The New Lodging Scoreboards The Uniform System of Accounts for the Lodging Industry

FOCUS: The Summary Statement of Income

by Raymond S. Schmidgall, Ph.D, CHAE

Editor's Note: This article is the third in a series reviewing various aspects of the Uniform System of Accounts for the Lodging Industry, Ninth Revised Edition.

The income statement reflects the results of operations and is prepared at least monthly for management's use and quarterly and/or annually for outsiders such as owners, creditors, and governmental agencies. The users of the income statement are able to answer many questions, including the following:

- How profitable was the hospitality organization during the most recent month?
- What were the total sales for the period?
- What were the total labor costs for the month?
- What is the relationship between food sales and the cost of food sales?
- How much did sales increase over the same period of the prior year?
- How much was spent to market the lodging operation's services?

These are only a few of the many questions that are answered by reviewing the income statements that cover several periods of time. Further, when the results of operations as shown on the income statement are compared to the numbers in the operating budget, management is able to determine how well the lodging entity is meeting its financial objectives!

This article presents the major elements of the income statement. It discusses the various sections of the prescribed format for internal use, and a section of the article is devoted to highlighting changes in the Summary Statement of Income prescribed by the ninth edition of the *Uniform System of Accounts for the Lodging Industry (USALI).*

Major Elements of the Income Statement

The income statement reflects the revenues, expenses, gains, and losses for a period of time. *Revenues* represent the inflow of assets, reduction of liabilities, or a combination of both resulting from the sale of goods or services. For a lodging operation, revenues generally include room sales, food sales, beverage sales, telephone sales, interest income from investments, and rents received from lessees of retail space.

Expenses are defined as the outflow of assets, increase in liabilities, or a combination of both in the production and rendering of goods and services. Expenses of

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Exhibit 1 - Statement of Income Format for External Use

	Period	
	Current Year	Prior Year
Revenue		
Rooms	$	$
Food		
Beverage		
Other		
Total Revenue		
Costs and Expenses		
Rooms		
Food		
Beverage		
Administrative and General		
Interest Expense		
Depreciation and Amortization		
Total Costs and Expenses		
Income Before Income Taxes		
Income Taxes		
Current		
Deferred		
Total Income Taxes		
Net Income	$	$

a lodging operation generally include cost of goods sold (for example, food and beverages), labor, utilities, advertising, depreciation, and taxes, to list a few.

Gains are defined as increases in assets, reductions in liabilities, or a combination of both resulting from the lodging operation's incidental transactions and from all other transactions and events affecting the operation during the period, except those that count as revenues or investments by owners. For example, there may be a gain on the sale of equipment. Equipment is used by the business to provide goods and services and, when sold, only the excess proceeds over its net book value (purchase price less accumulated depreciation) are recognized as gain.

To illustrate this point the following example is provided:

The Sunset Inn has just sold the van it has used to transport guests for the past three years. The van was sold for $6,000. It originally cost $25,000 and was depreciated by $20,000 over its three year life. The gain on the sale is $1,000 determined as follows:

Selling price		$6,000
Less:		
Cost	$25,000	
Accumulated Depreciation	20,000	
NBV		5,000
Gain on Sale		$1,000

Statements of Income for External and Internal Users

Lodging organizations prepare income statements for both external and internal users. These statements differ in the amount of financial information presented. The statement presented to external users is relatively brief as it provides only summary detail about the results of operations. The *USALI* contains two sample formats of statements of income for external users. The shortest of the two is shown in Exhibit 1.

The degree of detail presented in the statement of income is somewhat discretionary although the following captions—revenue, expenses, interest, depreciation and income taxes—should be shown unless the amounts are insignificant. Any significant individual items should be separately disclosed. Footnotes to provide supplementary information to the statement of income and other financial statements are also required.

