

# Hospitality Industry Accounting

## CHAPTER OUTLINE

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## Overview

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Hospitality is one of the world's most exciting and rewarding industries. When you choose it for your career, you will be able to choose from a wide variety of employers, locations, and daily job activities that can lead to your professional success and personal satisfaction. In this chapter, you will review some important ways in which the hospitality industry is unique. You will also learn the definition of accounting and how accounting helps managers like you use financial information to make good decisions. As you learn that there are several specialty areas (called branches) within accounting, it will be clear to you why knowing about hospitality managerial accounting, the specialty area of accounting examined in this text, will help you improve the operating effectiveness of any restaurant, hotel, club, bar, or institutional facility you manage. Finally, you will learn about some of the important ethical responsibilities you will assume when you apply managerial accounting principles to the hospitality operations you are responsible for managing.

## Unique Aspects of the Hospitality Industry

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Learning Outcome 1: Describe the primary purpose of accounting in the hospitality industry.

If you are reading this book for a class, to improve your business skills, or simply to better understand managerial accounting, you probably are familiar with the term hospitality. **Hospitality** can be defined as the friendly and charitable reception and entertainment of guests or strangers. Hospitality also refers to a specific segment of the **travel and tourism industry**.

The question of precisely which specific businesses should, or should not, be included as part of the hospitality segment of the travel and tourism industry is subject to honest difference of opinion and diverse perspective. As a result, the colleges and universities that offer educational programs preparing students for careers in the hospitality

**LEARNING OUTCOMES**

At the conclusion of this chapter, you will be able to:

- Describe the primary purpose of accounting in the hospitality industry.
- List and summarize the purpose of each of the five branches of accounting.
- Explain why managerial accounting in the hospitality industry is different from managerial accounting used in other industries.
- Identify the specific Uniform Systems of Accounts appropriate for the hospitality business you manage.
- Summarize your ethical responsibilities as a managerial accountant in the hospitality industry.

industry may elect to call the programs Hospitality Management, Culinary Arts Management, Hotel and Restaurant Management, Travel and Tourism Management, Restaurant Management, Hotel Management, Institutional Management, or any of a number of similar name variations. The difficulty with precisely classifying who is, or is not, a member of the hospitality industry becomes clearer when you realize that for most industry observers, each of the 10 following individuals would be considered professional hospitality managers:

Hospitality Manager	Job Title
Sofianna	Director of food services for a 5000-student public school district
Alberto	Managing Director of a 750-room resort hotel
Samantha	Regional manager of a 500-unit Quick Service Restaurant (QSR) chain with responsibility for the 30 units in her assigned territory
Carl	General manager of a 75-room limited service, all-suite hotel near a city's airport
Bethie	Manager of a 800-member country club offering dining services, swimming pool, and an 18-hole golf course
Trahill	Director of sales and marketing for a 2000-room casino hotel
Jackson	Food and beverage director for the Student Union of a 30,000-student university
Amanda	Dietary services director at a 500-bed hospital
Nuntima	Front office manager at a 350-room full-service hotel
Eddie	Chef/owner of "Chez Edward," an exclusive and upscale 60-seat restaurant emphasizing locally sourced ingredients

**Fun on the Web!**

According to the U.S. Commerce department, more than 25 subsectors make up the travel and tourism industry. The three sectors of accommodations, lodging, food service, and air travel, account for more than 50% of the industry's total sales. Accommodations is the largest of the three subsectors and accounts for 19% of total travel industry output. Food services is the second largest and accounts for more

than 16% of travel and tourism-related output, while air travel accounts for nearly 16%. To learn more about the size and economic impact of the travel and tourism industry, go to

<http://selectusa.commerce.gov/industry-snapshots>

When you arrive at the site, choose "Travel, Tourism and Hospitality."

While each of the industry subsegments these managers work in is very different and can be classified in very different ways (e.g., profit vs. nonprofit, or corporate vs. privately owned), one good way to classify them is by their emphasis on either lodging accommodations or food and beverage (F&B) services.

The authors not only recognize the potential over simplification of such a classification but also believe that it is the act of providing away-from-home lodging and meals (in a variety of settings), which most distinguishes those considered to be working in the hospitality industry.

When hospitality is defined as the lodging and food services industries, it can include a variety of managers in related fields. These fields include clubs, resorts, casinos, cruise ships, theme parks; the recreation and leisure market such as arenas, stadiums, amphitheaters, civic centers, and other recreational facilities; the convention center market; the education market such as colleges, universities, and elementary and secondary school nutrition programs; the business dining market such as corporate cafeterias, office complexes, and manufacturing plants; the healthcare market such as long-term care facilities and hospitals; and the corrections market such as juvenile detention centers, jails, and prisons.

When all of the different segments of the hospitality industry are included, it is easy to see that there are literally hundreds of specialized management positions available. The number of opportunities offered by the hospitality industry is significant, as are the opportunities for those managers who understand and can utilize their hospitality accounting skills.

With such a diverse hospitality management audience, the challenge of creating a “hospitality managerial accounting” text such as this one is daunting. But as you will discover as you read this book, the authors have created a managerial accounting text that can be of maximum help to the widest possible range of hospitality managers.

## The Purpose of Accounting in the Hospitality Industry

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Some hospitality students believe that learning accounting is very difficult. *It will not be difficult for you.* The term accounting originated from an old Middle French word (*acompter*), which itself originated from Latin (*ad + compter*) meaning “to count.” As a result, you already have years of experience as an accountant (a counter)! A more detailed definition of **accounting** would be the process of recording financial transactions, summarizing them, and then accurately reporting them. As a result, a good definition for an **accountant** is simply a person skilled in the recording and reporting of financial transactions.

Just as you learned in elementary school about the rule that says  $2 + 2$  always equals 4, accountants in business have developed their own specialized rules and procedures that govern counting, recording, and summarizing financial transactions as well as analyzing and reporting them. This book will explain many of the accounting rules and procedures that are frequently utilized by professional hospitality managers.

In the business world, as well as in many other fields, accounting is used to report (account for) an organization’s money and other valuable property. Accounting is utilized by all managers in business and especially by those in the hospitality industry. In fact, in almost every hospitality job, accounting is important. Accounting in the hospitality industry is utilized every time a guest purchases food, beverages, or a hotel guest room.

