*Case Study—Sunrise Country Club: Where do we stand financially?*

## Learning Objectives

Upon completion of this case, students should be able to:

- Rearrange items in an income statement.
- Convert income statement to common-size income statement.
- Compute absolute and relative variances for different income statement items.
- Compute a statement of cash flow using indirect method.
- Compute financial ratios.
- Suggest different ways to increase operating revenues in country clubs.
- Discuss inventory turnover issues.
- Compute breakeven point.
- Explain how a club can decrease product waste and improve internal control matters.
- Discuss concepts of depreciation and capital improvements in a context of country clubs.

## Introduction

Dennis Gonzales, a controller in Sunrise Country Club in Florida, is getting ready to present to the Board of Directors the financial ratios for his private club together with some other financial information. A current case presents real accounting and financial data obtained from one of the country clubs in Florida. The purpose of this case is to enhance selected topics that are usually discussed in accounting and finance college level courses. Furthermore, it presents ratios that are very industry specific. This case may be suitable for undergraduate and graduate hospitality management students and undergraduate and graduate business students. Students will be presented with six exhibits that would include an income statement, a balance sheet, and additional financial data related to capital improvements, golf course maintenance and equity additions.

It is recommended that students work in groups that consist of 2-3 students in a group, unless a student strongly prefers to work by himself/herself. An instructor should monitor the progress that each group is making and be able to assist students if they do not know how to move forward with the assignment. If an instructor observes that most of the groups experience the issue, the instructor should explain a perceived challenging position in front of the class.

### *General Teaching Approach*

It is suggested that the case is not covered with students all at once. It would be more effective to approach specific topics in this case after that topic was initially covered or discussed in a classroom (for traditional classroom) or on-line (for web-based courses). It may be beneficial to work on this case after performing textbook practice problems that are usually presented at the end of a chapter. A level of assistance that students need to receive with this case depends on their familiarity with the subject matter.

1. Rearrange the income statement to reflect dues as a part of operating revenues and depreciation as a part of operating expenses. *See Exhibit A.*

The presentation of the income statement would be more representative of what is normal. For example, operating revenues, including dues, are part of the operations. Most of the trustees have business experience and would appreciate an income statement with which they have experience.

2. Compute a common size income statement. *See Exhibit B.*

Over the years, the food and beverage revenue as a percent of total revenues has increased. It is much higher than the industry standard of 13.7 percent. CCF is less dependent on dues as a revenue source. Employee expenses have increased. However, when compared to the industry, they have lower costs as a percent of total revenues in this area.

With the decline of dues as a source of funds, it is good to see that some of it is being replaced by the food and beverage operations. Golf revenues have not grown over the years. The only real growth in revenue comes from the food and beverage area.

The employee expenditures need to be studied. It has grown as a percent of revenue. Management needs to get this under control. One of the major employee expenses is the hiring of a chef. This could be the reason for the increase, but they need to get this area under control.

3. Compute the variances for 2013. Which variances are most out of line? *See Exhibit C.*

Any item with a negative 10 percent of more should be analyzed. The golf cost has a variance of 16.9 percent above budget. The food and beverage costs are higher than budgeted. Supplies are another area of concern. Finally, the marketing expenses are much higher than budgeted.

What is causing the large increase in the cost of sales expenditures for golf? The food and beverage cost is not so much of a concern since the revenue grew by 7.5 percent. It should be watched over the next year.

Another area of concern is the supplies expense. It is well above the budgeted amount. No breakdown of the supplies is given, but it needs to be reviewed. Is it a one-year occurrence, or is the increase permanent? If it is permanent, it needs to be reflected in the future budgets. The last area of concern is the marketing expense. Given the state of declining golfers in the state of Florida and nationwide, courses are going to have to increase their marketing efforts to attract new members. Therefore, the budget for this expense needs to be

