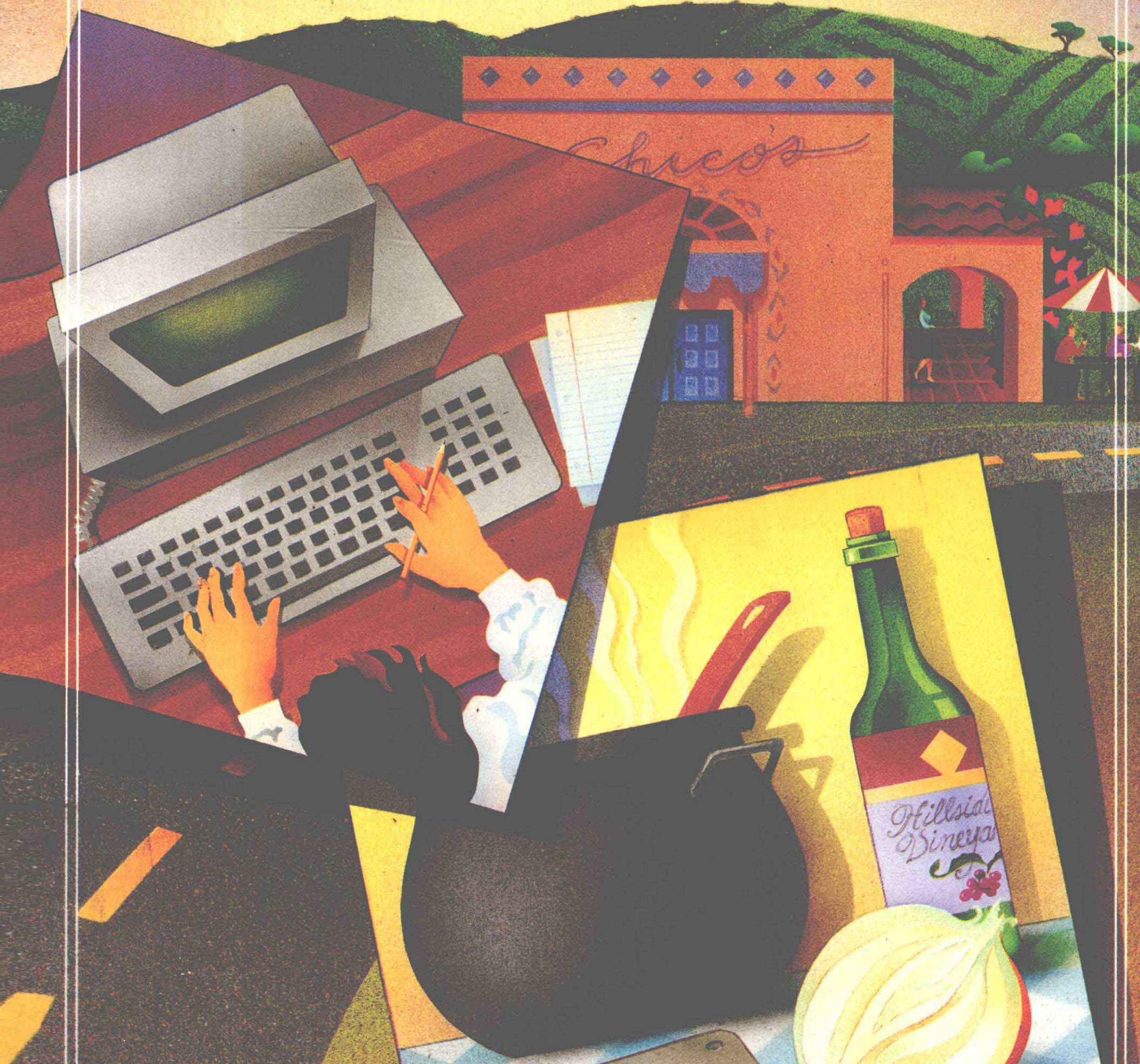
Principles of Food, Beverage, and Labor Cost Controls

Fifth Edition

Paul R. Dittmer • Gerald G. Griffin



PRINCIPLES OF FOOD, BEVERAGE, AND LABOR COST CONTROLS

for Hotels and Restaurants

Fifth Edition

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PRINCIPLES OF FOOD, BEVERAGE, AND LABOR COST CONTROLS

for Hotels and Restaurants

Fifth Edition

For Barbara and Charlene

Preface

This text has been developed for use in courses introducing food, beverage, and labor cost controls to students preparing for careers in food and beverage management. The present edition consists of twenty-two chapters, divided into four parts, as follows.

