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Corruption by design?

L'ArtiMarché's struggles in Russia

Urs Müller

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This case study was prepared on the basis of generalized experience, articles and books on corruption in Russia. The company L'ArtiMarché and all individuals mentioned in this case are fictitious.

This case study was written by Urs Müller of ESMT European School of Management and Technology. It was prepared solely to provide material for class discussion. The author does not intend to illustrate either effective or ineffective handling of a managerial situation.

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Disclaimer. This case is written solely for educational purposes and is not intended to represent successful or unsuccessful managerial decision making. The author/s may have disguised names; financial and other recognizable information to protect confidentiality.

Part A

In 2001, Russia was still seen as a bit of the wild, wild East and L'ArtiMarché (LAM) – the world's sixth largest do-it-yourself retail chain – definitively wanted to be part of the expected gold rush. LAM was preparing to open its first store on the outskirts of Saint Petersburg – just the first of several planned projects. After substantial investments for the first store in Saint Petersburg, the first general manager of LAM in Russia, Jules Corbusier, faced a problem: a few weeks before the planned opening, the local utility company had decided not to provide their services for the huge store if LAM did not pay a bribe. What should LAM and Jules Corbusier do? Was there an alternative to “playing the game the Russian way” and paying?

Building the world

In 1953 Pascal Favre opened a small carpenter workshop in Fribourg, a small town in the French speaking part of Switzerland. Not even 50 years later – by the end of 2000 – the still privately owned LAM Group selling all types of do-it-yourself equipment (ranging from tools and heating devices, over materials for construction and renovation (e.g. colors, tiles, stairs, windows, plumbing equipment), to wood, lighting equipment and gardening and many others) in 135 stores in 29 countries and had a turnover of almost €6.5 billion (Figure 1 and Table I). LAM aimed at providing a full range of do-it-yourself equipment with Swiss quality at prices as low as possible to local craftsmen, small business but most of all to consumers with or average income that wanted to improve their homes and houses. LAM had described its vision as:

L'ArtiMarché aims at supporting ordinary people, craftsmen and small business in their effort to improve their homes and houses. We offer the full range of do-it-yourself equipment and materials with Swiss quality. We will be industry leader in managing our cost in order to offer the lowest possible prices to our customers.

After a few journeyman years, Pascal Favre opened a small carpenter workshop at the outskirts of the city of Fribourg in 1953. At the beginning he tried to sell low-cost furniture. But, he soon also sold wood and tools that would allow his customers to build their own furniture. Favre had very good relations (and even family ties) with several wood farmers in the Valais area (in the Swiss Alps). Therefore, he was able to buy and sell wood cheaper than even the specialized stores. He soon also realized that he could produce many of the tools at very low cost. Accordingly, he successively expanded the range of products he was selling out of his carpenter workshop – always driven by the idea to offer prices significantly lower than anybody else in the greater area around Fribourg. Quickly he managed to increase the output and opened his first do-it-yourself store in 1955 – for the first time, he also included electrical items (lighting, electrical power tools, etc.) and a gardening section. As brand name for his store he combined the two French expressions “artisan” (craftsman) and “marché” (market) and formed the name “LAM”. Over the years he enlarged this first store

Figure 1 Development of LAM's turnover (in million euros)

