



Hospitality Management
Essentials Series

ACCOUNTING AND FINANCIAL ANALYSIS IN THE HOSPITALITY INDUSTRY

Jonathan A. Hales

Series Editor: Hubert B. Van Hoof

ACCOUNTING AND FINANCIAL ANALYSIS IN THE HOSPITALITY INDUSTRY

Jonathan A. Hales

Northern Arizona University



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*To my family—Judy, Laura, and David, my parents Lynn
and Eleanor Hales, and Ben Bearden*

FOREWORD

Accounting and Financial Analysis in the Hospitality Industry by Dr. Jonathan A. Hales is the first text in the new Pearson series *Hospitality Management Essentials*. Dr. Hales served as a controller, resident manager, and general manager for the Marriott Corporation in nine different hotels for 25 years, prior to moving into higher education in 1995. Not only does Dr. Hales know exactly what students and entry-level managers need to be aware of when it comes to managerial accounting, he also has the educational expertise to convey this knowledge in a very applied and easy-to-understand format. He teaches this subject every day and has incorporated the comments of many of his colleagues around the country in the text.

The Pearson series *Hospitality Management Essentials* is designed to cover all aspects of the management of hospitality enterprises from an *applied perspective*. Each book in the series provides an introduction to a separate managerial function such as human resources or accounting; a distinct management segment in the hospitality industry such as club management, resort management, or casino management; or looks at other topic areas closely related to hospitality management, such as information technology, ethics, or services management.

The books in the series are written for students in two- and four-year hospitality management programs, as well as for entry- and mid-level managers in the hospitality industry. They present readers with three essential features they are looking for in textbooks nowadays: they are *affordable*, they are of *high quality*, and they are *applied*, and their approach to hospitality management issues appeals to students and instructors alike. The authors in the series are selected because of their classroom and industry expertise and experience and their ability to make complex materials easy to understand. As with Dr. Hales, they all enjoy sharing those experiences with the aspiring hospitality managers of the twenty-first century.

Students and educators alike will find affordability, relevance, and high quality in this and all other texts in the series. As we say in the hospitality industry: welcome and enjoy!

Hubert B. Van Hoof, Ph.D.

Series Editor

PREFACE

This textbook is written for college students in two- and four-year programs. The objective is to provide hospitality students with a solid foundation of accounting concepts and methods of financial analysis that he or she will need to possess to be successful in their hospitality industry careers. This book can also be used by any hospitality manager who has operations responsibilities in a hotel, restaurant, or any other business. It is not a textbook for accounting majors as it does not contain the details, procedures, processes, and requirements to prepare financial information to meet established accounting and reporting guidelines.

Most hospitality accounting textbooks provide too much accounting information that is very complicated and difficult for college students to understand. More importantly, hospitality managers responsible for operating Rooms Departments or Food and Beverage Departments will never use that kind of accounting information in their daily operations. However, accountants and financial managers do need to understand and use this detailed information to prepare management reports and financial statements to conform to established standards and requirements. Hospitality operations managers just need to understand the accounting basics and be able to use them in performing and evaluating their job responsibilities.

Hospitality students need to have a fundamental understanding of using numbers in order to operate their departments and analyze management reports and financial statements. This textbook focuses on the following important goals in teaching hospitality accounting:

1. Presenting students with a solid foundation of fundamental accounting concepts and methods of financial analysis.
2. Teaching students to understand numbers and to enable them to use numbers in performing their managerial responsibilities more effectively.
3. Assisting students in understanding that using financial analysis to evaluate business operations involves basic arithmetic and fundamental formulas and need not be complicated and overwhelming.
4. Teaching students to understand that numbers resulting from operations are used as a management tool and as measures of financial performance.
5. Enabling students to apply accounting concepts and methods of financial analysis in managing their departments and understanding and evaluating financial statements.

I wrote this book based on how I have taught Hospitality Managerial Accounting at Northern Arizona University the last ten years. The examples, exercises, and materials included in the book are based on what hospitality students need to know about accounting and financial analysis to be successful. Directors of Finance for several major hotel companies have reviewed a major portion of this book's content. Their input was instrumental in enabling this textbook to be current and consistent with the actual accounting processes and procedures

used in today's hospitality industry. I appreciate their willingness to share detailed information about their management reports, financial statements, and operational procedures, as well as their expectations of what graduating seniors should know and understand about accounting concepts and financial analysis to be successful managers.

The fact that most students are intimidated by and afraid of working with numbers greatly influenced the way the contents are presented. Often, students just get by in accounting classes, are relieved that they have passed, and are happy that it is over, rather than use the class as an opportunity to learn important information about accounting and financial analysis that will help them in their careers. This textbook seeks to reduce students' fears and anxieties by focusing on the fundamentals of using numbers to operate a business. The objective is not to teach them to prepare financial reports or make them understand the complexities of the accounting discipline, but to enable them to understand and use management reports and financial statements to help them operate their departments.

