015) Arena (2009, 2010 – 2016)	Retired
R.U.N	October 24, 2019	Luxor, Las Vegas	Resident	Active
Saltimbanco	April 23, 1992	Touring show	Grand Chapiteau (1992 – 2006) Arena (2007- 2012)	Retired
Séptimo Día - No Descansaré	March 9, 2017	Touring show	Arena (2017-2018)	Retired
The Beatles Love	June 2, 2006	The Mirage, Las Vegas	Resident (since 2006)	Active
Toruk - The First Flight	November 12, 2015	Touring show	Arena (2015-2019)	Retired
Totem	April 22, 2010	Touring show	Grand Chapiteau (since 2010) Arena (2017)	Active
'Twas The Night Before...	November 29, 2019	The Chicago Theatre, Chicago (soft launch) and Madison Square Garden, New York City	Seasonal Theatre	Coming Soon
Varekai	April 24, 2002	Touring show	Grand Chapiteau (2002 – 2013, 2017) Arena (2013 – 2017)	Retired
Viva Elvis	December 16, 2009	Aria Resort and Casino, Las Vegas	Resident (2009 – 2012)	Retired
Volta	April 20, 2017	Touring show	Grand Chapiteau (since 2017)	Active
Wintuk	November 1, 2007	Madison Square Garden, New York City	Seasonal Resident (2007 – 2011)	Retired
X (The Land of Fantasy)	August 10, 2019	Hangzhou, China	Resident (since 2019)	Active
Zaia	July 26, 2008	The Venetian Macao, Cotai Strip, Macao	Resident (2008 – 2012)	Retired
Zarkana	June 29, 2011	Aria Resort and Casino, Las Vegas	Arena (2011 – 2012) Resident (2012 – 2016)	Retired
Zed	August 15, 2008	Tokyo Disney Resort, Tokyo, Japan	Resident (2008 – 2011)	Retired
Zumanity	July 31, 2003	New York-New York, Las Vegas	Resident (since 2003)	Active

\* A “Grand Chapiteau” is literally a **mobile village**. It houses the venue as well as a kitchen, school, rehearsal space and items needed for the cast and crew.

## Appendix B

### Cirque du Soleil Important Timeline

Source: <https://www.cirquedusoleil.com/press/kits/corporate/about-cirque>

#### 1984

Cirque du Soleil is born with the assistance of the Quebec government, as part of the celebrations surrounding the 450th anniversary of Jacques Cartier's arrival in Canada. The first production, *Le Grand Tour* debuts in the small Quebec town of Gaspé, and is then performed in 10 other cities throughout the province. The first blue-and-yellow big top seats 800.

#### 1985

After performing in Montreal, Sherbrooke and Quebec City, with *Le Grand Tour*, Cirque du Soleil leaves its home province for the first time to take its show to neighboring Ontario. It performs in Ottawa, Toronto and Niagara Falls and the show is simply named Cirque du Soleil.

#### 1986

Cirque du Soleil takes *La Magie Continue* across Canada, including Vancouver, where it puts on several performances at the Children's Festival and Expo 86 and in seven other Canadian cities. The big top now has room for 1,500 spectators.

#### 1987

Having triumphed in five cities in Quebec, *We Reinvent the Circus* is performed at the Los Angeles Art Festival and then moves on to San Diego and Santa Monica. Exhilarated by the Californian public's response, Cirque du Soleil is an overnight success. The participation of Cirque du Soleil at the L.A. Art Festival is not only an important milestone in its history but also its first visit to its American neighbors.

#### 1988

*We Reinvent the Circus* continues its North American tour, after a brief appearance at the Calgary Winter Olympics. Wherever it goes, the result is the same: the performances sell out, and the critics rave.

#### 1990

Montreal is the setting for the world premiere of a brand-new production, *Nouvelle Expérience*, in a new, 2,500-seat big top. With this new production, Cirque du Soleil shatters all previous records for ticket sales. Meanwhile, Cirque makes its first foray into Europe, staging *We Reinvent the Circus* in London and Paris.

