Gilbert Equipment, SA a French transportation equipment manufacturer, is heavily decentralized. Each division head has full authority on all decisions regarding sales to internal or external customers. The Provence Division has always acquired a certain equipment component from the Normandy Division. However, when informed that the Normandy Division was increasing its unit price to E325, the Provence Division’s management decided to purchase the component from outside suppliers a t the price of E300.

The Normandy Division had recently acquired some specialized equipment that was used primarily to make this component. The manager cited the resulting high depreciation charges as the justification for the prive boost. He asked the president of the company to instruct the Provence Division to buy from Normandy at the E325 price. He supplied the following data to back his request:

Normandy Division was increasing its unit price to E325

Provence Division Purchase the Component for E300

Provence’s annual purchases of component 2,000 units

Normandy’s variable costs per unit E 280

Normandy’s fixed costs per unit E 30

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10-A2

1. Suppose there are no alternative uses of the Normandy facilities. Will the company as a whole benefit if the Provence Division buys from the outside suppliers for E300 per unit? Show computations to support your answer.

See spreadsheet

1. Suppose internal facilities of Normandy would not otherwise be idle. The equipment and other facilities would be assigned to other production operations that would otherwise require an additional annual outlay E45, 500. Should the Provence Division purchase from outsiders at E300 per unit?
2. Suppose that there are no alternative uses for Normandy’s internal facilities and the outsiders’ selling price drops by E30. Should the Provence Division purchase from outsiders?
3. As the president, how would you respond to the Normandy Division manager’s request? Would your response differ depending on the specific situations described in numbers 1 through 3 above? Why?