

# Corporate Governance and the Former East Germany: the Role of the Treuhandanstalt in Moulding the New German Economy \*

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*This paper demonstrates the development of economic reform of the new Germany following the collapse of the Berlin Wall. The analysis focuses on the Treuhandanstalt (THA), established in 1990, with responsibility for dividing up East Germany's national assets. The role of the THA is shown as a key social actor in moulding the new German economy. Decisions that were highly detrimental to the former German Democratic Republic (GDR) – resulting in job losses and de-industrialisation on a massive scale – were treated in an entirely perfunctory fashion. The manner in which the THA conducted its business thus took little account of the economic need to conserve employment and the symbolic need to preserve enterprises in the East.*

*Der Aufsatz stellt die Entwicklung der Wirtschaftsreformen in den neuen Bundesländern nach dem Fall der Berliner Mauer dar. Der Fokus liegt auf der 1990 gegründeten THA, die den Nachlaß der DDR aufteilen sollte. Die Rolle der THA wird als sozialer Schlüsselfaktor angesehen, der die Wirtschaft im neuen Deutschland formte. Entscheidungen, die sich als nachteilig für die ehemalige DDR auswirkten – die u.a. zu Massenentlassungen führten – wurden äußerst nachlässig gefällt. Die Art, in der THA ihre Geschäfte abwickelte, nahm wenig Notiz von der wirtschaftlichen Notwendigkeit, Arbeitsplätze zu erhalten oder der politischen Erfordernis, Unternehmen in Ostdeutschland zu erhalten.*

*Key words:* Germany / Treuhandanstalt / employment / GDR / political influence

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## Introduction\*

Corporate governance has been defined, variously, as 'the system by which companies are run' (Charkham 1994), or 'the mechanisms by which companies are controlled and made accountable' (Peck and Ruigrok 2000), or 'the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment' (Schleifer and Vishny 1997). Such definitions, however, do not reflect the fact that each nation has a system of corporate governance in its own image, moulded over time by the particular capitalist creed to which it adheres (Maclean 1999). At the centre of the German governance system is the principle of *Mitbestimmung* or co-determination, as well as the two-tier company board, the *Vorstand* and *Aufsichtsrat*<sup>1</sup>. Co-determination is well suited to the German 'habit' of consensus. The German system has instinctively assumed a much broader view of governance than the narrow agency view that prevails in the Anglo-American system. It has been fundamentally pluralistic, being oriented naturally to a range of stakeholders, marked by a deep-rooted belief in the need to mould together a common destiny. The word 'stakeholder' does not exist in German. This implies, however, that the concept is so deeply ingrained as to be part of those quintessential values that are taken for granted. For any German CEO, saving jobs has been every bit as important as satisfying shareholders. Viewed in this light, the manner in which the Treuhandanstalt (THA) – the Trust Holding Company established by government in March 1990 to divide up East Germany's national assets – conducted its business conflicted with this key tenet of the German governance system.

Now, approaching a decade after the THA completed its radical programme of privatisation, and following an alarmingly slow rate of national economic growth over this period (15 per cent since 1991, compared to 41 per cent in the United States), the entire system of corporate governance in the new Germany is under scrutiny, critics arguing that 'social market' orientation cannot be sustained in a new global economic order.

This position is well captured in a recent paper composed on behalf of the Federal Reserve Bank of St Louis and the U.S. Federal Reserve System, in which the authors state:

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<sup>1</sup> The *Mitbestimmung* Gesetz or Co-determination Act, passed in 1976, endows companies with more than 2,000 employees with a supervisory board comprised of half shareholders' and half workers' representatives, while companies with smaller workforces (500-2,000) must have supervisory boards with one-third worker representation (Maclean, 2001).

The presence of underinvestment and overstaffing problems in codetermined firms, together with inefficiency-induced migration of economic activity away from firms subject to codetermination, may be sufficient to detract from overall economic performance. (Emmons and Schmid 2001:3)

Although this free market critique of an alternative, and historically validated, system of governance may be disputed, it is undoubtedly the case that the Rhineland model has been subject to liberalist dilution over the past decade to necessitate increased managerial responsiveness to shareholder values. From 1990 to 1997 stock market capitalisation as a proportion of German GDP rose from 23 per cent to 40 per cent. This implies that share price movements are now likely to play a stronger role in the discipline and motivation of senior managers. The move towards shareholder accountability was perpetuated in the mid 1990s through the launch of the Neuer Markt, a domestic stock exchange for small, growth companies. Tax legislation has sought to facilitate the disposal of corporate shareholdings, whilst the 1998 Kontrag Act on the Control and Transparency of Enterprises has increased corporate transparency from a shareholder perspective. More recently the 2002 Cromme Code, based on recommendations rather than binding rules, seeks to establish a set of corporate governance rules that do not choke business.<sup>2</sup> Flexibility is regarded as crucial. Whilst it would be premature to signal the demise of the social market approach, there has undoubtedly been a growing exposure of the German institutional edifice to the volatilities, and fragmentary effects, of the market over the past decade. Such exposure has been accompanied by the internationalisation of controlling interests in German concerns. Shortly following re-unification in 1993 it was highly symbolic that Germany's largest industrial company, Daimler Benz, needed to tap into extra capital by listing its shares on the New York stock exchange.

The purpose of this paper is to trace normative shifts in corporate values in the new Germany, and to reflect on the pressures bearing on the social market model in the immediate aftermath of privatisation. In examining the affairs of the THA it is clear that, at this critical time in German history, the erstwhile pre-eminence of social values in industrial life was subsumed in a headlong and pragmatic rush to fix economic problems in the short term. Although we are wary of implying cause and effect between past and present economic agencies and agendas, we are struck by the status of the THA as a harbinger for a re-ordered set of economic and cultural priorities in the new Germany. It is salutary to note that the birth of the new Germany was accompanied by a substantial breach of a Weberian-inspired system of industrial organisation that

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<sup>2</sup> „Principles of Good Corporate Governance“, paper presented by Dr A. Stefan Kirsten, Chief Financial Officer and Member of the Executive Board, Thyssen Krupp AG, Royal Institute of International Affairs, London, 11 February 2003.

had promoted social peace through the integration of the interests of labour through voice-based participation of major stakeholders. Through its radical programme of privatisation, the THA disseminated a new set of values into the new Germany in which short-term profitability transcended social orientation and in which there were clear 'winners' and 'losers' in the refurbishment of economic structures. Far from integrating 'Eastern' interests into the new German economy, by the end of the privatisation programme in many senses Germany remained as two nations, with a predominantly dispossessed 'Eastern' contingent. Although observers have described the re-unification process as little more of a 'Western' takeover of the East, it is clear that, in a climate of recession, the values instigated by the THA hold sway in the morphing model of corporate governance across the new Germany. The 'Easternisation' of West German industrial relations is now a well-observed phenomenon (Hyman 1996) particularly in respect of plant-level wage bargaining exerting upward pressure on centralised, participation-based, organisational architecture for regulating employment conditions (Hassel and Rehder 2001). It is our contention, however, that such developments form only one element of a larger ideological rubric, fundamentally impacting on the future direction of corporate governance in the new Germany, which is seeking to reconcile past institutional securities with the new imperative of global competitiveness.

