6

Hotel Management Reports

Learning Objectives

1. To learn about internal hotel management reports.
2. To understand and be able to use Daily Revenue Reports.
3. To understand and be able to use revenue forecasting reports.
4. To understand and be able to use labor productivity reports.
5. To understand the relationship between revenue changes and profit changes.

Chapter Outline

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The three financial reports that we have discussed in previous chapters—the Profit and Loss (P&L) Statement, the Balance Sheet, and the Statement of Cash Flow—are used by both management and outside parties in evaluating hotel operations. We will now talk about two types of internal financial and management reports that hotel managers use:

- One report summarizes and presents the operating results for the previous day or week.
- The second report forecasts or schedules operations and functions for the next day or next week.

Managers use these reports to understand and evaluate past operations and to plan their daily and weekly future operations. They will make any necessary changes to daily operations to achieve budgets and forecasts or to respond to market or outside conditions.

Internal management reports are prepared by the accounting office and distributed to hotel managers for their use. Refer again to the Financial Management Cycle:

1. Operations produces the numbers.
2. Accounting prepares the numbers.
3. Operations and accounting analyze the numbers.
4. Operations applies the numbers to change or improve operations.

The reports that we will discuss in this chapter are examples of the Financial Management Cycle. Operations produces the numbers, whether they are good or bad. It is accounting's job to collect and prepare the management reports from these operational numbers so that managers can use them to identify and analyze operations. Then management can apply the information from the numbers to the next day's or week's operations. The goals are to understand what happened, why it happened, and how it can be changed or improved.

Internal Hotel Management Reports

Definition

An internal management report contains detailed operating information covering a specific time for a specific product, customer, department, or for the entire hotel or restaurant. It can contain the operational results for activities of the previous day or week, or it can contain the information required to plan the next day or week. Daily and weekly reports are used internally as management tools, whereas monthly reports are used both as a management tool and to report the monthly financial results for the three formal financial statements: the P&L, the Balance Sheet, and the Statement of Cash Flow.

These internal management reports are extremely valuable to operations managers. They are a guide—a true management tool—for them to use in managing their daily operations. The more a manager understands these reports, the better she or he will be able to use them to improve or change operations.

Types and Uses

Reports contain daily, weekly, monthly, and quarterly information. They include reports that provide actual operating information and financial information for previous time periods and reports that plan in detail for future time periods. Daily and weekly reports that provide the results of actual operations are used to forecast and schedule operations for the next day, week, month, or quarter. Table 6.1 illustrates the types and uses of internal management reports.

We will discuss these reports in detail, including examples of the reports used by some of the major hotel and restaurant companies. Keep in mind that one type of report provides historical operating information and the other type forecasts and schedules operations for the next week.

Daily Reports

The two most important daily reports provide information on revenues and labor costs. The names and formats of these reports can be different from company to company, but the content is the same. They focus on providing the actual operating results for the previous day and comparing those results with forecasts, budget, the previous month, and last year's information.

TABLE 6.1
Internal Management Reports

	Daily	Weekly	Monthly	Quarterly	Annually
Performance Reports—The Past					
Daily revenue report	X				
Daily labor report	X				
Weekly financial report		X			
Monthly P&L			X		
Profitability measurement			X	X	X
Planning Reports—The Future					
The daily room count	X				
The daily banquet schedule	X				
Weekly revenue forecast		X			
Weekly labor forecast		X			
Monthly revenue forecast			X		
Quarterly revenue forecast				X	
End-of-year revenue forecast					X

Daily Revenue Reports

This report is prepared during the night audit or day audit shift and collects and presents all of the operating information for the previous day. It can be called the Sales and Occupancy Report, the Daily Revenue Report, or the Gross Revenue Report depending on the company. All contain virtually the same information. We will discuss a Daily Revenue Report that is organized into the following section: (1) hotel daily revenue by department, (2) hotel daily room statistics, (3) Restaurant and Banquets Summary, and (4) hotel market segment information.

