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Instructors' Notes

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LETTER FROM THE EDITORS

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The notes contained in this volume have been double blind refereed, and each was required as a companion to a complete teaching case, which are published in a separate issue. The acceptance rate for manuscripts in this issue, 25%, conforms to our editorial policies. The Instructor's Note for each case in this volume will be published in a separate issue of the *JIACS*.

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SPEEDY DSL CORPORATION

Leah Marcal, California State University, Northridge
Richard Tontz, California State University, Northridge

CASE DESCRIPTION

The primary subject matter of this case concerns the pricing decision of a service firm, and the use of the appropriate economic model to analyze that decision. A comparison of price-elasticity and cross-elasticity of demand highlights the market structure in which the firm operates and thereby an understanding of how a price change will impact the firm's total profit. Secondary issues involve classifying the cost of the firm's business activities and allocating those costs by sales revenue.

The case has a difficulty level of three and is intended for use in junior-level courses. It can be covered in three hours, including a class presentation by a student team. The case requires a minimum of nine hours of outside preparation by students.

This case is designed for use in an upper-division, inter-disciplinary business course. The purpose of the course is to enable students to apply the knowledge they have gained in their lower-division, business core courses that include microeconomics, financial accounting, and managerial accounting. Specifically, the case incorporates the understanding of profit-maximizing pricing under monopoly and duopoly models of competition, how price and cross-elasticity of demand are interpreted, and how cost data can be organized for management decisions.

CASE SYNOPSIS

Students view the case through Susan, a recent business graduate, who has struggled to find employment and lives with her parents. Susan is anxious to turn her paid internship into a job. She interns for a local, Internet service provider, Speedy DSL. Speedy has a profit margin that is below the industry average and faces strong competition from Timely Cable in the local broadband market. Currently, the two firms (Speedy and Timely) charge the same price for basic Internet connectivity that is similar in speed and reliability. Another Speedy intern, Matt, uses an estimated monopoly demand schedule and Speedy's own cost data to argue that Speedy should raise its price. Speedy's Marketing Director asks Susan for an evaluation of Matt's proposal. Susan has read industry reports with an estimate of the cross-elasticity of demand between DSL price and Cable subscriptions. Understanding that Timely's gain of customers would be Speedy's loss; students (placed into Susan's position) evaluate the impact of a price increase on Speedy's profit in a *duopoly setting. Students must also categorize the cost of Speedy's business activities and show the breakdown of those costs against sales revenue.*

INSTRUCTOR'S NOTES

Recommendation for Teaching Approaches

This case is designed for use in an upper-division, inter-disciplinary business course. The purpose of the course is to enable students to apply knowledge they have gained in the lower-division business core. In addition, the course aims to improve students' communication and teamwork skills. Student teams evaluate the issues presented in the case, perform the appropriate analysis, and recommend a course of action. All teams submit a formal, written business report containing their analysis and recommendations. One team of students formally presents their case analysis to the class. A second team of students acts as a "discussion team" by asking the presenting team for further explanation or clarification of their recommendations. Following the discussion team's exchange with the presenters, the entire class is welcome to participate in an active question and answer session.

Although the case is designed for use in an upper-division, inter-disciplinary business course, the case can easily be modified for use as an in-class or take-home assignment in an introductory microeconomics course.

Background

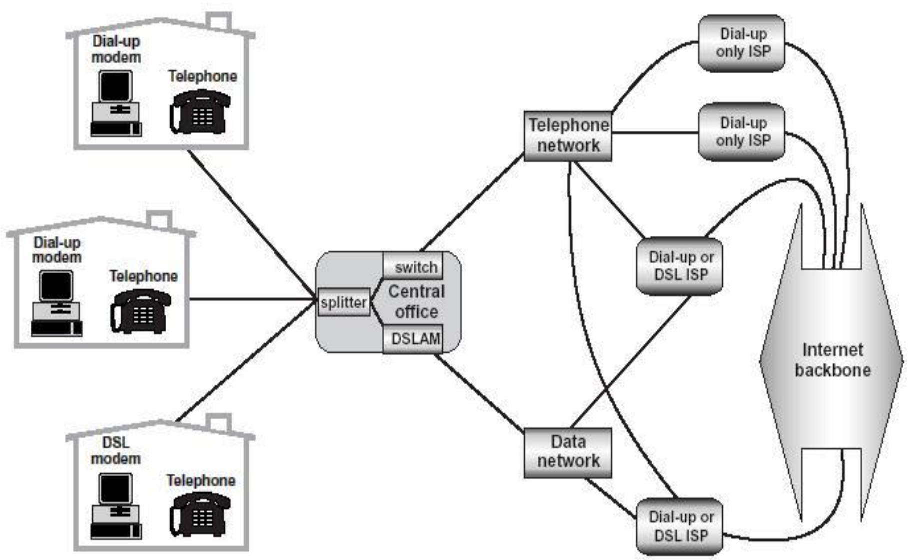
This case covers three lower-division core disciplines -- microeconomics, financial accounting, and managerial accounting. The concepts covered are: market structure and pricing, profit-maximizing output level, returns to scale, price-elasticity of demand, cross-elasticity of demand, return on sales, computing the cost for different cost objects, and organizing cost data for management decisions.

This case emphasizes the adoption of the correct economic model when analyzing a firm's pricing decision. Students are given a demand schedule (in Exhibit 2) based on the monopoly model. Pure monopoly assumes there is only one firm in the industry and that firm does not face competition from suppliers selling close substitutes. Additionally, students are told that the market contains two suppliers that produce close substitutes. The cross-elasticity of demand (of 3.49 given in the case) further emphasizes the presence of a competitor and the loss of customers to that competitor via a price increase. Thus, the duopoly model (or two-firm oligopoly) is the correct economic model to use when analyzing the impact of a price increase on the firm's profitability.

From an accounting perspective, most students are not familiar with the production process in this industry. They are accustomed to the retailing or simple manufacturing firm examples used in lower-division course textbooks. It may be difficult for many students to determine the cost of goods sold because the case does not have beginning and ending inventory.

It may be helpful to ask students to diagram the process flow for this business so they can visualize how DSL service works. The diagram allows them to see that the production function consists of two steps: installation of hardware (e.g., modem and signal splitter) at a customer's house and providing connectivity by establishing an IP address for the customer, entering their address into a router, and making the last mile connection to the Internet via copper wires and fiber-optic cables.

Figure 1. Speedy DSL Process Flow



Note: the splitter and digital subscriber line access multiplexer (DSLAM) is part of Speedy's network equipment. The splitter separates voice and data signals. DSLAM aggregates individual DSL connections and transmits data signals to Speedy's data network from which the customer's ISP takes traffic.

Figure 1 makes it easier for students to deal with cost classifications and to understand the substantial investment in infrastructure needed to support a data network (Guerrero, 2000). As an extension, instructors may use the large investment in a network as an example of strategic comparative advantage (via high fixed costs) that keeps potential competitors from entering the broadband industry.

Susan's Memo to Robert Baker

Student memos should address the following issues: (1) Speedy is not a monopoly; (2) Speedy cannot use the arc price-elasticity of monopoly demand to predict the change in its subscriptions following a price increase; (3) cross-elasticity is used to estimate how Speedy's price increase will raise (lower) Timely's (Speedy's) subscriptions; (4) the reduction in subscriptions alters Speedy's revenue, cost, and profit; (5) profit falls with the price increase; (6) Speedy's return on sales is slightly below the industry average; and (7) a breakdown of total revenue by cost categories highlights the enormous cost of providing a network connection. A sample memo is provided below.

Memorandum

To: Robert Baker, Marketing Director
From: Susan Katz, Marketing Intern
Date: Oct. 24, 2013

Subject: Evaluation of Proposed Price Increase and Classification of Cost

Last week, Matt Peterson proposed that Speedy raise its DSL price from $39.95 to $42.25. He indicated that this price increase would lower subscriptions by 11.4% and raise total profit. However, Matt's analysis relied on a monopolist's demand schedule.

Terra Loop provides DSL in a comparable Northeastern county but it faces no competition for Internet connectivity and therefore faces a monopoly demand schedule. Terra's arc price-elasticity of demand between $39.95 and $42.25 can be calculated as:

$$\text{arc } \varepsilon_d = \left|\frac{\%\Delta Q_d}{\%\Delta P}\right| = \frac{\dfrac{\Delta Q_d}{\text{average } Q_d}}{\dfrac{\Delta P}{\text{average P}}} = \frac{\dfrac{42,762}{386,719}}{\dfrac{2.30}{41.10}} = \frac{0.11058}{0.05596} = 1.98$$

where Δ = change; P = price; average Qd = average of the two quantity demanded numbers (i.e., Qd = 408,100 when P = $39.95 and Qd = 365,338 when P = $42.25); and average P = average of the two prices. Matt's prediction that Speedy will lose just 11.4% of its subscribers after the proposed 5.76% price increase would only be applicable if Speedy faced Terra's monopoly demand schedule.

$$\text{arc } \varepsilon_d = \frac{\%\Delta Q_d}{\%\Delta P} \Rightarrow \text{arc } \varepsilon_d \times \%\Delta P = \%\Delta Q_d \Rightarrow 1.98 \times 5.76 = 11.4$$

Unlike Terra Loop, Speedy has strong competition from Timely Cable because Timely provides an Internet connection that is similar in speed, reliability, and customer satisfaction. Speedy must consider how many subscribers it will lose to Timely following the proposed price increase. An estimate of lost subscriptions can be obtained from the cross-elasticity between Speedy DSL price and Timely Cable subscriptions (i.e., 3.49, as indicated in industry reports).

$$\text{cross } \varepsilon_d = \frac{\%\Delta Q_{d\ \text{Cable}}}{\%\Delta P_{\text{DSL}}} = 3.49 \Rightarrow \%\Delta P_{\text{DSL}} \times \text{cross } \varepsilon_d = \%\Delta Q_{d\ \text{Cable}} \Rightarrow 5.76 \times 3.49 = 20.1$$

The cross-elasticity of demand indicates that a 5.76% increase in DSL price will lead to a 20.1% increase in Cable subscriptions. This suggests a 20.1% reduction in DSL subscriptions as 82,028 (i.e., 20.1% x 408,100) customers switch from Speedy DSL to Timely Cable.

This loss of 82,028 DSL subscribers will alter Speedy's total revenue, total cost, and total profit. Total revenue falls to $13,776,542 (i.e., [408,100 – 82,028] x $42.25). Speedy's constant marginal cost of $22.52 can be used to estimate the reduction in total cost. Thus, total cost falls to $10,942,241.02 (i.e., $12,789,511.58 – [$22.52 x 82,028]). The proposed price increase (from $39.95 to $42.25) has thereby reduced total profit from $3,514,083.42 to $2,834,300.98. This represents a loss of $679,782.44 in monthly profit. These calculations are summarized in the table below.

How the Proposed Price Increase Impacts Speedy's Total Profit

Economic Model	Price	Quantity Demanded	Total Revenue	Total Cost	Total Profit
Pure Monopoly	$42.25	365,338	$15,435,531	$11,826,718	$3,608,813
Duopoly	42.25	326,072	13,776,542	10,942,241	$2,834,301
Current Price & Qd	39.95	408,100	16,303,595	12,789,512	3,514,083

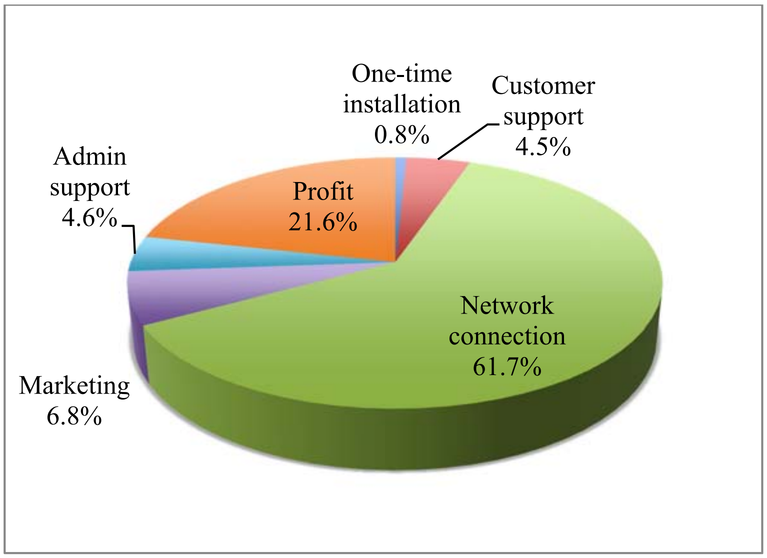
By using Terra Loop's demand data, Matt implicitly assumes that Speedy is a monopoly that faces no competition from firms offering substitute broadband service. His analysis is summarized in row one in the table above. By contrast, I assume that Speedy operates in a duopoly where two firms (Speedy and Timely) offer competing broadband service. My analysis is summarized in row two and I conclude that Speedy should maintain its current price of $39.95.

Given the negative impact of raising price and Speedy's goal of increasing profit, perhaps management should consider a cost reduction. While I am not in a position to make specific cost-cutting recommendations, I thought it might be helpful to classify costs by activity and present a breakdown of revenue by cost categories for management's consideration.

There are four major groups of activities performed by Speedy. These are: (1) install equipment; (2) provide subscribers with an on-going connection to the Internet (connectivity); (3) marketing services; and (4) general administrative support. Please note that I was unsure how to categorize "trouble-shooting and repair costs" as I am unaware if these costs are incurred at the time of installation or after installation is complete. Thus, I have placed "trouble shooting and repair" with "customer support help line" into a separate category called "direct customer support" in the table below.

Costs of Speedy's Business Activities During the Previous Year		
Direct (One Time) Cost of Installation	**Total**	**Per installation***
Signal splitter, modem, and other parts	$856,888	$69.99
Installation labor	674,834	55.12
Total direct installation costs (for 12,243 new customers only)	*1,531,722*	*125.11*
Direct Customer Support (Recurring Cost)		
Trouble shooting and repair	5,452,505	13.36
Customer support help line	3,374,171	8.27
Total direct support costs	*8,826,676*	*21.63*
Direct (Recurring) Cost of Providing Network Connection		
Depreciation on network equipment	15,552,000	38.11
Rent on building housing network equipment	254,000	0.62
Utilities and insurance on network equipment	420,000	1.03
Line charges paid to local phone co. ($20.40/installation/month)	99,902,880	244.80
Salaries of network maintenance staff	2,135,680	5.23
Network administration salaries	2,532,713	6.21
Total cost of providing network connection	*120,797,273*	*296.00*
Direct Costs of Marketing Services		
TV, web, and mail advertising	*13,309,311*	*32.61*
Direct Costs of General Administrative Support		
Amortization of leasehold improvements on building	1,828,680	4.48
Office salaries	6,501,054	15.93
Utilities and insurance for office	35,356	0.09
Office rent	85,000	0.21
Office equipment and supplies	559,067	1.37
Total general administrative costs	*9,009,157*	*22.08*
*Note: Calculated for 408,100 installations unless stated otherwise.		

The pie chart below illustrates the breakdown of Speedy's annual, total revenue of \$195,643,140 (i.e., \$39.95 x 12 x 408,100) by cost categories and profit. The bulk of Speedy's costs (i.e., 61.7%) can be attributed to its primary business activity of providing customers with a connection to the Internet. Further, 82.7% of that connectivity cost comes from the line charges paid to the local telephone company (i.e., \$244.8/\$296). Additionally, as indicated in the chart, Speedy's return on sales is slightly below the industry average (of 25%) at 21.6% (\$3,514,083/\$16,303,595).



I hope my analysis of the proposed price increase; classification of costs; and breakdown of total revenue will be helpful to management. Please let me know if you have any questions or if you would like additional analysis.

Best Regards,

Susan Katz, Marketing Intern
Speedy DSL Corporation

Optional Discussion Questions

After discussing the information available to Susan with your students, you may wish to provide specific questions for greater guidance. Seven discussion questions are provided (in bold font) below, followed by answers. Many instructors have strong beliefs about whether students should be supplied with case questions. Advocates of supplying questions argue that students will not provide enough detailed analysis of case facts to reach an insightful conclusion. Critics counter that students supplied with case questions tend to ignore the "big picture" and treat the case as one long problem set. We have left this pedagogical choice to the instructor by including discussion questions in the instructor's notes but not in the case body.

Q. 1. Calculate Speedy's total revenue, average cost, and total profit for every price given in Exhibit 2.

(a) Is Speedy charging the profit-maximizing price? If not, what is the profit-maximizing price?

Total revenue (TR) is calculated as price (P) x Quantity demanded (Qd). Average Cost (AC) is calculated as Total Cost (TC) divided by Qd. And Total profit is calculated as TR minus TC. The revenue and cost figures are provided in Table 1.

Table 1. Demand and Cost Figures for Speedy, Assuming Pure Monopoly

Price	Qd	Total Revenue	Total Cost	Avg Cost	MC	MR	Total Profit
$43.40	343,957	$14,927,733.80	$11,345,321.20	$32.98	$22.52	$24.90	$3,582,412.60
42.25	365,338	15,435,530.50	11,826,717.99	32.37	22.52	22.60	3,608,812.51
41.10	386,719	15,894,150.90	12,308,114.79	31.83	22.52	20.30	3,586,036.11
39.95	408,100	16,303,595.00	12,789,511.58	31.34	22.52	18.00	3,514,083.42
38.80	429,481	16,663,862.80	13,270,908.38	30.90	22.52	15.70	3,392,954.42
37.65	450,862	16,974,954.30	13,752,305.17	30.50	22.52	13.40	3,222,649.13
36.50	472,243	17,236,869.50	14,233,701.97	30.14	22.52	11.10	3,003,167.53
35.35	493,625	17,449,643.75	14,715,121.28	29.81	22.52	8.80	2,734,522.47

Note: MC = marginal cost and MR = marginal revenue.

Speedy is currently charging $39.95 and earns a total profit (per month) of $3,514,083.42. This is not the "profit-maximizing price" of $42.25 where total profit is highest at $3,608,812.51.

However, these demand and cost figures assume that Speedy is a pure monopoly and thereby faces no competition from alternate suppliers of broadband connectivity. In reality, Speedy faces competition from Timely Cable so the "pure monopoly, profit-maximizing price" of $42.25 (and its corresponding profit level) is not possible for Speedy.

(b) Over the range of output considered, does Speedy exhibit increasing, constant, or decreasing returns to scale? Is this what you would expect of a firm that provides broadband connectivity? Why or why not?

Speedy shows increasing returns to scale over the range of output considered because its average costs fall as the level of output increases. This is expected for a firm that provides broadband connectivity because of the large fixed cost of its network equipment. To provide Internet connectivity, Speedy must purchase an extensive network of servers, routers, and communications software. This represents a fixed (or sunk cost) of millions of dollars. Exhibit 1 indicates that last year's depreciation on Speedy's network equipment was over $15 million.

Q. 2. Calculate the arc price-elasticity of demand when the price for DSL rises from $39.95 to $42.25. Is demand elastic or inelastic between these two prices? Is the demand for DSL more or less elastic than the demand for Internet connectivity (broadly defined)? Explain.

The arc price-elasticity of demand is 1.98 when the price for DSL rises from $39.95 to $42.25. The calculation of arc price-elasticity of demand (εd) is shown below.

$$\text{arc } \varepsilon_d = \left|\frac{\%\Delta Q_d}{\%\Delta P}\right| = \frac{\dfrac{\Delta Q_d}{\text{average } Q_d}}{\dfrac{\Delta P}{\text{average P}}} = \frac{\dfrac{42,762}{386,719}}{\dfrac{2.30}{41.10}} = \frac{0.11058}{0.05596} = 1.98$$

where Δ = change in; P = price; l l = absolute value; average Qd = the average of the two quantity demanded numbers (i.e., Qd = 408,100 when P = $39.95 and Qd = 365,338 when P = $42.25); and average P = the average of the two prices.

Demand is elastic between these two prices because εd = 1.98 > 1. If, instead, εd < 1, then demand is considered to be inelastic.

DSL, cable modem, and satellite service are close substitutes because they all provide high-speed Internet connections. If consumers can now obtain a good substitute (like cable modem or satellite broadcast) for a service (like DSL) whose price increases, they will readily switch. Thus, when the market offers consumers close substitutes for a particular service (like DSL), its demand will become more elastic. The demand for Internet connections (broadly defined) is *inelastic* because we cannot reach the Internet without a physical connection. However, the demand for *any particular type of Internet connection* is more elastic, because other physical connections will work just as well.

Q. 3. The cross-elasticity of demand between Speedy DSL price and Timely Cable subscriptions is 3.49. Does the cross-elasticity suggest a stronger reaction by DSL

subscribers (to a 5.76% price increase) than that implied by the arc price-elasticity of demand (calculated in Q.2.)? If so, explain why.

The cross-elasticity of demand (for Timely Cable subscriptions to a change in Speedy's DSL price) is 3.49. The formula for cross-elasticity of demand (cross εd) is shown below. It can be rewritten to calculate the impact of a 5.76% DSL price increase on the number of Cable subscriptions.

$$\text{cross } \varepsilon_d = \frac{\%\Delta Q_{d\ \text{Cable}}}{\%\Delta P_{\text{DSL}}} = 3.49 \Rightarrow \%\Delta P_{\text{DSL}} \times \text{cross } \varepsilon_d = \%\Delta Q_{d\ \text{Cable}} \Rightarrow 5.76 \times 3.49 = 20.1$$

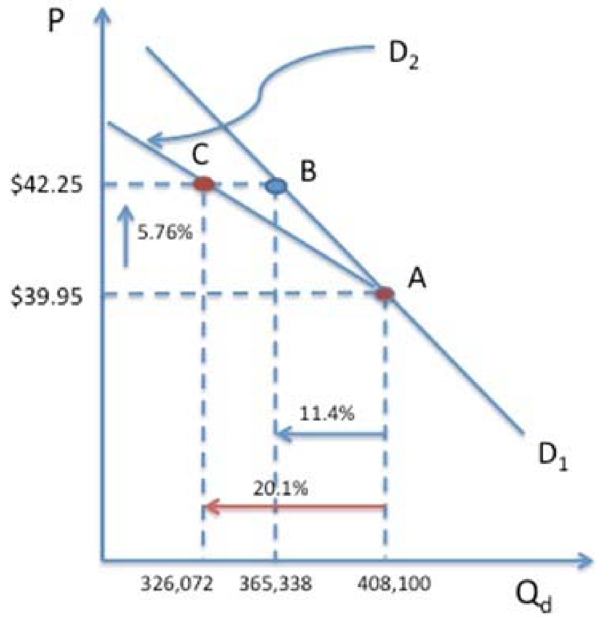
where Δ = change in, P = price, and Qd = quantity demanded. Compared to the arc price-elasticity of demand (i.e., 1.98), the cross-elasticity of demand does suggest a stronger reaction by Speedy's customers to a price increase. The cross-elasticity of demand indicates that a 5.76% increase in DSL price will lead to a 20.1% increase in Timely Cable subscriptions. This represents a 20.1% reduction in DSL subscriptions as 82,028 (i.e., 20.1% x 408,100) customers switch from Speedy DSL to Timely Cable. However, the arc price-elasticity of demand suggests that a 5.76% increase in DSL price will lead to an 11.4% reduction in DSL subscriptions (as shown below).

$$\text{arc } \varepsilon_d = \frac{\%\Delta Q_d}{\%\Delta P} \Rightarrow \text{arc } \varepsilon_d \times \%\Delta P = \%\Delta Q_d \Rightarrow 1.98 \times 5.76 = 11.4$$

This 11.4% reduction in quantity demanded represents a loss of 46,523 customers (i.e., 11.4% x 408,100) versus the loss of 82,028 customers suggested by the cross-elasticity of demand.

Why the difference? Because Speedy does not have a monopoly demand curve (as shown by D_1 in Figure 2). Instead, Speedy faces a more elastic demand curve (like D_2) for price increases because it faces competition from Timely in the local broadband market. The arc price-elasticity of demand is calculated using points A and B on D_1, whereas the cross-elasticity is interpreted using points A and C on D_2.

Figure 2. Price-Elasticity Versus Cross-Elasticity of Demand



Q. 4. There are four major groups of activities performed by this company. These are: install equipment, provide subscribers with an on-going connection to the Internet (connectivity), marketing services, and general administrative support. Estimate the cost of each activity.

Table 2 categorizes the costs of Speedy's major business activities. The main item that students may categorize differently is "trouble-shooting and repair costs." Some may treat it as a cost of providing connectivity service (production cost) and others may treat it as a marketing and support cost. Both answers are acceptable if students provide an appropriate assumption. Under GAAP, if trouble-shooting and repair costs are incurred at the time of installation, then they are part of the installation cost and therefore classified as production costs. If instead, these costs are incurred after the installation is complete, then GAAP accounting rules would treat them as after-sales support and warranty costs and therefore require that trouble-shooting and repair costs be classified as marketing and support costs.

Table 2. Categorization of Cost by Speedy's Major Activities		
Direct (One Time) Cost of Installation	**Total**	**Per installation***
Signal splitter, modem, and other parts	$856,888	$69.99
Installation labor	674,834	55.12
Total direct installation costs (for 12,243 new customers only)	*1,531,722*	*125.11*
Direct Customer Support (Recurring Cost)		
Trouble shooting and repair	5,452,505	13.36
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Direct (Recurring) Cost of Providing Network Connection		
Depreciation on network equipment	15,552,000	38.11
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Salaries of network maintenance staff	2,135,680	5.23
Network administration salaries	2,532,713	6.21
Total cost of providing network connection	*120,797,273*	*296.00*
Direct Costs of Marketing Services		
TV, web, and mail advertising	*13,309,311*	*32.61*
Direct Costs of General Administrative Support		
Amortization of intangible costs (leasehold improvements on building)	1,828,680	4.48
Office salaries	6,501,054	15.93
Utilities and insurance for office	35,356	0.09
Office rent	85,000	0.21
Office equipment and supplies	559,067	1.37
Total general administrative costs	*9,009,157*	*22.08*
*Note: Calculated for 408,100 installations unless stated otherwise.		

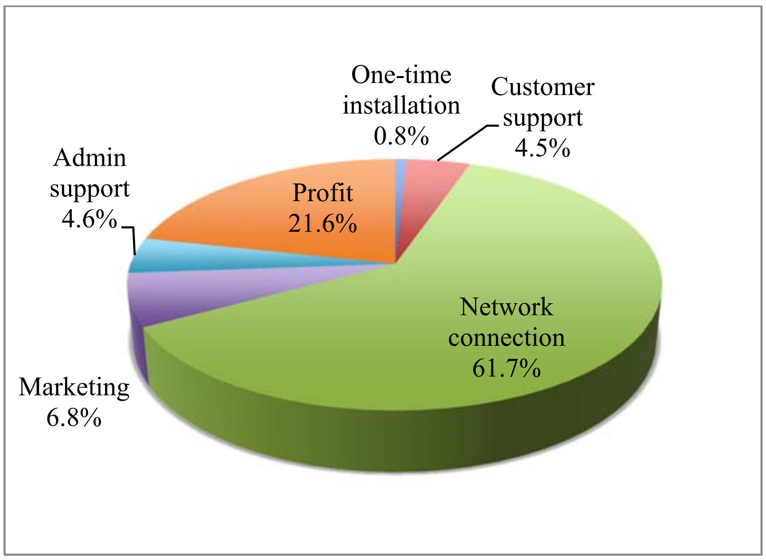
Q. 5. Consider the annual revenue for the company ($39.95 per month per customer). Using EXCEL, prepare a pie chart that shows management the breakdown of total revenue by:

- **(a) One-time equipment installation at customer site**
- **(b) Trouble shooting and technical support**
- **(c) Network maintenance and support**
- **(d) Marketing services**
- **(e) General and administrative support**
- **(f) Profit**

The annual revenue of $195,643,140 (i.e., $39.95 x 12 x 408,100) is split as shown in Table 3 and illustrated in a pie chart, in Figure 3.

Table 3. Breakdown of Total Revenue		
One-time installation (for 12,243 new customers only)	$125.11	0.8%
Customer support	21.63	4.5%
Network connection	296.00	61.7%
Marketing	32.61	6.8%
Administrative support	22.08	4.6%
Profit	103.33	21.6%
Revenue per installation	$479.40	100.0%

Figure 3. Pie Chart Showing Breakdown of Total Revenue



Q. 6. Is the company's profit margin (return on sales) lower than the industry average?

The company's profit margin (calculated as net income/sales revenue) is 21.6% --which is slightly lower than the industry average of 25%.

Q. 7. Based on your findings, would you recommend that Speedy raise price to improve its profitability? Why or why not?

Since total profit equals total revenue minus total cost, we must consider how a price increase will impact both total cost and total revenue. Speedy's management might be tempted to charge the "pure monopoly" profit-maximizing price of $42.25. However, Speedy is not a pure monopoly. It is a duopoly because Speedy faces strong competition from Timely Cable. The cross-elasticity of demand suggests that a 5.76% price increase will lead to a loss of 82,028 Speedy subscribers.

Given this estimated loss of 82,028 customers, total revenue is calculated as ([408,100 – 82,028] x $42.25 = $13,776,542.) This loss of customers (from the price increase) also reduces Speedy's total cost. The reduction in total cost can be estimated by using the constant marginal cost of each customer (i.e., $22.52), or ($22.52 x 82,028 = $1,847,270.56). Thus, total cost is now $10,942,241.02 (i.e., $12,789,511.58 - $1,847,270.56). The price increase (from $39.95 to $42.25) has thereby reduced total profit from $3,514,083.42 to $2,834,300.98. This represents a loss of $679,782.44 in monthly profit. These calculations are summarized in Table 4.

Thus, the price increase will lower Speedy's profits. Intuitively, it is risky for Speedy to raise prices in this duopoly environment. Speedy and Timely each have 50% of the local market and they are close competitors on nearly every aspect of broadband service that customers care about (i.e., price, speed, and reliability). Speedy can expect a large drop in subscribers as many will switch to Timely Cable if Speedy charges a higher price than Timely's price of $39.95.

Table 4. How the Price Increase Impacts Speedy's Total Profit

Economic Model	Price	Quantity Demanded	Total Revenue	Total Cost	Total Profit
Pure Monopoly	$42.25	365,338	$15,435,530.50	$11,826,717.99	$3,608,812.51
Duopoly	42.25	326,072	13,776,542.00	10,942,241.02	$2,834,300.98
Current Price & Qd	39.95	408,100	16,303,595.00	12,789,511.58	3,514,083.42

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NEW PRODUCT INNOVATION AT CHET'S FAN MANUFACTURING, INC. (CFM)

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CASE DESCRIPTION

The primary subject matter of this case concerns the application of target costing, an accounting approach applied during product or process design. Secondary issues examined include using activity based costing data during product and process design, applying entrepreneurial thought and action principles, and pursuing entrepreneurial opportunities within an established organization. The case has a difficulty level of three. The case is designed either to be taught in one and a half class hours and is expected to require about 3 hours of outside preparation by students or in two 75 minute classes with less than 2 hours of outside class preparation.

CASE SYNOPSIS

CFM, established to manufacture and distribute ventilation equipment, was known for superior products, dependable service, competitive pricing, and custom fans. Initially CFM's sales were to original equipment manufacturers of industrial and commercial fans. Seeking growth, CFM entered the residential market with standard fans and blowers to exhaust bathrooms, laundries and kitchens. These products were sold to builders through major wholesalers in Canada and the US. The quality of CFM's products caused Home Depot to offer the company a two year contract for 40,000 basement ceiling fans, sold under Home Depot's brand, and exclusively in their stores.

With adequate capacity, CFM's managers must determine how to design and produce this new product to satisfy both Home Depot and CFM's requirements. Home Depot's customer specifications must be met at a retail selling price of $150, with a 30% gross margin to Home Depot. CFM must earn its required profit margin, which would be impossible without considering cost during design.

This case about a fictitious company and transaction provides students an opportunity to use target costing as an analytical tool for entrepreneurial creation and prediction. Students experience the entrepreneurial concepts of affordable loss, enrolling stakeholders, and working with the means at hand as they suggest ways that profit and cost targets can be met. Through the case, students experience some of the organizational complexity of shaping an entrepreneurial opportunity within an established organization. Students apply target costing's principles from the initial product concept through the design of product and its manufacturing process. They develop an estimate of the product's

cost using activity based costing information and a value index. The case also allows students to consider cash flow consequences of growing sales. Earlier versions of this case have been used successfully in undergraduate planning and control courses at the junior level.

INTRODUCTION

The CFM case describes an entrepreneurial opportunity within a small, established company that is facing slow sales growth. The fictitious transaction between CFM and Home Depot falls into the suicide quadrant of Ansoff's famous matrix, which classifies strategies for achieving growth, because it involves developing a new product to sell to a new market. Risk is high in this quadrant, and companies have to approach these opportunities with disciplined focus to succeed.

Motivation for case development. Target costing offers a disciplined approach to new product development that focuses simultaneously on satisfying customers' requirements while achieving required profit targets. Unfortunately, there are few teaching cases that demonstrate how the target costing process shapes profitable opportunities. This case fills that void. It provides students an introduction to target costing and requires them to apply the process from product concept through the preliminary design phase. Students develop the product's target cost, perform a first look cost estimation, and use activity based costing data and a value index to suggest ways that the target can be met. Through these requirements, students not only learn how to perform the managerial accounting analysis to support new product and process design, but they also experience and explore the entrepreneurial behavior required to shape an opportunity within an established organization.

Class testing and approach. Earlier versions of this case have been used successfully in undergraduate cost management courses at the junior/senior level at Babson College, where we focus on teaching management accounting analysis to support entrepreneurial behaviors in start-ups and in large organizations. Instructors may choose to highlight the entrepreneurial context and discuss elements of entrepreneurial thought and action contained in the case, before delving into the target costing analysis. Alternatively, an instructor can use the entrepreneurial context as a backdrop and focus on how to apply target costing concepts to product and process design and the organizational difficulty of getting others to participate in the process. This case has been developed for management accounting students with a difficulty level of three. Alternatively, it can be used at level five in a core managerial accounting course.

Specific strategy for teaching the case. We offer two specific approaches, one for a 90 minute class; another for two 75 minute classes (this also works for a 3 hour class.)

For a 90 minute class. We recommend that students read the case (which contains a teaching note on Target Costing in Appendix A) and develop the product's target cost, the first look cost estimate, and the value index prior to class. This should require about three hours. If you wish to focus on entrepreneurial behaviors as well, assign students the Saravathy reading, "What Makes Entrepreneurs Entrepreneurial" available online at http://catalogue.polytechnique.fr/site.php?id=537&fileid=6243. This reading is enjoyable and may add another half hour to students' preparation time.

To begin the class, we suggest that students overview case facts; identify the entrepreneurial behaviors exhibited in the case and compare them to Sarasvathy's description in her Note "What Makes Entrepreneurs Entrepreneurial"; and discuss how/why target costing fits into her framework. The instructor may wish to discuss how target costing appears to be a "rational" predictive mode of thinking – which it is – but at the same time it is also a creation form of thinking because it is about shaping the future rather than simply predicting it. From a technical point of view, it is also good to contrast the target costing to a "cost-plus" pricing approach. Spend about 20 minutes of the class doing this; revisit the ideas briefly later in the class as students report results from their analysis and suggest how to design the product.

Next, form student teams and ask team members to compare their calculations and develop a team consensus. Have one team present and defend their calculations. Use approximately 15 minutes of class time for this activity. Ask students to identify how the value index and ABC data might help them develop product redesign ideas, and allow teams to work together for 25 minutes to model different redesign ideas and to develop their suggestion of how to achieve the target. Bring the class back together and ask a team to volunteer their analysis and suggestions. Subsequent teams should volunteer to present different brainstorming ideas about product and process design. Spend about 20 minutes for team presentations and save the last 10 minutes of the class to discuss how Sam Washington will get cooperation within the organization to implement the solutions suggested and capture the lessons that students learned.

For two 75 minute classes or one 3 hour class. We recommend that students read the case, the teaching note on Target Costing in Appendix A, and the Saravathy reading, "What Makes Entrepreneurs Entrepreneurial" and note the ways that her description of entrepreneurial behavior is exhibited in this case. This should require less than two hours of preparation time outside the class.

To begin the class, we suggest that students overview case facts; identify the entrepreneurial behaviors actions exhibited in the case compared to Sarasvathy's description; and discuss how/why a target costing approach is appropriate for this context. Spend about 20 minutes of the class on this discussion; revisit the ideas briefly as students report results from their analysis.

Next, form student teams to analyze the product's target cost, estimate the cost of the product based on the preliminary design and compute the cost gap. Allow teams about 20 minutes to do this. Have two teams present and defend their analysis; one team should present and defend their calculation of the target cost and the other should focus on the estimate of the product as designed. Use approximately 20 minutes of class time for this activity. Spend the last 15-20 minutes of the class to capture lessons learned and to set up the second class period. Assign teams to develop a value index for the case prior to the next class.

At the start of the second class period, ask students to discuss what Target Costing tools are available to drive brainstorming to achieve the target cost (a value index and ABC data in this case) and to identify the information needed to perform this analysis. A short discussion about getting others to cooperate in a target costing team should be included. This conversation should take about 15 minutes. Ask teams to work together for about 25 minutes to perform the required analysis and develop their suggestions of how to achieve the target. Bring the class back together and ask teams to volunteer their analysis and suggestions. During the first team's presentation, reach class agreement on the value index calculations and how to interpret and use ABC data. Subsequent team presentations should be shorter and only provide different brainstorming ideas about product and process design. Spend about 20 minutes for team presentations. After the teams have presented, use the remaining class time to discuss how Sam Washington will get cooperation within the organization to implement the solutions suggested and capture the lessons that students learned.

CASE OVERVIEW

CFM, established to manufacture and distribute ventilation equipment, was known for superior products, dependable service, competitive pricing, and custom fans. Initially CFM's sales were to original equipment manufacturers of industrial and commercial fans. Facing slow sales growth, they entered the residential market with standard fans and blowers sold in the US and Canada to builders and contractors through wholesale home building supply companies. This case presents information about an opportunity they have to enter a new market with a new product, potentially growing both sales and profits. The case allows students to use target costing to approach that entrepreneurial opportunity.

Facts that students should identify during the class overview

Home Depot offered CFM a two year contract for 40,000 basement ceiling fans, sold under Home Depot's brand, exclusively in their stores, and designed to their customer specifications for a $150 price point. CFM can sell the product in other markets under CFM's own brand.

Home Depot's terms included a provision that Home Depot must earn 30% gross margin on their sales to customers, a requirement that CFM arranges and pays for customs and transportation to a Home Depot US distribution hub, and a requirement that CFM must accept Home Depot's one year "no questions asked" warranty policy, which probably means a loss of about 3% of CFM's sales revenue. Further Home Depot specified delivery of 10,000 fans in the first and third quarters of each year, and stated that they would pay CFM 90 days after delivery.

This fan represents a new product for CFM because it becomes part of the basement décor, moves more air than their other fans, and is installed by the homeowner. CFM's existing residential products are exhaust fans or blowers for use in kitchens, bathrooms and laundry rooms and are standard products, not decorator type items, and are installed by experts.

CFM has the "know how" and the capacity in its manufacturing facilities for standard fans.

Home Depot represents a new type of customer. Home Depot is much larger than CFM, so it has power over them in the deal. Big box retailers provide customers wide product variety, low cost, and accept returns without question. This is a marketing environment that CFM hasn't operated in before.

CFM's sales currently are at the $100 million level and have been growing slowly. This proposed transaction provides meaningful sales growth (they haven't calculated the amount yet, but should be able to recognize it is large), but more importantly, Home Depot's offer provides a less risky way to explore whether or not CFM wishes to be in this market. This transaction "de-risks" the exploration of a whole new, large market for them. This market has growth potential for CFM.