In seeking to show how the economic fortunes of East and West were recast in the years following the collapse of the Berlin Wall, we concentrate our analysis on the operations and structures of the Treuhandanstalt. Its programme of economic rationalisation, which lasted approximately four years, was designed to dispose of East German assets worth approximately DM600 billion. These included some 13,700 industrial units that constituted the fall-out from large industrial combines, either through sale or closure. It also disposed of the properties belonging to the secret police and armed services. As a central economic actor at a critical phase in the transformation of East Germany, it is clear that the agency had a vital formative role in structuring the new German economy. As an ideological custodian of government in the sphere of privatisation, the agency set an economic train in motion which countervailing forces have struggled to halt. Through our research we aim to cast new light on the operations of the THA, by appraising its nature as a social actor. We assert that organisational tenets of the THA reflected the *status quo* in power relations between East and West, and that its activity could not be disassociated from these.

Recent reports on the German economy reveal continued divergence in the economic fortunes of 'the two Germanys'. Behind a headline unemployment figure of around 17 per cent in the East persists a range of social and economic problems. Unemployment has risen steadily in the East over the past decade, and more East Germans are employed in low paid jobs than Westerners. By the end of 1997, wages within firms linked to the tariff system in the East had

reached 89.2 per cent of those in the West. However only about half of private sector employees are paid in accordance with the tariff system. Easterners work longer hours and have fewer benefits. As many as 22 per cent of children in East Germany live in poverty, as against 12 per cent in the West. Easterners spend approximately 20 per cent less time on leisure than their Western counterparts. The Eastern Länder are affected by a continuous loss of population: in 1998 alone 160,000 migrated from the former German Democratic Republic. And finally crime figures are much higher in the East, as are road deaths (Thomaneck and Niven 2001: 1, 2, 72).

The research on which this paper is based derives from 39 face-to-face interviews with individuals who were stakeholders in the privatisation process (see Table 1). Many had worked for the Treuhand or for one of its successor organisations; others had been buyers or potential buyers; others still had opposed the activities of the Treuhand, such as union representatives. The buyers came from three categories: East German Management Buy-Outs (MBOs); West German investors; and foreign investors.<sup>3</sup> The interviews were carried out over five months in 1994 and 1995 (August-October 1994, and May-June 1995). They were thus conducted sufficiently close to events to record valuable detail and insights. At the same time, the passage of time since the interviews took place provides a necessary critical distance, allowing events to be viewed objectively in the context of the situation that currently obtains. Now, over one decade since re-unification, the economic and cultural ramifications of decisions made in the period after the collapse of the Berlin Wall may be evaluated with the benefit of hindsight. The semi-structured nature of the interviews accorded some structure and focus, while allowing flexibility to explore and probe other pertinent issues (Howard 2001).

## **The Origins of the THA: Economic Logic and Cultural Identity**

After the fall of the Berlin Wall, there ensued in East Germany a period of intense political and economic turmoil, marked by frequent changes of government. The THA was established in 1990 by an East German government in crisis. It was designed as part of a 'third way' political and economic agenda. This entailed gradual economic reform towards a 'market-orientated planned

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<sup>3</sup> West German investors which participated in the study include: Berliner Großwaagen (Growa) GmbH; Berliner Lufttechnische Anlagen GmbH, Deutsche Interhotel AG, Mercedes-Benz AG Nutzfahrzeuge, NARVA and Siemens AG. Foreign investors include Berlin Cosmetics GmbH (US), Berliner Schreibfeder GmbH (India), Coca-Cola Erfrischungsgetränke GmbH (US), Deutsche Waggonbau AG (US), Elf Oil AG (France), Hewlett-Packard (US), KWO Kabel GmbH-BICC (UK) and Otis GmbH (US). Only one East German MBO participated in the study, reflecting the difficulties of MBOs for former employees: Florena Cosmetic GmbH. All interviews were conducted by Dr Jutta Howard.

economy', and the involvement of East German representatives in the restructuring of their own economy. However, the pace of economic and political change soon began to accelerate, beyond the reach of East German representation.

*Table 1 (adapted from Howard, 2001): Interviewees according to Stakeholder Group*

Organisation	Name	Position	Date
Berlin Cosmetics GmbH	Karl Maier	Chief Financial Officer	24 Aug 1994
Berliner Großwaagen	Peter Strempel	Managing Director	26 Jun 1995
Berliner Lufttechnische Geräte GmbH	Michael Nagl	Managing Director	27 Jun 1995
Berliner Schreibfeder GmbH	Wolfgang Lemme	Managing Director	26 Jun 1995
Coca-Cola Erfrischungsgetränk e GmbH	Hans-Joachim Kloetz	Manager	24 May 1995
Deutsche Interhotel	Reinhard Pöllath	Managing Director	30 Jun 1995
Deutsche Waggonbau (DWA)	Dietrich Papsch	Confidential Clerk to the Head of the Managing Board's Office	12 May 1995
Elf Oil AG	Thomas Vanicek	Member of the Board of Directors	11 May 1995
Florena Cosmetic	Günter Haferkorn	Managing Director	21 Oct 1994
Forena Cosmetic	Dr. Reinhard Hübner	Managing Director	21 Oct 1994
Florena Cosmetic	Günter Haferkorn	Managing Director	6 Jun 1995
Hewlett Packard	Edmund Mästele	Managing Director, Berlin Branch Office	4 May 1995
KWO Kabelwerk Oberspree	Gerd Schlenzka	Chief Financial Officer	19 Jun 1995
Mercedes-Benz Nutzfahrzeuge Ludwigsfelde GmbH	Dr. Rolf Bartke	Managing Director	12 Jun 1995

