

Multi-Family Ventures, LLC and the 2008 Financial Crisis: Ethical Decisions Regarding Keeping the Board Informed

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Abstract. This true account provides a summary of a firm and its CEO caught up in the housing market frenzy that occurred in the mid to late 2000s. Although confronted with a number of economic, strategic management, human resource, ethical, and legal challenges, the owners make decisions that cause the firm to grow at an exponential rate. The case documents the eventual results of many of those decisions. Readers are challenged to identify ethics issues involved and the business decisions that precipitated those ethical issues. Some issues include working with business partners who have different ethical stances from your own, whistle blowing for illegal actions, the impact of problem employees on ethical and legal issues, and being transparent and honest when informing the board of directors about business conditions. Teaching notes include lessons learned by the CEO. Ways to avoid similar mistakes in the future are provided.

Keywords: business ethics, housing bubble, economic crisis, legal issues, ethical issues, multi-family real estate, REIT, private equity, strategic planning, business partners, transparency, honesty.

1. The Dilemma

Mike Morawski was walking toward a board of directors meeting for Multi-Family Ventures, LLC (hereafter referred to as MFV),¹ to attend an important meeting in May of 2010. He fully intended sharing information with the men and woman on his board about the stress he, as CEO, and the company, were experiencing. The agenda of topics he intended to address that night included such items as how upside down the company had become, the fact that the properties were likely headed into foreclosure, the lack of cash flow they were experiencing, the extent to which investors would get hurt as a result of foreclosure, their

1. Most names, locations and the company name have been changed.

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inability to improve operations across the portfolio, and the results of executive staff conversations about turning all the properties over to a receiver.

Mike had always believed that transparency and honesty were central to any successful business. But recently he had not been transparent and honest with those who needed it most. Due to the market climate, he found himself in a fearful defensive mode, operating out of chaos, and secluded within the walls of his company.

Before the board meeting, he was met in the parking lot by Jack Blevins, MFV's in-house legal counsel. The attorney stopped Mike and said, "Hey, before we go in, I need to counsel you not to talk about our situation. Don't talk about the receivership, the losses, and the upside down deals."

Needless to say, Mike was shocked and felt like he had just been punched in the gut. Jack went on to say, "We don't have enough information to be able to report reliably. So, instead, let's gather some additional facts, and then we can do a conference call with everyone in a week or two. You understand?"

Jack's comments threw Mike's world into even more chaos. He was faced with an important decision he had to make on the fly. As the CEO faced with this ethical dilemma about whether to be honest and transparent, what should he do now? Should he tell the board or not? Who does he turn to for information to help him make this decision? Does he try to get a second opinion? Does he just ignore the request of MFV's legal counsel? On the other hand, Jack should have Mike's best interests at heart, right?

2. The Creation of MFV

While many are familiar with at least some of the nuances of buying and selling homes to individual homeowners, the world of multi-family real estate (apartments, condominiums) often has more complexities. For example, in order to fund the relatively larger purchase price and operational expenses of multi-family units, multiple investors and lenders are often required. These can include traditional banks, institutional investors like mutual funds and insurance companies, as well as wealthy individual investors. Organizations and individuals invest in these real estate offerings in addition to, or as an alternative to, traditional investing (e.g., investing in the stock market). To learn more details on the industry, readers are encouraged to view summary websites on exactly how real estate investing works (e.g., <https://www.investopedia.com/mortgage/real-estate-investing-guide/>, <https://fundrise.com/education/blog-posts/how-to-invest-in-real-estate-the-basics>), and the legal issues that can arise (e.g., <https://iclg.com/practice-areas/real-estate-laws-and-regulations/usa>).

In 2005 Mike Morawski made a decision to move into the sponsorship² and private equity³ world of multi-family real estate, by opening MFV, a small