PART	AREA COVERED	NO. OF CHAPTERS
I	Introduction/overview	4
II	Food cost control	9
III	Beverage cost control	5
IV	Labor cost control	4

Part I offers an introduction to food, beverage, and labor cost controls, defining a number of key terms and concepts and providing a foundation for the balance of the work as well as some sense of its scope. It identifies working definitions for the terms cost and sales, discusses the control process in some detail, and introduces the basics of cost/volume/profit analysis. Finally, it offers some very basic information about computers for those who have not had the benefit of an introductory course.

Part II addresses the application of the four-step control process to the primary phases of foodservice operations: purchasing, receiving, storing, issuing, and production. Specific techniques and procedures for each phase are explained and discussed in detail. Three chapters are devoted to determining costs and using them as monitoring devices in foodservice operations. One chapter deals specifically with food sales control, offering a broad definition of the term and providing detailed discussion of several approaches to sales control.

Part III discusses the application of the four-step control process to the various phases of beverage operations: purchasing, receiving, storing, issuing, and production. Here, too, specific techniques and procedures for each phase are explained and discussed in detail. One chapter is devoted to the principal methods used to monitor beverage operations. The final chapter in Part III specifically addresses beverage sales control, offering a broad definition of the term and providing detailed discussion of several approaches to controlling beverage sales.

Part IV is a four-chapter exposition of labor cost control. The first of the four explores the factors affecting labor cost and labor cost percent. Admittedly, some of these are beyond the control of management, but it is important for managers to know about them. The second chapter discusses the need for performance standards. This leads naturally to a chapter on training, a topic many believe to be central to labor cost control. The concluding chapter in Part IV deals with monitoring performance and taking corrective action.

In developing and revising the text, flexibility has always been a key concern. For example, each of the four parts can generally stand alone. Eliminating any one will not make it difficult to use others. Thus, in programs that include extensive accounting courses, some instructors may choose to disregard Part I. In courses without beverage components, instructors may prefer to skip Part III. And instructors in courses that do not include labor cost control can choose to ignore Part IV.

The book has a greater number of chapters than most instructors use in a one-term course. In our view, this is a virtue, because it provides instructors with opportunities to select chapters dealing with the specific subjects identified in their course outlines. We believe this is the best way to meet the varying needs of instructors in the broad range of courses and programs in this field.

Because a great many chapters include more questions and problems than most will be inclined to assign, instructors will find it easy to make selective use of the end-of-chapter materials for written assignment or for in-class discussion.

ACKNOWLEDGMENTS

In revising this work, we had advice, assistance, cooperation, and support from many people. Without their interest and clear willingness to help, the final product would have been far less than it is. Therefore, we are glad to have this opportunity to acknowledge the considerable aid we have received and to list below the names and affiliations of those who have given it so readily:

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Through the many months required to produce this work, the staff of Van Nostrand Reinhold has been extraordinarily professional, patient, helpful, and supportive in every way. In particular, Judith R. Joseph, Pamela Scott Chirls, Amy B. Shipper, Linda Wetmore, and Sherrel Farnsworth of VNR and Kate Scully of Northeastern Graphic Services have all earned this public acknowledgment of their special efforts on our behalf.

If this edition of the text is successful, proving to be a useful addition to the growing number of professional texts available for those planning careers in food and beverage management, a healthy measure of the credit will be due to the many individuals whose help we have acknowledged above. If not—if the work is somehow off the mark—the authors accept full responsibility for the shortcomings.

Finally, many instructors are likely to be interested in the various additional text-based materials available from **John Wiley & Sons, Inc.** For example, answers for all end-of-chapter questions and problems can be found in the *Instructor's Guide*, along with various other materials designed to assist classroom teachers. In addition, Karen Eich Drummond has prepared an excellent *Student Workbook* that can be adopted by those seeking additional learning aids for their students. The *Instructor's Guide* and an examination copy of the *Student Workbook* are available without charge from the publisher.

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CONTENTS

Introduction to Food, Beverage, and Labor Controls

Cost and Sales Concepts

1

LEARNING OBJECTIVES

After reading and studying this chapter, you should be able to:

1. *Define the terms* **cost** *and* **sales**.
2. *Define and distinguish between various types of costs.*
3. *Describe the significance of cost-to-sales relationships and identify several cost-to-sales ratios important in food and beverage management.*
4. *Perform various calculations using cost percent formulas.*
5. *List and discuss factors that cause industry-wide variations in cost percents.*
6. *Distinguish between monetary and nonmonetary sales concepts.*
7. *Explain the value of comparing current cost-to-sales ratios with those for previous periods.*
8. *Define each of the Key Terms at the end of the chapter.*

INTRODUCTION

The Rush Hour Inn

Until he purchased a restaurant two years ago, Larry Rusher had been a successful salesman of heavy machinery. His annual income was substantial, and he augmented it by investing in some profitable real estate ventures with his brother. However, his job as a salesman required that he travel most of the time, and his feeling that he was a stranger to his own children made him decide to give it up in favor of operating his own business.

