

The Business Ethics Center of Jerusalem

ONLINE HI-TECH MAGAZINE: After the NASDAQ Crash

Introduction

The bursting of the NASDAQ bubble is already old news. Everyday the newspapers are full of horror stories: Company X's stock price falls by 70%, Company Y resizes and lays off half of their workforce.

When times are this tough, is it possible for a manager to still act morally? When you know that the survival of your company requires cutting your workforce, what do you do?

In an earlier edition, we focused on the ethical dilemmas caused by the shortage of qualified workers in the Hi-Tech industry. At that time, companies could not hire enough employees to keep up with business. Now seven months later, the reverse problem exists. Companies have too many employees and not enough business. What is a company's ethical responsibility to its employees when it must cut costs? When it must resize, what is a company's moral responsibility to the workers it has fired? What is its responsibility to those that remain?

Important Facts

Across the world, the Internet economy is singing the blues. With the bursting of the NASDAQ bubble, and the recognition that many of the Hi-Tech companies would never make a profit, financial support has dried up. Whereas a year ago venture capitalists were throwing money at anyone with a dot com on their business plan, Internet companies now find little money to support their plans.

When trying to stay afloat, one of the main ways to save money is by downsizing employees. In the last quarter of 2000, **42,000 workers were laid off in Israel**, reports the Ministry of Labor and Social Welfare. This reflects a worldwide downturn. A recent study by the Information Technology Association of America said that **demand for Information Technology workers is down 44% in the U.S.**, with 425,000 less job openings than in the previous year.

Several well-known companies in Israel have recently had to lay off some of their employees or even close down completely. When the layoffs first began several months ago, few companies were firing employees, and those employees that were fired were rehired by other companies quickly. Now that many companies are in dire financial straits and there are few job openings, the number of unemployed is high. A recent report issued by Business Data Israel said that 20% of Israeli firms established in the last five years are at "high risk" of being unable to fulfill their financial commitments, which may mean that more downsizings are on the way.

Jacob Richman is a computer programmer who runs the *Computer Jobs in Israel* email list and website, which advertises job openings in Israel on a weekly basis. He says that

he has seen a large jump in subscribers in the recent months to his email list. "I can often see what's coming before the newspapers hear about it. People will suddenly start subscribing from a certain company, so I can tell that people in the company are afraid for their jobs." Richman said that there has also been a large drop in job openings on his list and in the press. "If you look in the newspaper today, there are few job ads. The only ads you see are for job training, or from agencies."

Resizing is now an international problem. In the U.S., the first companies to be hit were the prototypical Hi-Tech companies, those known for having inexperienced managers and poor business plans. However because of a global downturn in advertising revenue, many companies, including established companies such as Yahoo, The New York Times, and The Wall Street Journal, have had to fire some employees. The Internet downturn has also caused a drop in demand for hardware, which has forced many companies to let employees go, including Cisco, Motorola and Intel.

A View From the Trenches

A company's reasons for deciding to resize are complicated. Whatever the impetus, the moral character of the management shines through in the way they lay off employees. It should come as no surprise that companies that do a sloppy job in firing employees also did a poor job in managing them. While being fired is always traumatic, companies can cause extra pain to employees by bumbling their way through the process.

Employees swap horror stories about how they were fired by former companies like war veterans swap stories of the battles they fought in. A common story in Israel is of employees showing up for work on Sunday morning (the first day of the workweek in Israel) to find the doors locked. Employees sometimes hear about downsizings via email or through gossip. In one extreme case in the U.S., a woman was hired by an Internet company, and immediately fired, even before she began her job! (She sued in court, and won the case.)

The most common horror story is that companies don't pay the last month's salary of employees who will be fired, says Jonathan Gad, CEO of Selis Networks. His company creates business service monitoring and management solutions, and has hired several employees who were recently fired by other companies. "We recently hired an HR person who hadn't been paid by her previous employer for 3 months! When I asked her why she stayed with the company, she said that she kept expecting the company to pull through and pay her salary." This woman had such a belief in her company and faith in its management that she kept working even when it seemed increasingly likely that she would not be paid.

Gad attributes the poorly managed downsizings in many companies to management's not having predicted that they would run out of money. "I doubt that most of the horror stories are intentional. What has happened in the market has been the withdrawal of commitments by financial houses at the last minute. Companies need cash ASAP and have a commitment which they rely on. At the last minute, a deal takes longer than expected, the Venture Capitalist intentionally drags its feet to get better terms from the company, or the VC gets cold feet, and so the company is left unable to pay employees."