NARVA	Michael Müller	Chairman, Works Council	29 Jun 1995
Otis Elevator	Dr. Roland Fischer	Managing Director HR and IS and Legal Affairs	18 May 1995
Promochem	Dr. Joachim Kaiser	Managing Director	16 Jun 1995
BVS	Lorraine Davis	Privatisation agent	20 Jun 1995
BVS	Dr. H.W. Klein	Attorney	15 Jun 1995
BVS	Margaret Knudson	Privatisation Agent	27 Jun 1995
BVS	Dr. Hilmar Schmidt	Privatisation Agent	23 May 1995
BVS	Bernd Stephan	Department Manager	21 Jun 1995
BVS	Hans Benno von Brauchitsch	Department Manager	19 May 1995
BVS	Götz von Stumpfeldt	Privatisation agent	22 Jun 1995
BVS	Dr. Klaus-Peter Wild	Executive Director	22 Jun 1995
Waggonbau Niesky GmbH	Michael Clausecker	Managing Director	16 Jun 1995
IBM Germany GmbH	Wilfried Daudt	Managing Director, Small-Business Division	18 May 1995
DIW	Heiner Flassbeck	Economist	5 May 1995
DIW	Frank Stille	Economist	5 May 1995
IG Metall	Dieter Scholz	Director, Business and Economics Department	19 May 1995
PDS	Dr. Dietmar Bartsch	Treasurer	14 Jun 1995
Senatsverwaltung für Wirtschaft und Technologie Berlin	Franz Bertsch	Coordinator for Treuhand-related Affairs	8 Jun 1995
Bodenverwertungs- und –verwaltungs GmbH (BVVG)	Wolfgang Hanke	Chairman of the Board	8 Jun 1995
Beteiligungs- Management- Gesellschaft mbH Berlin (BMGB)	Dr. Heiner Bonnenberg	Managing Director	30 May 1995

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BA für vereinigungs- bedingte Sonder- aufgaben (BVS)	Dr. Hilmar Schmidt	Privatisation Agent	23 May 1995
DISOS GmbH			
DV-Informations Systeme, Organisation und Service GmbH	Manfred Koebler	Managing Director	15 May 1995

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TLG Treuhand Liegenschafts- gesellschaft mbH	Dr. Volker Oerter	Director, Marketing and Regional Development	12 Jun 1995
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\* Official title of Wolfgang Lehmann Abteilungsleiter, Berliner Büro der Leitung; Kunden- und Besucherbetreuung.

\*\* Official title of Gert Zschiesche: Abteilungsdirektor Infrastrukturdienste Berlin; Kaufmännischer Geschäftsführer Siemensstadt Grundstücksverwaltung.

Most notably the swift introduction of currency union in July 1990 struck an instant body blow to East German competitiveness. In these new circumstances, the unification treaty of 31 August 1990 excluded East German influence, so that effectively 'the west German system was simply extended eastwards' (Thomaneck and Niven 2001: 70). Nevertheless, despite being couched in rather vague terms, the original remit of the THA was for privatisation and renovation (*Sanierung*), not just the former. The treaty also stressed the principles of regeneration and fair competition (Thomaneck and Niven 2001: 71). The THA's new mandate was to reorganise firms, preparing them for the demands of a market economy before transferring them into private ownership. Both Smyser (1992) and Glaßner (1992) identify the work of the THA most closely with the assumption of responsibility for the liabilities and assets of state-owned companies. Either the companies were restructured, generally to shed labour and to cut costs in preparation for sale, or they were sold off. Firms not thought to be viable were closed down.

The THA's legal status was that of a 'federal agency<sup>4</sup> with a high degree of independence, at one remove from direct control of government. With respect to its operation, control of the THA was shared between the Ministry of Finance, the THA's supervisory board, the Federal Accounting Office (Bundesrechnungshof) and Parliament. The agency possessed, in many respects, a structure similar to a German public company. The government appointed a supervisory council consisting of a chairman and 16 members, including

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<sup>4</sup> Bundesunmittelbare Anstalt des öffentlichen Rechts.

representatives of large German companies, trade unions, the Bundesbank and East German Federal states, as well as representatives from the Ministries of Finance and Economic Affairs (Carlin 1994). The supervisory council in turn appointed the executive board, which included a president and four directors. The agency's head office in Berlin had responsibility for policy making, large-scale privatisation projects and complex cases. HQ also supported the operations of fifteen branch offices responsible for marketing and privatising smaller businesses. Operations were distributed between four departments: Reconstruction, Privatisation, Labour Market/Social Policy and Finance.

With few exceptions, the THA used a single privatisation procedure known as formal bidding. Potential investors were expected to present a business plan, and to be prepared to make job and investment commitments. By 1992, a flurry of activity had resulted in the privatisation of approximately 25,000 small shops, restaurants, hotels, cinemas, bookshops and pharmacies – mostly to *in situ* East German nationals, since few interested Western investors could then be found. Airports, ports, water and sewerage companies and public transport were transferred to the State and municipalities. Stevens-Strohmann (1993) notes that, to accelerate the process, the agency preferred to deal with buyers with proven management skills and the capacity to launch enterprises into world markets. To reach a wider market, and 'to soften the one-sided predominance of West German buyers', THA offices were set up in New York and Tokyo to facilitate consultation with potential investors (Owen-Smith, 1994). The top foreign investors included Canada, USA, France, Switzerland and other countries.

In addition to formal bidding, the THA employed two other methods of privatisation: management buy-outs (MBOs) and management buy-ins (MBIs). With MBOs, existing management bought THA company spin-offs. This had the advantage of granting some East German participation in the privatisation process, particularly in the early stages. MBIs offered a second means of enticing capable managers to acquire a business enterprise in East Germany.