Accounting in business occurs even before a hospitality facility ever opens. This is so because businesspersons estimate their costs before they decide to build their facilities and often seek loans from banks to help them. Those banks will assuredly want to know about the proposed business’s estimated financial performance before they decide to lend it money.

Accurate accounting is important to many other individuals in the hospitality industry. The owners of a restaurant or hotel will certainly want to monitor their business's financial condition. These owners may be one or more individuals, partnerships, or small or very large corporations, but they all care about the performance of their investments. Investors in the hospitality industry generally want to put their money in businesses that will conserve or increase their wealth. To monitor whether their investments are good ones, investors will always seek out and rely upon accurate financial information. When it is done properly, the accounting process provides that important information.

Accounting is actually quite a large field of study. To understand why accounting plays such a significant role in business, consider just a few examples of the type of basic and important questions the discipline of accounting can readily answer for hospitality managers:

1. What was the total sales level achieved by our business last month?
2. What was our most popular menu item? What was our least popular one?
3. What was the average selling price of our hotel rooms last week? Was it higher or lower than our competitors?
4. Are we more or less profitable this month than last month?
5. What is our company realistically worth if we were to sell it today?

The above are just a few of the many questions hospitality managers can utilize accounting to answer; however, it is important to understand that accounting is not the same as management.

Accounting is a tool used by good managers. To understand why you, as a talented hospitality manager, will play a more important decision-making role in your business than will the field of accounting, consider these examples of the type of questions that *cannot* be best answered by using accounting information alone.

1. Should I select Jackie or Samuel as the person assigned to train our new dining room wait staff?
2. Should the portion size of fish used to make our signature "Blackened Trout" be 8 ounces or 11 ounces?
3. Would our country club members prefer to have an increase in the number of inexpensive or of higher-quality (but more costly) wines when we create the club's new wine list?
4. Our hotel swimming pool currently closes at 10:00 p.m. Would our guests be happier if the pool were to remain open 24 hours per day instead? Would that increase the number of times they returned to stay with us? By how many?
5. Would our new 500-room resort be more successful if it were built in Punta Cana in the Dominican Republic, or is the future of the Riviera Maya near the city of Tulum in Mexico likely to become, in the long term, a more profitable tourist destination for us?

Notice that in each of these questions, the best decision requires that you utilize your own experience and judgment of what is "right" for your guests, your business, your employees, and yourself.

As a result, while accounting alone could not make the decisions called for in the questions above, when properly used, it can help you make *better* decisions about these types of issues than those that would be made by managers who do not understand how accounting could help them. The purpose of this book is to teach you how to use accounting techniques as well as your own education, experience, values, and goals to make the very best management decisions possible for yourself and the businesses you are responsible for managing.

# Branches of Accounting

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Learning Outcome 2: List and summarize the purpose of each of the five branches of accounting.

Proper accounting includes both recording financial information and also accurately reporting it. Some accountants are skilled at one or both of these processes. Most of those who work as accountants recognize that there are actually very specialized fields or branches of accounting. While some of these branches do overlap, they include

- Financial accounting
- Cost accounting
- Tax accounting
- Auditing
- Managerial accounting

Most hospitality managers are not accountants, but the function of the accounting work performed in each of these branches is important for them to understand.

## Financial Accounting

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In nearly all cases, a business essentially consists of the buying and selling of goods and/or services. In the hospitality industry, the items sold by businesses are typically food, beverages, and hotel rooms. Depending upon the specific area within hospitality, however, a wide variety of other products and items such as spa services or activities like golf, gaming, and entertainment may be sold to guests.

Business accountants who specialize in **financial accounting** are skilled at recording, summarizing, and reporting financial transactions. Financial transactions include **revenue**; the term used to indicate the money you take in when your business makes a sale, **expense**; the cost of the items required to operate your business; and **profit**, the amount of money that remains after all your expenses have been paid.

These transactions can be used to develop the following profit-producing formula:

$$\text{Revenue} - \text{Expenses} = \text{Profit}$$

Financial accounting also includes accounting for **assets**, which are the items owned by a business, and **liabilities**, the amounts the business owes to others. Finally, financial accountants record and report information about **owners' equity**, the amount remaining in a business after subtracting its liabilities from its assets.

These transactions can be used to develop the following equation, which is so important and is known as the basic **accounting equation**, or the balance sheet equation (see Chapter 4).

$$\text{Assets} = \text{Liabilities} + \text{Owners' equity}$$

In this book, you will discover that the work of financial accountants can be extremely helpful to professional hospitality managers, and as a result, in later chapters, we will examine, in detail, how these accountants do some of the important parts of their jobs.

To better understand how financial accounting can help hospitality managers, consider the case of Faye Richards. She is interested in buying her own small pizza shop. The shop would be located in a strip shopping center and would sell primarily

pizzas, hot subs, and soft drinks. Some of the many financial considerations Faye would have as she tries to determine whether buying and operating the shop is a good idea would be

1. How much revenue do pizza shops like this typically achieve on an average day? An average month?
2. What do pizza shops normally spend to properly staff their stores?
3. How much should I spend on the equipment I need to buy to make the food I will sell?
4. Given the size and location of my store, what is a reasonable price to expect to pay for obtaining insurance for my business?
5. How much money am I likely to make for myself during the first year I own the store? How much in future years?

Faye can get important information from her financial accountant, but she will also need managerial skills and her own intuition and talents to provide answers to these and other business questions she must address.

## Cost Accounting

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**Cost accounting** is the branch of accounting that is concerned with classifying, recording, and reporting a business's expenses or costs. Because all businesses seek to control their costs and not waste money, those who operate businesses are very concerned about where they spend their money. For cost accountants, a **cost** or expense is most often defined as "the time or resources expended by a business."

To better understand why cost accounting is so important, consider Mike Edgar, the manager of a private country club. Reporting to Mike, among others, are those individuals responsible for the operation of the club's golf course, pro shop, swimming pools, and F&B services. Each of these major areas will expend money to achieve the goals set for them by Mike and the club's members.

It is very unlikely that that Mike could know, on a daily basis, about all the purchases his staff will make. Mike will, however, be responsible to the club's members for the money they have spent. Because this is true, it will be important for Mike to have a reliable system in place that allows him to fully understand what has been purchased, who purchased it, and the reason for the purchase.