CHAPTER DESCRIPTION

Chapters 1 and 2 are written to provide an introduction to accounting and to provide a solid foundation of accounting concepts and methods of financial analysis. The focus is on the fundamentals of using numbers as a management tool and to measure financial performance in hospitality operations.

Chapter 3 explains organization charts for hotels and for the accounting Department and how they establish accountability and responsibility for operating results and financial performance. This is intended to help hospitality students understand how accounting department operations fit into hotel operations and how they can help hospitality managers operate their departments.

Chapters 4 and 5 explain the three main financial statements used in financial analysis. **Chapter 4** discusses the importance of Consolidated and Department P&L Statements in successfully understanding and managing hospitality operations and the financial results that they produce. **Chapter 5** discusses the important aspects of Balance Sheets and the Statement of Cash Flows in operating a hospitality business. These chapters also discuss how the three statements interrelate by organizing and presenting the financial results of a business.

Chapters 6–8 discuss the hotel management reports that are used as management tools and as measures of financial performance. **Chapter 6** provides examples of daily revenue and labor reports that hospitality managers review daily and weekly. **Chapter 7** focuses on revenue management and discusses its importance in maximizing total hotel revenues and profits. Variation analysis and comparative reports are presented in **Chapter 8**. It also discusses how they are used to measure and understand financial performance. The purpose of these three chapters is to introduce students to the actual use, application, and analysis of financial statements and management reports in the operations of departments within a hotel or restaurant. The focus is to present accounting and

financial information that students will need to know and be able to use in managing their departments on a daily and weekly basis.

Chapters 9 and 10 emphasize the importance of budgeting and forecasting as management tools and as ways to measure financial performance. The different types of budgets and how to prepare annual operating budgets are discussed in **Chapter 9**. Forecasting revenues and scheduling wages are two important responsibilities of hospitality managers and **Chapter 10** provides detailed exercises to practice forecasting revenues and scheduling wages. These chapters focus on the importance of a manager's ability to review current operations and to prepare weekly forecasts that update the budget and reflect current market conditions.

Chapters 11 and 12 are intended to provide students with additional knowledge to broaden their financial skills and understanding. **Chapter 11** introduces Corporate Annual Reports and familiarizes students with their content and use. **Chapter 12** focuses on personal financial literacy and is intended to encourage students to apply fundamental financial skills to the management of their personal finances. This includes fundamental financial concepts such as budgeting and planning for today, tomorrow, and for retirement.

The **Glossary** includes over 160 key terms and summarizes the key terms presented in each chapter that students should understand and be able to use in their hospitality careers.

As students read this text and progress through a hospitality managerial accounting course, it is my hope and intent that they will be able to not only learn fundamental accounting concepts but also confidently use them as management tools and to measure the financial performance of their departments. By focusing on accounting fundamentals and building on accounting concepts, students' fears and anxieties of accounting will hopefully be replaced with a solid and useful understanding of accounting that they will be able to use and apply in their hospitality careers.

The textbook is organized in such a way that the fundamentals of accounting concepts and financial analysis are clearly presented. The content is written in a user-friendly manner, avoiding complicated terminology, detailed rules and procedures, and endless spreadsheets. Definitions come from operations or Webster's Dictionary rather than from accounting manuals and complex accounting codes and rules with requirement after requirement.

At the end of each chapter are the following sections:

- Hospitality Manager Takeaways, which highlight how students will apply the material as a hospitality manager.
- Key Terms that are essential for students to understand in working with numbers and that relate to the accounting concepts presented in the chapter.
- Review Questions that reinforce an understanding of the chapter material.
- Practice Exercises that give students the opportunity to use formulas, analyze numbers, and apply the chapter content to examples and problems.

FEATURES OF THE BOOK

The book includes the latest information provided in the 10th Revised Edition of the *Uniform System of Accounts for the Lodging Industry*, published in 2006 by the American Hotel and Lodging Educational Institute. Further, it incorporates the recent changes in format and terminology recommended in the 10th Revised Edition. Students will find the most current lodging accounting information available in this textbook.

Practice exercises are included at the end of each chapter that will provide students the opportunity to work out problems and answer questions that will help them apply and understand the material presented in the chapter. These are basic exercises with the objective of creating a strong foundation of the fundamentals of accounting concepts and financial analysis.

Each chapter has a picture of a hotel, restaurant, or other hospitality operation and a description of that property. Specific questions about material presented in the chapter are asked and applied to the property pictured. This is intended to provide students an opportunity to visualize an actual property and think about how that property would use the accounting concepts and material presented in the chapter. Web sites for these hospitality properties are provided so that students can refer to them and see what that property looks like and consider the accounting processes that support the operation of the property.