By the end of 1994, of its total portfolio of 14,600 enterprises, some 2,983 had been purchased through MBOs/MBIs and 860 firms by foreign investors. The vast majority of East German firms, however, had been purchased by West German investors. Clearly, large West German and foreign firms, vastly experienced in terms of strategic and financial management and project planning, enjoyed a massive inbuilt advantage in business planning and in inspiring the THA's privatisation agents with confidence. In contrast, East German individuals, firms and MBO teams were sorely disadvantaged, and doubtless gave every appearance of being imbued with anachronistic management techniques. Under the 'old order', for example, they had never had to market anything. Long-standing cultural tension between the two Germanies, encapsulated by the widespread use of the pejorative terms 'Ossis' and

‘Wessis’, was exacerbated in turn by tension between two disparate management systems, such that communication problems frequently arose despite an ostensibly ‘common’ language. As one West German interviewee put it:

We used the same words, we thought we understood each other, but the words had different meanings. For example, the word ‘order’, which we understood as a purchase order, was used to mean ‘delivery’ order [in East Germany]. Since they were the only suppliers of elevators in East Germany, an order was simply a request to deliver an elevator.<sup>5</sup>

Liberal economic logic dictated that almost all the prime assets and organisations in the THA’s portfolio were released into West German or foreign hands, amounting to a wholesale transfer of East German assets to the West. Some former GDR-combines were purchased with a view to preventing the development of new competition in East. Lesser and more marginal assets and organisations were normally the only eligible candidates for privatisation by MBOs. Nor were buyers guaranteed even-handed treatment by the THA. While firms sold to Westerners frequently had their debts written off prior to sale, those of firms sold to East German purchasers were often made to carry existing company debts (*Altschulden*), thus mortgaging their future. In addition, East German buyers were often charged a high purchase price, and, as one East German interviewee was at pains to stress, were scrutinised much more closely than West German buyers: ‘We, as East Germans, were strictly checked out with respect to trustworthiness, our past was investigated, business plan scrutinised, and high purchase price demanded. We had to let the *Gauck Behörde*<sup>6</sup> investigate all facets of our lives’<sup>7</sup>

This biased, unfair treatment of East German buyers existed despite the fact that many of the THA’s privatisation agents were themselves East Germans (see Table 2). One interviewee recalled that the THA did not know how to approach his MBO proposal: ‘We had an additional disadvantage because we were East Germans negotiating with East Germans. We perceived a certain envy and resentment, and also a certain arrogance and *Machtgehabe* [blustery behaviour from individuals who act as if they have power].<sup>8</sup> Another interviewee confirmed this: ‘Everything from the East was wrong, everything the East

<sup>5</sup> Interview with Dr Roland Fischer, Otis Elevator, Managing Director for Human Resources and Information Systems, May 1995.

<sup>6</sup> A reference to the Stasi. Pastor Joachim Gauck was instrumental in setting up a special office for the purpose of handling Stasi archives.

<sup>7</sup> Interview with Günter Haferkorn, Managing Director, Florena Cosmetics, June 1995.

<sup>8</sup> Interview with Peter Strempel, Berliner Großwaagen, Managing Director, June 1995.

Germans knew was wrong. It was frustrating to think that a 25-year-old had the power to decide [the future of the company]<sup>9</sup>.

The cultural alienation experienced by East German buyers in their dealings with the THA can be explained in part by the fact that many of its East German agents seem to have identified more closely with the West German identity, than with their East German counterparts. This in itself reflects the efficacy of the process of absorption, or takeover of the East German identity by the West. In the first few years after unification, West Germans dominated top management positions not just in economic organisations or within the THA (see Table 2), but also in financial and educational institutions or in public administration in the East. As a result, East German THA agents felt uncomfortable with their own (or former) cultural identity. Would-be East German buyers felt underestimated and overlooked, as another East German interviewee acknowledged: 'When we first made contact with the Treuhand, it immediately became clear that for the most part the Treuhand agents were 'hot-air merchants' [Schaumschläger] who underestimated us'. Such unequal treatment by the THA fuelled resentment against West Germans in the new Länder. Dubbed 'Besserwessis', they were perceived as know-alls who always knew best (Edwards and Lawrence 1994).

In summary, it was clear that in the new post-Communist order, all buyers were not equal, and that from 1992 in particular a hierarchy of buyers prevailed. Western buyers (foreign and West German) were clearly perceived as the most desirable, rich in capital and management know-how. In contrast, East German buyers were acceptable only when no other buyers could be found. That they lacked both capital and relevant managerial know-how effectively excluded them from participating in the economic transformation of their own country. The fact that there were powerful cultural and historical reasons for their lack of finance and skills was ultimately irrelevant as the economic logic which had served West Germany so well since 1945 determined the way forward, and the West German cultural identity asserted itself over the East. In what was understandably perceived by East Germans as an act of dispossession – accentuated by the concomitant fear that West Germans might repossess their houses and flats – only one sixth of the industry of the former GDR was sold to its own citizens (Thomaneck and Niven 2001: 70).

## The Legacy of the THA

Praising the work of the THA, Trust Fund adviser Andre Leysen stated: 'It is easy to make fish soup out of an aquarium, but harder to turn the soup back into an aquarium' (Schirrmacher, Schiwy and March 1995:100). Indeed, according

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<sup>9</sup> Interview with Michael Müller, NARVA, Chairman Works Council.

to most indicators, the privatisation agenda pursued by the agency met with considerable success. At its inception, the THA assumed responsibility for some 8,000 major enterprises employing more than four million people (Roestler 1994). By the time the agency was disbanded in 1994, only 350 enterprises remained, these being passed over to a Department of the Finance Ministry (Turnock 997: 190).

*Table 2: Origins of THA Management and Staff at 30 June 1992*

Position	East Germany (as percentage)	West Germany (as percentage)
Directors	0	100
Department Managers	19	81
Privatisation Agents	41	59
Employees	69	31

Sources: Siebel, W. with Kapferer, S., 1993, cited in Howard, 2001.

There were some notable examples of what Thomaneck and Niven (2001: 73) describe as 'sincere investment in and commitment to the east'. Carl Zeiss in Jena, with Western support, has survived and thrived. Deutsche Bank had extended some 300 new branches into the East by the end of 1993, comprising some 12,500 employees. Daimler-Benz AG, Volkswagen and Bayer AG are amongst the companies that have made considerable investment into the former GDR.