Cost accountants determine costs by departments, business function or area of responsibility, and the products and services sold by the business. They create systems to classify costs and report them in ways that are most useful to those who need to know about how a business spends its money.

Some of the kinds of questions that cost accountants could help Mike answer include the following:

1. How much does it cost the club to host one member who is playing golf?
2. What were the total costs of utilities (water, electricity, and natural gas) incurred by the country club last month?
3. Did it cost more this year to fertilize the golf course than it did last year?
4. Are all country club managers accounting for the cost of the meals eaten during work hours by their departmental staff in the same manner?
5. Does it cost more money to operate our country club than other clubs of the same size and type?

The work of cost accountants is critical for hospitality managers who seek to fully understand the costs of operating their businesses. As a result, throughout this text, we will utilize many of the techniques that have been developed by these accounting specialists.

## Fun on the Web!

The control of costs is important to every business and especially so in the restaurant business. Professionals working in the F&B industry have a variety of tools available to them to help manage their costs. One of the very best is the textbook *Food and Beverage Cost Control* written by the same author team that produced this book.

You can review the table of contents of this extremely popular book by going to

[www.wiley.com](http://www.wiley.com)

When you arrive at the Wiley website, select “Culinary & Hospitality” and then choose “Accounting” to select and examine this book’s most recent edition.

## Tax Accounting

A tax is simply a charge levied by a governmental unit on income, consumption, wealth, or other basis. In the United States, governmental units that can assess taxes include townships, cities, counties, states, and various agencies of the federal government. Nearly all businesses are subject to paying some taxes.

**Tax accounting** is the branch of accounting that concerns itself with the proper and timely filing of tax payments, forms, or other required documents with the governmental units that assess taxes. Professional tax accounting techniques and practices ensure that businesses properly fulfill their legitimate tax obligations.

In the hospitality industry, managers are required to implement systems that will carefully record any taxes that will be owed by their businesses. Consider, for example, Latisha Brown, the general manager of a 220-room full-service hotel located in her state’s capital and very near the airport. The work of tax accountants could help Latisha ensure that she has the systems in place to

1. Record the **occupancy tax** her hotel must pay. This tax, which is the money paid to a local taxing authority based upon the amount of revenue a hotel achieves when selling its guest rooms, is typically due and payable each month for the room revenue the hotel achieved in the prior month.
2. Maintain records of the total taxable revenue achieved by the hotel and collect all money required to pay the state or local **sales tax** that will be due as a result of realizing those sales.
3. Address specific tax-related questions such as, “Is the hotel required to collect and pay occupancy tax on those guests who were assessed a no-show charge because they failed to arrive at the hotel when they had a confirmed reservation?”
4. Monitor changing laws to ensure that all **payroll tax** due on those individuals employed by Latisha are properly recorded and submitted.

As you can see from these very few examples, the work of tax accountants is critically important to hospitality managers. Throughout this text, we will often examine how the specific actions taken by hospitality managers will affect the amount of taxes that must be paid by the businesses they manage.

## Auditing

An **audit** is an independent verification of financial records. An **auditor** is an individual or group of individuals that completes the verification. As you have seen, the accurate reporting of financial transactions is important to many different entities

## Fun on the Web!

The 2002 SOX became law to help rebuild public confidence in the way corporate America governs its business activities. The act has far-reaching implications for the tourism, hospitality, and leisure industry. To examine an overview of its provisions, go to

[www.sec.gov/about/laws.shtml](http://www.sec.gov/about/laws.shtml)

When you arrive at the site, choose "Sarbanes–Oxley Act of 2002."

including managers, owners, investors, and taxing authorities. The auditing branch of accounting is chiefly concerned with the accuracy and truthfulness of financial reports. It is also concerned with safeguarding the assets of a business from those unscrupulous individuals who would seek to defraud or otherwise take unfair advantage of it. Properly performed, the auditing branch of accounting is designed to point out accounting weaknesses and irregularities and thus help prevent accounting fraud.

In part because of the potential damage that could be done by unscrupulous corporate managers, the U.S. Congress passed the **Sarbanes–Oxley Act (SOX)**. Technically known as the Public Company Accounting Reform and Investor Protection Act, the law provides criminal penalties for those who are found to have committed accounting fraud. Sarbanes–Oxley covers a whole range of corporate governance issues including the regulation of auditors assigned the task of verifying a company's financial health. Ultimately, Congress determined that a company's implementation of proper accounting techniques was not merely good business, it would be the law and violators would be subject to fines or even prison terms.

Not surprisingly, as a result of SOX, the role of the auditor responsible for conducting an audit, or review, of the accounting methods and techniques used by a company has become increasingly important. Individuals who are directly employed by a company to examine the company's own accounting procedures are called **internal auditors**. They can play a valuable role in assessment because they usually understand the company's business so well. **External auditors** are individuals or firms who are hired specifically to give an independent (external) assessment of a company's compliance with standardized accounting practices.

In the hospitality industry, managers of smaller restaurants, clubs, and lodging facilities most often serve as their own in-house auditors. If the facility they manage is part of a larger company or chain of units, their company may also employ in-house auditors. In larger hotels, the **controller**, who is the person responsible for managing the hotel's accounting processes, may serve as the auditor, or, in very large properties, full-time individuals specifically to act as the property's in-house auditors are employed.

Auditors not only help ensure honesty in financial reporting, but they also play an important role in devising the systems and procedures needed to help ensure the protection and safeguarding of business assets. As a result, hospitality managers use auditors and auditing techniques to address many internal questions, a few of which are as follows:

1. Are all purchases we make supported by the presence of a legitimate invoice before we process payment for it?
2. Are any guest adjustments from their initial bill supported by written documentation explaining why the bill was adjusted?



3. Is all the revenue reported as achieved by the business fully documented and **reconciled** (compared and matched) to bank statements that list actual deposits made into the businesses bank accounts?
4. Are wages paid to all employees supported by a written and verifiable record of hours worked?

The best auditors help ensure that financial records are accurate. They also assist managers in reducing waste and preventing fraud. In this text, the procedures, techniques, and strategies developed by this important branch of accounting will often be utilized to help you learn to become the best hospitality manager you can be.

