

**Certified Hospitality Accountant
Executive (CHAE) Review**

HITEC

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**These Review Notes for the CHAE Examination Are
Based on the CHAE Study Guide
Volumes 1 and 2**

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Certified Hospitality Accountant Executive (CHAE) Designation Hospitality Financial and Technology Professionals

CHAE Examination – Five Parts

- Financial Accounting
- Managerial Accounting
- Asset Management
- Hospitality Tax and Law
- Hospitality Operations

Part I - Financial Accounting

Introduction to Accounting

Questions Answered for Hospitality Managers from Accounting

- How much cash is available to pay bills?
- What was the total payroll last pay period?
- What amount of property taxes did we pay this year?
- What amount of interest did we pay on long-term debt last year, and how much must be paid during the current year?
- How much does a current guest owe the hotel?
- What were the total food sales for the dinner period last night?
- What amount of food inventory was on hand at the beginning of the month?
- When did we purchase the kitchen range, and how much did it cost?
- How much do we owe the bank on the mortgage?
- What are payroll costs as a percentage of room sales?
- What amount of dividends did we pay to stockholders this past year?
- What is the ratio of food and beverage sales to room sales this past month?
- How much do we owe the meat purveyor?
- When is the utility bill, received yesterday, due?

Accounting

- The American Accounting Association defines accounting as “the process of identifying, measuring, and communicating economic information to permit informed judgments and decisions by users of the information.”

Bookkeeping

- Clerical
- Routine
- Part of Accounting

Accounting is a Profession

- Financial
- Cost
- Managerial
- Tax
- Auditing
- Accounting Systems

Organizations That Influence Accounting

- American Institute of Certified Public Accountants (AICPA)
- Financial Accounting Standards Board (FASB)
- Securities and Exchange Commission (SEC)
- Internal Revenue Service (IRS)
- Hospitality Financial and Technology Professionals (HFTP)

Forms of Business Organizations

- Sole Proprietorship
- Partnership
- Limited Partnership
- "C" Corporation
- "S" Corporation

Principles of Accounting

- Cost Principle
- Business Entity
- Continuity of the Business Unit
- Unit of Measurement
- Objective Evidence
- Full Disclosure
- Consistency
- Matching
- Conservatism
- Materiality

End Products

- Income Statement
- Balance Sheet
- Statement of Cash Flows

Methods of Recording

- Cash Basis Accounting
- Accrual Basis Accounting

Fundamental Accounting Equation

- $\text{Assets} = \text{Liabilities} + \text{Equity}$
- Balance Sheet
- Assets - Things Owned
- Liabilities - Obligations
- Equity - Residual Claims on Assets

Expanded Fundamental Accounting Equation

- Revenue and Expense Accounts
- Income Statement
- Temporary Accounts
- Nominal - Exist in Name
- Netted and Closed to Equity

Accounting for Business Transactions

Debits and Credits

- Debits on Left
- Credits on Right
- Debits Must Always Equal Credits
- Debit Does Not Necessarily Mean Increase or Decrease
- Credit Does Not Necessarily Mean Increase or Decrease
- Normal Balances
- Asset - Debit
- Liability - Credit
- Equity - Credit
- Revenue - Credit
- Expense - Debit
- Contra Assets – Credit
- Equity Withdrawals - Debit

Accounting Cycle

- Transaction Recorded in Journals With Equal Debits and Credits
- Amounts are Posted From Journals to Ledgers
- Trial Balance is Prepared
- Adjusting Entries are Prepared in Journals
- Adjusting Entries are Posted to Ledger Accounts
- An Adjusted Trial Balance is Prepared
- Income Statement and Balance Sheet are Prepared
- Revenue and Expenses Accounts are Closed
- Post Closing Trial Balance is Prepared

Accounts

- Economic events are reflected in accounts
- T-account - title, left side, right side (debit or credit)
- Accounts have balances - either debit or credit (left side or right side)

Asset Accounts

- Cash
- Notes Receivable
- Accounts Receivable
- Accrued Interest Receivable
- Marketable Securities
- Inventories of Merchandise
- Office Supplies
- Other Prepaid Expenses
- Investments
- Property and Equipment

Liability Accounts

- Notes Payable
- Accounts Payable
- Taxes Charged to Guests and Withheld from Employees
- Income Taxes Payable
- Accrued Expenses
- Unearned Income
- Mortgage Payable

Owners' Equity Accounts

- Capital Accounts
- Retained Earnings
- Preferred Stock
- Common Stock
- Capital Surplus

Revenue Accounts

- Room Sales
- Food Sales
- Beverage Sales
- Gift Shop Sales
- Revenue Accounts
- Green Fees Pro Shop Sales
- Banquet Sales
- Interest and Dividend Income

Expense Accounts

- Cost of Food Sold
- Cost of Beverage Sold
- Wage and Related Costs
- Expense Accounts
- Supplies
- Rent
- Utilities
- Advertising

Recording Asset, Liability and Equity Changes

- Purchasing a Hotel. Debit Building and Land and Credit Mortgage Payable and Cash
- Borrowing Cash. Debit Cash and Credit Notes Payable
- Purchasing Furniture. Debit Furniture and Credit Cash

Recording Revenue and Expense Changes

- Sold a Room. Debit Cash and Credit Room Sales
- Paid Wages. Debit Wage Expense and Credit Cash

Recording Changes in Owners' Withdrawal Account

- Withdrew Cash From the Business. Debit Owner's Drawing Account and Credit Cash

General Ledger

- Group of Accounts
- Have a Chart of Accounts
- Accounts are Numbered in a Uniform Manner
- Uniform System of Accounts for Hotels
- Suggestions for Handling Certain Transactions

Journalizing

- We do not record into ledgers directly.
- Journalizing process is first.
- Journals provide space to provide details of the transactions, include all the information in one place, and help minimize errors.

General Journal

- Date
- Account titles that are being debited or credited and amounts
- Explanation of the transaction
- Transactions are then “posted” to the appropriate ledger accounts with reference back to the journal.

Trial Balance

- A list of all accounts and the balances (either debit or credit in separate columns)
- All debit balances are added and all credit balances are added.
- The totals are compared - should be the same - if not posting/transaction errors
- Not proof of accuracy

Compound Journal Entries

- More than one debit or more than one credit in the transaction.
- All debits must equal all credits in total for each transaction

Accounting Adjustments

What Are Adjusting Entries?

- Entries required to record expenses that have been incurred but not paid
- Entries to recognize some liabilities
- Entries to correct earlier journalizations of transactions

Why Adjusting Entries Are Needed

- Time Period Principle
- Matching Principle
- Accrual Accounting
- Materiality Principle

Accounts Affected

- Every adjusting entry affects a balance sheet (asset, liability, equity) account and an income statement account (revenue, expense)
- Adjusting entries never ever include cash as an affected account

Cash Vs Accrual Basis

- Cash basis recognizes revenues only when cash is received and expenses only when cash is disbursed
- Accrual basis recognizes expenses when they are incurred rather than paid such as depreciation, inventory, operations expenses

Deferral and Accrual Adjusting Entries

- Deferrals - previously recorded assets that become expenses (prepaid insurance) and previously recorded liabilities that become revenue (deposits on events)
- Accrued - assets and revenues not previously provided (account receivable) and liabilities and expenses not previously recorded (utility bill received and not paid)

Deferred Example

- Paid \$12,000 for a one year fire insurance policy on January 1
- Probably debited prepaid insurance and credited cash. Exchanged on asset for another since the insurance wasn't used at the time of the purchase.
- At the end of the month we want to recognize one month's insurance expense
- Debit Insurance Expense \$1,000 ($\$12,000 / 12$) and Credit Prepaid Insurance (asset) \$1,000

Straight Line Depreciation - Cost minus Salvage Value divided by periods of life

- One of Many Ways to Compute Depreciation Expense - Non Cash Expense
- Cost Principle is Applied
- Debit Depreciation Expense and Credit Accumulated Depreciation (contra asset)
- Unearned Revenues - Sometimes Customers Pay in Advance for Services - Debit Cash and Credit Liability to Customer
- When Customer Receives Service - Debit the Liability to Customer and Credit Revenue

Accrual Example

- Wages - Need to record the amount of wages earned by employees at the end of the period but not paid yet (Debit Wage Expense Credit Accrued Wages Payable)
- Utilities - Estimate the utilities expense and record as a liability since the bill has not been received
- Accrued Interest Earned - Interest not yet received is still income

Failure to Prepare Adjusting Entries

- Erroneous Income Statements and Balance Sheets
- Violation of Matching Principle
- Violates Accrual Accounting
- End up with inaccurate financial records

Corporate Accounting

Advantages of Corporations

- Limited Liability
- Unlimited Life
- Ease in Acquiring Capital
- Ease of Transfer of Shares
- Professional Management

Disadvantages of Corporations

- Double Taxation
- Regulation

Corporation Fundamentals

- Pays Taxes on Profits
- Common Stock
- Par Value
- Additional Paid-In Capital in Excess of Par
- Dividends
- Retained Earnings Statement
- Stock Subscriptions

Preferred Stock

- Preferred in Terms of Dividends
- Preferred in Event of Liquidation
- Cumulative
- Callable
- Non-Voting
- Some Are Convertible
- Some Are Participating Preferred

Other Corporation Issues

- Cash Dividends Versus Stock Dividends
- Stock Splits
- Treasury Stock
- Book Value Per Share of Common Stock

The Balance Sheet

Uniform System of Accounts

- Standardized Accounting System
- Industry Driven
- Basic Formats
- Departmental Statement and Schedules
- Explanations and Discussions
- Allows Comparison - Other Operations and Self
- Can be Used by Any Size Operation
- Property Level Designed Use
- Direct Operating Expense Based
- Cost of Goods Sold
- Direct Labor Expense
- Direct Expenses

Balance Sheet - The Statement of Financial Position

- $Assets = Liabilities + Equity$
- Statement of Assets, Liabilities, and Owners' Equity at a Point in Time

Assets

- Current Assets
- Noncurrent Receivables
- Investments
- Property and Equipment
- Other Assets

Liabilities

- Current Liabilities
- Long Term Debt
- Deferred Income Taxes
- Commitments / Contingencies
- Other Long-Term Liabilities

Owners' Equity

- Capital Stock
- Additional Paid In Capital
- Retained Earnings
- Treasury Stock

Questions Answered by Balance Sheet

- Amount of Cash on Hand?
- What is the Total Debt?
- What is Funding Mix?
- How Much is Owed to the Hotel?
- Questions Answered by Balance Sheet
- What are the Tax Liabilities?
- Can Current Debt be Paid?
- What is the Financial Strength?
- How Much have Stockholders Invested in the Assets?