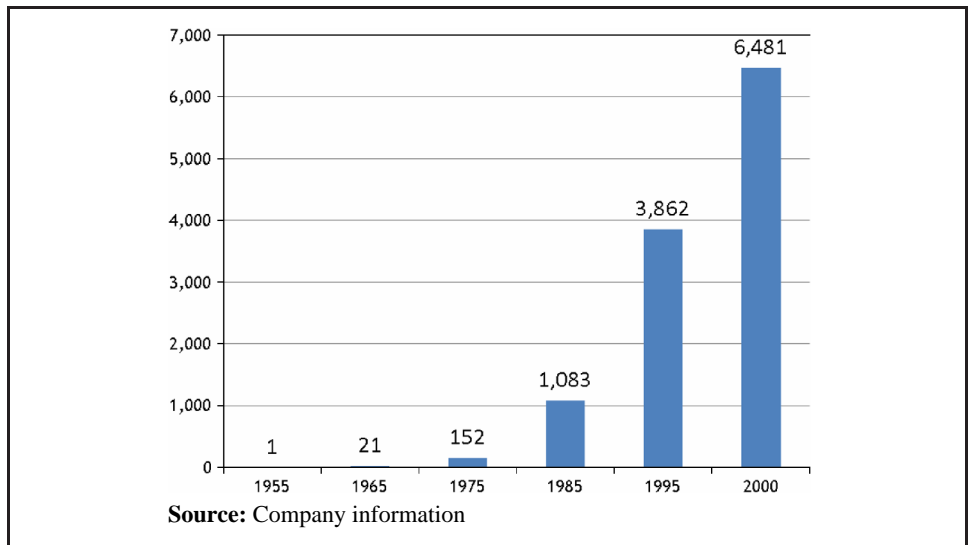


Table I List of countries with LAM presence

<i>Year of entry</i>	<i>Country</i>	<i>Number of stores end of 2000</i>
1955	Switzerland	11
1962	France	13
1963	Austria	6
1969	Germany	22
1973	Denmark	3
1975	Sweden	9
1976	Australia	5
1977	Canada	5
1977	Norway	2
1979	The Netherlands	4
1979	New Zealand	3
1980	Spain	4
1981	Iceland	1
1981	Belgium	2
1982	Singapore	1
1983	Hong Kong	1
1983	Turkey	4
1984	USA	10
1986	UK	9
1988	Italy	4
1990	Poland	4
1991	Hungary	2
1991	Czech Republic	2
1991	Slovakia	1
1992	Slovenia	1
1994	Malaysia	1
1996	Finland	1
1997	Taiwan	1
1998	China	3

Note: Including year of entry and number of stores end of 2000

Source: Company information

and finally also expanded – in 1958 – to Geneva and in 1959 to Zurich. In both cities, he demonstrated that his idea of selling low-cost do-it-yourself material and equipment could also succeed in metropolitan markets.

LAM began its international expansion in the early 1960s, first with its neighbor France (1962) and then by moving into Austria (1963). The following two decades saw LAM opening stores in much of Western Europe, expanding into Germany in 1969 and Scandinavia in the mid-1970s (Denmark: 1973; Sweden: 1975; Norway: 1977). Having opened stores in Australia in 1976, Canada in 1977 and New Zealand in 1979, LAM took on the US market several years later, opening its first store in Boston, Massachusetts in 1984 – even after entering Singapore in 1982 and Hong Kong in 1983.

In 1989, the founder Pascal Favre stepped down as CEO of LAM, but as sole owner he maintained significant influence on strategy and culture of LAM – which was often described as highly cost-cautious, sometimes even as stingy. LAM's internationalization was not only driven by the desire to sell more products to a broader customer base. The search for low-cost production opportunities and capacities had already turned LAM into an international business early on.

Going East: LAM in Eastern Europe and Russia

LAM recognized the advantages of buying supplies from Eastern European countries long before the fall of the iron curtain in 1989. As the company expanded internationally, Pascal Favre quickly realized that sourcing wood from Switzerland was not economic enough to offer competitive prices in many attractive markets. Already in the late 1960s, the company had contracts with wood suppliers and factories in East Germany, Poland and Yugoslavia. Since the 1970s supplies from Eastern European suppliers made up for around 25 per cent of the company's total needs.

After the fall of the Berlin Wall and the opening of new markets once captured behind the Iron Curtain, LAM quickly took the opportunity to expand its sales concept into Eastern Europe, first opening a store in Warsaw, Poland, in 1990 and then moving into Hungary, the Czech Republic and Slovakia the following year. LAM's immediate success in these markets clearly showed that Eastern Europe had a very high demand for renovation and construction of homes and houses: between 1990 and 2000 LAM opened a total of ten stores in Poland (four stores), Hungary (two stores), Czech Republic (two stores), Slovakia (one store) and Slovenia (one store). A move further to the East – to Russia just seemed as a logical next step.

In 2001, LAM planned to open its first store in Saint Petersburg. By entering Russia, LAM wanted to reach this huge and potentially highly lucrative market of up to 140 million consumers: an emerging middle class in Russia (fueled by the country's oil wealth and a constant growth in the GDP) was eager to improve its standard of living, including making changes to the interior and exterior of its homes and apartments. There had been little improvement since Soviet times. Russian apartments, houses and gardens (the famous Russian "Dacha"!)) just seemed to be a goldmine of need. And next to regular consumer that wanted to do some reconstruction or renovation, there were also a fair number of small construction companies and individual craftsmen opening businesses in Russia in the 1990s. However, craftsmen complained about difficulties to get good quality tools and materials at low prices. One of the reasons for that was the lack of large international DIY chains. Even ten years after the fall of the wall none of the top five global DIY chains (Home Depot, Lowe's, Kingfisher, Groupe Adeo, or Ace Hardware) had started operations in Russia in 2000. Several analysts perceived presence in the Russian market to be of great importance for the competitive position of international retail chains in general and the DIY industry and LAM in particular.