#### 1992

*Fascination*, a collage of the best acts from past shows, enables Cirque to make a name for itself in Japan. The show opens in Tokyo and then moves on to seven other cities. Meanwhile, in Europe, Cirque du Soleil joins forces with Switzerland's Circus Knie and stages a show in over 60 towns throughout the country. In North America, 1992 sees Cirque du Soleil make its Las Vegas debut when *Nouvelle Expérience* kicks off a year-long engagement under a big top at the Mirage Hotel. *Cirque du Soleil* *adad*: a monument to its repertoire of shows, *Saltimbanco*. Premiering in Montreal, this latest production begins a lengthy tour of North America.

#### 1993

Following the successful Las Vegas run of *Nouvelle Expérience*, Cirque du Soleil moves into a theatre built to its specifications at the new Treasure Island Hotel. A 10-year contract is signed with Mirage Resorts to stage *Mystère*, a gigantic production befitting this show business capital.

#### 1994

Cirque du Soleil celebrates its 10th anniversary with another production, *Alegria*. True to tradition, the world premiere is held in Montreal. *Saltimbanco* embarks on a six-month run in Tokyo that attracts a great deal of attention.

#### 1995

Cirque du Soleil responds to a request from the Canadian government and creates a show for the heads of state gathered at the G7 Summit in Halifax, Nova Scotia. Also in 1995, *Saltimbanco* sets out to open officially the European market. Cirque's spectacular white big top with seating for 2,500 spectators makes its first stop in Amsterdam, followed by Munich, Berlin, Düsseldorf, and Vienna.

#### 1996

In April, Cirque launches *Quidam* in Montreal. After finishing its hometown run, *Quidam* heads off on a North American tour. Meanwhile, *Alegria* sets out to tour Japan for a few months.

**Appendix B, cont.**  
**Cirque du Soleil Important Timeline**

**1997**

In Montreal, the inauguration of the brand new International Headquarters is held; the Studio is now where all of Cirque's shows will be created and produced.

**1998**

In October, the second resident show for Cirque du Soleil, "O", takes to the stage of a new theatre at the Bellagio in Las Vegas. This production is Cirque's first aquatic show and an important milestone in the company history. With this show, Cirque is now known internationally. In December of the same year, Cirque inaugurates yet another permanent show, La Nouba, at the Walt Disney World Resort near Orlando, Florida.

**1999**

A brand-new Cirque du Soleil production, Dralion, launches its North American tour in Montreal. With Saltimbanco, Cirque sets up shop in Asia and the Pacific.

**2000**

Movie fans come out in droves to see Cirque du Soleil on the IMAX screen for the first time ever, as its large-format film production Journey of Man (Passages in French), distributed by Sony Pictures Classics, premieres worldwide.

**2001**

Cirque du Soleil keeps on growing with the inauguration of a 15, 000-square-metre addition (Les Ateliers) to its International Headquarters in Montreal.

**2002**

In April, a fifth touring show is added to the seven Cirque du Soleil shows already performing simultaneously in 2002. Varekai premieres in Montreal, and from there begins a tour of North America. Cirque du Soleil made its first stop in Mexico this year with Alegriá. Cirque's Multimedia Division, called Cirque du Soleil Images at the time, produces its first television series, Cirque du Soleil Fire Within, for the Canadian and American television market.

**2003**

The newest addition to the Cirque family, Zumanity is born in August. It is an adults-only resident show at the New York-New York Hotel & Casino in Las Vegas. The filming of a new television series—the first to be produced entirely by Cirque du Soleil Images—is wrapped up in the late summer. This unique family TV series brings together acrobatic acts within a dramatic comedy framework. The series is aimed at international television markets, including Canada and the United States.

**2004**

Cirque du Soleil celebrates its 20th anniversary in 2004. A number of events mark the occasion: among other things, a book is launched, entitled 20 Years under the Sun, which recounts the unusual history of Cirque du Soleil step by step, and Cirque sets the first Guinness World Record for the largest number of stilt-walkers (544) at the same time and place. Cirque du Soleil launches a new resident show, KÀ, in the fall at the MGM Grand in Las Vegas.