## Managerial Accounting

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Managerial accounting is the primary topic of this book as well as the final branch of accounting we will examine. To clearly understand the purpose of managerial accounting, assume that Karen Gomez is the person responsible for providing in-flight meals to international travelers on flights from New York to Paris. She manages a large commercial kitchen located near the John F. Kennedy Airport. Karen's clients are the airlines who count on her company to provide those who have chosen to fly with them tasty and nutritious meals at a per-meal price the airlines find affordable.

One of Karen's clients wishes to add a new flight beginning next month. The evening flights will carry an average of 500 travelers, each of whom will be offered one of two in-flight meal choices for dinner. The client would like to provide each flier with a choice of a beef or a chicken entrée. To ensure that the maximum number of fliers can receive their first choice, should Karen's company plan to provide each flight with 500 beef and 500 chicken entrées? The answer, most certainly, is no.

To prepare 1000 meals (500 of each type) would indeed ensure that each traveler would always receive his or her first meal choice, but it would also result in the production of 500 wasted meals (the 500 meals *not* selected) on each flight. Clearly, it would be difficult for Karen to provide the airline with cost-effective per-meal pricing when that many meals would inevitably be wasted.

The more cost-effective approach would be to accurately forecast the number of beef and chicken entrées that would likely be selected by each group of passengers and then produce that number. The problem, of course, is in knowing the optimum number of each meal type that should be produced. If Karen had carefully and consistently recorded previous meal-related transactions (entrées chosen by fliers on previous flights), she would be in a much better position to use this information to estimate the actual number of each entrée type the new passengers would likely select. If she had done so, she would be using managerial accounting. **Managerial accounting** is simply the system of recording and analyzing transactions for the purpose of making management decisions of precisely this kind.

Because it consists of utilizing accounting information (historical records in this specific case) to make informed management decisions, managerial accounting is one of the most exciting of the accounting branches. Its proper use requires skill, insight, experience, and intuition. These are the same characteristics possessed by the best hospitality managers. As a result, excellent hospitality managers most often become excellent managerial accountants.

The branches of accounting we have reviewed and the main purpose of each are summarized in Figure 1.1.

FIGURE 1.1

**Branches and Purpose of Accounting**

Branch	Purpose
1. Financial	Record financial transactions
2. Cost	Identify and control costs
3. Tax	Compute taxes due
4. Auditing	Verify accounting data and procedures
5. Managerial	Make management decisions using accounting information

**Fun on the Web!**

The AICPA is the national professional organization for all CPAs. Its mission is to provide members with the resources, information, and leadership that enable them to provide valuable services in the highest professional manner to benefit the public as well as employers and clients. To view

their website, enter "AICPA" in your favorite search engine.

When you arrive at the site's main page, click on "Publications" to review just some of the resources they have available for professionals working in each of the major branches of accounting.

Now that you have reviewed the major branches of accounting, it may be easier to understand why it is so important for businesses to employ highly skilled professionals to perform their accounting functions. In the United States, those individuals who are recognized as highly competent and professional in one or more of the branches of accounting have earned the designation of **Certified Public Accountant (CPA)**.

To become a CPA, professionals must meet the requirements of the state or jurisdiction in which they want to practice. These requirements, which vary from state to state, are established by law and administered by each state's Board of Accountancy. Once certified, most CPAs join the American Institute of Certified Public Accountants (AICPA), which is the national professional organization for all CPAs.

Another certification that may be earned is the **Certified Management Accountant (CMA)**. A CMA assists businesses by integrating accounting information into the business decision process. To become a CMA, professionals must meet the educational and experience requirements of the designation. They must also successfully complete the CMA examination, which includes the general areas of business analysis management accounting and reporting, strategic management, and business applications. The certification also requires compliance with ethical standards and practices. The Institute of Management Accountants (IMA) is the organization that grants the CMA certification.

Those hospitality professionals who work extensively in the areas of accounting and technology often become members of the Hospitality Financial and Technology Professionals (HFTP). HFTP was formed in 1952 and has its headquarters in Austin, Texas. It offers its own certifications for hospitality

## Fun on the Web!

The Association of Accountants and Financial Professional in Business (IMA) is a professional organization for CMAs. Its mission is to provide a dynamic forum for management accounting and finance professionals to develop and advance their careers through certification, research and practice development, education,

networking, and the advocacy of the highest ethical and professional practices.

To view the IMA website, enter "Certified Management Accountant/IMA" in your favorite search engine. When you arrive at the site, click on "CMA Certification" to review the requirements for obtaining this worthy designation.

## Fun on the Web!

The HFTP association has nearly 5000 members. You can view their website by entering "HFTP" in your favorite search engine.

When you arrive at the site's main page, click on "Membership" to review the various membership categories available to hospitality managers.

professionals working in the accounting and technology areas, and it provides for them a global network.

The majority of hospitality managers are *not* likely to become CPAs or even certified members of HFTP. As a practicing hospitality professional, you are most likely interested in learning how using accounting information in the management jobs you will hold can help you make better, more informed decisions. Because that is true, before you start to learn more about managerial accounting, it is important for you to understand exactly *why* you should learn more about it.

## Why Hospitality Managers Use Managerial Accounting

Learning Outcome 3: Explain why managerial accounting in the hospitality industry is different from managerial accounting used in other industries.

**Hospitality accounting** is not a separate branch of accounting, but it is a very specialized area that focuses on the accounting techniques and practices used in restaurants, hotels, clubs, and other hospitality businesses. If hospitality were very similar to other industries, there would be little reason to create a separate book about, or even to study, managerial accounting specifically for the hospitality industry. It is true that accountants in the hospitality industry follow the same rules as do accountants in any other field. The hospitality industry, however, like the people who work in it, is unique. Those who would maintain that any managerial accountant or CPA can be equally effective as the one very familiar with the hospitality industry fail to recognize the culture, history, language, and norms that differentiate this exciting field.

To confirm some of the reasons why managerial accounting is a separate field of study, take the hospitality accounting term quiz in Figure 1.2.

**FIGURE 1.2**

**Hospitality Accounting Term Quiz**

Match the hospitality accounting term on the left with its corresponding manager's definition on the right.