***Exhibit A***

| | 2013 | 2012 | 2011 |
|---|---|---|---|
| Golf Revenue | $ 2,180,536 | $ 2,061,066 | $ 2,157,700 |
| Tennis | $ 91,257 | $ 80,408 | $ 72,748 |
| Food and Beverage | $ 2,152,938 | $ 2,054,180 | $ 1,925,894 |
| Other Operating Revenues | $ 55,696 | $ 71,231 | $ 267,562 |
| Dues | $ 4,092,904 | $ 4,153,387 | $ 4,163,956 |
| **Total Revenue** | **$ 8,573,331** | **$ 8,420,272** | **$ 8,587,860** |
| | | | |
| **Cost of Goods Sold** | | | |
| Golf | $ 592,184 | $ 472,673 | $ 511,431 |
| Tennis | $ 23,125 | $ 22,528 | $ 20,762 |
| | | | |
| Food & Beverage | $ 912,151 | $ 844,170 | $ 809,043 |
| | $ 1,527,460 | $ 1,339,371 | $ 1,341,236 |
| **Gross Margin** | **$ 7,045,871** | **$ 7,080,901** | **$ 7,246,624** |
| | | | |
| **Operating Expenses** | | | |
| Employees | $ 4,330,655 | $ 4,164,186 | $ 4,071,951 |
| Contractual and Rentals | $ 484,596 | $ 567,126 | $ 594,456 |
| Utilities | $ 381,515 | $ 389,677 | $ 377,058 |
| Supplies | $ 416,498 | $ 398,138 | $ 378,969 |
| Marketing Expenses | $ 182,867 | $ 181,320 | $ 180,515 |
| Repairs and Maintenance | $ 650,673 | $ 701,522 | $ 718,554 |
| Other Office Expenses | $ 228,298 | $ 225,770 | $ 198,905 |
| **Bad Debt Expenses** | | | |
| Taxes & Insurance | $ 342,467 | $ 324,468 | $ 354,787 |
| **Other Expenses** | | | |
| Total Operating Expenses | $ 8,545,029 | $ 8,291,578 | $ 8,216,431 |
| EBITDA | $ 28,302 | $ 128,694 | $ 371,429 |
| Depreciation | $ 1,192,503 | $ 1,260,628 | $ 1,314,279 |
| EBIT | $ (1,164,201) | $ (1,131,934) | $ (942,850) |
| Non-operating (income)/Expenses | $ (114,073) | $ (6,872) | $ (21,568) |
| **Net Income** | **$ (1,050,128)** | **$ (1,125,062)** | **$ (921,282)** |

***Exhibit B***

| | 2013 | 2012 | 2011 |
|---|---|---|---|
| Golf Revenue | 25.4% | 24.5% | 25.1% |
| Tennis | 1.1% | 1.0% | 0.8% |
| Food and Beverage | 25.1% | 24.4% | 22.4% |
| Other Operating Revenues | 0.6% | 0.8% | 3.1% |
| Dues | 47.7% | 49.3% | 48.5% |
| **Total Revenue** | 100.0% | 100.0% | 100.0% |
| | | | |
| **Cost of Goods Sold** | | | |
| Golf | 6.9% | 5.5% | 6.0% |
| Tennis | 0.3% | 0.3% | 0.2% |
| Food & Beverage | 10.6% | 9.8% | 9.4% |
| Total | 17.8% | 15.6% | 15.6% |
| | | | |
| **Gross Margin** | 82.2% | 82.6% | 84.5% |
| | | | |
| Operating Expenses | 0.0% | 0.0% | 0.0% |
| Employees | 50.5% | 48.6% | 47.5% |
| Contractual and Rentals | 5.7% | 6.6% | 6.9% |
| Utilities | 4.5% | 4.5% | 4.4% |
| Supplies | 4.9% | 4.6% | 4.4% |
| Marketing Expenses | 2.1% | 2.1% | 2.1% |
| Repairs and Maintenance | 7.6% | 8.2% | 8.4% |
| Other Office Expenses | 2.7% | 2.6% | 2.3% |
| Bad Debt Expenses | 0.0% | 0.0% | 0.0% |
| Taxes & Insurance | 4.0% | 3.8% | 4.1% |
| Other Expenses | 0.0% | 0.0% | 0.0% |
| Total Operating Expenses | 99.7% | 96.7% | 95.8% |
| | | | |
| EBITDA | 0.3% | 1.5% | 4.3% |
| Depreciation | 13.9% | 14.7% | 15.3% |
| EBIT | -13.6% | -13.2% | -11.0% |
| Non-operating (income)/Expenses | -1.3% | -0.1% | -0.3% |
| **Net Income** | -12.2% | -13.1% | -10.7% |