**2005**

The year 2005 is marked by the Montreal launch and world premiere of Corteo, Cirque's latest touring show. In July, Montreal hosts the XI FINA World Aquatic Championships, for which Cirque du Soleil creates the opening ceremony show.

**2006**

Cirque du Soleil first-ever musical show in arena, DELIRIUM, premiered in Montreal in January and has begun its U.S. tour. Cirque du Soleil is also preparing a fifth permanent show in Las Vegas: The Beatles LOVE, which celebrates the musical legacy of the Beatles and premieres in June at The Mirage. After touring in North America, Europe, Asia and Australia, Cirque du Soleil has set out to make a name for itself in South America by presenting its show Saltimbanco in Chile, Argentina and Brazil in 2006. Cirque du Soleil entered into an exclusive agreement with CKX Inc.



## Appendix B, cont.

### Cirque du Soleil Important Timeline

#### 2007

KOOZA, a new touring show, is launched in Montreal in April 2007. In February, Cirque du Soleil puts on a pre-game show performance for Super Bowl XLI in Miami. In November, Cirque presents Wintuk, a show designed exclusively for the WaMu Theater at Madison Square Garden in New York. Starting in 2007, this seasonal show has been performed for 10 weeks for four years. Cirque du Soleil has also launched a fiction/non-fiction book entitled *The Spark*, which invites readers to discover the power of creativity and imagination and apply it in their own lives. Written by John Bacon and based on an original idea by Lyn Heward, the book is distributed in several countries. After having toured for 14 years and being performed before more than 9.5 million spectators, *Saltimbanco* is reborn in July as it takes off on an arena tour of more than 40 cities in Canada and the U.S.

#### 2008

This was an historical year for Cirque du Soleil as the company launched three new permanent shows that year: ZAIA at The Venetian Hotel in Macau (China), ZED at the Tokyo Disney Resort in Tokyo (Japan) and *CRISS ANGEL Believe* at The Luxor Hotel in Las Vegas (United States). Cirque du Soleil also created a show-event presented at Colisée Pepsi in Quebec City in the scope of the 400th anniversary of the city. Istithmar World, the investment arm of Dubai World, and Nakheel have together acquired a 20 per cent stake in Cirque du Soleil.

#### 2009

Cirque du Soleil celebrates its 25th anniversary and launches the 25th production of its history. This new creation, *OVO* premieres in Montreal in April. The publication of a book on Cirque costumes and the launch of a double CD containing a music compilation, are among the commemorative activities of this anniversary. In September 2009, Guy Laliberté became the first Canadian private space explorer. His mission was dedicated to raising awareness on water issues facing humankind on planet earth. Under the theme *Moving Stars and Earth for Water*, this first Poetic Social Mission in space aimed at touching people through an artistic approach: a special 120-minute webcast program featuring various artistic performances unfolding in 14 cities on five continents, including the International Space Station.

#### 2010

Cirque du Soleil launches three new productions in 2010. *Viva ELVIS*, Cirque's seventh show in Las Vegas begins in February at ARIA Resort & Casino. *Banana Shpeel* is presented from November 2009 to June 27, 2010 in Chicago and New York. In April, *TOTEM*, first show designed to adapt to various performance spaces such as Big Top and arenas, celebrates its world premiere in Montreal. Cirque du Soleil, James Cameron (*Titanic*, *AVATAR*), and Andrew Adamson (*Shrek*, *Chronicles of Narnia*), joined their creative forces to develop and produce immersive theatrical 3D projects. In November, Cirque du Soleil's founder, Guy Laliberté gets a star on the Hollywood Walk of Fame.

#### 2011

Cirque du Soleil will launch three new shows: *Zarkana*, written and directed by acclaimed film and theatre director François Girard will begin at the legendary Radio City Music Hall in New York City on June 9. Written and directed by director-choreographer Philippe Decouflé, *IRIS* created exclusively for the Dolby Theatre at the Hollywood & Highland Center will begin on July 21. The show *Michael Jackson THE IMMORTAL World Tour™* written and directed by Jamie King will begin in Montreal on October 2nd.