Hospitality Term	Manager's Definition (Formula)
1. ADR	a. Selling price – Product cost
2. Check average	b. Cost of goods sold/Revenue
3. Occupancy %	c. Fixed costs/Contribution margin %
4. Sales break-even point	d. Rooms sold/Rooms available for sale
5. RevPAR	e. EP weight/AP weight
6. Profit margin	f. Total sales/Number of guests served
7. Product cost %	g. Room revenue/Rooms available
8. Product yield %	h. Beginning inventory + Purchases – Ending inventory
9. Contribution margin	i. Net income/Total sales
10. Cost of goods sold	j. Room revenue/Rooms sold

Turn to the next page to find out the number of questions you got right, and then read the test results key below.

Test Results Key	
Number Correct	Rank
9–10	<b>Chief Executive Officer (CEO):</b> Congratulations you are already a star!! With your current knowledge, you can quickly learn to be an exceptional managerial accountant in the hospitality industry.
7–8	<b>Company Vice President:</b> You are well on your way to mastering all of the concepts you must understand to become an excellent managerial accountant.
5–6	<b>District Manager:</b> Achieving this score means you already have the conceptual skills and understanding you will need to move up rapidly.
3–4	<b>Unit Manager:</b> You know more than most. Experience and more practice will help you advance rapidly.
2 or less	<b>Don't worry!</b> When you finish learning the material in this book, you will get a perfect score!

As you may have discovered by taking the quiz, those professionals using managerial accounting in the hospitality industry must have specialized knowledge. That knowledge is the result of learning the intricacies of the restaurant or hotel business and then applying what they know to a financial analysis process. Managers in the hospitality industry have found that it is helpful to standardize some aspects of their own industry segment's accounting procedures. They have done so by creating standardized, or uniform, methods of reporting their financial accounts.

## Consider the Cost

"This is a bit new for me," said Maddie, the new controller at the 600-room Fairmont Hotel.

"I know," said Marcus, the hotel's general manager, "but you will catch on pretty quick I'm sure. And I am convinced you'll do great job for us."

Maddie had just been hired by Marcus to manage the three-person controller's office at the Fairmont. Previously she had served as the head accountant for a small chain of retail clothing outlets. Maddie had received her Bachelor of Science degree in accounting from State University, and when the controller's position came open at the Fairmont, she impressed Marcus in the interview process with her understanding of business and the importance of accuracy in accounting.

"One thing that I'm quickly learning," said Maddie, "is that sales in the hotel industry are certainly different than sales in the retail world."

"In what way?," asked Marcus.

"Well in several ways really," replied Maddie. "First, when a sale is made in retail, the same item of clothing sells to everyone at the same price. But here at the Fairmont the same hotel room can have dozens of prices. There's one price for people who are members of AAA and another for the groups that negotiate special rates with the sales department. There are a

number of different prices for members of the various corporations that use our hotel and still other prices depending on whether a room is purchased on a website or directly at the front desk. In addition, rooms sell for different prices based on the day of the week or time of year."

"That's certainly true," said Marcus. "Room rates and room rate management are very important to us. In most cases, we vary our rates depending on the demand for our rooms. And that means we change rates often. And I do understand that doing so makes it more difficult sometimes to track whether or not we actually received the proper amount of money for the rooms that we do sell. Welcome to the hotel business!"

1. The existence of variable room rates and their collection is just one unique aspect of hospitality management accounting. What are some other aspects?
2. Assume you are hiring a person to manage the accounting process in your hospitality business. If two candidates had equal accounting skills, do you think a candidate with experience in the hospitality industry would be preferable and more cost-effective for your business than one that did not have that same experience? Explain your answer.

## The Uniform System of Accounts

Learning Outcome 4: Identify the specific Uniform Systems of Accounts appropriate for the hospitality business you manage.

It is helpful when all managers in a segment of the hospitality industry utilize the same guidelines for recording and computing their financial data. The manner in which operating statistics are compiled and revenue or expense data is reported can be very significant to the proper interpretation of that data.

Laws exist requiring owners to properly report and pay taxes due, to file certain documents with the government, and to supply accurate business data to various other entities. As a result, many hospitality companies require that their managers use a series of standardized (uniform) accounting procedures created specifically for

their own segment of the hospitality industry. These are called a **uniform system of accounts** and simply represent agreed upon methods of recording financial transactions within a specific industry segment.

In the hospitality industry, some of the best known of these uniform systems are

- **Uniform System of Accounts for the Lodging Industry (USALI)**
- **Uniform System of Accounts for Restaurants (USAR)**
- **Uniform System of Financial Reporting for Clubs (USFRC)**

## **Uniform System of Accounts for the Lodging Industry (USALI)**

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The hotel industry was one of the first of the segments within hospitality to encourage its members to standardize their accounting procedures. In the United States, the first USALI was developed in 1925 by members of the Hotel Association of New York City.

The USALI is currently developed by the Hotel Association of New York City Inc., the HFTP, and the Educational Institute (EI) of the American Hotel & Lodging Association (AH&LA). The USALI gives hoteliers and their accountants a consistent and easily understandable “roadmap” to record revenues, to record expenses, and to report a hotel’s overall financial condition. It is continually updated as those in hotel management stay abreast of the many changes occurring in their industry. The hotel-related financial documents presented in this text use the formats and procedures recommended in the eleventh edition of the USALI, published in 2014.

## **Uniform System of Accounts for Restaurants (USAR)**

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The USAR, prepared by the National Restaurant Association (NRA), assists restaurant operators by suggesting a common financial language for the food service industry. This gives users the opportunity to compare the results of one restaurant to another and one accounting period to another. In addition, it allows those managers using it to compare the financial results of their own operation to industry norms. The restaurant-related financial documents presented in this text use the formats and procedures recommended in the eighth edition of the USAR, published in 2012.

## **Uniform System of Financial Reporting for Clubs (USFRC)**

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Club management is another example of an industry segment that requires specialized knowledge and thus its own uniform system of accounts. The USFRC is a club accounting resource for club managers, officers, and controllers. It is produced through the joint efforts of HFTP and the Club Managers Association of America (CMAA). The USFRC is a financial reporting system geared specifically to member-owned, not-for-profit city and country clubs.

Whenever practical and possible, hospitality managers working in a specific segment of the industry should seek out and then use the uniform system of accounts that has been developed especially for them.

