MANAGEMENT ACCOUNTING FOR HOSPITALITY AND TOURISM

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Management accounting is concerned with the provision and use of accounting information to managers within organizations, to assist management making decisions and managerial control functions.

This paper examines the ways in which internally generated information is recorded and reported for management decision making, and how these records and reports can be used to improve or maximize the profitability of organizations for their shareholders. Also, is distinguish between expenses and costs, is define the three main components of costs, is calculate the total cost of o product or service. Traditionally management accounting is concerned of the recording, measuring and control of costs and the paper covered how it possible to build up a full cost for a product or service. The essential difference between expenditure and cost is the distinction between what expenditure is generated and where it is consumed and is indicative of the difference between financial accounting perspective and the management accounting perspective.

Key words: *Management Accounting, Expenses, Cost, Total Cost*

Management accounting is concerned with measuring and providing operational and financial information that guides managerial action, motivates behavior, and supports and creates the cultural values necessary to achieve an organization's strategic objectives.

Unlike financial accountancy information (which, for the most part, is public information), management accounting information is used within an organization and is usually confidential. Contemporary managerial accounting systems are focusing more on the activities that occur at all levels of the organization.

As the hospitality industry continues to grow and the business environment become ever more competitive, it must become increasingly profit and cost-conscious in order to maximize revenue and minimize costs, all while maintaining the level of service necessary for a successful operation.

The tourism and hospitality sector is, arguably, one of the largest components of the global economy, with a growth rate in consumption that supersedes that of most other goods and services. As a consequence, the profile of tourists is changing as consumers become more experienced, more demanding, and more likely to treat tourism purchases in very much the same way as they do any other item of consumption. This coupled with the globalization of communications transport and technology is creating a new environment for tourism professionals.

The challenge is now to recognize the breadth of the information environment and to be able to manage it successfully.

Hospitality management accounting is concerned with providing specialized internal information to managers who are responsible for directing and controlling operations within the hospitality industry. Internal information is the basis for planning alternative short- or long-term courses of action and the decision as to which course of action is selected. Specific detail is provided as to how the selected course of action will be implemented. Managers direct the needed material resources and motivate the human resources needed to carry out a selected course of action. Managers control the implemented course of action to ensure that the plan is being followed and, as necessary, modified to meet the objectives of the selected course of action.

Hospitality business operations, as well as others, are generally identified as having a number of different cyclical sales revenue cycles. First, there is the **daily operating cycle** that applies particularly to restaurant operations where daily sales revenue typically depends on meal periods. Second, there is a **weekly cycle.** On one hand, business travelers normally use hotels, motels, and other hospitality operations during the week and provide little weekend hospitality business. On the other hand, local people most often frequent restaurants on Friday through Sunday more than they do during the week. Third, there is a **seasonal cycle** that depends on vacationers to provide revenue for hospitality operations during vacation months. Fourth, a generalized **business cycle** will exist during recessionary inflationary cycles, and hospitality operations typically experience a major decline in sales revenue.

These types of businesses do not normally require the use of the unique accounting procedures and techniques required by hospitality operations. In manufacturing operations, all costs are generally assigned to products or product lines and identified as direct costs and indirect costs. **Direct costs** include all materials and labor costs that are traceable directly to the product manufactured. **Indirect costs** generally refer to manufacturing or factory overhead, and include such items as administrative salaries, wages and miscellaneous overhead, utilities, interest, taxes, and depreciation. The basic nature of indirect costs presents difficulties isolating specific costs since they are not directly traceable to a particular product. Portions of supporting *indirect costs* are assigned by allocation techniques to each product or product line.

Managerial accounting uses historical and estimated financial information to develop future plans. Managerial accountants may help managers make decisions by assessing the financial impact of alternatives being considered. For example, should the restaurant open or close on a specific day or for a specific meal period? A managerial accountant can study actual and estimated information and provide managers with recommendations.

Expenses are classified according to the types of products or services used in generating the revenues. In management accounting there is a need to classify expenses in a more sophisticated manner in order to help management plan and control expenditure incurred, and to provide a basis for decision making.

If in financial accounting we can classify expenses in wages, depreciation and materials expenses, in management accounting those same expenses would be cross-classified according to where and for what purpose expenses were incurred. In other words, the management accountant would analyze the expenses in terms of where they were finally consumed as costs. In fact, management accountant would need to further sub classify the costs in each department in order to establish exactly what, who, where, when, how and why expenditure has been incurred. If a business is to control costs and plan expenditure appropriately, managers need to know the answers to all of the above questions, and this may not be easy.

The distinction between what expenditure is generated and where it is consumed is the essential difference between expenditure and cost, and is indicative of the difference between financial accounting perspective and the management accounting perspective.

The overall costs consumed in a department or business, as a whole can be sub classified under there different components: **direct costs, indirect costs and remote costs.** It is easiest to think of these three cost components in relation to producing a product, but they can also applied to a service, perhaps a service in the hospitality and tourism industry.

Direct costs, indirect costs and remote costs can themselves be subdivided:

- **Direct costs**: direct materials, direct labor, direct expenses;
- **Indirect costs**: costs, which, although clearly identified with a particular revenue-earning function, are not directly determined by the level of activity within that function.
- **Remote costs**: costs which cannot be associated closely with any particular revenue-generating function within the business, but which are incurred on behalf of the whole organization.

The direct costs are those costs, subdivided into materials, labor and expenses, that are easily associated with the revenue-generating activity, and may be directly influenced in the short term by the level of activity within a revenue-generating function. They are also known collectively as the **prime cost** of the product or service. All indirect costs are known in costing terminology as **overheads** but is possible to make the distinction between costs which, albeit indirectly, can be associated with a specific revenue-generating activity, and costs which cannot be so easily associated.

