
Memorandum

To: Theodore Solso CEO, Cummins
From:
Date: 15 October 2003
Re: Revising Cummins Code of Business Conduct.

I worked in the Fleetguard Division of Cummins Inc, as a finance intern in Summer 2003. As part of my summer project, I was in charge of the division's compliance with Sarbanes Oxley Act. This project gave me the opportunity to review many of Cummins' existing internal policies on business conduct in detail, perform self-assessment surveys to senior management across the departments, and visit some of the plants. I am writing this memorandum to outline my suggestions for the revision of Cummins Code of Business Conduct, based on my observations in the summer and my analysis of the current code of conduct.

Cummins Inc., a manufacturer of diesel engines, generators and filtration products, has operations all over the globe. It sells its products to original equipment manufacturers (OEMs), distributors and other customers worldwide. The company has long-standing relationships with manufacturers in the markets it serves, including DaimlerChrysler, Volvo and General Electric. The high standards of business conduct set in these industries that Cummins serve, the strict requirements of certifications for supplier quality and request for the environmental and social responsibility necessitate Cummins to have a high-standard code of conduct that is frequently reviewed and revised.

What is Cummins currently doing to achieve high standards of ethical business conduct?

Senior management at Cummins Inc has always been committed to the ethical business practices, supporting local communities and taking into consideration all the stakeholders that are affected by the company's actions in the decision making process. The company is renowned for its social responsibility, but with the changing global demands and the increasing size of the company, it is getting more challenging to meet the goals of ethical business conduct. For this purpose, the company had initiated a formal training program on ethics and management in early 1990's to continuously improve on its ethical business conduct. ¹

Currently, the company publishes an annual sustainability report that outlines the company vision and mission, governance structure and management systems, commitment to stakeholders, economic, environmental and social performance indicators, and diversity.

Furthermore, the company is working for the development and commercialization of fuel cell technology to significantly lower fuel consumption and exhaust emission than

¹ Training on Ethics: Cummins Engine Company. The Journal of Management Development, 1992. Vol. 11, Issue 4.

existing systems. This project has utmost importance not only for the company, but also for paving the way for a sustainable future for tomorrow's generations.

What are Cummins' competitors doing?

Before developing some of my recommendations, I conducted an extensive benchmarking study with our main competitors. Cummins defines itself as a global leader in power and manufacturing, therefore I expect Cummins to set a goal of being ahead of all its competitors in terms of ethical business conduct.

Caterpillar:

Caterpillar regards its reputation for integrity as a fundamental part of its heritage and one of its most valuable assets. Caterpillar has outlined on its website highlights of how it is contributing to sustainable progress in environmental, social and economic areas. In addition, Caterpillar has an admirable "Making a difference" booklet, a guide to Caterpillar employees worldwide to understand the part they play in making Caterpillar a responsible corporate citizen. Another report available in Caterpillar's website was the Caterpillar Foundation Annual Report, that outlined the distribution of funds for philanthropic organizations and activities, but this report is addressed in the social responsibility section of the sustainability report in Cummins. I believe these reports would be valuable additions that Cummins should consider to increase transparency and improve the flow of information to all stakeholders about Cummins business practices.

Furthermore, the company has published a detailed Code of Worldwide Business Conduct to serve as guidance for Caterpillar employees in making sound, ethical decisions. The code of conduct is very similar to Cummins Code of Conduct, except for its detailed language addressing environmental issues, worldwide business practices and dealer/distributor relationships. You can find my recommended revisions to the Cummins Code of Conduct based on the superior characteristics of Caterpillar Business Conduct.

John Deere:

On its corporate website, John Deere has published environmental and safety metrics that it uses to evaluate its annual progress towards achieving environmental goals as well as giving examples from environmental and community projects. In addition, John Deere publishes a Deere & Company Environment, Health and Safety Annual Review. John Deere has both a report on Business Conduct Guidelines and a separate Code of Ethics. The Business Conduct Guidelines covers the same issues and principles addressed by Cummins, but the section on environment and safety is much more comprehensive in John Deere's report. The website also summarizes corporate governance principles that Cummins has not reported as much in detail.

A unique feature in the John Deere's report was the assist-line and PO Box addresses set up to report violations of business ethics. I strongly recommend Cummins to follow this example in the future, as outlined in my recommendations section.

Ingersoll Rand:

Ingersoll Rand website features a code of conduct, environmental policy principles and corporate governance principles. In general, Cummins Code of Conduct is much more comprehensive compared to Ingersoll Rand's. The only section that is addressed more in detail, as in the case of our other competitors, is the section outlining principles for international business.

Unfortunately, Ingersoll Rand doesn't have an environmental policy on its website, but there is a notice saying that it will be developed soon. Although Cummins code of conduct and sustainability report are far ahead compared to Ingersoll Rand, the framework in which Ingersoll Rand provides corporate governance principals (as in John Deere's case) could set a successful example for Cummins. I strongly encourage Cummins General Counsel to review the detailed description of board and committee selections that was made publicly available in contrast to other competitors and Cummins.