## Managerial Accounting Around the World

In the United States, the Financial Accounting Standards Board (FASB) is a nonprofit entity whose objective is to establish and improve generally accepted accounting principles (GAAP) (see Chapter 2). Use of these accounting principles is intended to ensure the financial statements and reports produced by those organizations utilizing GAAP provide their readers with information that is clear, useful, and relevant to their needs. The FASB is independent of all other business and professional organizations.

The work of the FASB is so important that the Securities and Exchange Commission (SEC), an agency within the U.S. federal government, has designated the FASB as the organization responsible for developing accounting standards for use by public companies in the United States.

As useful as GAAPs are, it is important to recognize that over 110 countries around the world rely on the International Financial Reporting Standards (IFRS) recommendations when developing their financial reporting documents. The IFRS contain some key differences when compared to the GAAPs used in the United States.

To cite just one example, when establishing the value of their product inventories, U.S. hospitality managers can elect to use the First-In, First-Out (FIFO) valuation method in which assets produced or acquired first are the ones sold or used first. Alternatively, GAAP also allows them to utilize the Last In, First Out (LIFO) valuation method in which assets produced or acquired last are the ones that are sold or used first.

Because, in most situations, income tax deferral is the only justification for the use of the LIFO method, it is banned under international financial reporting standards and under IFRS the LIFO method for accounting for inventory costs is simply not allowed.

As they have in the past, it is highly likely that hospitality management organizations based in the United States will continue to expand internationally. As they do, it will become increasingly important for managers at the highest level of these organizations to understand the unique differences that exist within each of the countries where their businesses operate. These differences extend to accounting principles and practices, and they too must be well understood.

## Ethics and Hospitality Accounting

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Learning Outcome 5: Summarize your ethical responsibilities as a managerial accountant in the hospitality industry.

The hospitality industry is one of the most honorable, exciting, and rewarding industries in the world. It will continue to offer its members solid employment opportunities and serve as the backbone of many local economies only if its current managers maintain the integrity of those who have gone before them. Among a variety of responsibilities, this includes preparing and presenting their important financial information in a manner that is both legal and ethical.

Sometimes it may not be clear whether an actual course of action is illegal or simply wrong. Put another way, an activity (including an accounting activity) may be legal, but still the wrong thing to do. As a future hospitality manager, it is important that you be able to make this distinction. **Ethics** refers to the choices of proper conduct made by an individual in his or her relationships with others. Ethical behavior refers to behavior that is considered “right” or the “right thing to do.” Consistently choosing ethical behavior over behavior that is not ethical is

important to your long-term career achievements. This is so because hospitality managers often will not know what the law may actually require in a given situation. As a result, when managerial activities are examined, employers, in many cases, will simply consider whether a manager's actions were intentionally ethical or unethical.

How individuals determine what constitutes ethical behavior can be influenced by their cultural or environmental background, religious views, professional training, and their own moral code. It is certainly true that the definition of ethical behavior may vary based upon an individual's own perception of what is ethical. While it may sometimes be difficult to determine precisely what constitutes ethical behavior, the five guidelines in Figure 1.3 can prove to be very useful when you are evaluating the ethical implications of a specific decision or course of action.

An example of the way an individual would actually apply the five ethical guidelines is demonstrated in the following hypothetical situation.

Assume that you are the controller of a large hotel. Along with the F&B director, executive chef, director of sales and marketing, and other managers in the hotel, the general manager has assigned you to assist in the planning for your hotel's New Year's Eve gala. The event will require a large amount of wine and champagne. As part of your responsibilities, you conduct a competitive bidding process with the wine purveyors in your area, and, based upon quality and price, you agree with the F&B director's recommendation that you place a very large order (in excess of \$20,000) with a single purveyor. One week later, you receive a case of very expensive champagne, delivered to your home with a nice note from the purveyor's representative stating how much he appreciated the order and that he is really looking forward to doing business with you in the years ahead. What do you do with the champagne?

**FIGURE 1.3**

### **Ethical Guidelines**

**1. Is it legal?**

Any course of action that violates written law or company policies and procedures is wrong.

**2. Does it hurt anyone?**

Are benefits accruing to the manager that rightfully belong to the owner of the business? Discounts, rebates, and free products are the property of the business, not the manager.

**3. Am I being honest?**

Is the activity one that you can comfortably say reflects well on your integrity as a professional, or will the activity actually diminish your reputation?

**4. Would I care if it happened to me?**

If you owned the business, would you be in favor of your manager behaving in the manner you are considering? If you owned multiple units, would it be good for the business if all of your managers followed the considered course of action?

**5. Would I publicize my action?**

If you have trouble remembering the other questions, try to remember this one. A quick way to review the ethical merit of a situation is to consider whom you would tell about it. If you are comfortable telling your boss about the considered course of action, it is likely ethical. If you would prefer that your actions go undetected, you are probably on shaky ethical ground. If you wouldn't want your action to be read aloud in a court of law (even if your action is legal), you probably shouldn't do it.



## Ethical Analysis

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Your first thought may be the most obvious one and, that is, you drink it! However, it is hopeful that you will first apply the five questions of the ethical decision-making process to your situation.

### 1. Is it legal?

From your perspective, it may not be illegal for you to accept a case of champagne. However, there could be liquor laws in your state that prohibit the purveyor from gifting that amount of alcoholic beverage. You must also consider whether it is permissible within the guidelines established by the company for which you work. In this case, violation of a stated or written company policy may subject you to disciplinary action or even the termination of your employment.

### 2. Does it hurt anyone?

When asking this question, you have to recognize who the stakeholders are in this particular situation. How might others in your company feel about the gift you received? After all, you probably agreed to work for this hotel at a set salary. If benefits are gained because of decisions you make while on duty, should those benefits accrue to the business or to you? Besides, any gifts received by you will most likely be paid by your business through future price increases.

### 3. Am I being honest?

Do you really believe that you can remain objective in the purchasing/bid aspect of your job and continue to seek out the best quality for the best price, knowing that one of the purveyors rewarded you handsomely for last year's choice and may be inclined to do so again?

### 4. Would I care if it happened to me?

If you owned the company you work for, and you knew that one of the managers you had hired was given a gift of this size from a vendor, would you question the objectivity of that manager? Would you like to see all of your managers receive such gifts? Would you be concerned if they did?

