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ENMG 652

**Case Study III: Kitchen Best**

## **Executive Summary**

Founded in the 1980s, Kitchen Best Appliance Company Ltd. (hereafter referred to as *“Kitchen Best”*) is a Hong Kong-based manufacturer of small appliances. The SME (small/medium-sized) company was founded by Chan Dong-hwa, who grew Kitchen Best into a competitive appliance maker. Chan Dong-hwa began his business while directly supervising the Foshan, China factory, located within Guangdong, a vital small appliances manufacturing hub. After the first ten years of Kitchen Best’s initial growth, the company expanded and moved part of its business operations to Hong Kong. Kitchen Best’s current business operations are now separated between the Foshan factory in mainland China, and leadership of business operations within Hong Kong. Kitchen Best has also undergone a leadership change: Chan Dong-hwa has transferred daily leadership to his son, new CEO Henry Chan, though he continues to manage and oversee Kitchen Best’s existing business partnerships.

Henry Chan is western-educated, and has set his sights on growing Kitchen Best’s overseas operations. Under Chan Dong-hwa’s leadership, Kitchen Best focused almost-exclusively on Asia, but Henry hopes to break into the American and European markets, as he sees growth potential for Kitchen Best. Early into his tenure as CEO, Henry sets lofty growth and revenue goals for Kitchen Best. However, Henry’s attempt at a company transformation is imperiled by a divergent cultural reality- he finds the Chinese markets and production practices far different from western business practices.

As Kitchen Best attempts to partner with western companies, it experiences struggles related to quality control and safety controls. These issues are endemic to the larger company whole. A series of recent incidents reveal the questionable business practices of important Kitchen Best managers, as Ma Luk, Kitchen Best’s Operations Director/Head of Greater China Business, Horatio Sze, the purchasing and production manager, and May Wei, the quality control manager have all played roles in allowing the recent incidents to happen. For Kitchen Best to reach its future goals, it will need to look for improvement on its business practices from top to bottom.

## **Company Challenges**

1. Quality Control Issues and Potential Customer Endangering: Under Henry Chan’s early leadership, Kitchen Best has experienced multiple issues directly stemming from its lack of quality control.

* In late 2009, Kitchen Best received a contract from Shago, a Malaysian distributor, to produce appliances and dinnerware for a special collection of appliances. The appliances were produced without issue, but Kitchen Best’s subcontracting of the dinnerware led to breach of contract when the dinnerware was not microwave-safe, a requirement established by Shago, leading to direct customer complaints to the distributor.

Using a non-microwave safe product can cause danger and harm for customers. The FDA cautions against these usage of certain plastics, especially those not ‘microwave-safe’, which can melt in the microwave and burn customers (“Microwave Over Radiation”, 2020). Additionally, with specific foods and usage of non-microwaveable plastics which contain melamine (common within many Chinese plastic products), people “may put people at risk of conditions such as kidney stones and kidney failure, and of death.” (“Melamine in Tableware Questions and Answers”, 2020).

* In a related case, Henry Chan was anonymously informed of quality control issues with their electric water dispensers. Kitchen Best was contracted by Haus de Metro (“HdM”), a German retail chain who contracted Kitchen Best for production of water dispensers. Kitchen Best subcontracted Qinghua Electrical Appliance Ltd., another local factory, for production of the dispensers.

The products produced by Qinghua did not meet safety standards, as the subcontractor was cost-cutting and produced with an inferior (and potentially dangerous) chemical paint. While Qinghua claimed that the paint was “too minor to jeopardise consumers’ safety”, their expectation was that it would not meet the EU standards for lead and mercury that HdM products would need to meet. Even in small quantities, both are particularly dangerous. In “Mercury poisoning linked to skin products”, the FDA states how Mercury can cause behavioral changes, and can affect entire households. Lead is also dangerous- Black (2005) cautions against exposure to lead, especially in the cases of children “Lead exposure, even at low levels, is well known for its harmful effects on children, resulting in lowered IQ.”

