

Management Accounting

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Introduction

In general, costing relates to allocation of cost to various elements of the business. The development of the cost has taken into consideration factors such as the presence of subsidiaries, processors, product lines, products, geographic regions, customers, distribution channels and employees. The given case is based on Harriot Hotel's expansion strategy for increasing the room capacity in China and overcome the losses in Europe and the Americas due to COVID-19 pandemic. In this regard, the projected cost breakdown for the UK division of the hotel has provided the contribution of a percentage of revenue items for each item such as employee wages, customer discounts, housekeeping, stationeries, interest on loan, cleaning supplies and advertising cost. As per the given list, is to be decided the costs, which can be increased, decreased or eliminated for ensuring that Harriot Hotel is able to maintain its leading position in the market. The study provides relevant justification for the aforementioned decisions, thereby indicating whether they are part of the fixed cost or variable cost.

Discussion

Typically, the overhead cost of small business shares the same attributes as overhead cost of a large business. The varying nature of the business decides the appropriate overhead cost. The three types of overhead cost ranges between fixed, variable and semi-variable, however, in order to maintain the simplicity of the discourse of this essay, the cost for the given items has been only classified as per the fixed or variable cost. The fixed cost remains the same for every month and such overhead cost does not vary as per the business activity (Li, Zhu and Liang, 2018). The general types of fixed cost are mainly evident with government fees, depreciation of assets, property taxes, insurance, utilities, wage paid to

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fixed time workers and annual salaries (Li, Zhu and Liang, 2018). On the other hand, the variable cost gets impacted by the relevant business activities. In other words, the increase in business activity also increases the overhead costs and vice versa. Thus, it can be discerned that decreasing nature of business activity can eliminate variable cost (Chacon *et al.* 2017). The different types of variable and semi-variable overhead costs include, legal expenses, equipment maintenance, office supplies, consulting services, materials, shipping, salaries of salespersons, commissions, vehicle usage, and wages for overtime hours (Graff *et al.* 2017). The overhead cost is calculated as per the rates for specific time periods and compared accordingly with the revenue. A clear understanding of the overhead cost is important for evaluating the actual bottom line of the business which is calculated by subtracting all the overhead cost and expenses from the gross profit (Meer 2017). In addition to this, based on the proportion of the items contributing to the bottom line, it can be decided whether the expenses are less than the revenue generated (Graff *et al.* 2017).

Assessment of each item costs to be increased, decreased or eliminated should be decided not only as a percentage of revenue contribution but also their importance to the business. For instance, stationery used in the front desk and restaurants may not contribute to a significant revenue but is still necessary for daily operations of the business. Based on this assumption, eliminating such an item can be also detrimental to the business. As per the given costs in the case study and the general overview of the overhead costs, it can be seen that employees' wages, advertising cost, housekeeping, cleaning supplies, customer discounts and stationeries comprise of variable cost for the company. On the other hand, the interest on loan and wages paid to the employees is a fixed cost. The interest is computed as a total percentage of the loan balance which is being paid to the lender on a periodic basis. This type

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of amount is seen to be quoted at an annual rate and applicable for both long term and short term borrowings. In this regard, it can be clearly observed that the fixed cost such as interest on the loan cannot be avoided. Based on the nature of the overhead cost, this cannot be increased, decreased or eliminated (Susan 2018). Moreover, this component is second highest contributor to revenue with 17%, which is after employees' wages.

The wages overhead can include the fixed amount of wages paid to all the employees of Harriot Hotel. Additionally, comprises of the cost such as a contribution to the PF, employee welfare, leave encashment, gratuity, future benefits and other benefits. The variable cost such as employee's wages cannot be reduced as they not only account for a significant portion of the revenue but also related to employee morale. Therefore, any type of reduction in such costs can significantly affect the morale among the employees. The advertising cost is defined as any cost which is related to the promotion of the business and this is generally seen in terms of the publications in magazines and newspapers, social media, television commercial or any other form of media. As the advertising cost cannot be measured for the future benefits, it is often reported by the name of advertising expense. As per the advertising cost contributing to 12% to the revenue of the company, it can be slightly reduced to augment the deteriorating performance of the hotels in the USA and Europe. The advertising cost can be maximum reduced by 2%.

The cost associated to housekeeping and cleaning supplies relates to laundry carts, cleaning supplies, brooms, moping equipment, drain cleaning, chemicals used for cleaning and odour control. The housekeeping and cleaning supplies attribute to 8.3% of the overall revenue generated by the business; however the decision to eliminate such an item is not possible. This type of equipment is essential for operating the office premises. In order to

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reduce the costs associated with such items, the hotel needs to provide more work from home to the employees based in China. Such a decision would in turn allow to assign more costs for the office premises in the US and European regions related to housekeeping and cleaning supplies, thereby keeping the costs same by compensating with the reduction in the costs in the Chinese counterpart offices. Harriot Hotel can consider a reduction of housekeeping and cleaning supplies cost up to 3%. The cost related to the customer discount is associated with a reduction in the prices over the original MRP. This cost is mainly related to attracting the new customers, building customer loyalty, increasing the sales and driving site traffic (Petřík 2020). However, the hotel can consider to reduce this cost to compensate the loss in the cities of the US and America. The reduction in the customer discount should be done cautiously so that sales are not impacted. In this aspect, a total of customer discount can be allowed up to 5%. This is identified as the highest area for consideration of discount for the given list of items.

The stationeries required at the front desk relate to envelopes, office supplies and writing paper. The contribution of such an item is identified to be lowest at 5%. However, as mentioned earlier, this item cannot be removed as this form an indispensable item for the operations of the hotel. This attributes to recommending the management to reduction of this variable cost to as low as possible. The management can consider a reduction up to 1%. The rationale for such a low reduction in the variable cost has been taken into account for their importance in the day to day operations of the business (Purbasari and Arimbawa 2019).

Conclusion

The excerpt of the essay has depicted interest on loan and wages as the fixed cost. The rest of the items comprise of the variable cost for the hotel. The discourse of the study has

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interpreted that the identified fixed costs of the hotel cannot be reduced. This decision was based on the importance of the fixed cost, which is evident with consideration of employee morale. If the fixed cost such as wages is reduced then the hotel may face acute attrition. Similarly, any changes in the fixed cost related to interest on the loan is not possible. In terms of the variable costs components, the most important item is recognised with advertising and stationeries. In this aspect, the management is recommended to consider a reduction up to 1% for the stationeries needed for the front desk items. In addition to this, the hotel can decide to reduce the costs related to the housekeeping and cleaning supplies maximum up to 3%. The relaxation of the 3% reduction is recognised with work from home given to certain employees. The advertising cost can be also reduced up to 2%. Such a small change in the advertising is due to the fact that they do not hamper the company's position in maintaining the leadership position in the market. Along with this, the hotel can reduce the discounts offered to the customers up to 5%. The reason for the highest reduction in this item is depicted with its nature of add-on service for the customer. In this regard, the slight reduction in this cost component will be conducive for positively impacting the operations in the US and European office.

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