Oceania!

Role of Buyer, General Manager, Windy City Theater

By Leigh Thompson & Jennifer Bloniarz

You are the general manager of the Windy City Theater (WCT), a magnificent 4,000-seat venue in downtown Chicago. Located at the busy intersection of Lake and Michigan streets, the WCT is one of Chicago's oldest and most prestigious theaters, boasting a decorative main floor and two exquisite balconies. The finest Broadway musicals and the most hailed entertainment masters from around the globe have performed at the WCT. Like most major theater houses, WCT seeks to bring in the best musicals, concert productions, and nationally touring, live entertainment productions to the theater.

Although the WCT is privately owned and operated by a board of directors, the bulk of the major decision making concerning WCT productions falls to you. As general manager, your key responsibilities include booking the entertainment productions and structuring deals that are profitable for the theater.

It is now September. You have limited availability for booking shows in your busy WCT spring schedule. However, the week of April 14th is open due to an unexpected cancellation of a previously booked show. You would prefer to have a show at the WCT rather than not schedule anything. However, in order to justify the expenses of putting on a show, you need to structure a deal that is profitable for WCT.

Since the time that you found out about the cancellation, you have talked with three promotion companies about possible shows for the April time slot. Specifically, you have spoken with JAZZ Productions about bringing in a lyric opera. And, you have talked with CLEMENS Production Company about bringing in a new political satire play, "Stares and Strips." You have most recently spoken with UPSTAGE Productions about bringing in a variety show, "Five & Dime." Whereas each of these alternatives are attractive, none is perfect. Lyric Operas are well suited to WCT, but you have three others already in your spring schedule. Thus, you are a little worried about ticket sales. "Stares and Strips" has received mixed reviews and has not been popular in the big cities. The variety show has received favorable reviews and attracts an older audience. Of the three, you believe it has the most potential in terms of ticket sales – your major source of revenue. Your financial analyst estimated that the WCT profits of "Five & Dime" in the weeklong April 14th time slot would be $100,000.[1]

In addition to these three companies, you have also talked with the sales manager of POP production about bringing the ever-popular Broadway musical, **Oceania!** to the WCT next spring. Based on a literary classic, **Oceania!** is a well-known, family-oriented musical featuring a full orchestra, a large cast, elaborate sets and lavish costumes. A Polynesian romantic comedy, **Oceania!** is appropriate for audiences of all ages. POP Productions (POP) is one of the largest producers of live entertainment – Broadway musicals, off-Broadway musicals, concerts, and classic and contemporary plays. You have a long working history with POP, who finds that the Chicago area is a profitable market for their shows and particularly enjoys the WCT's elegance and reputation.

As is customary in the live entertainment business, the deal that you will structure with a production company will be a co-promotion, meaning that WCT and the production company will share show expenses and ticket revenues. However, the exact split of ticket profits has not been determined. Once the box office revenues are settled, additional profit generated through special events, specifically catering and concessions profit, goes into the WCT coffers. Likewise, the sale of show merchandise and memorabilia (e.g., T-shirts, souvenirs, etc.) is the sole

[1] Your financial analysts compute projected profits using a complex formula that considers projected ticket sales, ticket pricing and production and performance costs.

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profit of the production company. The purpose of negotiating with POP is to structure a deal for bringing **Oceania!** to the WCT that would be more profitable to you than your current alternative, "Five and Dime." If this is not possible, then "Five and Dime" is your best alternative.

Your job as the general manager of WCT is to get the best negotiated contract for shows at the WCT. In calculating the profit of a show to WCT, you realize that the value – determined by expected net ticket profits – is really a function of the ticket sales. Although you expect that **Oceania!** will draw a 75% house (roughly 3,000 seats), you know realistically that the ticket sales are uncertain. Your best estimate of the likelihood of ticket sales and their corresponding profits is the following:

Tickets	**Profit**[2]	**Expectation**
3600-4000	$1,200,000	10%
3000-3600	$1,000,000	30%
2400-3000	$800,000	60%

Thus, you compute the likely show profits for a week run of **Oceania!** as follows: (0.10 x $1,200,000 + 0.3 x $1,000,000 + 0.6 x $800,000) = $900,000. This figure is projected to be highly accurate (within a 98% confidence interval) by your financial analysts.

You realize, however, that your share of the ticket profits depends on the deal that you negotiate with POP. The board of directors has strictly stipulated that WCT's share of the ticket profits must be at least 50% -- in this case, $450,000. Ideally, you would like WCT's share to be 75%, or $675,000.

Your calculation of net profit is based upon 9 performances of **Oceania!** (6 evenings and 3 weekend matinees).[3] Ideally, you would like to offer additional performances to increase ticket sales. However, the only available time slots are weekday matinees, as the regular schedule cannot be altered and the run cannot be extended. Weekday matinees must be heavily discounted, as they are difficult time slots to sell and the groups that can attend expect large discounts. You have found that a profitable way to offset the nearly break-even ticket prices is to offer a dining package with the matinee performance, wherein customers buy a package deal (ticket with a luncheon). By packaging the ticket with a luncheon, you can add a high markup to the food and beverage, which are the sole profit of WCT. You have computed that each additional matinee performance would net $40,000 in catering profits, which would be the sole profit of WCT**.** The available time slots for weekday matinees are Tuesday through Friday.

