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| Manage First: Controlling Foodservice Costs  Instructor’s Materials | |
| 1 | The Importance of Cost Control In Restaurants |

Chapter Learning Objectives

* Explain how restaurant and foodservice costs affect profitability.
* Describe the manager's role in cost control.
* Identify the types of costs incurred by restaurant and foodservice operations.
* Explain the importance of controlling prime costs.
* Explain the basic restaurant and foodservice cost control process.

Chapter Summary

**1. Explain how restaurant and foodservice costs affect profitability.**

If costs become disproportionate to revenue, the profitability goals of a restaurant or foodservice operation might not be realized. Controlling costs begins with the menu and continues through purchasing to the receiving process, storage, production, and finally, service. Without controls in place, an operation can neither determinenor evaluate whether the operation is profitable or meeting its budget. Controlling and reducing costs are both necessary for ensuring the ongoing financial health of an operation.

**2. Describe the manager’s role in cost control.**

The size and scope of an operation will determine the extent to which its managers exercise direct control or delegate that responsibility to other staff. Managers, employees, and suppliers are expected to meet the standards set by management. Standards cover the entire spectrum of the restaurant and foodservice business.

**3. Identify the types of costs incurred by foodservice operations.**

Costs can be classified in several ways. The most common classifications are fixed, variable, and semi-variable costs. Fixed costs are those costs that remain the same regardless of sales volume, while variable costs increase or decrease in direct proportion to increases or decreases in sales volume. Semivariable costs increase when sales increase and decrease when sales decrease; however, the change in semivariable costs is not directly proportional to sales.

Costs also can be either controllable or non-controllable. Controllable costs are those costs that management can directly control. Non-controllable costs are those costs over which managers have little or no control.

**4. Explain the importance of controlling prime cost.**

The major cost categories that managers have to control are food , beverage , and labor . These costs are referred to as *prime costs*, because when considered together, they comprise the highest costs in the operation. For most operations, a prime cost of less than 65 percent is required for that establishment to be profitable.

**5. Explain the basic foodservice cost control process.**

Managers are responsible for developing performance standards for a given operation. The income statement allows foodservice managers to monitor actual financial performance. Once actual sales and costs are calculated, these figures are compared to budgeted amounts, operational standards, and historical information in order to identify any variances. When costs are determined to be other than as planned, the cause of the disparity should be investigated and management should take action to correct the problem.

Key Terms

controllable cost, p. 5

controls, p. 11

corrective action, p. 15

cost structure, p. 4

cover, p. 11

fixed cost, p. 5

line item review, p. 14

loss, p. 4

noncontrollable cost, p. 5

operational standard, p. 10

prime cost, p. 9

profit, p. 4

quality standard, p. 12

quantity standard, p. 12

sales, p. 4

semivariable cost, p. 5

variable cost, p. 5

variance, p. 14

Chapter’s Concepts and Teaching Tips

The key concepts identified in this chapter are:

1. Understanding types of costs in restaurants:
   1. Fixed costs
   2. Variable costs
   3. Semivariable costs
   4. Controllable costs
   5. Noncontrollable costs
2. Grasping the importance of the prime cost in restaurants
3. Knowing about the steps of the cost control process

Teaching tips related to this chapter include:

1. Ensuring students recognize that many of the costs that will directly affect their operational success (i.e., profitability) will be external to their operations and thus will not be within their direct control (i.e., noncontrollable costs). While this situation creates some challenges, managers can still be proactive by finding ways to increase their sales to offset any increases in fixed costs.
2. Distinguishing between fixed costs, semivariable costs and variable costs is critical for restaurant operations. These costs must be carefully explained to students and illustrated by examples. Please emphasize that the difference between fixed costs and variable costs is that variable costs change in a direct relationship to sales while a fixed cost stays the same no matter the level of sales.
3. In addition, the essence of prime costs in restaurant operations should be explained so that students understand that the majority of money that a restaurant spends falls into one of the prime cost categories; food, beverage and labor.
4. Explaining the importance of the cost control process and its individual steps.
5. Students should grasp the managerial role in the cost control process.
   1. List categories of managerial roles

Case Study Answers

Susan and her business partner Ryan sat at the kitchen table. They were reviewing a franchise agreement, discussing the pros and cons of opening up a franchise restaurant.

Susan waved at the pile of papers and said “Look, if we open up a franchise, we have to do everything their way. We have to run the front of the house their way. We have to cook only items on THEIR menu exactly the way they tell us to. We won’t have any chance to be creative and try out new ideas.”

Ryan replied “But that’s the whole point! The guys running the chain have already figured out what works. Customers go to these restaurants because they know exactly what they’re going to get. The whole point behind all of those rules is to make sure that we give the customers a consistent product. Plus, we know what we’re getting in to. We have an idea of what our labor and foodcosts will be going in to this. There’s a lot less guessing.”

“I hear you” said Susan, “But I’m pretty sure we can figure out how to make a

good product and control our costs running an independent operation.”

1. How can standardization and consistency help managers control restaurant and foodservice operating expenses?

Standardization and consistency lead to lower labor and food costs. Standardization enables employees to better apply production standards. In addition, standardization and consistency lead to better production planning and lower level of food waste.