CFM's existing managers were unwilling to take on this entrepreneurial opportunity and want to hire someone with expertise in the retail market. The case implies that they are not risk takers and may be afraid they will not be able to satisfy Home Depot's requirements and CFM's profit targets of 7% return on sales simultaneously.

The residential product development director, Arjun Patel, recommended a person in his network, Sam Washington, a recent MBA with retail experience and strong financial skills for the job. Sam recognized the scope and risk of the assignment, evaluated it against his desire for entrepreneurial experience, got assurances that Arjun would support his efforts, and accepted the job.

Sam wants to employ target costing, an approach that has not been used by CFM before. That approach requires input and participation from customers as well as different functional area experts within the organization. Sam must get others to engage in the target costing process with him, or he won't succeed.

His friend Arjun is on board, but Arjun has to persuade his engineering team to cooperate. Sam has to get cooperation from Home Depot, who represents the ultimate customer. Exhibit 1 contains customer requirements to assist in the design process. Sam also needs cooperation from Par Supitayaporn, a representative of the Thailand manufacturing facility in charge of production planning, and Alina Baskov, a representative from Finance who supplied information about activities and the cost per unit of driver shown in Exhibit 3.

Sam learns that he pays an overhead charge of approximately 20% of sales revenue for marketing and administration costs; incurs a charge of 1% of sales revenue for financing because of Home Depot's payment schedule; and faces $200,000 in product development charges.

CFM's upper management will evaluate the project's success based on its ability to return 7% on sales.

DISCUSSION QUESTIONS

Optional question. Where does this new product idea fall on Ansoff's strategy matrix?
Students can debate the positioning of the new venture within CFM. From the recommended Sarasvathy reading (p. 7), we find the new venture in the "Suicide Quadrant":

	Existing Market	New Market
Existing Product	OEM – Industrial Fans; Distributors – Residential Fans user: professional	
New Product		Big Box Retailer, do it yourself installer – new Ceiling Fan – Suicide Quadrant

Some students may argue that the product is really just an extension of the residential fan business. That would put it in the new market, existing product quadrant, a much less risky placement. Sam may, in fact, want to persuade others in the organization that is the proper placement of this opportunity so they aren't afraid to go along with him on this venture.

Optional Question. In what ways do you think the challenges faced by Sam Washington are similar to those faced by entrepreneurs who start their own businesses?

The instructor can then guide the discussion around issues such as "risk". While Sam does not face the risk of funding that new startups face – obtaining funds and earning a decent return for the fund providers – he does have his reputation and job at risk. In this respect, he is taking on the same level of risk that an external startup must take.

Another similarity between Sam and traditional new startup entrepreneurs is that he has to calculate his affordable loss from this opportunity. In his case, the affordable loss is the loss of his job which he must weigh against the learning he will get to start his own venture. Since affordable loss is a personal and subjective measure, it is hard to quantify.

A third area in which Sam and a traditional new startup entrepreneur are similar is in their ability to network and get other stakeholders to help them. This is clearly a key to Sam's success as well. Unless he can get the manufacturing, engineering and finance people to work with him, he is unlikely to succeed.

Finally, the use of target costing as a tool is a perfect illustration of "cognitive ambidexterity" that requires entrepreneurs to constantly shift between predictive and creation logics. In the early stages of new product development, target costing requires a creation approach. The product has to be "shaped and molded" to a broadly based market opportunity. For example, Toyota defines itself in the business of moving people from point A to point B – not the car business! It is only after it rules out alternative modes of "moving people" that Toyota decides to build a car. In this respect, Sam is different from a traditional new startup entrepreneur because he is already at a stage where the decision is to produce a fan. If Sam had started at the stage in which the problem was to "move or freshen air", he might have seen the opportunity quite differently and may have decided to create a different product. However, even though the product has been determined, the creation logic is still useful to shape this product to better meet customer needs. The discipline of making the product affordable, on the other hand, requires not only an act of creativity but also a highly structured process of cost prediction at each stage. This is why the practice of target costing requires cognitive ambidexterity -- creation mixed with highly predictive cost estimation.

Optional Question: Which of the characteristics, habits or behaviors of an entrepreneur did you see exhibited in CFM?

The recommended Sarasvathy reading suggests that successful entrepreneurs use "effectual reasoning" (or "creation logic" in Babson's terms) rather than "causal reasoning" (or "prediction logic") that is taught in most MBA programs. According to the recommended reading,

In prediction or causal logic, managers begin with a predetermined goal that doesn't change. Once they have a goal, managers identify the means that they need to achieve it and then elaborately plan how to obtain those resources. Their plan specifies resource needs and forecasts results by time period. (See the discussion around p. 1 of the reading). What this means in the CFM case is that the product design team would get customer requirements from Home Depot and design the product to those requirements. This would become the predetermined goal to achieve. The product manager's job would be to arrange for resources to produce and deliver the product and manage the customer relationship. The finance representative would provide costs using the existing cost structure, and the product manager would specify everything he/she needed to manufacture, deliver, and service the customer.

Through modeling, the product manager would discover that the product doesn't return a profit margin of 7%. More than likely he/she would then suggest that the contract be studied further rather than proceeding. Perhaps he/she would look for other contracts with retailers rather than pursuing the opportunity, because the risk of failure would be high. If the product was placed into production, manufacturing would try to "tweak" the manufacturing process to make the process cost less, and purchasing would try to source materials more cheaply. Unfortunately, most of the costs would have been designed into the predetermined product, and the profit goal probably would never be achieved.

"Effectual reasoning, however, does not begin with a specific goal. Instead it begins with a given set of means and allows goals to emerge contingently over time from the varied imagination and diverse aspirations of the founders and the people they interact with." (p. 2) In this case, Sam and Arjun would work with the customers' requirements, the excess capacity on the production line, and activity costs per driver, and figure out how to design a product within their means. They would realize that there are probably multiple designs that would work, and they would accept the challenge of creating with what they have.

Entrepreneurs also have other means that they exploit (p 2). They understand and use their own abilities, preferences, and network. Point out to students that during their review of case facts, they identified how Sam and Arjun had engaged in identifying and using these means effectively.

Additional distinctions between the principles of causal and effectual reasoning are suggested in the Sarasvathy reading (p. 4):

"Whereas causal reasoning focuses on expected return, effectual reasoning emphasizes affordable loss."

"Whereas causal reasoning depends on competitive analysis, effectual reasoning is built on strategic partnerships."
"Whereas causal reasoning urges exploitation of pre-existing knowledge and prediction, effectual reasoning stresses the leveraging of contingencies."

The CFM case provides an opportunity for students to test these distinctions:

While CFM clearly has an expected return for the new venture, the venture is a very "affordable loss" for both CFM and the new product manager, Sam Washington. For CFM, the new venture represents an opportunity to add approximately $2 million per year in new revenue to an existing revenue base of $100 million. Because Sam is creative, they won't have to acquire a new manufacturing plant, driving up their asset base; they can use excess capacity until they test the market. For Sam Washington, it represents an opportunity to be entrepreneurial and salaried in an environment where his greatest risk is losing his job in three years if the new venture fails.

Sam Washington, new to CFM, has to rely on several "strategic partnerships" to be successful. First, there is the external partnership with Carlos Batista, the Home Depot buyer. Carlos appears from the case to be quite inflexible in his requirements but perhaps over time Sam can loosen him up a little without compromising product requirements. Second are the internal relationships. Arjun Patel, the Development Director for Residential ventilation systems, is an ally; however, he has to convince his team of somewhat reluctant design engineers to go along with the target costing experiment. Alina Baskov, the finance representative, appears to be a collaborative partner though is most likely to be an independent reviewer of all financial matters. Par Supitayaporn is a critical partner for Sam's success but needs to be won over – she was unsympathetic to Sam's questioning of the proposed batch size.

Sam needs to gain these people's cooperation and have them help design the product and process and not simply stick with the first design as a predetermined goal. The team has to be ambidextrous, switching between creative and predictive logics. Sam needs to engage everyone in a process of making and unmaking plans until the team can develop one that best uses the available means while satisfying customers' requirements.

Hopefully, when Sam and his team encounter unexpected results from this venture, they will figure out how to leverage them to develop additional products and gain additional customers. In entrepreneurial ventures, actions taken create unexpected results. This will happen to Sam and his team. What distinguishes entrepreneurs is their willingness to take these "failures" and figure out how to use them to create something of value. Instead of redoubling efforts to accomplish exactly what your original goal was, the goal changes as results emerge.

The conclusion one can draw from this discussion is that Sam has a very difficult job to successfully establish this new venture within an established firm. He needs to use the target costing process and its related activity based costing and value index tools and convince both his external and internal strategic partners to help him be successful.

Question. Develop a target cost and a "first look" manufacturing cost for the product.

The instructor should lead a discussion around target costing's principles, how it differs from cost plus pricing, and provide examples of companies that use target costing (typically those in the assembly industry, including giants such as Boeing and Caterpillar). Following are the requirements:

Required: Calculate the per unit target manufacturing cost for the new ceiling fan					
	$ Estimate	%	%/unit base	Per unit	Amount
Retail Price					$ 150.00
less: Discount for Home Depot		30%	Retail price		$ 45.00
CFM Selling Price					$ 105.00
Design Cost	$ 200,000		40,000	$ 5.00	$ 5.00
Warranty Cost		3%	Retail price		$ 4.50
Marketing & Administrative Cost		20%	CFM price		$ 21.00
Freight	$ 50,000		10,000	$ 5.00	$ 5.00
Interest		1%	CFM price		$ 1.05
Target Profit		7%	CFM price		$ 7.35
Target Manufacturing Cost					$ 61.10

Question. Now that we know that the selling price for the product is $105.00, how important is this product to CFM?

The projected revenue and pre-tax profit for the business based on 20,000 units each year is:

What will the product contribute to CFM revenue and profit?		
	Year 1	Year 2
Units	20,000	20,000
Price per Unit	$105.00	$105.00
Revenue	$2,100,000	$2,100,000
Target profit %	7%	7%
Profit before Taxes	$147,000	$147,000

We know from the case that management has a revenue growth goal and the company has expanded into the residential market to provide growth. This contract with Home Depot provides them a strategic partner, which helps CFM develop a new product and test a new market, reducing the risk of their entrepreneurial activities, and it provides revenue growth of 2.1% ($ 2.1 million/ $100 million.) The contract, by itself, is important to CFM.

Optional Discussion. The contribution to profit before tax doesn't tell the whole story. The marketing and administration cost is a corporate allocation, and while there may be some incremental costs associated with this contract, many marketing and administrative costs will not be impacted by this contract. Therefore it is useful to understand what the business will contribute to these corporate expenses and profits:

Optional Question: What will the product contribute to CFM Marketing & Administrative costs and profits?			
		Year 1	Year 2
Units		20,000	20,000
Price per Unit		$ 105.00	$ 105.00
Revenue		$2,100,000	$2,100,000
Manufacturing Cost	$ 61.10	$1,222,000	$1,222,000
Design Cost	$ 5.00	$ 100,000	$ 100,000
Warranty Cost	$ 4.50	$ 90,000	$ 90,000
Freight	$ 5.00	$ 100,000	$ 100,000
Interest	$ 1.05	$ 21,000	$ 21,000
Contribution to Marketing & Administrative costs and profit		$ 567,000	$ 567,000

Students should recognize that as long as the incremental cost for marketing and administrative activities is less than the $420,000 charged to them annually ($21 * 20,000 units), this product actually makes the company better off by more than the $147,000 contribution to operating income before tax – it contributes $567,000 to cover incremental marketing and administrative costs and operating profit before tax.

The cash flow implications are also important as the 90 day payment term is much longer than normal – hence the 1% interest charge on sales:

Students don't have enough information at this time to estimate cash outflows, although they may try. If they want to do this, have them come back to it at the end when they have an understanding of the product cost.

Optional Question: Show the pattern of cash inflows for the two year contract				
	Q1	Q2	Q3	Q4
Year 1		$ 1,050,000		$1,050,000
Year 2		$ 1,050,000		$ 1,050,000

Next, have students share their estimates of product cost using the activity based costing data in Case Exhibit 3. Before developing the cost estimate, ask students the difference between a "zero" and "first look", making sure that students recognize that the team has already decided that the same technology and manufacturing lines will be used on this product as on their residential product line, so the zero look has conformed to the entrepreneurial adage to use the "means at hand."

What is the first look manufacturing cost of the new ceiling fan and what cost gap exists?				
		Quantity	Cost per Qty	Total Cost
Materials	Blades	4	$ 3.00	$ 12.00
	Motor	1	$ 18.00	$ 18.00
	Shaft	1	$ 6.50	$ 6.50
Overhead				
Schedule/setup	# batches	1	$ 300.00	$ 7.50
Assembly	# parts	35	$ 0.40	$ 14.00
Test/inspect	# units	1	$ 5.00	$ 5.00
Manage material	# unique*# batches	10	$ 21.00	$ 5.25
Manage plant	# unique	10	$ 0.14	$ 1.40
Total estimated manufacturing cost				$ 69.65
Note: units per batch:	40			

For the two activities involving batches, the total cost per batch is divided by the batch size of 40.

Question. What is the Cost Gap?

Estimated Cost	$69.65
Target Cost	$61.10
Gap	$ 8.55

Question. Perform value analysis and create a value index for the proposed design.

The Value Index requires:

Survey results of customer perception of the importance of each fan feature (Case Exhibit 1)
Map of each component's contribution to each feature
Cost of each component as % of total product cost
Calculation of Value Index = Customer Value %/Component Cost %

Students need to combine the information from Exhibit One with information in the case from Arjun's engineering group.

To calculate the Total Value for each component, multiply the component contribution % for each feature by the survey score for that feature (e.g. motor % total value for silent operation would be survey score of 9 times component contribution of 60% = 5.4).

Feature	Survey Score	Component Contribution	
Silent operation	9	60% motor; 40% blades	
Variable speed	7	100%motor	
Install & Low maintenance	6	80% motor; 20% shaft	
Appearance	5	70% blades; 30% shaft	

Feature	Survey Score	Component	Component %	Total Value
Silent operation	9	Motor	60%	5.4
		Blades	40%	3.6
Variable speed	7	Motor	100%	7.0
Install & Low maintenance	6	Motor	80%	4.8
		Shaft	20%	1.2
Appearance	5	Blades	70%	3.5
		Shaft	30%	1.5
Total	27.0			27.0

To complete the analysis, the student needs to calculate % of total cost and % of total value. Calculate the % total cost for each component (e.g. for the blades, $12.00/$36.50 = 32.9%).

Calculate the % total value for each component by adding and dividing by the total (e.g. for the motor, 5.4 + 7.0 + 4.8 = 17.2/ Total 27.0 = 63.7%).

The Value Index is then calculated by dividing % total value by % total cost. As explained in Appendix A, if the Value Index is less than 1, the manufacturer is spending more on that component than its value to customers; if the index is greater than 1, the manufacturer is spending less on that component than its value to customers.

Component	Cost	% Total Cost	% Total Value	Value Index
Blades	$ 12.00	32.9%	26.3%	0.80
Motor	$ 18.00	49.3%	63.7%	1.29
Shaft	$ 6.50	17.8%	10.0%	0.56
	$ 36.50	100.0%	100.0%	

Lead a discussion of what the value index numbers actually show. For the new fan, the Value Index analysis suggests that CFM could spend less on both the blades and the shaft and perhaps spend a little more on the motor.

The remainder of the case requires judgments, because students are asked to provide a recommendation as to whether the team should proceed with the new fan and suggestions for reducing the currently projected cost. There are no correct “answers” to this portion of the case, and students should be allowed to discuss and their ideas and opinions. Push students to support their ideas using the results of modeling and analysis; this case provides an opportunity to practice excel modeling skills.

Use activity based management and value index tools to improve on the first look cost.

Reaching the target cost will require a further manufacturing cost reduction of $8.55 (the cost gap calculated earlier) or 12.3% of the current estimated cost. Hopefully most students will concur that this is close enough for the team to proceed since failure to innovate and grow will likely doom the company in the long run.

The philosophy behind target costing is to design costs out during the planning stage. In this situation there are two opportunities to reduce costs. One is to work with the drivers in the activity based costing system to reduce the use of manufacturing overhead. The other is to deliver customers' desired features and functionality with less expensive parts and subassemblies. Again answers will vary and students should support their ideas by testing their impact on product cost.

First, the team can reduce overhead costs by reducing the cost driver quantities required for the new fan. Possible suggestions include:

Increase batch size – an increase in batch size to 60 would reduce cost by $4.25 as it impacts both the scheduling and managing materials activities. (Note: Since this involves changing the planned production of existing products on the line it may not be implementable until year 2. Can Sam convince upper management that it's okay to achieve less than the 7% target in year 1 if he can reach it in year 2?)

What is the revised manufacturing cost of the fan with batch size of 60?				
		Quantity	Cost per Qty	Total Cost
Materials	Blades	4	$ 3.00	$ 12.00
	Motor	1	$ 18.00	$ 18.00
	Shaft	1	$ 6.50	$ 6.50
Overhead				
Schedule/setup	# batches	1	$ 300.00	$ 5.00
Assembly	# parts	35	$ 0.40	$ 14.00
Test/inspect	# units	1	$ 5.00	$ 5.00
Manage material	# unique*# batches	10	$ 21.00	$ 3.50
Manage plant	# unique	10	$ 0.14	$ 1.40
Total estimated manufacturing cost				$ 65.40
Note: units per batch:	60			

Another suggestion involves reducing the number of unique parts to 8 by using the same screw/washer sets for all three applications – this would reduce cost by an additional $0.98 and perhaps more, if purchasing a larger quantity of the same screw/washer sets entitled CFM to a larger volume discount. Note that the calculations below use both a batch size of 60 and a part count reduction.

Students may share different ideas for reducing these costs such as re-considering the three fan blade configuration as this would reduce the number of unique parts and therefore the cost of those activities with unique parts as a cost driver. When they do, encourage them to iteratively model their ideas. Also have students share how they decided which drivers to address, making sure that they understand how to use the rate per unit of driver to identify the importance of batch size on cost.

What is the revised manufacturing cost of the fan with batch of 60 and 8 unique parts?				
		Quantity	Cost per Qty	Total Cost
Materials	Blades	4	$ 3.00	$ 12.00
	Motor	1	$ 18.00	$ 18.00
	Shaft	1	$ 6.50	$ 6.50
Overhead				
Scheduling/setup	# batches	1	$ 300.00	$ 5.00
Assembly	# parts	35	$ 0.40	$ 14.00
Test/inspect	# units	1	$ 5.00	$ 5.00
Manage material	# unique*# batches	8	$ 21.00	$ 2.80
Manage plant	# unique	8	$ 0.14	$ 1.12
Total estimated manufacturing cost				$ 64.42
Note: units per batch:	60			

Second, the team can focus on the design of product features and the cost of fan subcomponents by using the Value Index they previously created.
Achieving a Value Index of 1 (by multiplying the total cost of components by each component's % of total value) would result in target cost for each component as shown below:

Component	Cost	% Total Cost	% Total Value	Value Index
Blades	$ 9.60	26.3%	26.3%	1.00
Motor	$ 23.26	63.7%	63.7%	1.00
Shaft	$ 3.64	10.0%	10.0%	1.00
	$ 36.50	100.0%	100.0%	

The results contained in the table above are used in practice to provide engineering and sourcing teams a target cost for each of the components that go into the product. For example, the team designing engineering specifications for the motor would be given a target of $23.26 for the motor subassembly.

Finally, students should combine both the activity analysis and the value index analysis to create a target cost for each component and for each activity – one possible solution would be:

		Quantity	Cost per Qty	Total Cost
Materials	Blades	4	$ 2.40	$ 9.60
	Motor	1	$ 19.94	$ 19.94
	Shaft	1	$ 3.64	$ 3.64
Overhead				
Schedule/setup	# batches	1	$ 300.00	$ 5.00
Assembly	# parts	35	$ 0.40	$ 14.00
Test/inspect	# units	1	$ 5.00	$ 5.00
Manage material	# unique*# batches	8	$ 21.00	$ 2.80
Manage plant	# unique	8	$ 0.14	$ 1.12
Total estimated manufacturing cost				$ 61.10
Note: units per batch:	60			

In this proposed solution, the activity cost driver quantities were set as recommended in the ABC analysis; the blades and shaft were set at the costs that resulted in a value index of 1 as shown above but the motor was set at a cost of $19.94 in order to achieve the target cost of $61.10. While this is arbitrary, it was done to show a potential way to achieve the exact target. This results in the following Value Index showing all three components reasonably close to 1.

Component	Cost	% Total Cost	% Total Value	Value Index
Blades	$ 9.60	28.9%	26.3%	0.91
Motor	$ 19.94	60.1%	63.7%	1.06
Shaft	$ 3.64	11.0%	10.0%	0.91
	$ 33.18	100.0%	100.0%	

Since this is a case with limited data and students are not engineers, they are expected to develop ideas that would need to be analyzed further to test feasibility. Students should be encouraged to develop ideas using both product subcomponents and the manufacturing process. Remind them that new prototypes would be shown to Home Depot for reaction. The goal is to introduce students to the idea that by using target costing to create and explore design alternatives, they can engage in, promote and assist entrepreneurial behavior.

ADDITIONAL RESOURCES FOR THE CASE:

If instructors would like additional material to read to prepare for this case, the following are suggested:

ENTREPRENEURIAL THOUGHT AND ACTION

Greenberg, Danna & McKone-Sweet, Kate (2011, November). Entrepreneurial Leaders: You can take five actions to become one. www.LeaderExcel.com

Greenberg, Danna, McKone-Sweet, Kate & Wilson, H. James (2011) *The New Entrepreneurial Leader; Developing Leaders Who Shape Social & Economic Opportunity.* San Francisco, CA. Berrett-Koehler Publishers, Inc.

Sarasvathy, Saras D. (2005), *What Makes Entrepreneurs Entrepreneurial,* Darden Business Publishing, University of Virginia, Case # UVA-ENT-0065 accessed October 25, 2013 from the online version at http://catalogue.polytechnique.fr/site.php?id=537&fileid=6243.

TARGET COSTING

Ansari, Shahid, Bell, Jan and Klammer, Thomas. (2009) "Target Costing: The Next Frontier in Strategic Cost Management" www.lulu.com.

Crow, Kenneth. Target Costing by Kenneth Crow, DRM Associates http://www.npd-solutions.com/target.html accesseed October 25, 2013.

Ansoff's Matrix

Saravathy, Saras. (2008). *Effectuation: Elements of Entrepreneurial Expertise.* Northampton, MA. Edward Elgar Publishing, Inc.

Online at a variety of sites, including: http://ezinearticles.com/?Success-in-the-Suicide-Cell&id=1535460; http://www.quickmba.com/strategy/matrix/ansoff/; http://labs.openviewpartners.com/how-to-be-successful-in-the-%E2%80%9Csuicide-cell%E2%80%9D/; among others.

CIRQUE DU SOLEIL: AN INNOVATIVE CULTURE OF ENTERTAINMENT

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CASE DESCRIPTION

Cirque du Soleil (French for Circus of the Sun) has remained one of the most successful theatrical producers in the history of the entertainment industry. It is a hybrid of circus, acrobatics, and dance performance. Today, the organization has blossomed to 5,000 employees, 1,300 are artists, on five continents. The case is how Cirque du Soleil manages organizational culture and teamwork in a challenging entertainment industry.

It is intended for class study and the application of concepts learned in the classroom and designed to complement knowledge derived from concepts in organizational culture and teamwork.

CASE SYNOPSIS

Despite early financial hardships, Cirque du Soleil (French for Circus of the Sun) has remained one of the most successful theatrical producers in the history of the entertainment industry. What started as a troupe of street performers in Baie-Saint-Paul, Quebec, Canada named Les Échassiers de Baie-Saint-Paul (French for the Wading Birds of Baie-Saint-Paul) has grown into a global entertainment business whose performances have been seen by over 100 million spectators in nearly 300 cities worldwide (Cirque du Soleil, 2013; Hoovers, 2013).

Cirque du Soleil is a hybrid of circus, acrobatics, and dance performance (Berry, Shankar, Parish, Cadwallader, & Dotzel, 2006). It is a multi-level production without the menagerie of exotic animals, yet is one that captures the magnificence of the human form, agility, and creativity. The performers toured the Canadian province of Quebec in the 1980s as a performing theatre troupe. Les Échassiers encountered financial setbacks that were relieved in 1983 when the government of Quebec extended a grant to the troupe as part of its 450th anniversary celebrations of Jacques Cartier's discovery of Canada (Biography.com, 2013). In less than 30 years, the company had over 5,000 employees worldwide, including more than 1,000 artists, and redefined the circus industry (Hoovers, 2013). The company integrated street entertainment, eccentric costumes, and cabaret with its worldly performers and artistic shows, winning the hearts of millions of spectators worldwide.

While Daniel Gautier was the financial and production manager, Laliberté was responsible for all creative elements of productions and performances. Initially, Cirque employed only 73 people, yet by 2001, that number had grown to 2,100 employees worldwide, 500 of whom were performers (Hoovers, 2013). Between 1984 and 1989, Cirque performed only one show at a time. Today, the organization has blossomed to 5,000 employees, 1,300 are artists, on five continents (Cirque du Soleil, 2013). The productions are divided into groups designated as Resident and Touring. Resident indicates occupancy of one location, whereas Touring indicates visiting different cities. Cirque had eight Resident locations in Las Vegas and one in Orlando, Florida. The ten Touring productions can be found across five continents. Of these, five are under the Big Top and five are in arenas (Cirque du Soleil, 2013). The International Headquarters in Montreal is home to 2,000 employees, administration offices, creative laboratories, artisans, and expert performers.

As the company traveled across the U.S. and Europe, the success of the organization grew, but not without managerial and organizational disputes, including "artistic rebellions" and partnership clashes (DeLong & Vijayaraghavan, 2002). Furthermore, given that no global entertainment competitor is on par with Cirque du Soleil, the company has to make strategic decisions as it embarks on its third decade in business.

Cirque management was aware of the fact that whiles their high-end market disruption strategy, which shifted their competitive focus from head-to-head competition to the creation of a brand new entertainment industry. Cirque was also aware that this new market creation strategy might generate new players who may possibly compete for same scarce resources in the future and present new challenges.

Given that no global entertainment competitor has ever been on par with Cirque du Soleil, the company must make strategic decisions as it embarks on its third decade in business. Pivotal questions were:

> *"How can Cirque maintain its high creative standards and expand its appeal to a larger audience?" And "How does Cirque stay loyal to its original values while continuing to move forward?"*

Since everyone will be shooting at Cirque, leadership needed to pro-actively respond to possible future threats from competitors in order to preserve its success.

Keywords: Cirque du Soleil, Cirque, Les Échassiers de Baie-Saint-Paul, Organizational culture, Teamwork, Norms, Values, and Entertainment Organization.

INSTRUCTORS' NOTE

This case is intended for both undergraduate and graduate courses in management and organizational development. It is intended for class study and the application of concepts learned in the classroom and designed to complement knowledge derived from concepts in organizational culture and teamwork. The provided case details could easily help the instructor add more relevant questions if needed.

Answers to the questions in the case will derive from what students learn from theories and concepts. At the completion of this case, students will be able to:

1. Compare and contrast the differences between values and norms and their importance as the building blocks of organizational culture.
2. Illustrate and appreciate how a company's culture is transmitted to employees formally through its socialization practices or informally through its on-the-job-learning.
3. Understand and discuss the factors shaping organizational culture and the differences among cultures.
4. Identify and appreciate the relationship that national culture has on the culture of the organization.
5. Analyze and appreciate why teams are important for organizational innovation.

SUGGESTED CLASSROOM APPROACHES TO THE CASE

1. Introduction of the Case to the Class

It is recommended that the instructor introduces the script two or three weeks before the class discussion (duration: 30 minutes-one hour) and creates teams consisting of 4 to 5 students to study the case and respond to the questions. An early introduction of the case ensures that the students have read and understood the issues of the case. A PowerPoint presentation and a written report of 10-15 pages should address the case questions.

Based on the authors' experiences, requiring a formal response to the questions to help students enhance their written communication skills is a good approach. Please note that this formal write-up of the case requires the instructor to read and grade the students' work more critically.

Finally, instructors should have enough copies of the script with its instructions to distribute to students at least three to four weeks before the class discussion.

Answers to the questions in the case will derive from what students learn from the course concepts, textbook, and outside reading material. The case is to be completed and presented for class discussions.

2. Forming Groups

At least a week before the class discussions, students will be encouraged to network and get to know fellow students in order for them to decide with whom they want to team. Allow 10-15 minutes towards the end of the class meeting to submit group members' names. Students need to form a group of up to five students to conduct this required study.

3. **Process**

Each group will start working on this case after the instructor introduces the subjects of organizational culture, work, groups, and teams.

Students are expected to develop and build their responses (as a group) based on their acquired knowledge. It is recommended that the instructor address and clarify case questions ahead of time with the class.

4. **Use of PowerPoint and Audiovisuals**

It is recommended that students be encouraged to create an effective group presentation. This can be achieved using a variety of audio-visual materials, including but not limited to PowerPoint. The case itself does not come with a video.

5. **Group Report and Presentation**

Each group is required to write at least a 10-page report (12-point font, double-spaced and using the APA writing style). One report is needed for each group with relevant and substantive answers. Additionally, each group is required to prepare a 15-20 minute PowerPoint presentation explaining its answers. Students are required to use the chapters assigned for the course.

To support their responses and enhance their reports, students must include outside references such as books, journals, newspapers, internet information, or a direct interview as resources for the case answers (in case of an interview, they need to include the interview questions as an appendix of the report).

6. **Recommended Outline**

The structure of the written report is critical. In the first part of the case write-up, students should provide salient points of the case before proceeding to answer the case questions.

In the second part of the case write-up, students present their answers and recommendations. Instructors need to encourage students to be comprehensive in their answers, and make sure that answers are in line with the previous ones so that they fit together and move along logically.

7. **Starting the Class Discussion**

Before engaging in a class case discussion and conducting presentations, it is recommended that you remind students that they might disagree with the points that are being made by other students and that this disagreement is healthy and should not be taken personally.

8. **Analysis**

Since this case is an application of topics covered in the subjects of organizational culture and teamwork, students' understanding of these concepts will be essential.

9. **Content and Grading**

Students' answers and presentations should clearly and concisely demonstrate their knowledge and comprehension of the subject concepts learned, as well as the individual or the group's ability to apply knowledge learned in class and through research (synthesize, analyze, and evaluate his/her/their work). Students will be graded based on the following criteria: (a) The use of innovative and creative ideas, (b) the application of concepts learned in the class, and (c) the use of outside research to support the case.

The recommendation is that this case study constitutes 10-15% of the student's participation grade.

CASE RESEARCH METHODOLOGY

The case is based on primary (i.e. interviews with corporate officials) and secondary research (i.e. published articles, databases, and other published materials).

DISCUSSION QUESTIONS

1. Based on your reading from the case and the chapters, in what ways does Cirque du Soleil try to create strong organizational values and norms? What affects do these values and norms have on employees' behavior?
2. Assume that you are the CEO of Cirque du Soleil. What are the basic cultural challenges you face as your organization continues its talent searches and performs in the global arena? Give some specific Cirque du Soleil related examples.
3. Define organizational socialization and briefly discuss socialization tactics. How does Cirque du Soleil socialize new members (and performers)? Do you think what they are doing helps newcomers learn their culture better?
4. Based on your readings of this case and on the subject of culture, how does the national culture affect the culture of Cirque du Soleil or other organizations? Discuss Hofstede's national and cultural differences.
5. What factors shape the Cirque du Soleil culture? Why do organizations have different cultures?
6. Explain and support your explanation of why teamwork is a source of Cirque du Soleil's competitive advantage. Why are teams important for Cirque du Soleil's innovation?

POSSIBLE ANSWERS TO DISCUSSION QUESTIONS

NOTE: The following answers provide only guidelines that are designed to assist in the case analysis process and engage students in critical thinking. These guidelines are not intended to be rigid. Therefore, each question is intended to raise issues that will be helpful in analyzing and resolving the case.

Students must be reminded that their answers to the case discussion questions should be well reasoned and supported with evidence/research when applicable. Although there is no best answer to the discussion questions, some answers might be more appropriate than others might. Furthermore, students should be told that simplistic answers are not satisfactory answers.

1. **Based on your reading from the case, in what ways does Cirque du Soleil try to create strong organizational values and norms? What affects do these values and norms have on employees' behavior?**

Answer: In order to understand how Cirque creates strong organizational values and norms, it is important to first understand what Cirque has established as its values and norms. Norms are defined as the acceptable standards of behavior shared by a group. This is expanded upon in business through a very common group norm within a company known as a performance norm. Work groups provide members standards such as how hard the employee should work, how to best get the job done, what is the expected level of output, and for example, what level of tardiness is tolerated. Other types of norms include appearance norms, social arrangement norms, and resource allocation norms (Judge & Robbins, 2009).

A review of the organizational values and norms at Cirque du Soleil clearly indicates that the company takes good care of its artists/employees, and the employees appreciate it. This unique organization with its one of a kind talent pool and performance magic has values and norms that are unique to this industry. One example of how Cirque created strong organizational values and norms was explained by Alison Crawford, artistic director for "Dralion." Ms. Crawford said that many of the artists loved performing for Cirque because of the travel experience, rather than "in spite of it" (DeLong & Vijayaraghavan, 2002, p. 6). Traveling can be a drain on any type of business – being away from one's family and familiar surroundings is difficult and can have a negative effect on performance. However, at Cirque, all of the artists gave their hearts and souls to the audiences while on tour, and even though they were far away from their native homelands of Russia, South America, and China, they formed deep friendships, despite language barriers and cultural differences.

This can be attributed to the organizational value of caring about the individual artists and accommodating different cultural norms. While the diversity of the employees adds to the creativity of the shows, the employees must be open to working with people from all different countries, learning about new cultures, and traveling to and living in different countries around the world. In the traditional circus world, performers are not given much in the way of employee benefits, but at Cirque, the artists have excellent benefits and part of the norms and values of the company are to treat them exceptionally well. The performers are provided housing and food when they are on location for a show. Cirque du Soleil hires a renowned chef to manage its international cooking needs, providing foods from all over the world so the performers feel at home.

The home offices in Canada have training facilities with elaborate and large gyms, dance studios, and weight rooms. Cirque du Soleil organizational values are dedicated to supporting its performers to the extent that it has enlarged the studio and training spaces three different times over the past 25 years. The performances are extremely physically demanding necessitating the need for physical therapists and trainers on staff to assist all the performers (DeLong & Vijayaraghavan, 2002). Vincent Gagne, who served as tour director at one time, emphasized to his staff that they were there to serve the artists.

Different from the norms of most companies, Cirque did not have a termination policy in place until Marc Gagnon was asked to create one in 1989. True to the passionate nature of performers, it was common for artists at Cirque to be fired and re-hired for better positions in the company. Gagnon noted, “If we told our employees what to say or how to say it or whether they can get tattoos, we would be finished” (DeLong & Vijayaraghavan, 2002, p. 7). Gagnon maintained open communication with all of the staff and artists and established a sense of family and community while on tour. Since Cirque is a company comprised of performers with a culture of fun as well as hard work, Gagnon also hosted many parties for the artists while on tour. The values and norms that promoted communication between artists who spoke different languages and came from various cultures, along with the sense of a family environment, promoted a positive and successful environment at Cirque, especially during hard times on tour.

2. **Assume that you are the CEO of Cirque du Soleil. What are the basic cultural challenges you face as your organization continues its talent searches and performs in the global arena? Give some specific Cirque du Soleil related examples.**

Answer: While students’ answers will vary, it is important to stress that Cirque du Soleil has grown into a global entertainment business in less than 30 years. Performances have been experienced by over 100 million spectators in nearly 300 cities worldwide. The company has over 5,000 employees worldwide, including more than 1,300 artists (Hoovers, 2013). Therefore, globalization and a diverse workforce is no stranger to this global organization. The basic cultural challenges posed to the CEO and upper management includes values, symbols, beliefs, and language.

While cultural values and beliefs are often unspoken, they may be taken for granted by many who are not culturally familiar and who live in a particular country. Usually cultural differences do not pose challenges to management when cultures are similar (Griffin, 2008). In reality, challenges occur when cultures are dissimilar or there is little overlap between performers or employees’ culture(s). For instance, when working with the Japanese, many managers came to realize that “hai” (pronounced “hi”), which translated to “yes” in English, did not always mean “yes” in Japanese. Similarly, arriving late to a meeting in some cultures does not constitute “disrespect, but is a simple reflection of different cultural values (Newsweek, 1997). Other cultural differences have a big impact on belief and business practices. For example, Islam teaches:

> That people should not make a living by exploiting the misfortune of others; as a result, charging interest payments, for example, is seen as immoral. This means that in Saudi Arabia there are few businesses that provide auto-wrecking services or tow stalled cars to the garage (because that would be capitalizing on misfortune), and the Sudanese banks cannot pay or charge interest. Given these cultural and religious constraints, those two businesses—automobile towing and banking—do not seem to hold great promise for international managers in these particular countries. (Griffin, 2008, p. 133)

Additionally, language can be a big cultural challenge. In fact, often a major communication barrier between management and the performers who speak different languages exists. Understanding and giving instructions is not always easy and requires translation and interpreters' services. Subtle differences in meaning can pose another challenge too. An example of such a subtle difference is the time when Chevrolet first introduced its U.S. model "Nova" in Latin America. General Motors executive management did not understand its poor selling performance until they learned that "Nova" in Spanish (pronounced "no vá") means, "It does not go" (Griffin, 2008, p. 133). Many other subtle differences exist that require managers and management to be careful and not make quick judgments.

Finally, symbols including the size of the offices and living spaces, the quality of the furniture, or the availability of parking spaces might signify major cultural differences. Additionally, colors signify different things to different cultures. While in the U.S. the color pink is associated with femininity, yellow is the most feminine color in different cultures (Griffin, 2008).

Organizational norms and values serve to engender a culture of family and teamwork. Cirque du Soleil is doing a superb job in responding to the challenges posed by different cultures. For instance, the company understands the value of human companionship when talent is acquired from remote locations such as small villages in Africa, China, and South America. Cirque's practice is to request at least two friends or family members to accompany the performer to help ease the challenging cultural transition due to changes in language and environment. In addition, language course and educational opportunities are provided for both performers and their children. Troupe parties are also commonplace in the Cirque culture and serve to celebrate diversity. Medical care, transportation assistance, and living facilities are standard benefits that Cirque performers receive. Overall, the Cirque community is made up of diverse and exotic ethnicities working interdependently in an international, communal environment (DeLong & Vijayaraghavan, 2002).

Speaking more than 25 different languages and dialects, artists and performers originate from more than 40 countries. As an organization, Cirque is home to 4,000 employees, 500 of whom are performers (DeLong & Vijayaraghavan, 2002). Thus, given the diversity of merging cultures, communications among recruits and personnel is indeed challenging but certainly not impossible. Add to the mix the complexities of living arrangements and the constant adaptation required on a daily basis, one could easily imagine the critical trust requirements needed when performing highflying stunts with precarious drops and turns. The Cirque culture relies upon strong communication and ethics to bridge any possible cultural differences, building trust between performers living and functioning in close quarters (DeLong & Vijayaraghavan, 2002). Such behavioral norms and values result in the fulfillment and affirmation of family or, at the very least, community.

3. **Define organizational socialization and briefly discuss socialization tactics. How does Cirque du Soleil socialize new members (and performers)? Do you think what they are doing helps newcomers learn their culture better?**

Answer: Organizational socialization is a term used for norm conformity that occurs as a newcomer makes the transition from an outsider to becoming an insider of the individual's new organization (George & Jones, 2012). It takes place when a newcomer to an organization, for instance, learns new norms like working hours, interpersonal relations, dress, etiquette, etc. As an individual adopts these new learned norms, he/she is being socialized into the new organizational culture.

