

Case 1

PACIFIC OIL COMPANY*



NEGOTIATION 7e
LEWICKI • BARRY • SAUNDERS

Objectives

- To understand the multiple causes of a negotiation failure
- To reinforce the importance of planning, goal setting, and preparation for negotiation;
- To reinforce the importance of developing a strategy, and the liabilities of being on the defensive, responsive to the opponent's strategy;
- To demonstrate the important role played by time and deadlines in negotiation;
- Show how negotiators are liable to "entrapment" in negotiations, and demonstrate ways to understand and prevent these dynamics.

Changes from 6th Edition:

None.

This case was originally written in 1983, and still contains financial information from the first writing. The editors of this volume have been unable to secure permission to revise and update the financial information, or to find a comparable case that is more contemporary. However, we believe the teaching points in the case continue to justify its use with the original financial information. We therefore encourage the instructor to be very public with the students about the age of the case, but also assure them that the learning objectives have not been compromised by the age of the case.

RECOMMENDED READING ASSIGNMENTS TO ACCOMPANY THIS EXERCISE:

For a greater understanding of the nature of the 'contract' that is part of this case, you may wish to assign Petrochemical Supply Contracts: A Technical Note (printed as an Appendix to this case before reading the case, or cross-referencing it as they read the case.

Reader:

- 1.4 The Negotiation Checklist
- 1.5 Effective Negotiating Techniques
- 1.6 Closing your Business Negotiations
- 2.1 Negotiating Rationally
- 2.2. Managers and their Not So Rational Decisions
- 2.6 Staying With No

Text: Chapters 2, 4

Essentials: Chapters 2, 4

* Teaching Note prepared by Roy J Lewicki.

Operational Needs

Group Size Any size. Small groups may discuss the case before a general class discussion.

Time Required Allow at least 60 minutes to discuss the case. Add 30 minutes if you also conduct the Dollar Auction as part of the case discussion/debrief.

Special Materials None. The B case (at the end of this Note) should be reproduced or read to the students after the A case is discussed.

Physical Requirements No special requirements.

Advance Preparation

Decide whether you wish to have the students read the “Technical Note” before reading the case, or reference it while reading the case.

Copy the B case for distribution, or have it available to read to students.

Decide whether you want to conduct the Dollar Auction in conjunction with the case. If so, be prepared to explain the rules to the students, and have dollar bills and small change available to make change with students after each auction.

Discussion Questions to be assigned for the A Case:

1. Identify the strengths and weaknesses of Fontaine's and Gaudin's negotiating strategy in their deliberations with Reliant Chemical Company.
2. Identify the strengths and weaknesses of Hauptman's and Zinnser's negotiating strategy.
3. What action should Fontaine take at the end of the case?

Operating Procedures

Pacific Oil Company, like many major oil companies, produces fuel and diesel oil, gasoline, and a variety of industrial chemicals. One of its major industrial chemical lines is Vinyl Chloride Monomer—VCM—primarily used for the manufacture of polyvinyl chloride plastics. Pacific Oil had a number of VCM customers in its European market, one of whom was Reliant Corporation, which manufactured plastic pipe and pipe fittings for residential and industrial plumbing. Pacific had negotiated a sales agreement with Reliant that had been renewed. During the term of the contract and because of changing market conditions, Pacific decided to try to get the contract extended beyond its current expiration date.

The case describes the actions of two negotiators for Pacific—Fontaine and Gaudin—and their efforts to get Reliant's cooperation in a contract extension. Reliant's negotiators primarily use the tactics of delay, limited authority, "nibbling" and tough negotiating to undermine Pacific and

minimize their effectiveness. As the case ends, Fontaine is being pressed to give "one last concession" to assure the Reliant deal, while a staff advisor is trying to talk him out of it.

Case Analysis

In 1968, Pacific Oil Company had established a four-year agreement with Reliant Chemical to sell VCM. In October 1972, this agreement was successfully renegotiated to extend to December, 1977. However, by December of 1974, Pacific was deeply concerned about the status of the contract, for the following reasons:

1. The market for VCM had been in a significant "shortage" situation for years. However, a number of new chemical plants were being built, and between the added capacity to produce VCM and a drop in demand, it was clear that the market would be oversupplied in a few years.
2. A few large customers that bought huge amounts of VCM dominated the market. It was therefore important to keep contracts with these customers, because if a company lost one, it would be almost impossible to make up the business with new customers.
3. Corporate headquarters of Pacific Oil was talking about setting up a new company division to produce its own line of PVC products. If Pacific entered the PVC market, it would buy its own VCM chemical stock and not have to be as dependent on external sales.

