



The Profit and Loss Report

5

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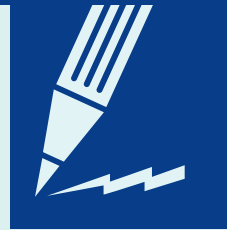
After completing this chapter, you should be able to:

- Describe a profit and loss report, and explain its use.
- Prepare a profit and loss report based on sales and cost information.
- Analyze information found on a profit and loss report.

Chapter 5 *The Profit and Loss Report*

Test Your Knowledge

- 1 **True or False:** Another name for the profit and loss report is the *income statement*. (See p. 56.)
- 2 **True or False:** An operation has made a profit when its expenses are equal to its income. (See p. 58.)
- 3 **True or False:** It is important to manually check the calculations of any reports run from POS systems. (See p. 57.)
- 4 **True or False:** The total amount of taxes paid by an operation is referred to as “the bottom line.” (See p. 58.)
- 5 **True or False:** A variance in costs between two similar periods might indicate a problem. (See p. 59.)



Key Terms

Income statement

Profit

Sales

Loss

Profit and loss report

Variance

Introduction

How can a foodservice manager quickly assess the status of an operation’s finances? The best way to see at a glance how the operation is performing is by reading its profit and loss report. The profit and loss report provides a brief snapshot of the operation’s financial activity. Profit and loss reports also provide financial data that is used in turn to analyze trends and identify areas for improvement.

What Is a Profit and Loss Report?

In simple terms, a **profit and loss report** is a compilation of sales and cost information for a specific period of time. This report shows whether an operation has made or lost money during the time period covered by the report.

The profit and loss report, which is also called the **income statement**, is a valuable management tool. It helps managers gauge an operation’s profitability as well as compare actual results to expected goals. Carefully monitoring this information periodically—such as monthly or quarterly—helps management determine areas where adjustments must be made to bring business operations in line with established financial goals.

Managerial Accounting

An example of a profit and loss report appears in *Exhibit 5b* on p. 59. Note how the report is organized. It lists sales income first, then lists all expenses. The end of the report reflects the amount of profit or loss for the period covered.

Preparing Profit and Loss Reports

Step 1: Determine Time Period for Report

The first step in preparing a profit and loss report is to determine what time period the report should cover. Once that is decided, the financial records should be gathered. Accurate data is important. Most point-of-sale (POS) systems can generate reports directly from computerized sales and accounting records, avoiding the need for manually looking up and calculating the data.

Step 2: Calculate Total Sales

The next step in preparing a profit and loss report is to figure out total sales for the period selected. **Sales** includes all of the income the restaurant has made in the given time period. This can be done by totaling receipts for each category, such as food or beverage. Some restaurants also sell merchandise—such as souvenir T-shirts and other specialty products—which might have their own sales category. Then, these categories are added together to calculate the total sales for a certain period. Sales information can be broken down even further. Many operations will also separate their sales by types—like catering or banquets.

Step 3: Calculate Total Costs

Next, total costs—or expenses—need to be calculated for the same period. These costs might include invoices paid, payroll reports, or accruals. Expenses can be determined from either paper records or through the POS system reports. For example, labor cost can be determined by reviewing payroll reports.

As discussed in Chapter 3, there are various categories of costs, including controllable or noncontrollable costs, and also variable, semivariable, or fixed costs. Because fixed expenses do not change regularly, managers only need to figure out fixed expenses for a set time period to determine the cost of those expenses over a greater period of time. For instance, if a manager wants to know the yearly expense of a fixed rent, all that needs to be done is multiplying the monthly rent expense by twelve to determine the total yearly cost.

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Exhibit 5a

Types of Taxes

Taxes Due from the Operation

- **Income taxes.** These can be federal, state, or local.
- **Property taxes.** Real property taxes can be a major expense and may be imposed by state or local jurisdictions. They are based on the assessed value of the property.
- **Personal property taxes.** This could include such categories as kitchen equipment and improvements; small wares such as china, glassware, and dining room equipment; and construction in progress.

Taxes Collected by the Operation on Behalf of the Government

- **Sales taxes.** Most states have some sort of sales and use tax. Although it is paid by customers, it is collected by sellers.
- **Payroll taxes.** These can be considered in two categories. One is tax money withheld from employees' paychecks and then paid to the government by the employer. These taxes are also paid by the employee. The other payroll taxes include federal unemployment insurance, workers' compensation, and unemployment compensation.