According to George and Jones, (2012), organization socialization tactics require that:

- A newcomer to an organization must learn the values and norms that guide all members' behavior, relationships with all stakeholders (internal and external), and decision-making.
- Learning the culture of the organization: Accordingly, a newcomer must obtain information regarding the organization's cultural values through formal participation in the organization's socialization program or informally via observing and working with other employees. Other learning methods could include mentoring or "shadowing" experienced employees or a "boot camp."

For Cirque du Soleil, an employee's well-developed cultivation is a priority. The preparation of its employees (including performers) to promote their own growth, develop training, culture, sophistication, and collective acculturation is a daily, major task. Certain patterns of behavior have nurtured the building of norms and values of a cognitive performance culture. Laliberté's innovative style and creativity has crowned him a talent harvester and cultivator of people, committed to building others' talent levels while maintaining a stewardship for their physical and emotional welfare. The strategy he developed will continue to be applied to future productions.

4. **Based on your readings of this case and on the subject of culture, how does the national culture affect the culture of Cirque du Soleil or other organizations? Discuss Hofstede's national cultural differences.**

Answer: While students' answers vary, it is important to stress the fact that culture, whether national or organizational, is a product of the values and norms that people use to guide and control their behavior. Furthermore, a national culture is based on a country's values and norms that, in turn, determine what kinds of attitudes and behaviors are acceptable or appropriate. For example, the culture of the U.S. is based on individualistic and competitive social values, capitalistic economic values, and democratic political values (George & Jones, 2012). In the U.S. and elsewhere, peoples' values and norms are relevant to their country's values and norms, and as a result, the culture of the organization is subject to these shared norms and values as well. This set of shared values, beliefs, and norms that constitute the culture of the organization influence the way employees think, feel, and behave towards each other and towards people outside of the organization.

Geert Hofstede developed a model of national culture that argued that differences in the values and norms of different countries are captured by five cultural dimensions of the country (Hofsted, Hofsted, & Minkov, 2010).

These dimensions are:

1) **Individualism versus Collectivism**. This dimension focuses on the values that govern the relationship between individuals and groups. Individual achievement, freedom, and competition are stressed in countries where individualism prevails (such as in the U.S. and most Western cultures). On the other hand, in countries where collectivism prevails, values of group harmony, consensus, cohesiveness, cooperation and agreement are very strong. The Philippines is a good example of a country that would score low on individualism, but high on collectivism (Hofsted, Hofsted, & Minkov, 2010).
2) **Power Distance**. This dimension refers to the degree to which a country accepts the fact that differences in its citizens' physical and intellectual abilities create inequalities in their well-being. It also examines the extent to which countries accept economic and social differences in wealth and status. Accordingly, countries that allow such disparity to occur are labeled as having a high power distance (the Philippines, for example, would score high on power distance) (George & Jones, 2012; Hofsted, Hofsted, & Minkov, 2010).
    a. On the contrary, countries like the U.S. that discourage such gaps between its citizens are said to have low power distance (George & Jones, 2012).
3) **Achievement versus Nurturing Orientation**. A cultural dimension asserting that countries are achievement oriented value assertiveness, success, performance, and competition, and are results-oriented like the United States (George & Jones, 2012). On the other hand, nurturing-oriented countries such as many Latin, Asian, and Middle Eastern countries value the quality of life, care for the weak, service, and the warm personal relationships.
4) **Uncertainty Avoidance**. This dimension highlights those countries that are low on uncertainty avoidance (such as the United States), that value diversity, are

tolerant of differences in what people believe and do, and are easy going. On the other hand, countries high on uncertainty avoidance value conformity to the values of social and work groups and tend to be rigid and intolerant. These countries stress structured situations and are high on uncertainty avoidance, providing a sense of security (George & Jones, 2012).

5) **Long-Term Versus Short-Term Orientation**. This dimension concerns citizens' orientation towards life, work, and if this orientation is long or short-term. A long-term orientation is likely to be the result of values that include thrift and persistence. On the other hand, a short-term orientation is likely to be the result of values that express a concern for maintaining personal stability or happiness and for living in the present (George & Jones, 2012).

Important to mention here is that if the differences in values between countries cause differences in attitudes and behaviors between workers in different organizations or its subsidiaries, global learning benefits will be difficult to attain. Additionally, differences in national values and norms can make partnerships between organizations difficult.

What global organizations must do to prevent the emergence of different national subcultures within the organization itself, or within its subsidiaries, is to be flexible and create a global culture that has the elements of the organization's values and norms, fostering cohesiveness among its operations and divisions. Global managers and teams could be used to develop and transmit shared values to the organization's worldwide divisions. Additionally, the transfer or the rotation of top managers to various divisions (global locations) can also help to foster a more cohesive value system and shared culture.

The authors of this case believe that Cirque du Soleil has an adaptive culture where values and norms are helping the organization grow, build momentum, and change when needed, in order to be effective and achieve its goals.

5. **What factors shape the Cirque du Soleil culture? Why do organizations have different cultures?**

ANSWER: "Organizational culture refers to a system of shared meaning held by members that distinguish it from other organizations" (Judge & Robbins, 2009, p. 551). The system of shared meaning, in essence, refers to certain key characteristics or traits valued by an organization that best exhibit its culture, including common perceptions held by its members. Research on this topic provides seven primary traits that, as a whole, illustrate an organization's culture. To best evaluate the organizational culture at Cirque du Soleil, an analysis of each of these traits and its application at Cirque is discussed.

1) Innovation and risk taking refers to the extent to which employees are urged to be innovative and take risks (Judge & Robbins, 2009). From its inception in the 1980s, Cirque du Soleil was based on a culture of innovation and risk taking. The idea of a circus without animals was the innovation of Guy Laliberté, himself a street performer, and his unique, creative ideas have continued to influence Cirque to this

day. Laliberté's innovation and risk taking are the basis of every employee's dream at Cirque and are visible in the unique productions. At Cirque, the performers encompass a large and diverse group of talented individuals who must work as a team, as discussed in the task interdependence model developed by James D. Thompson. This model highlights the fact that the extent to which an individual performs is directly affected by what each group member does (Thompson, 1967).

Imagine the aerialist hanging in mid-air, hand extended, as she waits for an acrobat to grasp her hand and fling her to the safety of the group on center stage. The degree and intensity of actions and tasks increase among group members when interdependence across group boundaries increases. Such actions may require risks to be taken in terms of both talent and circumstance. To capitalize on the ingenuity of Cirque's innovative ideas, designers, artists, performers, choreographers, and producers must all take risks.

2) Attention to detail refers to the level at which employees are expected to demonstrate precision, analysis, and attention to detail (Judge & Robbins, 2009). This characteristic is present at Cirque in a number of ways, one of which includes the training facilities provided to its performers, allowing their performances to reach a level of perfection. At Cirque's home offices in Canada, there are state of the art training facilities with elaborate gyms, dance studios, and weight rooms. Cirque du Soleil is dedicated to supporting its performers and has expanded the studio and training spaces three different times over the past 25 years (DeLong & Vijayaraghavan, 2002). Because of the physical demands of the performances, physical therapists and trainers are on staff to assist the performers.
3) Outcome orientation refers to the degree that management focuses on results rather than on the techniques used to achieve these outcomes (Judge & Robbins, 2009). This organizational cultural trait does not seem to be a priority at Cirque. Although the performers at Cirque are the best of the best before they are even hired, a critical aspect of the culture at Cirque includes constantly improving upon the creativity of the artists and the excellence of each performance. Although management and every employee must focus on the success of an entire production (i.e. - results), the organization must still concentrate on the isolated, individual skills and talents of each of its performers to achieve successful performances.
4) People orientation refers to the degree to which management decisions consider the effect of outcomes on people within the organization (Judge & Robbins, 2009). This characteristic is one of the strongest traits in the organizational culture at Cirque. The creative freedom given to the artists provides unending opportunities for the development of revolutionary and visually stunning acts. From the company's inception, the paternalistic Laliberté established a work culture at a high-trust level through the maintenance of a comfortable and open working environment for its artistic employees. His global reach helped to leverage a diverse artistic pool that took the best from each region combined into something new and exciting.

The organizational culture revolved around the daily needs of the artists, ranging from accommodations to nutrition, transportation, medical needs, and training sets and most importantly, the voice, look and feel of a particular show. Through people orientation, Laliberté empowered the artists to reach new expressive heights. Imparting their artistic employees with control of their own section of the performance, performers in turn felt a responsibility to and connectedness with each audience. In addition to the physical needs of the performers, Laliberté was also sensitive to the emotional needs of his youngest talent, particularly concerning the traveling shows during which a young artist recruited by Cirque had a friend or relative accompany him during the production's tour. In addition, Cirque's talent scouts recruited sibling acts, as well as entire family acts, to create a semblance of normalcy while on the road. Potential language barriers were addressed by bringing along teachers familiar in French as well as the artist's native tongue (DeLong & Vijayaraghavan, 2002).

5) Team orientation refers to the degree to which work activities are organized around teams rather than individuals (Judge & Robbins, 2009). At Cirque, the organizational culture is very much focused on teams composed of individuals with unique and far-reaching talents who work together on each production from a narrative idea on a storyboard to stage design, choreography, music, engineering, and set development. As discussed in characteristic number one, at Cirque, the performers encompass a large and diverse group of talented individuals who must work as a team, per the task interdependence model developed by James D. Thompson in 1967. This model highlights the fact that the extent to which an individual performs is directly affected by what each group member does (Thompson, 1967). Separate from the work activities at Cirque, after-hours events were arranged with the touring employees, which allowed them to bond over their shared experiences. The team concept was also present in monthly cook offs where an artist from a particular part of the world prepared a favorite regional dish and shared it with the Cirque team. This enabled employees to introduce each other to their customs and habits.
6) Aggressiveness refers to the degree to which people are aggressive and competitive rather than easy going (Judge & Robbins, 2009). The organizational culture at Cirque is such that competition among its artists and its casting directors is not "easy going," but may not reach the description of "aggressive." Cirque du Soleil employs 5,000 employees including 1,300 artists in 100 different occupations representing 50 different nationalities and speaking over 25 languages. A major challenge at Cirque du Soleil is the task of constantly creating new and exciting ideas for performances. This can create a culture of aggressive behavior as employees vie for positions. In addition, casting directors at Cirque are continually faced with finding the right artists to fill the over 20 shows that are currently running.

Management at Cirque du Soleil discovered that trying to manage a team of creative people was not always an easy thing to do. Many disputes by performers broke out as they tried to understand whether management was doing what was best for them (DeLong & Vijayaraghavan, 2002). In the mid-1990s, Cirque tried to decentralize management into three regions, North American, Europe, and Asia. By doing so, important decisions about organizational resources and initiating new projects were left to managers at all levels of the hierarchy. However, this model did not work. In one instance, the company asked Asia to meet the same standards that the North American market was producing. This required Asia to pay employees less and manage costs, which created widespread dissatisfaction. Eventually, all management decisions were recentralized and originated from the Montreal Headquarters.

7) Stability refers to the degree to which organizational activities emphasize maintaining the status quo in contrast to growth (Judge & Robbins, 2009). The tremendous growth and expansion of Cirque du Soleil since its humble beginnings is indicative that stability is not part of its organizational culture. Cirque is the constant innovator of bigger and more illustrious productions and has expanded into different genres over the years. The culture at Cirque is anything but stable.

6. **Explain and support your explanation of why teamwork is a source of Cirque du Soleil's competitive advantage? Why are teams important for Cirque du Soleil's innovation?**

ANSWER: A team is a unit of two or more people who interact and coordinate their work to accomplish a specific goal. Different from a group, the team concept implies a sense of a shared mission and joint responsibility (Daft, 2003). The effectiveness of teamwork is based on productive output and personal satisfaction (Sundstrom, DeMeuse, & Futrell, 1990). These definitions illustrate the concept of teamwork at Cirque and its positive effect on Cirque's competitive business advantage.

As in any business that implements teamwork, the team members must complement each other. All team members should help each other and work in unison. Personal interests must take a back seat and all of them must deliver their best to achieve the team objective. Team members must not argue amongst themselves or underestimate the other members. Organizations have a sales team, administration team, human resources team, operation team and so on. Just as all of the members of a company's sales team work together to achieve the sales target and generate revenue for the organization, all of the members of the acrobatics, musical, choreography, set design, or engineering team must work together to achieve success for Cirque.

The enormous number of talented individuals working in a team format requires interdependence and group performance applications so that everyone can "play together." This requires a concept known as *task interdependence*, a model developed by James D. Thompson to identify task characteristics and effective distribution of outcomes or rewards among group members. Thus, the extent by which individuals perform is directly affected by what each group member does (Thompson, 1967).

The degree and intensity of actions and tasks increase among group members when interdependence across group boundaries increases. Thus, teams are an important part of Cirque's innovative culture because each member of a team is co-dependent on the others for success. A single acrobat is only as successful as the performance of the entire acrobatic team in any given production, just as an individual dancer's performance is dependent on the innovation of the entire dance team.

ENDNOTE

The authors developed the case for class discussion rather than to illustrate either effective or ineffective handling of a management situation. The case is based on secondary (i.e. published) data. *The authors extend their appreciation to Tony Ricotta, Company Manager for Zarkana; Ann Paladie, Senior Publicist; Pauline Fretté, of Cirque du Soleil's department of Global Citizenship; and Cirque's artistic consultant Stefan Haves for their assistance, advice, input, and feedback to the contents of this case.* *Contact person: Issam Ghazzawi, University of La Verne, 190 Third Avenue, La Verne, CA 91750.*

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FAMILY FEUD AT JOHN BLAINE TRUCKING COMPANY, INC.

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CASE DESCRIPTION

The primary subject matter of this case concerns family business estate and succession planning for a small oilfield trucking company. Secondary issues examined include sibling rivalry, conflict management, and the integration of family counseling theory into family business counseling. This case is appropriate for senior and first year graduate students. It is designed to be taught in three class hours and is expected to require three hours of outside preparation by students.

CASE SYNOPSIS

Carolyn Blaine is the recently widowed owner of John Blaine Trucking Company, LLC. She and her deceased husband, Trevor, have five children and two grandchildren between the two of them. The company was founded in 1961 by Trevor's parents and is currently being managed by the third generation son-in-law. Sibling rivalry has been a significant issue since the two married (a second marriage for both of them). The case opens with Carolyn expressing both anger and heartbreak caused by Trevor's death. In a dream sequence Carolyn shows how Trevor's failure to adequately address estate and succession planning, even though he knew he had cancer and was not going to recover, has left her a nightmare situation to deal with. Trevor's mother, one of the original founders of the company, is suing his widow (Carolyn) for an undocumented debt. Carolyn's daughter, Diana, is trying to take control of her and the company and block the other siblings from sharing in any of the financial aspects of the company. More attorneys and accountants have been hired to help straighten out the mess. As the case ends, one of the grandchildren has been seeing a professional counselor and other family members are also seeking these services. Diana has separated from her husband Brad, who is managing the company, and is trying to get Carolyn to remove him from the company. The two grandchildren are also experiencing problems and Diana is relying heavily on Carolyn for help with Nora. Carolyn is overwhelmed with the business and personal issues she is facing and is contemplating taking the family dog and running away.

RECOMMENDED TEACHING APPROACHES

There are several ways that this case can be used in the classroom. The teacher can use the supplemental materials provided in this instructor's note on family counseling theory to provide basic information that students can integrate into the family business area. Also the teacher can have a counselor who specializes in family business counseling as a guest speaker for the class prior to the use of this case. Another guest speaker that can enhance the use of this case is an attorney and/or an accountant who specialize in family business estate planning and succession issues.

The discussion questions which are included in the teaching materials can be used to structure the class case discussion. Alternatively, students could be selected to role play the various scenarios provided in the case to examine the different alternatives available to Carolyn.

DISCUSSION QUESTIONS, ANSWERS, AND SUPPLEMENTAL MATERIALS

1. Discuss the actions that Trevor Blaine took to prepare his company for the transfer of power during the succession process that would take place upon his death.

   CEOs committed to the continuity of his/her family business during the succession process should serve as the architect of the transition plan. There is no one best succession plan due to the unique circumstances surrounding each family business. Ideally, as architects these CEOs understand they need to surround themselves with and utilize the right people to achieve continuity. The "right people" include members of the top management team, board members, and outside advisors. Although there is much research showing the importance of formal succession planning for successful transition, CEOs of family owned businesses tend to have longer tenures than non-family CEOs and they may even be entrenched within the family business and unwilling to leave. This entrenchment can be a serious weaknesses in the ability of family members to continue in the business across generations (Poza, 2010).
   In this case, Trevor did not seek input from anyone but his trusted friend and attorney. When family members questioned him about his succession plans, he always responded that it had been taken care of. It does not appear that he spent time talking with family members about his transition and estate plans. Some students may question whether he spent time in honest reflection regarding what plans would be in the best interest of the family given the family relationships. This is evidenced by the lack of conversation between Carolyn and Trevor regarding succession and transition planning.

2. Discuss which CEO exit type Trevor exhibited in the case.

   There are six identifiable CEO exit styles (Sonnenfield, 1989; Poza, 2010). These include:
   Monarch – believe that no one can replace them; do not talk about succession or set a date for his/her departure; death or serious illness only happens to others; chaos generally follows his/her death in the form of greed and hidden agendas.

General – leave office and secretly plot his/her return; patiently wait for younger successor to fail; anxiously await the day that he/she is called back to office.
Ambassador – exit the business through delegation of operational responsibilities while retaining his/her spokesperson or representational activities.
Governor – define his/her departure date publicly so that they are committed to the transfer of power within a defined period.
Inventor – more creative type that build the business including the infrastructure that will help the next generation make the transition successfully; during the transition the Inventor will start to pursue his/her next dream while serving as a mentor to the next generation.
Transition Czar – most complicated exit style because the CEO coaches the next generation to ensure successful transition as the CEO transitioning out of the organization; difficult for many CEOs to help the next generation move forward in ways that are different than the CEO's so they are helping to change what they have created.
Most students select the Monarch exit style for Trevor, even though he did work with his attorney on his will and provisions for the company. Trevor did not announce an exit date nor did he reveal the provisions with anyone, including Carolyn. None of the other exit styles really apply because he really didn't groom the next generation or formally exit as leader before his death.

3. Discuss the CEO spouse role type best representative of Carolyn's role in the business.
CEO spouses have many roles within the family business. For example, they may serve as the steward of the family legacy, moderator of family relations or facilitator of communication during periods of conflict. They have different levels of influence in the family business based upon the roles that they play. These roles include (Poza, 2010):
Business Partner – help start the business and serve as a partner in the early years and remain as business partner or move on to other roles at some point; advice from this business partner is often sought. This role can provide a lot of benefit for the firm, but, it is complicated and can enable a culture of secrecy to develop.
Chief Trust Officer – trust catalysts in the family business; hold the family business together during the changes that come with evolution of the family business; facilitators, mediators, healers, and source of communication. This spouse appreciates the need for balance between the family and business and can help achieve this by advocating a family first agenda.
Senior Advisor/Keeper of Family Values – ensures children in family businesses grow up with an appreciation for and knowledge of the business and its history, values, and customers. They may have an invisible role in the business which can lead to greater degrees of respect in important family matters.
Free Agent – spouse has a separate identity from the CEO and family business; sometimes believe that others are performing effectively in the family business so his/her input and involvement is not needed.
Jealous Spouse – This role is the opposite of the free agent because the jealous spouse believes that the CEO loves the business more than the spouse. She/he competes for the spouse's attention and affection which can lead to family conflict.

Most students will identify Carolyn as the Chief Trust Officer. This choice is usually supported by the activities that she did during the marriage to try and build relationships with all of the family children and Trevor's mother. She also encouraged Trevor to take time away from the business by planning the short trips that they took.

4. If you were a family business consultant, what advice would you have provided to Trevor regarding estate and succession planning?

   In terms of succession planning, the students can refer to the CEO exit styles given above and talk about which would have been a better role for Trevor to pursue. Many will identify the Governor or Ambassador as roles that Trevor should have used before his illness intensified. Other students will also discuss the infrastructure that Trevor should have put into place to support either of these exit styles including the establishment of a family constitution, family council meetings, processes, policies, buy- sell agreements, etc.

   Estate planning assistance should have been provided by a team of outsiders including an attorney and accountant that specialize in family business estate planning. Trevor could have used the estate planning process as an opportunity to educate the next generation family members and establish a legacy, rather than just the financial assets that are the source of conflict. His focus should have been on ensuring the continuity of the family business since he trusted his son-in-law and ultimately hoped that his grandson would run the business at some point. Unfortunately he allowed guilt and his concept of love to guide his decisions rather than fairness. Also, his lack of communication with his heirs led to his failure to consider each member's needs, wishes, values, etc. led to a less than optimal estate plan for his family.

5. Discuss the importance of a genogram and how it helps a family member understand the family system. Should the genogram provided in the case be altered in any way?

   The genogram is similar to a family tree, but in addition to showing family names, ages, and lineage, the genogram also shows critical family events such as divorce, the quality of relationships, and the values and messages shared across generations (Poza, 2010). A genogram is an important visual that can help family members identify generational issues. It would be important for the family therapist to include aspects of the business as part of the family genogram in order to assist family members in seeing how the business impacts the family on a generational level. Members can see how the family and business may be acting out generational patterns. This tool is also used by family practice physicians to help family members identify and understand relationships and behavior in stressful times.

   Some students will add additional information regarding the relationships and messages shared across generations. The current genogram shows critical family events such as the deaths of Trevor and James, and the divorces that occurred in the family

   To assist faculty members who do not have any counseling background, the following teaching information is included in these Instructor Notes to show how the integration of family systems theory can be included in this case study.

   Using a systems approach, found in the fields of counseling and business, is an important way to view and interrupt or intercept problems occurring in a family business. It would be important for a family business consultant to consider the emotional health of family members and how they interact both within the context of the business and in the home. As well, any family therapist who is working with a family who owns a business should consider how the business is affecting family interactions and relationships and how much of the stress involved in running the business spills over into those interactions and emotional responses to each other in the home. In addition, for some family business owners, there are little if any boundaries between the business and the home especially if the business is based out of the home or if the business is next door to the home. This can add additional stress to an already tense situation.

Hardly any family, much less family business, has failed to feel the economic crunch. Many times, money is the underlying cause of divorce. According to an article in the New York Times (December 7, 2009), couples who disagree about finances once a week are 30% more likely to divorce than couples who argue about money a few times a month. Approximately 45 - 50% of all first marriages end in divorce. The statistics for second and third marriages are progressively more dismal: 60 – 67% and 70 – 75% (www.divorcestatistics.org) will likely end in divorce.

The current economic crisis has done little to relieve the stress of owning a business for most families. Perhaps the head of a family business begins to feels the stress of trying to make money or even make ends meet. Even if s/he tries to keep this information to him/herself, it will spill over in other ways—perhaps yelling at the partner or children with little provocation. Another scenario might be that of a family member who is part owner in the business or works in the business full time and begins to exhibit the symptoms of an emotional disorder. The business will likely suffer as everyone struggles with the situation. Again, it is important to consider therapy along with financial counseling. It would be prudent for any family business consultant to consider a systems approach when working with the members of a family business and include a family therapist if any family members are exhibiting emotional issues.

Family systems grew out of the work of Ludwig von Bertalanffy in the 1920s with his general systems theory. Early family therapists were drawn to this theory because they were looking for a scientific model. Systems theory focuses on the relationship and interactions between members of the family rather than the members themselves (Goldenberg & Goldenberg, 2008).

In order to conceptualize a systems approach, some important concepts for students to be familiar with are: systems (open and closed), subsystems, homeostasis, rules and meta-rules.

An open family system is one that allows interactions to flow in and out of the family. In other words, people are allowed into the family system and members of the family system are allowed to interact with people outside the system. Closed systems, on the other hand, restrict interaction with the outside environment which may lead to isolation and resistance to change. Closed systems cut themselves off from the outside world, control the members' interaction with the outside world, and control who and what is admitted into the home (Goldenberg & Goldenberg, 2008).

Subsystems are parts of the whole system that carry out different tasks or functions. A typical family contains many subsystems—husband-wife, father-child, mother-child, sibling-sibling. Subsystems may be organized in a variety of ways: by generation, gender, and function to name a few. Within subsystems, there are different levels of power, responsibilities and skills (Goldenberg & Goldenberg, 2008). There are no set numbers for how many individuals are in a sub-system at any given time. A change in one subsystem can affect other subsystems. It is important to consider that family members may belong to more than one subsystem at any given time (Pieper & Klein, 2007).

Homeostasis is analogous to stability. It is the system's attempt to maintain balance. If something throws the system off, the system will try to achieve stability again. However, any change, no matter how small, has the potential to affect the family business and members of the organization in some way, whether positively or negatively, and on a large or small scale. If one person in the system changes, the other members of the system are forced to change in some manner as they figure out a way to deal with the person who has changed and interact with them in a different way.

Every family has rules which are stated or overt. However, there are meta-rules that are unstated or covert. Meta-rules are rules about the rules. An example of a meta-rule might be a teenager who figures out she can get whatever she wants from her father after he's had a few drinks in the evening. Nobody specifically says this, but on some level, everyone knows this.

A family therapist can help members of the business and family think in systemic terms, examine relationships and problems, and assist them in identifying dysfunctional relationships (Boverie, 1991) which has far-reaching significance for a family business.

ADDITIONAL DISCUSSION QUESTIONS

6. Identify 3 subsystems in the Blaine Trucking Company.

There are a variety of possibilities that students might suggest:

John, Shelia, Trevor; Trevor, Steve, Jennifer; Steve, Jennifer, Diana; Trevor, Steve, and Brad; Brad, Steve, Diana; Diana and Nora; Diana and Trevor; Brad and Diana, etc.

Once you have identified your sub-system, identify the person with the power in that particular sub-system and what generation the person represents. In what way does the power structure change within the sub-system? An example is the sub-system of John, Shelia, and Trevor. John and Shelia are the generation who started the company. Trevor is the second generation. Initially, John has the power in the sub-system, but when he dies, Trevor assumes the power as he takes over the company and runs it. However, Shelia actually owns the company when John dies. Another example is the sub-system of Trevor, Steve, and Brad. Steve and Brad are the third generation assuming control of the company. Brad is assuming more and more responsibility for the company even while Trevor is still alive. Once Trevor dies, Brad runs the company. Steve has very limited power. In the sub-system of Brad and Diana, while Brad has the power in the company, he may not necessarily have power in the home. Diana seems to assume power in the home as she threatens Brad with leaving him. Brad and Diana are the third generation.

7. Give one example of a situation where Trevor attempts to maintain homeostasis.

Suggested responses:

Trevor does not confront his son, Steve, who is taking advantage of the company financially by stealing and even smoking pot at work. He doesn't confront his son because he doesn't want to have to deal with what happens if he does. Trevor just wants to maintain things as they are rather than "rock the boat".

Rather than confront Diana who rarely works a 40-hour week to earn her salary, Trevor chooses instead to let it slide. It's actually easier for him when she isn't there.

8. Name one instance where counseling might have been beneficial to one or more members of the family.

Suggested responses:

Family counseling might have assisted Trevor and Marilyn prior to their divorce.

Assertiveness training and counseling might help Trevor develop the ability to confront situations that are diminishing the family business such as Steve's stealing and Diana's salary drain on the family business.

Counseling for all members of the family (including Carolyn, Diana, and her children as well as Marilyn and her children) could help all of them cope with Trevor's death and subsequent estate situation.

It is not necessarily family counseling, but a lawyer who specializes in family law could have helped John plan his estate so that the family would not be in the situation of suing each other as they are now which is detrimental to the family business and their relationships with each other.

9. Critical Thinking Discussion Question: What are the implications for the family business when one of the owners/family members has a diagnosed or undiagnosed mental disorder?

Suggested responses:

An undiagnosed family member could cause destabilization of the company to occur and possible loss of revenue, if not failure of the company. In the case of a bipolar owner/family member who spends the revenue when in a maniac phase, the business may suffer huge financial loses that may not be recouped.

If the mental or emotional disorder is diagnosed and the individual is treated with medication and counseling, that can be an important step in helping the family business to regain stabilization and become productive again.

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EPILOGUE

Carolyn and her daughter Diana have been attending counseling sessions separately. Carolyn's therapist is working with her to help her learn how to establish boundaries with Diana. Carolyn has also recently been dating a friend from high school and Diana is very angry with Carolyn about this. At one point their relationship deteriorated to the point that they didn't talk for several weeks. Diana and her therapist are working to help Diana resolve issues from her childhood. Diana has stated that she believes that her mother never really loved her. She and her therapist are exploring issues to try to help Diana understand that she cannot change the past, nor can she change anyone but herself. Diana is spending most of her time in her new business endeavor and visits friends from college that live out of town when she can get away.

Brad continues to run the family business and Trent is currently living with him. Trent is working at the family business in the pipe yard. He has gotten engaged and is taking his work more seriously now. Diana and Nora live separately but Nora stays with her dad periodically. Carolyn also continues to help Diana with Nora when needed. This is a boom period for oil and related businesses in east Texas and the business is performing very well. Brad has started to make some changes in the business including moving the location from the original site selected by Shelia and John to save money and reduce the amount of access Shelia has to the business.

Carolyn continues to work with her new outside advisors to straighten out the business trust. She has been able to buy out the interests of Shelia and Steve, so they are no longer involved in the trust. She is now focusing on the interests of Mary and Tiffany. She would like to purchase their shares of the trust for a fair amount that will also settle their debt to the company.

There are times when Carolyn still wants to sell the business and run away – but she stays to help Brad and the grandchildren.

TINY'S TINY PIES: PIE IN THE SKY

Robert M. Crocker, Stephen F. Austin State University
Marlene C. Kahla, Stephen F. Austin State University
Kristan Royal Smith, Stephen F. Austin State University

CASE DESCRIPTION

Tiny's Tiny Pies has been in Austin, Texas since 1976 but only emerged as a Limited Liability Company in November 2010. Tiny Pies are made with all natural ingredients and without preservatives. They come in a several different sizes including the original 3" Tiny Pies, the traditional 9" Not So Tiny Pies, Teeny Tiny bite size pies, Pie Pops that come in different shapes and on a stick and the 1/2 pint Mason jar pies. These products can be found in Austin, Dallas, San Antonio and Houston, mostly in Central Market stores and they also ship within the contiguous United States. Tiny's Tiny Pies also caters weddings, corporate and other special events and offers cooking and baking classes locally.

Jack Horner is a fictitious millionaire that wants to return to his Texas roots after a 30-year hiatus, but he has no desire to retire. He is actively looking for a business interest that would provide both an opportunity to return to Texas and a daily challenge to grow and prosper in the community. A chance encounter puts him in touch with the owners of Tiny's Tiny Pies and he is now weighing the opportunity to partner with these entrepreneurs.

The case is examined from Jack's viewpoint that he has an opportunity to partner with the current owners, or possibly buy them out altogether. Jack is on a four hour flight from Austin to San Francisco as he reviews basic information about Tiny Pies, the pie industry, and other factors relevant to the investment decision.

CASE SYNOPSIS

This case offers a multitude of teaching opportunities but is centered on Jack's evaluation of Tiny Pies as an investment/partnering opportunity. Jack's analysis of Tiny Pies looks at the products, the buyers, the markets, competitors, and growth potential for the company. This case could easily be turned inside out and challenge the student to evaluate from Tiny Pies' perspective whether or not a partner is desirable.

Students can evaluate Jack's analysis of Tiny Pies and determine whether enough information has been identified to allow for an informed decision. They may decide that additional information is needed.

The case can easily be turned upside down so that the student is challenged to view the case from the owners' point of view. Questions then can address the needs of the business, including, but certainly not limited to, whether or not taking on a partner or selling are viable alternatives.

An undercurrent to the entire case is Jack's familiarity with Amanda. They were good friends in high school but drifted apart over the years. Had fate brought them together again? He felt as if he was home again.

He wants to return to his roots, return to Texas. The fact that he would be working with an old friend is appealing. This will give him an opportunity to actually run the day-to-day operations of a business. He has yet to actually run a company, become a part of the operations.

INSTRUCTORS' NOTES

PREPARATION

Require that students read the case prior to actually addressing the decision points in class. Many business concepts are applicable to the case, i.e., SWOT analysis, market potential, industry investment potential, market growth opportunities, and changing demographics and their impact on the product market.

Teams from two to four students can enhance discussion and presentation of the decision points. When students are thinking of their own ideas and interpreting material, many times they need encouragement from another student or two to verbalize their solutions to a case.

Decision point discussions in class will require at least one-half hour. Students should be encouraged to use the Internet and business resources to verify, validate, and explore alternative solutions to the case.

The material presented throughout the case builds a solid, but incomplete picture of the case, which in itself is an opportunity for discussions. The case is presented with limited information because it simulates Jack's limited access to information while onboard the airplane. This allows students to contribute to Jack's SWOT analysis by supplying additional information that enhances the decision.

DECISION POINTS

1. Current picture via S. W. O. T. of Tiny Pies.

Emphasize the unique roles of strengths and weaknesses, opportunities and threats. Remind the students of the internal characteristics of strengths and weaknesses and the external characteristics of opportunities and threats. Is there enough information to make a decision? What additional information would enhance the decision?

2. Flip the case! Ask students to see the case from the owners' point of view.

Does the SWOT analysis look the same? If different, what are the most glaring differences?

3. Address the emotional issues working in this case. Is Jack's motivation to get back to Texas clouding his judgments? How will rekindling an old relationship affect his judgment? Is this a spur of the moment decision or something that has been building for some time? What roles should emotions play? Is Jack's desire to stay busy indicative of his character?

Point out that Jack has the material resources to do what he wants. He could easily move back to Texas and simply retire. While there is no indication that Jack has any other issues that are driving his desire to get back to Texas, students' can be asked to speculate on other factors that contribute to his motivation. Direct students' toward Maslow's hierarchy of need and ask them to frame Jack's motivation accordingly.

Also, address the impact of emotional decision-making versus rational decisions.

4. Do the pressing needs for growing the business impact his decision making processes? How does the retirement of a partner, i.e., Kit, affect the business?

Essentially, it creates a new business with a significant change in management and possibly processes. Students will need to think about the restructuring of the business, decision making and authority.

5. Flip the case! Assess the various funding options available to the owners including borrowing, taking on a partner, or any other viable funding option.

Students can assume several different alternatives to partnering with Jack Horner.

6. **Can Jack Horner actually run the operations of a business?**

   He focuses on investment opportunities and money management, not the day-to-day operations of the business. Will he be able to participate in actual management of a small business?

7. **What does Amanda think about the opportunity of actually getting to work with Jack? How will this be?**

   She has only worked with her mother all these years. Now that her mother is retiring, she is concerned about the possibilities of working with a new partner, new processes, and new ways of doing things.

8. **Should we market toward the natural product?**

   This decision point will require thinking about society's increasing interest in products that have not been exposed to chemicals and hormones. Many grocery stores have recognized this concern by customers and have separate sections for organic and natural produce and meats. These products demand higher prices that other products, yet the demand for them increases. The students will need to learn more about Millennials to provide answers to this decision point.

THE GROWTH AND DECLINE OF THE NEW REVIVAL PENTECOSTAL CHURCH

Raymond J Elson, Valdosta State University
Beverley J Alleyne, Belmont University

CASE DESCRIPTION

The primary subject matter of this case is organization and taxation issue affecting a nonprofit organization. The case is appropriate for a senior or graduate level government and nonprofit accounting course. It could be used in the nonprofit portion of the advanced accounting class. The case is designed to be taught in one class hour and is expected to require approximately three hours of outside preparation by students. The events described in this case are based on real world experiences, but all names have been disguised.

CASE SYNOPSIS

The case concerns the humble beginnings followed by the rapid expansion and subsequent decline of the New Revival organization. New Revival Church ("the church") started as a small congregation in Brooklyn, New York. The church grew based on the charisma of its young minister, Pastor Thomas. The minister created an oversight board, the Board of Elders, to provide structure and to make decisions on behalf of the organization. However, decisions such as the building of a new church building, the expansion of New Revival through the creation of daughter churches, and the acquisition of bank loans, were made by the minister without prior board approval. The case demonstrates the challenges faced by some nonprofit organizations especially religious organizations, when management control is centralized and the corporate governance structure is either ineffective or nonexistence.

INSTRUCTORS' NOTES

RECOMMENDATIONS FOR TEACHING APPROACHES

The objectives of the case are to help students understand (a) organizational and taxation issues that could impact nonprofit organizations, and (b) the importance of corporate governance and specifically, the role of the board of directors, in nonprofit organizations. This case is flexible and could be used in a number of courses at the senior or graduate level. For instance, it is ideal for a discrete government and nonprofit accounting class or the nonprofit portion of the advanced accounting class. It could also be used in auditing and strategic management courses to supplement a discussion on corporate governance. Students may need to supplement classroom discussions by researching applicable nonprofit organization and taxation issues in the Internal Revenue Code or other third party sources. The references provided at the end of the teaching note could serve as a starting point.

The case is best completed in groups either as an in-class or out of class graded assignment. The group size, grading scale and assigned points is at the specific instructor's discretion. If completed in class, the case should be read prior to class by the students and the discussion questions answered in class. It should take approximately one hour to complete the discussion and no advanced preparation time is required by the instructor.

LEARNING OUTCOMES

Students should be able to:

1. Identify the organizational and tax reporting issues in nonprofit organizations especially religious organizations.
2. Understand the distinction between the classification of personnel as employees versus independent contractor and the resulting tax implications
3. Understand the importance of an effective governance structure (e.g., an oversight board and internal controls) in nonprofit organizations.

CASE IMPLEMENTATION AND EFFECTIVENESS

The case was tested using graduate government and nonprofit accounting students during the summer 2013. Overall, students found the case interesting and easy to read. They also noted that the action steps were clear and that it should be easy for the typical student to answer them. One student commented that "the case provides an excellent example of what can happen to an organization lacking proper internal controls…it's a great case that incorporates a lot of what we discuss in both auditing and GNP." Another student noted that "I found the case to be very interesting. It was entertaining, and I found myself wanting to read more about the church and the minister behind it all." Finally, a student commented that ""I found the case very interesting. While reading, I could easily identify areas in which the church lacked proper procedures…It was a pleasure to read.

DISCUSSION QUESTIONS AND ANSWERS

The following are proposed solutions to the discussion questions in the case. The answers are not intended to be all inclusive.

1. How should the church be established for tax purposes?

Churches qualify for exemption from federal income tax under Internal Revenue Code [IRC section 501(c)(3)] and are generally eligible to receive tax-deductible contributions. This tax exempt status must meet specific requirements:

- The church must be organized and operated exclusively for religious purposes.
- Net earnings may not inure to the benefit of any private individual or shareholder.
- No substantial part of its activity may be attempting to influence legislation.
- The church may not intervene in political campaigns, and
- The church's purposes and activities may not be illegal or violate fundamental public policy.

Although churches do not have to apply to the IRS for tax-exempt, it is still advisable to do so because it assures members and other contributors that the church is recognized as exempt and qualifies for related tax benefits.

As a tax exempt organization, the church should have an Employer Identification Number (EIN), whether or not the organization has any employees. The EIN should be used on bank accounts and other church related arrangements. New Revival never applied for tax exempt status and the case is silent on whether it has an EIN.