The above profit projections do not include salaries for the cast and crew – the costs of which are subtracted from WCT profits. Per union guidelines, the cast is paid a weekly salary by the theater (rather than on a per show basis so as to prevent theaters from closing shows after a poor opening night). Thus, cast and crew salaries are the same no matter how many performances are made. The WCT board of directors will not authorize more than **$250,000** in cast and crew salaries for the week run of the 100-member cast and crew of **Oceania!** Ideally, you would like cast and crew salaries to be $**175,000**.

The other issue that you must discuss with POP concerns lodging and board for the cast and crew while the show is in town. You would prefer that POP make, handle, and of course, pay for their own lodging and board. However, you are aware that production companies prefer the theater to pick up the tab for lodging and boarding the cast and crew. Accordingly, you have obtained lodging and board price quotes from the nearby Hedgson Hotel (a four star hotel). Although not the most elegant hotel, the Hedgson provides quality service and reasonable prices. Because of your long-term relationship with the Hedgson, they offer you special, favorable rates on food and lodging. The Hedgson has quoted you the following rates for food for a 100-member cast and crew, 7-days, and 50% prepaid at time of booking:

breakfasts:	$6,000
lunches:	$12,000
dinners:	$18,000
all meals:	$30,000

The Hedgson has quoted you the following room rates, based upon a block of 100 rooms, 6-month advance booking arrangement, 7-night stay, and 50% prepaid at time of booking:

rooms:	$70,000
rooms w/cont. brkfst:	$75,000
rooms w/all meals:	$95,000

You would like things to work out with POP so that you can bring **Oceania!** to the WCT. You are well aware that many theatergoers are prepared to spend way beyond the ticket price to make an evening

[2] Profit based on $75 ticket, for 9 performances less performance costs, advertising costs, and ticket discounts. Figures have been rounded.

[3] These scheduled performances cannot be changed.

special. For example, your group sales manager has informed you that one of your largest corporate groups has suggested a "meet-the-cast autograph party" on opening night. Autograph parties with the cast can be extremely lucrative as your key corporate groups and patrons will often pay a large amount of money for this special occasion. You have calculated that an autograph party on opening night (Tuesday) could net $5,000 for WCT. Further, because the party is a "special event" the profits would go solely to WCT. You have also had other corporate groups inquire about autograph parties with casts on Friday and Saturday evenings. You calculate your profits after expenses to be $5,000 for each of these evenings. (It is not feasible to have autograph parties on other evenings because the clientele profile is different.)

Although you would like the best deal possible, you also know that your relationship with POP will continue as new shows for future seasons become available. For example, POP has another show, **Bugles**, currently on Broadway that has been doing well. Though much smaller in cast and crew, Bugles draws audiences. You have talked with your board of directors about bringing Bugles to WCT for a weekend next summer. Your board is prepared to authorize $120,000 for cast and crew salaries, profit sharing, and related expenses. Anything more than $120,000 in cast and crew salaries would result in negative profit for WCT.

You are about to meet with the Sales manager for POP to discuss bringing **Oceania!** to the WCT. To assist you during the negotiation, the "Negotiation Agreement Worksheet" (attached) can be used as a guide in calculating the final net worth of any agreement. In addition, an example of the net value calculation is provided on the attached sheet. At a minimum, the agreement should specify the items listed below:

- *Profit sharing*: How much of the expected net ticket profit should be shared with POP?

- *Salaries for cast and crew*: How much should WCT pay for **Oceania!** cast and crew salaries for the weeklong run?

- *Lodging/Board costs*: What lodging and board costs (if any) will be covered by WCT?

Upon completion of a deal, please complete the contract and give it to the instructor.

Negotiation Agreement Worksheet

EXAMPLE: Net Value Calculation for Buyer, General Manager, WCT Theatre

Assume: You reach an agreement with the Seller (POP Productions) on the run of **Oceania!** at WCT that involves the following terms:

Profit Share: Lump sum payment made to POP of $400,000
Cast and Crew Salaries: WCT pays $235,000 for cast and crew salaries for 1-week run of **Oceania!**
Lodging and meals: WCT provides rooms with continental breakfast and all lunches for 100-member cast. ($12,000 + $75,000 = $87,000).

The calculation of the net worth of this agreement would be the following. (So that you can better compare the projected WCT profits of **Oceania!** to your best alternative, "Five and Dime," the last figure represents profits over and above those projected for "Five and Dime.")

EXAMPLE: BUYER'S WORKSHEET: (WCT)	**BUYER**
1. Expected profit from show:	$900,000
2. Profit sharing (amount paid to POP productions):	-$400,000
3. WCT show profit less profit sharing:	$500,000 (1-2)
4. Salaries paid to cast and crew (amount paid to POP productions):	-$235,000
5. Lodging/board costs for cast and crew (paid by WCT directly):	-$87,000
6. Show profit less costs	$178,000 (3-4-5)
7. Other terms (specify)	(N/A)
8. Value of alternative deal ("Five & Dime")	$100,000
9. Net value of negotiated agreement:	$78,000 (6-8)

BUYER'S WORKSHEET: (WCT)

1. Expected profit from show:	$900,000
2. Profit sharing (amount paid to POP productions):	-$
3. WCT show profit less profit sharing:	$ (1-2)
4. Salaries paid to cast and crew:	-$
5. WCT lodging/board costs for cast and crew:	-$
6. Show profit less costs	$ (3-4-5)
7. Other terms (specify)	$
8. Value of alternative deal ("Five & Dime")	$100,000
9. Net value of negotiated agreement:	$ (6-8)