

TEACHING MATERIALS: ROLE PLAY SIMULATION ON BRAZILIAN GOVERNMENT AND NON-MARKET FORCES NEGOTIATION

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ABSTRACT: *This paper presents new teaching materials designed to: (a) provide teachers with educational tools and new insights about how to address insights on market and non-market forces' strategies integration; negotiation with government; corporate compliance; mutual gains perspective; decision making process; ethics; uncertainties management; confrontations; relationship and credibility building; communication; strategic thinking. (b) enhance students' skills on complex negotiations and consensus building; and (c) provoke debates in classroom regarding to changes in the Brazilian non-market forces, in particular the influence of government, on companies' corporate strategies. a teaching material for professionals intending to study and explore the many variables present when negotiating with government. One key lesson to be absorbed by the participants is how to apply negotiations principles and methodologies. A full set of instructions to practitioners and to facilitators complete the present work.*

KEYWORDS: Market, Non-Market Forces, Government Negotiation, Compliance.

INTRODUCTION

The present teaching set was designed for adults education, especially MBA courses and overall executive education, and it also discusses the market and non-market forces' strategies integration; negotiation with government; corporate compliance; mutual gains perspective; decision making process; ethics; uncertainties management; confrontations; relationship and credibility building.

This exercise is based on real events, where the author had direct participation. The main objective is to illustrate the impact of a subset of non-market forces – the influence of government – on business strategies. In particular, it deals with a volatile and highly regulated sector, fostering the participants to seek ways to deal with these forces appropriately, comparing their results to the ones achieved on the real case.

It shows how it was possible to combine the building of an adequate regulatory environment to enable exports of finished goods (cigarettes) from Cigar Brazil(CB) according to its specific marketing needs, as defined by its headquarters (CigarInternational - CI), which were initially identified as conflicting with current regulation and impossible to achieve.

The final solution and concrete results of the real case, to be revealed in the exercise conclusion, contributed to improve CB's corporate image, allowing to achieve both key government stakeholders interests (IRS – Internal Revenue Services) and CB's strategic intents, generating production volume and revenue growth, as well as capturing the desired sourcing opportunities for CI.

In order to avoid disclosure of proprietary and/or strategic information and for privacy purposes, names and selected data were changed. The next section presents the Methods used in the present research.

METHODOLOGY

The role play simulation is supported by Goffman's dramaturgical theory, where negotiations are faced as social interactions, like a theatrical drama where there are a full set of actors, stage, and script (Goffman, 1959, 1961). Therefore, the role play simulations provide the actors (students, executives) a prepared role set (case instructions) to perform on a stage (in classes). There are also audiences and facilitator (professor, monitors, observers and students/participants), timely entries (written instructions), and performances (from players in general). This case follows previous teaching materials (Dias, Murillo de Oliveira; Teles, André; 2018; Dias, M.; 2018; Dias, Murillo & Navarro, Rodrigo, 2017; Dias, M.; Duzert, Y; 2017).

Teaching Objectives

The main objective is to provide a relatively simple, but effective exercise to be used as a teaching material for professionals intending to study and explore the many variables present when negotiating with government. In particular, there are relatively few teaching cases based on recent real events involving the Brazilian regulatory environment, especially related to a so complex and highly regulated sector, such as tobacco.

Teaching Case: Mechanics

This exercise involves two parts. The first is Mr. M, Director of Government Relations of CB, an experienced professional used to deal with complex and volatile business environments, and especially aware of non-market forces' impacts on corporate strategies. The second is Mr. Noo, General Secretary of the Brazilian IRS, with a strong personality, firmly committed with the prosperity of the country through a tight control of rules enforcement set up by the government.

In this approximately 2-hour exercise, a first 15-minute preparation phase starts with each participant reading its part (Parts I and II of the Teaching Case), comprised by a common one containing a brief background, and a specific confidential one.

Then, during the next 30 minutes the parts are instructed by the professor (acting as a facilitator) to reflect and in silence prepare their negotiations strategies.

In sequence, a 45-minute period is given for the parts to interact, make considerations and negotiate possible solutions to the case, aiming to achieve their respective goals.