#### 2012

Cirque du Soleil launched a new touring show in Montreal called *Amaluna*. The company has developed a new creative and production service dedicated to businesses and artists wanting to call on Cirque du Soleil's creative know-how for their projects. Within that context, Cirque du Soleil collaborated with pop star Madonna providing artistic direction services for her performance at the Super Bowl XLVI halftime show. In December, Cirque du Soleil and Bell Media created a new joint venture to develop media content for television, film, digital, and gaming platforms. Cirque du Soleil Media's mandate is to develop original entertainment projects, leveraging Cirque du Soleil's creative inventiveness and resources, consumer insight, and infrastructure, with Bell Media's production experience, media platforms, and diverse distribution capabilities.

## Appendix B, cont.

### Cirque du Soleil Important Timeline

#### 2013

Cirque du Soleil launched a new resident production inspired by pop icon Michael Jackson, *Michael Jackson ONE*, at the Mandalay Bay Hotel in Las Vegas. *Michael Jackson THE IMMORTAL* show ranked among the 10 more lucrative tours of rock history, a first for a Canadian artist.

#### 2014

Cirque du Soleil celebrates its 30th anniversary and launched a new touring show in April in Montreal, *Kurios – Cabinet de curiosités*. In November, Cirque opened a new resident show in Riviera Maya (Mexico), *JOYÀ*, in a custom-designed theatre. In December, as part of its 30th anniversary, and for the first time in its history, Cirque du Soleil presents a unique, exclusive music event in Montreal celebrating 30 years of music.

In the context of an on-going strategy of diversifying its content and live-entertainment activities worldwide, Cirque du Soleil has created some 10 subsidiaries among which: 45 DEGREES, Cirque du Soleil Hospitality, Cirque du Soleil Theatrical, 4U2C, Cirque du Soleil Média and Outbox.

#### 2015

Cirque du Soleil announced an agreement under which TPG, a global private investment firm, was to acquire a majority stake in Cirque du Soleil to fuel growth and take Cirque's iconic blue and yellow big top to exciting new markets.

On December 21, Cirque du Soleil launched *TORUK – The First Flight*, an arena-touring show inspired by the world of James Cameron's history-making motion picture *AVATAR*.

#### 2016

Two new productions launched in April: *LUZIA*, a touring show under the big top inspired by the rich Mexican culture launched in Montreal, and *PARAMOUR*, a production created specifically for Broadway presented at the Lyric Theatre in New York.

#### 2017

In March, a new arena show will begin a South American tour. This show called *Sep7imo Dia* is inspired by the music of a popular band from Argentina, Soda Stereo. The most recent touring show *VOLTA*, inspired by action sports, will lift its marquee at the Old Port of Montreal in April.

The international success story known as Cirque du Soleil is, above all, the story of a remarkable bond between performers and spectators the world over. For at the end of the day, it is the spectators who spark the creative passions of Cirque du Soleil.