On the advice of his brother, he decided to go into the restaurant business, even though he lacked previous experience in the field. After all his years of travel, he felt he knew more about restaurants from the customer's point of view than most restaurateurs. So he began to look around for an appropriate property. Fortunately, he soon found a place just twelve miles from his home, located on a main road on the outskirts of a city of 75,000 people. The building and equipment were only 6 years old and apparently in fine condition, and the retiring owner was anxious to sell at a very fair price. The owner's books revealed a successful operation, with a restaurant profit of approximately $40,000 per year. Larry Rusher decided to buy.

The restaurant had 100 seats. It was open seven days a week, from 6:00 A.M. to 10:00 P.M., serving a varied menu of standard American fare. Larry felt he would be able to run it successfully with the help of his wife and a few loyal employees.

In the first year, Larry's profits were less than those of the previous owner. After two years, profits were continuing to decline. The restaurant was simply not showing an adequate profit, even though he had increased the volume of business over that of the previous owner. The place was reasonably busy, his customers often complimented him on the food, and his employees appeared to be loyal and helpful in every way. The truth was that Larry Rusher was operating a popular, but not very profitable, food and beverage business. At the end of the second full year of operation, the statement of income prepared by his accountant revealed a restaurant profit of $9,870 (Fig. 1.1).

FIGURE 1.1

THE RUSH HOUR INN STATEMENT OF INCOME
For the Year Ended December 31, 19XX

SALES		
Food	$559,300.00	
Beverage	98,700.00	
Total Sales		$658,000.00
COST OF SALES		
Food	$223,720.00	
Beverages	29,610.00	
Total Cost of Sales		$253,330.00
GROSS PROFIT		$404,670.00
CONTROLLABLE EXPENSES		
Salaries and Wages	$157,920.00	
Employee Benefits	39,480.00	
Other Controllable Expenses	98,700.00	
Total Controllable Expenses		$296,100.00
INCOME BEFORE OCCUPANCY COSTS, INTEREST, DEPRECIATION, AND INCOME TAXES		$108,570.00
OCCUPANCY COSTS		60,800.00
INCOME BEFORE INTEREST, DEPRECIATION, AND INCOME TAXES		$ 47,770.00
INTEREST EXPENSE		5,000.00
DEPRECIATION		32,900.00
RESTAURANT PROFIT		$ 9,870.00*

*As a subchapter S corporation, The Rush Hour Inn is not subject to the income taxes that would otherwise appear next on the statement. Restaurant profit from this special type of corporation is reported as income by Larry Rusher on his personal income tax return.

It quickly became apparent to Larry, his family, and his accountant that, unless something could be done to increase the profit, continued operation would not be worth the effort required.

The Graduate Restaurant

Just a few miles down the road from the Rush Hour Inn, Jim Young owns and operates the Graduate Restaurant. After four years in the air force, Jim had worked for an insurance company for a few years before enrolling in a nearby college to study hotel and restaurant management. His interest in the food and beverage sector of the hospitality industry began in his high school days when he worked part time in a famous fast-food chain. While his interest had grown steadily over the years, it took considerable courage for him to give up a fairly promising insurance career to go back to school. He earned a degree in hotel and restaurant management, and then went to work as the assistant manager in a local restaurant. Over the next several years, he worked in three food and beverage operations in the area—the Rush Hour Inn among them—before deciding that he was ready to own and operate his own restaurant.

With the help of his family and a local bank, he was able to purchase the Graduate Restaurant, a fairly popular establishment with the same type of menu as the Rush Hour Inn, as well as comparable prices and hours of operation. In fact, the only differences to the casual observer were size and location: The Graduate Restaurant had only 50 seats and was in a somewhat less favorable location.

Under the previous owner, the restaurant had shown a profit of $18,000 per year. But Jim felt sure he could increase the restaurant profit by applying the principles he had learned in the college's hotel and restaurant management program. The employees he inherited with the restaurant were both loyal and cooperative, and he found them receptive to the changes that he made gradually over the first year of operation. None of the changes were dramatically apparent to the customers; in fact, at the end of the first year, most had not noticed any changes at all. In general, they were as pleased with the establishment as they had been when Jim first took it over, and they continued to return. In addition, newcomers tried the restaurant, liked it, and became regular customers. At the end of the first full year of operation, Jim's accountant presented him with a statement of income showing a restaurant profit of $37,375 (Fig 1.2).