### 5. Would I publicize my action?

Would you choose to keep the champagne in the event that you knew that tomorrow, the morning headlines of your city newspaper were going to read:

*“Controller and Food and Beverage Director of Local Hotel Each Receive Case of Expensive Champagne After Placing Large Order with Beverage Purveyor: Hotel Owners to Investigate.”*

Your general manager would see it, other employees would see it, all of the other purveyors that you are going to do business with would see it, and even potential future employers would see it.

What are some of the realistic alternatives to keeping the champagne?

1. Return it to the purveyor with a nice note telling them how much you appreciate it but your company policy will not allow you to accept it.
2. Turn the gift over to the general manager to be placed into the normal liquor inventory (assuming that the law will allow it to be used as such).
3. Donate it to the employee Christmas party.

Use the five questions listed in Figure 1.3 to evaluate each of these three courses of action. See the difference? If you are like most managers, each of the three alternatives presented will “pass” the five-question test, while the alternative of accepting the champagne for personal use will not.

Just as the ethical nature of a manager’s daily actions can be examined, so too can that manager’s approach to recording and reporting financial data. Everyone would agree that hospitality managers should follow any laws that regulate the reporting of financial information. Laws do not exist, however, to cover every situation that future managerial accountants will encounter. Society’s views of acceptable behavior, as well as specific laws, are constantly changing. Ethical behavior, however, is always important to responsible individuals as well as their organizations.

There are rules that must be followed if a manager’s financial records are to be trusted and if the interpretations made about the financial data they contain is to be perceived as honest. As you continue through this text, you will see that, in many instances, hospitality managers may be faced with ethical choices about how they report and assess financial data. As well, in your own career, you will likely find many instances in which you are faced with ethical choices about your own managerial decisions. It is important to understand that each management decision you make partially shapes and helps define the type of manager you are as well as the type you are perceived to be by others. In nearly all instances in which a company’s financial officers have deceived its investors and owners, there were instances where lapses in ethical judgments directly resulted in significant harm to the company’s shareholders and employees.

In the following chapters, you will discover exactly how hospitality managers use information related specifically to the hospitality industry and their own personal skills and experience to analyze their businesses using ethical managerial accounting techniques for the hospitality industry. As you have learned, however, the hospitality industry is very broad. As a result, some of those managerial accounting techniques that may be of great interest to the manager of a large hotel may be of less interest, for example, to the manager of a small carry-out pizza shop. As the authors of a managerial accounting text, it was important that we create a book that serves the widest possible audience at the same time realizing that, for example, the specific interests of a future hotel general manager will vary from that of a student interested in a career in college and university food services. Because you now know that the field of accounting is specialized by branches as well as by the business in which accountants may work, this book’s title “*Managerial Accounting for the Hospitality Industry*” should give you a very clear idea about the useful, interesting, and fun things you will learn about accounting in its remaining chapters.

## Blue Lagoon Case Study

You have learned that managerial accounting in the hospitality industry is a unique field of study. In this text, you will come to better understand some of the managerial accounting issues faced by hospitality professionals by examining the operation of the fictitious Blue Lagoon, and the challenges facing Paige Vincent, its newly appointed General Manager.

For purposes of this book, features of the Blue Lagoon include extensive water park play areas, a 240-room hotel, and a variety of food service

outlets. The resort achieves gross revenue of over \$25,000,000 per year. In the remaining chapters of this text, we will use, when it is helpful to do so, the inner workings of the Blue Lagoon as our reference point for managerial accounting activities.

As you examine the issues facing Paige Vincent, you will actually be examining many of the accounting-related issues you will face as a managerial accountant in your own specialty area.

## Fun on the Web!

If you have not personally visited a major indoor water park, you can take a mini-tour of several facilities that are similar to the hypothetical one Paige Vincent will be managing in this text.

To do so, enter "Kalahari Resorts" in your favorite search engine and view one or more of their operations.

## Here's How It's Done

Some students who begin their managerial accounting course are concerned that they will have difficulty with the math portion of the course. Answer the following questions and then score yourself to see if you will have difficulty with the math presented in this text.

### Questions

- A  $2 + 2 =$  \_\_\_\_\_
- B  $6 - 2 =$  \_\_\_\_\_
- C  $8 \times 2 =$  \_\_\_\_\_
- D  $16 / 2 =$  \_\_\_\_\_
- E  $(8 + 2) / 2 =$  \_\_\_\_\_

### Answers

- A 4
- B 4
- C 16
- D 8
- E 5

Readers who were able to easily solve math problems just like these already have all the quantitative math skills they need to successfully master all of the material in this text. This is true because the mastery of managerial accounting is primarily related to knowing which numbers to use in a calculation and how to interpret the results of the calculation, not the application of advanced mathematics!

In this text, you will learn about the specific managerial accounting methods, procedures, and strategies used by those managing hospitality businesses. The Here's How It's Done boxes located throughout the text will help you practice using the formulas and calculations hospitality managers actually apply when analyzing their businesses.

## Apply What You Have Learned

Samara Tate couldn't have been happier. As she looked back on the past two years, she realized just how much her hard work had paid off. First, she had been hired as a waitress at the exclusive Sycamore Country Club working in the "Member's Only" dining room. Then, as she continued to work part-time at the Club and pursue a degree in hospitality management, she had been promoted to banquet bartender. After one year in that position, she had been promoted to banquet bar supervisor. Her knowledge and strong leadership skills had impressed the Club's managers as much as her personality had impressed the Club's membership.

Now, just as she was about to graduate, the Club’s F&B director called Samara into her office to offer her the job of beverage manager. It was an important job, as the Club’s beverage department grossed over \$500,000 per year. Samara was excited about the opportunity and the pay!

1. Properly accounting for beverage sales is an important part of a beverage manager’s job. What are two additional specific areas of financial accounting that would be important for Samara to understand if she is to succeed in her new job?
2. Maintaining accurate records about costs is an important part of nearly every manager’s job. Name two hospitality-specific areas of costs that you think would be important for Samara to understand well if she is to excel in her new job.
3. Assume that Samara accepts the beverage manager’s position. Identify at least two specific tasks she is likely to be assigned in which she would be required to apply her knowledge of managerial accounting.
4. Do you think Samara could do a good job of managing the Club’s entire beverage department without a good understanding of the way managerial accounting information is used by hospitality managers? Why or why not?

## Key Terms and Concepts

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The following are terms and concepts discussed in the chapter that are important for you as a manager. To help you review, please define the terms below.

