

## **Smithwell machine tools, incorporated: ethical dilemmas in international business**

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### **Abstract**

This case draws on a series of real-world vignettes that capture ethical dilemmas faced by international marketing people. The vignettes are used to create a narrative of Janet Leigh Smithfield's first year as the Senior Vice President of International Markets at Smithwell Machine Tools. All vignettes are disguised composites of real situations related by experienced international sales and marketing executives.

Key Words: international business ethics, business ethical reasoning, cross-cultural ethics, exporting problems, international marketing



## **JANET LEIGH SMITHFIELD**

Janet Leigh Smithfield was born in Arlington VA after her mother was evacuated by a medical flight from Kenya. Her father was a diplomatic attaché and her mother held some position in the diplomatic service but was never clear about what she did. Janet grew up believing that her mother worked for the CIA. Janet attended Virginia Polytechnic Institute where she completed her undergraduate degree in mechanical engineering. She joined Smithwell Enterprises as a mechanical engineer in the product development group. Smithwell was billion-dollar company that designed and manufactured machine tools. She was soon making calls on customers to get their input for customizing Smithwell machines to the customer's production process. She showed a strong affinity and skill for machine-tool sales. During her career with Smithwell, she worked in a variety of positions alternating between engineering and marketing/sales.

She has just achieved her career objective by being named Senior Vice President (SVP) – International Markets at Smithwell effective January 1. Her annual salary is \$219,000 and she can earn a bonus of up to 50% of her salary if she exceeds sales performance targets in her division. The company was emerging from a deep recession as seen from its stock price in Figure 2. The sales target for this year is \$477.6M. It was based upon the assumption that there would be an improvement in customer CAPEX (capital expenditure) budgets with the expected return to growth in the developed world economies. The developing world countries had shown a slight growth in demand over the same time so International was not hurt as badly as its domestic counterparts. She also needed to deliver a total contribution to overhead of \$170M. The division's five-year revenue and operating margin are shown in Table 1 (Appendix).

Her plan was to complete a five-year stint as the International Markets SVP, and position herself for becoming the CEO of Smithwell. To do this she had to show the qualities of leadership needed to accomplish stretch goals in a difficult environment. She must achieve the division sales and contribution objectives this year to have any chance of becoming CEO.

## **SMITHWELL ENTERPRISES**

Smithwell Enterprises is a fictional, publicly traded company incorporated in Delaware. Table 2 (Appendix) shows its recent profit performance and Table 3 (Appendix) shows its stock price over the same period.

Smithwell earns its revenue through five different market groups that sell mid-to high-quality machine tools to four industries. They are 1) Mining and Construction Equipment, 2) Power Generation, 3) Aviation, and 4) Cement. International Markets is the fifth group. The company markets machine tools, after-warranty service contracts, and purchase finance to manufacturing companies in each industry.

The entire product line is sold in the US and across international markets. There are significant market differences across geographic, political, currency and cultural boundaries. In some cases, the ability to do business is limited by local competition. For example, the primary customer in Europe for machine tools in the aviation industry is Airbus with its strong bias for European machine tools. The same bias can work for Smithwell as is the case with Embraer in Brazil.

## **THE YEAR**

Year Revenue Objective = \$477.6M; Operating Contribution Objective = \$170M

### **January 4th**

Janet arrived at the office early. Her first task that morning was to call John Fitzgerald, the Vice President of Sales, to get the year's revenue forecast. John told her that the revenue forecast for this year based on assumptions that nothing changed in the overall division effectiveness was \$430M. She realized she and the division had work to do to reach the \$477.6M revenue objective. She looked at her marketing plan, and she was confident that as long as she did not lose a large revenue project in a way not foreseen in the plan the revenue and contribution targets would be achieved with at least \$30M revenue and \$10.5M in overhead contribution to spare. If the division revenue and overhead contribution dropped by more \$30M and \$10.5M respectively, she could see no way that the division could make up the loss before the end of the year.

At 11:30, the CEO gave her a call. The informal organization grapevine had found an on-line video of Jeremiah Mountain that was getting thousands of hits. He was one of the division's most effective PAC-rim sales people. The CEO wanted to know what had happened and what she was going to do about it. Mountain handled the Power Generation products for all of Asia except Japan, Philippines and Australia. He was divorced last year, and was given custody and sole support for his three kids when his wife moved to Europe.

Janet asked her secretary what the rumor was. A video that showed Jeremiah in a compromising situation with an oriental woman in a hotel room had been posted online. She called Jeremiah and found him depressed and ready to resign. The woman had knocked on his hotel room and said a Smithwell client had sent her. He did not know that she was planning on taping the evening, and then blackmailing him for details of an upcoming business negotiation. He had refused to pass information on to the man who delivered the threat. This was not the way Janet had planned on starting her first day.

She did some checking and found that Jeremiah generated \$40M in sales in high margin contracts yielding \$16M in contribution to overhead. Fitzgerald, the VP of Sales, said if Jeremiah left, he would take at least 75% of the business with him, and that it would take several years to replace it. To make matters worse, the project related to the blackmail was a new \$20M contract with a \$10M overhead contribution. This project would also be lost because the client did send the woman, but they did not know she was also working for a Smithwell competitor. Janet wondered what she should do because Jeremiah's behavior did violate Smithwell policies.