2. Was the classification of the administrative secretary correct, i.e., was she an employee or independent contractor?

The classification of the administrative secretary initially as an independent contractor was incorrect. Ms. Morgan performed duties consistent with being an employee and reported directly to the Minister. There is an IRS test that can assist in determining the status of a worker. The IRS test often is termed the "right-to-control test" because each factor is designed to evaluate who controls how work is performed. Under IRS rules and common-law doctrine, independent contractors control the manner and means by which contracted services, products, or results are achieved. The more control a company exercises over how, when, where, and by whom work is performed, the more likely the workers are employees, not independent contractors.

As an employee, the church is therefore responsible for deducting the applicable income, social security, and Medicare taxes from Ms. Morgan's pay and timely submitting these taxes to the appropriate government authority. Additionally the church will be responsible for paying payroll taxes on Ms. Morgan's behalf.

3. How effective was the board of elders in their oversight of the church?

The oversight of the church makes it financially vulnerable. Some of the issues in the case are as follows:

Operational

- The minister is the sole decision maker regarding the church's operations.
- No procedures are in place for handling the unpaid pledges.
- There is no evidence of formal training provided to the administrative staff to properly perform administrative functions (e.g. payroll).
- No management authority given to the individual pastors of the four sister churches.
- The Board of Elders may be influenced by the presence of Ms. Thomas on the board which could impact their independence.
- Downsizing eliminated any segregation of duties that existed among the administrative staff.
- The change orders for the construction were made exclusively by the minister without the input of the Board of Elders.

Financial

- The minister as the sole authorized signatory on the bank account and appears to be the "owner" of the loan. No approval from any other members.
- The minister having total control over the finances of the sister churches.
- Inconsistency in completing the financial statements required by the bank.
- The construction loan initially in arrears and now being called by the bank.
- No formal financial statements provided on a regular basis to members.
- No input from the Board of Elders in preparing the financial statements.
- No written copy of the financials provided to Board of Elders or members.
- The "calling of the loan" eliminated future funding.

4. Did the organization expand too quickly with the new building and daughter churches?

It appears that the organization expanded too quickly. Over a short period of three years New Revival started four churches, with two starting in the same year. This prevented them from thoroughly evaluating and identifying any issues that may have been corrected in subsequent churches. It was difficult to determine whether these sister churches were independently successful. Each new church required funding through borrowing.

5. What actions should the church take to ensure the funding of the new construction?

To ensure the funding of the new construction the church should:

- Meet with the Board of Elders to discuss options such as new negotiations and possible refinancing with the same bank. Possible new negotiation with other banks and lender.
- Evaluate the possibility of getting investors to invest into the construction/church.
- Follow-up with pledge donors to determine their ability to fulfill the outstanding pledges.
- Develop a plan of action for new funding – one borrower or several borrowers
- Consider the advantages and disadvantages of combining the sister churches which could allow more funds to be available toward completing the building.

6. What role did the minister play in the unraveling of New Revival?

The minister appears to play an integral role in the unraveling of New Revival. For instance the minister had total control over the New Revival organizations including the newly established daughter churches. As such, he made all decisions involving the organization without prior approval from the board. Although not specifically mentioned in the case, the minster's ego grew larger as the organization expanded and he wanted to control all activities.

7. Assume you are requested by the Board of Elders to assist it in understanding the challenges facing the organization. The board is especially concerned about the loan default and the organization's ability to complete the construction project. Prepare a report to the board providing them with possible steps that the organization could take to ensure its continuity

A suggested report is provided in Appendix A

DISCLAIMER

This case and teaching note was prepared by Raymond Elson, and Beverley Alleyne and is intended to be used for class discussion rather than either effective or ineffective handling of the situation. The case is loosely based on a real situation therefore the names of the organizations, the individuals, and locations have been disguised.

REFERENCES

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Appendix A: Suggested Report

Date: November X, 20XX

To: The Board of Elders
New Revival Church

From: Group Name

Introduction

At your request, we performed an assessment of New Revival ("the organization") to help you better understand the challenges and obstacles that it faces. We also evaluated the ability of the organization to continue into the future in light of the loan default and the delayed construction project. Our suggestions regarding your next steps are provided below.

Recommendations

In order to improve accountably and transparency in the organization and to ensure its viability, we recommend the following:

- Decentralize decision making to each daughter church with New Revival having oversight responsibility. This change would provide the churches with autonomy as well as control over their finances. Each daughter church would provide New Revival with monthly financial reports. Decentralization would ensure that an unsuccessful daughter church would not impact the health of New Revival, and could possibly be eliminated or merged with another church.
- Create separate bank accounts for each of the daughter church with appropriate authorized signers.
- Evaluate the expenses and debt of the organization and develop a plan of action to reduce expenses and eliminate some of the debt. As part of this process, determine the appropriate staffing model (especially administrative and financial) of the New Revival organization to ensure that transactions are identified,

recorded, and reported in a timely and accurate manner. In addition, the organization should consider hiring temporary help to ensure that the financial information is brought current.

- Evaluate the composition of the board to ensure that members are able to perform their fiduciary or oversight role. Elect a chairman of this reconstituted board and have formal meetings at least quarterly.
- Schedule a membership meeting as soon as possible and discuss the problems encountered by the organization. Obtain their support before moving forward with any financial commitment.
- Prepare an employment agreement that stipulates the responsibilities, reporting and performance standards, and compensation for the minister.

Negotiate a loan extension or a new loan with the current bank or a new bank to ensure completion of the building project. The reconstitute board should be in charge of this initiative

EB03 BANK OF NIGERIA

Basil Okoli, Baze University
D.K. (Skip) Smith, Baze University

CASE OVERVIEW

This case invites students to play the role of Mr. Edi Agbam, a Nigerian who worked for many years at EB03 Bank of Nigeria (EB03 Bank is the disguised name of a real bank in Nigeria). At one time, EB03 Bank of Nigeria was the market leader in the banking industry in Nigeria; over the years, however, EB03 Bank has fallen from #1 to "emerging big bank." Currently, Mr. Agbam serves as a lecturer for the Faculty of Business Administration at Baze University, a new private University located in Abuja, Nigeria; yesterday, however, Mr. Agbam received an offer to take up a consultancy appointment with EB03 Bank, so as to assist the bank in developing a strategy to regain (in retail banking) the market leadership position it once held in Nigeria in many areas including retail banking. The case is appropriate for senior level undergraduates as well as students in MBA and/or executive development programs. It is designed to be taught in a one-hour and a half class session and is likely to require at least a couple hours of preparation by students.

CASE SYNOPSIS

Mr. Edi Agbam, a former EB03 Bank of Nigeria employee currently employed as a lecturer at Baze University in Abuja, has been offered a consultancy at EB03 Bank of Nigeria, so as to assist the bank in developing a strategy to regain (in retail banking) the market leadership position it once held in the banking sector in Nigeria in many areas including retail banking.

Additional data and information in the case include:
For Nigeria, the Nigerian environment, and the Nigerian economy: Historical background plus selected statistics.
For the banking sector in Nigeria: Historical background plus selected statistics.
For EB03 Bank of Nigeria: Historical background plus selected statistics.

INSTRUCTORS' NOTE

As indicated in the case, the challenge faced by Mr. Edi Agbam, a member of the Faculty of Business Administration at Baze University in Abuja Nigeria, is to decide how to assist EB03 Bank of Nigeria in developing a strategy to regain (in retail banking) the market leadership position it once held in Nigeria, in that sector. As regards lessons and/or information which students should learn from this case, at least the following four points can be made:

1) At the beginning of the case, students will need to consider the extent to which developed-world models and conceptual frameworks can be applied to challenges and opportunities in the developing world. By the end of the case discussion, they will have discovered that some conceptual frameworks (for example, the Sheth 1985 turnaround strategy model and/or the marketing strategy model) can be useful guides to managerial action not only in the developed world but in the developing world as well.
2) Students will be able to compare their solutions to the one chosen by the central figure in the case, Mr. Edi Agbam.
3) Students will discover that managers' decisions are likely to be powerfully impacted by the conceptual framework they use; they will also discover that the recommendations flowing from alternative conceptual frameworks (for example, the Sheth 1985 turnaround strategy model on the one hand or the marketing strategy model on the other) could be quite different.
4) As they work through the case, students are exposed not only to a bit of information on an important market in Africa (that is, Nigeria) and the financial services industry in that country and EB03 Bank of Nigeria; in addition, they are also exposed to a bit of history on Baze University, one of several new private universities in Nigeria which are growing very rapidly and enjoying (in terms of growth in student enrollments) a high level of success.

DISCUSSION QUESTIONS

We often select one student to lead the discussion. Another approach would be to solicit input from various students at various stages of the analysis. Either way, our usual approach to this case is threefold:

1) Solicit from many students the details of the case, including information about the country, information about the organization, information on the individuals involved in the case, and so on. Usually, we write much of this information on the board, so that if questions regarding "facts of the case" come up, we will have much of that information on the board in front of us.
2) Ask an individual student or the class as a whole to address a very specific series of questions. These questions, and comments relating to possible answers to those questions, are as listed below:

Q & A(#1) : WHAT IS THE MAIN PROBLEM? Students usually conclude that Mr. Agbam needs to develop a retail banking strategy for EB03 Bank of Nigeria which will permit EB03 Bank to regain (in retail banking) the stature and status it held during the time that the bank was the market leader in the financial services sector in Nigeria.

Q & A(#2): WHAT KIND OF PROBLEM IS THIS? Instructors should not be surprised if there are as many answers to this question as there are students in the class. Clearly, there is no one right answer. However, two alternative approaches, each of which seems quite relevant to the situation, are as indicated below:

i. Turnaround strategy
ii. Marketing strategy

Q & A(#3): FOR THE KIND OF PROBLEM IDENTIFIED ABOVE, WHAT ARE THE KEY VARIABLES AND WHICH EXPERT SAYS SO? For students concluding that the main problem is the need for a "turnaround strategy," Sheth (1985) suggests there are nine strategies which can be considered: 1) Entrenchment (that is, fight for a larger share of existing uses of products in existing markets); 2) Consider selling through intermediaries; 3) Mandatory consumption (that is, ask government to pass a law requiring the purchase by consumers of a company's product or service); 4) Go international; 5) Broaden product horizons (that is, don't sell just the computer; rather, sell the computer plus a full set of ancillary products and services); 6) In existing markets, identify new applications for products; 7) In existing markets, identify new usage situations; 8) Repositioning (that is, in new markets, identify new uses for products by changing the image of the product); and 9) Redefining markets (that is, in new markets, identify new uses for products by making functional changes in those products. For students concluding that the main problem is "marketing strategy," Perreault and McCarthy (2002) suggest that the key marketing strategy variables are: 1) Target market; and 2) The "4Ps" of the marketing mix (that is, place, price, product, and promotion).

Q & A(#4): WHAT DATA FROM THE CASE RELATE TO THE KEY VARIABLES? As implied above (and this is one of the key learning points of the case), the data students present will depend on the main problem they identify. Students believing the main problem is "marketing strategy" will focus on the five key variables in that concept; Appendix 1 identifies data from the case which relate each of those key variables. Students believing the main problem is "turnaround strategy" will focus on the nine key alternatives identified earlier; Appendix 2 identifies data from the case which relate to each of these key variables

Q & A(#5): WHAT ALTERNATIVE SOLUTIONS CAN BE IDENTIFIED? Because research suggests we make better decisions if we first identify alternative solutions and then choose one of those solutions, we require students to identify at least two alternative solutions. Of course, students having difficulties coming up with a second alternative can be reminded that one possible solution is to "do nothing."

Q & A(#6): WHICH OF THE ALTERNATIVE SOLUTIONS SET FORTH ABOVE DOES THE CLASS/STUDENT TO RECOMMEND, AND WHY? "Doing nothing" is unlikely to help Mr. Agbam resolve the dilemma he faces, that is, how to regain for EB03 Bank of Nigeria the stature and status it enjoyed during the years when it was the market leader in the financial services sector in Nigeria. Thus, students believing the main problem is "turnaround strategy" will likely recommend an approach which focuses on the nine alternatives in Sheth's turnaround strategy model from 1985. Students believing the main problem is "marketing strategy" are likely to recommend focusing on the five key variables of the marketing strategy concept.

The decision reached by Mr. Agbam was to use the "turnaround strategy" conceptual framework to guide his thinking and his recommendations. For additional information on the recommendations associated with this decision, please see the epilogue.

Q&A #7) WHAT NEGATIVES ARE ASSOCIATED WITH THE ALTERNATIVE SELECTED BY THE CLASS LEADER AND/OR OTHER MEMBERS OF THE CLASS? Very few solutions are risk and/or problem-free. Negatives associated with the solution proposed by the class leader and/or other members of the class could include the following: The chosen alternative, if it requires EB03 Bank to acquire specialized equipment and/or skills the organization doesn't currently possess, could be expensive both in terms of time and money. Also, because the case probably doesn't provide all the data a decision maker would need (in other words, it is likely that some important data is missing), it is possible that assumptions made by the class leader regarding the actual situation faced by EB03 Bank are incorrect. If so, the proposed solution might be inappropriate.

3. The third and final step in discussing a case with students is to share with them what actually happened and to discuss with them the implications of that outcome. As indicated above, as he thought about developing a strategy to rebuild the retail banking

operations of EB03 Bank, Mr. Agbam's thoughts turned to a turnaround strategy conceptual framework developed by Sheth (1985). Based on the nine turnaround strategy alternatives suggested by Sheth (1985), Mr. Agbam identified and suggested to the Non-Executive Director the following alternatives for rebuilding the retail banking Operations of EB03 Bank:

A. Entrenchment-related recommendations. Based on the four entrenchment-related EB03tions identified by Sheth (segmentation, specialty markets, heavy users of the product, and multiple channels of distribution), Mr. Agbam identified the following alternatives for creating a successful retail banking strategy for EB03 Bank:

   i. Segmentation: From the full set of all AB consumers in Nigeria, identify subsets (or segments) of interest. Segments which might be of special interest include: consumers in the A&B socioeconomic classes who have never before borrowed from a bank; consumers in the A&B socioeconomic classes who are heavy (and successful) users of bank loans; and consumers in the A&B socioeconomic classes who have nonstandard (that is, not household appliances, not vehicles) needs for loans from banks. Regarding consumers in the A&B socioeconomic classes who have never before borrowed from a bank: Develop a system which makes it very easy for these individuals to borrow (and repay) for the first time; once the system is developed, vigorously promote the system to these individuals.
   ii. Specialty markets: Again, for the subset of consumers in the A&B socioeconomic classes in Nigeria who have nonstandard (that is, not household appliances, not vehicles) needs for loans from the banks: identify the needs of consumers in this category and develop specialized products and services to serve the needs of these individuals.
   iii. Heavy users of the product: From the full set of all AB consumers in Nigeria, identify the subset (or segment) who are heavy users (that is, consumers who have successfully used (that is, not only borrowed from banks but also repaid those loans) bank loans in the past. It seems reasonable to set these individuals up as "preferred customers" and, while ensuring that the bank continues to be properly protected, make it quick and easy for these customers to access additional loans from the bank.

iv. Multiple channels of distribution: The case indicates that to date, EB03 Bank offers its products and services through its branches and Business Development Centers (BDC). For at least some of its products (for example, the EB03 Household and the EB03 Auto Loan products), EB03 Bank could consider partnering up with auto and/or home appliance dealerships, with the idea that customers coming to dealerships with whom EB03 Bank has developed a partnership agreement will be urged (at the dealership) to finance their purchases through EB03 Bank.

B. Sell through intermediaries-related recommendations. Under this heading, Sheth (1985) recommends that companies re-organize their selling efforts and utilize third parties (in the case of EB03 Bank, likely 3rd party candidates could include home appliance dealers, auto dealers, etc.).

C. Mandatory consumption-related recommendations: It seems unlikely that the government of Nigeria will pass a law requiring members of the AB socio-economic class to become customers of EB03 Bank.

D. Go international-related recommendations. Sheth indicates that sometimes a failing company can rescue itself by pursuing overseas opportunities. The case indicates that in the past EB03 Bank had a network of overseas correspondent banks in Europe, Asia, and North America; the case also indicates that EB03 Bank operates a free-standing bank in London called "EB03 Bank(UK)." The case does not, however, describe any organized plan for EB03 Bank to pursue retail banking opportunities overseas. While EB03 Bank may not wish to mount a major retail banking overseas initiative, one possibility which might be worth exploring would be to identify and then reach out (with "EB03 Bank" and/or "EB03 Bank(UK)" products and services) to Nigerians in the A&B socioeconomic classes who live and work overseas.

E. Broaden the product horizon-related recommendations. Sheth (1985) indicates that sometimes a company can rescue itself by adding ancillary products and/or services to their basic product and/or services. Mr. Agbam believes that two initiatives which might be worth considering include:

i. Review the products and services offered by other banks in Nigeria, and look for products and services offered by competitors which appear to be well regarded and heavily patronized by one or more of the three key segments of retail customers identified earlier (that is, members of the A&B socioeconomic classes who have never yet borrowed from a bank, members of the A&B socioeconomic classes who are heavy users of loans from banks, and members of the A&B socioeconomic classes who have specialized financial needs of one sort or another).

ii. Develop (through research) a deeper knowledge of the attitudes and behaviors of the three segments of the A&B socioeconomic classes in Nigeria and, based on that deep knowledge, develop new products and services for each of these groups of customers.

F. New situations-related recommendations. Sheth (1985) suggests that sometimes a business can be turned around by putting an existing product or service into new usage situations. Assuming the bank develops (through research) "deep knowledge" of each of the three key segments of retail customers identified earlier, it seems very likely that "new situations" for the products and services offered by EB03 Bank will emerge.

G. New applications-related recommendations. Sheth (1985) suggests that sometimes a business can be turned around by putting products and/or services to work in new and different applications. Assuming the bank develops (through research) "deep knowledge" of each of the three key segments of retail customers identified earlier, it seems very likely that "new applications" for the products and services offered by EB03 Bank will emerge.

H. Repositioning-related recommendations. According to Sheth, this strategy involves redefining a product's image into new usage situations within the same general application context. The case does not provide any evidence to support the idea that the existing positioning of EB03 Bank and its products and services is especially compelling to members of the A&B socio-economic groups in Nigeria. To the contrary, EB03 Bank's decline from market leader to "emerging big bank" suggests that the positioning EB03 Bank has adopted is not especially compelling to the three key segments of retail customers identified earlier, that is, members of the A&B socioeconomic classes who have never yet borrowed from a bank, members of the A&B socioeconomic classes who are heavy users of loans from banks, and members of the A&B socioeconomic classes who have specialized financial needs of one sort or another. The implication here is of course that conducting research so as to develop deep knowledge of the attitudes and behaviors of each of the three key segments could make it possible for EB03 Bank to position itself and its products in ways which members of the three key segments would find especially compelling.

I. Redefine markets-related recommendations. Sheth identifies four alternative approaches to using this strategy. Those four approaches, and comments relating to them, are as indicated below:

   i. Generic to specialty products: The products and services offered by
      EB03 Bank are not generic products; this option does not seem relevant to this situation.
   ii. Primary to secondary products: It seems possible that the individual products and services offered by EB03 Bank(EB03 Household Loans, EB03 Auto Loans, EB03 Salary Advance, EB03 Mortgage, and EB03 Share Purchase) could become part of a package or portfolio of financial services developed and offered by EB03 Bank; the purpose of this package or portfolio of financial services would be to help consumers in the three key segments identified earlier to achieve their broader life-related goals including the ones already mentioned, that is:
      1. To ensure that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
      2. To become powerful, so as to gain access to additional business and/or financial opportunities.
   iii. Industrial to consumer products: The current retail products offered by EB03 Bank are already consumer products; this option does not seem relevant to this situation.
   iv. Consumer to industrial products: While it seems unlikely that industrial organizations and/or government ministries, departments, and agencies would be interested in purchasing retail banking products from EB03 Bank, it is possible that such entities would (as part of their benefits package to employees) be eager to partner up with EB03 Bank, so as to assist salaried employees by providing access to financial services from EB03 Bank to assist their salaried employees in achieving their broader life-related goals, that is:

1. To ensure that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
2. To become powerful, so as to gain access to additional business and/or financial opportunities.

CONCLUDING COMMENTS

The above comments describe the alternatives identified by (and recommended by) Mr. Agbam to achieve the objectives set by the Non-Executive Director. Readers may be interested in the answers to the following questions:

QUESTION #1: Of the suggestions made by Mr. Agbam, which ones did the Non-Executive Director find especially interesting and/or useful?

ANSWER. Of the recommendations made by Mr. Agbam, those the Non-Executive Director found especially useful and/or interesting included:

a. Entrenchment-related recommendations:
    i. Segmentation: The non-Executive Director comments that "segmentation is a key marketing strategy for retail banking especially in a country with a large un-banked population. There is a huge opportunity for extending services to new users."
    ii. Specialty markets: The non-Executive Director comments that "most banks in the industry are constantly researching special needs of various target groups (e.g. young families requiring support to finance their children's schooling) and developing products to address these needs."
    iii. Multiple channels: The non-Executive Director comments that "the bank is exploring the use of cooperatives and/or staff unions of some of its large corporate customer, to offer loans to members."
b. Other recommendations: The non-Executive Director comments that "the introduction of electronic banking (especially through the use of ATMs and POS technologies) have offered new Opportunities which the bank is also pursuing."

QUESTION #2: Have any of the alternatives suggested by Mr. Agbam already been implemented? If so, which alternatives have been implemented and what results have been achieved so far?

ANSWER: The Non-Executive Director indicates that "all of the above alternatives have been implemented by the bank along with other strategies; as a result, the bank is now back to profitability and gaining ground in the market."

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QUESTION #3: Are there other alternatives (that is, alternatives other than those suggested by Mr. Agbam which have been put into play? If so, what are these additional alternatives and what results have been achieved so far?

> ANSWER. The Non-Executive Director indicates that many EB03 Bank branches are being remodeled and/or relocated. Regarding remodeling, the Non-Executive Director indicates that "many branches are being remodeled and upgraded to conform to the tastes and expectations of today's customers." Regarding relocation, the Non-Executive Director indicates that "branches . . . located in areas which are no longer viable as the market has moved to new population centers. . . are being relocated . . "

QUESTION #4: Overall, does it appear that EB03 Bank is likely to achieve its objectives, that is, to re-establish itself as the market leader in the retailing banking sector in Nigeria?

> ANSWER. The Non-executive Director indicates that "the bank has returned to profitability and is steadily regaining its customer base and reasserting itself in the market. The prospects of regaining its position as an industry leader within the next three years are very high."

QUESTION #5: Are there any other comments and/or observations which the Non-Executive Director would like to make at this time, regarding either the current situation and/or prospects for the future?

> ANSWER. The Non-Executive Director indicates that "a major strategy the bank is also implementing is to withdraw from other non-core banking activity such as insurance, real estate, properties, etc. in order to concentrate on core banking services. This strategy has led the bank to dispose of many of its subsidiary businesses including subsidiary banks outside of Nigeria. The only exception (to the withdrawal from overseas operations) is EB03 Bank(UK) which is vital for its core banking services."

APPENDIX 1
CASE DATA RELATING TO MARKETING STRATEGY MODEL

TARGET MARKET: The case indicates that the current retail banking strategy of EB03

Bank is to target members of the AB socio-economic group in Nigeria. Over and above the general characteristics of Nigerians in the AB socio-economic categories (consumers in the "A" socioeconomic class include upper-class individuals such as senior-level managers and administrators plus highly successful professional people; consumers in the "B" socioeconomic class include middle-class individuals such as mid-level managers and administrators), the case indicates that Mr. Agbam believes (based on his research over the years) that the banking services-related attitudes and behaviors of individuals in these socio-economic classes include:

1) Members of these socio-economic groups are very keen to work up strategies to create businesses opportunities and/or strategies to enhance their quality of life; once they have devised a business and/or a lifestyle-enhancing strategy, they are likely to come to a bank looking for the money to implement that strategy.
2) For many members of the A&B socio-economic group, their earliest memories of banks and banking-related services will relate to the fact that after they (or someone they know) identified an idea and registered a company to pursue that idea, they came to a bank looking to borrow money to finance their company. Mr. Agbam's suspects that for many of these individuals (when they arrived at a bank seeking a loan for the first time):
    a. Because they had very little knowledge of the policies and procedures which banks follow when making loans (the need for a primary source of repayment, the need for collateral and a second source of repayment, the importance to the bank of the character and credibility of the borrower, the service charges and/or fees associated with loans, etc.), there was a lot they needed to learn about banks and banking and borrowing.
    b. What they learned about banks and banking and borrowing (the interest rates, the fees and service charges, the need for collateral, and so on) may not have pleased them very much. Borrowing money for the first time to pursue a business opportunity and/or to enhance their quality of life may (at first glance) have looked and sounded painlessly easy and simple; what they would have discovered very quickly is that dealing with banks and banking and borrowing is neither painless, easy, nor simple.

2) The best experience members of the A&B socioeconomic class have experienced is that after they have paid off their loan to the bank, all of the net cash flow generated by their business flows into their own pocket. The worst outcome members of the A&B socioeconomic class have experienced is that their business fails and the bank not only seizes their business but also liquidates the collateral they had provided to the bank as well.

3) Regarding pivotal (that is, attitude and/or behavior-changing) experiences with banks: Mr. Agbam believes that a very negative (and potentially behavior-changing) situation experienced by some bank customers is when they go to the bank to withdraw funds from their account but are told (because the bank is short of funds) that the bank is not able (at that moment) to give them cash from their account. A related and very negative experience would be if the bank is unable (due to its liquidity position) to provide the financial assistance (including loans) which the customer has requested.

4) Regarding ideal and/or "worst case" experiences with banks:
    a. An ideal experience might look approximately as indicated below:
        i. When the individual walks into a bank, he or she is greeted in a friendly and courteous manner by a bank employee.
        ii. After greeting the individual, the bank employee asks the individual what he or she wishes to accomplish and then takes the individual to the bank employee who can do what needs to be done.
        iii. The individual explains to the bank employee what he or she is trying to accomplish and what service he or she is requesting from the bank.
        iv. The bank employee requests key bits of information from the individual; having collected that information, the bank employee tells the individual whether it should be possible for the bank to provide the support which the individual is requesting.
        v. If the bank employee says that it is possible that the bank will be able to provide the support the individual is requesting, the bank employee now tells the individual exactly what additional information and/or documentation the individual must provide to the bank.
        vi. Once the individual has provided the additional information and/or documentation requested by the bank, the bank reviews the situation and (in a very timely manner) decides whether or not to provide the requested financial support.

vii. Assuming the bank has decided to provide the requested financial support, that financial support is provided in a very timely manner and as requested.

b. A “worst case” experience might look approximately as indicated below:
   i. When the individual walks into a bank, there is no bank employee to greet them in a friendly and courteous manner.
   ii. There is no bank employee to ask the individual what he or she wishes to accomplish and/or to take the individual to the bank employee who can do what needs to be done.
   iii. There is no bank employee to whom the individual can communicate what he or she is trying to accomplish and what service he or she is requesting from the bank.
   iv. The bank employee does not request all of the information which he or she needs from the individual, so as to be able to make a decision as to whether it should be possible for the bank to provide the support which the individual is requesting.
   v. Assuming the bank employee says that it is possible that the bank will be able to provide the support the individual is requesting, the bank employee does not tell the individual all the additional information and/or documentation the individual must provide to the bank.
   vi. Once the individual has provided all the additional information and/or documentation requested by the bank, the bank does not review the situation in a timely manner and/or is not able to give a clear answer as to whether or not the bank will provide the requested financial support.
   vii. Although the bank has agreed to provide the financial support requested by the individual, that financial support is not provided in a timely manner and/or as requested.

5) Regarding issues which prevent individuals from experiencing an ideal experience with a bank:
   a. Lender-related issues which prevent individuals from having an ideal experience with a bank include:
      i. The bank employee interacting with the individual does not know enough to handle the individual’s request but is not willing to admit that he or she is not knowledgeable enough.
      ii. Moving through the bank’s policies and procedures and requirements can be time-consuming.

iii. Certain characteristics of the loan which a bank offers (the interest rate, the duration of the loan, the collateral which the bank will require, and so on) may not be acceptable to the borrower.

b. Borrower-related issues which prevent individuals from having an ideal experience with a bank include:

a. Certain characteristics of the borrower and/or the borrower's request (interest rate, duration of the loan, collateral to be provided, the character of the borrower, the credibility of the borrower, etc.) may not be acceptable to the bank.

6) Regarding their concerns at this time in their life, not only about the financial services offered by banks but also in general:
    i. Ensuring that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
    ii. Becoming powerful, so as to gain access to additional business and/or financial opportunities.

7) Regarding the issues which they were happiest about: Mr. Agbam believes that the thing which makes members of the A&B socioeconomic classes in Nigeria most happy is when they finish paying off loans they owe/money they have borrowed from banks.

8) Regarding the most important things members of the A&B socioeconomic class in Nigeria are trying to achieve at this time in their lives, Mr. Agbam believes that these include:
    a. Ensuring that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
    b. Becoming powerful, so as to gain access to additional business and/or financial opportunities.

9) Regarding the one thing members of the A&B socioeconomic classes in Nigeria would change about financial services from banks, if they had a magic wand: Mr. Agbam believes that members of the A&B social class believe that banks need to make available to customers a full range of short-term and long-term loans, so as to be able to provide the total package of financial services which members of the three key segments of the A&B socioeconomic classes believe they need, to be able to achieve their overall objectives, that is:

i. To ensure that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
ii. To become powerful, so as to gain access to additional business and/or financial opportunities.

PRODUCTS: The case indicates that the financial product and services EB03 Bank currently offers its customers include:

1) A variety of loan products including:
    a. EB03 Household (that is, personal loans for the acquisition of household items including furniture, television, computers, generators, laundry and kitchen appliances, etc.)
    b. EB03 Auto Loan (that is, a personal loan for the acquisition of a vehicle)
    c. EB03 Salary Advance (that is, easy access to funds for customers receiving a regular and steady monthly salary)
    d. EB03 Share Purchase Loan (that is, personal loans to purchase shares of blue-chip companies)
    e. EB03 Mortgage Loan
2) Credit Cards

PRICE: The case indicates that the interest rates EB03 Bank charges its retail banking customers are 20% per annum or higher. Case indicates that in addition to the interest, retail customers can also end up paying service charges, management fees, lawyers' fees, etc.

PROMOTION**:** Regarding media, banks in Nigeria (including EB03 Bank) promote themselves and their products using a variety of media including electronic (radio, television, etc.), print (newspapers,etc.), the internet, etc. The mission statement, vision statement, and theme of EB03 Bank's current promotional indicate that EB03 Bank of Nigeria aspires to be perceived as the best and leading financial institution in Nigeria, that it aspires to be perceived as providing high levels of customer satisfaction, and that it aspires to be perceived as being a very large and very strong bank.

PLACE (Distribution): The case indicates that EB03 Bank has divided Nigeria up into three regions (Lagos, South, and North) and that within these regions the bank has a total of 39 Business Development Centers (BDCs) and 340 branches. The case also indicates that EB03 Bank operates a related free-standing bank in London named "EB03 Bank(UK)."

APPENDIX 2
CASE DATA RELATING TO THE "TURNAROUND STRATEGIES" MODEL

1.ENTRENCHMENT. According to Sheth (1985), this approach involves taking market share away from competitors. He suggests four alternatives which firms may be able to use; those alternatives and data from the case relating to those alternatives include:

a. Segment the market (and introduce different products and/or services for each segment). Regarding the product of interest (that is, products and services offered by EB03 Bank to retail customers) the case indicates that the segments EB03 Bank has targeted (that is, consumers in the A&B socioeconomic classes) have the following characteristics:
   i. Regarding first things members of the A&B socio-economic groups think about when thinking about financial services-related products from banks: Mr. Agbam believes that members of these socio-economic groups are very keen to work up strategies to create businesses Opportunities and/or strategies to enhance their quality of life; once they have devised a business and/or lifestyle enhancement strategy, they are likely to come to a bank looking for the money to implement that strategy.
   ii. Regarding their earliest memories regarding the financial services offered by banks, Mr. Agbam believes that for many members of the A&B socio-economic group, their earliest memory will relate to the fact that after they (or someone they know) identified an idea and registered a company to pursue that idea, they came to a bank looking to borrow money to finance their company. Mr. Agbam's suspects that for many of these individuals (when they arrived at a bank seeking a loan for the first time):
      1. Because they had very little knowledge of the policies and procedures which banks follow when making loans (the need for a primary source of repayment, the need for

collateral and a second source of repayment, the importance to the bank of the character and credibility of the borrower, the service charges and/or fees associated with loans, etc.), there was a lot they needed to learn about banks and banking and borrowing.

2. What they learned about banks and banking and borrowing (the interest rates, the fees and service charges, the need for collateral, and so on) may not have pleased them very much. Borrowing money for the first time to pursue a business opportunity and/or to enhance their quality of life may (at first glance) have looked and sounded painlessly easy and simple; what they would have discovered very quickly is that dealing with banks and banking and borrowing is neither painless, easy, nor simple.

iii. Regarding their experiences with financial services offered by banks, Mr. Agbam believes that the best experience members of the A&B socioeconomic class have experienced is that after they have paid off their loan to the bank, all of the net cash flow generated by their business flows into their own pocket. The worst outcome members of the A&B socioeconomic class have experienced is that their business fails and the bank not only seizes their business but also liquidates the collateral the borrower had provided to the bank as well.

iv. Regarding pivotal (that is, attitude and/or behavior-changing) experiences with banks: Mr. Agbam believes that a very negative (and potentially behavior-changing) situation experienced by some bank customers is when they go to the bank to withdraw funds from their account but are told (because the bank is short of funds) that the bank is not able (at that moment) to give them cash from their account. A related and very negative experience would be if the bank is unable (due to its liquidity position) to provide the financial assistance (including loans) which the customer has requested.

v. Regarding ideal and/or "worst case" experiences with banks: Mr. Agbam believes that:

1. an ideal experience might look approximately as indicated below:

a. When the individual walks into a bank, he or she is greeted in a friendly and courteous manner by a bank employee.
b. After greeting the individual, the bank employee asks the individual what he or she wishes to accomplish and then takes the individual to the bank employee who can do what needs to be done.
c. The individual explains to the bank employee what he or she is trying to accomplish and what service he or she is requesting from the bank.
d. The bank employee requests key bits of information from the individual; having collected that information, the bank employee tells the individual whether it should be possible for the bank to provide the support which the individual is requesting.
e. If the bank employee says that it is possible that the bank will be able to provide the support the individual is requesting, the bank employee now tells the individual exactly what additional information and/or documentation the individual must provide to the bank.
f. Once the individual has provided the additional information and/or documentation requested by the bank, the bank reviews the situation and (in a very timely manner) decides whether or not to provide the requested financial support.
g. Assuming the bank has decided to provide the requested financial support, that financial support is provided in a very timely manner and as requested.

2. A "worst case" experience might look approximately as indicated below:
   a. When the individual walks into a bank, there is no bank employee to greet them in a friendly and courteous manner.
   b. There is no bank employee to ask the individual what he or she wishes to accomplish and/or to

take the individual to the bank employee who can do what needs to be done.

c. There is no bank employee to whom the individual can communicate what he or she is trying to accomplish and what service he or she is requesting from the bank.
d. The bank employee does not request all of the information which he or she needs from the individual;, so as to be able to make a decision as to whether or not it might be possible for the bank to provide the support which the individual is requesting.
e. Assuming the bank employee says that it is possible that the bank will be able to provide the support the individual is requesting, the bank employee does not tell the individual all the additional information and/or documentation the individual must provide to the bank.
f. Once the individual has provided all the additional information and/or documentation requested by the bank, the bank does not review the situation in a timely manner and/or is not able to give a clear answer as to whether or not the bank will provide the requested financial support.
g. Although the bank has agreed to provide the financial support requested by the individual, that financial support is not provided in a timely manner and/or as requested.

vi. Regarding issues which prevent individuals from experiencing an ideal experience with a bank, Mr. Agbam believes that there are issues relating (on the one hand) to lenders and (on the other hand) to borrowers:

1. Lender-related issues which prevent individuals from having an ideal experience with a bank:
   a. The bank employee interacting with the individual does not know enough to handle the individual's request but is not willing to admit that he or she is not knowledgeable enough.

b. Moving through the bank's policies and procedures and requirements can be time-consuming.
c. Certain characteristics of the loan which a bank offers (the interest rate, the duration of the loan, the collateral which the bank will require, and so on) may not be acceptable to the borrower.

2. Borrower-related issues which prevent individuals from having an ideal experience with a bank include:
   a. Certain characteristics of the borrower and/or the borrower's request (interest rate, duration of the loan, collateral to be provided, the character of the borrower, the credibility of the borrower, etc.) may not be acceptable to the bank.

vii. Regarding their concerns at this time in their life, not only about the financial services offered by banks but also in general: Mr. Agbam believes that the key concerns of members of the A&B socioeconomic classes in Nigeria include:
   1. Ensuring that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
   2. Becoming powerful, so as to gain access to additional business and/or financial opportunities.

viii. Regarding the issues which they were happiest about: Mr. Agbam believes that the thing which makes members of the A&B socioeconomic classes in Nigeria most happy is when they finish paying off loans they owe/money they have borrowed from banks.

ix. Regarding the most important things members of the A&B socioeconomic class in Nigeria are trying to achieve at this time in their lives, Mr. Agbam believes that these include:
   1. Ensuring that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
   2. Becoming powerful, so as to gain access to additional business and/or financial opportunities.

x. Regarding the one thing members of the A&B socioeconomic classes in Nigeria would change about financial services from banks, if they had a magic wand: Mr. Agbam believes that members of the A&B social class believe that banks need to make available to customers a full range of short-term and long-term loans, so as to be able to provide the total package of financial services which members of the A&B socioeconomic classes believe they need, to be able to achieve their overall objectives, that is:

1. To ensure that the day-to-day needs of themselves and their family are dependably and ongoingly provided for.
2. To become powerful, so as to gain access to additional business and/or financial opportunities

b. Identify specialty markets: While the case indicates that EB03 Bank has targeted A&B consumers, the case does not identify any specialty markets within that group.
c. Go after heavy users of the product: The case does not provide information on the characteristics of heavy users of retail banking products in Nigeria.
d. Seek multiple channels of distribution: The case indicates that EB03 Bank has multiple Business Development Centers and branches in Nigeria, and that it operates a free-standing bank (EB03 Bank(UK)) in London. The case does not identify any other channels which EB03 Bank might be using to distribute its products and services.

2. SWITCH TO INTERMEDIARIES. If getting the product into the hands of ultimate
consumers is difficult, Sheth suggests that marketers may be able to succeed by selling to intermediaries (wholesalers, processors of agricultural products, etc.) instead. As indicated above, while the case indicates that EB03 Bank has its own large branch network, the case does not identify any other channels which EB03 Bank might be using to distribute its products and services.

3.MANDATORY CONSUMPTION. Sheth indicates that sometimes it is possible to revive a business by getting government (state, local, or federal) to pass a law making in mandatory for consumers to purchase certain categories of products. It seems unlikely that the government of Nigeria will pass a law requiring members of the AB socio-economic class in Nigeria to utilize financial products and services offered by EB03 Bank.

4.GO INTERNATIONAL. Sheth indicates that sometimes it is possible to revive a business by beginning to sell the product in markets outside the home market. The case indicates that EB03 Bank has had in the past (through its network of correspondent banks in EurEB03e, Asia, and North America) an overseas presence; the case also indicates that

EB03 Bank Operates a free-standing bank in the UK called “EB03 Bank(UK).” The case does not, however, suggest that EB03 Bank is making any concerted effort to develop any sort of international retail banking presence.

5.BROADEN THE PRODUCT HORIZON. Sheth indicates that this approach often involves focusing on the function that a product performs and then thinking of the product as a component in a system. The case does not appear to consider the question of whether the financial products and services EB03 Bank currently offers could be part (but only a part) of a system designed to deliver the benefits desired by consumers in the A&B socio-economic classes in Nigeria (that is, assurance that their own needs and those of their family are dependably and ongoingly provided for; and increasing their power so as to increase their access to money-making opportunities in Nigeria).