Balance Sheet Formats and Structure

- Account Format - Assets on Left and Liabilities and Equity on Right
- Report Format - Assets First Followed by Liabilities and Equity
- Current Assets - Converted to Cash or Used in Operation in One Year or Normal Operating Cycle
- Listed in Order of Liquidity
 - Cash (All Forms)
 - Marketable Securities
 - Receivables
 - Inventories
 - Prepaid Expenses
- Current Liabilities - Obligations expected to be Satisfied in One Year or Normal Operating Cycle
- Current Liability Presentation
 - Payables
 - Advance Deposits
 - Current Maturities of Long Term Debts
 - Dividends Payable
 - Income Taxes Payable

Noncurrent Assets

- Noncurrent Receivables - not expected to be collected within one year - owners are shown separate
- Investments - securities, land not in use, and affiliate advances not to be collected within one year
- Property and Equipment - Fixed Assets, Capital Leases - Less accumulated depreciation
- Smallwares - New USOA Recommends to Expense or Write off Over 3 Years
- Other Assets - Deferred Charges, Security Deposits
- Preopening Expenses - New USOA Recommends to Expense in Current Period

Other Assets

- Goodwill
- Cash Surrender Value of Life Insurance
- Deferred Charges
- Possibly Deferred Income Taxes

Long Term Liabilities

- Obligations Beyond One Year
- Notes Payable
- Mortgages Payable
- Bonds Payable
- Capitalized Lease Obligations
- Possibly Deferred Income Taxes

Owners' Equity

- Preferred Stock, Par @ \$\$\$
- Shares Authorized
- Shares Issued
- Common Stock, Par @ \$\$\$
- Shares Authorized
- Shares Issued
- Owners' Equity
- Treasury Stock
- Additional Paid in Capital
- Retained Earnings
- Sole Proprietorship Capital
- Partnership - Show Each Owner's Capital
- Withdrawal Accounts

Footnotes

- Significant Accounting Policies
- Accounts and Notes Receivable
- Inventories
- Investments
- Property and Equipment
- Current Liabilities
- Long Term Debt
- Capital Stock
- Employee Benefit Plans
- Leases
- Segments of Business
- Supplemental Financial Information
- Commitment/Contingent Liability
- Income Taxes

Balance Sheet Analysis

- Comparative Statements or *Horizontal Analysis*
- Compute Absolute Change
- Compute Relative Change
- Investigate Significant Differences
- Internal Analysis

Balance Sheet Analysis

- Common Size Statements or *Vertical Analysis*
- Total Assets Equal 100%
- Total Liabilities and Equity Equals 100%
- Balance Sheet Analysis
- Each Individual Account is Shown as a Percentage of the Total
- Compare to Industry, Like Businesses or Self

Balance Sheet Analysis

- Base Year Comparisons
- Series of Years
- Compared to a Base Year

Balance Sheet Limitations

- Does Not Reflect Current Values of Assets (Booked According to Cost Principle)
- Does Not Include Some Things of Value Such as Personnel, Location, Customer Base, Goodwill
- Balance Sheet Limitations
- Becomes Quickly Outdated
- Some Account Balances are Estimates Such as Depreciation and Estimates for Uncollectibles

The Income Statement

Income Statement

- Statement of Earnings
- Profit and Loss Statement
- Statement of Operations
- Frequency - Daily, Weekly, Monthly, Quarterly, Annually
- Reports on a Period of Time
- Departmental Income Statements
- Uniform System of Accounts

Questions Answered

- How Profitable Was Business?
- What Were the Total Sales?
- How Much Was the Labor Cost?
- What Was Food Cost Percent?
- Are Sales In(de)creasing?
- Are Expenses In(de)creasing?
- What Were Marketing Costs?
- What Percent of Sales Is Profit?

Elements of Income Statement

- Revenue - Sale of Goods and Services; Investment Income; Rental Income
- Expenses - Outflows to Produce Goods; Cost of Goods Sold; Labor; Controllable Expenses; Noncontrollable Expenses
- Elements of Income Statement
- Other Gains and Losses - From Incidental Transactions; Acts of Nature
- Period Income or Loss - Add/Deduct To/From Equity
- Internal Users - Management
- External Users - Summary Statement

Uniform System of Accounts

- Standardized Accounting System
- Industry Driven
- Basic Formats
- Departmental Statement and Schedules
- Explanations and Discussions
- Allows Comparison - Other Operations and Self
- Can Be Used by Any Size Operation
- Property Level Designed Use
- Direct Operating Expense Based on Cost of Goods Sold, Direct Labor Expense, Direct Expenses

Contents of the Income Statement

- Operated Departments
- Net Revenues by Department
- Cost of Sales
- Payroll and Related
- Other Direct Expenses
- Departmental Income - Net Department Revenues Less Departmental Expenses
- Non Operated Departments
- Undistributed Operating Expenses
- Payroll and Related and Other Are Shown Separately
- Administrative and General
- Data Processing
- Human Resources
- Transportation
- Marketing
- Property Operations and Maintenance
- Energy Costs
- Other Expenses (Board Decisions)
- Management Fees
- Fixed Charges (Capacity Costs)
- Other Gains or Losses
- Sale of Property/Equipment

Comparative Statements

- Horizontal Analysis
- Absolute Change
- Relative Change
- Income Statement Analysis
- Investigate Significant Differences
- Internal Analysis

Common Size Statements

- Vertical Analysis
- Total Revenue Equal 100%
- Income Statement Analysis
- Each Expense Shown As Percentage of Total
- Compare to Industry, Like Businesses or Self

Data Availability

- PKF Consulting - Trends in the Hotel Industry (U.S. and Worldwide)
- PKF Consulting - Clubs in Town and Country
- Smith Travel Research - The Host Report - Hotel Operating Statistics
- NRA - Restaurant Industry Operations Report
- Local Hotel Organizations

The Statement of Cash Flows

The Statement of Cash Flows Answers

- How Much Cash Was Provided by Operations
- What Amount of Property and Equipment Was Purchased
- How Much Long Term Debt Was Borrowed
- The Statement of Cash Flows Answers
- What Funds Were Raised by the Sale of Capital Stock
- What Amount of Dividends Were Paid
- How Much Was Invested in Long Term Investments

The Statement of Cash Flows

- Required Statement Since 1988 by the FASB
- Replaces the Statement of Changes in Financial Position
- Focused on Cash Changes From Operating Activities Investing Activities Financing Activities
- Cash Equivalents = Cash

Use and Purpose of The Statement of Cash Flows

- Assess Ability to Generate Future Cash Flows
- Assess Ability to Meet Current Obligations
- Shows the Difference Between Net Income and Cash Generated
- Shows the Effect of Cash and Non Cash Financing and Investing Activities
- Internal and External Users
- *Management*
 - Assess Liquidity
 - Assess Financial Flexibility
 - Determine Dividend Policy
 - Plan Investing and Financing
 - Use and Purpose of The Statement of Cash Flows
- *Investors and Creditors*
 - Assess Ability to Pay Bills
 - Assess Ability to Pay Dividends
 - Assess Need for Financing

Six Steps...

- Determine Change in Cash Account - The "Answer"
- Summarize Operating Activities
 - *Cash in From Sale of Services*
 - *Cash in From Interest and Dividends*
 - *Cash Out for Expenses*
- Summarize Investing Activities
 - *Cash in From Property Sales*
 - *Cash in From Investment and Security Sales*
 - *Cash Out for Loans and Purchases of Property and Investments*
- Summarize Financing Activities
 - *Cash in From Sale of Stock*
 - *Cash in From Issuing Debt*
 - *Cash Out for Paying Debt*
 - *Cash Out to Pay Dividends*
 - *Cash Out to Reacquire Capital Stock*
- Schedule of Noncash Investing and Financing Activities
 - *Exchange of Capital Stock for Property and Equipment*
 - *Capital Lease Obligations Incurred*

- Present the Statement of Cash Flows
 - *Cash Flows From Operating Activities*
 - *Cash Flows From Investing Activities*
 - *Cash Flows From Financing Activities*
 - *Net Increase (Decrease) in Cash*
 - *Cash At Beginning of Period*
 - *Cash At End of Period*
 - *Supplemental Schedule - Non Cash Transactions*

Operating Activities - Direct Method

- Accrual Accounting - Recognize Expenses When Incurred Revenue When Earned.
- Convert Each Item on the Income Statement From Accrual Basis Accounting to Cash Basis Accounting
- Ignore Non Cash Transactions
- Cash Receipts From Sales Plus Interest and Dividends Received
- Cash Disbursements for Operating Expenses
- FASB Prefers Direct Method

Operating Activities - Indirect Method

- Used in Hospitality Operations
- Start With Net Income
- Adjust for Non Cash Expenses - Such As Depreciation (Add)
- Adjust for Gains or Losses on Sale of Noncurrent Assets or Marketable Securities (Add or Deduct)
- Adjust for Changes in Current Accounts Except Cash and Dividends Payable
- Accounting for Changes in Current Accounts Using Indirect Method
 - A Decrease in a Current Asset Is Added to Net Income
 - An Increase in a Current Asset Is Deducted From Net Income
 - A Decrease in a Current Liability Is Deducted From Net Income
 - An Increase in a Current Liability Is Added to Net Income

Net Cash Flows From Investing Activities

- Examine Non Current Asset Accounts for Changes Between the Balance Sheet Dates
 - *Investments*
 - *Property and Equipment*
- Look at Journal Entries
- Read Footnotes to Statements
- Examine Non Current Liability and Owners' Equity Accounts for Changes Between the Balance Sheet Dates
 - *Look at Journal Entries*
 - *Read Footnotes to Statements for Non Cash Transactions*
- Analyze Dividends Payable Account for Cash Payments

Part II - Managerial Accounting

Introduction to Managerial Accounting

Financial Vs Managerial Accounting

- Financial Accounting Is Historical
- Managerial Accounting Provides Information, Enhances Controls, and Plans for Events

The Hospitality Business

- Lodging \$100 Billion
- Food and Beverage \$425 Billion
- Lodging and Food and Beverage Equates to 5% of GNP
- Seasonal Business
- Fluctuating Demand
- Short Conversion Time - Food
- Selling Space - Now or Never
- Labor Intensive
- Intensive Fixed Asset Investment

Hotel Revenue

- 64.1% Rooms
- 19.5% Food
- 5.1% Beverage
- 7.0% Other Departments
- 2.5% Telephone Department
- 1.8% Rentals and Other Income

Hotel Costs and Expenses

- 44.9% Salaries, Benefits and Meals
- 30.0% Operating Expenses
- 11.0% Cost of Sales
- 5.5% Energy Costs
- 8.6% Taxes, Management Fees, Insurance

