

Management 306—Midterm Exam—Spring, 2011

Five years ago, you bought local territory rights to own and operate independent franchises for Tire King, a successful franchiser headquartered in Massachusetts. The 100-outlet retail chain sells private label tires alongside national brands, such as Michelin, BF Goodrich, Sumitomo, Goodyear, etc. Each retail location also performs routine car maintenance. The contract you signed requires you to pay an annual franchise fee of \$30,000, plus a royalty fee of 5% of gross annual profits (per location). In exchange, Tire King promised to support the franchises with ongoing brand advertising in both regional and national media. The contract also requires you to purchase your inventory from the franchiser.

You opened your first store in San Bernardino, and it was an immediate success. You then opened three more stores over the next several years, borrowing heavily to do so. However, six months ago, you began to have problems with your inventory shipments from headquarters. Critical parts were missing. Delivery dates slipped. And the local and national advertising stopped. You've called headquarters many times, but have never gotten a satisfactory answer. The problem has become so acute that your stores are forced to turn away business and sales have plummeted. If nothing is done soon, you will default on your loans and be forced out of business.

Yesterday, you received a call from an old friend who told you he has a warehouse full of inventory he can sell to you at rock-bottom prices. This new inventory is just what you need. And because of the extremely low prices, not only will your stores turn a profit, but you'll be able to repay your loans ahead of schedule and retire all outstanding debt--putting your stores on a rock-solid footing.

Before the first shipment arrives, however, you become suspicious about the inventory you are buying. You suspect--but cannot prove--it may be confiscated, repossessed, or even stolen. When you ask your friend, he winks and says, "Why do you think it's so cheap? Come on, everyone's doing it. It's business."

You have a silent partner, Megan Shush, who owns 50% of the business. Write a memo to her explaining what you intend to do. Will you go forward with the new merchandise? Or will you reject it? Be sure to include at least three well-supported reasons to back up your decision.