



Departmental Contributory Income Statement

Most hospitality operations consist of multiple departments and management needs to be able to analyze the performance of each department. **Departmental contributory income** is one important way to evaluate a department's performance. Departmental contributory income is equal to **departmental sales revenue less departmental expenses (or direct costs)**. Basically, it shows us how much profit each department contributed to the overall business.

We can also look at the **contributory income percentage** (which is the **dept. contributory income divided by dept. sales revenue**) to look at the impact of each department on total contributory income and on net income. This number tells us how we may want to shift the focus of marketing to bring in more revenue for a department that would increase our overall profit.

Indirect expenses are those costs not directly related to the sales revenue-producing activities of a business. Indirect expenses are divided among the entire business, rather than belonging to one specific department. For instance, a hotel will have one utility bill. It is impossible to tell how much energy a hotel uses for its guest rooms as opposed to the hotel restaurant. Some examples of indirect costs are administrative expenses, marketing, building utilities, etc. These indirect expenses are allocated to each department by using a reasonable measure such as a revenue ratio basis or a square footage basis.

A side by side comparison of departmental contributory income has the following format:

	Department 1	Department 2	Total
Sales revenue	\$80,000	\$60,000	\$140,000
Cost of sales	(26,800)	(14,000)	(40,800)
Gross margin	\$53,200	\$46,000	\$99,200
Wages and salaries cost	(12,000)	(10,200)	(22,200)
Other direct costs	(4,000)	(5,000)	(9,000)
Contributory income	\$37,200	\$30,800	\$68,000

Example: Use the information above and the following details to prepare a departmental contributory income statement. In addition to the direct expenses listed above, there are administrative expenses of \$15,000 and utilities expenses of \$3,000 to be distributed between the two departments. The indirect expenses are distributed based on revenue. Find the contributory income percentage for each department.

Solution: We already know the contributory incomes for each department. Next, find out each department's percent of total sales revenue and distribute the indirect expenses. Dept 1 sales revenue is 57% of the total revenue ($\$80,000/\$140,000 \times 100$). Multiply this percentage by each indirect expense to find out how much dept 1 is responsible for. Repeat the process for dept 2.

	Dept 1	Dept 2	Total
Contributory income	\$37,200	\$30,800	\$68,000
Sales Rev %	57%	43%	100%
Admin expenses	(8,550)	(6,450)	(15,000)
Utilities expenses	(1,710)	(1,290)	(3,000)
Total indirect exp.	(10,260)	(7,740)	(18,000)
Income before Tax	26,940	23,060	50,000

To find the contributory income percentage for each department, take the contributory income and divide by sales revenue. Note that these percentages are NOT related and will not add up to 100.

$$\text{Dept 1 contributory income percentage} = \frac{\$37,200}{\$80,000} = 47\%$$

$$\text{Dept 2 contributory income percentage} = \frac{\$30,800}{\$60,000} = 51\%$$

Since department 2 has the higher contributory income percentage, a shift in revenue from dept 1 to dept 2 will increase the overall net income.

Practice Problems

1. JR's Bistro has three sales revenue departments with direct costs and average monthly figures as shown below.

<i>Departments</i>	<i>Dining</i>	<i>Catering</i>	<i>Beverages</i>
Sales revenue	\$194,000	\$102,400	\$86,000
Cost of sales	77,600	28,912	27,528
Wages and salaries cost	64,020	30,700	10,680
Other direct costs	17,460	8,192	6,548

The bistro has the following indirect, undistributed costs:

Administrative expenses	\$11,500
Advertising expenses	9,500
Property maintenance	11,800
Utilities expense	4,200
Depreciation expense	12,500
Insurance expense	5,000

- (a) Prepare a consolidated departmental contributory income statement showing each of the divisions side by side for comparison.
- (b) Calculate the contributory income percentage for each of the three divisions (round to the nearest whole number).
- (c) Allocate the indirect costs to the divisions and prepare a departmental income statement. Administrative and advertising expenses are allocated based on sales revenue. The remaining indirect costs are allocated based on square footage used by each department. (Round percentages to whole numbers before finding out the dollar values.)
 Dining 2800 sq. ft. Catering 1200 sq. ft. Beverages 600 sq. ft.
- (d) If \$12,000 of revenue transfers from dining to catering, does it increase or decrease the net income for the business?

