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Financially Managing Your Vacation Rental Business

Present by:

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Agenda

- Introduction to Financial Accounting
- Chart of Accounts and General Ledger
- Understanding the Balance Sheet, the Income Statement and the Cash Flow Worksheet
- Why You Need a General Operating Budget and How to Create One
- Managing by Budget
- Financially Managing your Business

Successful Financial Vacation Rental Managers...

- Have the financial knowledge and resources to meet the company's financial obligations
- Ensure the company remains a going concern for the benefit of owners, shareholders, employees, guests and the community
- Use the financial reports generated by accounting to make decisions and plans for their business.

Introduction

- Bookkeeping, Accounting and why you should know both...
 - Bookkeeping is a systematic recording of every transaction, including dates, amounts and descriptions.
 - Accounting provides a bigger picture by tracking bookkeeping transactions and using them to analyze business results.
 - Why...To effectively manage your company to ensure it remains a viable operation
 - Why...To avoid being taken advantage of financially (particularly embezzlement and fraud)
 - Why...To assist in the planning and control of your business
 - Why...To be able to knowledgably communicate financial information to employees, potential lenders and investors, shareholders, and the media

Introduction

- Accounting systems and financial reports are only as reliable as the information and processes used to create them.
- To create reliable information and processes, follow these steps . . .
- Ensure that transactions are complete, accurate and timely
- Ensure that transactions have source documents
- Hire knowledgeable, skilled employees

Introduction

- Create clear, standardized policies and procedures
 - This consistency creates trust
 - Ensure policies and procedures aren't just for accounting employees—every employee is involved in some aspect of financial accountability and needs to know where he or she fits into the bigger picture
 - Start by reviewing the workflow of accounts receivable, accounts payable and property management revenue to ensure your company has a fundamental accounting foundation
- Create and enforce strong internal controls to minimize errors and temptations to dishonesty as well as to safeguard assets

Chart of Accounts

- List of all the accounts your company uses to track transactions
- Keep it simple
- You decide the number of accounts within each category and level of detail
- When naming accounts, use common terminology that quickly allows managers and employees to determine the meaning of a specific account
- Organize the chart of accounts to allow decision making employees to quickly understand transactions and financial information
- Types of accounts or categories: assets, liabilities, owner's equity, revenue, and expense

Chart of Accounts

- Assets
 - Resources owned by a company and which have future economic value that can be measured and can be expressed in dollars. Examples include cash, investments, accounts receivable, inventory, supplies, land, buildings, equipment, and vehicles.
 - Assets are reported on the balance sheet usually at cost or lower. Assets are also part of the accounting equation:
 - $\text{Assets} = \text{Liabilities} + \text{Owner's (Stockholders') Equity}$

Chart of Accounts

- Liabilities are anything your company owes to people or businesses—they are financial obligations
 - Current Liabilities are payable within one year (wages, accounts payable, advance deposits, etc.)
 - Long Term Liabilities are payable after one year (long term leases, long term debt, retirement obligations, etc.)
- Owner's Equity or "capital" = Assets - Liabilities

Simple Chart of Accounts

Account Number	Account
1000	Assets
2000	Liabilities
3000	Owner's Equity
4000	Revenue
5000	Direct Operating Expenses
6000	G&A Expenses

Detailed Chart of Accounts Structure

- Revenues
 - Property Management Fees
 - Gross Lodging Revenue
 - (Payments to Owners)
 - Property Mgmt Fee Sub Total
 - Service Fees
 - Reservation Fee
 - Damage Wavier
 - Maintenance Revenue
 - (Maintenance Expense)
 - Housekeeping Revenue
 - (Housekeeping Expense)
 - Lift Ticket Revenue
 - (Lift Ticket Expense)
 - Credit Cards Fees
 - (Credit Card Expenses)
 - Travel Insurance Revenue
 - (Travel Insurance Expense)
 - Service Fee Sub Total
 - Total Revenue
- Expenses
 - Direct Operating
 - Operating Payroll
 - Advertising
 - Owner Satisfaction
 - Guest Satisfaction
 - Employee Training
 - Employee Uniforms
 - Contract Service
 - Supplies
 - Direct Operating Sub Total
 - General and Administrative
 - G&A Payroll
 - Agency Fees
 - Facilities Rental
 - Telephone/ Internet
 - Transportation
 - G&A Sub Total
 - Total Expenses
 - Net Operating Income

General Ledger and Transactions

- General Ledger (G/L) is the part of your accounting system used to record (post) transactions
- A general ledger is a grouping of perhaps hundreds of accounts that are used to sort and store information from a company's business transactions. The general ledger is organized as follows:
 - Balance sheet accounts (assets, liabilities, equity), and
 - Income statement accounts (revenues, expenses)

General Ledger and Transactions

- Two methods of recording transactions in G/L: Cash and Accrual
 - Cash Basis
 - Revenue recorded upon receipt of cash
 - Expense recorded upon payment of cash
 - No accounts payable or receivable
 - Accrual Basis
 - Revenue is recorded when earned
 - Expense recorded to match revenue or in period in which it is incurred
 - G/L uses a Double Entry accounting system
- For every transaction, two accounts are affected
- One is debited and the other credited

Financial Reports

- Balance Sheet
- Income Statement
- Cash Flow Worksheet
- Review and verify all transactions posted to the G/L for reasonableness and consistency before preparing these reports
- These reports are typically prepared and reviewed each month after month end close

Financial Reports: Balance Sheet

- Also known as Statement of Financial Condition
- Provides a snapshot of your company's financial condition at any one point in time
- $\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$
- Typically compared to last year's Balance Sheet at same point in time
- **IMPORTANT ACCOUNTS:** Cash and Advance Deposits

Financial Reports: Income Statement

- Also known as Profit and Loss Statement or Earnings Statement
- Reports how well your company operated over a period of time. Did it make or lose money?