***Exhibit C***

| | 2013 | Budgeted 2013 | Variance | Percentage |
|---|---|---|---|---|
| Golf Revenue | $ 2,180,536 | $ 2,150,795 | $ 29,741 | 1.4% |
| Tennis | $ 91,257 | $ 81,220 | $ 10,037 | 12.4% |
| Food and Beverage | $ 2,152,938 | $ 2,002,013 | $ 150,925 | 7.5% |
| Other Operating Revenues | $ 55,696 | $ 65,006 | $ (9,310) | -14.3% |
| Dues | $ 4,092,904 | $ 4,109,839 | $ (16,935) | -0.4% |
| **Total Revenue** | $ 8,573,331 | $ 8,408,873 | $ 164,458 | 2.0% |
| | | | | |
| **Cost of Goods Sold** | | | | |
| Golf | $ 592,184 | $ 506,700 | $ (85,484) | -16.9% |
| Tennis | $ 23,125 | $ 23,688 | $ 563 | 2.4% |
| Food & Beverage | $ 912,151 | $ 826,087 | $ (86,064) | -10.4% |
| | $ 1,527,460 | $ 1,356,475 | | 0.0% |
| **Gross Margin** | $ 7,045,871 | $ 7,052,398 | $ 6,527 | 0.1% |
| | | | | |
| **Operating Expenses** | | | | |
| Employees | $ 4,330,655 | $ 4,243,594 | $ (87,061) | -2.1% |
| Contractual and Rentals | $ 484,596 | $ 475,557 | $ (9,039) | -1.9% |
| Utilities | $ 381,515 | $ 396,427 | $ 14,912 | 3.8% |
| Supplies | $ 416,498 | $ 360,982 | $ (55,516) | -15.4% |
| Marketing Expenses | $ 182,867 | $ 151,025 | $ (31,842) | -21.1% |
| Repairs and Maintenance | $ 650,673 | $ 699,030 | $ 48,357 | 6.9% |
| Other Office Expenses | $ 228,298 | $ 210,092 | $ (18,206) | -8.7% |
| **Bad Debt Expenses** | | | | |
| Taxes & Insurance | $ 342,467 | $ 359,478 | $ 17,011 | 4.7% |
| Other Expenses | | $ 80,000 | $ 80,000 | 100.0% |
| Total Operating Expenses | $ 8,545,029 | $ 8,332,660 | $ (212,369) | -2.5% |
| EBITDA | $ 28,302 | $ 76,213 | $ - 47,911 | -62.9% |
| Depreciation | $ 1,192,503 | $ 1,211,825 | $ 19,322 | 1.6% |
| EBIT | $ (1,164,201) | $ (1,135,612) | $ 28,589 | -2.5% |
| Non-operating (income)/Expenses | $ (114,073) | $ 22,972 | $ 137,045 | 596.6% |
| **Net Income** | $ (1,050,128) | $ (1,158,584) | | |

***Exhibit D***

| | 2013 | 2012 | 2011 |
|---|---|---|---|
| **Operations** | | | |
| Net Income | (1,050,128) | (1,125,062) | (921,282) |
| Depreciation | 1,192,503 | 1,260,628 | 1,314,279 |
| Receivables | 92,412 | 112,303 | (50,331) |
| Inventory | (12,526) | (12,526) | (31,440) |
| Prepaids | (29,343) | 23,104 | 8,221 |
| Accounts Payable | 107,226 | 25,566 | (145,673) |
| Accrued Expenses | 115,310 | (6,664) | 10,325 |
| Other Short-term Liabilities | 56,426 | 24,434 | 21,319 |
| Changes in Working Capital | 329,505 | 139,041 | (187,279) |
| Cash Flows from Operations | 471,880 | 274,607 | 205,718 |
| | | | |
| **Investing** | | | |
| Capital Improvements | (524,115) | (821,440) | (474,383) |
| Cash Flows from Investing | (524,115) | (821,440) | (474,383) |
| | | | |
| **Financing** | | | |
| Short Term Notes | (204,985) | 183,381 | (47,333) |
| Long-Term Liabilities | (647,333) | (805,992) | (692,388) |
| Membership Dues Liabilities | (21,700) | (47,600) | (108,600) |
| Equity | 897,506 | 915,078 | 1,191,758 |
| Cash Flow from Financing | 23,488 | 244,867 | 343,437 |
| Change in Cash | (28,747) | (301,966) | 74,770 |

increased in future years.

The reasons above explain the large percentage drop in the earnings before depreciation, interest, taxes, depreciation and amortization.