Yet, overall, the costs of the liberal economic agenda are aptly summarised as follows:

In contravention of the fairness principle, west German firms bought up east German industry to kill potential competition and cream off investment subsidies. Promises to maintain certain levels of employment were frequently broken. Rather than revitalise industry bought from the Trust Fund, there was a tendency to sell off properties to the booming service industry, or use the industrial plant as an extended workbench for west German industry. Often, such 'extended workbenches' were the first to be shut down when economic problems hit. (Thomaneck and Niven 2001: 71-72)

By the end of its existence, the THA had been involved in the loss of around two million jobs, having presided over the closure of prime East German industries (such as Trabant and Interflug). It had complied with unscrupulously low estimates by Western investors of the value of East German assets, and had had to take responsibility for existing debts and clean up costs to expedite sales. Consequently, at its close, the THA had accumulated a debt of DM265 billion on behalf of German taxpayers. Commentators bear witness to the de-industrialisation of Eastern economic territory (Luft 1996) with only around one

sixth of East German industry having been retained. The result, according to cynics, is that the new Eastern landscape resembles not the 'blossoming landscapes' promised by Kohl in March 1990, but rather 'a huge nature reserve with a sausage stall' (Thomaneck and Niven 2001: 73).

## **The THA as a Social and Political Entity**

It is clear from this brief investigation of the economic and social 'fall-out' of the activity of the THA that it cannot be regarded as a politically and ideologically neutral force in reconstructing the German economy. Although ambiguity and misconception surrounded the 'mission' of the THA, it became clear at an early stage of its operations that the agency was strongly committed to a radical neo-liberal credo. Despite its concern with brokering financial deals and facilitating economic transactions, it is important to recognise that the agency combined a grouping of individuals from West and East, albeit for a limited period (see Table 2). The organisation existed within a turbulent environment, characterised by the collapse of one economy and its assimilation into or absorption by another. Economic matters in such circumstances could not be separated from the euphoria and crisis that accompanied transformation in all walks of life. It is our assertion that the transactions that privatised the bulk of East German industry, and brought it into Western hands were not merely economic in nature, but were also conditioned by the social orientation of the actors responsible for their generation. Decisions were taken and administered by individuals and groups who possessed a particular 'window on the world', and who occupied a personal niche in a distinctive organisational hierarchy. In the section that follows, we analyse the THA as an organisational form, referring to critical organisational phenomena and events, notably establishment, structure and evolution, leadership and key employment policies. We do not address organisational culture as a discrete factor, but view it rather as an intangible notion that embraces and transcends the various areas forming the basis of our deliberation.

## **Background**

As a new organisation, the agency experienced severe growing pains, and, at the end of its life cycle, the uncertainties of contraction and downsizing. Rarely have such a large number of people, from diverse educational and professional backgrounds, been assembled for a limited period of time to achieve a specific goal, and then disbanded. Stability has been crucial to Germans since the traumas of World War II and the forced division of the nation. Despite the euphoria that surrounded the event, the unification of the two Germanys was threatening to the established order, and the burden of historical expectation was laid on the THA and its employees. Inside the THA, environmental turbulence exacerbated internal chaos. Initially it lacked systems, policies and

procedures, its employees were not specifically trained for their roles, there was a lack of technology and technological expertise, and there were intense time pressures resulting from the rapid pace of privatisation. Given the consistent pursuit of stability and organisational harmony by German institutions, the conditions at the THA came as a shock, not only to East German staff, but also to West German bureaucrats and public servants. A fundamental requirement of the organisation was that it should be comfortable with continuous change. Managers moving from a stable to a dynamic environment inevitably experienced tensions, and internal tensions were in turn communicated to external critics and clients. Many of these were quick to point out that the agency acted inconsistently and made too many errors. Organisational crises were commonplace (including the assassination of its second president); there were several changes in leadership during the THA's brief existence; and staff turnover rates were high. The THA became inseparably bound up in German minds with all the errors made – and all the criticism of those errors voiced in the press – in the early stages of unification. In this sense it functioned as a (convenient) scapegoat for government. There is evidence also that the THA was 'hijacked' by influential politicians pursuing 'pet' projects and personal agendas. The fact that it had a limited life span served government interests: the errors could at a stroke be attributed and thus disposed of.

## Start-up

Initially, the THA suffered serious labour shortages when it needed to recruit personnel at short notice to convert approximately 150 gigantic former East German *Kombinate* into publicly traded companies (AGs) or limited liability companies (GmbHs). Following currency union in July 1990 and unification in October 1990, the THA's mandate changed to unbridled privatisation. To achieve this required a significant number of employees. So, from tiny beginnings, with just 91 employees, the agency eventually grew to employ nearly 5,000 people.

After a staggering increase of 1,800 per cent in staffing between July 1990 and September 1991 as a result of the new mandate, the rate of growth slowed to 38 per cent between September 1991 and July 1992. Undoubtedly part of the attraction of working in the agency resulted from its generous remuneration package. According to Dyck (1997), in 1991 the THA board set directorial salaries at between DM 250,000 and DM 300,000 per year, 'which placed THA managers in the 15<sup>th</sup> percentile of average salaries of top executives in the 100 largest German firms in the same year'.

The annual salaries of the THA's 135 departmental heads in 1992 ranged from DM 120,000 to DM 276,000, and for directors the range was from DM 228,000 to DM 400,000. Dyck points out that in the same year, the average salary of the 46 THA directors was DM 379,000. The most sought-after applicants had

business-related qualifications, management experience, or a business degree as well as legal training. Perhaps not surprisingly, given its mission, as Table 1 demonstrates West Germans quickly established themselves as the dominant force within the agency, comprising 100 per cent of directorial staff, 81 per cent of department managers and 69 per cent of non-executive positions.

It emerged from our research that managers could broadly be classified into three distinct groupings. First, the privatisation agents were predominantly young and male, recent university graduates at the start of their careers, and thus inexperienced in management. At the next level, the departmental managers were in their early 30s and came to the THA either as civil servants, or because they were dissatisfied in subordinate positions in the private sector. The final group consisted of experienced managers in their late 40s, 50s and early 60s who were appointed to senior positions, and many of whom were close to retirement.