6.NEW APPLICATIONS. According to Sheth, new applications usually involve some
sort of functional change in the product. He indicates that a good way to search for new applications is to ask consumers how they actually use the product. The case does not provide detailed information on how members of the A&B socio-economic groups in Nigeria feel about using EB03 Bank products (as opposed to using the financial products and/or services offered by other banks in Nigeria) to achieve the desired benefits (assurance that their own needs and those of their family are dependably and ongoingly provided for; and increasing their power so as to increase their access to money-making opportunities in Nigeria).

7.NEW SITUATIONS. Sheth indicates that this strategy requires marketers to seek out
different times, places, and/or positioning for product usage. The case indicates that EB03 Bank currently positions itself as being very big and very strong. The case does not provide any evidence to support the idea that members of the A&B socio-economic groups in Nigeria believe that members of the A&B socioeconomic classes find this positioning especially compelling and/or relevant to their needs. In fact, the fall from market leader to “big emerging bank” could be interpreted as confirmation that A&B consumers in Nigeria do not find EB03 Bank’s current positioning especially compelling.

8.REPOSITIONING. According to Sheth, this strategy involves redefining a product’s image into new usage situations within the same general application context. As indicated above, the case does not provide any evidence to support the idea that the positioning EB03 Bank is currently using is especially compelling to members of the A&B socio-economic groups in Nigeria.

9.REDEFINE MARKETS. Sheth identifies four alternative approaches to using this strategy. Those four approaches, and data from the case relating to them, are as indicated below:

a. Generic to specialty products: The financial products and services offered by EB03

Bank are not a generic product; this option does not seem relevant to this situation.

b. Primary to secondary products: The case makes no mention of secondary products.

c. Industrial to consumer products: The retail banking products and services offered by

EB03 Bank are already consumer products; this option does not seem relevant to this situation.

d.Consumer to industrial products: It seems unlikely that corporate and/or governmental bodies would purchase retail banking products and services from EB03 Bank. While the case does not address this issue, it does seem possible that (as parts of a benefits package), companies and/or governmental bodies might offer financial products and services provided by EB03 Bank to their employees.

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EXECUTIVE EXPRESS

Michael J. Pesch, St. Cloud State University
Larry A. Logeman, Executive Express

CASE DESCRIPTION

The primary subject matter of this case concerns how focusing on excellence in customer service can drive success and profits. But success in a service business does not stem from a lot of "feel-good" exhortations about serving customers. It happens because of leadership experience and vision, understanding customer needs, hiring and training the right employees, technology investments that enhance communication and streamline non-value-added activities, and quality metrics that drive continuous improvement. Executive Express is an airport shuttle company that provides passenger ground transportation services to the Minneapolis/St. Paul International Airport (MSP). The case discusses how Larry Logeman became the new owner of Executive Express and turned a poorly managed, inwardly-focused company into the dominant provider of airport transportation in Central Minnesota by building a customer-focused organization. The case has a difficulty level of three or four, appropriate for junior and senior level students, and is designed to be taught in a one-hour class period, with two hours of outside preparation by students.

CASE SYNOPSIS

Imagine you are Larry Logeman, the owner and CEO of Executive Express, an airport shuttle company based in St. Cloud, Minnesota that you've owned for seven years. You have been successful at building a company that is focused on delivering service excellence to customers who need transportation to the Minneapolis/St.Paul International Airport, located 75 miles away. Meeting your customers' needs was at the core in making technology decisions, hiring and training employees, and tracking performance measures for quality improvement. Although Executive Express has been successful with this business strategy, it now faces a new threat from the City of St. Cloud's efforts to recruit an airline to reestablish air service at the St. Cloud airport. You need to decide whether to implement an aggressive competitive response to this threat by increasing the number of roundtrips per day to attract new customers who are currently driving themselves to the airport, and to contend with a potential new airline by maintaining your position as Central Minnesota's most convenient and reliable airport transportation option. What do you do?

INSTRUCTORS' NOTES

RECOMMENDATIONS FOR TEACHING APPROACHES

This case can be used in a service operations management course, a strategic management course, or an entrepreneurship course. The case depicts a small business owner with the experience, passion and vision for delivering excellence in customer service. The case shows how a company that excels in customer service requires a leader with the ability to understand customer needs. The leader then translates those needs into strategic imperatives that build a culture of customer service and drive decisions on employees, technology, quality, and other business elements.

The case instructor should have the students read the case outside of class and prepare answers to the discussion questions contained in this note. At the beginning of the class session, the instructor might consider having the students discuss their answers in small groups with fellow students. The instructor might open the class discussion with the question, "Who is Larry Logeman?" This is a great launching point for discussing the case issues. The question fosters discussion of issues such as the culture and customer service goals of Executive Express, Larry Logeman's priorities as owner and CEO, the relevance of Logeman's extensive background in service industries, and the fact that striving for excellence in customer service must be done in concert with making good business decisions that provide opportunity, while mitigating excessive risk.

CASE OVERVIEW

This case is focused on a real company, Executive Express, and its owner and CEO, Larry Logeman. The facts and statistics communicated in the case are real (except for the identities of the previous owner and office manager), and the data were collected from interviews with Larry Logeman and the documents, financial figures, and information he provided.

The case opens with Larry reading the newspaper headlines, announcing the search by the City of St. Cloud (where Executive Express is based) to establish a new air service out of the St. Cloud airport. As an airport shuttle company owner, Larry recognizes this news as a potential threat to his business, and he considers how he might take preemptive actions to protect his share of the Central Minnesota air travel marketplace. This is the decision point of the case, and is revisited in the final section.

The case then provides an extensive description of Larry Logeman's background, and how he developed his knowledge and passion for serving customers. Details include Larry's undergraduate degree in sociology and public communication, and his work experiences in a wide variety of service businesses such as the Holiday Inn, the Days Inn, the Radisson Hotel, a health maintenance organization (HMO), the YMCA, and ServiceMaster. Larry's customer service philosophy is captured by his descriptions of what it means to have a "service heart," and how he strives to imbue his employees with a "Yes I Can!©" approach to serving customers.

The next section provides examples of the stale and backward management approaches employed by the former owner. This section provides a baseline for showing in the following sections how Larry revived the business and transformed it into a customer-focused organization.

The next three sections provide descriptions of the focus, persistence, and expense of building an organization that excels at customer service. The first of these sections discusses the importance of hiring, training, and motivating the right *people* (drivers and office staff). The second section delves into the details of how new software *technology* drives customer service by providing 24/7 access to customers, reduces errors, and provides information transparency to all employees so they know what needs to get done to serve customers at any given moment. The third section discusses customer service *quality* measures and the details of how Executive Express tracks and documents service performance, conducts root problem analysis, and develops solutions to block future mistakes. Misplaced luggage and missed passenger pickups are highlighted.

The case then describes how Larry Logeman determined that convenience and reliability in transportation to the Minneapolis/St. Paul (MSP) airport best defined his customers' needs. He used "We Never Cancel!" as a marketing slogan to convey to customers that a paid reservation meant a customer was guaranteed of getting to the MSP airport to make their flight. A timeline is used to describe how Executive Express expanded its service routes and the number of roundtrips per day to build customer loyalty and attract new customers to its service. Larry's goal was to make his shuttle service the "airport transportation option of choice," because customers would come to realize that it was more convenient and reliable (and often cheaper) than driving themselves to the airport.

The final section provides a detailed description of the pros and cons of expanding daily roundtrips between St. Cloud and MSP from 10 to 14. Both quantitative and qualitative information are provided to enable an in-depth discussion of the strategic decision Larry is contemplating.

DISCUSSION QUESTIONS

1. How did Larry Logeman's background prepare him to lead a business where success depends on delivering excellence in customer service?

Answer:
The case provides a number of facts and details that support an argument that Larry had both a personal orientation and a wide range of experiences to prepare him to lead a customer-focused service business. These include:

- An undergraduate double major in sociology and public communication (indicating an extroverted person who is interested in people).
- Feeling unrewarded in his first job in direct sales.
- Finding fulfillment in working for the Radisson hotel, where he benefitted from the mentorship of Jim Graves, who helped Larry develop an intense focus on the customer's experience in the design and execution of a service business.
- The "service heart" idea that self-defines Larry: "I get an adrenaline high from working with people who are service-oriented."
- The Radisson's "Yes I Can!©" spirit that Larry incorporated into his personal leadership philosophy that he now conveys to his employees.
- Several other customer service management positions that brought Larry into contact with both internal and external clients from a wide variety of walks of life, from the highly educated professional to employees needing basic coaching on punctuality.

2. <u>How does technology help drive service excellence at Executive Express?</u>

Answer:
The purpose of this question is to get students to recognize how essential technology is in 1) managing increasing complexity in a growing business, and in 2) providing timely access to information so employees are equipped to best serve the customer. Evidence to support the view that information technology was absolutely essential to Larry's success in meeting the needs of his customers, include:

- Larry's recognition that "we live in a global economy, and Executive Express needs to be available to serve customers 24 hours-a-day/7 days-a-week…There is an expectation from customers that we will have the ability to communicate and conduct commerce over the Internet."
- Immediately after purchasing the company, Larry installed a new phone system to capture messages from customers so he could get back to them.
- The failed experiment of trying to develop his own management software taught Larry that if the software doesn't work, the business cannot function.

- The capabilities of the Hudson Group software provided real-time information to Larry and other employees so they knew what they needed to do to best serve customers at any given moment.
- The technology allowed Larry to hire "Home-Base Reservationists" (HBRs) who are paid for each reservation they make. This was a significant cost savings.
- The technology provided data that Larry used to coach his HBRs and incentivize them to sell more roundtrip reservations to customers.

3. <u>Compare the different orientations toward people (i.e. customers and employees) held by the former owner/office staff of Executive Express and under Larry Logeman's leadership.</u>

Answer:
Evidence in the case indicates that the previous management had the view that both employees and customers were in many ways nuisances that needed to be managed and controlled:

- The former owner, Jerry counseled Larry not to answer the phone after business hours.
- The stern answering machine message that essentially told customers to wait until tomorrow to be served.
- Cheryl the office manager's explanation that if you let the drivers into the office, they'll just want coffee and stand around and talk.
- Cheryl's hanging up on an international customer whom she couldn't understand.

Larry's orientation toward both employees and customers is in stark contrast with the former owner's:

- Larry recruited drivers who wanted to serve customers, then trained them on how to do it.
- Larry made overt efforts to welcome his employees and make them part of his customer service team, providing coffee for drivers and exhorting them to join him in the office.
- Saying "yes" to customers whenever possible (e.g. driving the customer to International Falls).
- Communicating the "We Never Cancel!" slogan to customers to let them know that getting them to the airport is Executive Express's most important goal.

4. What is the break-even number of customers that Larry needs to cover the additional costs of moving from 10 to 14 daily roundtrips?

Answer:
From Figure 3:

4 additional roundtrips per day, Monday through Friday, * 5 days = 20
6 additional roundtrips per day, Saturday and Sunday, * 2 days = 12
Total number of additional roundtrips per week: 20 + 12 = 32
Total number of additional roundtrips per month: 32 * 4 = 128
128 roundtrips * 150 miles per roundtrip = 19,200 miles
19,200 miles / 15 miles per gallon fuel = 1,280 gallons
1,280 gallons fuel * $3.60 per gallon = **$4,608 additional fuel cost**
19,200 miles * $0.15 per mile maintenance expense = **$2,880 additional maintenance**
6 additional labor hours per day, Monday through Friday, * 5 days = 30 per week
10 additional labor hours per day, Saturday and Sunday, * 2 days = 20 per week
Total additional labor hours per week: 30 + 20 = 50
Total additional labor hours per month: 200
200 additional labor hours per month * $10 per hour = **$2,000 additional labor expense**

Total additional expenses per month: $4,608 + $2,880 + $2,000 = $9,488

$9,488 / $40 fare per one-way passenger = 237.2 one-way trips per month needed
237.2 trips per month / 30 days per month = 7.9 additional one-way trips per day needed
7.9 one-way trips per day / 14 roundtrips per day =
0.56 additional one-way fares needed per roundtrip to breakeven

5. What should Larry do regarding the decision to increase the number of daily roundtrips from 10 to 14 per day?

Answer:
Figure 2 of the case shows passenger volumes increasing steadily under Larry's leadership. The breakeven calculation in Question 4 indicates that a relatively modest increase of ½ customer fares (about $20) per roundtrip would cover the additional expenses of adding 4 more roundtrips per day from Monday-Friday, and 6 more roundtrips per day on Saturdays and Sundays. Given the history of growth in customer volumes over the past seven years, especially in the difficult environment of an economic recession, the chances are good that Executive Express won't lose money on the expansion.

Besides the breakeven calculation, there are a number of pros and cons that Larry must consider. Arguments that support Executive Express's service expansion include:

- Taking action now to build loyalty with existing customers, and build a base with new customers, could pay dividends if new competition (air service or another shuttle service) eventually enters in the market.
- The St. Cloud airport is a newly-renovated, beautiful, and functional facility that most likely will attract new air service.
- Adding more roundtrips per day supports the Executive Express business strategy of delivering convenience and reliability to customers.
- The new 14-trip schedule adds only a modest number of additional driver hours to the schedule, since drivers will be doing more driving and less waiting.
- Drivers will have more opportunity to earn tips because they will be serving more passengers per shift.

Arguments against the expansion include:

- A new air service might not be a significant threat, since twice-daily service would not fit the travel needs of many customers.
- There are short-term challenges of upgrading software and calling customers with existing reservations to switch over to the new schedule.
- Additional wear and tear on vehicles creates a need for more frequent vehicle replacements.
- Increasing to 14 roundtrips per day may generate a significant number of trips where no passengers are booked, especially on weekends. Larry will have to decide how to manage these costs while upholding the promises that were made to customers.

EPILOGUE

As of March 2012, Larry was working closely with The Hudson Group to get the software upgraded to handle the 14 roundtrips per day. He kept his team and drivers informed on the progress of the schedule implementation, and he was considering creating a new position to service the desk at the MSP airport to assist the drivers in customer check-ins, payments, luggage collection, etc. Larry was excited about the new schedule, while at the same time, he wondered if he was building capacity too far ahead of Executive Express's customer growth rate.

BEARKAT GAMES' CORPORATE TATTOO: A CASE FOR PERSUASION

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CASE DESCRIPTION

The primary subject matter of this case concerns the strategy for composing and delivering a written persuasive message in a business environment. Secondary issues examined include conducting primary and secondary research and employing APA citation skills. The case has a difficulty level of three to four (suitable for junior- or senior-level courses). The case is designed to be taught in approximately three class hours and is expected to require four hours of outside preparation by students.

CASE SYNOPSIS

Jon Osterman is the CEO of BearKat Games, a large gaming company headquartered in Houston, Texas, with offices in Dallas and San Antonio. Osterman has worked hard to make BearKat Games become a sought-after place to work. To achieve this goal, he has implemented practices that encourage employees to enjoy their work, feel pride in the company, develop strong relationships with co-workers, and—perhaps most importantly—stay with the company for the long term.

Two years ago, Osterman saw evidence that his efforts to increase employee loyalty had paid off. Brett Reed, a six-month BearKat employee, showed Jon his newest tattoo: the BearKat Games logo, prominently placed on his bicep. Brett's tattoo gave Jon an idea—what if he could persuade other employees to get tattoos of the company logo? Not only would the tattoos be a chance for employees to demonstrate their commitment to the company; they would also have great potential for marketing and publicity. He decided to offer a 15% bonus to any employee who chose to get a BearKat Games tattoo.

Pepper Potts is one of the employees who participated in the tattoo incentive; for the last several months, she has sported the BearKat Games logo on her ankle. Recently, however, the company decided to close its Dallas office, and Pepper's job was eliminated. She is now on the market for another job. Her BearKat Games tattoo—once a sign of professional pride—is now a professional liability. She would like to have the tattoo removed, and she wants BearKat Games to pay for it.

INSTRUCTORS' NOTES

RECOMMENDATIONS FOR TEACHING APPROACHES

The primary subject matter of this case concerns the development of a written persuasive message in a business environment. Secondary issues include conducting primary and secondary research and developing APA citation skills. The case has a difficulty level of three to four (suitable for junior- or senior-level courses). The case is designed to be taught in approximately three class hours and is expected to require four hours of outside preparation by students.

We use this case in conjunction with Shwom and Snyder's *Business Communication: Polishing Your Professional Presence* (2nd Edition) after classroom instruction in communicating persuasive messages. Before introducing this case, we discuss business research methodology and APA format with students. Students are further instructed that *how* a request is made—rather than the *nature* of the request—often determines the success or failure of the response. This case emphasizes the basic elements of persuasion:

Building credibility
Constructing a logical argument using the ACE (Analyze, Compose, Evaluate) approach
Appealing to the audience's emotions using *ethos*, *logos*, and *pathos.*

This case also enhances student understanding of the following issues:

Analyzing audience and establishing purpose, determining content, and choosing an appropriate channel
Composing the message using either an indirect or direct strategy (depending on the audience's receptivity), organizing the content and maintaining a professional tone, and formatting the document to support the message's purpose.
Evaluating the effectiveness of the message from the audience's viewpoint by: establishing that a problem exists; proposing a good solution with sound reasoning; addressing objections; emphasizing audience benefits; using effective paragraph structure and formatting; effectively using the principles of business communication; and maintaining goodwill.
Researching appropriate and convincing sources to add credibility to the appeal.
Documenting sources appropriately using APA format for in-text and reference citations.

DISCUSSION QUESTIONS AND WRITING ASSIGNMENT

PRELIMINARY QUESTIONS

1. Who is the primary audience for this message? Jon Osterman
2. Who is the secondary audience for this message? BearKat Games' insurance carriers, corporate management, and/or HR personnel.
3. Which strategy (direct or indirect) might be more effective in the BearKat Games scenario? Why? In answering this question, students should consider the company's decision to close the Dallas branch. How might the financial implications of this corporate action affect Jon's willingness to grant Pepper's request? The company may not be able to afford the costs associated with tattoo removal; further, insurance benefits may not apply unless former employees are offered the option of COBRA. What responses might the students' employ to overcome corporate objection to Pepper's request? Pepper might offer to pay half of the cost of removal herself or allow the company to reimburse her expense in several installments.
4. What channel would be the most appropriate for this type of message? E-mail attachment that could be easily forwarded to other constituents, business letter, or memo/ memo report for more permanent and long-term documentation.
5. What are the benefits to the company of removing the tattoo? The company would have more control of its brand (Pepper and other tattooed former employees would be walking proof of the company's failure). "Laid off" (and potentially unhappy) employees would be less likely to be asked what happened with the employer.
6. What business database would be most likely to contain information relative to this case? Business Source Complete is a good starting point. What other kinds of information will Pepper need to collect to make a convincing argument? Information from medical sites/dermatologists regarding tattoo removal and cost.

Writing Assignment

For this assignment, students should assume the role of Pepper Potts. They should write a persuasive message to BearKat Games' CEO, Jon Osterman, asking that the company pay for the removal of their tattoo. Students should use the ACE process and the information they learned in Chapter 5 of the course textbook.

Before composing the message, students will need to use primary and secondary research to discover the process for, and the time and cost involved in, removing a two-inch square tattoo. In constructing the argument, students should incorporate the issues in the preliminary questions discussed in class. Finally, students should follow APA in-text and reference citation format for any external sources used.

TECS TIME KEEPING FRAUD

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CASE DESCRIPTION

This case introduces students to a real fraud that occurred at a company called TECS. Students are introduced to the CEO of the company and his interactions with the employee who uncovers the fraud. Students get a firsthand account of the investigation as the employee investigators try to determine which employees were involved in the fraud. The employees involved in the fraud were time keepers within the company. The fraudsters were altering their time clock data to add extra hours to their paychecks. This case is targeted for students in undergraduate auditing, fraud, or forensic accounting courses. The case may be used as a take home assignment or as the focus of an in-class discussion.

CASE SYNOPSIS

This case is taken directly from the internal audit files of a large construction company. The paper illustrates a case of employee fraud where the manager of a time keeping department and one of his subordinates have been altering the time card data of the time keepers in their office. The fraudsters developed a scheme to be able to close their office for 2-3 hours a week and add the hours back to their time card data. In the case, a time keeping employee comes forward and identifies that at least two of her fellow employees have been altering the time card data for the entire local time keeping staff. The CEO of the company, Jim Edwards, is informed of the fraud by his director of internal auditing. Students are put in the role of Jim Edwards as he tries to think through the issues and tell his employees how the company will respond to the situation.

CASE OBJECTIVES AND USE

This case illustrates two separate fraud schemes perpetrated by the time keepers at a construction company. Students are introduced to the case through the eyes of the CEO of the company, who has just been informed of the fraud. The fraud occurs when the supervisor of the time keeping department is caught adding hours to him employees time card data. In one of the schemes, the supervisor takes advantage of a system flaw that ignores any two time card punches that are in very close proximity to each other. The second scheme involves the time keepers editing temporary data files after the time clocks are downloaded and before the data has been uploaded to the mainframe. The case can be used in an auditing course, fraud, or forensic accounting course. The case demonstrates a lack of proper preventative and detective controls within the time keeping department.

CASE OVERVIEW

This case is taken directly from the internal audit files of a large construction company. The paper illustrates a case of employee fraud where the manager of a time keeping department (Jay Gonzales) and one of his subordinates (Fay Fleming) have been altering the time card data of the time keepers in their office. The perpetrated a scheme to be able to close the office for 2-3 hours a week and add the hours back to the employees' time card data. In the case a whistleblower, Joan Degut, comes forward and identifies that at least two of her fellow employees have been altering the time card data for the entire local time keeping staff. The students are put in the role of Jim Edwards, the CEO of the company. Mr. Edwards is trying to determine what should be done now that the fraud has been discovered.

SUGGESTED CLASSROOM USE

This case has been specifically designed for use in an undergraduate auditing, fraud, or forensic accounting class. Before being exposed to the case students should be familiar with the following accounting topics:

1. The Fraud Triangle
2. Internal Controls
3. Preventive, Detective, Corrective Controls
4. Segregation of Accounting Duties
5. Forensic Evidence Protection
6. Whistleblower Protection Act

The case may be used as a group or individual project. Students should expect to spend about 60 minutes outside of class reading the case and background material.

STUDENT ASSIGNMENT

The students are asked to assume the role of Jim Edwards, the CEO of TECS and determine what factors he should consider, and what actions he should take. This assignment is designed for free flow discussion based only on the facts as presented in the case. Case Questions are presented in the instructor notes below. These questions may be used by professors to provide the students with a more structured exercise to approach the case. The Case Questions have been also been designed to provide instructors a structured approach to the Student Assignment requirements.

LEARNING OBJECTIVES

1. To read about how an actual fraud has occurred at a company.
2. To understand how a company may react after being of a fraud.
3. To understand the reasons for segregation of accounting duties.
4. To explore how internal controls could have prevented or detected the fraud that has occurred.
5. To foster a discussion regarding the types of controls that should be in place to prevent and/or detect theft.
6. To foster a discussion regarding management's treatment of employees who may be deemed whistleblowers.

CASE QUESTIONS

These questions may be used by an instructor to develop an in class discussion from the case. They may also be used for a structured take home assignment.

UNDERSTANDING THE SITUATION

1. It is important to understand all of the people involved in a case. Using the information provided in the case, identify the employees who are being investigated. Create a list of each employee involved in the fraud. Your list should contain: the name the employee, their job title (if given), and their role in the fraud.
2. It is important to understand the team you are working with in your investigation. Using the information in the case, identify each member of the investigative team. Make sure you list their name, job title, and each person's role in the investigation.
3. Explain how the time keeping employees used the manual data entry to alter their time clock data.
4. Explain how the time keeping employees were able to manipulate the temporary file on the local computer to alter their time clock data.
5. Criminalist Donald Cressey dubbed the term the "Fraud Triangle" to describe the three elements that are common in most frauds. These elements include: (1) Perceived Pressure/Motivation, (2) Perceived Opportunity, and (3) Rationalization. Discuss how each of these elements can be applied to Jay Gonzales's actions with respect to this situation.
6. There were two employees who were known to have altered the time clock data. What was their motivation for changing the time clock data?

7. List the legal requirements for fraud as defined by one of your textbooks or any definition you find using a credible online source.
8. Do the actions of the employees Jay Gonzales and Fay Fleming in this case meet the legal definition of fraud?
9. Sometimes the terms "Larceny" and "Embezzlement" are used to clarify the type of crime that has been committed. Which of the following term is most appropriate to schemes perpetrated in this case?
10. In determining internal controls for a company we discuss segregation of accounting duties which distinguish between custody of assets, record keeping, and authorization functions. How do the time keepers at TECS fit into the segregation of accounting duties for the other functional departments of TECS?
11. In what manner is Tony Lemond responsible for this fraud occurring? What was his role in the perpetrating of this scheme? What could he have done differently?
12. We often discuss controls as preventive, detective, and corrective. With respect to the scheme perpetrated by the employees in this case, what internal controls could the company put in place in each of these categories?

FORENSIC EVIDENCE MANAGEMENT

13. In the case we are told that the audit team and computer specialist opened and searched the computer files. How would their actions impact the possibility of criminal prosecution of the employees involved in the fraud?
14. If the company planned to prosecute the individuals involved, what steps should have taken when they suspected that a fraud was occurring?

WHISTLEBLOWER

15. Should Joan Degut be considered a whistleblower?

SUGGESTED ANSWERS TO CASE QUESTIONS

UNDERSTANDING THE SITUATION

1. It is important to understand all of the people involved in a case. Using the information provided in the case, identify the employees who are being investigated. Create a list of each employee involved in the fraud. Your list should contain: the name the employee, their job title (if given), and their role in the fraud.

Note to Professor: The purpose of this question is to make the students identify the employees involved in the fraud. The list allows students to summarize and demonstrate their understanding of the complex interchange of employees in the case.

The employees involved in the fraudulent scheme are as follows:

> **Jay Gonzales** is the central time keeping supervisor. We know that Jay has told Joan that he has "Taken care of her" with respect to hours being added to her paycheck. It is suspected that Jay Gonzales has used the manually entered punches to trigger the "proximity punch" mechanism in the system to override the system data. Jay may also be responsible for altering the time clock data on the local computer.
>
> **Fay Fleming**, senior time keeping clerk. While Jay was out of the office Fay was responsible for altering the time clock data on at least one occasion. Fay claims she understood that the scheme could be perpetrated using the manual punches but she feigned ignorance to being able to alter the time card data on the local computer.
>
> **Penny Moore** (and other unmentioned time keepers), central office time keeper. These people responsible for time keeping all stated they never realized they were underpaid.

2. It is important to understand the team you are working with in your investigation. Using the information in the case, identify each member of the investigative team. Make sure you list their name, job title, and each person's role in the investigation.

Note to Professor: The purpose of this question is to make the students identify the employees who are involved in the investigation. The list allows students to summarize and demonstrate their understanding of the employees who investigated the time clock data scheme.

1. Tony Lemond, Administrator and Risk Manager. Tony and another employee built the time keeping system. Tony Lemond oversees all company operations, including central time keeping.
2. Joan Degut, central time keeping. Joan is the employee who noticed she is overpaid. She first goes to her manager Jay Gonzales to see if it was a mistake. Jay indicates that he "took care of her." She finds her time card data has been altered again after Jay is out of the office and she realizes the situation is really bad. She then notifies Tony Lemond.
3. Jim Edwards, CEO. Mr. Edwards is responsible for putting together the investigative team, including the student who is asked to assume the role of a consultant.

4. Sandy Morgan, IT Staffer. Mrs. Morgan's role in the investigation was to help pull data from the system as needed.
5. Kat White, internal audit director. Ms. White helped to create the narrative of how things were supposed to happen in the Central Time Keeping department. She also documented the investigation and reported the results of the investigation to Jim Edwards.

3. Explain how the time keeping employees used the manual data entry to alter their time clock data.

Note to Professor: This question requires students to differentiate between the two methods of fraud that occurred at the company.

The time keeping software at TECS had two features that were used in tandem to alter the time clock data. The first feature known as a "proximity punch" was designed to cut down on the amount of manual adjustments that had to be made to data collected in the field. The company found that employees often "double punched" that is, they would swipe their card once thinking they were leaving for the day and then be called back into the location and swipe back in. The time keeping system was designed to ignore both of the punches if they occurred within five minutes of each other. The system was also designed to allow time keeping employees to enter manual time card punches directly into the system. In the first scheme, Jay and or Fay would let the time keeping employees go home early. The employees would clock out when the left the office. The fraudsters would then enter a manual time card entry within five minutes of the employees legitimate clock punch. The fraudster would then enter a second manual clock entry clocking the employees out two hours later. The time keeping system would ignore the two clock punches that were within five minutes of each other (the actual punch and the manual punch) and calculate the extra two hours on the employees' time sheet.

4. Explain how the time keeping employees were able to manipulate the temporary file on the local computer to alter their time clock data.

Note to Professor: This question requires students to differentiate between the two methods of fraud that occurred at the company.

The time clocks have a temporary memory that is downloaded to a local computer. The local computer stores the downloaded time clock data in a temporary file where it awaits a command to upload the new data to the central time keeping system. Once the local computer uploads the data the temporary clock data is added to a cumulative log file that shows what data has been uploaded. The employees perpetrating this scheme were able to get into the temporary data file on the computer and alter the data before it was uploaded into the system. So the time keeping system only shows the edited data with no manual punches for the March 15th and March 22nd data.

5. Criminalist Donald Cressey dubbed the term the "Fraud Triangle" to describe the three elements that are common in most frauds. These elements include: (1) Perceived Pressure/Motivation, (2) Perceived Opportunity, and (3) Rationalization. Discuss how each of these elements can be applied to Jay Gonzales's actions with respect to this situation.

Note to Professor: This question allows students to examine the motivation and factors that may have allowed the fraud to occur as well as my Jay Gonzales may have committed the fraud. The question allows students to expand their knowledge of the fraud triangle beyond textbook definitions.

Pressure/Motivation- In this case, the pressure and motivation is not what we normally see with respect to frauds. Jay Gonzales and Fay Fleming were in fact stealing from the company as they were altering their own time card data. But the fraud perpetrators were also stealing from the company on behalf of other employees. Normally we see fraudsters who are either in personal debt or who have aspirations of acquiring nicer things than they can afford. In this case it appears the motivation may be that of a manager trying to give his employees unsanctioned company perks. He was allowing them to leave early two hours a week and still paying them for those hours.

Perceived Opportunity- The opportunity in this case is clearly the ability the time keepers have in this system to either overwrite data in temporary files on the local computer and/or to create manual clock punches. The time keepers are a critical part of the segregation of accounting duties. The time keepers play the role of record keepers from the other departments within the company. The time clock punches are source data and the time keepers take this data and record the data into the time keeping system. Unfortunately, the time keepers are also employees of the company. When it comes to recording their own time card data the time keepers have access to both the source documents and authorization to record and/or edit the data.

Rationalization- Jay Gonzales seems to rationalize his role in this scheme as both an underappreciated worked who has spent "many nights and weekends fixing problems for this company" and as a good guy boss who told Joan Degut "I took care of you." Jay may have felt that he and his staff were under appreciated by upper management when it came to salaries. The company deals with such large amounts on their contract that the time keeping employees see large amounts of money being paid to highly skilled workers. There is a change the time keepers felt underpaid and Jay was just trying to keep his employees happy.

6. Put yourself in the shoes of Jay Gonzales and explain why you should not be fired for perpetrating this scheme.

Note to Professor: The purpose of this question is to allow the students to discuss the factors commonly associated with frauds. In the current case it does not appear that the common fraud factors are at work here. This question allows students to try to put themselves in the shoes of a manager just caught for altering his employees' time cards. Students answer will vary on this question. Many students will try to take an easy way out and state that Mr. Gonzales should be fired. But these students are being asked to answer the question from Jay Gonzales' perspective.
Some of the reasons students may come up with when thinking like Jay Gonzales:

1. He was trying to be a good manager and reward his employees with a small perk.
2. The amount was immaterial to the company.
3. The system should have prevented this from happening.
4. They cannot prove that he did anything wrong!
5. His years with the company should mean something.

7. List the legal requirements for fraud as defined by one of your textbooks or any definition you find using a credible online source.

Note to Professor: This case has been designated as an employee fraud. Students should have a working legal definition of fraud.
Student answers to this question will very as different sources have different definitions of fraud. One definition of fraud as stated by Romney and Steinbart in the textbook Accounting Information Systems 12th Edition (Page 123), is the "Fraud is a gaining an unfair advantage over another person." The authors also identify five items that are required for an act to be legally considered fraudulent. Those five items are:

1. Some type of statement that is false
2. The statement must be in regards to a material fact
3. The statement must be made with an intention to deceive.
4. The victim must have been justified in relying on this statement
5. There must be some injury or loss to the victim.

8. Do the actions of the employees Jay Gonzales and Fay Fleming in this case meet the legal definition of fraud?

Note to Professor: This question requires the students to apply the definition of fraud they find in question 7 to the details of this case.

The actions of Jay Gonzales and Fay Fleming absolutely meet the definition of fraud as given in answer 7. The false statement was the altered time clock data. The employees entered this data or altered this data with the intention of deceiving management. Time keepers are supposed to be trustworthy employees and even small deviations from the truth could be considered material. The amount of theft for each instance might have been low but over time, these small amounts add up. The employees altered this data with the intention to deceive the company into thinking they and they employees worked when in fact they had not. The company was justified in relying on the time card data. The injury to the company was the extra wages they paid to these employees.

9. Sometimes the terms “Larceny” and “Embezzlement” are used to clarify the type of crime that has been committed. Which of the following term is most appropriate to schemes perpetrated in this case?

Note to Professor: Often in a forensic class the terms larceny and embezzlement are a part of the textbook. This question requires students to consider the fraud in this case and to go beyond memorizing a simple definition.

> Larceny- larceny is a crime of possession. That is one individual intentionally takes personal property from someone else without consent and then they appropriate it for their own use. In several legal resources they make specific note that with larceny there was no prior legal possession of an asset before it was misappropriated (Black, 1977).
>
> Embezzlement- Embezzlement differs from larceny in that with embezzlement the person misappropriating the asset has legal custody of the asset (not legal title but legal custody) at the time they misappropriate the asset for their own use (Black, 1977).

In this case the employees would be committing larceny. If the employees were in the payroll department and were responsible for cutting the checks for payroll we may say they perpetrated an embezzlement as they were given legal custody of the payroll accounts to make legitimate payroll payments. In the TECS case, the employees submitted what amounted to false documents to the payroll department which then issued payments to the time keepers. Since the time keepers had no possession of the assets they were acquiring, they would be guilty of the crime of larceny.

10. In determining internal controls for a company we discuss segregation of accounting duties which distinguish between custody of assets, record keeping, and authorization functions. How do the time keepers at TECS fit into the segregation of accounting duties for the other functional departments of TECS?

Note to Professor: This question requires students to really think about the role the time keepers play at TECS with the respect to the segregation of accounting duties.

With respect to the segregation of accounting duties the time keepers are in a unique position. They play the role of record keepers and authorizers in the company. The data they receive, evaluate for errors, store, and approve is used to authorize the payroll department to release company funds to employees. The time keepers are also employees of the company and at TECS they are responsible for recording and storing records regarding their time card data. This is a violation of the segregation of duties and as we can see from the fraud in the case, the employees took advantage of this system limitation to alter their time card records.

11. In what manner is Tony Lemond responsible for this fraud occurring? What was his role in the perpetrating of this scheme? What could he have done differently?

Note to Professor: This question is designed to make students think about the role that upper management and the designers of the system had in the incident.

Tony Lemond is the administrator and risk manager who over sees all operations of the company, including the time keeping department. Mr. Lemond was also one of the developers of the time keeping system being used by TECS.

Students should be able to construct an argument that as the administrator overseeing operations which include the time keeping department that Mr. Lemond should be responsible for developing a system of controls that would prevent his employees from altering their time card data and not being caught. As a risk manager, Mr. Lemond should be aware of the risk of having the time keepers serving as the record keepers over their own records and also having the power to authorize the payroll department to pay them for the amounts they have recorded. Students may also point blame to Mr. Lemond as the time keeping system designer. Mr. Lemond helped create the system in use and he should have been away of the risks of the combination of manual data entries and proximity punches being used to defraud the system. Mr. Lemond should have also realized the temporary data files downloaded from the time clocks were not password protected or encrypted.

Mr. Lemond should have also noticed that an entire department of employees was closed for a few hours each week during normal business hours.

12. We often discuss controls as preventive, detective, and corrective. With respect to the scheme perpetrated by the employees in this case, what internal controls could the company put in place in each of these categories?

Note to Professor: The purpose of this question is to allow the students to discuss the three types of internal controls (preventive, detective, and corrective).

Preventive controls:

Preventative controls are controls that prevent employees from engaging in illicit behavior or behavior the company does not want them to do. In this case, preventive controls can be broken down by accounting duties and application system functions. With respect to accounting duties, the time keepers in central time keeping should not be allowed to the record keepers and authorizers of payroll funds for any of their own personal data. A separate employee from the central time keepers should be responsible for keeping the records pertaining to the central time keepers. If it is not feasible to have independent employees keeping the records the company should have good detective controls and managements monitoring in place to prevent the employees from getting away with such schemes.

With respect to the time clock system and installing preventative controls, the company should make sure the software that downloads the clock data prevents users from altering that clock data on the location machine before it is uploaded to the time keeping system. Password controls on the file as well as possibly encrypting the file may prevent unauthorized users from altering the file. Employees not authorized to handle time keeping data should not use the computer terminal for other purposes.

Detective Controls-

Detective controls should be designed to detect if employees have engaged in behavior that management does not want them to do.

The company should design detective controls to determine if manual time clock entries were entered into the system. This can be a simple report that looks at all of the data marked as manual entries. These entries should be reviewed by someone outside of the time keeping department.

The company should also design detective controls to determine if the time card data has been altered on the local computer. In the current case, the historical log files stored only the changed data. There was not a way of comparing the historical log on the computer with the temporary file. There is technology available that can track changes to files and keep records of different files and versions of files. I use a program that does an online backup of my files. This program also keeps a historical record of files I delete or change so that I may restore the changed files. The company could employ such as system and if a historical version is present it would indicate there were changes to the file.

The company can also do surprise audits of the time clock data by taking the time clocks and downloading the data themselves before the time keepers download the data. The raw data could then be compared to the data that was uploaded to the system.

The company could also have detective controls built into the network monitoring system. These controls could indicate a lack of activity from specific departments.

Corrective Controls

Corrective controls are controls put into place after there has been a detected violation of company policy. In this case, TECS had employees hastily dig through the computer system to see what evidence they could find to support Joan Degut's claims. These actions will be discussed in the forensic evidence questions below.

The company interviewed and fired a few of the employees involved in the scheme. They should probably re-train or re-assign the employees who were not fired.

The company should also modify the way the time keepers work by having independent employees record the central time keepers' hours. Having additional monitoring by supervisors can be a new control put in place to prevent this from happening.

Forensic Evidence Management

13. In the case we are told that the audit team and computer specialist opened and searched the computer files. How would their actions impact the possibility of criminal prosecution of the employees involved in the fraud?

Note to Professor: It is important for students to understand how employees' actions after allegations of an incident of fraud may impact the company's ability to prosecute guilty individuals.

If the company had any hopes of having the employees who perpetrated this scheme prosecuted by law enforcement, the actions of the audit team may have made that impossible. We are told that the audit team began by examining electronic records. By simply opening up the electronic records, the audit team can corrupt important metadata within the files. If the corrupted evidence was given to law enforcement, the criminal investigators would have a difficult time determining if the changes in the system were made by the employees in the time keeping department or if the changes were made by investigative team.

