Running Head: ETHICS OF WITHHOLDING INFORMATION

"In an environment where over 50% of income is earned by commission, is it ethical for a salesperson selling technology to be used in a manufacturing environment, to withhold information that new technology will be available in less than three months which make the equipment financially obsolete and will therefore significantly negatively impact the buyer's ROI of the proposed purchase, so that he can make a sale and receive his commission?"

Jeffrey J. Bowe

Anderson University

December 10, 2008

The payment of sales commissions has been a source for comedic routine and of buyer angst since the first commission was paid. The discussion of commission is important to marketing because one of marketing's primary purposes is to help a company sell its offerings, and commissioned salespeople are a significant cog in that process. Unlike salary or hourly wages where there is no direct relationship between activity and financial impact to the company, commission directly rewards the contribution of the employee to the employing (or principal) entity.[1] In theory, commission is straight-forward pay for performance. In reality, commission may prompt sales concept mentality which creates the issue of focus of this paper.

In selling equipment used manufacturing, the seller often provides data on capabilities of equipment to help justify purchase, including data on cost and potential revenue available over time through the use of new equipment. Some replacement equipment renders existing equipment financially obsolete, defined as an inability to produce and sell at a profit. It is common for salespeople to have knowledge of replacement offerings before they are announced to the public, and may be identified as confidential and not for distribution. However, this awareness becomes part of the salesperson's knowledge from which he will base ethical decisions. Borrowing a term from the financial markets, we will say this inside knowledge creates "imperfect information" between the seller and buyer.

A major role of marketing is to understand the needs of prospective buyers and feed this information back to R&D so that new variations or generations of offerings can be developed. This practice reflects a market orientation on the part of the company. "Market orientation (MO) refers to the organizationwide generation, dissemination, and responsiveness to market intelligence (Kohli & Jaworksi, 1990)." A market-driven organization is one which has a

[1] For this paper, non-employee sales agents are treated as sales employees.

"superior ability to understand, attract, and keep valuable customers (Day, 1999, p.5)." It is this information exchange to understand customer needs that creates an ethical issue for technology salespeople who become aware of upcoming products before they are announced to the public.

In other words, during the sales process, did the salesperson make untrue comments about the capabilities over time of the equipment being considered? This would be a clear ethical violation. More germane to this paper, did the salesperson fail to disclose information about a soon to be available alternative—an example of imperfect information? This is a "sin by omission" where information was available that was not provided to the buyer.

Roman and Ruiz (2005) state "unethical sales behavior is defined as a short-run salespersons' conduct that enables them to gain at the expense of the customer" (p.440). Salespeople are often compensated for their success when in the same transaction the buyer ends up with a purchase that does not provide their anticipated financial return on investment (ROI). In situations where this is due to inaccurate analysis or forecasting on the part of the buyer, the buyer is responsible for the non-achieved ROI. We are looking here at the situation where the buyer does not achieve his anticipated ROI due to imperfect information.

The last scenario is very possible in manufacturing environments and foreshadows the question of whether commission compensation encourages unethical behavior by the salesperson when the non-disclosed information will negatively impact the ROI calculations of the buyer. Specifically, we are focused on technology offerings for a manufacturing environment which have a financial life span less than five years, where financial lifespan is defined as the timeframe during which the equipment can make a contribution to profit. Further, we are concerned with equipment which the purchaser plans to use to offer new products to generate new sales revenue to generate an acceptable ROI. These criteria exacerbate the impact of the imperfect information imbalance in the transaction—if the buyer knew as much about soon to be released alternatives as the seller, he might make a different purchase decision.

MO is the antithesis of the sales concept which is generally, "I need to convince people to buy from me what I have today." This antithesis is observed in commission compensation which puts the salesperson in the position where, to get paid, he must practice the sales concept today even if his MO is about to introduce improved equipment. Therefore, a stressor in the ethical decision process is compensation structure as a potential motivator for unethical behavior.

Common thought assumes a salesperson who is compensated primarily by salary is more willing to invest time in longer term prospects because low current sales will have less impact on their current income. Conversely, a person who receives a higher percent of income by completing sales is financially motivated to push harder for completed sales. "The straight-commission compensation system (SCCS) is an example of an outcome-based contract because it directly rewards the agent [salesperson] for performance, i.e., it rewards a measureable outcome of the agent's effort" (Kurland, 1996, p.54). The implication in high or straight commission is that the failure to make a sale today means the employer received no economic value from the time and effort spent by the salesperson with the prospect who did not buy today. For this paper, we focus on compensation plans where the majority (over 50%) of anticipated income of the salesperson is received from commissions, so that there is high financial motivation to achieve sales.

The last element of the developing ethical question is the timing of availability of replacement equipment. When making a decision involving an investment, assumptions are made regarding the size and duration of any. Manufacturing technology sales present a challenge because the buyer knows that replacement technology will be faster and less expensive, but does not know when it will be available as he calculates his ROI. As an example of an ethical conflict, the buyer may reasonably project that the first 40 months will be profitable, followed by ten months of zero profit, and then ten months of loss, and that this combination provides an acceptable ROI. However, if the salesperson knows that a new technology will be released in three months which will make the equation ten months of profitability, twenty months of zero profit, and twenty months of a loss, then the salesperson has an ethical conflict in whether to provide complete information that will change the buyer's ROI calculations.

Truthfulness in selling has been an issue as long as there have been merchants and traders. Milton Friedman said, "There is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits as long as it stays with the rules of the game, which is to say, engages in free and open competition without deception or fraud" (Bowie, 2005, p.22). "It goes without saying that his sales claims should be honest and that he [the businessman] should not corrupt the integrity of his sales employees by asking them to make false or misleading representations to customers (Bowen, 1953, p.214)." But what about a lack of disclosure? Bowie admits, "The seller usually has information the buyer does not know and could not reasonably be expected to know (p. 62)." It is not misleading to say, "This is the best option available today." Is not adding, "But there is a better option that will be available in three months" an ethical failure by omission? Does this imply that *caveat emptor* is supreme?