Taxes

Another item usually included in costs is taxes. Taxes are a cost of doing business that most operations must pay. Taxes must be paid and records kept for those taxes. A business could have many types of taxes, including those from the local, state, and federal government. These include the types listed in *Exhibit 5a*.

Step 4: Subtract Total Costs from Total Sales

The profit or loss of a restaurant operation is simply the difference between the total sales (or income) and the total costs (or expenses). This figure, found at the end of the profit and loss report, is also known as "the bottom line." If sales are higher than

costs, then the operation is making a **profit**. Conversely, if the total costs are higher than the total sales, then the restaurant is running at a **loss** for the specified time period.

If you look at the example in *Exhibit 5b*, you can see that Rancher's Steak House made a profit of \$6,200 for the month of April 2008.

Activity

Income or Expense?

Classify each of the items listed below as either *income* (I) or *expense* (E).

- | | |
|------------------------------------|--------------------|
| _____ 1 Revenue from T-Shirt sales | _____ 4 Food Sales |
| _____ 2 Wages | _____ 5 Utilities |
| _____ 3 Marketing | |

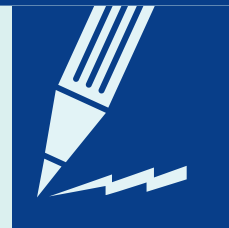


Exhibit 5b

Rancher's Steak House Profit and Loss Report

For the Period: 4/1/08 to 4/30/08

Sales

Food	\$ 80,000
Beverage	20,000
Total sales	\$100,000

Cost of Sales

Food	\$ 32,000
Beverage	5,000
Total cost of sales	\$ 37,000

Gross Profit

Food	\$ 48,000
Beverage	15,000
Total gross profit	\$ 63,000

Controllable Expenses

Salaries and wages	\$ 26,000
Employee benefits	4,000
Legal/accounting	500
Music and entertainment	5,000
Marketing	250
Utility services	2,000
General and administrative	3,800
Repairs and maintenance	2,000
Other income	250
Total controllable expenses	\$ 43,800

Fixed Expenses

Rent	\$ 5,700
Depreciation	1,000
Utility services	0
Licenses/permits	100
Insurance	3,000
Loan payments	2,500
Total fixed expenses	\$ 12,300

Profit/(Loss)* **\$ 6,900****Income Taxes** **\$ 700****Net Earning (Loss)** **\$ 6,200**

*before income taxes

Analyzing Profit and Loss Reports

Managers collect profit and loss data on their operations for a purpose. Most larger organizations have an internal auditing staff that sets the requirements for such financial reporting. Investors, owners, and managers look carefully at these reports to determine the profitability of an operation. The reports might also be used to judge the efficiency of an operation, to determine where costs have gotten out of line, and to make basic management decisions.

There are several approaches to analyzing a profit and loss report. When comparing a recent profit and loss report to the budget, company standards, industry standards, or historical trends, you need to be looking for any **variances**—changes that have occurred. This is a good way to check how the operation is running and can prevent future problems by catching them early. As soon as variances are observed, you should analyze what happened and develop a plan of how to correct the problem.

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Comparing Actual Values to Budgeted Values

Profit and loss reports are useful when comparing what is actually occurring to what was budgeted or planned for. Any variance between actual amounts and the budget could indicate that something unexpected has occurred. For instance, actual sales amounts might not be as high as were expected due to bad weather conditions or emergency road repairs in front of the operation. It is easy to see where such unforeseen conditions have affected sales.

In addition, variances might indicate that the assumptions made during creation of the budget were inaccurate. If this is the case, you will want to take a closer look at these assumptions when preparing future budgets.

Comparing Actual Values to Standards

Most restaurants will have standards to compare to as well. These standards are usually the basis of the operation's original budget. General industry standards reflect accepted ranges for certain costs within the foodservice industry. These standards are not an exact measurement. It is important to make sure the values being compared actually fit the nature of an operation. For example, a fine-dining restaurant will have a higher percentage of labor costs than a quick-service restaurant. If the fine-dining manager's goal is to have better service than any other restaurant in the area, then the operation should expect to have labor costs that are higher than the industry standard.

If an operation is part of a chain, there will likely be company standards to compare against. Company standards are used as a guide for how the operation can and should be run. This includes percentages of costs coming from food and beverage. It also could be broken down more specifically into certain food items. Other controllable and fixed expenses can be addressed by company standards as well.