A final 30-minute period is used by the facilitator to (1) check if the negotiation was successful; (2) evaluate each solution considering the part's desired goals and attitudes; and (3) make comments and comparisons while revealing the solution achieved in the real case (see Discussion section, for further information).

Topics Covered

Market and non-market forces' strategies integration; Negotiation with government; Compliance; Mutual gains perspective; Decision making process; Ethics; Uncertainties management; Confrontations; Relationship and credibility building; Communication; Strategic thinking.

Major Lessons

This exercise illustrates the impact of non-market forces, in particular the influence of government, on companies' corporate strategies. It also shows how it is possible to use negotiation methodologies, creativity and strategic thinking to integrate market and non-market strategies, achieving solutions that meets business objectives, enhancing the perspective of management theory and practice.

One key lesson to be absorbed by the participants is how to apply negotiations principles and methodologies, such as the ones known as the "Harvard Method"¹, when negotiating with Government. These include² some fundamentals to prevail in such negotiations, like:

- Understand that governments have special powers based on their privileges and role as defenders of the public interest;
- Follow an as-simple-as-possible goal-driven plan;
- Know the applicable government process to the case being discussed;
- Seek to determine previously to engagement what the government representative wants to achieve in the negotiation;
- Use the right persuasive strategy and tactics, which may include precedents citations, benchmarks and a draft agreement that outlines your objectives;
- Prepare alternative acceptable outcomes.

Teaching Case Features

Time required	2 hours
Number of participants	2 parties
Groups involved	No
Agent presente	No
Third party presente	No

¹ Based on the works of Professors William Ury, Roger Fisher and Bruce Patton (see recommended readings)

² A fine work on these and other related topics is made by Professor Jeswald W. Salacuse on the book *Seven Secrets for Negotiating with Government* (see recommended readings)

DISCUSSION AND CASE SOLUTION

It is recommended to disclose the case solution on the case debriefing and further debate session, after the negotiations are finished, or in case of no-deal, the time for the negotiation ended.

After analyzing the regulatory environment in detail, as presented by IRS, and comparing it to CI's requirements, the initial outcome was that CB could not export to African countries the packs with current requirements. This way, a task force team was formed to seek for a solution through a constructive approach with government authorities.

There were several challenges involved in the process to turn the potential export opportunity a success, including:

- To demonstrate why CB needed a change in current legislation, and bring this issue to their agenda;
- To achieve a satisfactory, non-discriminatory solution to both private sector and government, which meant enable exports and at the same time assure effective controls against illicit trade;
- From the legal and tax perspective, to guarantee that CB was able to proceed with the exports if new conditions were created.

The CB team built a strong case to request from government a change in legislation, so as to enable these exports to Africa, selected by CI as the first target markets. One of the main argument was the common view expressed by both parties during the first negotiation meeting that the possibility of a country to respond to needs of different international clients is essential to be considered as a global supplier in today's world trade. CB also leveraged on efforts of the Brazilian diplomacy, to establish at that time commercial partnerships with African countries.

The task force gathered at CB analyzed the laws that introduced such requirements to understand the purposes (intentions) they served, so as to come up with possible creative alternatives that could attend CI requirements, as well as government's concern regarding contraband and counterfeit fighting:

- The printing "Brazilian Industry" on packs was meant to avoid that cigarettes that leave factories intended for exports may return to the Brazilian market. In this case, CI's requirement to print "Imported by" or "For exports to", followed by the name of the importing country, could serve the purpose, since it would be even easier to identify such products.
- The use of export fiscal stamps is another instrument for avoiding exports products to be traded in the Brazilian market. There could be methods to replace the stamp and still prove control over production figures to the government.
- The CNPJ is an identification number for facilities. Other tracking devices could be available on packs, such as use of transparent ink to make the information available to the government, but invisible to consumers. It is also a way to assure that companies are paying taxes accordingly.

The CB team conducted negotiation meetings with IRS during the second semester of 2004. The first approach was at the technical level, where the company had the chance to present the issues and the opportunities involved, as well as to receive the first feedbacks. After that, CB set meetings with higher IRS levels and, in parallel, with the Development, Industry & Commerce Minister, which was interested in increasing Brazilian exports and could be a potential ally.