Richman concurs with this idea. "Companies don't want to treat workers like this. Most of the time they don't have a choice. If suddenly the bank or investor doesn't want to

give money, or a deal goes sour, there's nothing they can do. Some companies if they see the writing on wall will try to help workers if they can."

Another reason that companies failed to expect the financial difficulties they would face is due to the young age of many Hi-Tech companies' managers. "Most of the young peoples' experience was in a boom period, and they can't understand that VC money can dry up," says Gad. "A few months ago there was the feeling that it could never happen. Not having professionally lived through a down period means that they don't have the experience to make these tough decisions." Young managers who did not expect a downturn were unable to plan for it, and when it occurred, were often ignorant of their moral and legal obligations to their workers.

Ethical Issues

Many of the horror stories could have been avoided had the companies thought first about the impact of their actions. Before deciding how to cut costs to deal with financial difficulties, companies should think about their values, and act based on them.

The underlying principle that management must remember is that their employees are people too. Employees are not disposable goods that can be discarded by the wayside at the first sign of trouble. Workers are people with families to feed and bills to pay. Management's decision therefore affects many more people than simply the number on the payroll. Before making a decision to downsize, managers should ask themselves, "how would I want to be treated if I was in their shoes?"

Where possible, companies should do as much as possible to avoid downsizing large numbers of people. But when this is unavoidable, they should try to soften the blow as much as possible. "If you made the decision to fire employees, and it's the right decision, it should be done in a way that is consistent with the company's values," says Frank Navran, former management consultant and director of the Ethics Resource Center. "Make sure you deal with the humanity of it as well as the financial aspects. Remember that you are disrupting someone's life, that you're doing something you don't want to do." When companies are forced to downsize because of economic considerations, it is crucial to keep in mind the human impact.

Ethical Solutions

Companies should avoid massive resizings as much as is reasonably possible given the long-term goals of the organization. "Companies need to be creative in finding ways to save money without firing workers," says Navran. "Why not do a ten percent salary deferral? Give ten percent of the pay in stock options until good financial times return."

In the wave of downsizing announcements, some companies are managing to stay above water and keep their morals intact with creative solutions to the financial problems. For example, Sun Microsystems announced recently that they will shut down for a week in July as a cost-saving measure. All employees will be asked to take vacations or go on unpaid leave.

Agilent Technologies is another company which is trying alternative techniques in order to avoid firing employees. The test and measurement equipment manufacturer recently said that due to a slowdown in customer demand, it would temporarily cut the salaries

of all employees (including top executives) by 10 percent. The company, which was spun off from Hewlett Packard in 1999, said that their move to avoid layoffs is a trademark of the "HP Way" which stresses respect for the individual. "We really value our workforce," said Agilent spokeswoman Michele Drake. "We want our key people to be there when there is an upturn." (SiliconValley.com April 5, 2001)

If companies have no choice but to downsize, they should do so in ways which respect the dignity of their employees. One prime example is Cisco Israel. The company announced recently that it would be cutting 100 workers in its research and development center in Israel. "We have given the employees that were let go the most generous package in Israeli hi-tech history," marketing communications manager Dolly Shtreib said. "Cisco Israel has given each employee an average severance payment equal to his or her salary for half a year, plus 12 months' extended vesting in stock options." Cisco also hired an outplacement firm to help the former employees find new jobs. (Jerusalem Post, April 25, 2001) Cisco Israel realized that it was necessary to fire some employees, but it tried to limit the emotional impact of the event.

Why did Cisco treat its employees in this way? "Cisco- they're mensches," said Richman. "They have money, and they want to keep their good name. Cisco will definitely recover. They may want to hire these workers again in the future." When the workers see the respectful way they were let go, they may be more willing to return to the company when times are good. This is an example of how ethical decision making can also have a positive impact on the company's bottom line.

Responsibility to the 'Survivors'

When downsizings occur, the most obvious victims are the employees who are fired. However there is another class of victim to whom companies are also responsible: the 'survivors,' those employees who have survived the downsizing and stay in the company. It is easy to disregard the survivors of downsizings. However survivors suffer both practically and emotionally, which may affect their productivity.