Although the amount of operating information shown in the statement of income and accompanying footnotes may be adequate for external users to evaluate the lodging property's operations, management requires considerably more in-

formation. Management also needs this information more frequently than outsiders. In general, the more frequent the need to make decisions, the more frequent the need for financial information. Management's information needs are often met, in part, by detailed monthly income statements that reflect budget numbers and report performance for the most recent period, the same period a year ago, and year-to-date numbers for both the current and past years.

If major differences between the year-to-date numbers and the originally budgeted numbers are expected, the income statements of many firms in the lodging industry also show the latest forecast of results (re-forecasting). Management is then able to compare actual results against the most recent forecasts.

Management's need for financial information on a monthly basis may be met, to a large degree, by using an income statement and accompanying departmental statements that are contained in the *USALI*.

Contents of the Statement of Income

This section of the article focuses on the prescribed format of the summary statement of income prepared for internal use as shown in Exhibit 2.

The income statement per the *USALI* is divided into three major sections—operated departments, undistributed operating expenses, and the final section which includes management fees, fixed charges, gain or loss on sale of property, and income tax.

The first section, operated departments, reports net revenue by department for every major revenue-producing department. Net revenue is the result of subtracting allowances from related revenues. Allowances include refunds and overcharges at the time of sale that are subsequently adjusted. For example, hotel guests may have been charged $150 for their rooms when they should have been charged a group rate of $120. The subsequent adjustment of $30 is treated as an allowance. Revenues earned from nonoperating activities such as investments are shown with rentals on the lines "Rentals and Other Income." If individual amounts included are significant, they should be reported separately.

For each department generating revenues, direct expenses are reported. These expenses relate directly to the department incurring them and consist of three major categories: cost of sales, payroll and related expenses, and other expenses. Cost of sales is normally determined as follows:

	Beginning inventory
Plus:	Inventory purchases
Equals:	Goods available for sale
Less:	Ending inventory
Equals:	Cost of goods consumed
Less:	Goods used internally
Equals:	Cost of goods sold

Cost of sales is determined by starting first with beginning inventory. The beginning inventory is the value of the inventory at the start of the accounting period. Inventory purchases include the purchase cost of goods for sale plus the related shipping cost. An important, but relatively small, category of direct expense is "goods used internally." For example, food may be provided free of charge to employees (employee meals), to entertainers (entertainers—complimentary food), to guests for promotional purposes (promotion—food), or to other departments (transfers to the beverage department). In each case, the cost of food transferred must be charged to the proper account of the benefitting department and subtracted to determine the cost of food sold. For example, cost of employee meals for the rooms department is subtracted to determine cost of food sold. The cost of employee meals for rooms department employees is shown as an expense on the rooms department schedule.

The second major direct expense category of operated departments is "payroll and related expenses." This category includes the salaries and wages of employees working in the designated operated departments (for example, room attendants in the rooms department). Salaries, wages, and related expenses of departments not generating revenues but providing service, such as marketing, are recorded by service departments. The category of "related expenses" includes all payroll taxes and benefits relating to employees of each operated and service department. For example, in the rooms department, the front office manager's salary and related payroll taxes and benefits would be included in the "payroll and related expenses" of the rooms department.

The final major expense category for the operated departments is "other expenses." This category includes only other direct expenses. For example, the 14 major other expense categories for the rooms department (see Exhibit 3 from the *USALI*) are cable/satellite television, commissions, complimentary guest services, contract services, guest relocation, guest transportation, laundry and dry cleaning, linen, operating supplies, reservations, telecommunications, training, uniforms, and other. Expenses such as marketing, administration, and transportation are recorded as expenses of service departments. They benefit the rooms department and other operating departments, but only on an indirect basis.

Net revenue less the sum of cost of sales, payroll and related expenses, and other expenses results in departmental income or loss. The departmental income or loss is shown on each operated department's schedule. The schedule column on the Summary Statement of Income (Exhibit 2) references the departmental schedule. For the rooms operation the schedule is simply numbered "1."