The *daily revenue by department* is organized in a similar format as the P&L Statement. The *title* provides the name of the hotel, type of report, and date of the report. The *horizontal headings* provide revenue for the day and compare it to the budget and last year's revenues. It also provides month-to-date accumulated revenue for actual, budgeted, and last year's totals. Managers can then evaluate how their current financial results compare to the budget and to the previous year for both time periods. The *vertical headings* show the individual revenue centers (or departments) for the hotel. Exhibits 6.1 and 6.2 are examples of daily revenue report formats for two major hotel companies:

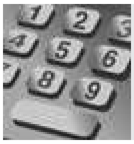

EXHIBIT 6.1

SALES AND OCCUPANCY REPORT

Hotel Name
Sales and Occupancy Report
Date

Revenue by Hotel Department

	Today			Period to Date		
	Actual	Budget	Last Year's Actual	Actual	Budget	Last Year's Actual
Transient Rooms Sales						
Group Rooms Sales						
Contract Rooms Sales						
Part Day/Guaranteed						
Adjustments						
Net Rooms Sales						
Telephone Sales						
Gift Shop Sales						
Rents and Commissions						
Other Sales						
Subtotal						

Restaurant Sales
Lounge Sales
Banquet Sales
  Total F&B Sales
Total Hotel Sales
  Over/Under Budget

Rooms Statistics

	Today			Period to Date		
	Actual	Budget	Last Year's Actual	Actual	Budget	Last Year's Actual
Room Nights						
Total Rooms in Hotel						
Complimentary Rooms						
Out of Order Rooms						
Rooms Available to Sale						
Rooms Rented						
Rooms Vacant						
Occupancy Percentage Available Rooms						
Occupancy Percentage Total Rooms						
Average Rate						
Transient Average Rate						
Group Average Rate						
Contract Average Rate						
Full Day Average Rate						
Net Average Rate						
REVPAR						
Miscellaneous						
Total Guests						
Arrivals						
Departures						
Drive-Ins						
Guaranteed No Shows						

Restaurant, Beverage, and Banquet Summary

	Food Today	Beverage Today	Period to Date
	Sales Customers Average Check	Sales & Food Sales	Customers Average Check
	Actual Budget Last Year	Actual Budget Last Year	Actual Budget Last Year
Restaurant			
Room Service			
Specialty Restaurant			
Lounge			
Total Restaurant and Beverage			
Banquet Sales			
Banquet Meeting Rooms			
Banquet Other			
Total Banquet			

Hotel Market Segment Information

	Today			Period to Date		
	Rooms Sold	Revenue	Average Rate	Rooms Sold	Revenue	Average Rate
Weekday						
Regular						
Corporate						
Special Corporate						
Discounts						
Total Transient						
Corporate Group						
Association Group						
Other Group						
Total Group						
Contract						
Total Weekday						
Weekend						
Regular						
Corporate						
Special Corporate						
Discounts						
Total Transient						
Corporate Group						
Associate Group						
Other Group						
Total Group						
Contract						
Total Weekend						

Group Business
Individual Groups Listed

Complimentary Rooms
Names Listed

Other Information
Contract Business
Out-of-Order Rooms
Walked Guests

As you can see, this is a lot of information. It is very complete and detailed. Each manager in the hotel will focus on the operating information for his or her department. The Front Office and Housekeeping managers will focus on room sales and statistics. The Restaurant, Lounge, and Catering managers will focus on food and beverage sales and statistics. Again, there is a lot of information in these reports, but each manager will focus on his or her own areas and will be familiar with trends, forecasts and budgets, recent events, and the status of the local economy. Working with the Daily Revenue Report each day will enable a hospitality manager to get familiar and understand better the operational results contained in the daily report and internal or external factors that affect those results.

Exhibit 6.2 is a second example of a hotel daily revenue report. This company organized the information into the following sections: (1) summary, (2) rooms sales and statistics, and (3) food and beverage sales and statistics. It includes labor productivities and profitability estimates.