On a practical level, those that remain with the company have many more demands placed on them. With fewer staff members but with an undiminished workload, they may have much more pressure on them to complete their work. On an emotional and psychological level, workers have to deal with the loss of friends, coworkers and mentors. Fear and distrust of the management are common feelings inspired by the downsizings, as feelings of "who's next" pervade the office. Navran says that this fear can be debilitating. "First among the fears is that once downsizing has begun, it will become an ongoing process. Though you may have survived this round, there is bound to be another and you may not be so lucky the second time around." In a climate of fear, in which employees are forced to constantly look over their shoulders, productivity drops at a rapid rate.

Employees can learn a lot about their company's management by watching the way in which a downsizing occurs. Companies that downsize sloppily, seemingly without caring for their employees, send a strong message to the survivors. Not only do survivors see what may be in store for them, but they may ask themselves, "Is this the kind of manager I want to work for? Do I want to stay in a company that treats its employees in this way?" These questions reduce an employees' loyalty to his company, and thereby

reduce his productivity.

Companies often overlook the impact that downsizings have on the survivors. "Most organizations don't realize the benefits of increased productivity that they expect from downsizing," says Navran. A major reason is that they do little to care for the feelings of the survivors. Employees that are paranoid and suspicious of management are usually not productive.

Navran has helped several companies go through downsizings, and so has practical advice for companies. "First, it is important to allow the survivors of downsizing to talk about it. It should not be taboo. Managers should say, 'at the next staff meeting, let's talk about what's the best way to move forward. How should we reallocate the work? How should we deal with the fact that people in our work group are no longer with us?' A downsizing is an impactful event, one which people need to talk about."

Navran admits that it is hard for companies to do this. "Managers rarely have the skills to deal with this. Hi-Tech companies especially have supervisors in positions of authority because of technical experience, and not because of people experience. The managers have employees who are angry, sad, and they don't know how to deal with it. Just spending time listening is important- we just went through a tough time. How should we deal with it?"

"There also needs to be honest communication from the leadership. Employees want to know the criteria for downsizings. Are more coming? What is considered when deciding who to fire?"

The bottom line is that to be a moral manager, one needs to care for the feelings of those who are fired and those who stay behind. It is necessary for managers to remember that their employees are fellow human beings, and to treat them with the necessary sensitivity.

A Jewish Perspective on Severance Packages

From an economic point of view, labor is an input into the production process, just like equipment or raw materials. The prudent manager chooses the most economical mix of all inputs in order to produce his output in the most efficient way.

However, every manager knows that it's much more disturbing to fire a loyal worker than to scrap a truck. The reason is simple: A successful company demands that its workers do more than perfunctorily carry out orders; they cultivate a sense of loyalty and devotion to the business. Management in turn wants to requite this loyalty whenever possible. One way of doing this is to give fired workers a generous severance package.

There is a fascinating parallel to this sentiment in the Biblical law of "furnishing" a bonded servant when his service is through. "And when you let him free, do not send him empty-handed. Furnish him liberally from your flock, and your threshing-floor, and your winepress; from what HaShem your G_d has blessed you shall you give to him". (Devarim 15:13-14.)

This seems like a very burdensome imposition; therefore, the Torah gives an

explanation: "Don't let it seem hard to you, when you send him away; for he was worked for twice the hire of a worker for six years; and HaShem your G_d will bless you in all you do". (Devarim 15:18.) A long-term worker like an indentured servant is not like a day laborer; because of the relationship he forms with the employer he works above and beyond the minimum his job demands.

Technically, the laws of "furnishing" apply only to an indentured servant. But the influential Medieval commentary Sefer HaChinukh points out that the underlying ethical principal applies to an ordinary worker as well: "Even nowadays, the wise person should pay attention and draw the proper conclusion; and if he hired a fellow Jew who worked for him for a long time, or even for a short time, he should give him a grant when he leaves from what HaShem has blessed him with." (Mitzva 482.)

In other words, when a loyal worker is discharged the employer should take some responsibility to care for him.

Just as interesting is the exact nature of the grant. The Talmud explains that the examples of "flock, threshing-floor and winepress" were carefully chosen, because these are possessions which will help the worker earn a living on his own. The obligation is not fulfilled with a money payment. (Kiddushin 17a.)

The best companies have a policy of giving outplacement services to long-term workers who lose their jobs due to downsizing. This policy is in the spirit of the Torah commandment of furnishing: it gratefully acknowledges the extra contribution and loyalty of the long-term worker, and gives aid which will help him or her create a new livelihood now that the old situation has been terminated.