14. If the company planned to prosecute the individuals involved, what steps should have taken when they suspected that a fraud was occurring?

Note to Professor: This question will help guide students in finding out what steps they should take or recommend their company takes if they ever discover a fraud occurring in their company.
The company brought in a forensic investigator as soon as possible. The forensic investigator would have documented the procedure performed on the system. These procedures would have most likely involved making exact images of the company files before doing any type of examination of the data. If management determines there is a strong possibility of a fraud occurring and management knows they want to prosecute the individuals responsible for the fraud, and then management should bring law enforcement into the investigation as well.

Whistleblower Protection

15. Should Joan Degut be considered a whistleblower?

Note to Professor: This question allows students to explore who should be considered a whistleblower depending on their actions and the company they work for.
Joan Degut is absolutely a whistleblower. What is not so clear cut is if she is afforded protection under the Sarbanes Oxley Act of 2002. TECS has been identified as a publically traded company on the NASDAQ exchange. As a publically traded company, TECS is subject to compliance with the Sarbanes Oxley Act of 2002. Since Joan Degut reported what amounts to an employee fraud against the company and not a corporate fraud against the shareholders, her actions would not be protected under the Sarbanes Oxley Act of 2002. There may be other state laws that would protect her actions. In the TECS case upper management was appreciative of Joan Degut's actions. The employees who remain employed at TECS must be instructed to not retaliate against Joan Degut.

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REAL ESTATE INVESTOR'S INC.

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CASE DESCRIPTION

This case can be used to focus on several different types of analysis – financial, management and investor goals, and strategy. The case traces the evolution of a small real estate investment company created by three individuals who meet in an MBA Program. The case also addresses the synergies and conflicts of meshing personal lives with the creation, management, and growth of a small business. This case would be most appropriate for undergraduate courses in small business management and graduate courses as a class discussion. The case is designed to be discussed in one to one and one-half hours and should take students no more than three hours of outside preparation.

CASE SYNOPSIS

Ryan Mathau is one of three partners in a relatively young and small real estate investment company, which was created in 2004 when capital is easily available. The three partners purchase inexpensive rental buildings in need of significant work, renovate and standardize the buildings, and then manage the rental properties. The partners stopped buying shortly before the 2008 banking crisis and were content to hold their current size until an opportunity presented itself in 2011. At the same time Ryan is experiencing increased time conflicts in his personal life and begins to question the long hours he is putting into this business while also employed full-time as an accountant. The company and Ryan must decide where to go from here.

INSTRUCTORS' NOTES

CASE QUESTION

1. What should Ryan and REI, Inc. Do? Possible options:
   Hold current size
   Buy current opportunity, and then hold new size
   Buy current opportunity and begin renewed growth
   Do not buy current opportunity, but pursue renewed growth
   Divest some holdings
   Change roles and / or the way company is operated

Compare and contrast each option above. Give one clear, well-defined option with supporting arguments and financial consideration.

ANSWER TO CASE QUESTION

1. What should Ryan and REI, Inc. Do? One of the first things that should be delineated in the student's response is their decision criteria, and most importantly what is the primary goal that the company is trying to achieve, and whether or not it is an agreed upon goal. What do the partners want, and how can that be best achieved. The student should also address the change in the market place after the banking crisis, what are the implications for the rental business.

This case opens up all kinds of issues. The first --- is this a good investment? Given that all of the financial analyses conclude with a positive NPV (net present value) --- this is a good investment (given the financial assumptions the NPV is between $8,000 and $35,000). Yet, there are other issues to consider --- HVAC, roof, foundation structure, and electrical wiring. If these four systems check-out it would appear to be a good investment.

The major issue is --- can this partnership survive? It appears that Ryan wants out. The changes in his life and the industry have impacted his out-look on this business. Consequently, he no longer is willing to contribute to the business and wants to exit (and that is the problem). REI is a partnership and the partners did not specify how they would dissolve the organization or divide the equity. When a partner becomes dissatisfied or just wishes to leave it can be a situation fraught with problems.

The major problem is --- how will the partnership handle this situation. The easiest way would be for the two remaining partners to agree to buy Ryan out (but all must agree on a price and/or method to execute this process). How much should Ryan receive as a payout? The easiest method would be to determine how much the organization is worth as a going concern and then pay Ryan one-third. In 2011 it is estimated that free cash flows will be around $57,000 (see income statements). A reasonable price earnings ratio would be 4 (or 4 X $57,000 = $228,000). A one-third share would be $76,000. The partners could agree to pay Ryan $76,000 and all would be happy.

Yet, this might not be the best or fairest valuation. The case states that the organization's properties are worth $4,137,630 and that the partners have a 29.5% equity holding. So the equity holding of the partnership is ($4,137,630 X .295 = $1,220,600). Ryan is entitled to one-third or $406,866. So the firm is worth between $76,000 and $406,866 depending on how the value is determined. This situation will have to be negotiate, and therein lies the problem. The dissolution of this partnership will hurt all three partners in some way.

Due to the current cash situation the two remaining partners cannot "buy-out" Ryan without selling properties. Because the real estate market is depressed this will hurt everyone. Ryan wants out and thus, is a drag on operations. All types of creative and viable options are available, but students should gain insights into picking partners wisely and/or establish a firm exit plan.

ALABAMA AIR SHUTTLE: FIGHT OR FLIGHT

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ABSTRACT

David Gentry, owner of Alabama Air Shuttle, had to decide whether to continue the operation of his charter service or close its doors. If he chose to remain in business, then a new strategic plan had to be developed to combat declining revenue streams. If he decided to leave the private flight industry, then several exit strategies had to be explored, including selling the business as a whole, liquidating the major assets, leasing aircraft to fractional owners, or simply shutting down.

INSTRUCTORS' NOTES

CASE INTENDED USES

This case was designed for an undergraduate level entrepreneurship or business strategy course. Following discussion of the case, students should be able to identify key factors that play defining roles in paths to entry and in the life of a business entity. Market analysis, operational strategy, and financial forecasting are all relevant issues that can be gleaned from this case study. It is recommended that this case be used in conjunction with textbook reading assignments covering business strategy applications.

RESEARCH METHOD

This case was derived from interviews and company documents provided by David Gentry, the owner and operator of Alabama Air Shuttle, as well as industry research by the authors. Financial figures have been omitted and/or adjusted to protect confidentiality.

TEACHING OBJECTIVES

1. To identify the need for decision makers to understand and use the proper tools available for industry, business, and economic analysis.

2. To examine ways in which poor implementation of analyses can have far-reaching effects on a business.
3. To understand the risks associated with initial debt and fixed costs for startup companies.
4. To examine how passion for starting a business can cause one to overlook negative information about the industry or market and lead to flaws in business strategy.

RELEVANT THEORIES

Theories that can be tied to this case include Marketing Mix Strategies, Fatal Strategic Implementation Mistakes (especially *Misunderstanding Industry Attractiveness*), Resource-based Management and Competitive Advantage, and Financial Analysis.

TEACHING SUGGESTIONS

The focus towards the beginning of class should be on understanding the broad outline of the case to include the Airline industry, the timing of the economic cycle, and the financial position of the company. After giving a brief overview of the various general topics, the instructor could then go into greater detail on the individual subjects that would include discussing more detailed information about types of planes, pricing of flights, marketing strategy, strategic planning, and financial trends of the company.

Discussion questions will be a good tool to utilize for the in depth discussions that should occur. When working through the SWOT make sure to encourage class involvement as well as extended class discussion about the various topics. Additionally, you may want to close the class with the final question (should Alabama Air Shuttle continue operations or exit the market place?) and have the class discuss all of the information of the case, weigh the positives and negatives and attempt to develop a class consensus on which direction Alabama Air Shuttle should head.

SUMMARY OF DISCUSSION QUESTIONS

1. Analyze Alabama Air Shuttle using the SWOT analysis.
2. What are some of the important key issues that are present in this case?
3. Analyze Alabama Air Shuttle's marketing strategy and define its marketing mix. What would you do the same/differently?
4. Discuss the challenges and/or pitfalls of the pricing strategy, including any surcharges.
5. Discuss Alabama Air Shuttle's competition. Does Alabama Air Shuttle have a competitive advantage? If so, was this competitive advantage sustainable/ realistic?
6. Are there any identifiable fatal flaws in Alabama Air Shuttle's business strategy?

7. What do the financial performance trends of Alabama Air Shuttle suggest about the viability to sustain operations?
8. What adjustments to Alabama Air Shuttle's strategic plans would benefit the business?
9. Should Alabama Air Shuttle remain open or exit the marketplace? If the decision to close is made, what is the best way to exit the market to minimize loss? If the decision to remain open is made, what needs to be done to increase revenues?

DISCUSSION QUESTIONS

An "A" student will identify most of the following assessments. Average students will identify the obvious points, but will fail to catch the subtle complexities of the situation. "A" answers are noted with an asterisk.

1. Analyze Alabama Air Shuttle using the SWOT analysis.
   - Strengths: (internal)
     - *David's passion for flying and his prior experiences with the bank in creating businesses and marketing plans were strengths for his company.
     - Alabama Air Shuttle also had few competitors in Alabama that used multi-piston planes.
     - They were also equipped with a multi-plane FAA Certification, which required a large amount of resources and time investment.
   - Weaknesses: (internal)
     - *The niche market of servicing small businesses (under $10 million in annual revenue) may have been too small. With economic fluctuations, these small businesses often cut business travel expenses first which would greatly decrease business in an industry that needed high volume to turn a profit.
     - *In addition to the niche market, there were many barriers to entry into the charter industry. These barriers included high capital investments in equipment and numerous regulations and requirements to obtain and maintain an FAA Certificate. These barriers placed Alabama Air Shuttle in a position of deep debt before any revenue stream was realized.
     - David overestimated industry attractiveness even though he was warned that this type of business would not succeed in Alabama because of the low profit margin.
     - The percentage of returning customers was relatively small (90% of his business came from 10% of his customers as compared to the traditional 80/20 rule. Also, 68% of his customer base only took one trip and 92% took less than five trips).
   - Opportunities: (external)

  - He could have exited the market using alternatives such as selling the company, leasing out the planes, or entering the Beech Barons into a charter management program.
  - David could have weathered the bad economy and searched for alternatives.
  - *Alabama Air Shuttle could have expanded its customer base by carrying cargo or expanded its target market to include bigger businesses, engaged in a personal selling campaign, co-branded with other businesses such as Carnival Cruise Lines or other air carriers, or explored the possibility of fractional ownership. ("A" students will address the possibilities that each option could bring to Alabama Air Shuttle's financial improvement.)

- Threats: (external)
  - The major external factor that affected Alabama Air Shuttle was the downturn of the economy as well as changes in the business environment. Since the fall of 2008, many industries were hit very hard with the collapse of financial and lending institutions. One of the hardest hit areas was construction and development (one of the major clients of Alabama Air Shuttle).
  - On the heels of the financial crisis came the poor press from the CEOs of the Detroit Auto companies, when they flew to Washington, DC to get "bailed out" in their private luxury jets. Combine the down-turn in the economy coupled with the negative stigma associated with chartered aircraft, and what developed was a "perfect storm" scenario where those businesses that had the capital to spend for private air charters were cutting back due to the public perception of flying a chartered aircraft.
  - Additional external factors that affected Alabama Air Shuttle were the majority of their flights, which originated from Birmingham, only covered areas which were easily driven for sales people and therefore cheaper alternative means of travel were able to be utilized during this economic environment.
  - All other competitive charter companies utilized larger, faster aircraft with longer flight ranges. The one other competitor that used a multi-engine piston plane also utilized larger turbo-props and jets.
  - *An "A" student may also recognize that the market research performed in 2002 may have misrepresented the market. Due to the attacks on the World Trade Center, the fears of flying commercially may have lead to an overly positive response to the surveys that inquired about the use of charter planes.

2. What are some of the important key issues that are present in this case?

- *Unrealistic expectations and projections. The expectation that within 2–3 years the business would have to add 2–3 more planes and a jet within 4–5 years was simply unrealistic. Also, the idea that working with Carnival Cruise lines would be a soft sell may have also been unrealistic. No strategic plans were made to accomplish these goals because David believed that the demand would be there to support such projections.

- Undercapitalization. Alabama Air Shuttle could have benefited from outside investors because the charter industry was so capital intensive.
- Overestimating industry attractiveness. This lead to mistakes such as overlooking negative feedback about the market. David received warnings from others in the aviation industry and failed to recognize the external factors such as the climate after 9/11 that may have caused a distortion of the market research from NFO Worldwide.

3. Analyze Alabama Air Shuttle's marketing strategy and define its marketing mix. What would you do the same/differently?

Alabama Air Shuttle's marketing mix was comprised of its product, price, promotion and placement (distribution).

- Product: Alabama Air Shuttle had very high standards for providing a first class service charter operation. Their goal was to provide a simple, safe and economical option for small business travel. The only downfall to the product offered was that multi-engine piston planes were slower and had a shorter range than other turbo-props or jets. And although piston planes were less expensive per hour, more time in the air not only meant a longer travel time, but also meant more expense for the client.
- *Price: Alabama Air Shuttle was priced competitively at $5 under their competitor's price per hour. However, this competitor also operated other aircraft at higher prices, which may have allowed them to keep their price low while still making enough revenue from their other aircraft to remain profitable. Alabama Air Shuttle did not have any other source of revenue. Both planes were priced at $695 per hour and provided a very thin profit margin. It may have benefited Alabama Air Shuttle to re-evaluate their pricing strategy.
- Promotion: Advertising included several print ads that produced little, if any, pull on the market. Additional charitable radio and TV spots produced little effect as well. The website did bring in a large percentage of new customers and David did a good job in increasing web presence through his blog and video. Marketing plans mentioned the possibility of expanding the business to manage other aircraft, perhaps increasing the promotion of this business aspect with direct advertising to aircraft owners and larger businesses would have produced a new revenue stream.

*Alabama Air Shuttle also outlined a very targeted market by focusing on small businesses that earned under $25 million in annual revenue with the assumption that larger businesses utilized company owned jets and small mom and pop operations had little need to travel.

- Placement: Alabama Air Shuttle was based in Huntsville and Birmingham, AL—a centralized location for the Alabama market. Although the planes could be positioned to any small airport in range, additional fees applied when this was necessary. Perhaps research could be done to determine if another airport (such as Montgomery, Mobile or even Atlanta) would be more beneficial as a base location.

4. Discuss the challenges and/or pitfalls of the pricing strategy, including any surcharges.

   Pricing was a challenge for Alabama Air Shuttle, just as it is for any business with tight margins; the company must set prices to make money, but must also set prices to attract clients. It was believed that a competitive advantage could be established by charging $169-$589 for the Huntsville-Birmingham-Montgomery-Mobile shuttle concept. There was little demand for this route and pricing structure, and Alabama Air Shuttle figured out relatively quickly that it must change its course of action to make the business work. The pricing structure was actually lower than most of the other private charter companies ($695/hr compared to a competitor's $700/hr), but the demand for actual flights was not as great as initially anticipated. The competitor also operated additional aircraft that charged substantially more per flight hour. Perhaps this allowed the competition to keep the price of multi-engine piston planes low while earning a higher profit by operating turbo-props and jets.

   *With the rise of oil prices also came the need to add a fuel surcharge. Since most companies in the business were adding a fuel surcharge, this did not affect Alabama Air Shuttle's ability to compete, however it did make the client's option of driving more attractive. Overall, the primary challenge with pricing was the inability to charge enough to make a larger profit margin.

5. Discuss Alabama Air Shuttle's competition. Does Alabama Air Shuttle have a competitive advantage? If so, was this competitive advantage sustainable/ realistic?

   *Alabama Air Shuttle faced both direct and indirect competition. There were many air charter businesses located in Alabama that served as direct competition, as well as pilots who flew passengers without FAA licensing. Indirect competition consisted of commercial air and private jet charter services. Automobile travel also served as a form of indirect competition. (An "A" student will note all of these competitors, while an average student will only note the direct competitors.)

*Business travelers had many options when considering business travel. In order to be successful, Alabama Air Shuttle had to form and maintain a competitive advantage against the competitors mentioned above. Time was the competitive advantage that was naturally achieved through flight when comparing Alabama Air Shuttle to any sort of automobile travel. Many travelers would have preferred to fly rather than drive in order to reach a destination in a shorter period of time. Alabama Air Shuttle also had a competitive advantage against commercial air services in the form of location. Because Alabama Air Shuttle used smaller aircraft, pilots could land at various airports throughout the state; commercial flights were only limited to large airports. Business travelers could fly directly into a smaller city, instead of having to land in a major city and then take a car to a smaller town. This saved travelers more time. ("A" students will notice competitive advantages over all travel options, while the average student will only make a comparison of Alabama Air Shuttle to other charter services.)

The hardest competitive advantage to achieve would be one that could put Alabama Air Shuttle in a better position than other air charter services. Time savings tactics and smaller airport locations could be achieved by any other private charter company. The only way for Alabama Air Shuttle to develop a competitive advantage was to be competitive in pricing. Different pricing factors could be considered, but Alabama Air Shuttle had to be able to deliver the same standard of service for a less expensive fare than its competitors. This was in fact the line of reasoning that Alabama Air Shuttle pursued. Although a good idea in theory, private chartering was an industry that was already marginally slim in profits—to slice away at profit margins in order to give customers a "deal" was business suicide. Alabama Air Shuttle attempted this technique, but ultimately realized that not enough profit was made per flight hour. The competitive advantage was legitimate but not sustainable. Alabama Air Shuttle would have had to make up in volume what it lost in revenue per hour, which it was unable to do.

6. Are there any identifiable fatal flaws in Alabama Air Shuttle's business strategy?

There were several strategic flaws that proved fatal for Alabama Air Shuttle. First, there was an inherent misunderstanding of industry attractiveness. David was told many times by many different people who were already in the aviation business to avoid private charter. He was told that the industry was too capital-intensive and too slim in profit margins.

There was also no real sustainable competitive advantage. Alabama Air Shuttle attempted to differentiate on a cost basis, but was unable to achieve this goal on a long-term basis.

*Market research could not be proven to be reliable or valid. So many of Alabama Air Shuttle's strategic decisions were based on the market research by NFO Worldwide; however, that research was questionable due to the timing and climate in which the surveys were conducted.

*Alabama Air Shuttle made poor financial projections in the upstart and failed to analyze financial data once the company was up and running. Using the proper tools, Alabama Air Shuttle could have diagnosed severe financial problems and made attempts to turn the business around at a much earlier date. (An "A" student will reference ROA and Debt/Service ratios mentioned in the case.)

7. What do the financial performance trends of Alabama Air Shuttle suggest about the viability to sustain operations?

   If Alabama Air Shuttle could have started with revenues that were being produced in 2008, then the company would have been much better off in facing the economic downturn in 2009. However this was not the case and the three years of building the business from 2004–2007 significantly harmed Alabama Air Shuttle's ability to weather any type of financial storm. Limited reserves in the form of cash or back up financing were crippling. With all of the resources to fund cash flow shortfalls being used in the first three years, the company could not face another year of cash flow deficits and that was what occurred in 2009.

8. What adjustments to Alabama Air Shuttle's strategic plans would benefit the business?*

   Any adjustment that could have been made to preserve emergency cash reserves or financing should have been made. One example would be to bring in investors on the front end. The downside to bringing in investors is that it takes time and energy to sell the company to people who are looking to invest. However, the feedback that would be received from the investors, both negative and positive, would have been beneficial to the upfront planning of Alabama Air Shuttle. A good adjustment that Alabama Air Shuttle made was getting away from the concept of the Alabama shuttle with regular routes, which did not seem to attract the demand needed for the business to succeed.

   *Another adjustment would have been to focus more on their webpage and internet marketing. The webpage could have included an option where potential customers to type in starting destinations and ending destinations with a price estimate being presented.

9. Should Alabama Air Shuttle remain open or exit the marketplace? If the decision to close is made, what is the best way to exit the market to minimize loss? If the decision to remain open is made, what needs to be done to increase revenues?

   The exit strategy is one of the most important parts of any entrepreneur's plan and should be included in every business strategy. Having a goal in mind can help to determine long-term company decisions and prevent the limiting of future options.

   *If the decision is made to close Alabama Air Shuttle, there are many different methods to exit the marketplace—liquidation, selling to a client/friendly buyer, using a business broker, or even the "bleed" method.

   Liquidation is a process in which the majority of business owners exit the market. In most cases, the entrepreneur reaches the point where it is time to close the business. The most common form of liquidation is bankruptcy, which involves the selling and breaking up of a company to satisfy creditors via court system. The other primary method would be to just close the doors and sell everything off for whatever the owner can get. The benefit is that there is no worry about transfer of control, and except in the case of bankruptcy, it relatively simple to execute. Drawbacks from using this method are that it destroys any business relationships and eliminates loyal customers should the owner open another business. An additional drawback is that in most cases, only market value can be recovered of what is sold.

   Selling to a client/friendly buyer most commonly refers to selling the business to another family member. Other methods include selling the business to your employees or even one of your clients. All three cases share similar pros and cons. The pros of this method is that typically less due diligence is required since both parties know each other, and the buyer tends to be committed to making the business work. The primary con of this method is that most owners are too close to the buyer and therefore sell the business for much less than they would have sold to an outside buyer. In the case of families buying a business, fighting and deep seeded issues can rise up and destroy not only the business but also the family without clear instructions given by the owner. Changing ownership from one family member to another can also affect the employees of the company based on their view of the new owner. When selling a business to employees, they believe in the company they have worked to help build and tend to preserve the goals and ethics from the previous owner. Selling to a client tends to benefit the client by allowing them to continue to have the service benefit of your company even after the owner has decided to leave the market.

   A business broker, sometimes called business transfer agents, act as intermediaries (essentially like consultants) helping buyers find sellers. The broker values the business, advertises, screens buyers, conducts negotiations, performs due diligence, and closes the sale. In addition to these steps, business brokers can also help mask the identity of the company during the selling process which helps keep from scaring customers and hurting the bottom line. While there are many benefits to using a business broker, the business owner must sign a listing contract with that broker (thus being only able to use them), and the broker normally takes a commission of 10–12% at closing.

The final method of exiting the marketplace is to use the “bleed” method. This method requires a company to generate consistent profits and the goal is to bleed the company dry over a period of time. In order to utilize this method, company investors must be at a minimum and entrepreneurs must have determined that the business is nothing more than a “lifestyle company.” Entrepreneurs raise their salaries to exorbitant levels, pay massive bonuses regardless of performance and sometimes even issue special shares only to themselves with ridiculous dividends. Typically because of the need for almost no investors, this method only works for private companies in order to avoid investor outcry.

*If the decision is made to stay open, Alabama Air Shuttle should consider: recapitalization, acquisition, or a repositioning and re-branding campaign.

Capital is what makes any business work. Without it, businesses crumble and die. One method for recapitalization is to get a loan from a banking institution. If no banking institutions are willing to provide loans, then venture capital firms should be approached as well as angel investors. While bringing venture capital firms and angel investors on board will provide much needed capital for a business, the owner also must give up partial or even majority ownership in the company in exchange for that capital. By giving up such a large stake in your company, you no longer control the destiny of your dream.

A structured acquisition of Alabama Air Shuttle by another air charter business would allow Alabama Air Shuttle to continue operations as a division or sub-company and expand market presence and market share. This would allow David to continue operations without selling his business outright and also provide access to additional planes and clients. Alabama Air Shuttle would be able to leverage against the acquiring company’s client list while also providing a new market niche product to the acquiring company. While this could benefit both David and the acquiring company, a carefully structured agreement would have to be put in place in order to ensure Alabama Air Shuttle’s continuing operations and also ownership stake.

By repositioning and re-branding, Alabama Air Shuttle will expose its company to new customers and even be able to expand services to its current customers. One avenue is to develop an air cargo business model. Most of the large air lines, especially Southwest, started with air cargo as the main revenue generator and then expanded to air carrier operations. While competition from FedEx, UPS, DHL, and the US Postal

Service would be present, Alabama Air Shuttle could never-the-less enter the market and for strategic partnerships with hospitals and automotive plants to help lower costs. Additionally, by repositioning Alabama Air Shuttle to take advantage of high end travel, David could build co-branding opportunities with travel agents and cruise operators. Even in recessions, the wealthy still have the disposable income to travel. By co-branding with travel agents in the area, along with in Huntsville, Montgomery, and Mobile, Alabama Air Shuttle could expand their travel offerings and build packages for cruises and football games.

EPILOGUE

David Gentry ultimately decided to close his business. After attempting several exit strategies—including fractional selling of aircraft and selling the business outright—the best scenario was simply to cut his losses. Revenue streams were not healthy enough to continue operations without increasing debt. David liquidated his assets and sold both planes, but at prices significantly less than their purchased values. Other assets such as headsets, cell phones and cabinets went to Paul Nation. David currently retains his customer list and FAA manuals that could possibly be sold in the future; however, his Air Carrier Certificate was voluntarily surrendered and could not be sold due to FAA regulations. Alabama Air Shuttle closed its doors in April 2010. Staying true to his entrepreneurial spirit, David has started a new business that aids small businesses in developing simple, easy and affordable websites.

THE SOUTHEASTERN THEATER COMPANY

Roger Gagnon, North Carolina A&T State University

CASE DESCRIPTION

The case concerns planning job/staffing needs and schedules for employees and management for a medium-size movie theater. The students are required to: (1) analyze the amount of time required to perform work activities; (2) recognize that the amount of work and time required may differ by season, day, or even hour; (3) recognize that particular work activities can only be performed by certain classes of workers or management; (4) calculate how many employees of each type are needed to complete the work required; and (5) create feasible schedules for each type of employee. This case is designed for level three and up and is appropriate for undergraduate juniors and beyond. The case can be taught in two class hours in an operations management, production management, services management, or human resources management course. It is expected to require about three hours of outside preparation and necessitates familiarity with spreadsheet software

CASE SYNOPSIS

One of the more difficult, but necessary, business areas to instruct is : how to design jobs – how to combine work tasks, not on an assembly line, into jobs; how many employees to have for each job category; and how to schedule them on a seasonal, daily, and even hourly basis. Production/operations text offer suggestions (e.g., job enrichment, job enlargement, team assignments), but few specific examples, problems, or cases are available. This case portrays an environment that all students have visited – a movie theater. The case requires the students to recognize the various job skills required; determine the amount of time required to perform various work activities and that this capacity can fluctuate by season, day, or hour; calculate how many employees of each type are needed to complete the work required; and create feasible work schedules for each type of employee.

INSTRUCTORS' NOTES

Suggested Questions and Answers to Case Questions

Before embarking on the specific questions and suggested solutions let us restate the assumptions presented in the case:

There is one general manager who works a 45 hour week and must be present for Friday, Saturday, and Sunday evening shows.
There is at least one assistant manager who works a 40 hour week and at least one assistant manager must be present for Fridays, Saturday and Sunday evening shows from 6:00 PM until 12:00 AM.
Any number of ticket sales personnel can be hired, but they are the only hourly employees who can sell tickets. They are not assigned to concessions, ticket collection duties, or cleaning/restocking duties.
Any number of concession workers can be hired to prepare the concession areas, sell concessions, perform clean-up, or do restocking.
The capacities of the screening rooms, the average sales per week per season, the average percentages of weekly sales attributed to each day, and the average percentages of daily sales per show time are provided in the case.

Potential Case Questions

1. How many assistant managers, ticket sales agents, projectionists, ticket collectors, and concession workers should the company schedule for an average week, per day, and per hour during the busy season and the slow season?

2. To simplify the case solution the instructor could ask the students to calculate just one or more from the following list (for one or both seasons):

   The number of assistant managers
   The number of ticket sales agents
   The number of projectionists
   The number of ticket collectors
   The number of concession workers

Since they can perform the most duties the number of concession workers is the most complex and time-consuming to calculate, but takes the students through all the necessary thought processes necessary to plan the number needed and their schedule.

3. **Another alternative is to ask the students to calculate the number of employees (one or more from the above list) for the busiest and/or slowest days of the year (i.e. Saturday during the busy season and Monday during the slow season).**

Thus, the case offers many possible question scenarios from very straight-forward to complex, but more realistic. For completeness the Teaching Notes will offer solutions and potential, feasible schedule assignments for all employee jobs.

Managers and Assistant Managers

For the management staff the theater operates 12.5 hours per day (11:30 PM to 12:00 AM) for 7 days per week. This totals 87.5 hours. If we assume that a manager or assistant manager is required for one-half hour after the theater closes each night to deposit the day's proceeds, then this adds an additional 3.5 hours per week. In addition **both** the general manager and one assistant manager must be present for all Friday Saturday, and Sunday evening showings from 6:00 PM to 12:00 AM, this adds another 18 hours for a total of 109 (87.5 + 3.5 + 18 = 109) manager hours needed per week. Since each general manager works a 45 hour week and an assistant manager works 40 hours per week, we will need one general manager and two assistant managers. This will provide us with a total of 45 + 2x40 = 125 manager hours available per week with obvious overlap on the busiest days of Friday, Saturday, and Sunday.

One possible weekly schedule for the managers for either slow or busy seasons could be:

	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday	Sunday
Manager	11:30-6:00	Off	6:00-12:30	5:00-12:00	4:00-12:30	4:00-12:30	4:00-12:00
Asst. Mgr. 1	Off	11:30-6:00	11:30-6:00	6:00-12:30	4:00-12:00	6:00-12:00	6:00-12:30
Asst. Mgr. 2	6:00-12:30	6:00-12:30	Off	11:30-6:00	11:30-6:00	11:30-7:00	11:30-6:00

Ticket Sales Agents

The theater sells an average of 7,000 tickets per week during the "slow seasons" (February to April and September to October) and an average of 15,000 tickets per week during the "busy seasons" (May to August and November to January). Given the daily percentages of weekly sales provided in the case, we can calculate the number of ticket sales per day of the week for each season, as shown in Tables 1 and 2. The case also provides the percentages of daily sales attributable to each movie (time) showing. Thus, we can calculate the average number of arrivals and tickets sold during each the three distinct sales patterns (30 to 10 minutes before, 10 before to 5 minutes after, and 5 to 20 minutes after the scheduled movie showing time) per scheduled movie show time (1:00, 4:00, 7:00 or 9:45 PM) per day of the week and season. The case states the percentages of patrons who arrive at certain time blocks for movies are:

28.6% arrive between 30 - 10 minutes before the scheduled showing time
50% arrive between 10 minutes before to 5 minutes after the scheduled showing time
21.4% arrive between 5 - 20 minutes after the scheduled showing time

These calculations are provided in Tables 1 and 2.

Table 1 TICKET SALES FOR EACH SHOW TIME PER DAY FOR THE SLOW SEASON Slow Season (7,000 ticket sales per week)											
					Number of Ticket Sales per Day and Show Times*						
	Daily % of Weekly Sales	**Daily Sales**	**Show Times**	**% of Daily Sales**	**MON**	**TUES**	**WED**	**THUR**	**FRI**	**SAT**	**SUN**
Mon	0.06	420	1:00 PM	0.10	42	70	84	105	140	175	84
Tues	0.10	700	4:00 PM	0.25	105	175	210	262.5	350	437.5	210
Wed	0.12	840	7:00 PM	0.40	168	280	336	420	560	700	336
Thurs	0.15	1,050	9:45 PM	0.25	105	175	210	262.5	350	437.5	210
Fri	0.20	1,400									
Sat	0.25	1,750		**SUM**	**420**	**700**	**840**	**1,050**	**1,400**	**1,750**	**840**
Sun	0.12	840									
	SUM	**7,000**									
*Daily sales x % of sales per show time											

Table 2 TICKET SALES FOR EACH SHOW TIME PER DAY FOR THE BUSY SEASON											
Busy Season (15,000 ticket sales per week)											
					Number of Ticket Sales Per Day and Show Times*						
	Daily % of Weekly Sales	**Daily Sales**	**Show Times**	**% of Daily Sales**	**MON**	**TUES**	**WED**	**THUR**	**FRI**	**SAT**	**SUN**
Mon	0.06	900	1:00 PM	0.10	90	150	180	225	300	375	180
Tues	0.10	1,500	4:00 PM	0.25	225	375	450	562.5	750	937.5	450
Wed	0.12	1,800	7:00 PM	0.40	360	600	720	900	1,200	1,500	720
Thurs	0.15	2,250	9:45 PM	0.25	225	375	450	562.5	750	937.5	450
Fri	0.20	3,000									
Sat	0.25	3,750		**SUM**	**900**	**1,500**	**1,800**	**2,250**	**3,000**	**3,750**	**1,800**
Sun	0.12	1800									
	SUM	**15,000**									
*Daily sales x % of sales per show time											

With this information, the assumption that the arrivals are uniformly distributed, and the average times given in the case for selling tickets, we can determine the number of ticket sales agents needed for each scheduled movie time for each day of the week and per season. As shown in **bold** print in Table 3 the busiest or "peak period" (greatest number of tickets sold per minute) for each show time is the 15 minute period, which includes the 10 minutes before and 5 minutes after the scheduled movie time (in which 50% of patrons arrive to purchase tickets), **this is the only period we need to highlight to determine the number of employees needed to sell tickets for that show time.** Focusing the resources needed to cover the "peak periods" should be a beneficial learning experience for the students. Table 3 shows the number of ticket agents needed to cover all show times for each day of the week for both the slow and busy seasons. As can be seen the required number of ticket agents needed varies from 1 to 4 during the slow season and from 1 to 9 during the busy season (the Saturday 7:00 PM show time being the busiest).

As an example of the calculations in Table 3, **12.01** customers arrive between 30 to 10 minutes before the 1:00 PM show on Monday during the slow season. This number was determined by multiplying to total attendees for the 1:00 PM show (42) times the percent who typically arrive during that time period (.286) or 42 x .286 = 12.01. The number .60 in the next row is simply the average arrivals per minute or 12.01/20 = .60. The number of theoretical ticket agents needed to sell these tickets during this time frame (evenly distributed) is simply .60/5 = .12 agents. The number of actual ticket agents needed is the theoretical number rounded up to the next integer.

Ticket Collectors

We need to determine how many "ticket collectors" are needed per season, days, and show times. While this calculation may appear burdensome, it is quite simple. The case mentions that a ticket collector can process up to 30 tickets per minute. Thus, only when the average number of patrons arriving exceeds 30 per minute does the theater require more than one ticket collector. An examination of Table 3 quickly reveals (**in bold numbers**) that we only need to examine the **peak period** (10 minutes prior to and up to 5 minutes after the show time) during the busy period for this determination. Two ticket takers will only be required during the Busy Season on Friday evenings for the 7:00 PM show time and Saturday evenings for the 4:00 PM, 7:00 PM, and 9:45 PM movie showings. The theater never requires more than 2 ticket collectors. Thus, the recognition of the importance of this peak period for this calculation is essential. One potential schedule for the days requiring only 1 ticket collector per show time could be as follows:

	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday	Sunday
1 Ticket Collector	12:00-4:00	12:00-4:00	12:00-4:00	12:00-4:00	12:00-4:00	12:00-4:00	12:00-4:00
	4:00-8:00	4:00-8:00	4:00-8:00	4:00-8:00	4:00-8:00	4:00-8:00	4:00-8:00
	8:00-11:30	8:00-11:30	8:00-11:30	8:00-11:30	8:00-11:30	8:00-11:30	8:00-11:30

Table 3
NUMBER OF TICKET SALES AGENTS FOR EACH SHOW TIME PER DAY FOR THE SLOW SEASON
(7,000 ticket sales per week)

	Monday				**Tuesday**				**Wednesday**			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**
Total number of patrons arriving from 30 to 10minutes prior to the scheduled movie time	12.0	30.0	48.1	30.0	20	50	80	50	24.0	60.1	96.1	60.1
Average number of patrons arriving per minute	0.60	1.50	2.40	1.50	1	2.50	4	2.50	1.20	3	4.80	3.60
Theoretical number of ticket agents needed	0.12[a]	0.30	0.48	0.30	0.20	0.50	0.80	0.50	0.24	0.60	0.96	0.60
Actual number of ticket agents needed	1	1	1	1	1	1	1	1	1	1	1	1
Total number of patrons arriving from 10 minutes prior to 5 minutes after the scheduled movie time	**21**	**52.5**	**84**	**52.5**	**35**	**87.5**	**140**	**87.5**	**42**	**105**	**168**	**105**
Average number of patrons arriving per minute	**1.40**	**3.50**	**5.60**	**3.50**	**2.33**	**5.83**	**9.33**	**5.83**	**2.80**	**7**	**11.2**	**7**
Theoretical number of ticket agents needed	**0.28[a]**	**0.70**	**1.12**	**0.70**	**0.47**	**1.17**	**1.56**	**1.17**	**0.56**	**1.17**	**1.87**	**1.17**
Actual number of ticket agents needed	**1**	**1**	**2**	**1**	**1**	**2**	**2**	**2**	**1**	**2**	**2**	**2**
Number of patrons arriving from 5 minutes to 20 minutes after the scheduled movie time	8.90	22.5	36.0	22.5	15.0	37.5	59.9	37.5	18.0	44.9	71.8	44.9
Average number of patrons arriving per minute	0.59	1.50	2.40	1.50	0.60	1.50	2.40	1.50	0.72	1.80	2.88	1.80
Theoretical number of ticket agents needed	0.12[a]	0.30	0.48	0.30	0.12	0.30	0.47	0.30	0.14	0.36	0.58	0.36
Actual number of ticket agents needed	1	1	1	1	1	1	1	1	1	1	1	1

	Thursday				**Friday**				**Saturday**			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**
Total number of patrons arriving from 30 to 10minutes prior to the scheduled movie time	30.0	75.1	120	75.1	40.0	100	160	100	50.1	125	200	125
Average number of patrons arriving per minute	1.50	3.75	6.01	3.75	2	5.01	8.01	5.01	2.50	6.26	10.0	6.26
Theoretical number of ticket agents needed	0.30[a]	0.75	1	0.75	0.40	0.83	1.33	0.83	0.50	1.04	1.67	1.04
Actual number of ticket agents needed	1	1	1	1	1	1	2	1	1	2[D]	2	2[D]
Total number of patrons arriving from 10 minutes prior to 5 minutes after the scheduled movie time	52.5	131	210	131	70	175	280	175	87.5	219	350	219
Average number of patrons arriving per minute	3.50	8.75	14	8.75	4.67	11.7	18.7	11.7	5.83	14.6	23.3	14.6
Theoretical number of ticket agents needed	0.70[a]	1.46	2.33	1.46	.93	1.94	3.11	1.94	1.17	2.43	3.89	2.43
Actual number of ticket agents needed	1	2	3	2	1	2	4[D]	2	2[b]	3	4	3
Number of patrons arriving from 5 minutes to 20 minutes after the scheduled movie time	22.5	56.2	89.9	56.2	30	74.9	120	74.9	37.5	93.6	150	93.6
Average number of patrons arriving per minute	1.50	3.75	5.99	3.75	2	4.99	7.99	4.99	2.50	6.24	9.99	6.24
Theoretical number of ticket agents needed	0.30[a]	0.75	1	0.75	0.40	1	1.33	1	0.50	1.04	1.66	1.04
Actual number of ticket agents needed	1	1	1	1	1	1	2	1	1	2[b]	2	2[b]

	Sunday			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**
Total number of patrons arriving from 30 to 10 minutes prior to the scheduled movie time	24.0	60.1	96.1	60.1
Average number of patrons arriving per minute	1.20	3	4.81	3
Theoretical number of ticket agents needed	0.24	0.60	0.96	0.60
Actual number of ticket agents needed	1	1	1	1
Total number of patrons arriving from 10 minutes prior to 5 minutes after the scheduled movie time	**42**	**105**	**168**	**105**
Average number of patrons arriving per minute	**2.80**	**7**	**11.2**	**7**
Theoretical number of ticket agents needed	**0.56**	**1.17**	**1.87**	**1.17**
Actual number of ticket agents needed	**1**	**2[b]**	**2**	**2[b]**
Number of patrons arriving from 5 minutes to 20 minutes after the scheduled movie time	18	44.9	71.9	44.9
Average number of patrons arriving per minute	1.20	3	4.79	3
Theoretical number of ticket agents needed	0.24	0.60	0.96	0.60
Actual number of ticket agents needed	1	1	1	1

a= The average number of patrons per minute divided by 5 (if arrival rate = 5 or less per minute) and 6 (if arrival rate exceeds 5 per minute)

b = While the number is rounded to the next highest integer, the theater would likely use the manager or assistant manager to fill in briefly as the partial ticket sales person.