## References

- Arcand, O.S. (May 9, 2019). "Cirque Gives Banana Shpeel the Hook." The article was originally published on October 7, 2010 and updated on May 9, 2019. Retrieved on November 8, 2019 from: <https://www.theglobeandmail.com/arts/theatre-and-performance/nestruck-on-theatre/cirque-gives-banana-shpeel-the-hook/article1370055/>
- Baillargeon, S. (January 15, 2013). "Compressions au Cirque du Soleil: Au moins 400 employés seraient touchés." Retrieved November 19, 2019 from: <https://www.translatetheweb.com/?from=&to=en&ref=SERP&dl=en&rr=UC&a=https%3a%2f%2fwww.ledevoir.com%2fculture%2f368378%2fcompressions-au-cirque-du-soleil-au-moins-400-employes-seraient-touchees>
- Bass, M. (2013). "Guy Laliberté Success Story – from Homeless Street Performer to Multi-billionaire Owner of Cirque du Soleil." Retrieved on November 27, 2019 from: <http://successgroove.com/success-stories/guy-laliberte-success-story-from-homeless-street-performer-to-multi-billionaire-owner-of-cirque-du-soleil.html>
- Berry, L. L., Shankar, V., Parish, J. T. Cadwallader, S., & Dotzel, T. (2006). "Creating new markets through service innovation," *Sloan Management Review*, 47(2), 56-62.
- Bjørn, A., Coenen, L. and Vang, J. (2005). *Face-to-Face, Buzz and Knowledge Bases: Socio-spatial implications for learning and innovation policy*. Circle Lund University. Paper no. 2005/14. Copenhagen, Denmark: CIRCLE and Copenhagen Institute of Technology, Aalborg University.
- Browse Biography.Com (2011). "Guy Laliberté Biography." Retrieved on November 27, 2019 from: [http://www.browsebiography.com/bio-guy\\_laliberte.html](http://www.browsebiography.com/bio-guy_laliberte.html)
- BussinessDataCodes.com (n.d.). *NAICS 7111 Performing Arts Companies*. Retrieved on November 6, 2019 from: <https://businessdatacodes.com/naics/code-7111-performing-arts-companies>
- CBC.CA (2015). "Cirque du Soleil sale to American, Chinese private equity firms gets approval." Retrieved on October 23, 2019 from: <https://www.cbc.ca/news/canada/montreal/cirque-du-soleil-sale-to-american-chinese-private-equity-firms-gets-approval-1.3134174>
- Cirque du Soleil-a (n.d.). About Cirque. Retrieved on October 23, 2019 from: <https://www.cirquedusoleil.com/press/kits/corporate/about-cirque>
- Cirque du Soleil-b (n.d.). Cirque du Soleil Shows. Retrieved on October 23, 2019 from: <https://www.cirquedusoleil.com/shows>
- Cirque du Soleil-c (n.d.). About Cirque du Soleil. Retrieved on October 23, 2019 from: <http://www.cirquedusoleil.com/en/about/intro/intro.asp>
- Cirque du Soleil-d (n.d.). Talent. Retrieved on November 20, 2019 from: <https://www.cirquedusoleil.com/citizenship/talent>
- Cirque du Soleil-e (n.d.). Community. Retrieved on November 20 from: <https://www.cirquedusoleil.com/citizenship/community>
- Cirque du Soleil-f (n.d.). Procurement and Partnership. Retrieved on November 20, 2019 from: <https://www.cirquedusoleil.com/citizenship/procurementpartnerships>

- Cirque du Soleil-g (n.d.). Environment. Retrieved on November 20, 2019 from: <https://www.cirquedusoleil.com/citizenship/environment>
- Cousineau, S. (2014). "Guy Laliberté on a mission to rejuvenate his Cirque du Soleil." *The Globe and Mail*. Retrieved on November 22, 2019 from: <https://www.theglobeandmail.com/report-on-business/guy-laliberte-on-a-mission-to-rejuvenate-his-cirque-du-soleil/article18502374/>
- D&B Hoovers (n.d.). *Live Nation Entertainment, Inc. Company Summary*. Retrieved on November 6, 2019 from: [https://app.avenion.com/company/ec3be0d1-79db-3e89-aa7f-5affa2bf3dc4#report/company\\_summary](https://app.avenion.com/company/ec3be0d1-79db-3e89-aa7f-5affa2bf3dc4#report/company_summary)
- Dan, A. (2012). "The Secret That Inspires Cirque du Soleil's Culture of Innovation: Creative Friction." Retrieved on October 24, 2019 from: <https://www.forbes.com/sites/avidan/2012/05/29/the-secret-that-inspires-cirque-du-soleils-culture-of-innovation-creative-friction/#78d51ed945f9>
- DeLong, T. J., & Vijayaraghavan, V. (rev. 2002, October 18). Cirque du Soleil. *HBS Premier Case Collection (Harvard Business Publishing)*, 403006-PDF-ENG.
- Denton, H. (1988, Sep 04). "Cirque du Soleil." *The Washington Post* (Pre-1997 Fulltext) Retrieved on November 1, 2019 from: <http://0-search.proquest.com.leopac.ulv.edu/docview/307069811?accountid=25355>
- Fuchs, G. and Shapira, P., eds. (2005). *Rethinking Regional Innovation and Change: Path Dependency or Regional Breakthrough?* Dordrecht: Kluwer, pp. 63-84.
- George, J.M. and Jones, G.R. (2012). *Understanding and Managing Organizational Behavior, Sixth Edition*. Upper Saddle River, NJ: Prentice Hall.
- Ghazzawi, I. Martinelli-Lee, T. & Palladini, M. (2014). "Cirque du Soleil: An innovative culture of entertainment," *Journal of the International Academy for Case Studies* 20(5):23-46.
- Gittleson, K. (2013). "How Cirque du Soleil became a billion dollar business." Retrieved on October 23, 2019 from: <https://www.bbc.com/news/business-25311503>
- Haves, S. (July, 4, 2013). Master Teacher and Artistic Cirque du Soleil consultant and contractor. An interview: Santa Monica, CA
- Heward, L. & Bacon, J. (2006). *The Spark: Igniting the creative fire that lives within us all*. Canada: Doubleday Canada, a division of Random House of Canada Limited.
- Heward, L. & Bacon, J. (n.d.). *The Spark: Igniting the creative fire that lives within us all*. Goodreads. Retrieved on November 12, 2019 from: [https://www.goodreads.com/book/show/3470.Cirque\\_Du\\_Soleil](https://www.goodreads.com/book/show/3470.Cirque_Du_Soleil)
- Hoovers.com (August 29, 2019-a). *Feld Entertainment. Company Overview*. Retrieved on November 5, 2019 from: Hoovers.com.
- Hoovers.com (October 1, 2019-c). *Cirque du Soleil. Competitors*. Retrieved on November 5, 2019 from: Hoovers.com.
- Hoovers.com (October 1, 2019-b). *Live Nation Entertainment. Company Overview*. Retrieved on November 5, 2019 from: Hoovers.com.