Uniform System of Accounts

- Industry Uses a Uniform System of Accounting
- Lodging Operations, Restaurants, Clubs

Principles of Accounting

- Cost Principle
- Business Entity
- Continuity of the Business Unit
- Unit of Measurement
- Principles of Accounting
- Objective Evidence
- Full Disclosure
- Consistency
- Matching
- Principles of Accounting
- Conservatism
- Materiality
- Cash Basis Accounting
- Accrual Basis Accounting

Fundamental Accounting Equation

- Assets = Liabilities + Equity
- Balance Sheet
- Assets - Things Owned
- Liabilities - Obligations
- Equity - Residual Claims on Assets

Revenue and Expense Accounts

- Income Statement
- Temporary Accounts Nominal - Exist in Name
- Netted and Closed to Equity

Forms of Business Organizations

- Sole Proprietorship
- Partnership
- Limited Partnership
- "C" Corporation
- "S" Corporation

Debits and Credits

- Debits on Left
- Credits on Right
- Debits Must Equal Credits - Double Entry Bookkeeping

Normal Balances

- Asset - Debit
- Liability - Credit
- Equity - Credit
- Revenue - Credit
- Expense - Debit
- *Other Types of Accounts*
 - Contra Assets - Credit
 - Equity Withdrawals - Debit

Accounting Cycle

- Transaction Recorded in Journals With Equal Debits and Credits
- Amounts are Posted From Journals to Ledgers
- Trial Balance is Prepared
- Adjusting Entries are Prepared in Journals
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- Revenue and Expenses Accounts are Closed
- Post Closing Trial Balance is Prepared

Basic Cost Concepts

Cost Related Questions

- What Are the Hotel's Fixed Costs?
- Which Costs Are Relevant to Purchasing a New Microcomputer?
- What Are the Variable Costs of Serving a Steak Dinner?
- What Is the Opportunity Cost of Adding 25 Rooms to the Motel?
- What Is the Standard Cost of Catering a Banquet for 500 People?
- What Are the Hotel's Controllable Costs?
- How Are Fixed Cost Portions of Mixed Costs Determined?
- How Are Costs Allocated to the Operating Departments?
- Which Costs Are Sunk Costs in Considering a Future Purchase?
- Which Costs Are Relevant to Pricing a Lobster Dinner?

Cost Terminology

- Fixed Costs - Costs That Are Normally Not Affected by Changes in Sales Volume Over a Relevant Range
- Relevant Range - Range of Activity Under Which Cost Data Are Valid
- Cost Terminology
- Variable Costs - Costs That Are Constant on a Per Unit Basis
- Mixed Costs - Also Called Semi Fixed or Semi Variable Costs and Have a Fixed and a Variable Component
- Controllable Costs - Costs That Can Be Changed in the Short Run and Are Under the Control of an Operating Manager
- Noncontrollable Costs - Costs That Normally Cannot Be Changed in the Short Run
- Prime Costs - Material Plus Labor
- Unit Cost - Cost Per Salable Unit
- Avoidable Costs - Fixed Costs That Are Eliminated During a Shutdown
- Capacity Fixed Costs - Costs Incurred When Providing Goods or Services
- Discretionary Fixed Costs - Costs That Management Can Avoid
- Step Costs - Costs That Change Due to Changes in a Range of Activity
- Overhead Costs - All Costs Other Than Direct Costs Incurred by Profit Centers (Indirect Costs)
- Differential Costs - Costs That Differ Between Two Alternatives
- Sunk Cost - A Past Cost Relating to a Past Decision
- Average Cost - Cost to Produce an Item (Include All Costs)
- Incremental Costs - How Much It Costs to Produce Another Unit (Variable Costs Only)
- Standard Costs - What Costs Should Be Under Ideal Situations
- Indifference Point - The Level of Activity Where Costs Are the Same Under Variable and Fixed Arrangements

Determination of Mixed Cost Elements

- High - Low (Two Point Method)
- Scattergram
- Regression Analysis (Method of Least Squares)
- High - Low (Two Point Method)
 - Select a Sample High and Low Month for Sales (or Costs)
 - Calculate Difference in Two Measures (Sales or Costs and Activity)
 - Divide Activity Difference Into Sales or Cost Difference
 - Result Is Variable Cost Per Unit
 - Solve for Fixed Costs

- Scattergram
 - Graph Sales (Cost) Data With Activity
 - Draw Best Straight Line Through Data
 - Where Intersects Y Axis Is Fixed Costs
 - Solve for Variable Cost Per Unit
- Regression Analysis Method of Least Squares
 - Computation of Best Straight Line
 - $Y = a + bx$
 - b = Slope of Line or Variable Cost Per Unit
 - A = Y Intercept or Fixed Cost

Cost Allocation

- Distribution of Overhead Costs to the Profit Centers
- Single Allocation Base Approach - Uses a Single Factor Such As Square Footage, Number of People, Revenue
- Multiple Allocation Approach - Use the Most Closely Related Factor

Analysis After Allocation

- What Is Income (Loss)?
- Which Allocated Overhead Costs Are Fixed?
- What Other Departments Are Affected?
- Any Operating Alternatives?

Use of Cost Data

- Which Piece of Equipment Should Be Purchased?
- How Much Should We Charge?
- Can We Sell Below Cost?
- What Time Periods Should We Be Open?
- Should We Close For the Season?
- Which Segment Should Get the Most Support?

Cost-Volume-Profit Analysis

Cost-Volume-Profit Assumptions

- Fixed Costs Remain Constant During the Period Being Analyzed.
- Variable Costs Fluctuate in a Linear Fashion With Revenues.
- Variable Costs Are Constant on a Per Unit Basis.
- Productivity Remains Constant.
- Revenues Are Proportional to Variable Costs.
- There Are No Volume Discounts.
- All Costs Can Be Broken Down Into Their Fixed and Variable Components.
- Joint Costs Are Not Eliminated When One Department Is.

CVP Basic Formula

- How Much Should Be Charged to Break-Even?
 - 10 Room Motel
 - Variable Costs Are \$5 Per Room
 - Fixed Costs Are \$2,500
 - 250 Rooms Will Be Sold
 - $SP = VC \text{ Per Room} + (\text{Fixed Costs} / \text{Number Rooms Sold})$
 - $SP = \$5 + (\$2,500 / 250)$
 - $SP = \$15 \text{ Per Room}$

- How Much Should Be Charged to Earn \$2,000 in a 30 Day Period?
 - 10 Room Motel
 - Variable Costs Are \$5 Per Room
 - Fixed Costs Are \$2,500
 - CVP Basic Formula
 - 250 Rooms Will Be Sold
 - $SP = VC \text{ Per Room} + (\text{Profit} + FC) / \text{Number Rooms Sold}$
 - $SP = \$5 + (\$2,000 + \$2,500) / 250$
 - $SP = \$23 \text{ Per Room}$

CVP Formula for Single Product Analysis

- I = Net Income
- S = Selling Price
- X = Units Sold
- V = Variable Costs Per Unit
- F = Total Fixed Costs (Plus Profit)
- CVP Formula for Single Product Analysis
- $SX = \text{Total Revenue}$
- $VX = \text{Total Variable Costs}$

Basic Formula for Break-Even (Income Equals 0)

- $0 = SX - VX - F$
- Break-Even Formula Variations
- Units Sold at Break-Even
- $X = F / (S - V)$
- Fixed Costs at Break-Even
- $F = SX - VX$
- Selling Price at Break-Even
- $S = (F / X) + V$
- Variable Cost Per Unit at Break-Even
- $V = S - (F / X)$

Contribution Margin

- Contribution Margin (CM) Is the Selling Price, or Sales, Minus the Variable Cost(s).
- Contribution Margin Percentage (Ratio) Is the CM Divided by the Selling Price (or Sales).
- To Get Break-Even in Units, Divide the Fixed Costs by the Contribution Margin.
- To Get Break-Even in Sales Dollars, Divide the Fixed Costs by the Contribution Margin Percentage.

Weighted Contribution Margin Percent

- Since Our Products Have Different CM, We Use CM Percent (Weighted) a Lot.
- The Weighted CMR Is Computed As Follows:
- $(\text{Total Revenue} - \text{Total Variable Costs}) / \text{Total Revenue} = \text{Weighted Contribution Margin Percent}$
- Divide the Weighted CMR Into the Fixed Costs (and Profit if Applicable) and the Result is the Required Sales Level.

Margin of Safety

- Excess of Budgeted or Actual Sales Over Sales at Break-Even
- Expressed in Units or Dollars

Sensitivity Analysis

- Study of the Sensitivity of Dependent Variables to Changes in Independent Variables
- Looks at the Incremental Number of Units Required to Sold to Cover Additional Costs

Operating Leverage

- Extent to Which Expenses Are Fixed Rather Than Variable
- "Highly Levered" When Fixed Costs to Variable Costs Ratio Is High
- Highly Levered Means a Small Increase in Sales Yields a Large Profit (Above Break-Even)

Providing for Income Taxes

- $B * R = T$ and $B - T = A$
- Substitute $(B * R)$ for T and We Have:
- $B - (B * R) = A$ or $B * (1 - R) = A$ or
- $B = A / (1 - R)$

Cost Approaches to Pricing

Pricing Questions

- Which Costs Are Relevant in the Pricing Decision?
- What Is the Common Weakness of Informal Pricing Methods?
- What Are Common Cost Methods of Pricing Rooms?
- What Are Common Methods of Pricing Food and Beverages?
- How May Profitability and Popularity Be Considered in Setting Food Prices?
- Will Departmental Revenue Maximization Result in Revenue Maximization for the Hospitality Firm?
- What Is Integrated Pricing?
- What Is Price Elasticity of Demand?