When the lights go out in Saint Petersburg: problems before opening the superstore in Gatchina

Soon after the decision to enter Russia, LAM had to learn that doing business in this country required some adaptation: LAM soon struggled to get hold of an interesting location at the

necessary low cost to fit into the business model. After an unsuccessful search within city limits of Saint Petersburg, the decision was made to open the first store 28 miles outside of the city in a place called Gatchina. Search for the site, development and construction took painful two and a half years. But new challenges emerged: the city of Saint Petersburg blocked the planned construction of a new highway that was supposed to ease the traffic to the new store. LAM initially was told by the region and the city of Gatchina to build parts of the highway at its own cost. But after already investing US\$6 million, the city of Saint Petersburg prohibited the connection of the new highway to the existing street system within the territory of the city. The day of the opening came closer and closer, but the traffic issue remained unresolved.

And finally a few weeks before the grand opening of the first LAM in Russia in 2001, the company's management was approached by the local utility company and given an ultimatum: the choice for the general manager of LAM in Russia, Jules Corbusier, was to either pay a bribe or do without electricity. Already under pressure after the previous challenges that had accompanied the work-up to the grand opening, Jules Corbusier had to act and to act fast. Could LAM afford to postpone or even totally cancel the opening in Gatchina? To pay, or not to pay the bribe: that was Jules Corbusier's question.

Part B

LAM was famous for finding creative solutions to reduce cost. Very much in line with this company image, its Russian organization came up with a creative solution *vis-à-vis* the local utility company's demand for some "special payments": instead of paying the required bribe for the provision of electricity to LAM first Russian outlet in Gatchina near Saint Petersburg, the Swiss DIY retailer bypassed the utility company by renting large diesel generators to power the outlet. Inspired by the small diesel generators that were in LAM's product portfolio, the prospective store manager suggested renting diesel generators until the connection to the grid was established. But as LAM still had to learn, corruption in Russia was systemic and not only to be defeated through innovation or creativity alone.

When the lights go on: LAM initial success in Saint Petersburg

The opening of LAM first store in Russia was an enormous success: when the diesel generators started operating in the morning to provide the necessary electricity for the lights, computers and cash registers, the customers were already lining up. In total, 30,000 people crowded the 25,000 m² store on the first day. But due to the unresolved issues with the municipality of Saint Petersburg, the planned highway for the traffic to the store was still not connected to the municipal highway system. Accordingly the line of cars that were trying to get to LAM through a small country road was close to 3 km long at noontime. Nevertheless, many people made it into the store: more than 200,000 people came to the outlet within the first two weeks. And even though two-thirds of the people just had a look, more than 70,000 people started to buy immediately. LAM assessment of the market proved to be correct: there was a desperate need of Russians with low to average income, of individual craftsmen and small-construction businesses for materials and equipment to be used for the construction and renovation of apartments and houses. Hopes and plans for even more new LAM stores on basis of a huge potential customer segment all across the country were high.

And things even got better: after realizing that LAM was not going to play the corruption game, the utility company caved in and finally started providing the needed electricity. But there remained significant challenges during the opening of the next stores: during subsequent openings in Russia during the following years, LAM faced similar corruption attempts from electricity companies. The DIY retailer then again followed the established pattern of renting diesel generators to provide enough electricity for the large stores. It became their standard operating procedure, and executives at LAM took pride in having found a creative solution to the bribery demands. In a newspaper interview LAM's country manager in Russia, Jules Corbusier, commented: "At the very core we are a family owned business from Switzerland – we don't accept corruption and will not give in."

Eastern expansion: LAM planned and real growth in Russia

As of the end of 2008, LAM had opened nine stores in the Russian Federation (Table II). Two LAM outlets were located in Saint Petersburg, where the first two stores were opened in 2001 and 2002. In 2003, LAM decided to move to Moscow and even opened a second store in Russia's capital in 2005. In 2006 LAM opened a total of three stores, the most in any single year, and then slowed down its expansion again, opening one store in 2007 and then one in 2008.