EXHIBIT 6.2

REVENUE REPORT

	Today Actual Preliminary		Month to Date (MTD) Actual Preliminary		MTD Variance to Preliminary		MTD Last Year's Actual		MTD Variance to Last Year	
	Dollar	Percentage	Dollar	Percentage	Dollar	Percentage	Dollar	Percentage	Dollar	Percentage
Room Revenue										
Food Revenue										
Beverage Revenue										
Food and Beverage Other Revenue										
Total Food and Beverage Revenue										
Telephone Revenue										
Other Revenue										
Total Revenue										
Rooms Profit										
Food and Beverage Profit										
Telephone Profit										
Other Profit										
Gross Operating Income										
Administrative and General										
Sale and Marketing										
Heat, Light, and Power										
Repairs and Maintenance										
Total Overhead Expense										
Gross Operating Profit (Estimated)										

Rooms Sales and Statistics

Transient Revenue
Group Revenue
Less Allowances
Total Rooms Revenue
Payroll
  Administration
  Front Office
  Housekeeping
  Guest Services
  Transportation
  Reservations
Total Wages
Employee Benefit Percentage
Total Payroll
Other Expenses
Department Profit
Statistics
Available Rooms
Rooms Sold/Average Rate
  Transient
  Group
  Total Rooms Sold/Average Rate
Complimentary Rooms
Total Rooms Occupancy/Average Rate
Occupancy Percentage
Hotel Guest and Guests per Room
Arrivals
Departures

Memo Statistics
Rack Rate
Discounts
Contracts
Wholesalers
Total Transient
Association
Corporate
Specialty Group
Travel Industry
Total Group
Labor Hours
Administration
Front Office
Concierge
Housekeeping
Guest Services
Transportation
Reservations
Total Labor Hours

Food and Beverage Sales and Statistics

<u>Food Revenue</u>
Restaurant
Specialty Restaurant
Rooms Service
Banquets
Total Food Revenue
<u>Beverage Revenue</u>
Restaurant
Specialty Restaurant
Room Service

Lounge
Banquets
Total Beverage Revenue
Other Banquet Revenue
Room Rental
Service Charge
Other
Net Food and Beverage Revenue
Food Cost
Payroll
Restaurants
Beverage
Banquet
Kitchen
Administration
Catering
Total Food and Beverage Wages
Employee Benefits
Total Payroll
Outside Labor
Other Expenses
Department Profit
Labor Hours
Restaurants
Room Service
Banquets
Total Food Hours
Total Beverage Hours
Total Kitchen Hours
TOTAL LABOR HOURS

This hotel company chooses to provide operating information such as costs and estimated profits for the day in addition to the revenues. This enables managers to relate revenues for the day to the costs incurred to produce those revenues. If they see problems, they can make changes and corrections immediately.

It is important to go back to one of the fundamental financial analysis concepts—comparing actual results to other measures to establish meaning. These daily reports provide the financial numbers that result from operations. These are compared to other operating time periods to show if operations are improving, if revenues and profits are increasing, or if established budgets and forecasts are being met. After reading these daily reports, a department manager can adjust revenue forecasts, labor schedules, or make other operational changes if necessary. These daily reports can be very effective management tools if understood and used consistently.

Labor Productivity Reports

The second example of a Daily Revenue Report also includes daily labor productivity and wage cost information. The managers in this hotel company have both revenue and labor information available to them on the same report. This is convenient, and by reviewing this report, they can make necessary changes.

The hotel company in the first example provides the labor and cost information in a separate daily labor report. This report contains detailed information and states the labor expenses for the previous day. These results are compared to budget or forecast numbers to determine if established labor guidelines have been met. Each department manager focuses on her or his specific department results. There are two parts to analyzing labor and wage costs: labor hours and wage cost percentages. Both are important.