Price Elasticity of Demand

- Measures How Sensitive Demand Is to Changes in Price
- Either Elastic or Inelastic
- Computed by Dividing Change in Quantity Demanded by Base Quantity BY Change in Price by Base Price
- If Less Than 1 - Inelastic (Demand Is Insensitive to Price Changes)
- If Greater Than 1 - Elastic (Demand Is Sensitive to Price Changes)
- Competition, Uniqueness Affect Elasticity
- When Change Prices, Test for Elasticity

Informal Pricing Methods

- Competitive
- Intuitive
- Psychological
- Trial and Error
- Follow The Leader

Informal Pricing Methods

- Consider First:
 - *Historical Price Changes*
 - *Guest Perceptions (Price/value)*
 - *Competition*
 - *Modify by Rounding*

Mark Up Approaches

- *Ingredient Mark Up*
 - Determine Ingredient Costs
 - Determine Multiple to Use
 - Multiply Costs by Multiplier
 - Adjust Using Qualitative Factors
- Multiplier
 - $1 / \text{Desired Food Cost Percentage}$
 - Example $1 / 40\% = 2.5$
- Alternative to Multiplier
 - Divide Costs By Desired Food Cost Percentage
 - Example $\$3.00 \text{ Cost} / 40\% = \$7.50 \text{ Selling Price}$
- *Prime Ingredient Mark Up*
 - Determine Prime Ingredient Cost
 - Some Versions Add in a Fixed Dollar Amount for Other Ingredients
 - Determine Multiple to Use - Higher Than Mark up (Arbitrary)
 - Multiply Costs by Multiplier
 - Adjust Using Qualitative Factors

Rooms Pricing Traditional Method

- \$1 Per \$1,000 Cost Per Room
- Doesn't Consider Current Value
- Doesn't Consider Other Services
- Rooms Pricing Traditional Method
- Assumes 70% Occupancy
- Assumes Profitable Food and Beverage

Rooms Pricing Hubbart Formula

- "Bottoms Up"
- Start With Profit
- Determine Pretax Profit
- Rooms Pricing Hubbart Formula
- Add in Fixed Charges
- Add in Undistributed Operating Costs
- Estimate Non Room Income (Loss)
- Sum Is Rooms Department Income
- Rooms Pricing Hubbart Formula
- Rooms Revenue Equals Rooms Income Plus Rooms Department Costs
- $\text{ADR} = \text{Room Revenue} / \text{Rooms to Be Sold}$

ADR to Single and Double Rates

- $(\text{Singles Sold} * \text{Single Rate}) + (\text{Doubles Sold} * (\text{Single Rate} + \text{Price Differential})) = \text{Average Rate} * \text{Rooms Sold}$
- Solve for Each Rate

Yield Management

- Increasing the Rooms Revenue
- Take the Guess Work out of Your Rooms Inventory
- The Business of Selecting the Most Profitable Reservations
- Yield Management Is the Process of Selecting the Most Profitable Reservations, When Demand Exceeds Supply.
- That Is, If You Have One Room Left to Sell, but More Than One Request for It, You Would Prefer to Sell to the Guest Who Provides the Greatest Long-Term Contribution to Your Company.
- The Business of Selecting the Most Profitable Reservations

Why Yield Management?

- Increase Room Revenues
- Improve Total Corporate Profitability
- Enter New Markets With Strategic Pricing
- Identify and Respond More Quickly to Changing Market Trends
- Manage Distribution Channels More Effectively

Yield Management System

- Maintenance Should Support Numerous Daily Adjustments
- Identify Excess Demand Dates
- Project Demand by Length-Of-Stay

Benefits from Yield Management

- Maximize Revenue
- Increase Occupancy
- Improve Average Rate
- Measure Revenue Performance
- Benefits from Yield Management
- Identify Sales Trends
- Respond to Occupancy "Gaps"
- Identify Booking Trends
- Manage Critical Dates
- Control Discount Availabilities
- Group Block Management

Benefits from Yield Management

- Analyze No-Shows
- Apply Total Property or Room Type Overbooking
- Length of Stay Opportunities
- Utilize Automated Tracking
- Identify Booking Trends

Menu Engineering

- A Tool to Increase Food and Beverage Profits
- Smith and Kasavana
- Analyzes Popularity and Contribution Margin
- Two by Two Matrix
- Classified Items As Stars, Dogs, Puzzles, or Plowhorses
- Popularity
- Item Is Popular If Individual Item's Sales Mix Exceeds 70% of the Average Popularity
- Average Popularity = $(100\% / \text{Number of Items}) * (70\%)$
- Popularity Example
- 10 Items
- Average Popularity = $(100\% / 10) * (70\%) = 7\%$
- If Individual Sales Mix Is $> 7\%$, Popular
- Contribution Margin
- Selling Price Minus Variable Costs or Gross Profit
- Compute for Each Item
- Contribution Margin
- Compare Against Weighted Average Contribution Margin for Menu Section Engineered
- If Item Is $> WACM$ - Label "High"
- Weighted Average Contribution Margin Calculation
- Compute Individual Contribution Margin
- Multiply Item Contribution Margin by Number of Item Sales
- Result Is Total Contribution Margin
- Weighted Average Contribution Margin Calculation
- Divide Total Contribution Margin by Number of Sales
- Result Is Weighted Average Contribution Margin

Internal Control

The Industry's Vulnerability

- Cash Business
- Many Transactions
- Low Skill Employees
- Perception of Industry As Low Social Status
- Items Used Have "Street Value"
- Items Used Are Used by General Population

AICPA Objectives of Internal Control

- Safeguard Assets
- Check Accuracy and Reliability of Accounting Data
- Promote Operational Efficiency
- Encourage Adherence to Prescribed Managerial Policies

Types of Internal Control

- Administrative - How the Company Operates
- Accounting - Impact on Financial Statements

Internal Control Basics

- System Requires - Methods and Procedures; and Reliable Forms and Reports
- Larger the Company - More Internal Control Required

Classification of Controls

- *Preventive Controls*
- Controls That Are Implemented Before a Problem Occurs Such As: Use of Locks or Segregation of Duties
- *Detective Controls*
- Controls Designed to Discover Problems and to Monitor Preventive Controls Such As External Audits or Surprise Cash Audits

Characteristics of Internal Control

- Management Leadership
- Organizational Structure
- Sound Practices
- Fixed Responsibility
- Limited Access
- Competent and Trustworthy Personnel
- Segregation of Duties
- Authorization Procedures
- Adequate Records
- Procedure Manuals
- Physical Controls
- Budgets and Internal Reports
- Independent Performance Checks

Documenting Internal Control

- Flowcharting
- Internal Control Questionnaire
- Narrative

Part 3 - Asset Management

Inventory

Accounting Principles Applied

- Consistency
- Full Disclosure
- Conservatism - Lower of Cost or Market (Item by Item or Total)

Internal Control

- Separate Custody and Records
- Take Periodic Physical Inventories
- Report Overages and Underages
- Inventory of High Priced Items Should be Taken Daily
- Storerooms Should be Secure

Periodic System

- No Continuous Records
- When Items are Bought Purchases Account is Debited (Cash or Accounts Payable is Credited)
- Value of Inventory is Known Only When a Physical Inventory is Taken
- Many Ways to Value the Inventory

Perpetual System

- Continuously Updates the Inventories
- Purchases are Added
- Items Released are Subtracted
- Merchandise Inventory Account is Used Rather Than Purchases
- Good for High Cost low Usage Items
- Tie to POS System

Basic Food Cost Calculation

- Beginning Inventory *PLUS*
- Purchases *EQUAL*
- Goods Available for Sale
- *LESS* Closing Inventory
- *EQUALS* Cost of Goods Consumed
- *Less* Goods Used Internally (Adjustments)
- *Equals* Cost of Goods Sold

Cost of Food or Beverages Sold

- Cost of Goods Consumed Plus or Minus Adjustments Equal Cost of Goods Sold
- Food or Beverage Cost Percent Equals Cost of Goods Sold Divided by Food or Beverage Sales

Adjustments

- Intraunit Transfers
- Interunit Transfers
- Grease Sales
- Steward Sales
- Gratis to Bars
- Promotion Expenses
- Employee Meals
- To General Manager
- "Comps"

Gross Profit

- Gross Profit Equals Sales Less Cost of Goods Sold
- If Understate Ending Inventory, Profit is Understated
- If Overstate Ending Inventory, Profit is Overstated

Physical Inventory

- Count Units - One Counts, One Writes
- Extend Inventory
- Foot
- Count if Own - Regardless of Location
- Don't Count if Don't Own

Transportation Costs

- Cost of Item Includes Shipping, Transportation (Freight)
- FOB Destination or Shipping Point

Value of the Inventory

- At Least Five Methods
- Doesn't Have to Follow Flow of Goods
- Specific Identification
- First In - First Out (FIFO)
- Last In - First Out (LIFO)
- Weighted Average Price
- Most Recent Price

Specific Identification

- Know Exact Date and Price of Purchase
- Extend Each Item
- Total

First In First Out

- FIFO
- Follows Flow of Goods
- Balance Sheet Method
- Rising Prices Gives Inventory Profits

Last In First Out

- LIFO
- Assumes Newest Inventory is Used First
- Does Not Follow the Flow of Goods
- Income Statement Method

Weighted Average

- Weighted Average Price of Purchases is Used to Value All Items in Inventory
- Price is Applied to Remaining Inventory

Most Recent Price

- Similar to FIFO
- Only Most Recent Price is Used
- Most Common in Industry

Inventory Example

Date	Quant	Price	Extension
7/01/08	0	0.00	
7/02/08	500	2.31	1,155.00
7/05/08	600	2.15	1,290.00
7/10/08	400	2.54	1,016.00
7/14/08	800	2.41	1,928.00
7/16/08	700	2.25	1,575.00
7/22/08	500	2.33	1,165.00
7/25/08	300	2.01	603.00
7/29/08	900	2.47	2,223.00
7/30/08	400	2.12	848.00
7/31/08	200	2.33	466.00
Total	5,300		12,269.00

7/31/08 900

Valuation Under FIFO

200 @ 2.33 = 466.00

400 @ 2.12 = 848.00

300 @ 2.47 = 741.00

Total 900 = \$2,055

Valuation Under LIFO

500 @ 2.31 = 1,155.00

400 @ 2.15 = 860.00

Total = 900 = 2,015.00

Valuation Under Weighted Average

Weighted Average Price = $12,269 / 5,300$

WAP = 2.31

Total = $900 * 2.31 = 2,079$

Most Recent Price

900 @ 2.33 = 2,097

Specific Identification Method Valuation

Must be Told Which Deliveries Comprise Ending Inventory

Assume 300 From 7/25; 200 From 7/29; and 400 From 7/30

300 @ 2.01 = 603.00

200 @ 2.47 = 494.00

400 @ 2.12 = 848.00

Total = \$1,945

Retail Method

- Used in Department Stores
- Not Recommended for Hospitality
- Maintain Inventory at Cost and Retail
- Take Goods Available for Sale at Retail and Subtract Sales
- Multiply the Difference by the Ratio of Cost Price of Beginning Inventory Plus Purchases, Divided by the Retail Price of Beginning Inventory Plus Purchases

Gross Profit Method

- Assumes Gross Profit Percentage is Constant
- Not Recommended for Hospitality
- Add Beginning Inventory and Purchases to Get Goods Available for Sale
- Multiply Sales by Gross Profit Percentage to Get Cost of Goods Sold
- Subtract Cost of Goods Sold From Cost of Goods Available for Sale

Property, Equipment, and Other Assets

Property and Equipment

- Balance Sheet Items
- Some are Depreciated
- Some are not Depreciated
- Used to be Called "Fixed Assets"
- Hospitality Industry is "Fixed Asset Intensive"
- Capital Not Revenue Expenditures