And even though these nine stores did run successfully, LAM's market entry in Russia was clearly behind plan: the company had planned to grow much faster in Russia, but the declining rate of openings reflected an increasing level of problems, most of which had to do with administration and an opaque Russian bureaucracy: just like the Kafkaesque constellation with the half-finished highway before the opening of the first store, LAM again and again ran into bureaucratic challenges. A classic example was the planned construction of a store in Sochi, Russia's famous port city at the Black Sea coast. The construction was started in 2004, but the company was repeatedly prohibited to open the Sochi store due to the alleged "violation of numerous safety regulations and other rules," according to local officials. It was problems like this that again and again put a damper on LAM's rapid expansion plans.

Despite the slowdown in opening new stores, Russia already accounted for almost 5 per cent of LAM global business at the end of 2008 (at a time when the international competitors just had started to enter the market (Leroy Merlin, part of Groupe Adeo, entered Russia in 2004 and Kingfisher only in 2006)). On average LAM grew at a rate of about 20 per cent per year in Russia and enjoyed an increasing popularity in the general public. LAM clearly wanted to be in Russia and to grow even faster than they did. The customers wanted their products. But the organization seemed to be slowed down by external obstacles.

Corruption within LAM: generating more than electricity

After several years of business in Russia the attention moved from external to internal challenges: not giving into the systemic corruption in Russia, LAM continued to rent diesel generators whenever a local utility company demanded a bribe in order to provide electricity. This tried-and-true method worked for years and seemed the ideal solution to getting around corruption. Confronted with bribery demands from utility companies before the opening of two LAM stores at the end of 2006, LAM once again rented diesel generators. The stores opened on schedule end of 2006, but at the end of 2008 both malls were still being supplied by these generators, because in these two cases, the companies asking for a bribe proved to be stubborn and electricity was never turned on.

At the beginning the skyrocketing rental costs for the diesel generators went unnoticed by the Swiss DIY giant. But over time first signals of an underlying issue surfaced: in 2008, the

Table II List of stores in Russia with year of opening

<i>Location</i>	<i>Year of opening</i>	<i>Size in m²</i>
Saint Petersburg (Gatchina)	2000	25,000
Saint Petersburg (Parnas)	2001	26,000
Moscow (Mytisci)	2003	27,500
<i>Sochi</i>	<i>Project started in 2004; still not open in 2008</i>	<i>20,500</i>
Moscow (Odintsovo)	2005	26,500
Novosibirsk	2006	25,000
Kazan	2006	25,000
Yekaterinburg	2006	24,500
Omsk	2007	25,800
Samara	2008	26,200

Note: Status 2008

Source: Company information

LAM headquarters were wondering about the comparably low margins of the Russian operation. LAM started in cooperation with the Russian management team an analysis and soon realized that the operating cost for the malls were disproportionately high and decided to hire a private investigation company from Finland. After examining the Russian operation, the investigators identified an employee who testified that the Russian LAM executive in charge of renting and managing the generators, Yuri Alexeyevich Gorsky, was taking substantial kickbacks (in form of weekly cash payments) from the diesel generator rental company Russian Generators International (RGI). LAM compared the prices paid to RGI with market prices and realized that they were significantly above alternative market prices. The investigation revealed that the fraud had continued for more than two years, and LAM estimated the damage to be at around €120 million. When confronted with the allegations, Gorsky denied any wrongdoing. And the owner and head of the generator rental company, Konstantin Ivanovich Kirillov, argued that the high costs were due to the fact that the generators had been rented as standby electricity, but had supplied the two large stores without pause for years.

While the diesel generators were still buzzing after two years in operation and while the customers were still rushing into the nine Russian stores, LAM now had to turn its attention also to the inside of the organization. What should the local company do now – in short and long-term perspective – after finding signs of corruption within LAM?

Part C

After the discovery of corruption within its own Russian management, LAM decided to follow its no-corruption policy. The company terminated the contracts with the diesel generator company RGI and with the purchasing manager Yuri Alexeyevich Gorsky, even though both insisted on being innocent. Yuri Alexeyevich Gorsky denied any wrongdoing and claimed instead that LAM country managers were trying to cover up their own expensive incompetence by blaming Russian subordinates.