Hospitality	Accounting equation	External auditors	Uniform System of
Travel and tourism industry	Cost accounting	Controller	Accounts for the
Accounting	Cost	Reconciled	Lodging Industry
Accountant	Tax accounting	(bank statements)	(USALI)
Financial accounting	Occupancy tax	Managerial accounting	Uniform System
Revenue	Sales tax	Certified Public	of Accounts for
Expense	Payroll tax	Accountant (CPA)	Restaurants (USAR)
Profit	Audit	Certified Management	Uniform System of
Assets	Auditor	Accountant (CMA)	Financial Reporting
Liabilities	Sarbanes-Oxley Act (SOX)	Hospitality accounting	for Clubs (USFRC)
Owners’ equity	Internal auditors	Uniform system of accounts	Ethics

## Test Your Skills

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1 Consider the table below that lists finance-related tasks for which hospitality managers are commonly responsible. Then, identify the branch of accounting that would most help these managers address those specific areas of responsibility.

**Branches of Accounting:**

- Auditing
- Cost
- Financial
- Managerial
- Tax

Area of Management Responsibility	Branch of Accounting
Recording financial transactions	
Identifying and controlling costs	
Computing taxes due	
Verifying accounting data and procedures	
Making management decisions using accounting information	

2 Match the branch of accounting that would be best used to answer the following questions.

Question	Branch of Accounting
How should I record transactions associated with cash, payroll, and short-term debt?	
How much does it cost to pay for maintenance for my swimming pool this year?	
What occupancy tax is owed by the hotel this month?	
How should I record transactions associated with revenue, expenses, and profit?	
How much sales tax should we have collected this month?	
Are all food purchases made this month documented with legitimate invoices?	
If I wanted to achieve a profit of \$10,000 in the month of April, how many pizzas will I need to sell?	
Are all bonuses paid to managers supported by documented revenue performance measures?	
What were the total costs of salaries and wages incurred by the restaurant this month?	
Would it be more profitable if I made my potato salad from scratch or purchased it pre-prepared?	

3 Kelly Pratt is the general manager of the Cherry Hill Hotel. Last month, Kelly’s operation generated \$85,000 in room sales revenue and \$5,000 in non-rooms revenue. The expenses required to generate her rooms revenue last month was \$71,000 and the expenses incurred to generate a \$5,000 in non-rooms revenue were \$1,500 as summarized below. Use this information to determine the total amount of profit generated by the Cherry Hill Hotel last month?

**Cherry Hill Hotel: Last Month**

Room sales revenue	\$85,000
Non-rooms revenue	\$5,000
Room expenses	\$71,000
Non-rooms expenses	\$1,500

**Cherry Hill Hotel: Last Month Profit**

Revenue	
Expenses	
Profit	

- 4 Richard owns a coffee bean shop that sells gourmet coffee and chocolates. Prepare both weekly and monthly profit formulas so that Richard has a good idea about his current profit situation.

Week	Revenue (\$)	Expenses (\$)	Profit/Loss (\$)
1	956.34	1258.75	
2	2286.45	1687.54	
3	2678.91	2563.87	
4	1875.23	1378.95	
<b>Month</b>			

- In which week did Richard have the most profit?
  - Did Richard show a profit for all four weeks? If not, which week(s) did he experience a loss?
  - As the owner, Richard wanted a profit of \$1000 for the month. Did he reach his goal?
- 5 Earlene Rensir is the owner of the Smokey Pit Bar-B-Q restaurant and she is preparing a balance sheet for her business. Using the data below, help Earlene complete the spreadsheet she will use to determine the amount of assets, liabilities, and owners' equity she has in the business.

**Smokey Pit Bar-B-Q Assets Owned by the Business**

Cash on hand	\$25,000
Inventory on hand	\$45,000
Value of equipment	\$300,000
Value of building	\$2,000,000

**Smokey Pit Bar-B-Q Liabilities Owed by the Business**

Amount owed to vendors	\$175,000
Amount owed to lenders	\$1,500,000

Assets	Liabilities	Owners' Equity

- 6 The Chief Financial Officer (CFO) of a restaurant chain notices that the "travel expenses" for the Chief Executive Officer (CEO) are much higher than anticipated for the year. She suspects that the CEO is committing corporate fraud by embezzling the extra money. She notifies the CEO of her concern but is told that all of the expenses are legitimate.
- How would this suspected fraud be detected?
  - What legislation does this fall under?
- 7 Laura Marie is a purchasing agent for a small restaurant chain. For the past two weeks, one of her meat suppliers has been late on deliveries. She has discussed this with the salesperson, and he assures her that the problem will be resolved.

In an effort to rectify the issue, the salesperson delivers two free cases of hot dogs to her office for "sampling." Laura plans to have a back yard barbecue this weekend for her neighbors. The free hot dogs would considerably lower her cost of holding this event at her home. From an ethical point of view, how should she handle this situation? Explain your decision-making process and defend your answer.

Use the five ethical guidelines in this chapter as a basis for your answer to explain what should be done with the hot dogs.

- Is it legal?
- Does it hurt anyone?
- Am I being honest?

- d. Would I care if it happened to me?
  - e. Would I publicize my action?
  - f. What should be done with the two cases of hot dogs?
- 8 **BONUS:** Aafreen Pashia has just been named the general manager of the Balmour Hotel. The hotel has 300 rooms and a full-service restaurant.

July 1 of this year is her first day of work and Aafreen is reviewing the hotel's operating results from the previous month. Aafreen has received the following information regarding the property's June of this year operating results:

Room revenue: \$945,000  
 Rooms sold: 6,300  
 Rooms available for sale: 9,000  
 Restaurant cost of goods sold: \$50,880  
 Restaurant revenue: \$169,600  
 Property net income: \$222,920  
 Property total sales: \$1,114,600

**Balmour Hotel June Operating Results**

(a)	ADR	
(b)	Occupancy %	
(c)	RevPAR	
(d)	Restaurant product cost %	
(e)	Property profit margin	

- a. What was the hotel's average daily rate (ADR) for June?
- b. What was the hotel's occupancy percentage for June?
- c. What was the hotel's RevPAR for June?
- d. What was the restaurant product cost percentage for June?
- e. What was the property's profit margin for June?