A submission was then officially sent to IRS presenting the business opportunity and the possible solutions for the issues identified, which key points were in summary:

Considering that:

- 1) The importing markets involved in these opportunities have no interest in buying finished products that bear, among other pieces of information, identification of the product's country of origin;
- 2) The demands of importing countries regarding packs already identify them as meant for exports only, which fulfills the purposes of current Brazilian norms, mainly avoiding that exported products are brought back to Brazil by contraband;
- 3) In today's international trade, most likely other importing countries will have similar demands for Brazilian cigarettes, if not the same, which seriously hinder exports for this sector as a whole.

The following request is presented:

- a) Grant the dismissal of the fiscal control stamp use when the country of destiny's regulation does not comprise this requirement or in the case the stamp is not desired by importers due to local marketing reasons;
- b) Grant the dismissal of the statement "Brazilian Industry" on the packaging for these exports, considering that similar identifying data can be included on coded markings on the packaging.

Alternatives and suggestions to be discussed for implementation:

- Printing of the country of destiny on the export packaging: Such text as "*For sale in [name of country]*" can be considered as an effective alternative control measure to substitute the current export control stamp;
- Special production information marking: specific codes on packaging can be used as an alternative origin indicator, in substitution of the "Brazilian Industry" and CNPJ printing.
- Requirement of a financial guarantee prior to export: this could be demanded by IRS to exporters, at a reasonable and compatible value, with a 6-month deadline for presentation of effective export documents; should the exporting company not present the documents within the established deadline, the financial guarantee would be executed in favor of the Union.

The focus of the meetings that followed the submission was to show that CB had a common ground with government on illicit trade fighting, but believed that a solution to achieve this objective was not incompatible with enabling the capture of export opportunities – another

objective among government's priorities, such as observed in previous similar cases (see Dias, Murillo de Oliveira; Teles, André; 2018; Dias, M.; 2018; Dias, Murillo & Navarro, Rodrigo, 2017; Dias, M.; Duzert, Y; 2017).

On January 2005, the Brazilian IRS published Normative Instruction 498/05, which makes it possible for companies to ask for differentiated exports conditions, including explicitly the exemption to not use export stamps, depending on a case-by-case analysis to be conducted by IRS, based on a series of defined information requirements, in the case of non-border countries.

The CNPJ number was accepted by IRS as a sufficient mechanism to be used as a fiscal control in these particular cases. From CI's side, after a creative solution proposed by the team, this was an acceptable type of marking to be included under the bar code of the packs, not to be perceived by African consumers as a differentiating element.

CB presented the new regulation to CI, attesting that it could be confirmed as a source, as the marketing and manufacturing requirements are met, and another submission were presented to IRS to have their final approval to proceed with the exports.

The special authorization was granted by IRS in March, 2005. The first brands for exports (Congress and L&M) were then registered at ANVISA (National Health Surveillance Agency), following all the enhanced IRS's regulatory requirements. Production started in April, 2005 and the exports began in the same month, being the first container arriving at its destination in May, 2005.

CB were this way enabled to recover its condition as an international cigarettes supplying source. In 2005, shipments reached 700 million cigarettes, going up to 2,4 billion in 2006, which represented approximately US\$ 16.

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APPENDIX I – PARTIES’ GENERAL INFORMATION

To be read by all parties, approximately 15-30 minutes

Background

The habit of smoking is for sure an increasing concern for governments, health authorities and society as a whole, as it is a legal drug, which is addictive and can lead to serious damages to health³. Despite these key issues, nowadays considered as common knowledge due to intense information programs and campaigns the industry was forced to implement by the majority of governments worldwide over the past years, the consumption of tobacco is a global reality, reaching a steady average of almost 6 trillion cigarettes annually, as shown on Table 1 below:

Table 1: Worldwide cigarette consumption

COUNTRY	Billions of units				
	2000	2005	2010	2011	2012
China	2,235.470	2,763.820	2,546.760	2,559.490	2,562.050
India	474.280	465.610	462.730	465.040	465.510
USA	489.910	441.810	439.080	441.280	441.720
Russia	301.480	279.570	264.240	268.480	268.750
Germany	175.300	154.530	146.060	148.410	148.560
Indonesia	170.540	147.980	147.060	147.790	147.940
Japan	164.700	142.120	141.230	141.940	142.080
Turkey	114.100	117.330	105.600	106.130	106.240
UK	100.440	96.100	90.830	92.290	92.380
Brazil	96.550	108.240	96.970	97.450	88.990
Others	2,036.330	1,608.020	1,296.460	1,297.410	1,307.260
TOTAL	6,368.100	6,325.130	5,737.020	5,765.710	5,771.480