The second major section of the statement of income is undistributed operating expenses. This section includes nine general categories: administrative and general expenses, human resources, information systems, security, marketing, franchise fees, transportation, property operation and maintenance, and utility costs. These expense categories are related to the various service departments. In the income statement two of the expense elements—payroll and related expenses, and other expenses—are shown for each category. Each of these nine general categories will be briefly discussed. The administrative and general expense category includes service departments such as the general manager's office and the accounting office. In addition to salaries, wages, and related expenses of service department personnel covered by administrative and general, other expenses include, but are not limited to, credit and commissions, professional fees, and provision for doubtful accounts. The administrative and general statement will be provided and discussed in detail in an article in a subsequent issue of *The Bottomline*.

The *USALI* recommends a separate departmental accounting of information systems expenses for those lodging op-

Exhibit 2 - Summary Statement of Income (Internal Use)

Operated Departments	Schedule	Net Revenues	Cost of Sales	Payroll and Related Expenses	Other Expenses	Income (Loss)
Rooms	1	$	$	$	$	$
Food	2					
Beverage	3					
Telecommunications	4					
Garage and Parking	5					
Golf Course	6					
Golf Pro Shop	7					
Guest Laundry	8					
Health Center	9					
Swimming Pool	10					
Tennis	11					
Tennis Pro Shop	12					
Other Operated Departments	13					
Rentals and Other Income	14					
Total Operated Departments						
Undistributed Operating Expenses[1]						
Administrative and General	15					
Human Resources	16					
Information Systems	17					
Security	18					
Marketing	19					
Franchise Fees	19a					
Transportation	20					
Property Operation and Maintenance	21					
Utility Costs	22					
Total Undistributed Operating Expenses						
Totals		$	$	$	$	
Income After Distributed Operating Expenses						
Management Fees	23					
Rent, Property Taxes, and Insurance	24					
Income Before Interest, Depreciation and Amortization and Income Taxes[2]						
Interest Expense	25					
Income Before Depreciation, Amortization and Income Taxes						
Depreciation and Amortization	26					
Gain or Loss on Sale of Property						
Income Before Income Taxes						
Income Taxes	27					
Net Income						$

[1]A separate line for preopening expenses can be included if such costs are captured separately.
[2]Also referred to as EBITDA—Earnings before Interest, Taxes, Depreciation and Amortization.

erations with significant investments in information systems. As with most of the other service centers, the two major sections of expense are payroll and related expenses, and other expenses. If information systems expenses are not considered significant, then the *USALI* recommends information systems expenses be included as part of administrative and general expenses.

Another service center for which the *USALI* recommends separate departmen-

Exhibit 3 - Rooms—Schedule 1

	Current Period
Revenue	$
Allowances	_____
Net Revenue	
Expenses	
Salaries and Wages	
Employee Benefits	_____
Total Payroll and Related Expenses	_____
Other Expenses	
Cable/Satellite Television	
Commissions	
Complimentary Guest Services	
Contract Services	
Guest Relocation	
Guest Transportation	
Laundry and Dry Cleaning	
Linen	
Operating Supplies	
Reservations	
Telecommunications	
Training	
Uniforms	
Other	_____
Total Other Expenses	_____
Total Expenses	_____
Departmental Income (Loss)	$_____

tal accounting is the human resources department. This schedule includes labor costs of departmental personnel and other expenses such as employee housing, recruiting expenses, costs of relocating employees, and training costs. If human resource expenses are not considered significant, then the *USALI* recommends they be reported as part of the administrative and general expenses.

The fourth service department is security. The purpose of this service department is to provide security services for the lodging facility and the guests. The expenses to be included on the security department schedule include payroll and related expenses, and other expenses such as armored car service, operating supplies, safety and lock boxes, and training. If security expenses are not considered significant, then the *USALI* recommends security expenses be included as part of the administrative and general expenses.