LAM realized that something had to be done and contacted the government. But Russia's political reaction was also one of (at least partial) denial. Pointing to the fact that the corruption issue was no longer just an external effect on the retailers business, a Russian Government official stated: "It was fraud, but L'ArtiMarché employees did it to themselves. L'ArtiMarché needs to do its homework internally – some renovation and reconstruction seems to be necessary." Pascal Favre, LAM's founder and owner, admitted publicly that the retailer was slow in recognizing the obvious signs for corruption within the company, especially the soaring rental costs for the diesel generators. He blamed the rush to enter the highly attractive market – especially as none of the large global competitors had taken the step to enter Russia before 2004.

A money-losing proposition: going to court in Russia

Once so proud of their innovative answer to bribery attempts, LAM's executives in Russia were forced to recognize that the systemic problem had not been solved – neither in the company's external environment, nor internally. Now the company wanted to regain control. Together with the termination of the contract with the diesel generator company and the purchasing manager, LAM went to court and claimed compensation for fraud. But instead of receiving reimbursement for the €120 million in damages from the kick-back scheme, an arbitration appellate court in Moscow ruled in April 2009 that LAM had to pay €5 million for breach of contract to RGI.

LAM appealed – but had to deposit the €5 million in an escrow account. This money was supposed to be paid out to the owner and head of the generator rental company, Konstantin Ivanovich Kirillov only if the appeal were lost as well. But in a separate instance a lower court ordered that the money be directly withdrawn from LAM's banking account in the country, and this was done so. Like this LAM had paid out €10 million – twice as much as the initial ruling, although the appeal had not even started (Tables III and IV).

Table III TI CPI 2009 for selected countries

<i>CPI rank 2009</i>	<i>Country/territory</i>	<i>CPI score^a</i>	<i>First LAM store</i>	<i>Number of stores</i>
1	New Zealand	9.4	1979	3
2	Denmark	9.3	1973	4
3	Singapore	9.2	1982	1
3	Sweden	9.2	1975	9
5	<i>Switzerland</i>	<i>9.0</i>	<i>1955</i>	<i>13</i>
6	Finland	8.9	1996	2
6	The Netherlands	8.9	1979	6
8	Australia	8.7	1976	5
8	Canada	8.7	1977	6
8	Iceland	8.7	1981	1
11	Norway	8.6	1977	3
12	Hong Kong	8.2	1983	2
12	Luxembourg	8.2	2007	1
14	Germany	8.0	1969	28
14	Ireland	8.0	2006	1
16	Austria	7.9	1963	6
17	Japan	7.7	2004	3
17	UK	7.7	1986	12
19	USA	7.5	1984	14
20	Barbados	7.4	n.a.	n.a.
21	Belgium	7.1	1981	3
[...]		(as of here, only a selection are provided)		
24	France	6.9	1962	17
27	Slovenia	6.6	1992	1
32	Spain	6.1	1980	10
35	Portugal	5.8	2002	2
37	Taiwan	5.6	1997	1
46	Hungary	5.1	1991	2
49	Poland	5.0	1990	6
52	Czech Republic	4.9	1991	3
56	Malaysia	4.5	1994	1
56	Slovakia	4.5	1991	1
61	Turkey	4.4	1983	6
63	Italy	4.3	1988	9
71	Greece	3.8	2005	1
79	China	3.6	1998	5
84	India	3.4	n.a.	n.a.
106	Argentina	2.9	n.a.	n.a.
111	Egypt	2.8	n.a.	n.a.
139	Bangladesh	2.4	n.a.	n.a.
139	Pakistan	2.4	n.a.	n.a.
146	Kenya	2.2	n.a.	n.a.
146	<i>Russia^b</i>	<i>2.2</i>	<i>2001</i>	<i>10</i>
154	Yemen	2.1	n.a.	n.a.
168	Burundi	1.8	n.a.	n.a.
176	Iraq	1.5	n.a.	n.a.
178	Myanmar	1.4	n.a.	n.a.
179	Afghanistan	1.3	n.a.	n.a.
180	Somalia	1.1	n.a.	n.a.