2. What are the benefits of product consistency for customers and for managers?

Product consistency leads to higher customer satisfaction because each time a customer visits a restaurant, he/she enjoys the same product quality. This, in turn, leads to a higher level of customer loyalty. The benefit of consistency for managers is that higher customer satisfaction means less time spent on guest complaints, which leaves more time for managers to focus on operations.

Manager’s Math Solutions

An establishment serves on average 165 meals per day and operates 360 days a year. Although business was brisk, the manager was concerned that the level of profit was very low. Therefore, the manager implemented a waste control program in the kitchen and reduced food cost expenses by $.15 per customer.

1. What is the total of cost savings for this restaurant?

Answer: 165 x 360 x $.15 = $8,910

1. What would be the total cost savings if management was able to find a way to reduce costs by an additional $.10 per customer?

Answer: 165 x 360 x $.10 = $5940 + $14,850

Application Exercise Solutions

Julia is reviewing a list of expenses for the operation of her establishment. She notices several jumps in costs compared to the previous month. These are the items that have increased in cost:

* Electricity
* Labor
* Produce delivery fees
* Milk

Given this information, answer the following questions:

1. What can Julia do to reduce these costs in the upcoming months?

The electricity bill can also be reduced by adjusting the thermostat and turning off lights in storage ares during slow hours. Julia can do a better job of labor scheduling to control labor costs. The cost of milk cannot be reduced directly unless Julia finds a new vendor that offers better prices. Management needs to review the usage for milk to see if there are any areas where milk is being wasted.

2. How might these changes affect the establishment’s customers?

Management needs to consider customer impac before making any changes. While turning off lights in non-customer areas or during slow times will probably not impact customers, adjusting the thermostat may if it is done during service hours. Management needs to monitor customer service responses to make sure that adequate levels of staffing continue. Perhaps better training will enable fewer staff to maintain customer service levels. Customers would only be effected by consilidated orders is the operation begins to run out of product between deliveries. Reviewing possible waste for milk products will not impact customers.

3. Are there any costs that Julia cannot reduce?

Noncontrollable costs, such as rent, cannot be reduced.

4. Which of the costs are semivariable, and how can Julia control the variable portion of those costs?

Electricity is a semivariable cost because while the rate for electricity cannot be negotiated, the amount of elecricity used can be controlled. . However, Julia can take some measures such as making sure the refrigerators and coolers are clean so that they can run efficiently. Also, cooks can delay pre-heating ovens and fryers so they are preheated for service but are not preheated for hours before the start of service. If there are multiple ovens and fryers, some can be turned off during slower hours.. If air conditioning is used, the thermostat can be set to a higher temperature during slow business hours or when restaurant is closed.

5. What can Julia do to increase profits even if she is not able to cut costs?

When costs cannot be cut, profits can still be increased by increasing menu prices and/or having a higher sales volume.

Review Your Learning Answer Key

Note: Answers to *Review Your Learning* are identified in red.

1. When an operation’s expenses exceed its sales, the restaurant is experiencing a

A. loss.

B. profit.

C. quality standard.

D. line item review.

2. What is one benefit of having cost controls?

A. It helps keep employees working their hardest.

B. Managers know if they are meeting their budget.

C. Managers can make changes whenever they want to.

D. It makes it simpler for an operation to change the menu.

3. Who is expected to meet standards set by managers?

A. Managers and customers

B. Employees and suppliers

C. Managers, employees, and suppliers

D. Customers, suppliers, and employees

4. Food cost is an example of what type of cost?

A. Fixed cost

B. Variable cost

C. Semivariable cost

D. Noncontrollable cost

5. A type of cost that increases or decreases in direct proportion to sales increase or decrease is known as a

A. fixed cost.

B. variable cost.

C. semivariable cost.

D. noncontrollable cost.

6. Rent and insurance typically are examples of what type of cost?

A. Variable costs

B. Semivariable costs

C. Controllable costs

D. Noncontrollable costs

7. What is the restaurant and foodservice industry standard for prime cost?

A. 45%

B. 55%

C. 65%

D. 75%

8. Which is the most important cost for a restaurant or foodservice manager to control?

A. Rental expenses

B. Equipment costs

C. Marketing costs

D. Prime costs

9. What is the first step in the cost control process?

A. Analyze costs

B. Take corrective action

C. Collect sales and cost data

D. Establish standards or define the goals

10. Actual costs should be compared against what type of costs**?**

A. Fixed costs

B. Competitors’ costs

C. Controllable costs

D. Standard costs

Suggested In-Class Activities

1. List several types of costs and ask students to categorize them as follows.
   1. Fixed costs, Variable costs and Semivariable costs
   2. Controllable costs vs. noncontrollable costs
2. List steps of the cost control process and ask students to discuss each step.

Suggested Homework Activities

1. Ask students to submit a recently published article about food costs by perusing major restaurant industry publications or online. Have students report about which food items were most frequently mentioned in press.
2. Ask students to visit at least two local restaurant managers or have a manager visit your class and ask them to report how frequently these managers evaluate their major variable costs. Students should discuss whether they agree or disagree with the frequency of evaluations of these costs by restaurant managers.