Solutions

1. (a)

Department	Dining	Catering	Beverages	Total
Sales revenue	\$ 194,000	\$ 102,400	\$ 86,000	\$ 382,400
Cost of sales	(77,600)	(28,912)	(27,528)	(134,040)
Gross margin	116,400	73,488	58,472	248,360
Wages and salaries	(64,020)	(30,700)	(10,680)	(105,400)
Other direct costs	(17,460)	(8,192)	(6,548)	(32,200)
Contributory income	\$ 34,920	\$ 34,596	\$ 41,244	\$ 110,760

(b)

Department	Dining	Catering	Beverages	Total
Sales revenue	\$194,000	\$102,400	\$ 86,000	\$382,400
Contributory income	\$ 34,920	\$ 34,596	\$ 41,244	\$110,760
Contributory Income %	18%	34%	48%	

(c)

Divisions	Based on Square Footage %		
Dining	2,800/4,600	=	61%
Catering	1,200/4,600	=	26%
Beverage	600/4,600	=	13%
Divisions	Based on Revenue %		
Dining	194,000/382,400	=	51%
Catering	102,400/382,400	=	27%
Beverage	86,000/382,400	=	22%

Department	Dining	Catering	Beverages	Total
Contributory income	\$ 34,920	\$ 34,596	\$ 41,244	\$ 110,760
Less:				
Administrative expense	5,865	3,105	2,530	11,500
Advertising expense	4,845	2,565	2,090	9,500
Property maintenance	7,198	3,068	1,534	11,800
Utilities expense	2,562	1,092	546	4,200
Depreciation expense	7,625	3,250	1,625	12,500
Insurance expense	<u>3,050</u>	<u>1,300</u>	<u>650</u>	<u>5,000</u>
Total expenses	(31,145)	(14,380)	(8,975)	(54,500)
Operating Income	<u><u>3,775</u></u>	<u><u>20,216</u></u>	<u><u>32,269</u></u>	<u><u>56,260</u></u>

(d) Since the contributory income percentage is higher for catering (23%) than dining (18%), the \$12,000 revenue transfer will result in a higher net income. Proof shown below:

Net income has increased to \$58,154 from \$56,260. Note to find the new departmental (direct) expenses for dining and catering, the direct expenses for each dept must be calculated as a percentage of the original sales revenue for that dept and then multiplied by the new sales revenue of that dept.

	Dining	Catering	Beverages	Total
Sales revenue	\$ 182,000	\$ 114,400	\$ 86,000	\$ 382,400
Cost of sales	<u>(72,800)</u>	<u>(32,300)</u>	<u>(27,528)</u>	<u>(132,628)</u>
Gross margin	109,200	82,100	58,472	249,772
Wages and salaries cost	(60,060)	(34,298)	(10,680)	(105,038)
Other direct costs	<u>(16,380)</u>	<u>(9,152)</u>	<u>(6,548)</u>	<u>(32,080)</u>
Contributory income	<u><u>32,760</u></u>	<u><u>38,650</u></u>	<u><u>41,244</u></u>	<u><u>112,654</u></u>
Sales Revenue %	48%	30%	22%	100.0%
Square Footage	2800	1200	600	4600
Square Footage %	61%	26%	13%	100.0%
Administrative expense	5,520	3,450	2,530	11,500
Advertising expense	4,560	2,850	2,090	9,500
Property maintenance	7,198	3,068	1,534	11,800
Utilities expense	2,562	1,092	546	4,200
Depreciation expense	7,625	3,250	1,625	12,500
Insurance expense	<u>3,050</u>	<u>1,300</u>	<u>650</u>	<u>5,000</u>
Total expenses	(30,515)	(15,010)	(8,975)	(54,500)
Income Before tax	<u><u>2,245</u></u>	<u><u>23,640</u></u>	<u><u>32,269</u></u>	<u><u>58,154</u></u>