### **Muddling Through**

Wagner (1992) observes that the THA was very active at advertising jobs: 'the Treuhand independently recruited staff through job advertisements and personnel consultants to win executives for both the Treuhandanstalt itself and the Treuhandanstalt companies'. Applicants responded to newspaper advertisements and Rohwedder, the second president, personally approached potential directors and asked them to join the agency. Others were referred through their previous (overwhelmingly East German) networks, especially in the early stages. Employment with the THA was considered to be a very demanding activity, and the agency appealed to potential applicants by stressing that 'executives prone neither to sleep or ulcers can apply to the Treuhandanstalt, Alexanderplatz, East Berlin' (*The Economist*, 28 July 1990: 54).<sup>10</sup>

The fifteen branch managers of the THA, each one an experienced manager from the West German industrial sector, began their work on 4 October 1990 (Wagner 1992: 289). However, there was still a considerable shortage of staff, and Rohwedder complained to Chancellor Kohl that while the THA had numerous purchase offers on file, the shortage of personnel had created such a bottleneck that the agency was not able to process them in a timely manner. In response the former Chancellor called on leading West German firms to make 100 top managers available to the THA. Chancellor Kohl's appeal was not without success. Wagner (1992: 289) notes that banks and the industrial sector in Western Germany leased managers to the Treuhand, which assisted its early start. By April 1991, the THA had been reorganised three times and its

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<sup>10</sup> The THA's headquarters were at the Alexanderplatz until July 1991, when the office was moved to the Leipziger Straße.

organisational structure had been subject to frequent modification. Rohwedder highlighted the reasons: 'We have not been around a hundred years like Siemens, we not only have top women and men, we have hired anyone we could' (Christ 1991: 17). Others argued that 'the Treuhand hardly attracted the best of the West. Many were retired businessmen looking to bump up their pensions, or failed managers hoping for another chance' (Eisenhammer 1995: 7). Occasionally western businessmen from rival firms were hired in a consultancy role to assess the viability of East German enterprises, this invariably leading to the demise of the latter. Consequently, external views of the status of the agency and its staff were mixed. According to some, the term *Altlästen*, literally 'old burdens', aptly described THA employees.<sup>11</sup> The following quotation – from the aptly named *Kolonie im eigenen Land* [*A Colony in one's own Country*] by Christ and Neubauer – epitomises this derogatory viewpoint:

Most of them [the employees] were GDR-citizens and therefore could not have any experience with firms in a market economy; they did not know how to draw up balance sheets and analyse them; how to value, sell or even restructure businesses so that they can withstand west German and foreign competition (Christ and Neubauer 1991: 122-3).

By way of contrast, Krumrey (1992) asserts: 'Most Treuhand employees were not political "Altlästen", but perfectly normal privatisation agents who were overworked and trying very hard to adjust'. In response to criticism about 'Ossis' in the THA office, Birgit Breuel, the agency's third president, made a point of ensuring that they were not sacked, but on the contrary allowed to continue working there as long as they were willing and able to do the job: 'It is not possible to do without people who have intimate knowledge of the conditions in the former DDR' (Neubauer 1990: 6).

At least in its early stages, prior to the shifting of its headquarters to the Leipziger Straße, the perceived inefficiency of the agency could be attributed, to some extent, to physical conditions. From all accounts, in the beginning an atmosphere of the 'American Wild West' prevailed, with six people sharing an office and a telephone. From there, the telecommunications system improved considerably to the point that the secretary managed to place three calls a day; although it took all day to make connections since the system was totally inadequate.<sup>12</sup> Although the early days were chaotic, there was a sense in which they were remembered with affection. One employee recalled that 'overall,

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<sup>11</sup> This term has two meanings: on the one hand, old, improperly disposed of harmful waste, synonymous with the legacy of environmental pollution in East Germany and, on the other, an inherited problem.

<sup>12</sup> Interview with Klaus-Peter Wild, BVS, Executive Director, June 1995.

people approached the task with tremendous energy and enthusiasm, because they understood the significance of their work'.<sup>13</sup>

## Leadership

The first president of the THA, Reiner Gohlke, was described as 'a workaholic of few words, who [had] moved from a top management job in IBM to become head of the chronically loss-making *Bundesbahn*, the federal railways' (*The Economist* 28 July 1990: 54). Gohlke stayed just a few weeks at the THA, demoralised by the constant criticism (*The Economist*, 25 August 1990: 60). Gohlke had clashed, moreover, with the chairman of the supervisory board, Detlev Rohwedder who succeeded Gohlke almost immediately as the agency's president. Originally, Rohwedder's appointment was temporary, since he was scheduled to return to his previous position with the Hoesch Steel Group after six months, although in the event he agreed to stay beyond his original period of tenure. Chancellor Kohl charging him with galvanising the process of East German transformation. His assassination in April 1991, for which the terrorist Red Army faction was implicated, throws into stark relief the cultural dissonance of the THA's liberalising mission in the former GDR. In one sense this was ironic, given Rohwedder's instinctive orientation towards social market economics and a desire to enhance the decision-making powers of the *Länder*. His successor, Birgit Breuel, subsequently pursued a more strident free-market agenda. She had been the only woman on the executive board and had distinguished herself in a political career that had begun in 1966 and included eight years as Director of the Department of Economics for the state of Lower Saxony, after which she served for three years as Head of the Ministry of Finance in Hanover. She had served on the THA's board as Rohwedder's deputy and on succeeding him pursued an ambitious strategy of 'speedy privatisation, rigorous restructuring, and if necessary, careful liquidation' (*Frankfurter Allgemeine* 15 April 1991). The bulk of the THA's privatisation mandate was accomplished under her leadership, which lasted nearly four years.

## Organisational Structure and Evolution

The THA made three major attempts to find its most appropriate organisational structure over the course of its existence. The early hierarchical structure was commonly regarded as inappropriate for the agency, given the transformational nature of its mission. This structure was thus abandoned at an early stage, to be replaced with one designed to promote decision-making freedom on the part of officials. The consultancy firm, Roland Berger, was engaged in 1990 to advise on suitable modification, and a flat structure transpired, organised along

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<sup>13</sup> Interview with Dr Joachim Kaiser, Managing Director, Promochem, June 1995.

functional lines (privatisation, restructuring, share deals, branch offices, finance, social programmes and special assets, properties and refinancing). This organisational form strengthened the position of the THA branch offices and was in keeping with a broader political agenda to avoid industrial concentration and centralisation of power. However, following the explosion in staff numbers, and the move to new headquarters, an internal formalisation process occurred. The agency continued to attract external criticism for its inefficiency and lack of transparency. As a result, the functional structure gave way to one based on matrix principles. Personnel and finance departments were separated from privatisation operations and elevated to the strategic level with representation on the executive board. Executive directors now shared overall responsibility for several different functional areas as well as designated industrial sectors. In effect, the matrix structure enabled employees to prioritise the privatisation agenda.

A number of observers reflected that the THA had become more bureaucratic during its life cycle. For example, a departmental manager explained that from 1993 a shift had been discernible from the previous dynamic, decision-orientated environment to a slower, encumbered approach. This observation was confirmed by a director, who claimed that there had been far greater scope for decision making in the embryonic stages of the agency.