Labor Hours and Labor Productivity

This measure of productivity does not include any dollar cost information. It relates units of labor to units of output. More specifically, what amount of labor hours is required to support a certain volume of business. A labor hour is defined as the number of hours one employee works in performing his or her job responsibilities. Typically, full-time employees are scheduled for an eight-hour workday and a 40-hour workweek. Any additional hours during the week will result in overtime. So our basic unit of labor hours measurement is an eight-hour day and 40-hour week. Examples of formulas and ratios used in the hotel and restaurant business are as follows:

1. *Labor hours per room sold.* The formula is total labor hours divided by total rooms sold. This measure is used by the front office and housekeeping departments. They have established guidelines that are used to prepare budgets and forecasts. If actual results are different from these guidelines, managers are expected to identify what caused the difference or variations and how to make any necessary corrections.

Photo: The Otesaga Hotel

Aerial View of the Leatherstocking Golf Course and Otesaga Hotel
Cooperstown, New York

This aerial view of the Otesaga Resort in Cooperstown, New York, highlights the resort's Leatherstocking Golf Course and Lake Otsego. The resort opened in 1909 with 136 guest rooms, five food and beverage outlets, 13,000 square feet of meeting space, and an 18 hole golf course. The Otesaga offers meal packages that include breakfast and dinner in the room rate. Because this resort is located in Cooperstown where the Baseball Hall of Fame is located, it enjoys a very busy summer season. This high season is extended into October because of the many people who come to see the beautiful fall foliage in the mountains.

The Otesaga closes for approximately five months during the winter. What effect will this have on the hotel's profitability? What expenses will it continue to incur while it is closed? What do you think the owners of the Otesaga have had to do over the years to keep the resort competitive with the newer resorts that have been built in the last 20 years? How do the owners and managers of the Otesaga have to plan the cash flow for the year when they are closed for five months?

2. *Rooms cleaned or credits cleaned per shift.* The formula is total rooms cleaned divided by one eight-hour shift. This formula is used by housekeeping. The number of rooms cleaned by one housekeeper on an eight-hour shift can range from as few as 12 at a resort to as many as 18 at full-service or limited-service hotel.
3. *Labor hours per customer.* The formula is labor hours divided by total customers served in the restaurant. This relationship describes the number of labor hours required to service or take care of a corresponding customer volume level.

These formulas are used to calculate the number of labor hours required to work based on forecasted rooms sold or customers. They are true measures of labor productivities because they relate labor input in labor hours to products and services produced in terms of rooms sold or customers served. They do not involve any cost dollars or revenue dollars.

Wage Cost Percentage

This productivity measure compares the wage cost in dollars to revenue produced in dollars. It converts the labor productivity to dollars. The relationship now measures the dollar cost in wages incurred to the corresponding revenue levels resulting from rooms sold or meals served. Examples of wage cost percentages are as follows:

1. *Front office wage cost.* The formula is total front office wage cost in dollars (front desk, reservations, bellmen, concierge) divided by total room revenue in dollars. The resulting wage cost percentage measures this relationship. A hotel will have budget and forecast guidelines to achieve expected productivities and the actual wage cost percentage will be compared to these guidelines to determine if expected productivities are achieved.
2. *Wage cost per occupied room.* This formula has two steps. First, labor hours used times average hourly wage rate equals wage cost in dollars. Second, wage cost in dollars divided by rooms sold (same as rooms occupied) equals wage cost per occupied room. This shows how well managers are controlling labor dollar costs as they relate to rooms sold.
3. *Housekeeping wage cost.* The formula is total housekeeping wage cost in dollars (housekeepers, housemen, public space, supervisors) divided by total rooms revenue in dollars.
4. *Restaurant wage cost.* The formula is total restaurant wage cost in dollars (servers, bussers, hostess) divided by total restaurant revenue in dollars.

Labor productivities like labor hours per occupied room are the truest measure of productivities because they just measure labor input with labor output. It is the main measurement to managing wages. The next productivity identifies the dollar cost incurred to produce products and services and the dollar revenue resulting from the sale of products and services. This is the best measure of the financial relationship between expenses and revenues. Both are useful in managing operating departments.

It really does not matter whether labor productivity is included in one report or in two separate reports. What is important is that the daily productivity reports are used and applied to make department operations run smoother and produce maximum revenues and profits.