Notes: ^aA high CPI score indicates a low level of perceived corruption in the respective country and vice versa; the scale ranges from zero to ten; ^bcountries tying at rank 146: Cameroon, Ecuador, Kenya, Russia, Sierra-Leone, Timor-Leste, Ukraine, Zimbabwe

Source: Compiled by case author using company information and the TI "CPI 2009" (www.transparency.org/policy_research/surveys_indices/cpi/2009/cpi_2009_table (accessed January 3, 2010))

The opposite of transparent

While the denial of corruption in Russia was widespread, politicians in the country started to admit that the country was having a problem. Several high-caliber politicians repeatedly criticized corruption as an important impediment to foreign investment. They were also

Table IV Average CPI 2009 for countries according the decade of first LAM opening

<i>Decade</i>	<i>Countries entered during this decade</i>	<i>Average CPI score^a</i>
1950s-1970s	Switzerland, France, Austria, Germany, Denmark, Sweden, Australia, Canada, Norway, The Netherlands, New Zealand	8.6
1980s	Spain, Iceland, Belgium, Singapore, Hong Kong, Turkey, USA, UK, Italy	7.0
1990s	Poland, Hungary, Czech Republic, Slovakia, Slovenia, Malaysia, Finland, Taiwan, China	5.4
2000	<i>Russia</i>	2.2
2000s	Portugal, Japan, Greece, Ireland, Luxembourg	6.7

Notes: ^aA high CPI score indicates a low level of perceived corruption in the respective country and vice versa; the scale ranges from zero to ten

Source: Compiled by case author using company information and the TI “CPI 2009” (www.transparency.org/policy_research/surveys_indices/cpi/2009/cpi_2009_table (accessed January 3, 2010))

urged to action from non-government organizations such as Transparency International (TI). TI published on an annual basis its “Corruption Perception Index” (CPI). In 2009, TI ranked Russia (together with Kenya) on the 146th place (seven places behind Pakistan) from 180 countries in the area of “clean government and business” in 2009 (Table III). Despite their public statements, Russian leaders did not seem to have an active answer to corruption by 2009.

In 2009, Russian President Dmitri A. Medvedev enacted a law prohibiting surprise inspections from state employees, a practice often used by fire fighters and health department employees as a decoy for extortion. This law also required that spouses of bureaucrats disclosed their income and assets so that tax evasion and money laundering within the family became more difficult. TI’s reaction was carefully positive, but they simultaneously pointed to the fact that not only LAM but also many other foreign investors were struggling with corruption in Russia.

The National Anti-corruption Committee estimated that one-fifth of the annual GDP in Russia, i.e. US\$200-300 billion, was paid out in bribes to bureaucrats. Jules Corbusier, first general manager of LAM in Russia remembered that there were often so many bureaucrats in the LAM offices that it was impossible to tell them apart from employees.

Loving Russia: why was the country so lucrative for LAM?

Russians wanted to improve their apartments, homes and gardens – and for that they needed DIY outlets. It was as simple as that. One legacy of the Soviet era had been a lingering deficit in the quality of apartments, houses and the legendary Russian Dacha’s. Accordingly, the growth rate within Russia averaged 20 per cent for LAM for most of the 2000s, which definitely made it easier to ignore the challenges of doing business in this market. And despite all their struggles LAM managed to open a tenth store with another 23,000 m² in Nizhniy Novgorod in 2009.

So far, LAM had seemed to be able to overcome graft, corruption, bureaucracy, etc. with persistence, with adherence to company policies and even more importantly with creativity: Jules Corbusier mentioned that sometimes it was necessary to get more than 300 separate permits to build a store: “Waiting for all these permits would have taken years.” Accordingly the company had always looked to come to agreements with local authorities so that they could begin construction and receive the permits “on the fly.” But the problems had not only spilled over from external to internal challenges: after the court’s ruling and the double withdrawal of the €5 million, it seemed as if the problems also extended beyond the area of business into the judicial system, which evoked even larger concerns. On the one hand LAM seemed to be lonely in this fight, but at the same time the Swiss retailer had to wonder if there was anything that the company could do to enable its continuous operation in a market that

seemed to be totally lost. How could LAM, one of the ten largest foreign investors outside the oil/gas-industry, continue to do business in a country that was placed in a cluster of the 20 per cent most corrupt countries in the world and in which even the legal system failed to provide the necessary level of security for operation. The average CPI of all countries into which LAM had expanded since its foundation per decade had fallen from 8.6 in the 1950s-1970s to 5.4 in the 1990s. In 2009, Russia scored only a shockingly low 2.2 (Table IV). Had LAM in its decades of geographic expansion grown too far?

Part D

Hoping that public pressure would compel Russian authorities to act, LAM went public with their problems with corruption in Russia. LAM executives talked to Switzerland's most influential newspaper *Neue Zürcher Zeitung* in August 2009 about their continuous challenges; the resulting article then was quickly picked up by international media. Now the company hoped that the unusual step of talking about the issues openly would finally help to mobilize the government and authorities to take decisive steps against corruption.