What's the bottom line?

- $\text{Revenue} - \text{Expenses} = \text{Net Income (or Loss)}$
- Net Income (or Loss) gets moved to the Balance Sheet and becomes Owners Equity

Financial Reports: Income Statement

- Typically compared to budget and prior year's operations
- Helps you determine which areas are under or over budget
- Frequently required by potential lenders and investors
- Variance Reporting - Investigate each variance

Financial Reports: Reviewing the Income Statement

- Top line revenue—Did you hit your forecast?
- Payments to owners—What is the percentage of top line? Are you paying more than you should?
If so, why?
- Review all other revenue accounts for reasonableness
- Review all expenses for reasonableness
- Compare each account to budget and/or prior year
- EBITDA
- Net operating income—Did you hit your forecast? If not, why?

Financial Reports: Cash Flow Worksheets

- Part of a larger and more complex report called Statement of Cash Flows
- Reports cash generated and used by your company over a period of time
- Don't confuse profitability (revenue – expenses) with cash flow -- you can be profitable and still lack cash and still go out of business
- Helps you determine if you'll have enough cash each month
- Helps you assess capability of generating future cash flow
- Focus on including all line items
- Cash Flow Worksheet is only as good as information provided therein

Financial Reports: Reviewing the Cash Flow Worksheets

- Ensure all accounts and transactions are included
- Look for irregularities or short falls in cash
- Short falls in cash will require you to add additional capital to your business
- Simple planning can negate or minimize the need for additional capital

Why You Need a Operating Budget

- It allows you to more effectively and efficiently manage the financial operation of your company
- It can provide you with a better basis for understanding your company's financial operations in relation to the general environment
- It leads to faster reactions to developing events, which increases your company's ability to perform more profitably
- It is an indicator of financial health, stability and sophistication to any potential lender, investor or buyer

Creating a Operating Budget

- Be kind to yourself (and others)—Realize that you'll make some mistakes and that there is a learning curve
- Start in October or November
- Use last year's financial statements and statistics to provide the foundation for this year's budget, then you can evaluate assumptions each year and make corrections
- Create a realistic and detailed budget—record true and accurate revenue and expense assumptions—avoid “sand bagging”
- Review your budget every month and revise your forecast (a revision detailing material increases or decreases to your budget) regularly

Identify Revenue Sources

- Use last year's revenue as a guide—pull amounts from your reservation system
- Be realistic and conservative—Don't overestimate income
- Understand Key Metrics and Terminology
 - Occupied Nights
 - Average Daily Rate
 - Focus on Gross Lodging Revenue because it will allow you to forecast expenses
 - Determine what you'll charge for services and fees—use your market to determine a viable price structure
- Create a Revenue Schedule

Identify Direct Operating and General & Admin Expenses

- Direct Operating Expenses
 - Are typically variable and fluctuate with Gross Lodging Revenue
 - Examples include housekeeping, maintenance, and hourly payroll
- General & Administrative Expenses
 - Are typically fixed —they stay the same each month
 - Examples include rent, management salaries, and other fixed payments
- Use last year's expenses as a guide
- Be realistic and conservative—Don't underestimate expenses

Develop Key Expense Schedules

- Payroll
- Leases (office, vehicles, copier, postage machine, etc.)
- Marketing
- Housekeeping and Maintenance (included in Operating Budget Worksheet—not done separately)

Remember Consensus is the Key

- Meet with dept managers to explain reason for budget and set goals
 - It is their planning tool
 - It is their chance to make requests (wish lists)
 - It is their opportunity to reveal their planning skills
 - It is their statement of resources required to meet their goals

Finalize First Draft (continued)

- Return to dept managers with request to cut money (not everyone)
- Prepare add/subtract list by department
- Note that Income Statement and General Operating Budget look identical

Conducting a Final Review and Sign Off

- Review all budgets one last time with overall picture in mind
 - Add items or money as needed
 - Cut items or money if you do not feel it is necessary to obtain department or company goals
- Review actual versus budget on a monthly basis
 - If income is down, why? If expenses are up, why?
 - Pay particular attention to:
 - Wages and employee benefits, including overtime
 - New project expenses
 - Accounts with previous problems
 - Advertising
 - Housekeeping income versus expense, Maintenance

Conclusions and Summary

- Benefits of fundamental financial management:
 - Stronger company
 - Unified approach to planning
 - Respect from banks, prospective buyers and greater chance of successful financial requests
 - Higher market value for your company
 - Positive equity position

Closing & Questions



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Other VRMA Sessions

Monday October 26th – 4:30 PM: *Selling Your Vacation Rental Business for Profit*

Tuesday October 27th – 11:00 AM: *The Art of The Deal*

Wednesday October 28th – 1:00 PM: *Financial Management and Budgeting*