Source: Afubra, Associação dos Fumicultores do Brasil (Association of Tobacco Growers in Brazil)⁴

³ World Health Organization: <http://www.who.int/tobacco>

⁴ Full data available at <http://www.afubra.com.br/index.php/conteudo/show/id/171>

Other relevant concerns present in this sector are related to the economic impacts of these products and the correspondent production/commercialization in many countries. In this context, measures to fight counterfeit and contraband and the application of high taxes, for instance, are commonly adopted by governments worldwide.

According to SindiTabaco (Interstate Tobacco Industry Union)⁵, Brazil is the world's second tobacco producer, only following China (state monopoly), and a global leader in tobacco exports, reaching US\$ 3.27 billion in 2013, shipping to 102 countries. Brazil has an excellent reputation on the international market, due to its excellent quality and competitive price.

Tobacco production is also important to the Brazilian economy, especially considering the south region of the country (where 97% of production is located), as the numbers below, provided by SindiTabaco, shows:

- 640 thousand people involved in the rural area;
- 30 thousand direct jobs at industry level;
- 332 thousand hectares planted;
- 706 thousand tons produced.

Alongside with its economic importance, another relevant characteristic is that the tobacco sector is one of the most regulated in the world. In particular, Brazil – as other countries like New Zealand and Canada – presents several restrictive legislations to reduce cigarettes consumption, being a pioneer in measures to regulate this market, like obligatory graphic health warnings on packages, product advertisement banning, and prohibition to smoke in public places, among others⁶.

Within this strength regulation context, illegal cigarettes – that comprehend piracy, contraband and counterfeit products – are one of the major concerns of governments and part of their strategies to reduce tobacco consumption, as these products can be offered at lower prices and without inspection from authorities.

Several control measures, seizure/destruction of apprehended materials, and a joint work from IRS and Federal Police to fight contraband especially at neighbor Mercosur border countries (like Paraguay) have been conducted over the past years. As a result, data from the Brazilian Ministry of Health⁷ indicates that:

- Illegal cigarettes manufacturing in Brazilian territory dropped from 17% to 11%, corresponding to a reduction of 250 million packs in 2008 and 430 million in 2009;
- The consumption of illegal cigarettes in the Brazilian territory dropped from 30% in 2000, to 20% in 2010;

⁵ SindiTabaco 2014 Report, available at <http://sinditabaco.com.br/wp-content/uploads/2014/03/relat%C3%B3rio-institucional.pdf>

⁶

http://www2.inca.gov.br/wps/wcm/connect/observatorio_controle_tabaco/site/status_politica/a_politica_nacional

⁷ Data available at

http://www2.inca.gov.br/wps/wcm/connect/observatorio_controle_tabaco/site/status_politica/mercado_ilegal

- Federal tax collection from tobacco sector increased from US\$ 2.6 billion in 2009 to US\$ 3.1 billion in 2011 and US\$ 3.8 billion in 2013.

Due to all these factors, the importance to integrate non-market forces into companies' strategies is vital to succeed in this sector. The following case is based on real events occurred in Brazil during 2004-2005 and involves Cigar Brazil(CB) and the Brazilian Internal Revenue Services (IRS), each one played in this exercise by one representative.

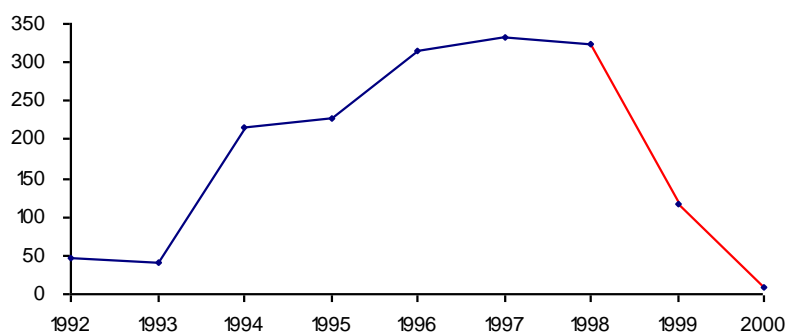
Brazilian Scenario

CB started operating in Brazil in 1973, being one of the affiliates of CigarInternational (CI), which is present in over 160 countries. It belongs to one of the major consumer goods group in the world (Altria Group, Inc.).