Property and Equipment Classifications

- Land
- Buildings
- Leaseholds
- Leasehold Improvements
- Construction in Progress
- Furnishings and Equipment
- Special Consideration of Certain Property and Equipment
- Capital Leases

China, Glassware, Silver, and Linen

- The Ninth Edition of the Uniform System of Accounts for the Lodging Industry Recommended a Change in This Account – We are now in the 10th Edition
- Initial Inventory of China, Glassware, Silver and Linen, (the Balance Sheet Amount) Should be Written off as an Expense Over a Short Period of Time (3 Years)
- Replacements Are Expenses

Cost

- Property and Equipment is recorded at the Cost of Putting in Service
- Lasts Over One Year
- Do Not Include Service Contracts (Expense Item)

Capital Leases

- Called "Leased Asset Under Capital Lease"
- Recorded at Present Value of Future Lease Payments
- Strict Criteria as to Whether a Leased Asset is a Capital Lease (Balance Sheet) or an Operating Lease (Income Statement)
- Operating Lease is Revenue Expenditure

Buying a Business

- Lump Sum Payment for Land, Building, Furniture and Fixtures, Equipment, Goodwill
- Value of Each Individual Asset is Expressed as a Percent of the Total Cost
- Lump Sum Payment is Allocated to Each Group of Assets
- Different Depreciation Schedules

Book Depreciation

- Straight Line
- Units of Production
- Declining Balance
- Sum of the Years Digits

Straight Line Depreciation

- Cost Minus Salvage Value Divided by Number of Years of Life
- Same Amount Each Year

Units of Production

- Current Percentage of the Asset Used times the Cost of the Asset less its Salvage Value
- Rarely used in the Hospitality Industry
- Manufacturing Term
- Perhaps appropriate with vehicles

Declining Balance

- Up to twice the Straight Line Rate
- 100% divided by the number of years provides the straight line rate
- Straight line rate times a factor (up to 2) equals the depreciation rate.
- Depreciation rate remains constant and is multiplied by the net book value of the asset
- Salvage value is not considered

Sum of the Years Digits

- add all the years or use the formula
- $(n * (n + 1) / 2)$
- This is the denominator of the fraction
- Take the years in reverse order for the numerator
- Multiply the fraction by the cost minus the salvage value for each year's depreciation

Financial vs Tax Reporting

- Any of These Four Methods can be used for Financial Reporting
- Tax Reporting Must Follow the Accelerated Cost Recovery System
- Instituted in 1981 - Revised - 1986 MACRS
- Therefore, There is a Difference Between "Book Depreciation Expense" and "Tax Depreciation Expense"

Effect of Differences

- Net Result is a Difference in Before Tax "Book Income" and Before Tax "Taxable Income"
- Income Tax Expense is Computed on Before Tax "Book Income" and Before Tax "Taxable Income"
- Difference is in "Deferred Taxes" Account
- Should Eventually Even Out

Depreciation is Estimated

- Can Update Information (Salvage Value or Life) and Recalculate Over Remaining Life
- Can Sell, Trade or Dispose
- Asset and Contra Asset Need to be Closed
- Difference is Either Gain or Loss and is Treated as an Extraordinary Item on the Income Statement - Except Gains on Trade
- Trade Gains Reduce Cost of New Asset

Intangible Assets

- Long Lives - No Physical Substance
- Amortize (Straight Line) over the Shorter of 40 Years or the Benefit Period
- Franchises and Trademarks
- Patents and Copyrights
- Goodwill
- Leaseholds
- Leasehold Improvements

Other Assets

- Security Deposits for Utility Services
- Deferred Charges (Assets) - Not Prepaid Expenses (Which are for 1 Year) - Amortize Over Periods Benefited
- Preopening Expenses - The Ninth Edition of the Uniform System of Accounts for the Lodging Industry Now Recommends to Expense This Account in Current Year

Current Asset Management

Working Capital Components

- Current Assets Minus Current Liabilities Equals Working Capital
- Current Assets Divided by Current Liabilities Equals Current Ratio
- Current Ratio Should be 2 to 1

Cash Budgeting

- *Cash Receipts and Disbursements Approach*
 - Up to Six Months
 - Direct Sources/Uses of Cash
 - Based on Operations Budget
- *Adjusted Net Income Approach*
 - Periods Longer Than Six Months
 - Emphasizes External Sources
 - Uses an Indirect Approach

Inventory Management

- Consider Non-Product Costs – Storage, Insurance, Personnel
- Compute Inventory Turnover – Cost of Sales Divided by Average Inventory
- Retail Method of Inventory Valuation Can be Used in Clubs – Must Maintain Records of Cost and Retail
- Gross Profit Method – Assumes Constant Gross Profit

Cash

- Petty Cash Funds - Minor Purchases, Replenished Periodically by Amount Disbursed (Imprest Basis)
- Cash on Hand - House Banks and Undeposited Receipts
- Cash in Bank - Demand Deposits, Time Deposits, Certificates of Deposit
- Transaction Motive - The Maintenance of Minimum Cash Balances to Cover Checks Drawn
- Compensating Balances - Amount Required to Remain on Deposit Without Interest to Cover Bank Services
- Integrated Cash Management

Is Net Income Different From Cash Flows?

- *Net Income - Summarizes Revenues and Expenses*
 - Accrual Accounting
 - Non-Cash Revenue
 - Non-Cash Expenses
 - Ignores Transactions Related to LTD and Fixed Assets
- *Cash Flow - Analyzes Cash Account From Receipts and Disbursement*
 - Cash Account Only
 - Cash Basis Accounting
 - Includes All Cash Usages/Receipts

Cash Budgeting

- Most Information Is From the Operations Budget
- Cash/Credit Split
- Estimated Other Receipts
- Estimated Other Disbursements
- Receipt/Payment History

Other Cash Management

- *Float* - Time Between the Addition or Subtraction to a Company's Books and the Actual Addition or Subtraction (Disbursement Float and Collection Float)
- *Lockbox System* - Speeds the Flow of Cash Into the Bank's Account. Payments of A/R Go Directly to the Bank. There Is a Breakeven Point for This.
- Breakeven = Bank Charge Per Item Divided by the Daily Interest Rate Times the Change in Time
- *Working Capital* - Current Assets Less Current Liabilities
- *Trade Credit* - Suppliers Don't Charge Current Interest From Delivery to a Date.

Effective Interest Rate Calculation

- Annual Interest on a Loan Divided By Loan Amount Less Any Compensating Balance Requirement
- Interest = Principal X Rate X Time
- Effective Interest Rate Calculation
- Example: \$100,000 Loan at 10% Annual Interest With a \$10,000 Compensating Balance Requirement
- $I = \$100,000 \times 10\% \times 1 \text{ Year} = \$10,000$
- $EIR = \$10,000 / (\$100,000 - \$10,000)$
- $EIR = 11.1\%$

Purchase Discount

- *Effective Interest Rate* - Compute to Determine If It Is Advantageous to Take It
- Purchase Term Example - 2/10, N/30
- 2% Discount off the Invoice Price If Paid Within 10 Days, Otherwise the Balance Is Due Within 30 Days.
- Effective Interest Rate Equals Cash Discount Divided by the (Invoice Amount Less Cash Discount) Times Days in Year Divided by the Difference Between End of Discount Period and Final Due Date
- If Money Can Be Borrowed at Less Than the EIR - Take the Discount

Other Issues

- Manage Accounts Receivable by Using an Aging Schedule
- Current Assets is Financed by Current Liabilities – Imperative in Clubs to Collect Receivables From Members

Capital Budgeting

Types of Capital Budgeting Decisions

- To Meet Governmental Requirements
- To Reduce an Operating Cost
- To Increase Sales
- To Replace an Existing Fixed Asset
- Apply Cost/Benefit Test
- Prepared Into the Future
- Use Cash Budgets

Time Value of Money

- *A Sum of Money Today Is Worth More Than the Same Sum of Money a Year From Today.*
- $F = A * (1 + I)^n$
- F = Future Value
- A = Present Amount
- I = Interest Rate
- n = Interest Periods

Present Value of a Future Amount

- *What Is the Value Today of a Sum Due in the Future?*
- $P = F \times 1 / (1 + I)^n$
- F = Future Value
- P = Present Amount
- I = Interest Rate
- n = Interest Periods

Capital Budgeting Terms

- Annuity - Stream of Equal Receipts at Equal Intervals (the Lottery). Can Be Brought Back to Present Value.
- Discount Rate - Same As Interest Rate.
- Incremental Cash Flow - Change in the Cash Flow As a Result of the Investment.

Accounting Rate of Return Model

- Considers Average Annual Project Income, Not Cash Flow.
- $ARR = \text{Average Annual Income} / \text{Average Investment}$
- Average Investment Is the Cost Plus Salvage Value Divided by 2.
- Proposed Project Is Accepted If It Exceeds the Minimum ARR Required.

Payback Method

- Uses Annual Cash Flows From the Project Against the Project Cost to Determine When Investment Is Recovered.
- Formula If There Are Equal Cash Flows - Payback Equals Project Cost Divided by Annual Cash Flow
- Formula If There Are Unequal Cash Flows – Compute Payback By Subtracting Cash Flows From Cost to Get Time to Recover Investment

Payback and ARR Flaws

- Do Not Consider Time Value of Money
- ARR Uses Income Instead of Cash Flows
- Payback Does Not Consider Cash Flows After the Payback Period

Net Present Value Model

- Discounts Cash Flows to Their Present Values.
- NPV Is Computed by Subtracting the Project Cost From the PV of the Discounted Cash Flow Stream.
- Accept the Project If NPV Is Greater Than Zero.
- If Alternatives Projects Are Considered, Choose the One With the Highest NPV

Internal Rate of Return

- Considers Cash Flow and the Time Value of Money.
- Determines the Rate of Return Earned by a Proposed Project
- The Sum of the PV's Minus the Project Cost Is Set to Zero.
- The Discount Rate Is Then Computed.
- Project Is Accepted If the Computed Rate Is Greater Than the Hurdle Rate.

Mutually Exclusive Projects With Different Lives

- Assume Shorter Lived Project Is Followed by Another to Equal the Length of the Longer Project.
- Assume That the Longer Lived Project Is Disposed of at the End of the Short-lived Life.
- Ignore the Difference in Length of Lives.