Marketing expenses include costs relating to personnel working in marketing areas of sales, advertising, and merchandising. In addition, other marketing expenses include advertising and merchandising expenses such as direct mail, in-house graphics, point-of-sale materials, and print, radio, and television advertising. Agency fees and other fees and commissions are also included as marketing expenses. Franchise fees, when applicable and significant, should be listed as a separate line item on the summary statement of income. If the franchise fees are insignificant, they would be included as part of the marketing expenses.

The transportation service department provides transportation services for lodging guests, such as transportation to and from the airport. The expenses to be included on the transportation department schedule include payroll and related expenses, and other expenses such as fuel, operating supplies, and repairs and maintenance. If guest transportation expenses are not considered significant, then the *USALI* recommends transportation expenses be included as part of the rooms department expenses.

The eighth major category of undistributed operating expenses is property operation and maintenance. Included in property operation and maintenance are salaries and related payroll costs of the property operation and maintenance personnel and the various supplies used to maintain the buildings, grounds, furniture, fixtures, and equipment.

The final category of undistributed operating expenses is utility costs. The recommended schedule includes separate listings of the various utilities, such as electricity and water. Sales by the hotel to tenants and charges to other departments are subtracted in determining net utility costs.

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Subtracting the total undistributed operating expenses from the total operated departments' income results in income after undistributed operating expenses. Many industry personnel continue to refer to this difference between operating revenue and expense as gross operating profit, or simply GOP, but this is terminology from an earlier edition of uniform system of accounts for hotels.

Operating management is considered fully responsible for all revenues and expenses reported to this point on the summary statement of income, as they generally have the authority to exercise their judgment to affect all these items. However, the management fees and the fixed charges that follow in the next major section of the income statement are the responsibility primarily of the hospitality property's board of directors. The expenses listed on this part of the statement generally relate directly to decisions by the board, rather than to management decisions.

Management fees are the cost of using an independent management company to operate the hotel or motel. Management fees often consist of a basic fee calculated as a percentage of sales and an incentive fee calculated as a percentage of income after undistributed operating expenses.

Fixed charges are also referred to as *capacity costs,* as they relate to the physical plant or the capacity to provide goods and services to guests. Fixed charges include rent, property taxes, insurance, interest, and depreciation and amortization. Rent includes the cost of renting real estate, computer equipment, and other major items that, if they had been purchased, would have been recorded as fixed assets. Rental of miscellaneous equipment for specific functions such as banquets is to be shown as a direct expense of the food and beverage department.

Property taxes include real estate taxes, personal property taxes, taxes assessed by utilities, and other taxes (but not income and payroll taxes) that cannot be charged to guests. Insurance includes the cost of insuring the property's building and its contents against fire, weather, and similar causes. In addition, the costs of general insurance including premiums for liability, fidelity, and theft are also included as insurance expense.

Interest expense is the cost of borrowing money and is based on the amounts borrowed, the interest rate, and the length of time for which the funds are borrowed. Generally, loans are approved by the operation's board of directors, as most relate to the physical plant. Thus, interest expense is considered to be a fixed charge.

Depreciation of fixed assets and amortization of other assets are shown on the income statement as fixed charges. The depreciation methods and useful lives of fixed assets are normally disclosed in footnotes.

The summary statement of income per the *USALI* then shows gains or losses on the sale of property and equipment. A gain or loss on sale of property results from a difference between the proceeds from the sale and the carrying value (net book value) of the fixed asset. In the *USALI*'s income statement, gains are added while losses are subtracted in determining income before income taxes.

Finally, income taxes are subtracted from income before income taxes to determine net income.

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It's part of a series of articles in Bottomline Magazine on the *Uniform System of Accounts for the Lodging Industry*

The first edition of the Uniform System of Accounts was published in 1926 by the Hotel Association of New York City, the founding chapter of the IAHA, now called the Hospitality Financial and Technology Professionals; and it was published well before the proliferation of computers.