The never-ending story of corruption

LAM had refused to “play the game” in Russia, and this caused many difficulties in opening the company's stores. Not only have several utility companies refused to provide electricity without a bribe. There have also been various instances when other bureaucratic agencies have hindered the opening of a finished store, as was the case in Sochi, where – six years after starting the project – the finished store still was not allowed to open; at least not as long as LAM was not willing to contract a local construction company to “fix” alleged deficiencies.

It was also some struggles with local authorities that made LAM open its 11th outlet in Dema in late 2009. This store had initially been planned for the neighboring city of Ufa, but the location was moved after city officials sold the property to a private dealer who then wanted five times more for the land than the price already negotiated.

Public lobbying

However, at some point LAM had enough and decided to take even more public action: on August 27, 2009, LAM founder Pascal Favre announced in a radio interview that LAM was stopping all new investments in the giant country. Addressing the issues of corruption in Russia, Favre said that LAM was not going to compromise its company policy and get involved in corruption.

LAM was one of the ten largest foreign investors outside of the oil/gas industry and one of the biggest owners of commercial real estate in Russia. The company had been present in the country for now eight years and been enormously successful in selling DIY equipment and material to craftsmen, small construction businesses and consumers. Despite this great success in Russia, LAM announced to stop all future investments in this country. This action was supposed to send a strong signal – but the company decided to put even more pressure on the Russian Government.

While most companies (including LAM up to this point) carefully avoided talking about corruption – at least as long as they could – the Swiss DIY retailer decided to get involved in politics: in order to force the government to take action, the company contacted the *Neue Zürcher Zeitung*. Pascal Favre, the founder and owner of LAM, and Jules Corbusier, the first general manager of LAM in Russia, provided detailed insight information into its experiences with corruption in Russia. The newspaper did grasp the opportunity and published a lengthy article on the cover page, which was then picked up by the British *The Times* and subsequently also from various different media (including TV channels such as *BBC* and *CNN*) around the globe. The case was finally on the table of the international debate. Hopes were high that the government had to act in order to ensure future foreign investments from LAM but also from other international companies.

Other international companies with Russian subsidiaries also had been struggling with corruption. And next to lobbying, some of them joined collective actions against corruption, e.g. industry led initiatives such as the “Russian Energy Compliance Alliance” founded in December 2010 (*Center For Business Ethics and Corporate Governance*: “Russian Energy Compliance Alliance” www.ethicsrussia.org/index.php?option=com_zoo&view=category&layout=category&Itemid=206 (accessed January 13, 2012)) or the anti-corruption pact initiated by members of the Russian-German Foreign Trade Chamber. The latter initiative – signed off in April 2010 – included companies such as MAN, Daimler and Siemens, which have had corruption scandals in Russia in the past (*Russia Briefing*: “Foreing Companies Working in Russia Sign Anti-Corruption Pact”, available at: <http://russia-briefing.com/news/foreign-companies-working-in-russia-sign-anti-corruption-pact.html/> (accessed January 13, 2012)). But the success of these initiatives still remained to be evaluated.

And again another turn of events

After firing Yuri Alexeyevich Gorsky, the purchasing manager, and restating the validity and importance of its non-corruption policy, LAM might have assumed to have taken the necessary internal steps to prevent future corruption issues. But soon the company had to realize that LAM was still not immune to corruption within its own ranks: Jules Corbusier, LAM’s deputy general manager in Russia was fired in February 2010 after being implicated for allowing bribes. Coming only a few months after Jules Corbusier himself had publicly underscored LAM anti-corruption stance in Russia and had announced the investment stop, this revelation disturbed many both Western and Russian commentators. It also begged the question of whether LAM’s internal controlling processes were adequate – and if LAM’s mission to conquer Russia was hopeless.

The benefit and value of challenges: learning lessons

On March 16, 2010, LAM owner Pascal Favre publicly announced to draw consequences from the Russian experience. He accepted the fact that the speed of LAM’s market entry in Russia was part of the problem. As lesson learned from the continuous challenges with corruption, he declared that LAM would slow down the speed of expansion in China and other emerging markets. Favre promised to not get carried away from the enormous growth potential in many emerging markets. Instead the company would make sure that all international subsidiaries adhere strictly to the company policy and values.

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