The statement confirmed Jim's expectations. It proved to him that his management of the operation was effective in the ways he had anticipated. At the end of his first year, he looked to the future with confidence.

A comparison of the statements of income for these two restaurants reveals some very important facts. As one might expect, the Rush Hour Inn, with twice as many seats as the Graduate Restaurant, as well as a comparable menu and comparable prices, shows approximately twice the dollar volume of sales.

THE GRADUATE RESTAURANT STATEMENT OF INCOME
For the Year Ended December 31, 19XX

SALES	$276,250.00	
Food	48,750.00	
Beverage		$325,000.00
Total Sales		
COST OF SALES		
Food	$ 96,687.00	
Beverages	12,188.00	
Total Cost of Sales		$108,875.00
GROSS PROFIT		$216,125.00
CONTROLLABLE EXPENSES		
Salaries and Wages	$ 65,000.00	
Employee Benefits	16,250.00	
Other Controllable Expenses	48,750.00	
Total Controllable Expenses		$130,000.00
INCOME BEFORE OCCUPANCY COSTS, INTEREST, DEPRECIATION, AND INCOME TAXES		86,125.00
OCCUPANCY COSTS		27,500.00
INCOME BEFORE INTEREST, DEPRECIATION, AND INCOME TAXES		$ 58,625.00
INTEREST EXPENSE		5,000.00
DEPRECIATION		16,250.00
RESTAURANT PROFIT		$ 37,375.00*

*The Graduate Restaurant is also a subchapter S corporation. Therefore, the restaurant profit is reported as income by Jim Young on his personal income tax return.

FIGURE 1.2

However, in spite of the apparently favorable sales comparison, the restaurant profit for the Rush Hour Inn is only a small fraction of the restaurant profit generated by the Graduate Restaurant. Since the difference between sales and restaurant profit on each statement of income is represented by costs of various kinds, we can infer that some part of the difficulty with the Rush Hour Inn is somehow related to cost. The costs of operation are somehow in more favorable proportion to sales in the Graduate Restaurant. Initially, it is to the nature of these costs and their relations to sales that we must look to uncover the differences between the two establishments. It is possible that the costs of operation are not well regulated, or controlled, in the Rush Hour Inn. It is also possible that sales are not well controlled and that, if Larry Rusher is going to increase his profit to a desirable level, he must begin by exercising greater control over the several kinds of operating costs, as well as over sales.

The statement of income from the Graduate Restaurant suggests that Jim Young has kept both costs and sales under control, and, as we shall see, this is critically important to the success of his business. Comparative investigation of the two restaurants would reveal that Jim Young had instituted various control procedures in the Graduate Restaurant that would be noticeably absent in Larry Rusher's business. These have enabled Jim to manage his business more effectively. It will be important, therefore, to look closely at the nature and effect of these control procedures in succeeding chapters. However, before proceeding, it will first be useful to establish clear definitions of the terms **cost, sales,** and **control.** Cost and sales will be defined and discussed in this chapter; control will be covered in Chapter 2.

COST CONCEPTS

Definition of Cost

Accountants define a **cost** as a reduction in the value of an asset for the purpose of securing benefit or gain. That definition, while technically correct, is not very useful in a basic discussion of controls, so we will modify it somewhat.

As we use the term in our discussion of cost control in the food and beverage business, cost is defined as *the expense to a hotel or restaurant of goods or services when the goods are consumed or the services rendered.*

Foods and beverages are considered "consumed" when they have been used, wastefully or otherwise, and are no longer available for the purposes for which they were acquired. Thus, the cost of a piece of meat is incurred when the piece is no longer available for the purpose for which it was purchased because it has been cooked, served, or thrown away because it has spoiled, or even because it has been stolen. The cost of labor is incurred when people are on duty, whether or not they are working and whether they are paid at the end of a shift or at some later date.

The cost of any item may be expressed in a variety of units: weight, volume, or total value. The cost of meat, for example, can be expressed as a value per piece, per pound, or per individual portion. The cost of liquor can be expressed as a value per bottle, per drink, or per ounce. Labor costs can be expressed as value per hour (an hourly wage, for example) or value per week (a weekly salary).

Costs can be viewed in a number of different ways, and it will be useful to identify some of them before proceeding.

Fixed and Variable Costs

The terms **fixed** and **variable** are used to distinguish between those costs that have no direct relationship to business volume and those that do.

FIXED COSTS. Fixed costs are those that are normally unaffected by changes in sales volume. They are said to have little direct relationship to the