Comparing Actual Values to Historical Trends

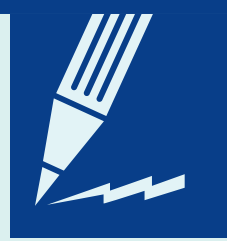
Another way to analyze the information on a profit and loss report is to compare it with historical data from the operation. This can be done for an individual unit or across multiple properties. Using historical trends is a great way to look for seasonal changes. It can also be used to remind managers of upcoming local events that had an effect on a previous year's sales.

Activity

Dare to Compare

Identify whether each of the following is an example of an industry standard (I), company standard (C), or historical trend (H).

- _____ 1 All John's Deli franchises should keep food cost below 25 percent.
- _____ 2 Most quick-service operations have a food cost of lower than 22 percent.
- _____ 3 A cost variance of more than 10 percent between two periods in a row must be reported.
- _____ 4 At the Florida Inn in Miami, sales during the month of August are typically half of what they are in December.
- _____ 5 Our target for next period is to reduce food cost by 1 percent.



Activity

Late Night at the Diner

It is 8:00 p.m. on a snowy Sunday night at Derek's Family Diner. The restaurant has very few customers—the basketball team from the local high school is playing in the finals of the state tournament, which is being broadcast on cable. Carl, the night manager, decides to cut two of the five servers from the floor early. They finish their sidework and clock out at 8:30 p.m. At about 9:20 p.m., a steady stream of people come into the diner—several large parties at the same time. Carl learns that the arts center down the street presented its opening night performance of "A Star-Filled Holiday," and most of the customers have come to enjoy coffee and pie before the diner closes at 10:00 p.m.

Given this information, answer the following:

- 1 What effect will these factors have on the profit and loss report for Derek's Family Diner for this week?

- 2 How might this period's report vary from those of previous periods?

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Summary

In simple terms, a profit and loss report is a compilation of sales and cost information for a specific period of time. This report shows whether an operation has made or lost money during the time period covered by the report.

The profit and loss report, which is also called the income statement, is a valuable management tool. It helps managers gauge an operation's profitability as well as compare actual results to expected goals. Careful, periodic monitoring of this information—such as monthly or quarterly—helps management determine areas where adjustments must be made to bring business operations in line with established goals.

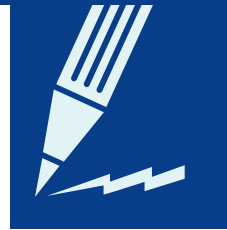
The profit and loss report lists sales income first. It then lists all expenses. The end of the report reflects the amount of profit or loss for the period covered. If sales are higher than costs, then the operation is making a profit. Conversely, if the total costs are higher than the total sales, the restaurant is running at a loss for the specified time period.

The first step in preparing a profit and loss report is to determine what time period the report should cover. Once that is decided, the financial records should be gathered. The next step is to figure out total sales for the period selected. Then, total costs, or expenses, need to be calculated for the same period. The profit or loss of a restaurant operation is simply the difference between the total sales (or income) and the total costs (or expenses).

Management looks carefully at profit and loss reports to determine the profitability of an operation, to judge the operation's efficiency, to determine where costs have gotten out of line, and to make basic management decisions.

There are several approaches to analyzing a profit and loss report. When a manager is comparing a recent profit and loss report to the budget, company standards, industry standards, or historical trends, he or she needs to be looking for any variances or changes that have occurred. This is a good way to check how the operation is running and can prevent future problems by catching them early. As soon as variances are observed, the manager should develop a plan of how to correct the problem.

Review Your Learning



- 1** The profit and loss report is also called the
 - A. balance sheet.
 - B. income statement.
 - C. bottom line statement.
 - D. statement of net worth.

- 2** Which is the correct formula for calculating profit or loss?
 - A. Monthly sales \times 12
 - B. Total costs – Total sales
 - C. Total sales – Total costs
 - D. Annual sales – Monthly costs

- 3** What is the *final step* in preparing a profit and loss report?
 - A. Calculate total sales.
 - B. Calculate total costs.
 - C. Subtract total costs from total sales.
 - D. Determine what time period the report should cover.

- 4** What information is included at the top of a profit and loss report?
 - A. Sales
 - B. Costs
 - C. Taxes
 - D. Expenses

- 5** Which *is not* commonly compared to profit and loss reports?
 - A. Historical trends
 - B. Company standards
 - C. Operational budgets
 - D. Customer service surveys

- 6** An operation's budget lists food expenses as \$14,000. The profit and loss report for the period indicates food expenses were \$18,000. What has occurred?
 - A. Variance
 - B. Tolerance
 - C. Standard deviation
 - D. Corrective action