Capital Rationing

- Limiting Funds for Capital Purposes.
- Competition for Available Dollars Exists.
- Lodging Chains Are Using NPV and IRR More Now.
- Prepare Thorough Analysis

Lease Accounting

Lease Accounting

- An Agreement Conveying the Right to Use Resources for Specified Purposes and Time
- Lessor Owns the Property and Conveys Right to Use
- Lessee Uses Property in Exchange for Periodic Payments

Advantages of Leases

- Conserves Working Capital
- Acquisition Requires Less Internal Processes
- Easy to Change Equipment and Update
- Tax Benefits - Pass Through Advantage of Lessors Tax Credits in the Form of Lower Rent
- Contracts Are Less Restrictive
- Not Shown on Balance Sheet - Improves Ratios
- May Acquire Without Capital Budgets

Disadvantages of Leasing

- Residual Value of Asset May Benefit Lessor
- Cost May Be Higher Than Purchase
- Lease Termination May Be Expensive

Provisions of Leases

- Term
- Purpose
- Rental Payment
- Renewal Options
- Obligations For Property Taxes, Insurance and Maintenance (Triple Net Leases)
- Inspection of Books
- Sublease
- Security Deposits
- Indemnity Provisions

Operating Leases

- Short Duration
- Lessor Retains Responsibility for Executory Costs (Property Taxes, Insurance, Maintenance)
- Easily Canceled
- Expensed on Income Statement

Capital Leases

- Long Duration
- Lessee Often Is Responsible for Executory Costs
- Non-Cancelable
- Capitalized on Balance Sheet

FASB Capitalization Criteria

- *If the Lease Meets Any One of the Following Criteria, It Must Be Treated As a Capitalized Lease - Not As an Operating Lease*
- Title Transfer Provision
- Bargain Purchase Provision
- Economic Life Provision - 75% Rule
- Value Recovery Provision - 90% NPV

Accounting for Operating Leases

- Simple Rental Agreement
- Debit Rent Expense and Credit Cash
- Accrual Accounting Rules Apply If Rent Is Paid in Advance
- If Pay in Advance Greater Than 12 Months - Treat As a Deferred Charge on the Balance Sheet

Accounting for Capital Leases

- Similar to the Purchase of a Fixed Asset
- Recognize Asset and Applicable Liabilities
- Asset Value Is the Net Present Value of Future Lease Payments - Excluding Executory Payments
- Use Lessee's Incremental Borrowing Rate or Lessor's Implicit Rate If Lower and Is Known

Other Lease Information

- Leasehold Improvements - Capital Improvements Made to Leased Space. Amortize Cost Over the Shorter of Life of Improvements or Life of Lease.
- Sale and Leaseback - Owner Sells Real Estate and Leases It Back From Investor. Raises Capital - Defer and Amortize Profit Over Life of Lease. Recognize Losses Immediately

Asset Turnover Ratio

- $\text{Revenue} / \text{Average Total Assets}$
- Capitalized Leases Increase Average Total Assets Reducing Asset Turnover Ratio

Return on Assets

- $\text{Net Income} / \text{Average Total Assets}$
- Capitalized Leases Increase Average Total Assets Reducing Return on Assets Ratio

Debt-Equity Ratio

- $\text{Total Debt} / \text{Total Equity}$
- Capitalizing Leases Result in Increasing Total Debt, Increasing the Debt-Equity Ratio

Number of Times Interest Earned Ratio

- $\text{Earnings Before Interest and Taxes} / \text{Interest Expense}$
- Capitalizing Leases Results in Increased Interest Expenses, reducing the Number of Times Interest Earned Ratio

Hospitality View

- May Prefer Not to Capitalize Leases
- Capitalized Leases Require Net Income to Increase to Maintain Constant Return on Assets
- Try to Negotiate Lease Agreements to Be Operating Leases

Part IV - Hospitality Tax and Law

Taxes

Tax Classifications of Clubs

- Member Owned – Organized Under Non-Profit Section 501(c)(7)
- Unrelated Business Income is Taxable
- Investor Owned – Taxable Profit Oriented Section 277

Tax Avoidance

- Planning Transaction to Minimize Tax Effects
- Nothing Improper
- Tax Evasion is Fraud and Illegal

Criteria for Tax Exemption

- Organization Must Be a Club
- Organized For Pleasure, Recreation or Other Nonprofit Activities
- Activities Must Be For Pleasure, Recreation or Other Nonprofit Activities
- Earnings Can't Benefit a Private Shareholder
- Can't Discriminate on Race, Color or Religion
- File Annual Return Form 990 Apply on Form 1024

Definition of Club

- Memberships of Individuals
- Personal Contacts
- Fellowship
- Commingling of Members

Americans With Disabilities Act Public Accommodations

Americans With Disabilities Act Public Accommodations

- Title III
- Effective January 26, 1992
- Covers Lodging Facilities Over Five Rooms
- Enforced By U.S. Attorney General or Private Lawsuit

Americans With Disabilities Act

- Employers May Not Discriminate Against an Individual With a Disability in Hiring or Promotion If the Person Is Qualified
- Employers Can Ask About Ability to Perform the Job
- Employers Cannot Ask If the Individual Has a Disability
- Employers Need to Provide Reasonable Accommodations to Disabled Individuals Such As Equipment Modification and Job Restructuring
- Employers Do Not Have to Incur Undo Hardships
- Cannot Discriminate Against Customers With Disabilities
- Auxiliary Aids and Services Must Be Provided to Individuals With Disabilities Unless an Undo Hardship Would Be Created
- Physical Barriers Must Be Removed

The Hotelkeeper and the Law of Contracts

Elements of a Contract - Agreement

- Offer and Acceptance
- Mistaken Offer
- Termination of Offer
- Counteroffer
- Consideration
- Legal Subject Matter
- Legal Capacity

Statute of Frauds

- Contracts Required to Be in Writing
 - Transfer of Real Property
 - Require Over One Year to Complete
 - To Answer for the Debts of Another
 - In Consideration of Marriage
 - To Personally Pay Debts of an Estate
 - Goods Over \$500
 - Plus Any Other State Specific Statutes

Voidable Contracts

- Between Adults and Minors
- Voidable on the Part of the Minor
- Ratification - When Become an Adult or for a Reasonable Time Thereafter
- Not Voidable If for Necessities

Contract Terms

- Executory - Contract That Has Not Been Performed
- Executed - Contract That Has Been Performed
- Express - Where Terms Are Openly Stated - Can Be Verbal or Written
- Implied - Contract Inferred by the Actions of the Parties
- Void Contract - a Contract That Lacks One or More of the Necessary Elements
- Valid Contract - a Contract Where All of the Elements Are Present
- Bilateral Contract - Promise Is Given in Exchange for a Promise (A Promises to Pay B If B Promises to Act and B Agrees)
- Unilateral Contract - Promise Is Given for an Act (A Promises to Pay B for an Act and B Says Nothing But Does the Act)

Statutes of Limitations

- Protect Persons From Suits After Witnesses Have Died, Evidence Lost, Claims Forgotten
- States Fix Time

Wage and Hour Laws Applicable to Hotel Employees

Fair Labor Standards Act

- Federal Statute
- Minimum Wage
- Overtime Pay
- Equal Pay
- Child Labor Laws
- Record Keeping

State Statutes

- If a State Has Statutes That Are More Beneficial to an Employee, Then the State Statute Would Take Precedence Over the Federal Statute.

What the FLSA Does Not Require

- Extra Pay For Work on a Particular Day
- Vacation Pay
- Holiday Pay
- Sick Pay
- Severance Pay
- Notice of a Discharge
- Granting of Days Off
- "Show Up" Pay
- Raises
- Benefits

Minimum Wage

- Effective July 24, 2009 \$7.25 Per Hour
- Tipped Employee Base Rate of \$2.13 Remains Frozen

Tip Credit

- Available to Regularly Tipped Employees
- Must Notify Employee
- Employee Must Keep All Tips
- Employee Must Earn (With Tips) the Minimum Wage
- Must Be in a Tipped Position Which Earns \$30 Month

Exceptions to FLSA

- Family Only Operations
- Seasonal - 6 Month Operation, or 1/3 of Sales Is From 6 Months
- Annual Sales Less than \$500,000

Employee Rights

- Can't Waive Rights Under FLSA
- If Work in Multiple Job Classifications with Different Rates of Pay, Overtime Is Computed at a Weighted Average Rate
- Overtime Is Time and One Half for All Hours Worked in Excess of 40
- Overtime Rate Is Computed Before the Tip Credit

Tip Vs Service Charge

- Tip Is a Sum Presented As a Gift or Gratuity for a Service Performed
- Service Charges Are Amounts Added to the Bill and Are Not Tips
- Service Charges Cannot Be Used to Reduce the Minimum Wage

Employee Declarations of Tips

- Form 4070-A by 10th of Month
- If Employee Earns More Than \$20 in Tips
- Employer Withholds Social Security Tax and Medicare Tax on Reported Tips
- Employee Rates 6.2% for Social Security on First \$106,800 of Wages and 1.45% on All Wages for Medicare (2009)

Tip Reporting Alternative Commitment (TRAC)

- Employers Agree to Educate Employees on Tips and Tip Reporting
- IRS Agrees Not to Bill Employers for Unreported Tips If Not Billing Employee

Tip Allocation

- Required If Total Tip Declarations Are Less Than 8% of Adjusted Sales
- Sales Are Adjusted for Take Out Service and Sales Where a Service Charge Was Included
- Required If Tipping Is Customary
- Employees Can Petition to Lower Allocation
- No Allocation to Employees Who Declared at Least 8%

Rest Periods

- The FLSA Does Not Require an Employer to Give an Employee a Rest Period.
- Rest Periods of 5 to 15 Minutes Are Common in the Industry. They Promote the Efficiency of Employees and Are Customarily Paid for As Working Time.
- Compensable Time for Rest Periods Cannot Be Offset Against Other Working Time.

Meal Periods

- Bona Fide Meal Periods During the Employee's Scheduled Work Day Are Not Work Time.
- The Employee Must Be Completely Removed From Duty.
- If Employees Meal Time Is Constantly Interrupted by Calls to Duty, Then Meal Periods Are Counted As Time Worked.

Other Tip Issues

- Credit Card Tips - The Employer May Reduce the Employee's Credit Card Tip by the Discount Rate That the Establishment Pays to the Credit Card Issuer.