Weekly Internal Management Reports

These reports are also used to review and critique the previous day and the previous week and to forecast and prepare for the next week. These weekly reports are the primary reports used by managers because operations are planned for in weekly time periods. Revenues are forecasted for the entire week, wages are scheduled for the week, employee schedules are posted, and all operations are planned in weekly planning meetings. The week is the key planning and measurement time period. Although managers are concerned with the daily operations, the planning generally involves a weekly time period. The two most important weekly reports again involve revenues and wages.

There are two main uses for the weekly reports: forecasting to prepare for upcoming operations and evaluating and critiquing the past week's operations. First, managers look at the budget that was prepared for the upcoming week. This will be the starting point for their weekly plan. Second, managers review recent reports and business volume levels to see if the budget should be adjusted upward or downward. Third, managers prepare the revenue forecasts and wage schedules for the next week based on this information. This becomes the weekly forecast and will be the main planning document for their department. Hotel operations will be conducted daily based on this schedule. This part of the weekly report is about forecasting and planning.

The second use of weekly reports is evaluating and analyzing the previous week's performance to see how actual operational results compared with the budget or forecasted operations. Fourth, managers analyze actual performance and compare it to the budget and the forecast. Any differences or variations will be analyzed and critiqued to identify both good and bad results. If a problem exists and forecasted revenues or productivities are not achieved, it is important to identify if the entire week had problems or if there were big problems for only one day. What caused the problem? Was the problem a result of lower revenues or higher costs?

Fifth, managers evaluate how accurate their forecast for the week was compared to actual operations. Because a weekly forecast is prepared only several days before the week starts, it should be fairly accurate. Results from the previous week are available to help prepare as accurate a forecast as possible. It is important to evaluate the accuracy of the forecast as well as the actual performance because the weekly forecast is the document that is used to plan the details of the next week's operations. Managers should be close in their forecasts to build reliability and credibility. A poor forecast can result in poor performance in controlling costs as well as maximizing revenues and profits. Sixth, managers apply what they learned from the weekly results to operations and use this information to forecast the next week's operations.

Weekly Revenue Forecast

As discussed previously, the weekly revenue forecast is the first step in planning operations for the week. It is typical for hotel management to have a weekly selling strategy meeting on Monday or Tuesday to prepare a detailed, day-by-day forecast for the upcoming week that includes detailed daily revenue information such as daily rooms sold, daily arrivals and departures, the average rate, and daily revenues. The weekly forecast is then distributed to all managers for their use in planning the week. They will also look at the next month in more general terms to see if any significant changes are expected that will affect their weekly schedules.

Weekly Wage and Cost Scheduling

The next step is to take the weekly revenue forecast and schedule the wages required for each day's operations. This is usually due on a Wednesday. Ratios and formulas are used to convert daily rooms sold or customer counts into daily wage schedules for each department. The labor hours and wage expenses for the week are then totaled and ratios calculated to ensure that the weekly productivities are maintained. Adjustments are made to get productivities in line. For example, if the housekeeping labor hours per room sold is too high, the housekeeping manager should determine which day or which wage department is above the wage standards and reduce the labor hours to get to the expected productivity levels. If higher wage levels are required, the manager needs to document why and what work will be completed.

Profitability Forecasting

The last area to forecast is profitability. This is done by adding other operating expenses to the forecast. These are generally based on historical averages and are often relatively fixed expenses. Forecasted profits are calculated by subtracting all forecasted expenses from forecasted revenues. By completing profit forecasts for the week, they can be compared to budgeted weekly profits to ensure that both revenue and expense forecasts are in line and will meet expected or budgeted productivities and profitability.

Monthly Internal Management Reports

Everybody on the management team uses monthly reports, and that is why they are so important. We again focus on the monthly P&L Statement and how it is used by internal management as well as external investors, bankers, and other interested parties. It is analyzed in great detail to measure financial performance and describe the operations for the month.