### **The Incentive Scheme**

Behrend (1995) claims that despite the fact that generous salaries, benefits and pensions were paid to top managers, they still seemed dissatisfied. In 1992, the THA implemented a bonus pay system for its managers that aimed to induce successful managers to remain at the agency until its closure in 1994. However, as Logger, Vinke and Kluytmans (1996) observe: 'The target of achieving speedy privatisation was enhanced by a bonus system for the executive staff of the Treuhandanstalt linked to the number of sales (privatisations) effected'. Nick (1995) contends that directors and department heads received substantial enhancements to their base salary, ranging from 19 to 24 per cent for directors and from 25 to 28 per cent for departmental heads. On top of the generous wages and bonus system, there was also a separation allowance and car leasing expenses. Clearly, in return for generous salaries, bonuses and other benefits, THA employees had to relinquish some of the securities normally contained in employment contracts. The usual social safety net, including pensions and supplementary private insurance, was not always provided. While the bonus scheme was designed primarily to benefit executives, it also assisted the companies in the THA portfolio and potential buyers since it speeded up transactions. However, flaws were also apparent in the new payment scheme. According to research by the Deutsches Institut für Wirtschaftsforschung (DIW): 'An internal premium system pressed the management of the Treuhandanstalt for quick privatisation. As a consequence, negotiations about

the details of privatisation were hurried; mistakes like insufficient control of bidders solvency were bound to occur.'

In summary, the THA had experienced rapid organisational transformation over its period of existence. Whilst the early stages were characterised by disorganisation and anomie combined with a pioneering spirit in rebuilding German economic structures, later developments in organisational form involved a conjuncture of structure, culture and human resource policies to deliver 'rational' administrative efficiency. Moreover, the 'new order' that overtook the organisational form of the THA served to lock the agency into an apparently immutable agenda for reform, based on liberal economic principles. This path was taken despite obvious and trenchant opposition to such economic pragmatism, and the availability of alternative strategies that could recognise the legitimate yet contrary concerns of prominent stakeholder groups.

### **An Alternative View of Reform**

Although an 'undersocialized' agenda (Geppert and Kachel 1995) dominated the work of the THA, this was not without mitigation. According to Geppert and Kachel (1995), in later phases of the THA's organisational development internal and external stakeholders sought to moderate its liberal economic instincts, countervailing opinion emerging from the Democratic Socialist Party (PDS) as well as from policy researchers, sections of the academic community and especially the media. In response, the THA periodically engaged with initiatives designed to stimulate active company restructuring and to sustain human capital. Some notable examples of enhanced proactivity occurred at a regional level, where the new Länder, supported by local government, developed strategies to maintain and establish traditional networks and relationships. Kern and Sabel draw attention to the ATLAS project in Saxony, as well as to the Brandenburg-EKO steel project, through which the THA sought to work with other actors – the regions, potential investors, as well as the unions – in order to find a middle way between 'mehr Politik' and 'mehr Markt' (Kern and Sabel 1993: 482, 484). Such initiatives were politically helpful, in that company restructuring was seen to be important. They also allowed more participation from East German managers in decision-making processes at company level. But sometimes such local actors participated in decisions against the restructuring of particular companies, as the price for the survival of the regional economy (Kern and Sabel 1993: 485).

Trade union interests in particular represented a counterbalance to the THA's economic radicalism during its period of existence and IG Metall, the major metalworkers' union, became a vociferous opponent. In examining the views of IG Metall we seek to identify strands of ideological counterbalance to the THA's agenda of rapid privatisation. However, we should point out that there were variations of opinion across the body of opposition.

As noted, the unification process involved the extension of West German institutional arrangements into the East, and the area of trade unionism and industrial relations was no exception. Upchurch (1995: 280) argues that that 'the collapse of the former Eastern trade unions and the consequent take-over of membership by unions based in the former Federal Republic is a unique phenomenon'. In incorporating East German members, it is clear that IG Metall, and other trade unions, were seeking to be active participants in the transformation process. Although they had some success in bidding up grossly inferior East German wages, their agenda was considerably more far reaching than such 'bread and butter' concerns. IG Metall's mission was to secure social equality for East Germans in the new Germany. In pursuit of this, the unions won minority representation on the board of management of the THA, thus enabling the voice of labour to be heard at a strategic level, albeit in a muted fashion.

IG Metall became one of the most outspoken critics of the THA's actions and policies. A senior representative from within its ranks takes issue with the rapid privatisation programme launched by the THA. According to Horst Scholz, Director of the union's Department of Business and Economics, the agency's radical agenda of economic liberalism was ultimately implemented at the expense of vital investment into research and development, and promoted depletion in the stock of available management skills in the Eastern Länder. He states that 'it may have been better to maintain a larger number of firms, even if not profitable, to restructure them and provide funds for research and development and for marketing, and have the government cover any potential losses for three or four years'.<sup>14</sup> According to Scholz, 'all the problems that existed in the enterprises before were still fully evident after privatisation. The way in which the THA dealt with this inequity was simply by selling the firm to an investor at a very low price and with subsidies'. Rapid privatisation allowed no time to establish the market economy structures necessary to support surviving businesses. Moreover, unions levelled the charge that rapid privatisation was a positive invitation to speculators of all kinds to plunder the assets of the former East Germany. That said, Scholz acknowledged that 'the majority of investors were sincere in their dealings with the THA. Most investors genuinely wanted to participate in the transformation of East Germany'. Unfortunately, others were less scrupulous, and many potential sales negotiations collapsed. One West German firm allegedly tried to persuade its East German target to defraud the THA by manipulating the company's balance sheet.

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<sup>14</sup> Interview with Dieter Scholz, Director, Department of Business and Economics, IG Metall, May 1995.

Turning to the highly contentious issue of unemployment, in an effort to halt the severe reduction of the labour force, and its concomitant social problems, IG Metall presented its own job creation scheme to the THA. This included the proposal that redundant employees should be transferred to 'job firms' for retraining with the possibility of returning to their original employer once it had established itself in the new market. The THA rejected the proposal, fearing that potential buyers would be deterred from investing in businesses that appeared to be overstaffed. IG Metall vented its frustration through mass protests. In July 1991, approximately 10,000 metal workers demonstrated in Rostock and bricked up the entrance to the THA branch office, while in Suhl, Thuringia, the THA office was occupied by demonstrators. Eventually the THA capitulated and contributed DM300-400 million towards job creation schemes. In the new Länder, these were geared towards job training, retraining and the creation of work in demolition and clean-up activities. Whilst such schemes cushioned job losses, women found themselves most affected by unemployment. Unfortunately, according to Scholz, 'none of the schemes represented investments in the future, but rather ways of coping with the past.'