CB headquarters is located in Curitiba (Paraná State), with sales offices in the cities of São Paulo, Araraquara, Porto Alegre and Rio de Janeiro, with a production facility currently located in Santa Cruz do Sul (Rio Grande do Sul State), which includes a print shop and units for tobacco processing.

CB used to be an important finished goods source to CI mainly for Eastern Europe markets such as Russia, and some Latin American markets. In 1997, the cigarettes exports shipments reached 44 billion cigarettes representing US\$ 333 million in revenue for the affiliate (see Graphic 1 below). CB was then recognized as a flexible and reliable CI manufacture, delivering products with high quality and competitive cost.

With the monetary crisis in Russian at the end of 1998 and the creation of a 150% Brazilian export duty applied for finished goods on exports to Latin America by the end of 1999 (which can be noted as another example of non-market forces influencing the business), CB ceased its cigarettes shipments and faced a substantial financial impact. The industrial plant, located in Curitiba, was shut down at the beginning of 1999 and all tobacco operations were relocated to Santa Cruz do Sul, close to the tobacco production.



Graphic 1: CB finished goods (cigarettes) exports, in US\$ MM

Source: CigarBrazil

In 2018, with the objective to expand its exports and generate additional cash to fund market initiatives, CB manufacturing department started to search global opportunities within CI markets. During this search, CI was restructuring its global sourcing of cigarettes, and after a highly disputed internal selection process conducted by CI, which included several affiliates worldwide eager to increase their results, CB was chosen to be an international supplier for cigarettes exports.

This was possible mainly due to the characteristics of CB production: low cost, high quality, flexibility and speed to respond to demands, besides the fact that no additional major investments were required due to its available capacity to meet the international demands. Also, the aforementioned excellent quality of Brazilian tobacco played an imported role as well in this CI decision.

The first markets to be supplied by CB were defined as a series of African countries, including Mauritania, Algeria, Nigeria, Congo and South Africa. This was a great test for CB – previously, CI's affiliate in the Czech Republic supplied Africa. If this initiative had success, it would represent initially over US\$ 15MM per year in exports, and as other markets could be included as additional targets, a potential US\$ 50MM per year on exports could be reached in the following years.

The promising scenario is set. The next step to occur is a meeting between the representatives of CB (Mr. M, Director of Government Affairs) and IRS (Mr. Noo, General Secretary), in order to respectively explain the commercial opportunities involved and assure the compliance with all existing rules and regulations applicable. Prepare adequately as the scheduled meeting approaches, reading your part presented in the annex.

APPENDIX II – CONFIDENTIAL INFORMATION PART 1

CONFIDENTIAL INFORMATION FOR MR. M, CB'S REPRESENTATIVE

You are Mr. M, Director of Government Relations of CB, an experienced executive used to deal with complex and volatile business environments, and especially aware of non-market forces impacts on corporate strategies. You were involved in this export process by CB's President only after the affiliate had signed a commitment with CI to supply the cigarettes to African countries. You always wish you were involved sooner in these processes; in this case, even before CB started to participate in the international selection for new export supplier. Anyway, as it is a common practice due to the transversal nature of your job, you started to work on the case (internally named "Africa Project") with a team of other Directors, including the ones responsible for the Legal and the Manufacturing departments. The former is – as usual – concerned mainly with the attendance of all requirements set up by current legislation, as the second is very excited to increase production volumes, cost reductions and revenue growth, especially considering the excellent perspectives this could bring to CB.

You know that the IRS representative has the final word on the case. If he sees any incongruence of the Project from the regulatory perspective, it will be a showstopper with drastic consequences for CB, as it would lose credibility before headquarters and immediately be replaced by other affiliate to perform these exports (not mentioning that other chance like this would not happen in the foreseeable future).