MATERIAL AND METHOD

The calculation of **the material cost** of product may be relatively straightforward or relatively complex, depending on the product or service concerned. Some products may have only one or two components or ingredients, such as loaf of bread, or an ice-cream, where as others may have hundreds or even thousands of parts, such as an outboard motor for a powerboat. To illustrate the method for calculating the material cost in a product, consider a standard main meal served in a restaurant. The standard ingredients and quantities are as follow:

Steak – 0,25 kilo
Prawns – 0,125 kilo
Avocado – ½
Mixed salad – 1 carton
Baked potato – one, medium – 0,20 kilo
Onion rings – 3 ready-battered

These ingredients are bought in the following quantities at these prices:

Steak – 68 euro per 20-kilo box
Prawns – 7,60 euro for a 5-kilo bag
Avocado – 8 euro for a box of 25
Mixed salad – 12 euro for a case of 50
Baked potato – 2,50 euro for a 25-kilo sack
Onion rings – 2,40 euro for 60 bags

To calculate the cost per standard portion of the ingredient within the meal, the first step is to calculate how many standard portions of the ingredient can be obtained from each stock item. For the frozen provisions, begin by subtracting the water content from the gross weight of the stock item, which is for steak – 15%, and for prawns – 5%.

So,
Steak – 20kilos * 0,85 = 17 kilos
Prawns – 5 kilos * 0,95 = 4,75 kilos

The next step is to divide the net weight of stock by the standard quantity of the ingredient in each meal to obtain the number of portions per standard stock item:

Steak – 17 kilos/0,25 = 68 portions
Prawns – 4,75kilos/0,125 = 38 portions
Avocado – 25/0,5 = 50 portions
Mixed salad – 50/1 = 50 portions
Baked potato – 25/0,20 = 125 portions
Onion rings – 60/3 = 20 portions

Finally divide the cost per stock item by the number of portions to be obtained from each stock item:

Steak – 68 euro/68 portions = 1 euro
Prawns – 7,60 euro/38 portions = 0,20 euro
Avocado – 8euro/50 portions = 0,16 euro
Mixed salad – 12 euro/50 portions = 0,24 euro
Baked potato – 2,50 euro/ 125 portions = 0,02 euro
Onion rings – 2,40 euro/ 20 portions = 0,12 euro
Total standard direct material cost of meal = 1,74 euro

The direct labor cost is totally identifiable or consumed in the product itself. However, a restaurant doesn't sell a product, it sells a complete service. We will continue with our example to illustrate the calculation of direct labor costs.

Staff wages rates per hour (euro)
Chef – 8,00
Assistant chefs – 5,00
Washing-up staff – 3,00
Waiting staff – 4,00
Hours worked on a standard batch of meals (hours)
Chef (1 person)– 6,00
Assistant chefs (3 persons*8h) – 24,00
Washing-up staff (2 persons*4h) – 8,00
Waiting staff (4persons*5h)– 20,00

The number of meals served throughout the week from past experience like average is 560. So, the average number of meals served per standard night of the week is 560/7 = 80.

Then we can calculate the total direct wages paid to staff associated with the provision of meals:

Chef – 6h*8,00 euro = 48 euro/80 meals served = 0,60 euro
Assistant chefs – 24h*5,00euro = 120 euro/80 = 1,50 euro
Washing-up staff – 8h*3,00 euro = 24 euro/80 = 0,30 euro
Waiting staff – 20 h*4,00 euro = 80 euro/80 = 1,00 euro
Total direct wage cost per batch of meals = 3,40 euro

Overheads are indirectly associated with the main activity and do not depend on the level of activity. The purpose of costing is to identify what costs are consumed and where, in order to control and monitor them. There is, however, another possible purpose of calculating costs, and that is to use them as a guide to pricing, and to estimate the profitability of product in advance. If this is the case, it is necessary to assign the overheads costs of the establishment to the product or service provided, in addition to the direct or prime costs.

We will continue example and identify those costs, which are defined as overheads that are indirectly associated with the main activity, providing meals or remotely associated with it.

The average weekly overheads are 7 euro:
Rent – 1 euro
Rates – 0,7 euro
Insurance – 0,45 euro
Manager salary – 3 euro
Telephone – 0,15 euro
Power – 0,35 euro
Wages for bookkeeper – 1,07 euro
Entertainment license – 0,28 euro

So it is reasonable to say that 7 euro/560 meals = **1,25 euro** who must be recovered per meal, this is known as the **overhead recovery rate.**

The restaurant can now estimate that the full or absorption cost of the meal is as follow:

direct material cost of meal = 1,74 euro
Direct labor cost of meal = 3,40 euro
Prime cost = 5,14 euro

Overhead recovery rate = 1,25 euro
Full absorption cost per meal = 6,39 euro

RESULTS AND DISCUSSION

This full cost indicates to the management of the restaurant that if the costs remain the same and the same quantity of meals are sold each week, a price of 6,39 euro per meal must be charged to recover all costs. The management of the business would need to add a profit loading to this full cost in order to charge a price that covers the full costs and yields an acceptable profit margin.

CONCLUSION

The total cost calculated for a product or service can appear very different depending on which judgments prevail, and which methods are adopted. The total costs are highly dependent on the accurate collection and recording of internal cost information, which requires reports and calculations from design engineers and work-study experts to ensure that the figures obtained are valid and reliable. The major area of controversy, however, is the apportionment of overheads because the greatest subjectivity as the choice of apportionment basis.

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