This is the conflict between market orientation in theory—with R&D and marketing collaborating on new products—and the sales concept in practice—with salespeople who need to sell today to receive personal income. But, recalling Plato and Aristotle, "What is a good X" must be answered with "What is the purpose of an X" which gets to conflict of MO and commission. (Bowie, 2005) A good sales person is one who sells, and perhaps the process is inappropriate but the result is right.

Should ethics say that it is not acceptable to mislead by omission in order to achieve that goal? "Too often salespeople and the incentive structures in the companies that support them are geared to maximizing the value of a sale [today] (Bowie, 2005, p. 64). "We maintain that it is the obligation of a sales manager to create an incentive system for salespeople in the organization to meet the needs of the consumer with an eye to repeat business. An ethical manager makes a profit by meeting consumer needs. An unethical manager makes a profit by exploiting information asymmetry (Bowie, p.64-65)." The concern is how information is provided or withheld. If the manufacturer provides data on for calculating an ROI, and the soon to be introduced replacement equipment will render the considered equipment financially obsolete during the ROI time contemplated, then the information provided is correct but incomplete.

The research on the impact of commission on ethical behavior is inconclusive. Some find support for the hypothesis that a higher ratio of commission to non-performance based compensation is associated with more unethical behavior (Kurland, 1995; Hoffman, Howe, & Hardigree, 1991; Honeycutt, Glassman, Zugelder, & Karande, 2001; Ross & Roberston, 2003) while other research did not find support for this hypothesis (Cupach & Carson, 2002; Schwepker, 2003). While ethics are universal, for this paper the scope of this question is narrower. ***"In an environment where over 50% of income is earned by commission, is it ethical for a salesperson selling technology to be used in a manufacturing environment, to withhold information that new technology will be available in less than three months which make the equipment financially obsolete and will therefore significantly negatively impact the buyer's ROI of the proposed purchase, so that he can make a sale and receive his commission?"***

Batory, S.S., Neese, W., & Batory, A. H. (2005, March). Ethical marketing practices: An investigation of antecedents, innovativeness, and business performance. *The Journal of American Academy of Business, Cambridge, 2,* 135-142.

Bowen, H. R. (1953). *Social responsibilities of the businessman.* New York: Harper Brothers.

Bowie, N. E. (2005). *Management ethics.* Malden, MA: Blackwell Publishing Ltd.

Brentano, F. C. (1973). *The foundation and construction of ethics.* New York: Humanities Press. Trans by Elizabeth Hughes Schneewind.

Cupach, W.R. & Carson, J. M. (2002). The influence of compensation on product recommendations made by insurance agents. *Journal of Business Ethics, 40,* 167-176.

Day, G. S. (1999). *The market driven organization.* New York: The Free Press.

Hoffman, K. D., Howe, V., & Hardigree, D. W. (1991, Fall). Ethical dilemmas faced in the selling of complex services: Significant others and competitive pressures. *Journal of Personal Selling and Sales Management, 11*(4), 13-25.

Holley, D. M. (1998). Information disclosure in sales. *Journal of Business Ethics 17*, 631-41.

Honeycutt, E. D., Glassman, M., Zugelder, M. T. & Karande, K. (2001). Determinants of ethical behavior: A study of autosalespeople. *Journal of Business Ethics, 32,* 69-79.

Jackall, R. (1988). *Moral mazes: The world of corporate managers.* New York: Oxford University Press.

Kohli, K. & Jaworski, B. J. (1990, April). Market orientation: The construct, research propositions, and managerial implications. *Journal of Marketing, (54),* 1-18.

Kotler, P. (1984). *Marketing management: Analysis, planning, and control.* Englewood Cliffs, NJ: Prentice-Hall, Inc.

Kotler, P. (1999). *Kotler on marketing.* New York: The Free Press.

Kurland, N. B. (1995, April). The unexplored territory linking rewards and ethical behavior. *Business & Society, 34*(1), 34-50.

Kurland, N. B. (1996, January). Sales agents and clients: Ethics, incentives, and a modified theory of planned behavior. *Human Relations, 49*(1), 51-74.

Luo, X. & Bhattacharya, C.B. (2006, October). Corporate social responsibility, customer satisfaction, and market value. *Journal of Marketing, 70,* 1-18.

McClaren, N. & Shaw, R. (2002). Research methods in sales ethics: A review of the empirical literature. Conference report to 2002 Australian and New Zealand Marketing Academy Conference. (pp. 602-609). Melbourne, Australia.

Philips, M. (1993) *How to think systematically about business ethics.* In "Applied Ethics: A Reader." Winkler, E. R. & Coombs, J. R. (eds) 1993. Cambridge, MA: Blackwell Publishers. (pp.185-200)

Roman, S. & Munuera, J. L. (2005). Determinants and consequences of ethical behavior: an empirical study of salespeople. *European Journal of Marketing, 39*(5/6), 473-495.

Roman, S. & Ruiz, S. (2005). Relationship outcomes of perceived ethical sales behaviors: the customer's perspective. *Journal of Business Research, 58,* 439-445.

Ross, W. T. & Robertson, D.C. (2003). A typology of situational factors: Impact on salesperson decision-making about ethical issues. *Journal of Business Ethics, 46,* 213-234.

Schwepker, C. H (2003). An exploratory investigation of the relationship between ethical conflict and salesperson performance. *Journal of Business and Industrial Marketing, 18*(4/5), 435-446.