As a result, Fontaine and Gaudin decided to try to get an extension of their contract with Reliant past the 1977 expiration date, while at the same time trying to determine whether Pacific was going to get into the PVC business on its own. The case describes the deliberations between Fontaine and Gaudin and Reliant's two major negotiators, Zinnser and Hauptmann. Fontaine and Gaudin approach the negotiation process, ineffectively, in the following ways.

1. Failure to Plan for Negotiations

Fontaine and Gaudin did no systematic planning; other than to be motivated to "get Reliant to resign the agreement." As a result of the vagueness of this objective, the two are so eager for a contract extension that they make a number of needless concessions in an effort to assure some kind of deal. No goals were defined for the new contract, and no "bottom line" was ever set to determine what would be a minimally acceptable agreement.

2. Failure to Understand the Role of Deadlines

Fontaine and Gaudin were aware of several things when they reopened negotiations with Reliant in early 1975:

- The current contract had three years to run;
- Reliant had no reason to want to extend the contract at this time;

- Reliant probably knew that the market was going soft (hence it would be in Reliant's best interest to wait until the contract almost ran out, and then approach a number of suppliers to get the best possible deal).

Yet Fontaine and Gaudin did not create any incentives for Reliant to want to resign before the expiration. As a result, they left themselves wide open to delaying and "nibbling" tactics by Reliant—tactics Hauptmann and Zinnser used. Reliant strung the negotiations out. They only discussed one issue at a time, while making Fontaine believe that this was "the last issue to be settled" before signing. Finally, Hauptmann and Zinnser introduced "dummy issues" to stall the negotiations. One example of this was the pipeline-metering problem—a question that would not normally be dealt with in negotiations but through independent inspection and monitoring.

3. Differences in Negotiating Style

Fontaine and Gaudin are often described as naive, clumsy and careless as negotiators. Their styles may also be contrasted against the calculating, tactical, precise "German" style evidenced by Hauptmann and Zinnser. (While executives and some students will be aware of cultural differences and their impact on negotiating style, be careful about generalizations and "stereotypes" that you, the instructor, use in class.)

4. Failure to Define a Strategy

By failing to set objectives, set deadlines, and understand how to achieve their objectives in the time period, Fontaine and Gaudin did not define a clear strategy. They had no "plan" for knowing how to proceed. Moreover, by not having a strategy, they were forced to play by the strategy defined by Hauptmann and Zinnser—one of delay and "nibbling." When opponents use delay and "nibbling" tactics, negotiators must be able to:

- Define a deadline for the negotiations. If the deadline is not identical with the other's deadline, then negotiators must invent ways to attract the opponent toward a quick resolution.
- Define a bottom line, or a minimally acceptable deal. Negotiators must know what is the least satisfactory contract they will sign.
- Aggressively seek out options (other new customers or even closing the plant).
- Protect themselves from "nibbling" by not allowing any new issues to be opened up unless the opponent is also willing to discuss issues previously settled. Contracts must be viewed as an acceptable package; if the opponent wants to discuss a new issue after everything is settled, the entire contract should be put on the table for renegotiation.

5. Failure to Manage and Deal with One's Own Constituency

Fontaine and Gaudin have several major problems with their own organization that affect their negotiations:

- a. The lines of responsibility for senior management regarding this problem are muddy and unclear. It isn't clear whether Meredith or Saunders should be monitoring this negotiation,

but one or the other clearly should have intervened to "stem the damage" and stop the constant concessions being made. Kelsey (a staff person) finally takes the most active role in trying to persuade Fontaine not to give any more away. The matrix organization of Pacific makes this problem even more serious.

- b. Pacific undermines its own negotiators and their use of a key bargaining point by deciding midway through negotiations not to go into the PVC market themselves. In addition, they publish it in the newspaper, thereby announcing to the world that Pacific will not be a major consumer of VCM. This weakens Fontaine and Gaudin's ability to tell Reliant that *"You better sign up now before we decide not to sell it to you."*

6. Entrapment

By virtue of the strategy they use (or, more precisely, don't use), Fontaine and Gaudin unwittingly make themselves susceptible to entrapment. Entrapment has typically been described in terms of waiting lines, or stock market investments, or "bad loan psychology" in banks. The instructor can learn more about entrapment by referring to the articles on decision biases (2.1, 2.2 and 2.3), and by referring to the other references listed at the end of this section. A set of "lecture notes" on entrapment is also included in these case notes.

Teaching Strategy

For students who have no knowledge of contracts and contract negotiations in the petrochemical industry, they should first read "Petrochemical Supply Contracts: A Technical Note" (in the text). Then read the case, and prepare the discussion questions.