4. Using the indirect method, compute a statement of cash flows for 2013. See Exhibit D.

There has been an increase in the operating cash flow, which is good. This is mainly due to the depreciation. The club has been paying off debt recently as evidenced by the notes and short term liabilities being an outflow of cash. This is positive since less debt implies less risk.

There has been a beneficial increase in the operating cash flow. This is mainly due to the depreciation, which is good since depreciation is a non-cash expense. The club has been paying off debt recently as evidenced by the notes and short term liabilities being an outflow of cash. This is positive since less debt implies less risk. An area of concern is the equity increases. Most of the equity change is initiation fees. Initiation fees and dues have been reduced in recent years to attract new members. Equity increases are used to purchase capital expenditures. Capital expenditures include building improvements and new equipment. In the future, there may be a problem with buying these items given the decreasing equity. It may mean more money from the operating budget will be needed to pay for these items.

5. Compute the current ratio and quick ratio. Is the liquidity improving? How does it compare to its peers? *See Exhibit E.*

*Current Ratio=Current Assets/Current Liabilities*

For example, for every $1 of liabilities in 2013, Sunrise has $1.87 of assets that are converted into cash within one year. The trend is down, implying that they are becoming less liquid, and if it continues, the club could have some trouble paying its bills. When compared to the industry average of 1.8, they are slightly more liquid than the rest of the clubs in Florida.

*Quick Ratio=(Current Assets-Inventories)/Current Liabilities*

For example, for every $1 of current liabilities in 2013, Sunrise has $1.63 in cash and receivables. As was the case with the current ratio, the club's liquidity has declined from 2011. When compared to the industry average of 1.50, the club is more liquid than its peers.

Overall, the liquidity of the club is near the industry averages. Consequently, there appears to be no problem with the liquidity of the club. The club should be able to meet its short-term obligations.

6. Compute the inventory turnover ratio and asset turnover ratio. How would you rate the management of its assets? How does it compare to its peers?

*Inventory Turnover=Sales/Average Inventory*

For example, for 2013 Sunrise replaces its inventory almost 25 times a year. The implication is that the club is replacing its inventory every two weeks. If inventory turnover is declining it implies the club is becoming less efficient in the management of its inventories. With an industry average of 25.7, the club is less efficient in the management of its inventories when compared to its peers.

This is an area that needs improvement. Most of the inventory is for food and beverages. Given the perishable nature of food, more attention needs to be given to this area. In conclusion, this is a problem area.

*Asset Turnover Ratio = Total Revenues/Total Assets*

For example, in 2013, asset turnover was 0.39 cents. The asset turnover for 2012 and 2011 was $0.38 and $0.37, respectively. Asset turnover ratio indicates an amount of sales revenues generated per one dollar in assets. The trend is upward so Sunrise is becoming more efficient in the management of its assets. The industry standard is $0.36, meaning that Sunrise is more efficient in the management of assets than its peers.

In spite of its poor management of inventory, Sunrise appears to manage its other assets well. However, since inventory is a significant asset, Sunrise needs to improve in this area.

7. Compute the debt/equity ratio, debt ratio, capitalization ratio, cash flow to debt ratio, and capital improvements / depreciation ratio. Is Sunrise becoming more or less risky? How does it compare to its peers?

*Debt/Equity Ratio=Total Liabilities/Shareholders' Equity*

For example, for every $1 of equity in 2013, Sunrise has 13.9 cents of liabilities. The trend is decreasing, meaning they are borrowing less relative to equity. It implies the club is becoming less risky. When compared to other clubs in Florida, Sunrise is less risky.

The use of debt does not appear to be a problem. Therefore, there is a decrease in risk, and they are less risky than other country clubs.

*Debt Ratio=Total Liability/Total Assets*

For example, for every $1 of assets owned by Sunrise in 2013, 12.2 cents were borrowed, and the remaining 87.8 cents represents equity or what the members supplied. The number is decreasing so they are borrowing less than previously. They are becoming less risky. When compared to its peers (18%), Sunrise borrows less than other clubs in Florida and is less risky than its peers.