### **February 2**

Her January revenue results arrived on her desk. As she looked through the report, she noticed that the distributor in Argentina who covered the mining and construction industry for Smithwell was earning a commission of almost 13% while almost the other Smithwell distributors were earning 3%. She called John Fitzgerald once more and asked him the reason for the discrepancy. There was a pause on the other end of the phone, and he said the Argentine distributor had "special expenses." She asked what expenses, and he said he never asked. What he did ask was what would happen to revenue if they paid only 3%. The distributor said revenue would drop by 80% without the extra commission to cover the extra expenses. The VP suggested that Janet think about it.

The only possible reason why the distributor needed 10% additional expense reimbursement was to cover bribes paid to customers and government officials to purchase

Smithwell products. However, no one in the company actually “knew” this. The Argentine distributor was responsible for \$120M in sales with an overhead contribution of \$46.8M. Now what does she do?

### **April 1**

Daneshwar Agarwal, the Smithwell salesperson who covered the Indian sub-continent, had received a call from their customs broker in Sri Lanka. The customs officials at the port of Unawatuna had blocked the shipment to the Tata Power Equipment factory. They claimed there were termites in the crates used to protect the machines during shipping. She knew this could not be true because all crates were fumigated and certified pest-free. The certification is attached as part of the shipping documentation with Export Declaration, necessary US Export Licenses, and the Pro Forma Invoice on all Smithwell shipments. The customs officials required a US\$15,000 payment wired to a Swiss account to pay for fumigation and legal costs. The machine cost \$35M, and Daneshwar wanted her permission to pay the fine. He was going to lose a \$180,000 commission if the shipment was not released within 3 days because the letter of credit would expire. If it did, then Smithwell would have to renegotiate the deal while their machine waited in storage. Returning the machine would cost over \$200,000. She was wondering how she could handle this without feeling like an April fool.

### **June 14**

Janet thought she had seen it all, and then she gets an emergency call about William Smith. Smith was in a restaurant in the Basque region of Spain when all of the patrons turned over the tables and fell on the floor. He was having lunch with a man named Sergei Petrovich. Three men, suspected Basque separatists, entered the restaurant and shot up the walls above the patrons. The patrons and staff started to pick up the tables and resumed eating when someone realized that Sergei had been shot and killed. Luckily, Smith was safe.

The police were called, and they were not happy. Apparently, they have an agreement with the separatists that they could shoot up a restaurant once in a while as long as they made sure no one got hurt. They pulled some bullets from the wall, and found they were a different caliber from the bullet that killed Sergei. They concluded that Smith had killed him. His sales territory is Milan, and Sergei turned out to be a suspected Serbian terrorist. The police decided Smith must have been operating as a spy for the US government. He was being held on a \$500K bond.

As she was wondering where she could find \$500K in her budget, she gets a call from Abel Distributors in Paris. They want to pay the fine because Smith has been invaluable in helping them close several deals in Milan and they do not want to lose his services. Janet was really confused now, so she called her mother. Her mother says she did not know anything about it, but she heard rumors that US Intelligence may have used civilian operatives who often worked as machine-tool salespeople. Her mother thought it was because machine-tool salespeople travelled internationally, had real companies as employers, and were well connected to people of interest to the government. The government would not want to lose such an operative. Given all this, Smith had a \$50M book of business on target for 2010 with a contribution of \$19.5M. She called the legal department. As she waited for them to return her call, she was not sure how to proceed.

## September 9

John Fitzgerald, Sales VP, kicked an order for 3 machines that drilled precise holes through long steel tubes onto Janet's desk. He asked her for a decision about the order. The machines could be used to bore the barrels for small artillery pieces. The customer was an importer in Angola who was known to re-export products to the militia in Zimbabwe. It was likely that the machines would be used to manufacture guns that could be used to kill Zimbabwe citizens without witnesses since the shells could be fired from a long distance. This would allow the government to deny responsibility. The three machines would sell for \$21M total and the payment would be made this year. 80% of the manufacturing costs would not be incurred until next year. This means the current operating contribution would be \$15.1M. The current-year sales trajectory was falling behind target, and the extra revenue and operating contribution would close the gap and provide a little cushion. Again, she had a decision to make, and she wondered what to do.

## DIRECTIONS

For purposes of this case, assume that you are in the last quarter of the year. Analyze what you think Ms. Smithfield should have done in her new position as Senior Vice President – International Markets to handle each of the situations outlined above. There are legal, procedural, marketing, management and ethical issues involved in this case. For some vignettes, additional research will help support the analysis of the vignette.

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**APPENDIX:****Table 1 - Five-Year Revenue and Operating Contribution for the International Division (in US\$ Millions)**

	This Year	+1 Year	+2 Years	+3 Years	+4 Years
Revenue Objective	442.3	425.8	390.6	342.1	243.2
Operating Contribution Objective	139.3	140.5	132.8	111.2	75.4

**Table 2 – Smithwell – Last Five-Years Consolidated Revenue and Operating Expenses**

	Smithwell Income				
	Year 1	Year 2	Year 3	Year 4	Year 5
Total Revenue	1,778	2,018	1,869	1,669	1,215
Cost of Revenue	1,228	1,380	1,249	1,120	836
Selling/Gen/Admin Expense	356	349	328	314	256
Interest Expense	28	25	26	39	30
Unusual Expense	262	-	-	-	-
Other Operating Expense	42	29	(2)	(4)	(3)
Net Income	(138)	235	268	200	96

*\*Numbers in US\$ Millions*

**Table 3 – Previous Four-Year Stock Prices for Smithwell Enterprises**

	<u>Yr -4</u>	<u>Yr -3</u>	<u>Yr -2</u>	<u>Yr -1</u>
January	33	40	29	22
May	36	43	57	28
September	30	41	24	32