**P 7-8: Jolsen International**

Jim Shoe, chief executive officer of Jolsen International, a multinational textile conglomerate, has recently been evaluating the profitability of one of the company’s subsidiaries, Pride Fashions, Inc., located in Rochester, New York. The Rochester facility consists of a dress division and a casual wear division. Danielle’s Dresses produces women’s fine apparel, while the other division, Tesoro’s Casuals, produces comfortable cotton casual clothing.

Jolsen’s chief financial officer, Pete Moss, has recommended that the casual wear division be closed. The year-end financials Shoe just received show that Tesoro’s Casuals has been operating at a loss for the past year, while Danielle’s Dresses continues to show a respectable profit. Shoe is puzzled by this fact because he considers both managers to be very capable.

The Rochester site consists of a 140,000-square-foot building where Tesoro’s Casuals and Danielle’s Dresses utilize 70 percent and 30 percent of the floor space, respectively. Fixed overhead costs consist of the annual lease payment, fire insurance, security, and the common costs of the purchasing department’s staff. Fixed overhead is allocated based on percentage of floor space. Housing both divisions in this facility seemed like an ideal situation to Shoe because both divisions purchase from many of the same suppliers and have the potential to combine materials ordering to take advantage of quality discounts. Furthermore, each division is serviced by the same maintenance department. However, the two managers have been plagued by an inability to cooperate due to disagreements over the selection of suppliers as well as quantities to purchase from common suppliers. This is of serious concern to Shoe as he turns his attention to the report in front of him.

|  |  |  |
| --- | --- | --- |
|  | Tesoro’s Casuals ($000s) | Danielle’s Dresses ($000s) |
| **Sales Revenue** | $500 | $1,000 |
| **Expenses:** |  |  |
| Direct Materials | $(200) | $(465) |
| Direct Labor | $(70) | $(130) |
| Selling expenses (all variable) | $(100) | $(200) |
| **Overhead expenses:** |  |  |
| Fixed overhead | $(98) | $(42) |
| Variable overhead | $(40) | $(45) |
| **Net income before taxes** | **$(8)** | **$118** |

1. Evaluate Pete Moss’s recommendation to close Tesoro’s Casuals.
2. Should the overhead costs be allocated based on floor space or some other measure? Justify your answer.

**P 7-23: Chicago Omni Hotel**

The Chicago Omni Hotel is a 750-room luxury hotel offering guests the finest facilities in downtown Chicago. The hotel is organized in four departments: lodging, dining, catering, and retail stores. Each of these departments is treated as a profit center. Lodging is the largest profit center and is responsible for room rental, maids, reservations, main lobby, and bell captains. Dining operates the coffee shop, room service, and three restaurants out of a single kitchen. Catering services is separate from the dining operations. It offers banquet services to large parties, weddings, and business meetings through its own kitchen and staff separate from the dining department’s kitchen. However, dining and catering coordinate purchasing and staff scheduling. Retail is responsible for leasing space off the lobby to independent store owners (gift shop, car rental agencies, airline ticket counters, jewelry, flowers, toys, liquor, etc.). There are currently 14 independent stores operating in the hotel. Profit center managers are paid a salary and a bonus. The annual bonus depends on a number of factors, including their unit’s profits, customer satisfaction, and employee retention.

The following table presents budgeted operating data for the first year:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Lodging | Dining | Catering | Retail Stores | **Total** |
| Revenues ($ millions) | $39.20 | $9.80 | $5.80 | $1.90 | **$56.70** |
| Separable operating expenses | $31.10 | $6.20 | $3.50 | $0.30 | **$41.10** |
| Square footage (1,000s) | 625 | 50 | 125 | 80 | **880** |
| Number of employees | 1,000 | 140 | 35 | 4 | **1,179** |

Besides the separable expenses traced directly to each profit center, the hotel incurs the following additional expenses:

|  |  |
| --- | --- |
| Occupancy costs (interest, taxes, insurance) | $5.6 million |
| Marketing costs | $1.4 million |
| Administration (accounting, human resource, security, maintenance, and senior management | $1.1 million |
| **Total** | **$8.1 million** |

Profit center performance is part of each profit center manager’s annual bonus. Also, to evaluate how each department of the hotel is performing, senior management desires a statement calculating a performance measure.

1. Design a performance report for the Chicago Omni Hotel. Provide a statement calculating the performance of each unit using your performance report format. This statement should calculate for each unit a bottom-line profit/loss, which will be used as part of the performance evaluation and reward systems.
2. Discuss the rationale underlying the design of the performance report you chose.
3. Using your report, discuss the relative performance of each profit center. Which ones are the best and which are the worst.