*Capitalization Ratio= Long-term Debt/(Long-term Debt + Equity)*

***Exhibit E***

## Sunrise Country Clubs Ratios

| Ratio | 2013 | 2012 | 2011 |
|---|---|---|---|
| Current Ratio | 1.87 | 1.98 | 2.44 |
| Quick Ratio | 1.63 | 1.75 | 2.20 |
| Inventory Turnover | 24.87 | 25.35 | 29.46 |
| Asset Turnover | 0.39 | 0.38 | 0.37 |
| Debt/Equity | 13.9% | 16.9% | 19.9% |
| Debt Ratio | 12.2% | 14.4% | 16.6% |
| Capitalization Ratio | 3.0% | 2.8% | 2.7% |
| Cash flow/Debt | 0.79 | 0.34 | 0.33 |
| Food Cost Percent | 44.6% | 42.9% | 44.5% |
| Beverage Cost Percent | 36.4% | 35.9% | 35.7% |
| Golf Course Maintenance | $ 57,545 | $ 60,498 | $ 60,022 |
| Capital Improvement/ Depreciation | 0.44 | 0.65 | 0.36 |
| Sports Revenue per member | $ 3,786 | $ 3,569 | $ 3,717 |
| Food and Beverage per member | $ 3,588 | $ 3,424 | $ 3,210 |
| Food Revenue to Beverage Revenue | 2.71 | 2.81 | 2.69 |
| Dues per member | $ 6,822 | $ 6,922 | $ 6,940 |
| Cash Flow Ratio | 0.22 | 0.13 | 0.11 |

***Exhibit F***

| 2013 | 2012 | 2011 | 2010 |
|---|---|---|---|
| $ 2,952,647 | $ 2,655,874 | $ 2,575,646 | $ 2,341,626 |

For example, in 2013, the capitalization ratio is 3.0%. This means that from the funding raised by debt and equity for Sunrise, three percent is borrowed and the rest is equity. This number has increased over the years, implying that the club is becoming more risky.

The implication is that although the total amount of debt is going down, the level of equity is decreasing more. When compared to the industry, Sunrise is doing a better job of managing its level of debt.

*Cash Flow to Debt Ratio*

Cash Flow to Debt Ratio=Cash Flow from Operations/Total Debt. Debt = Current Portion of Long Term Debt + Long Term Debt.

For example, in 2013, Sunrise has 77% in operating cash flow that can be used to pay off the debt of the club. The higher the percentage, the better the club's ability to carry its total debt.

The number has increased significantly. As of 2013, it is much higher than the industry average. This is also positive in the sense that club should be better able to pay its debts.

*Capital Improvements/Depreciation*

For example, in 2013, for every $1 of depreciation, Sunrise spent $0.44 on capital improvements. Depreciation represents the wear and tear on the buildings and equipment for the club. Eventually, they have to be replaced. The spending has fluctuated over the years. However, when compared to the industry average of $1.03, Sunrise is spending much less than its peers in this area.

8. Compute the food cost percent, beverage cost percent, golf course maintenance expense, sports revenue per member, food and beverage per member, food to beverage ratio and dues per member. What is happening in cost structures? What conclusions can you draw based on those ratios? Calculate some additional ratios that you think may be helpful.

*Food Cost Percent=Food Cost/Food Sales*

For example, in 2013, the food cost percent is 44.6 percent. In 2011, the food cost was 44.5 percent, and the food cost in 2012 was 42.9 percent. The trend in food costs from 2011 to 2013 showed no real change. As compared to the rest of Florida, Sunrise's costs are less since Florida is 48.6 percent. Sunrise has lower costs than the rest of Florida.

*Beverage Cost Percent=Beverage Cost/Beverage Sales*

For example, in 2013, the beverage cost is 36.4 percent. In 2012, it was 35.9 percent. In 2011, it was 35.7 percent. The trend is upward, meaning the cost of beverages is going up for Sunrise. The industry has average costs of 32.4 percent. Sunrise has higher beverage costs than the rest of Florida.

*Golf Course Maintenance Expense*

For example, Sunrise spent $57,545 per hole in 2013. This number is down from previous years. Sunrise is spending less than previously on the maintenance of the golf course. When compared to the industry average of $76,800, Sunrise is spending much less than other golf clubs. At first glance, the results would be a plus. However, unless they have developed some cost saving techniques, future golf course expenses may be in the future. Special assessments would likely follow.

Members do not like special assessments. It could lead to a decrease in renewals.

*Sports Revenue per member*

For example, Sunrise's sports revenue was $3,786 per member. This number is relatively constant over the three years. It compares favorably to the industry ($2,100). Sunrise is generating more sales from its members than its peers.