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Major Changes in the Summary Statement of Income

The changes in the Summary Statement of Income as recommended in the ninth revised edition of the *USALI* are fairly minor. In the prior edition food and beverage operations were reported on a single line, whereas they are shown separated in the ninth revised edition. The undistributed operating expenses section of the statement has been expanded to include separate line items for security and franchise fees. In addition, minor changes in terminology in this section include the use of information systems in place of data processing and the use of utility costs to replace energy costs. The prior edition had a separate line item for guest entertainment which has been dropped from the ninth revised edition.

The difference between total operated department income and the total undistributed operating expenses is called income after undistributed operating expenses. Finally, a separate line has been inserted in the fixed charges section of The Summary Statement of Income for EBITDA.

Summary

The Summary Statement of Income reflects the revenues, expenses, gains, and losses of the lodging property. The statement is considered to be dynamic as it covers a period of time rather than simply a point of time like the balance sheet. The statement consists of three major sections:

- operated departments
- undistributed operating expenses
- non-operating elements

The operated departments section reveals the net revenue, cost of sales, payroll and related expenses, other direct expenses, and income (loss) for each operated department. The payroll and related expenses, other direct expenses, and total expenses are shown for each service center included in the undistributed operating expenses of this statement. The final section includes management fees, fixed charges, gain or loss on sale of property, and income taxes. These items are either the result of ownership decisions (management fees and fixed charges) or are not directly related to operations (gain or loss on sale of property and income).

The next article covering the new financial scoreboards will cover the department schedules which supplement the Summary Statement of Income. ▪

The ninth revised edition of the Uniform System of Accounts for the Lodging Industry is available from the Educational Institute of the American Hotel & Motel Association at 800-752-4567. The cost is $55.95.

How to Staff Table Games

(continued from page 12)

62	93.0	82.7	77.5
64	96.0	85.3	80.0
66	99.0	88.0	82.5
68	102.0	90.7	85.0
70	105.0	93.3	87.5
72	108.0	96.0	90.0
74	111.0	98.7	92.5
76	114.0	101.3	95.0
78	117.0	104.0	97.5
80	120.0	106.7	100.0
82	123.0	109.3	102.5
84	126.0	112.0	105.0
86	129.0	114.7	107.5

Conclusion

This article addressed how unique staffing is in the table game area of the casino. The authors reviewed how to determine table games open and the stations required. Furthermore, the authors reviewed how to staff dealers in regards to a five-day work week, how to account for vacations, and how to staff floorpersons. ▪

SOURCES
Kilby, Jim. 1998. Casino Management and Operations. New York: John Wiley Publishers.

Capital vs. Revenue Expenditures: A Survey of the Lodging Industry

(continued from page 17)

- caulking (94 percent)
- repairing signs (93 percent)
- plumbing repairs (92 percent)
- repairs of swimming pool leaks (89 percent)
- regrouting tile (89 percent)
- painting (83 percent)
- normal roof repairs (83 percent)
- repairing swimming pool deck (73 percent)

Expenditures in which respondents were split included:

- reupholstering (59 percent expensed, 41 percent capitalized)
- repairs and major overhauls of existing equipment (55 percent expensed, 45 percent capitalized)
- boiler re-tubing (54 percent expensed, 46 percent capitalized)

A Need For Guidance

Nearly three-quarters of the respondents (74 percent) agreed that guidelines should be established to address the expenditures discussed above. Over one-third (34 percent) responded that Hospitality Financial and Technology Professionals should provide such guidance, 18 percent expected the FASB to respond, 15 percent expected the AICPA to respond, 8 percent looked to the lodging industry, 3 percent anticipated guidance from other sources, and 22 percent believed more than one of the above mentioned parties should provide guidance. In the meantime, hotel financial executives will have to rely on their gut instincts and studies such as this to make decisions on these gray matters. Thank goodness we accountants look good in gray! ▪

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