Together with the team, you summarized 3 key CI's requirements for the cigarettes' packs to be sold abroad, due to marketing reasons:

- a) Printing of "Imported by" or "For export to" followed by the name of the importing country, with no name of the manufacturing country;
- b) Use of no fiscal stamp, since the destination markets in Africa does not have them;
- c) Use of health warnings and other specific messages required by the importing countries.

The above conditions are fundamental to be met, since altering packs currently sold in different importing countries could represent a significant alteration in sales. You listed some initial arguments to support that:

- It is possible that exports to different international markets are shared with more than one supplying country, which demands assurance by any involved supplier that packs produced are identical to those produced by other suppliers, according to local requirements of the target-market;
- Different packs of the same product/brand in one market could lead buyers to seeing the imported products as counterfeit;
- Even being legitimate products, consumers could consider the imported products in packs different than the usual ones distinct from those they are used to smoking.

You are about to meet Mr. Noo, IRS General Secretary, that is known to have a strong personality and be firmly committed with the prosperity of the country through a tight control of rules enforcement set up by the government.

Your goals are to, briefly, (1) introduce yourself and the company you represent; (2) explain the "Africa Project" opportunity; and (3) present CI's marketing requirements in order to make sure no regulatory conflict can jeopardize CB's business objectives. If any problem rises, you have to seek an urgent solution that can be acceptable for both parties. Prepare yourself.

APPENDIX III – CONFIDENTIAL INFORMATION PART 2

CONFIDENTIAL INFORMATION FOR BRAZILIAN IRS' REPRESENTATIVE

You are Mr. Noo, General Secretary of the Brazilian IRS, who is an open-minded – although sometimes quite conservative – public service employee for your professional entire career. You are interested in the progress of the country above all, always having in mind that rules have to be respected by all. Having absolute intolerance regarding corruption and other types of misbehaving attitudes, you are used to work with difficult subjects and always try to engage discussions and negotiations in a constructive way, never forgetting your responsibility as a representative of a powerful Federal Government branch. You know your word is final to determine if any process that reaches your office may go ahead or not.

In particular, due to the importance of the recent growing tax collection generated by legal tobacco products commercialization, mainly due to several control measures you supported to fight the illegal market, you know this sector in detail. For instance, you understand the dichotomy involving the tobacco sector: if by one side it really has to be highly regulated and

even restricted due to health concerns, cigarettes consumption is a reality that would not vanish with a simple prohibition by law, and from the economic perspective its importance is unquestionable. This was especially true if considered the south region of Brazil, as many politicians from there regularly affirm to you when visiting your office to ask for less restrictive measures to be applied on tobacco growers...

In this context, you received with some concern the information that CB was seeking a meeting with you to discuss the exports of cigarettes. The rules and regulation for that kind of operation were already clearly set, so what should be the topics to discuss ? During the first contacts before the meeting, it was mentioned to you some “packaging requirements” to be discussed.

As a preparation for the upcoming meeting, even with few information about the specific case of CB, you gathered the current regulation that is applicable on cigarettes exports. In summary, the following information is mandatory to be displayed on packs destined to exports:

- a) Explicit reference to the manufacturing country (e.g. printing of “Brazilian Industry”);
- b) Mandatory use of the specific Brazilian export stamp;
- c) Printing of the manufacturing company number (CNPJ – *Cadastro Nacional de Pessoa Jurídica*), a 14-digit number used to identify all Brazilian companies before IRS.

You made some preliminary reflections on these points:

- These measures proved to be effective in reducing cigarettes contraband, especially at the border with Paraguay, as indicated by the numbers from apprehensions and tax collection increase you have available in your office;
- At the same time, you understand that the capability of Brazilian companies to respond to needs of different international clients is an essential pre-requisite to be considered as a global supplier in today’s world trade;
- You may be able to consider some adaptations and/or change on currents rules, if proven necessary and no risk of facilitating illicit trade is somehow granted.

You are about to meet Mr. M, CB’s Government Relations Director, a well known and respected professional in the area, who is used to deal with complex and volatile business environments. Your goals are to, first, (1) listen carefully to CB’s presentation; then (2) briefly present IRS’ regulatory requirements; and (3) identify the company’s positions and interests, comparing them with yours, trying to reach – if necessary and possible (considering your main concerns) - a solution to any conflict that may rise that can be acceptable for both parties. Prepare to negotiate.