Employer Provided Meals and Lodging

- Employee Must Voluntarily Accept in Lieu of Cash
- Employer Must Inform Employee of Credit
- Cannot Be Mandatory
- Employer Records Must Show Actual Use, Who Received Service, and the Employer's Cost
- Only Then Can a Credit Against Minimum Wage Be Taken

Uniform Maintenance

- Cannot Be Used As a Credit Against the Minimum Wage
- If Employer Requires but Does Not Maintain a Uniform, the Employer Must Pay One Hour at the Minimum Wage or the Actual Cost If Use of the Employer's Service Is Required.
- If the Uniform Is Wash and Wear, No Allowance Needs to Be Paid

Student Employees

- May Pay up to 6 Full Time Students 85% of the Minimum Wage If It Does Not Reduce Opportunities for Others
- Must Be Full Time Students
- Less Than 8 Hours a Day and Less Than 20 Hours a Week While in School
- Always Less Than 40 Hours a Week

Exempt Employees - Exempt From Overtime

- Executive - Directs 2 or More Employees; Less Than 40% in Non-exempt Work
- Administrative - Less Than 40% in Non-exempt Work; Exercises Discretion
- Professional
- Outside Sales People
- Salary And/or Title Does Not Mean Exempt

Overtime Computations

- Working in Multiple Job Classifications
- Cook - 30 Hours at \$10.00/hr = \$300.00
- Utility - 20 Hours at \$8.00/hr = \$160.00
- Prep - 10 Hours at \$7.00/hr = \$70.00
- Total Straight Time Earnings = \$530.00
- Weighted Average Hourly Rate = $530/60 = \$8.83$
- Overtime 20 Hours * .5 * 8.83 = \$88.30
- Total Earnings = \$530.00 (the Straight Time Piece) + \$88.30 (the Overtime Piece) = \$618.30 for the Week

Overtime for Tipped Employees

- Must Pay Time and One Half at the Minimum Wage
- NOT $\$2.13 \times 1.5$
- Should Be $\$6.55 \times 1.5$ - Tip Credit
- Tip Credit Is $\$6.55 - \$2.13 = \$4.42$
- Overtime Rate = $\$9.83 - \$4.42 = \$5.41$

The Family and Medical Leave Act

Provisions

- Effective August 5, 1993
- Unpaid leave Up to 12 Weeks
- Return to Same/Equivalent Job
- 50 or More Employees
- Employed 12 Months 1,250 Hours
- Top 10% of Salaried Employees Not Covered

The Leave

- Unpaid
- Maintain Health Benefits
- Family Leave
- Medical Leave
- If H/W Both Work Aggregate 12 Weeks

Laws Against Discrimination in Employment

Sex Discrimination

- Not Covered By Civil Rights Act of 1964
- 14th Amendment Protection

Equal Pay Act of 1963

Age Discrimination

- Age Discrimination in Employment Act of 1967
- 20 or More Employees
- Open 20 or More Weeks per Year
- Can't Discriminate Against Persons Over 40
- Bona Fide Occupational Qualification Exception
- Can Discriminate Below Age 40

Civil Rights Act of 1964

- Legal Foundation to Provide Equal Treatment for All.
- Unlawful to Hire, Fire, Pay, Offer Terms or Conditions, Serve, or Accept As Customers Based on Race, Color, Religion, or National Origin.

Private Club Exception From Civil Rights Act of 1964

- Membership Selective?
- Members Have Control?
- How Was the Membership Created?
- Are Formalities Involved?
- Comparison With Other Clubs (Dues/Fees)

Mrs. Murphy Tourist Homes

- Exempt From the Civil Rights Act of 1964
- Do Not Have to Accept All Who Apply
- Must Have Five or Less Rooms
- Must Be Owner Occupied

Remedies Under Federal Law for Violation of Civil Rights Act of 1964

- Injunctive Relief - Requires a Party to Refrain From Doing a Particular Act or Activity. This Guards Against Future Injuries. Damages Can Be Compensatory.
- Declaratory Relief - Expression of an Opinion Without Requiring Anything to Be Done.
- Civil Rights Act of 1991

Expanded Civil Rights Act of 1964

- Includes Sex and Disability

Sexual Harassment

- Unwelcome Sexual Advances, Requests for Sexual Favors and Other Verbal and Physical Conduct of a Sexual Nature Constitute Sexual Harassment When...
- Such Conduct Is Made Either Explicitly or Implicitly a Term or Condition of Employment or...
- Submission to or Rejection of Such Conduct by an Individual Is Used As the Basis for Employment Decisions Affecting Such Individual or...
- Such Conduct Has the Purpose or Effect of Unreasonably Interfering With an Individual's Work Performance or Creating an Intimidating, Hostile or Offensive Work Environment.

What Is Sexual Harassment?

- Insulting Sexual Comments
- Complimentary Sexual Looks or Gestures
- Insulting Sexual Looks or Gestures
- Non-Sexual Touching
- Expected Socializing Outside of Work With Job Consequences
- Expected Sexual Activity With Job Consequences

Federal Social Security, Unemployment Insurance, and Workers' Compensation

Independent Contractors

- Send 1099
- Send to SSA 1096 Detailing All 1099 Forms Mailed
- If Paid More Than \$600
- If Payee Is Not a Corporation
- Independent Contractors Must Provide Company With a W-9

Federal Unemployment Tax Act

- Employer Only Tax
- File Annually
- Rate Is 6.2% of First \$7,000 of Taxable Wages
- Can Get Credit of up to 5.4% for Payments to a State Unemployment Insurance

Other Issues

- Circular E Details Payments
- Withholding Taxes Must Be Deposited
- Employer Pays Equal Share of FICA and Medicare Tax
- Quarterly Reports on Withholding Taxes Must Be Filed

Workers' Compensation

- Compensation for Work Related Injuries
- Private Insurance Fund or State Insurance Fund
- Self-insured Requires a Significant Security Deposit
- Formulas for Losses
- Payout Is Tax Free

Federal Income Tax: Withholding and Reporting Requirements

Federal Withholding Taxes

- Need to Withhold From Employee Wages in a Specific Order
- Exclusive of Tips (All Taxes)
- Tip Income (All Taxes)
- Lastly, Any Other Deductions
- If There Is Not Enough Gross Income in One Paycheck, It Can Come From Future

Forms

- W-4 Is Used by Employee to Communicate to Employer Level of Deductions
- W-2 Is Sent to Employee by January 31st of Next Year Detailing All Income and Deductions
- Employer Files a W-3 and W-2 by February 28th

Part V - Hospitality Operations

Accounting for Payroll Related Liabilities

Payroll Control

- Authorization of Employment and Establishment of Wage Rates
- Reporting Hours Worked
- Preparation of the Payroll
- Signing of Payroll Checks
- Distribution of Payroll Checks
- Reconciliation of Payroll Bank Account
- Segregation of Duties
- Do Not Have the Same Person do More Than One Function if Possible
- Human Resources Adds/Deletes
- Time Clocks
- Do Not Pay in Cash
- Check Payroll Sheets and Paychecks
- Distribute Checks by Independent Person
- Return Unclaimed Checks to Controller

Payroll Records

- Master File of Employee Information
- W-4 Directs Tax Withholding
- Payroll Journal Lists Each Check's Gross Amount and All Deductions
- W-2 Summarizes Information Annually

Recording Payroll

- Gross Pay (Regular, Overtime, Tips)
- Value of Meals/Lodging
- Federal Withholding Taxes
- Social Security (FICA)
- Medicare Tax
- State Income Tax Withholdings
- Local Taxes, Employee Contribution to Health Care, Union Dues etc.
- Net Pay

Journal Entry to Record Payroll

- Debit Salaries for Earnings
- Credit All the Taxes and Salaries Payable (Net Pay) to Establish Liabilities
- Debit Salaries Payable and Credit Cash when Payroll is Paid for Net Pay

Recording Payroll Taxes

- Taxes Paid by Employer Based on Employees Wages
- FICA and Medicare Contributions
- FUTA and SUTA (Unemployment)
- Debit Payroll Tax Expense and Credit the Various Taxes Payable

Employee Status

- Question as to Whether an Employee or Independent Contractor
 - Common Law Employee Test
 - 20 Factor Test
- Can Tell "What to Do" But Not "How to Do" For Independents
- IRS Ruling 87-41 Developed a Factor List to Help

Ratio Analysis

Ratio Analysis

- *Compare Against Something*
 - Prior Period
 - Industry Standard
 - Budget
 - Ratio Analysis
- *Express in a Number of Ways*
 - Percentage
 - Per Unit Basis
 - Turnover
 - Coverage

Classes of Ratios

- Liquidity- Ability to Meet Short Term Obligations
- Solvency - Extent to Which the Enterprise Has Been Financed
- Activity (Turnover)- Ability to Use the Property's Assets
- Classes of Ratios
- Profitability - Measurement of Management's Overall Effectiveness
- Operating - Analysis of Hospitality Establishment Operations

Basic Rule

- When Computing a Ratio (Which Is Just a Mechanical Operation Using Two Numbers) and One of the Numbers Comes From the Balance Sheet and the Other Number Comes From the Income Statement or the Statement of Cash Flows...
- ...The Balance Sheet Number Is an Average of the Balance Sheet at the First Day of the Period and the Last Day of the Period Which Is Represented by the Income Statement or Statement of Cash Flows.
- For Our Purposes We Will Use This Simple Two Point Average.
- A More Accurate Representation Would Be to Use an "Average of Averages" From the Balance Sheet.

Liquidity Ratios

- Current Ratio
- Acid Test or Quick Ratio
- Operating Cash Flows to Current Liabilities
- Accounts Receivable Turnover
- Average Collection Period
- Working Capital Turnover

Solvency Ratios

- Solvency- Total Assets to Total Liabilities and Total Liabilities to Total Assets
- Debt-Equity
- Long Term Debt to Total Capitalization
- Number of Times Interest Earned
- Fixed Charge Coverage
- Operating Cash Flows to Total Liabilities

Activity Ratios (Turnover Ratios)

- Inventory Turnover
- Working Capital Turnover
- Property and Equipment Turnover
- Asset Turnover
- Paid Occupancy Percentage
- Complimentary Occupancy
- Average Occupancy Per Room
- Multiple Occupancy

Profitability Ratios

- Profit Margin
- Operating Efficiency Ratio
- Return on Assets
- Gross Return on Assets
- Return on Owner's Equity
- Return on Common Stockholder's Equity
- Earnings Per Share
- Price Earnings Ratio

Operating Ratios

- Mix of Sales
- Average Room Rate
- Revenue Per Available Room
- Average Food Service Check
- Food Cost Percentage
- Beverage Cost Percentage
- Labor Cost Percentage
- Revenue Per Seat Available

Limitations of Ratio Analysis

- Do Not Resolve Problems
- Only Indicate That There May Be a Problem
- Comparisons Must Be From Related Numbers
- Most Useful When Compared to a Standard
- When Comparing to Other Businesses - Must Be Comparable
- Uses Historical Data - May Not Tell the Whole Story
- Does Not Address Leases

Operations Budgeting

Budget

- A Management Plan Covering All Phases of Operations for a Definite Period in the Future.
- It Is a Formal Expression of the Plans, Objectives, and Goals Established by Management.