(20-30 minutes) Review the major events in the case. The following discussion questions and strategies may be used:

1. What was Pacific Oil's problem in late 1974?
2. How effectively did Fontaine and Gaudin approach the negotiation?
3. How effectively did Hauptmann and Zinnser approach the negotiation?
4. What were the events that transpired, beginning in January of 1975? (It is extremely helpful to draw a "time line" on the blackboard and summarize the events so that students can see the progress to the current state).
5. How did Fontaine and Gaudin "get themselves into this situation"?

(20 minutes) It is common for students to be very critical of Fontaine and Gaudin by this point. One teaching strategy that adds a lot of life to the discussion is for the instructor to role-play Fontaine at this point. Create a name tent for Fontaine, sit at the front of the room at a desk or table, and begin as follows:

"My name is Jean Fontaine. I have been sitting in the back of the room, at the invitation of Professor _____, listening to your comments. However, I don't think that 'what to do' in this negotiation is quite as simple and clear cut as you try to make it!"

At this point, the instructor can specifically respond to some of the students earlier comments, or simply invite suggestions and criticism about how Fontaine has handled the

negotiation. In addition, Fontaine should push the students to specifically address how he should deal with Kelsey's advice at the end of the case. In playing this role, Fontaine should try to convey the following:

- You always thought that you were just about to sign the deal, and that this was the last concession.
- You felt that your objective was to get a deal, almost at any price, and that was the objective you pursued.
- You did not get a lot of help with this problem from Saunders and Meredith, and, in fact, the company put you in an even bigger mess when they announced that the company was not going to go into the PVC business.
- The company people back in the United States always have a lot of helpful advice, but really don't understand what it is like over here "on the front lines."
- What would they have you do now—abort the entire negotiations over one small concession in the contract language? You've worked so hard and so long to get to this point! Beside, what are you going to do with all that VCM in an oversupplied market?

Continue the role-play until students see the binds that Fontaine feels and experiences. Then, step out of role and summarize the discussion.

(5 minutes) Read the (B) case to students (reprinted following these notes). This will confirm that the scenario did not end well, but ended predictably given the previous events.

(15 minutes) Stand back from the role-play and try to get the students to identify with Fontaine's feelings of being "trapped" by the circumstances. Talk about other analogous situations where people feel "trapped" and what they do about it.

Proceed to the Lecturette on Entrapment if time allows. The classic 'Dollar Auction' may also be done at this point to illustrate the dynamics of entrapping decision commitments.

VARIATIONS:

(30 minutes) As an option, you may choose to do the Dollar Auction exercise at this point, to demonstrate entrapment dynamics. It is recommended that you auction off at least 3-4 dollar bills, so that students can see the value of learning on their strategy in the game.

Rules for the Dollar Auction may be found in Keith Murnighan's *Dynamics of Bargaining Games*, or in multiple references to the Dollar Auction on the web. It may also be purchased from the Dispute Resolution Research Center at Northwestern University. Murnighan has also written several articles on his experiences with the Dollar Auction in the *Journal of Management Education*.

What to Expect

Pacific Oil Company is a case about a negotiation failure. Set in the context of a renegotiation of a purchase agreement for liquefied chemical, Pacific Oil Company highlights the

consequences of ineffective planning and negotiating strategy. The failure of the key negotiators to define clear objectives and a bottom line, failure to define a strategy, and failure to understand the importance of time deadlines all contribute to a weak and ineffectual strategy. The case ends on an action note—whether Pacific's chief negotiator should yield one more concession—and students are asked to determine whether there is anything that can be done to "salvage" the contract negotiation for Pacific.

This case extensively focuses on the dynamics of entrapment—that is, the Pacific managers are consistently being nibbled by Reliant, and make decisions that are progressively worse for the company. The discussion notes at the end of the case allow the instructor to focus on entrapment dynamics. It is often useful to conduct the Dollar Auction as part of this case discussion. If the instructor wishes to use the Dollar Auction (see below), he/she should prepare by bringing dollar bills and small change to the class in order to make change when students "buy" the dollars.

Debriefing the Exercise

Summarize the key negotiation failures depicted in the case:

1. Failure to adequately define objectives.
2. Failure to define a bottom line, or minimally acceptable deal.
3. Failure to cultivate alternatives to resigning a new agreement with Reliant.
4. Failure to set a deadline, and incentives for the other party to meet that deadline.
5. Failure to define a clear negotiating strategy, and as a result, to be manipulated by the other's strategy.
6. Failure to manage one's constituency—bosses and information sources—so that they give the negotiator the advice and support he needs.
7. Failure to recognize the "nibbling" strategy used by Hauptmann and Zinnser—and to combat it by only being willing to negotiate a package deal, rather than one concession at a time.
8. Failure to recognize that entrapment was occurring, and that only by setting limits and defining resistance points (and sticking to them) would they be able to "hold the line."

References

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