In both incidents, Kitchen Best’s indirect customers and their families would experience potential harm directly because of the lack of Kitchen Best’s quality and safety controls. The company and distributors would be fully liable were harm to occur, potentially leading to major lawsuits.

2. Corruption, bribery, and questionable business practices: Kitchen Best’s internal investigations revealed significant issues with questionable business practices, particularly nepotism and bribery, at multiple levels throughout the organization.

* Kitchen Best’s choice of subcontractor for the Shago dinnerware contract was based on a familial connection with Kitchen Best’s purchasing and production manager, Horatio Sze. Furthermore, due to the strength of this business connection, neither Sze nor Macy Wei (responsible for quality control) pursued a solution, even after the products were discovered to be faulty. The Shago incident reveals how managers at Kitchen Best elevate familial interests and connections over the risks posed to the company to their customers.
* As an organization, Kitchen Best benefitted from questionable ethics in partnerships. Ma Luk, in charge of opening and maintaining Kitchen Best’s accounts and connections with Chinese companies, was allowed free reign over how he built Kitchen Best’s network. Essentially bribing his contacts to work with Kitchen Best, Ma Luk was able to build and grow Kitchen Best’s partnerships with its Asian distributors, and personally benefit himself.

Because of the partnerships he was able to create, Kitchen Best did not question Luk’s methods. However, when company policies with its business partners changed, Kitchen Best was put at risk. With Kitchen Best inferior in production to similar competitors, Honghua (a major distributor partner with Kitchen Best) begins to rethink their partnership with Kitchen Best, who can no longer improve their standing through bribery. Because Kitchen Best allowed, created, and sustained relationships by essentially breaking the law, their relationships and partnerships are increasingly tenuous as their partners grow or reform their practices.

* Kitchen Best’s HdM contract’s issues revealed serious flaws with quality and testing procedures at Kitchen Best. The products produced by Qinghua did not meet standard, as the company was cost-cutting and produced with an inferior (and potentially dangerous) chemical paint. However, the subcontracted Qinghua factory was able to work with Keemark, the independent testing agency responsible for testing the Qinghua products.

Through bribes, Qinghua’s products were able pass product safety measures that had been in place. Therefore, for Kitchen Best, continued use of Keemark would mean little control on products meeting standard for any subcontracted products. Moreover, the incident reveals that Kitchen Best has little understanding of how good the production of their subcontracted products are.

3. Communication Issues: Kitchen Best is not run by one leader. Kitchen Best’s founder Chan Dong-hwa, and current CEO Henry Chan both hold significant power within the company. This problem is exacerbated by the importance of their roles within business operations. Chan Dong-hwa, the founder of the company, and his expertise is largely within Asian markets, a skill that he has cultivated through the growth of the company, forming business partnerships and employing subordinates who were knowledgeable about the reality of China’s markets. Henry Chan is foreign-educated, and his expertise and hopes are pinned on his leveraging of those talents in the western markets. While both leaders bring unique understanding to Kitchen Best, it is difficult for the company to have separate interests, as Chan Dong-hwa wants to maintain and grow his Asian market, while Henry wants to grow Kitchen Best’s presence abroad.

As CEO, Henry attempts to ingrain himself into day-to-day operations, but also relies on his father’s former senior managers as well as his father’s involvement. Thus, these communication issues work their way through the managerial chain. Ma Luk, who directly reports to the CEO, communicates both with Chan Dong-hwa and Henry Chan. The employees involved in questionable ethical behavior from previous cases all report to Ma Luk. Further exacerbating the problem is the lack of ethics that exist throughout the company chain. As Zachary (2017) writes, “Employees often follow the lead of those above them in the organizational chart as to what is acceptable or unacceptable behavior.” The poor behaviors and poor communication at the highest levels set the trend throughout Kitchen Best.