## Discussion

At the outset of the privatisation process, the THA was, perhaps uniquely, in a position to create its own political, social and economic environment, as well as being influenced by it. Its initial terms of reference (privatisation and renovation) were widely drawn and enabling, not binding it to a sweeping programme of economic restructuring on liberal capitalist lines. At least hypothetically, it was possible for the THA to counteract government policy through its own deliberations. Moreover, advocates of an economically balanced and socially inclusive approach to reform were given grounds for optimism by the staffing profile of the THA that included a critical mass of East German representation. What transpired in an organisational sense, however, was tantamount to a grand demonstration of the principles of oligarchy at a meta-political level. Envisaging the THA as a 'political system', (Morgan 1986), and despite its appearance of rationality and neutrality as a 'broker of deals', it is clear that the agenda of radical privatisation, promulgated by government, was implemented by senior West German THA officials with little effective challenge from Eastern colleagues. In this, it reflected the asymmetrical power relations within the society of the new Germany as a whole. Over its period of existence, decision-making machinery became increasingly centralised as bureaucratic tendencies intensified and 'relevant' know-how was monopolised within upper echelons. East Germans (and women) within the agency were confronted with a 'glass ceiling', whilst potential dissident groups were infused with a culture of complicity or consent, arising from the internalisation by East German groups of the criticism of their own system and from the need to ensure the survival of the regional economy. Such

ideological 'hegemony' was reinforced through employment policies, and notably the incentive pay scheme. This method of payment not only bolstered the status of senior (Western) managers, but also effectively made the agenda of rapid privatisation a condition of employment. In retrospect, the THA can be seen as representing a classical example of how the apparent pursuit of rationality can constitute a mode of domination (Morgan 1986). The economic logic of the West German view of the world superseded East German interests and legitimate concerns. Perhaps the lasting, and contradictory, image of the THA is that of a bureaucratic organisational entity which came close to achieving its specified targets, but which left an economic wasteland in its own domain.

As well as being instrumental in forming the economic hiatus that has now become a prominent feature of the New German economy, we argue that the THA, through its economic deliberations, exerted a subliminal influence on cultural and social values. It is now clear that the agency's broad approach to privatisation allowed liberal market values to prevail over social considerations, attaching a relatively low priority, in particular, to the protection of employment in the former GDR and to the symbolic significance of sustaining critical GDR enterprises. Indeed, the message that seemed to emanate from the corridors of the THA was that a yardstick measuring financial value and market sustainability would be used to calibrate both individual and corporate status in the new Germany. This state of affairs created the paradox in which the 'West' German commitment to the social market, as manifested in the principles of employee participation in corporate decisions through co-determination and preservation of job tenure, was equivocal in restructuring the economy of the Eastern Länder. Reflection on the pragmatic and liberal economic activity of the THA may now cause consternation amongst advocates of the social market model, particularly in the light of evidence of the 'Easternisation' of 'West' German employment systems (Hyman 1996). The implication here is that German traditions of investment in the skills of staff, and provision of job security, may be exposed, in a more complete sense, to market 'realities'. Such developments may now demonstrate, with some poignancy, the significance of establishing a THA office in New York.

## Conclusion

Extensive media coverage on the state of the German nation in recent years points to a continuing cultural dissonance between East and West, summed up by Glaeser in terms of growing 'estrangement' and 'incomprehension' (2001: 173). We have suggested in this paper that the seeds for continuing divergence were sown in the years immediately after the fall of the Berlin Wall. Our analysis is focused on the operations and structures of the Treuhandanstalt. As a key economic actor at a crucial phase in the transformation of East Germany,

the agency was in a unique position to play a critical formative role in structuring the new German economy.

The transactions that brought the bulk of East German industry into private, mainly Western hands were not just economic in nature; they were also determined by the cultural identity and predisposition of leading actors within the THA. Decisions concerning the future of East German enterprises were taken and administered by individuals and groups who were sympathetic to a West German vision of the new economic order, and ideologically predisposed towards economic liberalism. Thus, a hierarchy of buyers came to prevail, with Western investors viewed as most desirable and East German buyers accepted only when none other could be found. This was the case even when the privatisation agents involved in negotiations were themselves East German, testifying to the power of the West German *Weltanschauung*, and the extent to which its economic logic had come to hold sway at the THA. The speed with which assets were privatised also militated against East German investors, who, lacking the capital of their Western counterparts, arguably may have needed more time to put together a viable bid.

In retrospect, various authorities have argued that the initial phase of reform was conducted inappropriately. It is argued that the State should have mediated to protect the weaker East German economic position, thus setting up more of a 'mixed economy'. This course of action would have been entirely in keeping with the West German governance system, which is informed by a deep-seated belief that businesses should evolve according to consensus, based on the combined wishes of legitimate stakeholder groups.

Relating this to the work of the THA, it may be argued that the agency should have negotiated and modified the liberal agenda imposed by government. This might have occurred if its internal organisation had been positively remoulded so that more East Germans and more women were represented at senior level. Corporate 'anthropology' is important; the dominance of one 'tribe' by the other arguably conspired to determine outcomes. A range of policies (including the incentive scheme) could have been different, less uni-dimensional and more accommodating of pluralistic tensions and diverse circumstances. Similarly, a more positive iterative spiral between organisation and environment could have been put in place from an East German perspective. Had East Germans been accorded a greater role in influencing the new environment, they would arguably have been better equipped to deal with it, and more committed to it, as opposed to being stripped of real input and thus potentially alienated, bereft and dispossessed. Given the THA's unique environmental characteristics and limited life span, perhaps some of the lessons derived from the above can be applied in the present to relieve the economic gap between East and West, at a time when the future of the 'German model' appears increasingly uncertain. The corporate governance system in Germany accords as much importance to saving

jobs as it does to satisfying shareholders. Had the principle of co-determination – a cornerstone of the German governance system – been adhered to in the early days of German unification, the continuing inequality between East and West would arguably be much reduced.

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