Types of Budgets

- Long Term and Short Term
- Capital Budgets
- Cash Budgets
- Operating Budget
- Departmental Budget
- Master Budget
- Fixed Budget
- Flexible Budget

Benefits of Budgeting

- Forces Management to Examine Alternatives Prior to a Course of Action
- Compels Management to Examine Facts
- Provides a Standard for Comparison
- Allows Management to Prepare for Future
- Measures Progress and Self Evaluation
- Objectives Are Clear
- Management Is Participatory
- Aids in Pricing

Disadvantages of Budgeting

- Time and Cost
- Unknown Factors
- Breaching Confidentiality
- Spending Because "Available"

Budget Cycle

- Establish Realistic Goals
- Planning
- Comparing
- Corrective Action
- Improvement
- Establish Financial Objectives
- Forecast Revenues
- Estimate Expenses
- Forecast Net Income
- Budget Cycle
- If the Board Accepts the Budget, the Process Is Complete. If It Does Not, Another Budget Is Developed and Proposed.

Issues in Budgeting

- Who Is Responsible for Budgeting?
- Incremental Budgeting
- Zero-Based Budgeting
- Budgeting in a New Operation
- Issues in Budgeting

Budgetary Control

- Determine Variances
- Identify Significant Variances
- Analyze Significant Variances
- Identify Problems
- Correct Problems

Variance Analysis - Sales

- Volume Variance
- Price Variance
- Price-Volume Variance

$$VV = BP * (AV - BV)$$

$$PV = BV * (AP - BP)$$

$$P-VV = (AP - BP) * (AV - BV)$$

Variance Analysis - Cost of Goods Sold

- Cost Variance
- Volume Variance
- Cost-Volume Variance

$$CV = BV * (BC - AC)$$

$$VV = BC * (BV - AV)$$

$$C-VV = (BC - AC) * (BV - AV)$$

Variance Analysis - Variable Labor

- Volume Variance
- Rate Variance
- Efficiency Variance
- Rate-Time Variance

$$VV = BR * (BT - ATAO)$$

$$RV = BT * (BR - AR)$$

$$EV = BR * (ATAO - AT)$$

$$R-TV = (BT - AT) * (BR - AR)$$

Antitrust Laws and Hotels

Purpose of Antitrust Laws

- Preserve Competition
- Prevent Economic Coercion
- Between Competitors "Horizontal"
- Between Operator and Suppliers/Customers "Vertical"

Major Statutes

- Sherman Act of 1890
 - Restraint of Trade in Contracts
- Clayton Act of 1914
 - Robinson-Patman Act of 1936
- Celler-Kefauver Amendment of 1950
 - Can't Create Monopoly
- Federal Trade Commission Act of 1914
 - Enjoin Unfair Methods of Competition

Penalties for Violation

- Section 1 or 2 of Sherman Act is a Felony
- 3 Years Jail
- Fine of \$350,000
- Injunction
- Equitable Relief

Understanding Franchising

Franchising

- Conveying Right to Operate Business in a Like Manner
- Franchisee is an Independent Business Person
- Franchisor Does Not Guarantee Success
- Franchisor Does Not Have a Investment in the Individual Property
- First Example - 1907 Caesar Ritz Allowed Name to be Used on Hotels in New York, Montreal, Boston, Lisbon, and Barcelona

Uniform Franchise Offering Circular

- Required by Federal Trade Commission
- Must Provide to All Possible Franchisees at First Meeting
- Discloses Many Pieces of Information About the Franchise

Parts of the Uniform Franchise Offering Circular

- Description of Franchisor
- Identification of Major Players
- Litigation History
- Bankruptcy History
- Initial Fees
- Other Fees
- Franchisee's Estimated Annual Expenses
- Obligations on Where to Purchase
- Obligations to Use Specifications
- Financing Arrangements
- Obligations of Franchisor
- Exclusive Rights or Territories
- Contracts
- Financial Statements

Services Offered By Franchisors

- Site Selection and Market Analysis
- Provision of Plans and Specifications
- Development Assistance
- Publicity and Promotion Assistance
- Centralized Purchasing
- Referrals Between Properties
- Centralized Reservation System
- Proven Modes of Operation
- Marketing Offices
- Property Inspection/Evaluation
- Franchise Agreements
- Term - 10 to 20 Years
- Provide Proprietary Information
- Training and Guidance
- Franchise (Royalty) Fees
- Reservation Fees
- Initial Application Fee
- More on Fees
- Initial Fee - Flat Amount Plus Amount per Room
- Usually Advertising and Reservation Fees Just Cover the Cost
- Royalty Fee is For Use of Name
- Continuing Fee Assessment - %

What Does a Franchise Really Cost?

- Chains That Are Referral Organizations are the Lowest and Are Less Than 2% of Rooms Revenue
- First Class Full Service Hotels Such as Marriott May be as High as 9% of Rooms Revenue

The Hotel's Duty to Receive Guests and Its Right to Refuse Guests

Hotel Has A Duty To Receive Guests

- Engaged in Public Employment
- Take in All Travelers Who Apply
- 24 Hour Operation - Even When Hotel Is "Closed"
- Provides Interstate Service
- Subject to Federal Statutes - Civil Rights Act of 1964

Civil Rights Act of 1964

- Legal Foundation to Provide Equal Treatment for All.
- Unlawful to Hire, Fire, Pay, Offer Terms or Conditions, Serve, or Accept As Customers Based on Race, Color, Religion, or National Origin.

Advertising

- Cannot Advertise in a Discriminating Way
- Cannot Imply That Certain People Are Not Welcome

Private Club Exception From Civil Rights Act of 1964

- Membership Selective?
- Members Have Control?
- How Was the Membership Created?
- Are Formalities Involved?
- Comparison With Other Clubs (Dues/Fees)

Mrs. Murphy Tourist Homes

- Exempt From the Civil Rights Act of 1964
- Do Not Have to Accept All Who Apply
- Must Have Five or Less Rooms
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Remedies Under Federal Law for Violation of Civil Rights Act of 1964

- Injunctive Relief - Requires a Party to Refrain From Doing a Particular Act or Activity. This Guards Against Future Injuries. Damages Can Be Compensatory.
- Remedies Under Federal Law for Violation of Civil Rights Act of 1964
- Declaratory Relief - Expression of an Opinion Without Requiring Anything to Be Done.

Hotel Has a Right to Refuse Guests

- Drunk or Disorderly
- Contagious Disease
- Bringing in Unallowable Objects
- Unable or Unwilling to Pay
- No Accommodations

Minors in a Hotel

- Cannot Make a Binding Contract
- Must Accept for Necessaries
- What Is a Necessity?

State Civil Rights Laws

- States May Have Other Categories of Persons Protected.
- Examples - Sex, Marital Status, Disabilities, Age

Guest Reservations

Agreement for a Room Is a Contract

- Specific Price
- Specific Period of Time
- Both Hotel and Guest May Sue for Breach of Contract - Hotel Could Not Rent the Room - Guest Hotel Failed to Provide Accommodations

Remedies for Breach of Reservation Contract

- Hotel - Charge for "No Show"
- Price of the Room Less the Variable Costs
- (Unless Able to Rent Room Out)
- Guest - Difference Between the Contract Price and What Was Charged Elsewhere
- Remedies for Breach of Reservation Contract
- Guest Is Also Entitled to Travel and Other Inconveniences
- "Sleeping Giant" - Emotional Distress and Discomfort

Can Hotels Recover Profits From Other Services From No Shows?

- No
- The Courts Have Consistently Ruled That Hotels Cannot Recover Lost Profits From No Shows Who Might Have Used Other Services in the Hotel During Their Stay

Minimum Stays

- Acceptable to Have a Minimum Stay
- If Guest Leaves and Hotel Upheld Its Part of the Bargain Then No Refund for the Guest

The Guest's Right to Privacy

Guest's Right to Privacy

- Fourth Amendment - Guarantees a Person's Right to Privacy
- No Unauthorized Persons Are Allowed to Enter a Guestroom.
- Innkeeper May Enter for Routine Housekeeping and Emergency Repairs

Search Warrants

- Need a Search Warrant If the Room Is Paid for (Presentation of a Credit Card Means That It Is Paid)
- Do Not Need a Search Warrant If the Room Is Not Paid for (Unauthorized Overstays May Be an Example)

Front Office Tips

- Never Announce a Guest's Room Number So That Others May Hear
- Do Not Give Out Room Keys to Persons Who Are Not Registered Guests in the Particular Room
- Do Not Provide Room Numbers to Inquiring Parties

The Hotel's Right to Evict a Guest, Tenant, Restaurant Patron, or Others

Guest or Tenant

- Tenants Have the Exclusive Legal Right to Possess and Occupy the Premises.
- Guests Have a Right to Use the Premises and the Landlord Retains Control
- Evicting a Guest Is Easier Than Evicting a Tenant

Evicting a Tenant

- Breach of One of the Covenants in the Lease
- Lease Is Terminated
- Go to Court for a Dispossession Hearing
- Remember - A Guest Can Be Evicted Without Court Proceedings

When a Hotel Can Evict a Guest

- Violation of Hotel regulation
- Non-Payment
- Refusal of Service Because of an Unpaid Bill
- Illness With Contagious Disease
- Overstays

Improper Evictions - Can Lead to Punitive Damages

- Wrongful Act
- Intentionally Performed
- Gross Disregard for Rights
- Willfulness

Telephone Service and Resale Rights

Resale of Service

- October 21, 1980 FCC Allowed Resale of Interstate Telephone Service
- August 6, 1982 FCC Allowed Resale of International Telephone Service
- No Tariffs Needed to Be Filed

Telephone Operator Consumer Act of 1990

- Post Near Each Telephone
 - Provider of Operator Services and Toll Free Number
 - Rates Available on Request
 - Guest Has Right to Access Carrier of Choice
 - Contact Information For FCC
- States May Require More

Other Telephone Issues

- Intrastate Regulated By State Public Service Commissions
- Can Purchase and Operate Coin Telephones
- Establishments With More Than 20 Employees Must Have Hearing Aid Compatible Telephones Available

Copyright Laws for Music, Television, Video, and Movies

General Rule

- Owner of a Copyrighted Music Composition has the Exclusive Right to Print, Reprint, Publish, Copy and Sell the Work. Can Control Public Performances of the Work.
- Must Have a License Agreement to Play Music

Copyright Associations

- ASCAP
- BMI
- SESAC

Exemptions Under Copyright Law of 1976

- Private Homes
- Small Establishments Using Home Type Appliances

Cable Television

- Can't Unscramble
- Protected by the Communications Act of 1934
- Satellite Antennae May Not Be Used for Private Gain
- Can Rent Videos to Guests to View in Their Rooms