As this book was being written, the recession of 2009 was unfolding. The United States and the world had slipped into the deepest recession since the great depression of the 1930s. This provided the opportunity in several chapters to discuss and analyze the impact of such important economic changes on the daily operations and financial performance of businesses in virtually all industries. Dramatic changes in trends and financial history, large and continuous decreases in RevPAR, pressures on profits and cash flows, and significant changes in customer behaviors and market segments have forced hospitality managers to adjust to new trends, patterns, and customer expectations in providing expected products and services to their customers. All of these have also emphasized the importance of understanding and being able to use numbers in operating a hospitality operation or a business in any industry.

SUPPLEMENTS

There is an Instructor's Manual that will provide answers to Chapter Review Questions, Practice Exercises, and the discussion points relating to the hospitality property featured in each chapter. It also includes examples of midterm exams, final exams, and projects. It does not have accompanying PowerPoint slides or Excel programs as I believe that students can best learn accounting fundamentals by doing the actual calculations for the practice exercises. If they have this strong foundation, they will generally be able to understand and work with the systems that companies use in their daily operations.

ABOUT THE AUTHOR

Dr. Jonathan A. Hales spent 25 years with Marriott International, with the first half of that time in the accounting department as Assistant Controller and Controller and the second half in operations as Resident Manager and General Manager. This included working in nine different full-service hotels, including resorts, convention hotels, airport hotels, and corporate hotels ranging from 300 to 800 rooms. This presented him the opportunity to work in different market environments with different management teams in different positions in Washington, DC, New Orleans, Scottsdale, Philadelphia, St. Louis, Palm Springs, Houston, Miami, and Tampa. These many years of working with accounting concepts, management reports, and financial statements have provided Dr. Hales a strong background in how numbers are used to successfully operate a business.

Dr. Hales has been a professor at Northern Arizona University since 1995, teaching a range of classes, including those on front office operations, resort management, hospitality managerial accounting, hospitality finance, and revenue management, and senior seminars. He has completed faculty internships with Four Seasons, Hyatt, Marriott, and Omni Hotels and Darden Restaurants. He has also attended senior management meetings or orientations at Hilton Hotels, White Lodging, and Pappas Restaurants. Keeping up with what companies are doing in the hospitality industry has always been a priority for him.

Dr. Hales' academic background includes a bachelor's degree in Economics and Certificate in International Relations from the University of Utah, graduate business study at the University of Virginia, MBA in Finance from Arizona State University, and a master's and doctorate in Education Leadership from Northern Arizona University.

ACKNOWLEDGMENTS

I would like to acknowledge several hospitality industry leaders who graciously took their time to review specific chapters and make suggestions that greatly improved the material in this textbook. As a result of their contributions, this accounting textbook is current and real and teaches the accounting concepts that hospitality companies expect their managers to know, understand, and apply in operating their departments.

Mark Koehler, Area Director of Finance for Four Seasons Hotels and Resorts in Scottsdale, Arizona, reviewed the entire text and contributed many examples that clearly explain key accounting concepts and their importance in the successful operation of a hospitality department. Mark has been a guest speaker in many of our HRM classes since 2001 and has provided students valuable insight into the actual operations of resort and luxury hotels. His perspectives have made this a more useful textbook for college students.

Tom Forburger, Senior Director of Finance for the J. W. Marriott Desert Ridge Resort and Spa in Phoenix, Arizona, also reviewed the manuscript and provided valuable insight regarding the use of financial statements and what is expected of operating managers in their ability to work with management reports and financial statements. His comments and suggestions helped make the text more consistent with and relevant to the accounting reports and financial analysis that are used on a daily basis in the hospitality industry. Many other industry managers also provided helpful comments regarding the content of the book. They include financial and operations managers with Hyatt, Radisson, White Lodging, and Host Hotels and Resorts on the hotel side, and Pappas Restaurants and Red Lobster Restaurants on the restaurant side. I would like to thank the people at Northern Arizona University who helped make this textbook a reality. Kathleen Krahn took the time to help organize the photographs and make suggestions to convert material to the necessary electronic media. Marc Chopin, Dean of the W. A. Franke College of Business, and Rich Howey, Interim Executive Director of the School of Hotel and Restaurant Management, also provided support and direction that helped make this book a reality.

At Pearson Prentice Hall, Andrea Edwards was of great value to me in reviewing the manuscript, organizing all the necessary components, and guiding me through the initial manuscript submission process. She kept the process on track and I appreciate very much her assistance and support. Bill Lawrensen provided many answers and directions that helped bring this book to publication.

Finally, I would like to thank Bert Van Hoof, Director of the School of Hospitality Management at Penn State University, for inviting me to author a textbook in the hospitality series that he developed. Bert was a colleague at Northern Arizona University before accepting the Director position at Penn State and encouraged me early on to write and publish an accounting textbook.

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