Take-Home Final: Payne Motors and the Faulty Pawls

Monday March 22, 2021. Katherine Hastings, the recently hired CEO of Payne Motors, is facing a PR crisis and a class-action lawsuit. The company has received anecdotal reports of Hydras (the Payne Motor mid-range crossover SUV) rolling while parked. The head of Product Design, Cyrus Knight, believes that the root cause might be the locking pawls. In pre-launch design, the original pawls were replaced with less powerful parts to reduce costs, but Payne did not update the official specs in the dealer and owner documentation. Katherine and her senior staff discuss whether they should issue a recall to check the pawls and replace any faulty ones.

JACK FORDHAM, former assembly-line employee who was moved to the new CEO's staff at HQ: *When I was on the transmission line for the Hydra, we had to shelve 100,000 locking pawls because they weren't rated for the weight of an SUV.*

CYRUS KNIGHT: *So there's a chance that there are up to 80,000 cars out there whose weight exceeds the maximum capacity of their locking pawls. The pawl's the pin that keeps cars in park. If they break, cars can roll out of park. What do we do in a situation like this? Well, legally speaking, we need to inform NHTSA and then issue a very expensive recall (with the emphasis on* ***very*** *and also* ***expensive****). If this happened, wouldn't we be hearing that people's cars are rolling out of park? I think someone would complain.*

[Cyrus goes off to check on complaints about the Hydra and finds that the number of complaints about Hydras was in line with any other car, according to the NHTSA database.]

CYRUS: *Okay, I've checked every complaint about the Hydra since 2018, and not one mention of it rolling out of park…. Okay, so we keep talking about how expensive this recall will be, right? But it's a $40 part. So takes about an hour or so to replace. That's $100 worth of labor. 80,000 times $140, you're talking about $11.2 million. Except you can't tell a good pawl from a bad one just by looking at them* [without a lift and some disassembly]*. So we would have to recall every Hydra sold since 2018. That's a million cars.*

ELLIOT CHISHOLM, Payne's general counsel: *And the lawsuits, obviously. I mean, even if the pawls aren't defective, the minute this is announced, you're going to start seeing commercials being like, 'Oh, were you injured in an accident in your car? Well, it's not your fault for being a crap driver. It's all Payne Motors' fault. Why don't you sue them?'*

CYRUS: *And adding the cost of a recall campaign and dealers overcharging for repairs, all in, it could be, like, ten figures* [i.e. over $1bn].

SADIE RYAN, Head of Communications: *Let's think about the cost of not doing a recall and then learning that we had put the wrong pawls in, and a bunch of people died.*

JACK: *Yeah, I have to agree with Sadie here. How do we actually put a price on people dying?*

ELLIOT: *Oh, well, we don't have to. The lovely people of the Department of Transportation have actually done that for us already. So the value of a statistical life (or VSL) for this year is $11.6 million.*

JACK: *But isn't a person's life kind of priceless?*

ELLIOT: *No, it's $11.6 million. Then there's the cost of litigation, punitive damages, and the hit that our brand would take. It's going to cost way more than the price of a recall. If we installed the defective pawls. For all we know, we just lost them*.

CYRUS: *If we do the recall, it'll cost us around **$900 million**. And if we don't do the recall, my best guess of the total cost of lawsuits… comes out to somewhere in the neighborhood of, yep, **$900 million**.*

Katherine and her team decide to postpone the decision on the recall. Meanwhile, a family on a camping trip parks their Hydra on the side of a mountain road. The Hydra (loaded with 300 lbs. of fishing gear, but luckily no family members) rolls backward down a hill, crashing into the forest, then igniting, causing a wildfire that rages out of control for weeks. The car fire prompts extensive media coverage and social media commentary.

Katherine receives a letter from Davis Parker, an aggressive, consumer class-action attorney from the firm of Parker, Slipp, & Roel. Parker informs Katherine that he represents a group of Hydra owners who are filing a class-action lawsuit against Payne Motors. The class will consist of the 1 million owners of Hydras manufactured in 2018-2020, seeking the following remedies:

- Immediate **recall** of all potentially affected Hydras and **repair** of faulty pawls, at Payne's expense
- The use of **loaner vehicles** while the cars are being repaired
- A total of **$3.22bn** in compensation (in addition to the repairs)
  - $20,000 in compensation for each Hydra involved in an accident during 2018-2021, estimated to be 111,100 accidents, for a total of $2.22 billion
  - $10,000 in compensation to the owner of each Hydra whose pawls are determined to be faulty. Assuming 100,000 Hydras are defective, the compensation would total $1 billion.
- A formal **apology** from the board and a **promise** to do better in future.

Parker helpfully attached his assumptions and calculations for the remedies:

Exhibit 1. *Plaintiff's estimation of damages*	Year of Hydra sale			
	2018	2019	2020	Total
For Hydra owners who had accidents				
Hydras sold (k)	333	333	334	1,000
Hydras in use (k)	333	666	1,000	
Chance of accident	5.6%	5.6%	5.6%	
Estimated accidents (k)	18.5	37.0	55.6	111.1
Compensation per accident ($k)	$20	$20	$20	
Total comp ($mm)	$370	$740	$1,111	**$2,221**
For Hydra owners with defective pawls				
Defective pawl rate	10%	10%	10%	
Hydras requiring pawl replacement (k)	33.3	33.3	33.4	100.0
Compensation per owner ($k)	$10	$10	$10	
Total comp ($mm)	$333	$333	$334	**$1,000**

Your mission:

Develop a negotiation strategy for Payne Motors, including:

1. Identification of the **deal terms** (i.e. what will be the elements of the final agreement?)
2. An **expected value** equation for each side. The EV equation must translate the deal terms into a $ value.
3. The **BATNA** and **reserve price** for each side
4. The **ZOPA** (i.e. the range between each side's reserve price)
5. The **aspirational goal** for your side (with justification). What will be your side's EV, if you can convince your counterparty to accept your aspirational deal terms?
6. Any potential **integration** opportunities
7. Any other, **unquantifiable sources** of value that the EVs should include
8. How valuable (or not) **trust and collaboration** will be for the two sides after the deal (e.g. to execute the agreement)
9. Your **anchor** and planned **concessions**.

In addition to these items, give one or two insights and your rationale.

You may also choose to consider who from Payne Motors should negotiate with Davis, where and when to meet, the use of deadlines, “game tape” on your counterparty, and Shell/Voss/Cialdini tactics you plan to deploy in the negotiation.

You should make reasonable assumptions for values (e.g. recurring costs, revenues, one-time costs) and probabilities that are important in estimating BATNAs, RPs, and EVs but are not given in the case materials.

Please limit your strategy to 5 pages, single-spaced with 12-point font and reasonable margins, not including figures, tables, calculations, graphs, etc.

This is a solo project, an opportunity for you to embed your new GTIA skills by applying them. If you are not fully comfortable with the EV modeling, imagine that you had a CFO working for you who was supplying all the analysis, and simply make rough estimates of what those numbers would be.