- Hoovers.com (n.d.). *Performing Arts Companies Industry: Insights from D&B Hoovers*. Retrieved on November 6, 2019 from: <http://www.hoovers.com/industry-facts.performing-arts-companies.1945.html>
- Leslie, D. & Rantisi, N.M. (2011). "Creativity and the Place in the Evolution of a Cultural Industry: The Case of Cirque du Soleil," *Urban Studies*, 48(9), 1771–1787.
- Mclean, J. (2019). Visiting the beautiful Charlevoix region of Quebec. Retrieved November 5, 2019 from: <https://www.tripsavvy.com/charlevoix-quebec-guide-1482016>
- McGuire, S. (2003). *Entrepreneurial Organizational Culture: Construct definition and instrument development and validation* (Doctoral dissertation, George Washington University).
- Newswire Today (2018). "Cirque du Soleil Explores Augmented Reality, Powered by SAP Innovation Center Network". Retrieved on October 24, 2019 from: <https://www.newswiretoday.com/news/168803/Cirque-du-Soleil-Explores-Augmented-Reality-Powered-by-SAP-Innovation-Center-Network/>
- Palmeri, C. (2015). "Moody's reveals details of \$1.5 billion Cirque du Soleil deal." Retrieved on November 25, 2019 from: <https://www.bloomberg.com/news/articles/2015-06-10/moody-s-reveals-details-of-1-5-billion-cirque-du-soleil-deal>
- Pearson, L. (2019). "Art Business: Key Trends & Latest Statistics." Retrieved on November 6, 2019 from: <https://www.reportlinker.com/ci02217/Performing-Art.html>
- Ricotta, T. (2013). Cirque du Soleil, Company Manager: Zarkana. Interview on May 30, 2013
- Vault.com (n.d.). *Performing Arts: Industry Outlook*. Retrieved on November 6, 2019 from: <https://www.vault.com/industries-professions/industries/performing-arts/industry-outlook>
- Yelp.com (n.d.). Cirque Du Soleil's Saltimbanco. Retrieved on November 13, 2019 from: <https://www.yelp.com/events/cedar-park-cirque-du-soleils-saltimbanco>
- Zarov, S. (2014). "Guy Laliberté." *The Canadian Encyclopedia*. Retrieved on November 5, 2019 from: <https://www.thecanadianencyclopedia.ca/en/article/guy-laliberte>



***Journal of Case Research and Inquiry***

Peer-Reviewed Cases, Notes and Articles

A publication of the Western Casewriters Association

Vol. 5  
December 2019

ISSN 2377-7389