*Food and Beverage per member*

For example, Sunrise's members spent $3,588 on average for food and beverages in 2013. The number has increased over $300 since 2011. Sunrise compares favorably to the industry average of $2,300 per member. Sunrise generates more revenue per member than its peers do.

*Food to Beverage Ratio*

For 2013, for every $1 spent by members for beverages, $2.71 was spent on food. Since there are higher gross profit margins on beverages, it is preferable to have a low number. The trend has changed little over the three years. When compared to the industry (3.6 times), Sunrise's ratio is better than its peers. This is another positive for this club.

*Dues per member*

On average, Sunrise members paid $6,822 in dues in 2013. This has decreased slightly over the years. The industry average is $8,100. Sunrise has lower dues than its peers. There may be some potential to raise dues in the future since its peers charge more.

The problem with raising dues is the state of the industry. Fewer people are golfing than in previous years. Increasing dues may create a backlash, and present members may not renew. In addition, raising dues may not attract new members. Another complication is the amount spent on capital improvements. If the facilities are not modern, there may be no reason to join this specific club.

The instructor may ask students to calculate additional ratios that are not suggested in this case study, and students may also develop

their own ratios. It would be beneficial to remind students that multiple ratios can be calculated based on exhibits provided in this case, and that when one calculates a ratio it should make economic sense and that a proper interpretation of ratios is crucial.

The instructor may explain to students, especially to graduate students, that development of ratios may be seen either through a prism of deductive approach that follows the cause and effect relationship, or an inductive approach that focuses on learning from real data. Graduate finance students may find the following article interesting by Lev and Sunder (1979), "Methodological Issues in the use of Financial Ratios."

The article suggests that when considering calculating ratios one should take into account control for a size effect, choice of deflator size, and control other industry variables, such as technology. Graduate students, especially those who had a research method or statistics class and are pursuing research on an academic track, versus an industry academic track, may benefit from mentioning that a few empirical studies. For example, Piches, Mingo, and Caruthers, (1973); Johnson (1978); and Cowen and Hoffer (1982) utilized factor analysis and were attempting to determine under which construct ratios usually load. However, there is no agreement and consistency across the board.

The instructor may explain to students based on the current case study that ratios can be compared based on diachronic or synchronic approach. The first approach implies that Sunrise County Club will be looking at its own ratios over a period of time, and the second approach implies that Sunrise will be looking at ratios for other private clubs in the area.

9. Suggest ways to increase other operating revenues.

Each group of students may list different ways how they think revenues may be increased, and there is not one correct answer. It is suggested that the instructor ask each group of students to read only one factor at a time and explain why they think it would work. Students may list a variety of different factors, such as renting banquet rooms, organizing events and celebrations, offering massage and spa services, and selling partial membership to individuals.

10. Calculate the breakeven point. *See Exhibit F.*

Please note the employee costs are considered to be fixed costs as discussed in the case. The breakeven point is calculated using the formula: Breakeven Point = Fixed Costs/ (1-Variable Costs/Sales).

For 2013, it is calculated to be $2,952,467. To breakeven for 2013, Sunrise would have to have its sales 37 percent higher than the actual sales. For 2012, $2,655,874 in food and beverage revenues is needed to break even. For 2010 and 2011, the food and beverages need sales to be $2,341,626 and $2,575,646, respectively. For all years, these numbers are at least 30 percent more than the actual sales.

Given this, students may suggest raising prices. This is an alternative, but they should be aware that the members are expecting a below market price. Students may also suggest cutting down the menu to fewer items. Once again, this risks the goodwill of the members.

Another suggestion related to raising prices is to canvas the local restaurants to see what they charge for similar dishes and plan accordingly. Are Sunrise's prices significantly less than the market? If so, a price increase should be considered. If not, perhaps a price increase is not appropriate.

11. Suggest reasons for inventory turnover increase.

If inventory turnover goes up and sales volumes increase, it is a positive trend for a business. However, if the inventory turnover increases but sales volumes do not go up, it may be caused by a variety of different reasons. First, it may be caused due to stealing. Second, there could be product waste or spoilage. Students may suggest a variety of ways how issues that cause a problem may be addressed. Answers will vary depending on a student's educational and professional background.