4. Lack of Direct Oversight on Chinese Operations: Kitchen Best’s leadership is unable to provide direct oversight on its Foshan factories and business connections, which endangers their ability to manage their staff properly. In the early days of company operations, Chan Dong-hwa had a direct supervisory and managerial role within every aspect of the business. However, as it grew, he divested control and power onto his leadership team.

When Henry Chan succeeds his father, these leadership challenges are exacerbated, as Henry is further disconnected from knowledge or awareness of Chinese business practices. While Henry attempts to provide oversight on the factory during weekends, much of the oversight is left to senior managers, who allowed the recent incidents to happen. As the Shago, Honghua, and HdM incidents were discovered after they had occurred, it is clear that Kitchen Best does not have full understanding of the day-to-day operations within the production factory in mainland China. Because they operate and manage from a different office than production occurs, Henry and Chan Dong-hwa have lost a direct connection to their actual production.

**Root Causes**

Systemic “growth over ethics” mindset within Kitchen Best: The company’s employees are obsessed with growing the company and enriching themselves over maintaining a code of ethics. This starts with Kitchen Best’s top leadership. New CEO Henry Chan has obvious growth aspirations for the company, hoping to develop Kitchen Best through international partnerships. Historically, Chan Dong-hwa allowed growth at any cost, allowing Ma Luk to grow Kitchen Best’s Asian business in any way, ethical or not. Neither Chan Dong-hwa nor Henry Chan overtly advocated for breaking an ethical code, but their allowance of recent incidents sets a poor example for other employees. Kitchen Best’s hope for growth has led to a devaluing of ethical corporate practices. Similarly, lower managers Sze and Wei, involved with the Shago incident, show a similar mindset to upper management. In the Shago incident, they showed a willingness to overlook and ignore obvious warning signs on customer safety when they and Kitchen Best stood to receive financial benefit.

Similarly, the dangers presented by the subcontracting for HdM products were only revealed by an anonymous letter to Henry Chan. Likely internal, this finding suggests that employees are not willing or able to publically share dangerous cost-cutting measures with upper management. Most significantly, there was direct intervention in *none* of the recent incidents- no one was removed from their position within leadership, or even reprimanded. There were no consequences for poor ethical behavior, so long as contracts were filled. Henry Chan and Chan Dong-hwa continued their willful ignorance of these unethical behaviors, distracted by his larger goals of Kitchen Best’s expansion, growth, and profit-seeking.

Thus, misplaced profit emphasis has sickened the larger organizational culture at Kitchen Best. Ethics are dictated by leadership. Luckily, ethical standards can be changed within the workplace and do not remain static. Advocating for the use of character-driven leadership styles, Barnett (2003) writes, “...you can change you. You can change your department…. You can build a departmental culture based on character.” Chan Dong-hwa and Henry Chan have the opportunity to make ethical, character-based changes that would improve Kitchen Best as a whole. They only need to begin to establish them.

Lack of Company’s Ethical Standards and Code of Conduct: Kitchen Best lacks an established ethical code of conduct for its employees. In the case of Kitchen Best, as employees are not held accountable for their actions, they may not know what is legal in their job and what is not. Zachary (2017) writes, “Following the law is often regarded as an ethical minimum”. Without a code establishing legal behaviors, such as documentation like the “Important Sections Related to Bribery and Corruption Offences Under the Criminal Law of the People’s Republic of China” (Kitchen Best), Kitchen Best has not even fulfilled the basic minimum for establishing allowable behaviors.

Without them, Kitchen Best will continue to lack effective leadership, and employees will continue to engage in behaviors that endanger the company. Miller (2004) states the importance of effective leadership as relying on core values that include ethics and integrity. She states that it is also imperative for the company to establish and communicate those values to management and employees, which leads to effective leadership and communication within a company. Frederick Jones, a business and ethics lecturer, spoke to the importance that establishing ethical standards have for companies (McKenzie 2009). Ultimately, Jones says, “If every business is based on trust, your customers will feel better about dealing with you.” As Kitchen Best sees with the Honghua incident, the opposite also holds true as Kitchen Best’s major company partner moves towards more ethical, lawful corporate behaviors.