Monthly P&L Statement

This is the financial statement that gets the closest scrutiny and is used the most in analyzing financial performance. This close analysis enables the monthly P&L to become a useful management tool. It describes not only the operational performance of a department but also what financial results that operational performance produces. The P&L is a common ground for discussion of financial performance because it is the financial statement that is used most by internal and external parties.

The monthly Consolidated P&L Statement provides a summary of each department's revenues and profits for the revenue centers and a summary of each department's total expenses for the expense centers. It is used to review the overall performance of a hotel by presenting the big picture. Comparisons with the budget—or with the previous month or the previous year—show if the financial performance of the hotel is improving, staying the same, or declining. It also identifies which departments are underperforming and which departments are overperforming.

The monthly Department P&L Statements provide the detailed operating results by department. This is where the analysis of department operations begins. Department managers can see the financial results of the decisions and activities that they have made during the month in operating their departments. Each line account in revenues and expenses can be examined to see if established operating plans and expected productivities were achieved. It is the primary responsibility of the department managers to know and understand the operations that produced the numbers. They are assisted in evaluating their monthly Department P&L Statement by their Executive Committee member, the Director of Finance, or another member of the accounting office. This is the third step of the Financial Management Cycle—evaluate and analyze the numbers.

Profitability, Retention, and Flow Through

This aspect of financial analysis is important because it goes beyond comparing the monthly financial results of a department with the budget and forecast, as well as comparing them to last month or last year. It involves identifying revenue, expense, and profitability changes from the budget or the forecast. There is an expected relationship between increases and decreases in revenues and how they increase or decrease expense and profitability.

Refer back to Chapter 2 and the section on trends. One important trend in financial analysis is to identify the relationship between revenue, expenses, and profits. Department managers are expected to be able to forecast increases and decreases in revenues compared to the budget and recent forecasts. They are also expected to be able to manage expenses to maintain productivities and produce the maximum profit given the forecast change in revenues.

There are several important terms that we need to understand before we go on:

- **Incremental** refers to an increase, something gained or added. This term is used in financial analysis to describe revenues, expenses, or profits beyond what was expected. If sales increase, what are the corresponding increases in expenses and profits? They should all increase in varying increments. Analyzing the incremental revenues, expenses, and profits will identify where the department did well and where it did not do well.
- **Fixed expenses** refer to expenses that remain constant regardless of the volume and level of business. Fixed expenses do not change from month to month.
- **Variable expenses** refer to expenses that increase or decrease directly with the volume and level of business. Variable expenses change each month based on business volume.
- **The Cost Management Index (CMI)** is the formula used to identify what level of expenses and profits is expected given incremental changes in revenues. The formula expects higher levels of profits with higher levels of revenues and can be used to forecast expenses and profits that should result from incremental revenues. Terms used by two hospitality companies to describe this process are **retention** and **flow thru**. These terms measure how much profits go up and down as a percentage of how much revenues go up and down.
- **Variation** refers to something that is slightly different from another of the same type. In financial analysis, variation is the difference between numbers—for example, the variation between actual and budgeted numbers or between actual numbers for this year and those for last year.

To illustrate the concepts of retention and flow thru, we will use several examples. We start with the Rooms Department budget and forecast for a month. We will identify incremental revenues and the effect they are expected to have on expenses and profits at the new revenue level:

	Forecast		Actual		Difference/Variation	
	Dollars	Percentage	Dollars	Percentage	Dollars	Percentage
Room Revenue	$600,000		$625,000		+$25,000	+4.2%
Management Wages (fixed expense)	11,000	1.8%	11,000	1.8%	0	0
Hourly Wages (variable expense)	36,000	6.0	37,000	5.9	+$ 1,000	+2.8
Contract Cleaning (fixed expense)	2,000	.3	2,000	.3	0	0
Guest Supplies (variable expense)	8,000	1.3	8,400	1.3	+400	+5.0
Reservation Cost (variable expense)	20,000	3.3	20,500	3.3	+500	+2.5
Total Fixed Expense	$ 13,000	2.2	$ 13,000	2.1	0	0
Total Variable Expense	64,000	10.6	65,900	10.5	+1,900	+3.0
Total Expenses	$ 77,000	12.8%	78,900	12.6	+1,900	+2.5
Total Profit	$523,000	87.2%	$546,100	87.4%	+$23,100	+4.4%