The Current Cummins Code of Business Conduct

The Current Cummins Code of Business Conduct covers the following topics:

- Conduct Regarding our Customers, Suppliers and Competitors
- Conduct Regarding Conflicts of Interest
- Conduct Regarding Our Employees
- Conduct Regarding Our Communities
- Conduct Regarding Our Shareholders
- Conduct Regarding Our Property
- Conduct Regarding Political Campaigns and the Media
- Conduct of Leaders

Areas of Improvement in Code of Conduct

- In my opinion, looking at this list, Cummins Engine has not addressed a very important topic: Environment. One of the five mission statements of Cummins states that "Demanding that everything we do leads to a cleaner, healthier, safer environment". But this issue should have been emphasized much more in the code of business conduct. I suggest the inclusion of sentences that reflect Cummins commitment to this issue. An example can be:

The company is committed to developing superior products that continually meet or exceed emissions and noise regulations while improving fuel economy.

This statement is supported by the past performance of Cummins and its sensitivity to environmental issues. In 1998, a group of manufacturers of heavy-duty diesel engines signed a consent decree with the Environmental Protection Agency (EPA) and Department of Justice, committing to meet a 2.5-gram Nox+NMHC standard by October

2002. In 2002, Cummins became the first engine manufacturer to be certified as meeting the US Environmental Protection Agency's tightened diesel emission standards. Through its new emissions solutions business, Cummins filtrations work to help customers meet increasingly stringent emissions standards worldwide. Starting in early 1990s, Cummins has focused on research and engineering technology to ensure cooled-EGR direction to be implemented in the US heavyduty truck market by 2007. Cummins' pioneer product development effort is aimed at increasing the emission standards in the heavyduty truck industry.

- The competitors of Cummins clearly state the critical role played by dealers and distributors between the company and the customers worldwide. Cummins has an international distributor network of 17 company-owned and two joint-venture retail distributors, plus 111 sales and service locations in 50 countries and territories outside the US. However, Cummins doesn't address in its code of conduct how the international distributor business is responsible toward the parent company. It should clearly state in its code of conduct that:

The distributors are subject to the same environmental and social standards followed by the parent company. Each distributor must comply with the Cummins Code of Business Conduct and the supporting policies and procedures as outlined in the company's internal website.

- In the benchmarking section of this report, I demonstrated that Cummins competitors specifically address their global business practices. Although Cummins operate in more than 131 countries, currently, there is no mention of the countries that Cummins conduct business. A paragraph on global responsibilities should be added to section on the Conduct Regarding Our Communities as outlined below:

Cummins is committed to exercising global citizenship. The company will strive to meet all regulatory requirements or exceeding them for the health and safety of workers and consumers. The company will aim to contribute to the well being and social development of countries that it conducts business in.

Cummins is already an active participant in responsible global citizenship. It frequently shares its expertise and advanced environmental, noise and emission control technologies worldwide. For example, Cummins' clean energy engines are setting used in meeting international emission standards worldwide. Answering the Chinese government's call for cleaner vehicles due to increased air pollution, Cummins Corporation offered up its compressed natural gas (CNG) engines to green Beijing's massive fleet of public buses. Beijing has already purchased 2,000 Cummins CNG-powered buses and now has one of the world's largest natural-gas bus fleets.² These buses exceed the Euro Emissions Standards that China plans to meet after 2004. Similarly, in early 1990's, Cummins supported the Taiwanese government's adoption of stringent emission standards for heavy duty-engines by sharing information from its facilities, providing reference engines and expert personnel. However, by including its commitment to global citizenship in its code of business conduct, Cummins will reaffirm its values that are already in practice.

² Making Green in Beijing. Timothy Hindebrandt. The China Business Review. Nov/Dec 2003.

- As John Deere is currently doing, the company should set up an assist-line and a PO Box address to direct employees who are in doubt of their actions. Currently, the code of conduct directs the employees who are in doubt about their course of action to contact Cummins General Counsel. However, I believe that the assist-line and the PO Box would provide an alternative means for confidential reporting of possible unethical or improper actions .After setting up the assist-line and the PO Box Address, the Code of Conduct should be amended to include instructions for employees on these.
- Currently, the section on Media outlines the code of conduct for dealing with media. I suggest that the company adds a paragraph on the integrity of advertisement published in the media. Cummins' major competitor, Caterpillar Inc, addresses maintaining high standards of integrity in media in its code of Worldwide Business Conduct and Operating Principles. Cummins should add the following paragraph:

In our advertising and other public communications, we will avoid not only untruths, but also exaggeration and overstatement.

- With the implementation of the proposed changes in the Code of Conduct, I am confident that Cummins will achieve a higher standard of excellence. The additions to the Code of Conduct are already ethical principals that Cummins adhere to. However, by including them in the Code of Conduct, the company will emphasize once more its commitment to these values and guide its employers in making ethical decisions.

Thank you for giving me this opportunity to share my observations and recommendations on Cummins Code of Conduct. Please feel free to contact me for further questions and clarifications.