

Morton Corporation and Skyline Corporation each sell playground equipment. Morton Corporation's strategy is to focus on selling quality units at the best possible prices, while attempting to minimize selling, general, and administrative expenses (SG&A). Skyline Corporation has concluded that many customers will differentiate more on brand than quality, and is promoting its inferior goods with a significant marketing campaign.

Study each company's income statement below, and calculate the respective proportion of sales returns, the gross profit margin, and the net profit on sales. Both companies are subject to a 25% tax rate. Assuming no change in SG&A, which company would experience the biggest increase in profit from a 10% increase in net sales? Which company would experience the biggest decline in profit from a 10% decrease in net sales?

MORTON CORPORATION			
Income Statement			
For the Year Ending December 31, 20X6			
Net sales			
Gross sales	\$	945,876	
Less: Sales returns		<u>18,918</u>	\$ 926,958
Cost of goods sold			<u>709,407</u>
Gross profit			\$ 217,551
Selling expenses	\$	45,000	
General & administrative expenses		<u>120,000</u>	<u>165,000</u>
Income before taxes			\$ 52,551
Income tax expense (25%)			<u>13,138</u>
Net income			<u><u>\$ 39,413</u></u>

SKYLINE CORPORATION			
Income Statement			
For the Year Ending December 31, 20X6			
Net sales			
Gross sales	\$	985,876	
Less: Sales returns		<u>58,918</u>	\$ 926,958
Cost of goods sold			<u>417,131</u>
Gross profit			\$ 509,827
Selling expenses	\$	337,276	
General & administrative expenses		<u>120,000</u>	<u>457,276</u>
Income before taxes			\$ 52,551
Income tax expense (25%)			<u>13,138</u>
Net income			<u><u>\$ 39,413</u></u>