Table 3 (continued)
NUMBER OF TICKET SALES AGENTS FOR EACH SHOW TIME PER DAY FOR THE BUSY SEASON
(15,000 ticket sales per week)

	Monday				**Tuesday**				**Wednesday**			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**
Total number of patrons arriving from 30 to 10minutes prior to the scheduled movie time	25.74	64.4	102	64.4	42.9	107	172	107	51.5	129	206	129
Average number of patrons arriving per minute	1.29	3.22	5.15	3.22	2.15	5.36	8.58	5.36	2.57	6.44	10.3	6.44
Theoretical number of ticket agents needed	0.26[a]	.64	.86	.64	.43	.89	1.43	.89	.51	1.07	1.72	1.07
Actual number of ticket agents needed	1	1	1	1	1	1	2	1	1	2[b]	2	2[b]
Total number of patrons arriving from 10 minutes prior to 5 minutes after the scheduled movie time	**45**	**113**	**180**	**113**	**75**	**188**	**300**	**188**	**90**	**225**	**360**	**225**
Average number of patrons arriving per minute	**3**	**7.50**	**12**	**7.5**	**5**	**12.5**	**20**	**12.5**	**6**	**15**	**24**	**15**
Theoretical number of ticket agents needed	**0.60[a]**	**1.25**	**2**	**1.25**	**1**	**2.08**	**3.33**	**2.08**	**1**	**2.50**	**4**	**2.50**
Actual number of ticket agents needed	**1**	**2**	**2**	**2**	**1**	**3[b]**	**4**	**3[b]**	**1**	**3**	**4**	**3**
Number of patrons arriving from 5 minutes to 20 minutes after the scheduled movie time	19.26	48.2	77.0	48.2	32.1	80.3	128	80.3	38.5	96.3	154	96.3
Average number of patrons arriving per minute	1.28	3.21	5.14	3.21	2.14	5.35	8.56	5.35	2.57	6.42	10.3	6.42
Theoretical number of ticket agents needed	0.26[a]	0.64	0.86	0.64	0.43	0.89	1.43	0.89	0.51	1.07	1.71	1.07
Actual number of ticket agents needed	1	1	1	1	1	1	2	1	1	2[b]	2	2[b]

	Thursday				**Friday**				**Saturday**			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**
Total number of patrons arriving from 30 to 10minutes prior to the scheduled movie time	64.35	161	257	161	85.8	215	343	215	107	268	429	268
Average number of patrons arriving per minute	3.22	8.04	12.9	8.04	4.29	10.7	17.2	10.7	5.36	13.4	21.5	13.4
Theoretical number of ticket agents needed	0.64[a]	1.34	2.15	1.34	.86	1.79	2.86	1.79	.89	2.23	3.58	2.23
Actual number of ticket agents needed	1	2	3[b]	2	1	2	3	2	1	3	4	3
Total number of patrons arriving from 10 minutes prior to 5 minutes after the scheduled movie time	**112.5**	**281**	**450**	**281**	**150**	**375**	**600**	**375**	**188**	**468**	**750**	**468**
Average number of patrons arriving per minute	**7.5**	**18.8**	**30**	**18.8**	**10**	**25**	**40**	**25**	**12.5**	**31.2**	**50**	**31.2**
Theoretical number of ticket agents needed	**1.25[a]**	**3.13**	**5**	**3.13**	**1.67**	**4.17**	**6.67**	**4.17**	**2.08**	**5.21**	**8.33**	**5.21**
Actual number of ticket agents needed	**2**	**4[b]**	**5**	**4[b]**	**2**	**5[b]**	**7**	**5[b]**	**3[b]**	**6**	**9**	**6**
Number of patrons arriving from 5 minutes to 20 minutes after the scheduled movie time	48.15	120	193	120	64.2	161	257	1610	80.3	201	321	201
Average number of patrons arriving per minute	3.21	8.03	12.8	8.03	4.28	10.7	17.1	10.7	5.35	13.4	21.4	13.4
Theoretical number of ticket agents needed	0.54[a]	1.34	2.14	1.34	0.86	1.78	2.85	1.78	0.89	2.23	3.57	2.23
Actual number of ticket agents needed	1	2	3[b]	2	1	2	3	2	1	3	4	3

	Sunday			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**
Total number of patrons arriving from 30 to 10 minutes prior to the scheduled movie time	51.48	129	206	129
Average number of patrons arriving per minute	2.57	6.44	10.3	6.44
Theoretical number of ticket agents needed	0.51	1.07	1.72	1.07
Actual number of ticket agents needed	1	2[b]	2	2[b]
Total number of patrons arriving from 10 minutes prior to 5 minutes after the scheduled movie time	**90**	**225**	**360**	**225**
Average number of patrons arriving per minute	**6**	**15**	**24**	**15**
Theoretical number of ticket agents needed	**1**	**2.50**	**4**	**2.50**
Actual number of ticket agents needed	**1**	**3**	**4**	**3**
Number of patrons arriving from 5 minutes to 20 minutes after the scheduled movie time	38.52	96.3	154	96.3
Average number of patrons arriving per minute	2.57	6.42	10.3	6.42
Theoretical number of ticket agents needed	0.51	1.07	1.71	1.07
Actual number of ticket agents needed	1	2[b]	2	2[b]

a= The average number of patrons per minute divided by 5 (if arrival rate = 5 or less per minute) and 6 (if arrival rate exceeds 5 per minute)

b = While the number is rounded to the next highest integer, the theater would likely use the manager or assistant manager to fill in briefly as the partial ticket sales person.

Recall that high school and college students are scheduled for only 3-4 hour shifts on Monday through Thursday and, thus, the three shifts shown daily in the above table. However, on Fridays, Saturdays, and Sundays these students can be scheduled for up to 8 hours. Thus, on Friday, Saturday, and Sunday two students could split the 11.5 hours in various combinations. High school students, however, cannot be scheduled before 3:30 PM on Friday.One potential schedule for Saturday during the busy season requiring 2 ticket collectors for the 4:00 PM, 7:00 PM and 9:45 PM shows could be as follows:

Saturday 1 Ticket Collectors 12:00-8:00 (The first ticket collector arrives at 12:00 PM.) 2 Ticket Collectors 3:30-11:30* (Another ticket collector arrives at 3:30 PM.) 2 Ticket Collectors 8:00-11:30*, ** (The final ticket collector arrives at 8:00 PM.)*This overlap is necessary because patrons start arriving 30 minutes before the scheduled show times.** Another alternative is simply to schedule the first ticket collector from 12:00 to 3:30 PM and 2 ticket collectors from 3:30 PM to 11:30 PM. **Projectionists**At least one projectionist is needed 4 days a week (Monday through Thursday) and two on Friday, Saturday, and Sunday evening shows (60 minutes before the first the 7:00 PM show time until the end of the last showing (usually about 12:00 AM). This totals 105.5 hours (7 days x 12 hours per day + 1 additional projectionist x 3 days [Fri., Sat., Sun.] x 6 hours [6:00 PM to 12:00 AM] + 7 days x .5 hour for nightly deposit = 105.5 hours. Thus, at least 3 projectionists would be needed at a minimum. While some could work full time, they were paid on an hourly basis. To assure an adequate supply of projectionists the theater used up to 4 projectionists particularly during busy weeks (e.g. release of a new James Bond movie, AVATAR, etc.). Several would be scheduled on a full time basis and several for just partial shifts (4 to 6.5 hours) and on the busy weekends. From Monday through Thursday two projectionists could be scheduled for six hours each (one would work 6.5 hours to aid with the nightly deposits). On weekends one additional projectionist would be scheduled from 6:00 PM to 12:00 PM. One of the projectionists would work to 12:30 AM to assist with the nightly deposit. Thus, a weekly schedule could look as follows:

Projectionist	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday	Sunday
Number 1	12:00-6:00	Off	12:00-6:00	12:00-6:00	12:00-6:00	12:00-6:00	12:00-6:00
Number 2	6:00-12:30	6:00-12:30	Off	6:00-12:30	6:00-12:00	6:00-12:00	6:00-12:00
Number 3					6:00-12:30	6:00-12:30	6:00-12:30
Number 4		12:00-6:00	6:00-12:30				

Obviously, there could be swapping of shift assignments so that the same projectionist would not always “open the theater” or the same projectionists always deposit the nightly receipts. Also, the time allocated to projectionist #4 could easily be assigned to projectionist #3 giving that person a total of 32 hours.**Concession Workers (CWs)**Concession sales consumed the most time for concession workers.

As mentioned in the case 30% of patrons made purchases at the concession bar and an average concession purchase serves two patrons. Each concession purchase requires an average of 2 minutes. Table 4 shows the number of concession purchases, the time required to service them, and the number of concession worker hours and workers needed.The calculations for the data in Table 4 can be explained as follows. The number of patrons arriving from 30 to 10 minutes preceding the 1:00 PM show on Mondays during the slow season is 12.01 (420 x .286). Of these 12.01 patrons 30% (or 3.60) will desire some food and/or beverage from the concession bar. Each concession purchase typically serves an average of 2 patrons. Thus, on average 3.60/2 = 1.80 purchases will be made during this period. On average each concession purchases requires 2 minutes and, thus, 3.60 minutes of concession worker time will be required. Since the patron arrivals and concession purchases are considered equally spaced throughout this 20 minute arrival period, only 3.6/20 = .18 concession workers are required for this period. The theoretical number of concession workers needed is rounded up to the next integer or 1. Again note that the peak period (greatest number of concession purchases made per minute) occurs agano headerin during the 10 minutes prior to 5 minutes after the show time period; during this period the greatest number of arrivals occur and the available service time during this arrival period is shorter - only 15 minutes). Thus, this peak period controls the number of concession workers needed for each show time, day, and season. As shown in the Table 4 the number of concession workers varies greatly from 1 for Monday 1:00 PM shows during the slow season to 15 for the 7:00 PM show on Saturday during the busy season. However, since there are four point-of-sale registers per concession bar, two concession bars, and two concession workers can be assigned to each register the theater can handle the maximum demand (2 concession bars x 4 POS registers per bar x 2 CWs at each POS = 16 CWs). In addition to concession sales the CWs perform other duties including preparing, cleaning, and restocking the concession bar area. These work tasks are completed before the first patron arrivals (preparing the concession bars and equipment) or after the start of the last show (cleaning and restocking) and, thus, do not require additional concession workers.Table 5 shows feasible schedules for the concession workers covering the CW capacity needs for each day, show time, and season. The scheduling objectives are:*Satisfy the demand for concession worker serviceMinimize the number of concession worker hours scheduled per week.No concession worker should be scheduled for less than 3 hours per dayNone can be scheduled for more than 8 hours per dayHigh school and college students cannot be scheduled for more than 4 hours on Monday through Thursday.High school and college students can be scheduled for up to 8 hours on Friday, Saturday, and Sunday.High school students cannot be scheduled earlier than 3:30 PM on Monday through Friday. College students can be scheduled for any time of day.The number of high school or college students available for concession worker positions was unlimited.*

Table 4

NUMBER OF PATRONS PURCHASING CONCESSIONS, SONCESSION SERVICE TIME REQUIRED AND NUMBER OF CONCESSION WORKERS REQUIRED IN THE SLOW SEASON

	Monday				Tuesday				Wednesday				Thursday				Friday				Saturday				Sunday			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**
Number arriving 30 to 10 minutes prior to showtime	12.01	30.0	48.05	30.03	20.0	50.0	80.0	50.0	24.02	60.06	96.10	60.06	30.03	75.08	120.12	75.08	40.04	100.10	160.16	100.1	50.05	125.13	200.20	125.13	24.02	60.06	96.10	60.06
Number of concession purchases	1.80	4.50	7.20	4.50	3.00	7.50	12.00	7.50	3.60	9.01	14.42	9.01	4.50	11.26	18.02	11.26	6.01	15.02	24.03	15.02	7.51	18.77	30.03	18.77	3.61	9.01	14.42	9.01
Concession purchase time required (in minutes)	3.60	9.0	14.40	9.0	6.0	15.0	24.0	15.0	7.20	18.02	28.82	18.02	9.0	22.56	36.04	22.52	12.02	30.04	48.06	30.04	15.02	37.54	60.06	37.54	7.22	18.02	28.82	18.02
Theoretical # of CW staff needed	0.18	0.45	0.72	0.45	0.30	0.75	1.20	0.75	0.36	0.90	1.44	0.90	0.45	1.13	1.80	1.13	0.60	1.50	2.40	1.50	0.75	1.88	3.00	1.88	0.36	0.90	1.44	0.90
Actual number of CW staff needed	1	1	1	1	1	1	2	2	1	1	2	1	1	2	2	2	1	2	3	2	1	21	3	2	1	1	2	1
Number arriving 10 minutes prior to 5 minutes after show time	21.0	52.5	84.0	52.50	35.0	87.50	140.0	87.50	42.0	105.0	168.0	105.0	52.50	131.25	210.0	131.25	70.0	175.0	280.0	175.0	87.50	218.75	350.0	218.75	42.0	105.0	168.0	105.0
Number of concession purchases	3.15	7.88	12.60	7.90	5.25	13.20	21.0	13.2	6.30	15.75	25.20	15.75	7.88	19.69	31.5	19.69	10.50	26.25	42.0	36.0	13.13	32.82	52.50	32.82	6.30	15.75	25.20	15.75
Concession purchase time required (in minutes)	6.30	15.80	25.20	15.80	10.50	26.20	42.0	26.20	12.60	31.50	50.40	31.50	15.76	39.38	63.0	39.38	21.0	52.50	84.0	72.0	26.26	65.64	105.0	65.64	12.60	31.50	50.40	31.50
Theoretical # of CW staff needed	0.42	1.05	1.68	1.05	7.00	1.76	2.80	1.76	0.84	2.10	3.36	2.10	1.05	2.63	4.20	1.40	1.40	3.50	5.60	4.80	1.75	4.40	7.00	4.40	0.84	2.10	3.40	2.10
Actual number of CW staff required	**1**	**2**	**2**	**2**	**1**	**2**	**3**	**2**	**1**	**3**	**4**	**3**	**1**	**3**	**5**	**3**	**2**	**4**	**6**	**5**	**2**	**5**	**7**	**5**	**1**	**3**	**4**	**3**
Number arriving 5 to 20 minutes after show time	8.90	22.47	35.95	22.47	14.98	37.40	59.90	37.40	17.97	44.90	71.80	44.90	22.50	56.20	89.90	56.20	29.96	74.90	119.80	74.90	37.40	93.60	149.80	93.60	17.98	44.90	71.90	44.90
Number of concession purchases	1.30	3.37	0.39	3.37	2.25	5.61	8.99	5.61	2.70	6.74	10.77	6.74	3.38	8.43	13.48	8.43	4.49	11.24	17.97	11.20	5.61	14.04	22.47	14.04	2.70	6.74	10.79	6.74
Concession purchase time requires (in minutes)	2.60	6.74	10.80	6.74	4.50	22.40	17.98	11.20	5.40	13.48	21.54	13.48	7.76	16.86	27.96	16.86	8.99	22.48	35.94	22.40	11.20	29.08	45.94	29.08	5.40	13.48	21.58	13.47
Theoretical # of CW staff needed	0.17	0.45	0.72	0.45	0.63	0.75	1.19	1.75	0.36	0.90	1.45	0.90	0.52	1.13	1.80	1.13	0.60	1.50	2.40	1.50	0.75	3.75	3.06	1.85	0.60	0.90	1.44	0.89
Actual number of CW staff required	1*	1	1	1	1	1	2*	2	1	1	2	1	1	2*	2	2*	1	2	3	2	1	4	4*	2	1	1	2	1

* Indicates that although the number rounded to the next integer is shown, the theater would likely temporarily use an assistant manager (up to .20) plus the lower integer number of Customer Service Employees.
CW = Concession Worker

Table 4 Continued

NUMBER OF PATRONS PURCHASING CONCESSIONS, SONCESSION SERVICE TIME REQUIRED AND NUMBER OF CONCESSION WORKERS REQUIRED IN THE BUSY SEASON

	Monday				Tuesday				Wednesday				Thursday				Friday				Saturday				Sunday			
	1:00 PM	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**	**1:00 PM**	**4:00 PM**	**7:00 PM**	**9:45 PM**
Number arriving 30 to 10 minutes prior to showtime	25.70	64.40	102.9	64.40	42.90	107.3	171.6	107.3	51.40	128.7	205.9	128.7	64.40	160.90	257.40	160.90	85.80	214.50	343.2	214.5	107.3	268.10	429.0	268.10	51.48	128.7	205.9	128.7
Number of concession purchases	3.85	9.65	15.45	9.65	6.45	16.09	25.75	16.09	7.70	19.30	30.90	19.30	9.65	24.20	38.60	24.20	12.85	32.18	51.45	32.18	16.09	40.20	64.35	40.20	7.72	19.31	30.89	19.31
Concession purchase time required (in minutes)	7.70	19.30	30.90	19.30	12.90	31.18	51.50	32.18	15.40	38.60	61.80	38.60	19.3	48.30	77.20	48.30	25.70	64.35	102.9	64.35	32.20	80.40	128.7	80.40	15.44	38.60	61.80	38.62
Theoretical # of CW staff needed	0.39	0.97	1.55	0.97	0.65	1.56	2.58	1.56	0.77	1.93	3.10	1.93	0.97	2.40	3.85	2.40	1.29	3.22	5.15	3.22	1.60	4.02	6.44	4.02	0.77	1.92	3.09	1.93
Actual number of CW staff needed	1	1	2	1	1	2	3	2	1	2	4	2	1	3	4	3	2	4	6	4	2	5	7	5	1	2	4	2
Number arriving 10 minutes prior to 5 minutes after show time	45.0	112.5	180.0	112.5	75.0	187.5	300.0	187.5	90.0	225.0	360.0	225.0	112.5	281.3	450.0	281.3	150.0	375.0	600.0	375.0	187.5	468.5	750.0	468.5	90.0	225.0	360.0	225.0
Number of concession purchases	6.75	16.88	27.00	16.88	11.25	28.13	45.0	28.13	13.50	33.75	54.00	33.75	16.88	42.20	67.50	42.20	22.50	56.25	90.0	56.25	28.13	70.30	112.5	70.30	13.50	33.75	54.00	33.75
Concession purchase time required (in minutes)	13.50	33.75	54.00	33.75	22.50	56.25	90.0	56.25	27.00	67.50	108.0	67.50	33.75	84.40	135.0	84.40	45.00	112.50	180.0	112.5	56.25	140.30	225.00	140.30	27.00	67.50	108.0 0	67.50
Theoretical # of CW staff needed	0.90	2.25	3.60	2.25	1.50	3.75	6.0	3.75	1.80	4.50	7.20	4.50	2.25	5.60	9.00	5.60	3.00	7.50	12.0	7.50	3.75	9.35	15.00	9.35	1.80	4.50	7.20	4.50
Actual number of CW staff required	1	3	4	3	2	4	6	4	2	5	8	5	3	6	9	6	3	8	12	8	4	10	15	10	2	5	8	5
Number arriving 5 to 20 minutes after show time	19.3	48.2	77.0	48.2	32.1	80.3	128.4	80.3	38.5	96.3	154.1	96.3	48.2	120.4	192.6	120.4	64.2	160.5	256.8	160.5	80.3	200.6	321.0	200.6	38.5	96.3	154.1	96.3
Number of concession purchases	2.90	7.25	11.55	7.25	4.80	12.05	19.25	12.05	5.78	14.45	23.10	14.45	7.23	18.05	28.90	18.05	9.63	24.08	38.52	24.08	12.05	30.09	48.15	30.10	5.78	14.50	23.12	14.50
Concession purchase time requires (in minutes)	5.80	15.0	23.10	15.00	9.60	24.10	38.50	24.10	11.55	28.90	46.20	28.90	14.46	36.10	57.78	36.10	19.26	48.15	77.0	48.15	24.10	60.18	96.30	60.20	11.55	28.90	46.23	28.90
Theoretical # of CW staff needed	0.39	1.0	1.54	1.00	0.64	1.60	2.56	1.60	0.77	1.93	3.10	1.93	0.96	2.40	3.85	2.40	1.28	3.21	5.14	3.21	1.60	4.01	6.42	4.01	0.77	1.93	3.10	1.93
Actual number of CW staff required	1	1	2	2	1	2	3	2	1	2	4	2	1	3	4	3	2	4	6	4	2	5*	7	5*	1	2	4	2

* Indicates that although the number rounded to the next integer is shown, the theater would likely temporarily use an assistant manager (up to .20) plus the lower integer number of Customer Service Employees.
CW = Concession Worker

Table 5
DAILY SCHEDULE FOR CUSTOMER SERVICE REPRESENTATIVES FOR THE SLOW SEASON*

CSR #	MON	TUES	WED	THURS	FRI	SAT	SUN
1	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM
2	3:30-7:30PM	3:30-7:30PM	3:30-7:30PM	3:30-7:30PM	12:00-3:30PM	12:00-3:30PM	3:30-10:30PM
3	3:30-7:30PM	3:30-7:30PM	3:30-7:30PM	3:30-7:30PM	3:30-10:30PM	3:30-10:30PM	3:30-10:30PM
4	7:30-10:30PM	6:30-10:30PM	3:30-7:30PM	3:30-7:30PM	3:30-10:30PM	3:30-10:30PM	3:30-10:30PM
5	7:30-10:30PM	7:30-10:30PM	7:30-10:30PM	6:30-10:30PM	3:30-10:30PM	3:30-10:30PM	6:30-9:30PM
6			7:30-10:30PM	6:30-10:30PM	3:30-10:30PM	3:30-10:30PM	
7			7:30-10:30PM	7:30-10:30PM	6:30-9:30PM	3:30-10:30PM	
8					7:30-10:30PM	6:30-9:30PM	
9						6:30-9:30PM	
DAILY SCHEDULE FOR CUSTOMER SERVICE REPRESENTATIVES FOR THE BUSY SEASON*							
CSR #	**MON**	**TUES**	**WED**	**THURS**	**FRI**	**SAT**	**SUN**
1	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM
2	3:30-7:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM
3	3:30-7:30PM	3:30-7:30PM	3:30-7:30PM	12:00-3:30PM	12:00-3:30PM	12:00-3:30PM	3:30-10:30PM
4	3:30-7:30PM	3:30-7:30PM	3:30-7:30PM	3:30-6:30PM	3:30-10:30PM	12:00-3:30PM	3:30-10:30PM
5	6:30-10:30PM	3:30-7:30PM	3:30-7:30PM	3:30-6:30PM	3:30-10:30PM	3:30-10:30PM	3:30-10:30PM
6	7:30-10:30PM	3:30-7:30PM	3:30-7:30PM	3:30-7:30PM	3:30-10:30PM	3:30-10:30PM	3:30-10:30PM
7	7:30-10:30PM	7:30-10:30PM	3:30-7:30PM	3:30-7:30PM	3:30-10:30PM	3:30-10:30PM	3:30-10:30PM
8		7:30-10:30PM	3:30-7:30PM	3:30-7:30PM	3:30-10:30PM	3:30-10:30PM	6:30-9:30PM
9		7:30-10:30PM	3:30-7:30PM	3:30-7:30PM	3:30-10:30PM	3:30-10:30PM	6:30-9:30PM
10		7:30-10:30PM	3:30-7:30PM	6:30-10:30PM	3:30-10:30PM	3:30-10:30PM	6:30-9:30PM
11			7:30-10:30PM	6:30-10:30PM	3:30-10:30PM	3:30-10:30PM	
12			7:30-10:30PM	6:30-10:30PM	6:30-9:30PM	3:30-10:30PM	
13			7:30-10:30PM	6:30-10:30PM	6:30-9:30PM	3:30-10:30PM	
14			7:30-10:30PM	6:30-10:30PM	6:30-9:30PM	3:30-10:30PM	
15			7:30-10:30PM	6:30-10:30PM	6:30-9:30PM	3:30-9:30PM	
16						3:30-9:30PM	
17						3:30-9:30PM	
18						3:30-9:30PM	
19						3:30-9:30PM	

CUSTOM CIRCUITRY INTERNATIONAL

Eric Kyper, Lynchburg College
Leon Schimmoeller, Lynchburg College

CASE DESCRIPTION

The primary subject matter of this case concerns an audit of manufacturing defects for a manufacturer of printed circuit boards. Secondary issues examined include process analysis and statistical quality control. The case has a difficulty level of six, appropriate for first year graduate students. The case is designed to be taught in two class hours and is expected to require six to eight hours of outside preparation by students.

CASE SYNOPSIS

This case presents evidence of manufacturing quality control problems for a maker of printed circuit boards. The objective is for students to identify the primary sources of variation in quality and recommend solutions. The observations provided below (including defect categories, defect costs, production flow charts, control chart data, and range/proportion data) are sufficient to critically analyze the current process and enable one to present a revised production process.

INSTRUCTORS' NOTES

The control chart for proportion defective does not provide any clear evidence (outliers, trends, cycles) of problems (NOTE: more rigorous tests for patterns could be conducted). Since other evidence (complaints, returns, rework, defect analysis) indicates severe quality problems, it is evident that a p-chart and/or its implementation (sampling, testing) is inadequate and insufficient. Consideration should be given to more comprehensive final-product testing (*e.g.*, implementing a C-chart database). In addition, data is needed for monitoring board and component placement inspections. The production flow chart indicates that these inspections take place; no data were provided.

Instructor: The main goal of this case is to have the student recognize the way to prioritize the defects is by the cost to the organization. Cost of defects and their repairs and other actions such as re-test of repaired units needs to be calculated and organized in the Pareto diagram to determine which problems are the most significant. These significant problems should be analyzed by fish bone analysis to determine root cause and appropriate solutions. In this case, some of the problems with "wrong parts" are caused by incorrect information coming from the various databases.

The remainder of this paragraph provides a possible assignment for your students. As Susan's team leader you are tasked with defining the current set of problems and proposing possible solutions. She expects a report back within one week and has said it must include at a minimum the following items: a summary of where the problems exist in the production cycle; a financial analysis of the cost of poor quality and product reworks (illustrated with a Pareto diagram); a cause and effect (fishbone) diagram to help elucidate root causes for the most expensive defect problem; analyses of causes and effects to determine possible corrective actions; and finally a redesign of the production control process to resolve issues related to part identification, part selection, and part revision.

CASE SOLUTION

1: Is the process out of control, and how much variation exists?

Figures 1 and 2 below show control and range charts respectively. These figures indicate that variation is increasing over time and the process is occasionally out of control. We know this because in the R chart values before 15 do not exceed 0.2, but steadily exceed 0.2 after 15, and the control chart has observations above the upper control limit (UCL). Now that a problem has been established we continue with a more detailed analysis into the root causes.

Figure 1: Control chart data

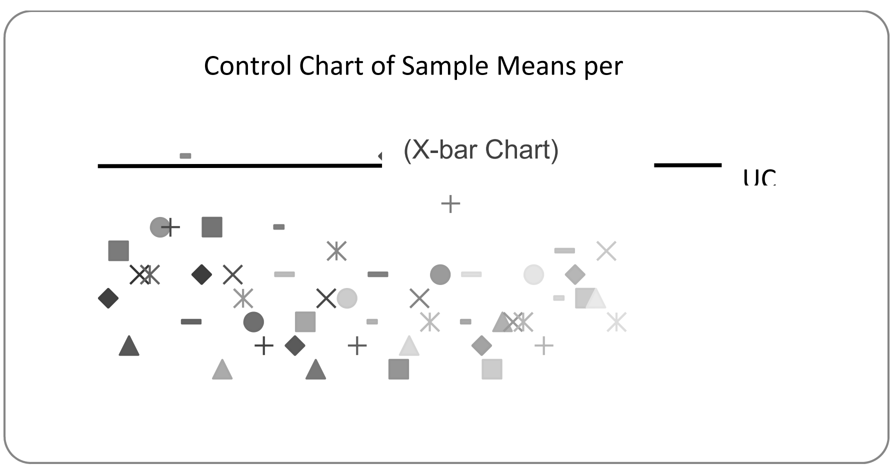
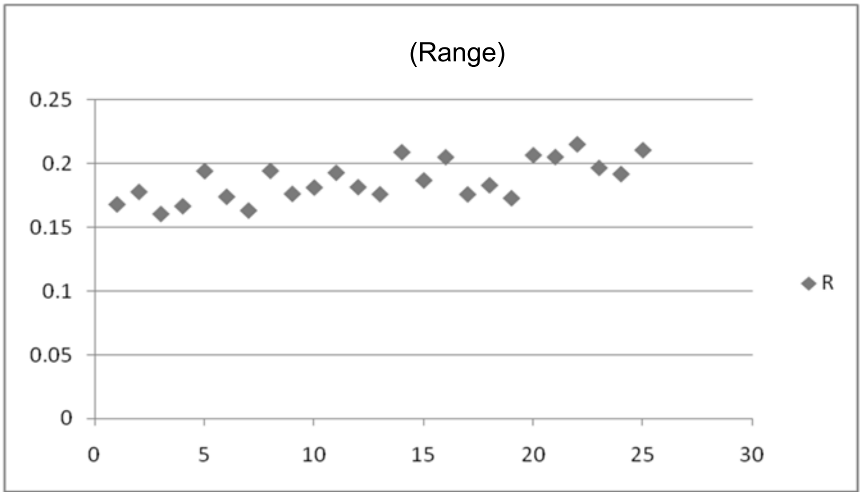


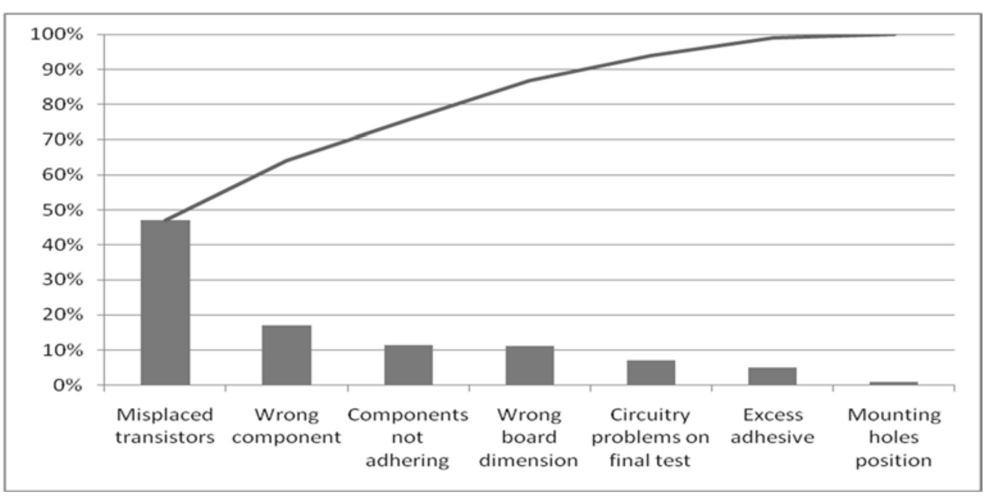
Figure 2: Range data



2: Chart frequency of defects by category.

The Pareto chart of defects (figure 3) suggests four general groupings of defects: *Component errors* (misplacement, wrong component), *Board errors* (dimension, misplaced holes), *Adhesive* (not adhering, excess adhesive), and *Circuitry errors*. Component errors are by far the most frequent (64%), followed by Adhesive (16%), Board (12%), and Circuitry (7%). Details are shown in the Pareto Chart below:

Figure 3: Pareto chart of defects

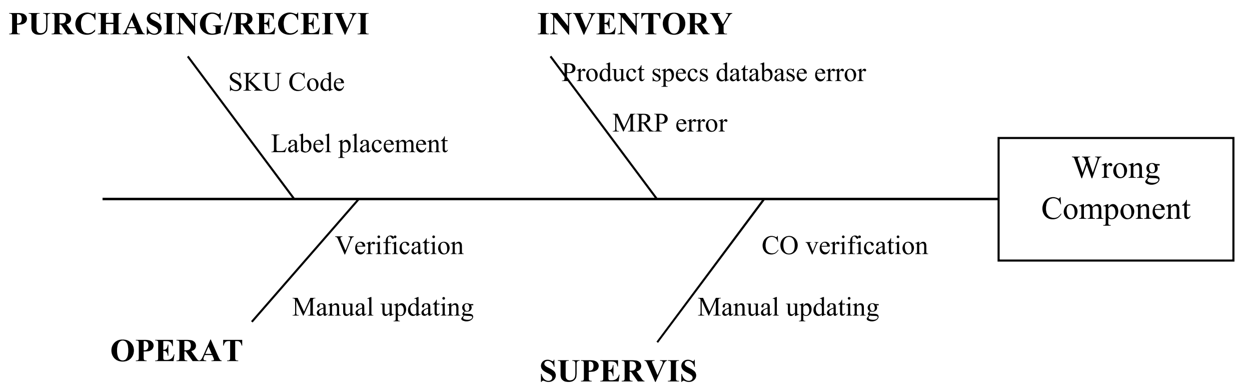


3. Create cause and effect model for "wrong component" defect category.

Based on the Pareto analysis and investigation of associated factors, the potential causes for the placing of wrong components are shown in the C&E diagram below:

As an example of the C&E analysis, the figure 4 below displays possible first- and second-level factors associated with the defect "Wrong Component." Similar charts could be constructed for each of the major defect categories (say those comprising 75-86%, the first four in the Pareto chart). The C&E diagram would of course be expanded to more levels. For example, the processes which lead to the recording of inventory labels at INVENTORY could be expanded one more level (*e.g.*, documentation, receipt, labeling), and beyond (specification, ordering, receiving).

Figure 4: Cause and effect (fishbone) diagram

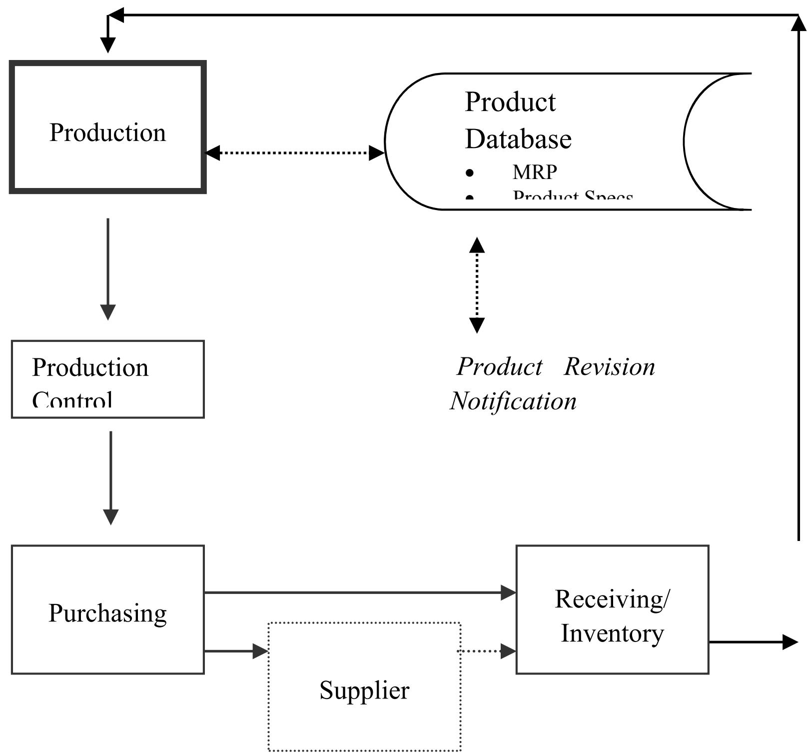


4: Construct revised control process review to reduce errors.

The processes of inventory and database maintenance are common factors in the potential causes shown above (look under Operator, Supervisor, and Inventory Control). Those discrepancies possibly arise from lack of coordination among the different databases. As shown in the original system diagram, different departments control related databases, and there is no indication that common data elements are simultaneously updated, or that there is a process whereby these elements are reconciled. The redesign shown in the system flowchart below is recommended. In this design, only one department (Production Control) would have responsibility for maintaining the Product Database, to include: The MRP (component specifications), Product Specifications, and the assignment of SKU/UPC (Stock Keeping Unit, Universal Product Code) codes. In addition, the database would to be keyed exclusively by SKU (*i.e.*, all of the sub-files would be organized by SKU, and the principal retrieval key would be the SKU). The file would also include a cross-referenced Product Name-SKU directory.

Figure 5: Revised control process

Legend: Database Process/activity



The above modification should eliminate a substantial proportion of the "Wrong Component" errors because the elimination of multiple databases resolves issues associated with product revisions and/or changes in part numbers. To ensure success of the new design the following steps should be taken:

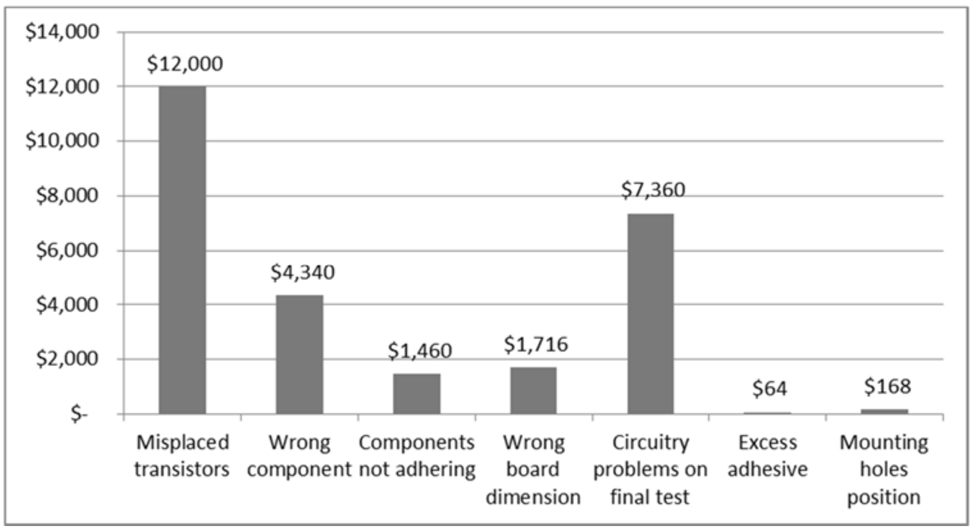
Training in the use of the new database, including mandatory daily notification of Change Orders for every duty shift.

5: Calculate costs of defects by category.

This proposed changes can potentially resolve 68% of defects (includes defect categories wrong component (17%), misplaces transistors (47%), and improperly positioned mounting holes (1%)).

As can be seen in figure 6 below this has initial cost savings of $17,800 (defect categories wrong component, misplaces transistors, and improperly positioned mounting holes). Additionally this also resolves 60% of the defects at final circuitry test (wrong components and misplaces transistors) saving another $4,416 (0.6 x $7,360). This is weekly data so the annual savings are over a million dollars. This is the figure used to justify the project costs to implement the proposed solution of database consolidation.

Figure 6: Costs by defect category



Potential solutions include:

1. Redesign of the database management system to improve inventory and database maintenance (defect savings should offset the redesign costs).