Retention or Flow Thru = $23,100 or 92.4% ($23,100/$25,000)

The forecast for the Rooms Department was $600,000 in room revenue and a $523,000 Rooms Department Profit. The forecasted profit percentage is 87.2%, which means that .872 cents out of every revenue dollar will be profit. Actual Room Revenue was $625,000, or $25,000 over forecast. Therefore, incremental revenue was $25,000. We can also calculate the percentage increase of the $25,000 incremental revenue, which is +4.2% ($25,000/$600,000). In other words, revenues were 4.2% higher than forecast.

Now let's look at the increase in expenses that resulted from the $25,000 incremental revenue. Fixed expenses did not change, so the incremental $25,000 in revenue incurred no additional fixed expense. Fixed expenses remained at $13,000. The fixed expense percentage will therefore decrease from 2.2% to 2.1%. This percentage decreases because the revenue increased without a corresponding increase in fixed expenses. We can therefore assume that for every incremental dollar increase in revenue, there will be no incremental increase in fixed expenses.

Variable expenses have a direct relationship with revenue—when revenue goes up, variable expenses should go up; when revenue goes down, variable expenses should go down. It is the department manager's ability to control and manage variable expenses such as labor costs that can have a positive or negative effect on profits. In our example, variable expenses increased $1,900, or 3.0%. This was the incremental amount of variable expenses incurred to support the $25,000 and 4.2% increase in room revenue. The variable cost percentage declines slightly from 10.6% to 10.5%.

The resulting profit increases $23,100 from $523,000 to $546,100, or +4.4%. The incremental revenue of $25,000 generated an incremental profit of $23,100. Stated in terms of percentages, 92.4% ($23,100/$25,000) of the incremental revenue of $25,000 resulted in an incremental profit of $23,100. This is a very high percentage and would indicate that the managers did a good job in controlling expenses.

The financial concept of retention or flow thru involves setting guidelines for the expected amount and percentage of incremental profit that will result from incremental revenue. Two examples of hospitality company standards are a 60% retention of incremental profits at Hotel Gross Operating Profit and the other is 50% flow thru at Hotel House Profit. The 60% retention standard would expect $15,000 of incremental profit and the 50% flow thru standard would expect $12,500 of incremental profits. In our example, the rooms department managers exceeded the guidelines by producing +$23,100 in incremental profits.

Keep in mind that the retention and flow thru standards are for Gross Operating Profit or House Profit. There are also specific department standards. For example, the rooms department retention standard is 80%, and the food and beverage department retention standard is 55% for one hotel company. The 92.4% actual retention in our example exceeded the room retention standard of 80%.

All department managers are responsible for controlling and managing expenses to achieve guidelines and standards. It is equally important for the Director of Engineering to control the repairs and maintenance expenses as it is for the Restaurant Manager and Housekeeping Manager to control the expenses of their departments. If each department does its part in managing expenses, the overall hotel productivity as measured by Gross Operating Profit or House Profits will achieve the goals and standards set.

Monthly P&L Statement Critiques

This refers to the process of analyzing the monthly department and consolidated P&Ls to evaluate the financial performance and to determine what action to take next. The critiques should be prepared by department heads and line managers and reviewed by the Director of Finance and Executive Committee member. The objective is to evaluate the numbers and explain what happened, why it happened, and what action will be taken as a result of the analysis. It is equally important to identify positive changes in revenues and profits *as well as* negative changes in revenues and profits.