Without such standards, Jones notes possibilities of lawsuits, and also indirect consequences, such as the minimization of long-term profits and loss of company morale. Last, a key weakness for Kitchen Best managers is that they appear to lack consequences to hold their employees to, further reinforcing any unethical behaviors. Without punishing illegal or unethical behaviors, or rewarding positive behaviors, Kitchen Best gives no reason for employees to act lawfully or ethically.

**Recommendations**

With consideration of the root causes, there are three recommendations below:

| **Recommendations** | **Rationale** | **Description/Time Frame** | **Criteria for Success** |
| --- | --- | --- | --- |
| **1. Develop a coherent and clear ethical policies and code of conduct for all employees to sign and review.** | Employees need to know what legal and ethical behaviors are.  This starts from drafting what legal behaviors are for Kitchen Best employees, and what management should expect in terms of larger ethical issues that could lead to problems. | **8/1/21 - 9/1/21:** Find legal documents relating to Chinese law on bribery/kickback/nepotism policies to establish the initial draft of the basic code of ethics.  **9/1/21 - 9/15/21:** All employees will meet and discuss, via open forum, any additional expectations from their peers. Employees should be allowed to submit requests anonymously.  **9/15/21-10/15/12:** HR will work with senior leadership to finalize the draft document  **10/1/21 - 11/1/15:** HR will draft a presentation about the basic expectations and provisions within the code of ethics, which will be presented to all employees before the 11/15 release of the code of ethics..  **11/15/21- 12/1/21:** Employees will receive the code of ethics and be expected to review and sign it before the 12/1 deadline. | Employees will have a chance to discuss and review new ethical policy and code of conduct documents. This document is created, signed, and drafted by all employees by December 1, 2021. |
| **2. Establish a series of training and meetings that reinforce proper management for all employees at Kitchen Best.** | Kitchen Best should establish and reinforce the code of conduct for its employees. | **11/15/21-12/1/21:** HR will look at the charter and early training materials to begin interviewing ethical stakeholders within Kitchen Best.  **12/1/21-1/1/22:** HR will discuss with different Kitchen Best employees what kinds of ethical issues they may run into for their specific jobs.  **1/1/22-3/1/22:** HR will work with leadership to share their concerns, and create a series of three training materials that provide examples of highest need ethical areas  **3/1/22-4/1/22:** HR will deliver these series of presentations to employees at Kitchen Best. | The ethical code of conduct has been thoroughly reviewed by HR, who will create a series of examples of allowable and disallowable practices, per tenet specified by the ethical policies.  Every employee has completed the three training sessions of highest ethical areas of need, as required by HR before April 1, 22. |
| **3. Create contractual financial incentives for employees to reward unethical behavior; set consequences (termination, etc.) for unethical behavior.** | To combat the previous interests of being profit-oriented on an individual level, Kitchen Best should create both consequences for bad actors, and incentives for good behavior for employees, which will be amended to contracts. | **3/1/22-5/1/22:** With the ethical issues seen by Kitchen Best employees, HR will use this information to provide both company consequences and incentives for review, and provide this draft document to senior leadership, based on job title and responsibilities.  **5/1/22-5/15/22:** All employees will sign the revised incentivization and consequence structure. | Employees will review, agree upon, and sign a finalized document specifying specific incentives and consequences for ethical behaviors. |

**Summary**

With proper actions taken, Henry Chan and Kitchen Best can establish a path for long-term growth, done the right way. He has the opportunity to reform a wayward corporate culture, and provide improved leadership through setting a strong ethical example. However, without significant changes being made to the company structure, Kitchen Best runs the significant risk of endangering their customers, and in-turn, themselves in their pursuit of growth.

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