2. *Poka-Yoke* templates for each type of board indicating the proper components (reduces wrong components).

3. Evaluation and monitoring of:
   C-charts and p-charts compiled at each inspection point.
   Investigate out of control processes.

MANAGERIAL CARROTS AND STICKS: ENCOURAGING STRATEGY IMPLEMENTATION

John Leaptrott, Georgia Southern University
J. Michael McDonald, Georgia Southern University
Jerry W. Wilson, Georgia Southern University

CASE DESCRIPTION

This case addresses many strategic management issues. Selected issues related to the formulation and implementation of both low cost and differentiation strategies are illustrated. The importance of lower level managers embracing their company's strategy and showing initiative to implement that strategy is also highlighted. The case illustrates the importance of having these managers understand and recognize the need to use informational resources available within an organization to objectively assess their area of responsibility in the context of strategy implementation and gives examples of how they can act constructively based on that information. Other topics include a discussion of challenges in transitioning from the role of college student to employee and from employee to manager. The case also provides students with a perspective as to how they might be evaluated by their superiors once they are employed as managers. The case has a difficulty level appropriate for senior level and graduate level students in strategic management courses. The case is designed to be taught in 1-2 class hours and is expected to require 3 hours of outside preparation by students.

CASE SYNOPSIS

The case chronicles the strategic evolution of a fictitious privately held small local company that grew to become a midsize regional sporting goods retailer. The company was founded by three brothers who used their enthusiasm for sports and the knowledge gained from their participation in those sports to formulate and implement a successful differentiation strategy. This strategy resulted in steady growth of the company in multiple locations. A private equity firm bought the company and after a failed attempt at pursuing a strategy primarily designed to lower costs and increase profitability prior to an initial public offering, the firm replaced their CEO hired to pursue that strategy with a new CEO who is orchestrating a return to a differentiation strategy. The company has now regained profitability by returning to that strategy.

As part of the company's new evaluation and control procedures associated with the differentiation strategy, the CEO and the Vice President of Managerial Development *meet individually with each store manager each year to review the performance of their store for the prior year. The case describes two of those meetings. In one meeting, a store manager receives praise for achieving a high level of performance by successfully formulating and implementing a differentiation strategy tailored to the local market. In the other meeting, a different store manager receives criticism for the substandard store performance at his store due in large measure to his failure to embrace the company's return to a differentiation strategy. This manager continued to implement the unsuccessful companywide cost-based strategy instituted by the prior CEO. The new CEO must decide how to reward the personnel at the high performing store and what changes need to be made at the lower performing store.*

INSTRUCTOR'S NOTES

The case can be analyzed by either individual students or by student groups. Suggested discussion questions and answers:

1. Describe the different strategies implemented by the company under the three different eras: The Lee brothers, Greg Baker, and Jack Colwood. How did the company's operations change to reflect the strategies used during each era?

Initially, the company pursued a differentiation strategy. The active participation by the company founders and sales staff in activities associated with the products sold by the company resulted in a high level of product knowledge and word of mouth advertising. The Lee brothers used this product knowledge to carry products that were in demand in the local marketplace, but were not sold in enough volume to be carried by large national retailers. In anticipation of an initial public offering Greg Baker was hired to change the company strategy to one that was based on cost while increasing volume through a program of rapid expansion. He centralized the purchasing function and standardized the products carried by the stores to the point that many were the same or very similar to that sold by the national retailers. In addition, he reduced the number of employees and their compensation levels. While saving some costs, the company could not compete on price with the national retailers that possessed a higher level of purchasing power. Because of the disappointing results from implementing this cost strategy, the company hired Jack Colwood to return the company to a differentiation strategy. The company has now successfully re-implemented a differentiation strategy due in large part to emphasizing the elements of differentiation that had proven to be successful for the Lee Brothers. This strategy fostered a return to an entrepreneurial organizational culture that empowered store managers and their sales staff to select and promote products tailored to their markets and rewarded them for successfully doing so.

2. The case describes two role transitions. One is the transition from the role of college student to employee and the other is from the role of employee to manager. These transitions require a transition in both attitude and behavior. What is the nature of those transitions?

The role of employee and college student differ in several ways. The roles differ as to the degree each role is structured. For example, the college student receives frequent, rapid and specific feedback. The employee may receive very infrequent and ambiguous feedback. The schedule for a college student is fairly rigid. Semester start and end dates, class meeting times and requirements for progression are known well in advance. Employee schedules may change drastically with little or no notice. Requirements for employee progression may involve factors beyond the employee's control such as overall organizational performance and the criteria for progression may never be fully disclosed to the employee. The college student enjoys a large measure of control over activities and how time is spent. An employee may be very limited as to control over his or her schedule. The college student also may enjoy a high degree of freedom with respect to personal appearance and behavior. Employees are often expected to conform to dress codes and behavior that conforms to organizational norms.

The transition from employee to new manager also requires a change in attitude and behavior. The new manager's future success is no longer primarily dependent on his or her individual efforts as an employee, but rather depends upon the collective efforts of all employees in their area of responsibility. A new manager that uses a too authoritarian management style often suppresses employee creativity and cooperation. The new manager should strive to create an organizational culture that fosters entrepreneurial activity by encouraging and rewarding innovative thinking by the employees that identifies new opportunities and successfully acts upon them. The new manager should attempt to foster a cooperative team attitude that works to readily adapt to changes in company operations. Such an organizational culture also seeks to help each employee develop competencies to better realize his or her full potential and to achieve the organizational goal of developing and maintaining a competitive advantage.

Experience also plays a significant role in developing managerial skills. To accelerate the process of experiential learning managers need to understand the value of peers and superiors as a source of guidance in gaining the necessary experience. Gaining experience lends insight into the realities of the manager's role, improves manager ability to accurately assess employee strengths and weaknesses and teaches managers how to successfully deal with them. Experience also improves a new manager's ability to manage stress, and to establish and maintain a beneficial organizational culture.

3. What assumptions were made in the due diligence process prior to the purchase by AAP and to what extent were those assumptions inaccurate?

The acquiring company assumed that profitability would not be affected by a change from a differentiation strategy to a low cost strategy. Granted, the rate of expansion for the company would have been much slower for the company if it had continued the differentiation strategy. However, the profitability of the company before acquisition was due in large measure to the competencies stemming from the differentiation strategy that was abandoned in favor of a cost based strategy.

4. How does the detailed information available through the IT system function as part of the control system potentially assist store managers in improving store performance and making the assessment of managerial performance at each store more objective?

Both the store manager and top company management have the ability to receive extremely detailed reports related to virtually all aspects of company operations. For example, sales and gross profit by product or product category is available for each store, each region or the company as a whole. Therefore, store performance details are easily visible. Using this information, top company management can easily identify the leaders and the laggards among the ranks of their store managers. Store managers can also use the system to easily determine what areas of their store are doing well and which are underperforming and adjust store operations accordingly.

5. Two store managers were highlighted in the case. One was successful the other failed. How did the behavior of these two managers differ?

The primary difference between the two managers was the degree each understood and embraced the differentiation strategy the company had implemented. The successful manager translated the company strategy into concrete actions at her particular store. She understood the value of establishing constructive relationships with superiors and peers to help guide her in configuring her store operations. In addition, she leveraged her abilities to entrepreneurially identify and exploit marketplace opportunities by empowering her employees to do the same. She utilized the managerial tools the company provided, such as the ability to receive custom IT reports, and to tailor her stores operations to the local market. She also conveyed and received information at the managerial retreats that not only lead to improvement of the performance of her store, but other stores as well. The unsuccessful manager failed to embrace the company's return to a differentiation strategy and to find ways to implement it at his store level despite being given several opportunities to do so. This manager also failed to take advantage of the managerial and developmental resources provided by top management. Because he did not conform to the strategic direction of the company and refused to utilize the guidance and tools provided by top management that would have facilitated a positive change of strategy and culture for his store, management is considering whether to terminate his employment or to make an additional attempt to change his managerial approach.

6. Company management must decide how to reward the performance of the Tacoma store. What process would you use to determine that reward, how large should the reward be and how would you recommend the reward be distributed among the employees at the store?

Management needs to foster behavior that is consistent with the strategic goals of the company. Providing financial rewards for that behavior should encourage more of it. Certainly the Tacoma store is deserving of a financial reward. Management must determine the size of the reward and how it is distributed among the store employees. Obviously, there is no single answer to how large the reward should be. Some factors management should consider include the level of performance in excess of that achieved by similar stores and the differences in each store's competitive environment. Similarly, the distribution of the reward can be done in many ways. Company leadership can specify the reward for each employee and the store manager. Alternatively, company management can decide the overall reward for the store and leave the allocation of the reward solely to the discretion of the store manager.

7. Company management must also decide what change, if any, to make at the Eugene store. What changes would you recommend that management make?

The store has not embraced the differentiation strategy and the organizational culture associated with it. The store manager has been made aware of the problem and has chosen not to make changes in his store to align it with the strategic direction of the company. Management will very likely have to terminate his employment and replace him with a person that has been successful in implementing a differentiation strategy in their area of responsibility at another store. Management does have the option of giving him further guidance and an additional opportunity to conform. Unfortunately, most current employees at the store do not fit the current strategic direction either, and, as a result, many of them will need to be eventually replaced as well. However, it is possible that the elements of differentiation strategy and the reasoning behind its implementation can be successfully communicated to them and many, if not all, would be then able to meet the expectations of the company once this is done.

INSTRUCTORS' NOTE
PARK STERLING BANK: THE BEGINNING

Michael D. Evans, Winthrop University

CASE DESCRIPTION

The purpose of this case is to highlight the risks and potential rewards of starting and/or investing in a community bank. This case, based on the formation of Park Meridian and Park Sterling Banks in Charlotte, NC, is intended for junior level courses in corporate finance, management, money and banking, or investments. The case can be discussed in 1 - 2 class periods and will require 2 – 3 hours of outside preparation by students. Specifically, students will assess the unique challenges faced by community banks and evaluate the attractiveness of investing in a de novo bank. Secondary issues include the importance of qualified management and the role of bank directors.

CASE SYNOPSIS

Larry Carroll, a prominent financial planner practicing in Charlotte, North Carolina, read with interest an article in the Charlotte Observer announcing the formation of a new community bank. Larry contacted the President of the proposed bank to express his interest in joining the organizing group. Through their efforts, Park Meridian Bank commenced operations. After ten years of steady growth, Park Meridian Bank was sold to Regions Bank. Larry experienced an attractive return on his investment. Now, Larry desires to "do it again!" He is now leading an effort to start another community bank and has recruited his friend and business colleague, Mike Evans, to join him in this business endeavor. Mike is extremely excited and flattered that he has been invited to join the organizing group. However, Mike faces some challenges. The reader will be introduced to the issues Mike faces in making the decision whether to participate or not.

LEARNING OBJECTIVES

Students will gain knowledge regarding the:

1. Distinction among national, regional and community banks
2. Opportunities and unique challenges faced by community banks

3. Risks inherent in starting a community bank and the risks assumed by officers and directors

Students will also assess the risks and potential rewards of investing in a community bank. They will analyze the attractiveness of starting a de novo bank. Students will also evaluate the merits of joining the organizing group of Park Sterling Bank.

PREPARATION

While helpful, prior knowledge of bank management is not required. Accordingly, this case can be used in junior level finance, economics and business management classes. The case can be used in the Principles of Finance class to highlight the process and challenges of raising capital. It clearly can be used in the Investments class to assess the attractiveness of investing in community banks and to discuss the decision faced by Mike Evans regarding joining the organizing group which will require a significant investment. The most natural fit for the case might be a class such as Bank Management or Money and Banking.

The case works best if students have completed the business "tools courses" such as accounting, economics and an Intro to Business course.

DISCUSSION

The discussion can begin with a distinction among national, regional and community banks. It should be noted that such classification is typically made based on size and scope of geographic operations. As one would expect, national banks are the largest in size and operate in markets across the country. Regional banks tend to operate in a specific section(s) of the country (e.g. the Midwest, the Southeast, etc.). Community banks typically operate in a much smaller geographic footprint (most operate within a single county or state). Banks are grouped by asset size. There are no firm cut-offs for classifying banks. However, community banks typically have less than $1 billion in total assets. Community banks tend to be locally owned and operated. The initial shareholders typically live in the community in which the bank operates.

Larry Carroll's experience in organizing and investing in Park Meridian Bank can then be discussed. Students could be asked to assess his return on investment. If they were in Larry's shoes, would they be interested and willing to start another community bank?

QUESTIONS

1. **As implied in the case, capital has been readily available for start-up community banks such as Park Meridian. Why?**

Investors have been attracted to the fact that there have been a number of qualified, experienced managers ready to "run their own ship". Typically, such bankers have received training and gained years of experience working for a regional and/or national bank. It is often believed that such bankers will be successful in starting and managing their own banking franchise.

Further, investors have received handsome returns from investing in community banks. Well-run community banks often become takeover targets for larger banks seeking to gain a toehold in a new market. Typically, the goal is to start a bank, operate the bank profitably and sell the community bank within a ten year timeframe.

Local investors also gain "pride of ownership." There is "psychic income" associated with owning a local entity, particularly a bank.

2. **What advantages do community banks, like Park Meridian and Park Sterling, have over larger financial institutions?**

Perhaps, the major advantage is customers have direct access to decision makers. Decisions regarding loans and/or interest rates for deposits are typically made locally and can be communicated to the prospective borrower/depositor quickly. Customers get to know their banker and have the ability to forge more personal relationships and receive a higher level of personal service because community banks do not experience the turnover in personnel that the larger banks do.

Community banks have the ability to tailor loan and deposit products to the needs of their customers. Changes in either can be made very quickly because there are fewer layers of management and it is easier for senior management to keep abreast of what is going on in the local market(s). Customers have the ability to contact the senior management of a community bank directly and receive a prompt response. This ability is not as readily available for customers of regional and national banks.

3. **What disadvantages do community banks, like Park Meridian and Park Sterling face?**

Community banks have fewer revenue streams. While some of the more established community banks provide investment, mortgage and insurance services, most rely on the traditional banking function (attract deposits at low cost and lend those monies at a higher rate to earn a spread) as their sole or major source of income. The regional and national banks have much greater opportunities to attract fee income from mortgage generation/brokerage, investment management, insurance services and investment banking activities. The generation of fee income is extremely important in a period of declining interest rates because the generation of such revenues may mitigate declines in a bank's net interest margin.

Community banks have limited access to capital. Typically, the organizers of a community bank are limited to raising start-up capital from local investors. Accordingly, the pool is much smaller. Similarly, it is typically harder for a community bank to raise secondary capital to support growth. Institutional investors often are not interested in investing in small community banks. They are perceived to be a risky asset class. If there is interest, it often comes at a steep price (i.e. higher interest rate for a bond issue, lower stock price for an issuance of new shares of stock) to compensate the investor for the risk assumed. The goal of raising additional capital is especially felt when the economy is performing poorly and declines in the stock market are experienced. During such times, community banks that are in dire need of additional capital may be unable to raise any. This often leads the bank to seek an acquirer or merger partner.

Operating in a limited geographic footprint is another risk faced by a community bank. The bank can find itself on the brink of failure if the economy in the community in which it operates undergoes a period of protracted decline. Bank of Granite is a case in point. For years, Bank of Granite was touted as one of the best run community banks in the country. Its CEO was widely respected within the financial services community. However, when the textile industry in North Carolina virtually ceased to exist, Bank of Granite fell on hard times. The bank ended up on "life-support" and ultimately was sold in a to a new investor group. Bank of Granite shareholders lost most of their investment.

4. What are the keys to successfully starting and operating a new community bank?

First and foremost, there needs to be a well-qualified CEO to lead the proposed venture. He/she should assemble a group of strong senior managers, particularly a Chief Financial Officer and Chief Credit Officer. The resume of the proposed CEO is critical for the capital raise. Potential investors are interested in a CEO with substantial banking experience (i.e., one who can demonstrate that he/she has the ability to run a bank) who also possesses strong ties to the local community.

The bank should pursue a specific niche. It cannot be all things to all customers. Park Sterling's initial plan was to be a business bank (as opposed to a retail bank) and market its services heavily to real estate developers and small business owners.

The CEO should recruit a strong Board of Directors. The proposed board members should have the ability to invest their own monies in the start-up bank as well as attract additional capital from friends, relatives and business associates. Note that board members should not be selected based solely on their ability to attract capital. They should be persons of integrity and held in high regard in the local community. Board members should also be knowledgeable business persons with the ability to work well with others. The ability to refer business (i.e., deposits and/or loans) to the bank is a plus. Prior bank board experience, while helpful, should not be a requirement. Park Sterling's initial board included three individuals with prior bank board experience. Larry Carroll was one of the three. He also was the largest initial investor and assumed the position of Chairman of the Board. Averill Harkey and Steve Luquire had also previously served on the board of Park Meridian Bank. Averill chaired the Loan Committee and Steve served on the Executive Committee. Experience and insight gained during the Park Meridian days was helpful in planning the start-up of Park Sterling Bank.

The CEO should have the ability to attract experienced bankers to the de novo bank. These bankers should have the ability to bring customers (loans and deposits) with them to the new bank. Bryan Kennedy was able to attract a number of bankers that he previously worked with at either Park Meridian or Regions Bank. These bankers were successful in bringing a substantial amount of business to the new bank.

5. What should potential Directors, like Mike, consider before committing to serve?

First, a potential board member should determine if there is room for another community bank in the proposed area of operation. Who is the competition and how stiff is it? What is the proposed operating plan and does it make sense? How will the bank attract deposits? What types of loans will it make? In essence, does the proposed bank's "story" make sense? How likely is it that the bank will be successful?

Each proposed director should determine if he/she can provide sufficient time to carry out the obligations of a board member including preparing for and attending scheduled board meetings and serving on a board committee(s).

Each board member is typically expected to invest during the initial capital raise. A prospective board member should ensure that he/she is comfortable investing the required sum and understands where the funds will come from. It must be recognized that this may be a relatively illiquid investment and there is no guarantee of success. Further, "political pressures" may prevent a board member from selling shares of the bank's stock if performance is less than anticipated. In fact, there may be pressure to make additional investments in subsequent periods if the bank needs to raise additional capital. Note: the shares of a number of community banks do not trade on one of the exchanges or over the counter. Instead, some bank CEOs maintain lists and attempt to match buyers and sellers.

One should review the background of the other proposed board members. Are you familiar with any of them? Are they individuals you would be comfortable working with? Do the proposed board members appear to possess complimentary skills and access to a wide-ranging group of potential customers?

There is also a question of liability. Board members should determine whether an Errors and Omissions policy will be obtained to provide protection for officers and board members. If so, one should determine the coverage provided and the amount of any deductible.

6. **Larry Carroll and Bryan Kennedy were interested in ensuring that there was diversity among the initial Board of Directors. Do you feel it is important to have a diverse board? Why or why not?**

It is important to have diversity on the board. First, having diversity broadens the pool of prospective investors. The board consisted of attorneys, small business owners, real estate developers, a medical doctor and financial planners. One member was African-American and one member was a woman. Each board member was able to bring a substantial list of potential investors to the table. As a result, Park Sterling Bank completed the largest capital raise for a North Carolina community bank. Further, this was accomplished without the utilization of fundraising consultants or any other outside assistance.

Diversity among the board is also helpful in attracting a broad group of customers to the bank and in keeping abreast of trends/opportunities in the community.

7. **What challenges would you expect Park Sterling Bank to face in its initial years?**

Park Sterling raised $45 million during its initial capital raise. The first challenge is to put this capital to work (i.e., make sound loans) in order to generate revenue. Credit quality is a key concern. While banks want to generate loans, they want to minimize the possibility that a borrower will not be able to meet his/her obligations as they become due. A major challenge is to screen prospective borrowers and proposed deal terms to avoid loans that may become past due, non-performing or in default (i.e., manage credit risk).

When Park Sterling began operations, Charlotte, NC was the home of two national banks, Bank of America and Wachovia. A number of regional and community banks also maintained operations in the Charlotte region. Competition for deposits was fierce. Banks compete for deposits by offering an attractive rate of interest on its deposit products. It was the norm to see banks operating in the Charlotte region offer an above average rate of interest on certificates of deposit. These rates were advertised aggressively in the Charlotte Observer. The result of offering a higher rate on deposits is a lower net interest margin which results in lower profits.

Park Sterling also had the challenge of funding its rapid growth. It could leverage its initial capital to grow the bank to about $450 million in assets. Additional capital would be needed to grow the bank further.

8. Assess each of Mike's options to make the required $100,000 minimum investment.

First, Mike could borrow some or all of the required investment. Terms had been negotiated with another financial institution to loan monies to any Organizer who wished to borrow monies for the initial investment. This represented an opportunity for an Organizer to make the investment with no out-of-pocket money. In Mike's case, he would not have to liquidate any personal investments which would constitute a taxable event. Nor would he be required to invest assets inside one of his retirement plans in the shares of Park Sterling. He would realize capital gain treatment on the sale of shares that had appreciated in value. Mike would be able to write off losses incurred in his personal tax return. He could also choose to gift shares to family members or to charity. It should be noted, however, that the use of leverage (i.e., borrowing money to make the investment) would further increase the riskiness of the deal. Mike would be obligated to pay back the bank loan even if the bank was not successful. Mike would also incur interest costs until the loan was repaid. Since Mike would not receive a Director's fee and the bank would not pay dividends during its early years, he would have to service the debt from his personal cash flow.

Second, Mike could make the investment inside one of his retirement accounts. If he did so, he would not incur any interest costs or the risk of using leverage because there would not be a loan. It would be easy to facilitate the investment. His cash flow would not be affected. Mike could simply sign the required documents and the investment would be made. However, making the investment in this manner would tie up $100,000 of retirement assets in a relatively illiquid investment that would not generate any current income. Mike would not receive capital gain treatment on the sale of appreciated shares nor have the ability to deduct losses incurred.

Third, Mike could utilize his liquid assets (i.e., cash on hand and investments outside of retirement accounts) to make the investment. Here, he would realize the same pros as those enumerated in the first alternative. Additionally, he would not incur interest costs or have a loan to repay. Mike would, however, significantly reduce the amount of monies available to meet any family emergency that might arise and impair his ability to pay the costs of having three children in college.

9. **Compare and contrast the attractiveness of receiving stock options as opposed to cash compensation.**

Clearly, cash compensation is a certainty. Each board member knows up front exactly how much he/she would receive on an annual basis. Note though that cash compensation is finite. Each board member would receive the stated amount irrespective of the bank's performance – good or bad. Each board member assumes more risk with the potential for greater reward when options are granted in lieu of cash compensation. The options can end up with no value. Alternatively, if the bank's stock price takes off, each board member is able to sell his/hers shares at a substantial gain.

10. **If you were Mike, would you choose to make the investment and join the Board? Why or why not?**

Students' response to this question will likely depend on how risk averse they are. Some would not want to make this investment due to the fact that it is a relatively illiquid investment. There was significant competition in the Charlotte region among national, regional and community banks so success was by no means guaranteed. A substantial investment is required. Some or all of the required investment could be lost. Some students may also be concerned about the liability incurred as a result of serving on a bank board.

First and foremost, it should be noted that Mike always wanted to serve on a bank board. There was an element of personal accomplishment in serving on a bank board with highly regarded business leaders and professionals in the Charlotte community. The stock options presented the opportunity to make a significant amount of money over time if the bank was successful. There was every indication of success given the caliber of management, strength of the proposed board and roster of bankers with an existing book of business who were waiting to come on board once the bank was up and running. Remember that the two senior executives and three of the proposed board members had previously been involved in the start, growth and sale of a community bank. There was no reason to think that they wouldn't be successful again. Community banks in the Charlotte region had proven to be a good investment in prior years.

EPILOGUE

Mike decided to join the Board of Directors of Park Sterling Bank. He chose to utilize $100,000 of his retirement monies to make the investment. This was the easiest way to facilitate the investment. Also, it did not require Mike to either borrow monies or reduce the level of his liquid assets.

Park Sterling Bank commenced operations in October 2006. It experienced unprecedented growth. The growth of the bank and the challenges incurred are examined in a follow-up case, "Park Sterling Bank – The Journey Begins."

ECAMPUS.COM: SITTING IN THE CATBIRD SEAT

Stephen L. Loy, Eastern Kentucky University
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CASE DESCRIPTION

The primary subject matter of this case concerns the current trends in the college rental textbook market. After studying this case, students should be able to (1) understand the competitive dynamics and emerging trends of the college textbook rental market, evaluate the competitive position of Ecampus and (3) assess the options facing Ecampus and recommend a course of action.

This case is suitable for graduate and undergraduate strategy classes and has a difficulty level of four. It is suitable for classes in management information systems and management strategy. Students should spend from six to twelve hours outside of class analyzing the case, depending on the breadth and depth of the analysis the instructor desires.

CASE SYNOPSIS

This case presents an overview of the college textbook rental market in which Ecampus competes. It presents a brief history of Ecampus and descriptions of its competitors. The case portrays the company as being in an enviable position in its industry and the company president thinking about the future of the company.

Ecampus.com was created during the "dot com bubble" by investors who hoped to grow it into an IPO. The plan was to "get big, fast" strategy and measure success by brand strength instead of earnings. In its first six months, Ecampus spent \$40M for commercials on three cable television networks. These ads created 87% brand name awareness, but only \$2M in sales.

Two events forced Ecampus into bankruptcy in 2000. First, the "dot com" bubble burst in March 2000 and venture capital and IPO markets dried up. Second, suppliers and potential investors were scared off by the personal bankruptcy of the CEO.

A Book Company, LLC purchased Ecampus for \$2.5M at a federal district court auction in 2001. The new owners employed a traditional business-driven strategy focused on internal efficiency, strict cost controls, highly targeted marketing, and internal financing for expansion. By 2007, Ecampus broke even and profits have steadily increased since.

Ecampus began renting textbooks in 2007. Since then, several new companies, financed by Silicon Valley venture capital companies and employing aggressive business models, have entered the rental market and grown rapidly. These rental companies are dependent on Ecampus' large supply of used books for their rental business. The president is now thinking about the future. How should Ecampus prepare itself for expansion into the e-textbook market? Could it use acquisitions and alliances? Should Ecampus continue using only internal financing for expansion?

INTRUCTOR'S NOTES

1. Develop a simple industry analysis for Ecampus using Porter's Five Forces model (Porter, 1980 and 1998).

The economy has changed significantly since Ecampus was launched. The readily available capital for e-commerce ventures virtually dried up as the "dot com" bubble burst and venture capital firms lost fortunes. Beginning in 2010, there has been resurgence in venture capital funding. The downward trend in the economy after 2000 resulted in increasing college enrolments, but a decline in the purchasing of new textbooks. The rapid increases in textbook prices due to the addition of associated CDs and ancillary websites to textbooks increased textbook prices substantially and created stiff resistance by both students and professors. The price increases have been so sharp that state legislators are started looking into this issue.

At first, textbook e-tailing did not take off as fast as predicted. However, many college students are very price sensitive conscious and use web-based searches for lowest prices. Still, the new prices for new textbooks are quite high. Used books cost less, but renting textbooks is the lowest cost option. Thus, the rental market has grown rapidly since 2007.

So far, e-textbooks are not yet as popular as hardcopy textbooks, but when they do become popular, as predicted, e-textbooks will change the entire textbook distribution chain dramatically.

***2.* Have the students discuss the SWOT analysis for Ecampus.**

Strengths
Ecampus is making a profit while other book renters are not
Well known
Relatively low cost and effective promotion
Modern facility and equipment
Excess capacity
Lean and efficient

Relationship with Amazon
Sheds books well
Markets to primary and secondary schools
Most efficient fulfillment center in the industry
Excellent relationships with publishing companies
Management and staff experienced in publishing industry and warehouse operations
Highly efficient target marketing strategy
Industries second biggest supply of used textbooks due a strong buy back program
History of competent management and stable growth
Best customer service reputation in the industry.
Wide selection of textbooks allows students to buy all or most of their books at the same time, which enables bundling the shipment to save shipping costs.
Strong sales in K-12 textbooks market. Provides textbooks to many public school districts and statewide systems.

Weakness

- Internal financing only
- Low level of capital for expansion
- Finding ways to finance faster growth
- Lacks product diversity
- Low level of social networking
- Lack above average rate of return
- Not unique and fairly easy to imitate
- Lack of a physical footprint on campus
- Not fully utilizing operational capacity due to seasonality of sales

Threats

- Publishers entering fulfillment function
- Publishers renting texts
- Amazon entering publishing
- Protecting its market share against the new, aggressive, deep-pocketed competitors, such as Chegg, CampusBookRentals and BookRen***ter***
- Impending threat of e-textbooks replacing physical textbooks

Opportunities

- Mergers
- Acquisitions
- New alliances
- Increases in bookstore presences/joint ventures
- Other fulfillment products
- Increased contract with state governments
- Increased primary and secondary market share
- New influx of capital
- E-textbooks

Ecampus competes with thousands of online retail booksellers and several large retail chains like Amazon, BarnesandNoble, and Follett. BarnesandNoble.com and efollett.com use their parental company's distribution systems and brand name to strengthen their online presence. Chegg, CampusBookRentals, and BookRenter have a very large presence in the textbook rental market in the last four years.

Although there is no substitute for a required textbook, there are many alternatives for buying textbooks. Brick-and-mortar companies do not offer the convenience of being open 24/7. However, they are likely to have a physical inventory on hand so students do not have to wait for their texts, and they can inspect the book before buying it.

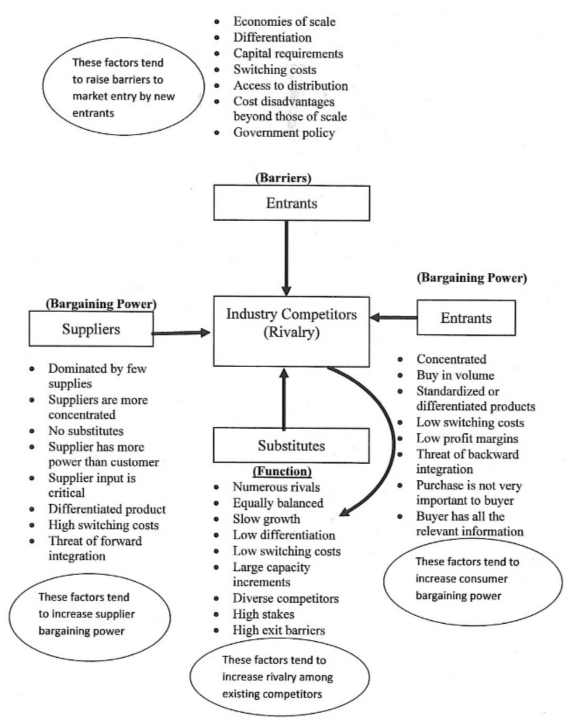
Entry barriers are contingent on the scope of operations. It is relatively easy to start an independent bookstore or establish an on-line company. However, becoming a major competitor requires large amounts of start-up capital to create a strong brand. Ecampus was able to attract this type initial funding and succeeded in creating a strong brand despite before going into bankruptcy.

Suppliers (i.e., publishing companies) have strong bargaining power in the industry. The overall wellbeing of the textbook resellers is dependent on their relationship with the publishers. Publishers are able to squeeze a large share of profitability out of the marketing channel than their value added might warrant. Large resellers might be able to negotiate volume discounts, but publishers pretty much set the market price.

The only way resellers can offer discounted textbooks to students is by reducing operational costs or by cutting their profit margins.

Before the introduction of Internet, students had little opportunity to do comparison-shopping. They were practically a captive market to the local bookstores. As more textbook outlets appeared on the Web, the buyers' bargaining power increased.

Figure 1: T***he Five Factors or Forces Affecting Competition in an Industry.*** Based on a diagram appearing on page 4 of *Competitive Strategy* by Michael Porter. Free Press (1980).



3. **Discuss the resources, capabilities, and core competencies of Ecampus before and after the bankruptcy.**

Firms have both tangible and intangible resources. Tangible resources include financial, physical, technological (hardware, software, networks) and organizational resources. Intangible resources include human knowledge and skills, creativity and brand. Ecampus created a strong brand name through its advertising, evidenced by the number of different individuals that visit its Web site and its Internet marketing effectiveness. Ecampus' fulfillment center system is highly efficient which contributes to low operating costs.

A firm's capabilities are determined by the ability to combine and employ both its tangible and intangible resources into outputs. The interactions among resources can be complex, but are critical for giving an organization a competitive edge. Capabilities extend across all functional areas. For Ecampus, its management team has extensive knowledge of the publishing industry and textbook market. Their long-standing working relationships with publishing companies and a strong used textbook supply chain are its most valuable resources.

Ecampus' fulfillment system produces is almost error free shipping system, which combined with in-house customer service, creates a high-level of customer satisfaction. The WooRank.com rating of 75.1 (see Table 2 in case narrative) indicates Ecampus is quite effective in reaching prospective customers, while spending far less on marketing than its competitors. The ability to achieve extensive exposure at extremely low cost is a core competency of Ecampus.

Businesses develop core competencies by combining resources and capabilities that business a competitive advantage over its competitors. Core competencies emerge over time to create unique value for a firm's products and services. However, the combination of a firm's resources and its capabilities do not always translate into a core competency. In order to create a sustainable advantage, capabilities must be either valuable (enable it exploit opportunities and neutralize weaknesses), rare (possessed by few competitors), costly to imitate (capabilities cannot be developed easily) or non-substitutable (do not have equivalents).

At this point, the instructor might want to discuss Ecampus' current resources, capabilities, and core competencies spelled out in the case.

***4.* What generic corporate strategies has Ecampus pursued?**

Ecampus employs a strategy of cost leadership across several market segments. The low cost leader in any market gains competitive advantage from being able to many to produce at the lowest cost.

A strategy is a pattern identified in a series of decisions or actions. Decision makers plan an intended strategy while an emergent strategy is a product of any planned and unplanned actions. A Book Company intended to grow Ecampus slowly while expanding into additional market segments. It expanded as a wholesale distributor to K-12 public and private schools, public school districts and statewide systems, sole contract supplier to community colleges and universities, wholesale and retail supplier of used textbooks, and, most recently, a renter of textbooks. Company expansion was completely internally financed. As Matt Montgomery said, "We grow internally by fulfillment center expansion and externally by reaching new markets."

5. **What is cooptation strategy? What other strategies does Ecampus use?**

Co-opetition is a method that goes beyond the old rules of competition and cooperation to combine the advantages of both. Co-opetition means cooperating to create a bigger business "pie," while competing to divide it up.

The main players in business are customers, suppliers, and complementors. Ecampus plays the role of both supplier and complementor. A complement to one product or service is any other product or service that makes the first one more attractive. Ecampus' large supply of used textbooks makes the low cost rentals of the competitors more attractive to students.

Complements are always reciprocal. For example, auto insurance complements new cars, new cars complement auto insurance. The more new cars people buy, the more insurance they buy, especially collision and theft insurance. Thus, auto insurance companies might want to use their expertise and influence to help their customers get a better price on new cars (Brandenburger and Nalebuff, 1996).

Complementors are Porter's sixth force. They are companies that sell goods or services that are compatible with, or complementary to, the goods or services of other firms within a given industry. Complements create a form a commercial symbiosis.

The presence of complementors can influence the competitive structure of an industry, which can benefit or hurt the firms competing in an industry, depending on the circumstances. If business is booming for the complementors, this could positively affect the business of the firms in the given industry. On the other hand, if business is slow for the complementors, this could adversely affect the business of the firms in the given industry. Therefore, complementors add another layer to the structural complexity of the competitive environment.

Ecampus employs several strategies involving cost leadership, differentiation and focused (niche) strategies. To move toward a category killer model, they could offer a large array of education-related products and services. Currently, Ecampus offers a wider variety of products and services than its direct rivals, excluding Amazon and BarnesandNoble.

Their cost leadership strategy focuses on delivering goods and services to customers at the lowest cost, relative to competitors. A differentiation strategy provides value to its customers by being different, such as higher quality product, more convenience, bigger product selection or options, free shipping and better customer service. The focused strategy creates value by serving a specific type of customer, such as college students or public school districts.

The answer to this question depends on how the scope of the market is viewed. If the industry is viewed as the entire textbook market or the textbook rental market, Ecampus' strategy can be viewed as a focused/differentiated strategy. If the industry is defined as the textbook rental market, it would be a focused strategy. The one thing Ecampus does differently than its competitors is that it owns and controls its inventory from which it fills orders, while the competitors use on third parties to ship textbooks to customers. Additionally, Ecampus does own or manage a chain of brick-and-mortar bookstores.

Ecampus could be considered differentiated because they have a different strategic model to create value for their customers. It has developed an excellent reputation and brand recognition among college students by promoting itself as a trustworthy company where students can buy new and used textbooks, rent textbooks, and sell their books with minimal hassle.

The company pursues the same value propositions for its textbook rental business. They do not employ a pure low-cost strategy, however. Among the book rental companies, they have lower costs due to their efficient system of acquiring a large volume of used books and an efficient fulfillment operation. Their buyback programs are the best and largest in the industry. The wide selection of new, used, and rental textbooks allows students to bundle a variety of books in a single order and shipment, which reduces shipping costs for Ecampus.

While Ecampus has process advantages, those processes could be imitated, although not quickly or easily. If someone did, however, Ecampus' advantages vanish. Amazon.com and Barnesandnoble have the advantages of scale and can spread costs over a much higher sales volume. They also have the resources to make huge capital investments in supply chain technology to reduce their costs further.

6. What makes the Ecampus strategy successful?

To be successful, a new venture requires: (1) a viable opportunity, (2) sufficient resources, and (3) and a skilled entrepreneurial team. At the entry stage, creating new ways to meet the consumers' needs is considered a pioneering strategy. A pioneering strategy is disruptive to the industry. If the consumers accept it, the established firms in the industry will rush to copy the new business model. At the start-up stage, Campus certainly had a viable opportunity, a skilled entrepreneurial team, and sufficient resources.

Ecampus followed the Resource-Based model. The Resource-Based model assumes that a firm's success is primarily due to a unique set of resources and capabilities, rather than industry structural characteristics. Firms that achieve competitive advantage produce above average returns in the industry. However, gaining a sustainable competitive advantage is rare and hard to duplicate. In the beginning, Ecampus developed a unique alliance with WCT, acquired state of the art computer equipment and industry experienced and e-commerce personnel, created a distinctive organization by combining elements of successful e-tailers with the established culture and policies of the WCT Bookstore, and implemented a highly successful promotional campaign. This was the new pure play business model better than those of its competitors were.

The company has a bare-bones management staff and outsources its technical functions. All of their administrative offices are located in the warehouse site that reduces cost and improves staff interaction and cooperation.

The business model is an adaptive strategy in which existing technology and processes are used efficiently to create value for customers and its competitors. To remain viable, Ecampus needs to keep innovating to maintain their advantages.

7. **Have students develop some suggestions for what Ecampus could do to prepare for the future transition from rentals of hardcopy textbooks to e-textbooks.**

Matt Montgomery does not want to sell the company. At this time, he wants to continue growing the company internally. Because of the talents and skills of the management team, they have made the right decisions at the right time, which is a key to their success. By keeping the funding internal, they avoid diluting ownership. However, to fund rapid growth in the e-textbook industry, A Book Company might need to bring in venture capital companies to achieve rapid expansion and, possibly an eventual IPO.

There are several ways to promote rapid growth. They could look at (1) acquisitions and mergers, (2) engage in joint ventures or strategic alliances, (3) utilize excess capacity and fulfillment resources in a counter cycle operation, or (4) expand full tilt in the e-text market. These are all opportunities for Ecampus but could prove risky if not implemented properly. Have your students look at the pros and cons of the four different paths it could take and make recommendations based on the facts found in the case.

REFERENCES

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