Below are several items that students may suggest:

- Segregation of duties among employees.
- Appropriate training/mentoring.
- Meaningful supervision.
- Properly recording changes in an inventory.
- Surprise physical inventory by an independent person.
- Standardized recipes.
- Limiting the number of individuals who may have access to an inventory.
- Implement a strong system of preventive internal controls.

12. What challenges may be facing the Sunrise Country Club that prevent the food and beverage department from achieving a breakeven point?

Right now, the Sunrise Country Club is a loss leader. It is not uncommon for country clubs to have food and beverage departments that lose money because the losses are subsidized by members' dues. However, country clubs compete for members who are obviously concerned about amount of dues.

Another arrangement is related to employees. Sunrise Country Club agrees to keep a certain number of servers to be on the premises, even though there may not be any customers. This is not an uncommon practice for private clubs and a true concern for all areas of private clubs. There is a certain level of minimum service expected, and private clubs may have to find more experienced servers or provide a more extensive training that would be affecting labor cost. Club members expect creative dishes that can be produced by a good chef versus an hourly paid cook. Most clubs are tax-exempt, and that is why advertising may not be freely launched to the extent that is feasible for commercial restaurants. Private clubs usually have several different food and beverage outlets, such as a formal dining room, casual dining, a bar, and a golf course snack outlet. Some of those outlets

may hardly have any guests on one selected day. Food and beverage outlets may be seen as an amenity for its members, and club amenities carry a cost, which is one of the reasons that members pay dues.

A simple increase in menu prices may encourage members who are not a capture audience, as would be in a case of hospitals or elementary schools to eat in other places.

13. What should Sunrise Country Club do about depreciation and capital improvements?

A functional, safe, and pleasant-looking club facility is a necessary element of a successful club existence. At some point, equipment has to be replaced and the building has to be renovated to attract and keep members. Capital improvements are necessary for any club to remain competitive to retain members. It is also needed to attract new members. Depreciation is an expense that represents wear and tear on the assets of the club. In the case of hotels and restaurants, depreciation is considered an operating expense. Historically, most of the money to replace the assets in private clubs originates from initiation fees. However, these days initiation fees are becoming less popular in private clubs.

Overall, the club needs to reduce the operating losses on the food and beverage operations to a lower level with a goal of breakeven. With the decrease in the number of golfers with no corresponding decrease in the number of golf courses, this is important. Second, the old days of "build it and they will come" is over. The club needs to develop a compressive marketing plan to attract and retain new members. Without one, the club will continue to see a decline in memberships and a growing deficit.

## Recommended Reading

Students may revisit their course materials (textbooks, Power Point slides, lecture notes) related to income statement, cash flow, and financial ratios topics. In addition, students may benefit from reading two reports prepared by McGladrey LLP and available on-line free of charge.

1. 2013 Florida Trends in Private Clubs http://mcgladrey.com/content/dam/mcgladrey/pdf/2013_florida_trends_private_clubs_report.pdf
2. Financial Ratios Analysis and Private Club Operations http://mcgladrey.com/content/dam/mcgladrey/pdf/financial_ratio_analysis_private_club_operations.pdf

### *Students may also benefit from other reading materials:*


Fridson, M. S., & Alvarez, F. (2002). Financial statement analysis a practitioner's guide (3rd ed.). New York: John Wiley & Sons.

Ittelson, T. (2009). Financial statements: A step-by-step guide to understanding and creating financial reports (Kindle version). Retrieved from Amazon.com.

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Perdue, J. & Koenigsfeld, J. (Eds.). (2012). Contemporary club management (3rd ed). American Hotel Lodging Educational Institute.

Welsh, T. (2012). 101 financial ratios 5.0 (Kindle version). Retrieved from Amazon.com.


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Financial ratio analysis and private club operations (2012). Retrieved June 4, 2014 from mcgladrey.com/content/dam/mcgladrey/pdf/financial_ratio_analysis_private_club_operations.pdf

Johnson, W.B. (1978). The cross-sectional stability of financial patterns. Journal of Business Finance and Accounting, 5 (2), 207-214.

Newman, P., & Tassitano, T. (2013). 2013 Florida trends in private clubs. Retrieved June 4, 2014, from http://mcgladrey.com/content/dam/mcgladrey/pdf/2013_florida_trends_private_clubs_report.pdf

Pinches, G.E., Mingo, K.A., and Caruthers, J.K. (1973). The stability of financial patterns in industrial organizations. Journal of Finance, 389-396.