The department P&L critique involves a narrative that identifies major variations and explains the causes of the variations in the accounts on the department P&L Statement. The focus should be on the largest dollar accounts and the largest variations from budget or forecast in terms of dollars and percentages. For example:

1. If revenues increased or decreased, which market segments or meal periods had the largest variation? Was it in rate or volume? Was it in one week or each of the weeks in the month?
2. If food or beverage costs increased, did the increase originate in the full-service restaurant, specialty restaurant, or banquet department? What caused the cost increase, and how will it be corrected?
3. If wage cost increased, did the increase originate in housekeeping or the front office for the rooms department? Did it originate in the restaurant, banquets, or kitchen for the restaurant department? Was it caused by increased labor hours or wage rates? What was the cause of the increase?
4. If other operating costs increased, which account reflected the increase? What caused the increase? How will it be corrected?

The Department P&L critique explains what happened and how the department will improve operations in the next months. It is important to remember that identifying the cause of increased revenues and profits is just as important as identifying the cause of problems that decrease profits. The department manager will want to know what actions produced the improvements and do what she or he can to keep those procedures or actions in place so that the improved operations will continue.

Summary

Internal management reports are essential to the successful operations of any hotel or restaurant. The entire hotel or restaurant management team uses these internal reports to evaluate past performance and to determine appropriate action to take in the upcoming months to ensure acceptable performance in the future. This is the third step in the Financial Management Cycle—operations and accounting analyze the numbers. Department heads and line managers implement and critique these reports with the assistance of the Director of Finance and their Executive Committee member.

Internal management reports cover two time periods. The first report contains actual operations from the previous day, week, or month. This looks back at completed operations and describes what has happened. The second forecasts revenues, expenses, and profits for the upcoming day, week, or month and is used to plan for expected business levels in the future. This report looks forward and forecasts what the managers expect and plan to happen.

There are daily, weekly, monthly, and quarterly reports. Although operations are managed daily, they are planned for in weekly forecasts and schedules. The monthly reports are the main financial reports and are used by both internal managers and external parties or stakeholders in the hotel's operations.

It is extremely important to understand the concepts of incremental revenues and the expected impact that changes in revenue will have on retention or flow thru to profits. These terms describe the guidelines set for managers to assist them in controlling expenses and maintaining expected productivities. Because some expenses are fixed, there should be no increase in them if revenues increase. That will have a positive effect on profitability. Likewise, there is no decrease in fixed expenses if revenues decline. This will have a negative effect on profitability. All department managers are expected to manage their variable expenses whether revenues increase or decrease.

Hospitality Manager Takeaways

1. **The ability of hospitality managers to understand and use internal management reports is essential to the successful operation of any department.**
2. **The Daily Revenue Report summarizes the previous day's results and can include revenues, statistics, and labor productivities. This is one of the most important management tools that a manager can use.**
3. **Weekly reports are used for planning and scheduling upcoming operations.**
4. **Retention and flow thru are essential financial concepts that identify management's ability to control expenses given incremental changes in revenues. This is a direct responsibility of department managers.**
5. **Managing variable wage costs is critical to maintaining productivities and maximizing retention or flow thru.**

Key Terms

Cost Management Index (CMI)—The formula that identifies what level of expenses and profits are expected given incremental changes in revenues.

Fixed Expense—Expenses that remain constant regardless of the volume and level of business.

Flow Thru—Measures how much profit goes up or down as a percentage of the change in revenue.

Incremental—An increase, something gained or added. In financial analysis it describes additional revenues, expenses, or profits beyond what was expected.

Retention—Same as Flow Thru.

Variable Expense—Expenses that increase or decrease directly with the volume and level of business.

Variation—Something slightly different from another of the same type. In financial analysis, variation is the difference between a planned number and an actual number—for example, the difference between actual results and budget.

Review Questions

1. Compare the format of a P&L Statement with a Daily Revenue Report. What is the same and what is different?
2. What information does the Daily Revenue Report contain, and how does a hospitality manager use it?
3. Explain how fixed and variable wage expenses are used to maintain labor productivity standards.
4. How are weekly revenue forecasts used to plan expenses for the upcoming week?
5. Define *retention* and *flow thru*. Why they are important?
6. How do department managers use retention and flow thru to manager their departments?
7. Define *incremental*. How is it used in financial analysis?
8. List three formulas for calculating labor productivities and percentages.