The Main Dish

Winter 2017

What lies ahead
By Bradley S. Dimond, CPA

I began my career in 1985 (I know, that lies behind) when the talk was all about tax reform. In 1986, the tax code was reformed and "simplified" (sort of). The multitude of brackets was paired down to two, 15% and 28%, and many deductions were axed and loopholes closed. Capital gains were taxed the same as ordinary income.

With the surprise election of Donald Trump and Republican control of both Houses of Congress, chances are improved that some sort of tax reform will be passed, sooner rather than later. Let's take a quick look at what the President-Elect has proposed. It will have to be brief because the details are few. As with any major tax reform, there will be winners and losers.

Much like the '86 Act, the multitude of brackets will be paired down to three: 12%, 25%, and 33%, although there is some chatter that flow-through, business income will be taxed at 15%; so perhaps four brackets. The top bracket is effective for income in excess of $112,500 (single) or $225,000 (married filing joint). The Head of Household status would be done away with; not in real life, just in the tax code. Single parents (including yours truly) might not be too thrilled about that. The 3.8% Net Investment Income Tax would be repealed (Yay!). This was a "back door" tax increase as part of Obamacare – also a target for reform. Finally, personal exemptions go away but the standard deduction for non-itemizers is raised to $15,000 (single) or $30,000 (joint). Although the proposal purports to cut everyone's taxes, large but low income families could see taxes raised so stay tuned. For those that itemize deductions, such deductions would be limited to $100,000 (single) or $200,000 (joint). The nonprofit industry would likely lobby hard against this proposal because significant charitable dollars are raised from high earning families.

In addition, since Trump proposes to do away with the Estate Tax – another significant driver of charitable contributions – expect this to be a battleground. Capital gains in excess of $10 million are not taxed to the estate but once that hurdle is cleared, the subsequent sale of an asset by the estate or an heir would be subject to tax rather than the step up in basis that occurs now under the estate tax regime.

Trump proposes to slash corporate tax rates to 15% and do away with a number of deductions. Corporate taxpayers could immediately expense asset purchases, but the price for that would be to forego interest deductions on debt. As mentioned before, there may be the ability to pay tax on flow-through business income at 15%. Not sure, however, if the same tradeoff of immediate write-off of asset purchases for relinquishing interest deductions would apply.

Finally, Trump proposes to do away with the "carried interest" benefit, which allows a person with a profits interest in a partnership (or an LLC taxed as a partnership) potentially to recognize capital gains rather than ordinary income from his/her work efforts. Since the tax rates will be lowered, however, the net effect would not be as drastic as prior proposals. Stay tuned...

If you have any questions, Bradley can be reached at (480) 483-1170 or BradD@hhcpa.com.

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Utilizing financial ratios to manage your restaurant
By Jonathan Poppel, CPA

How do you measure financial performance of your restaurant? Often, restaurant owners will just be concerned with their "bottom line," meaning that the more net income the restaurant produces, the better the restaurant is performing. While the amount of net income is one indicator of financial performance, it shouldn't be the sole indicator. Restaurants should also measure and analyze key financial ratios. Some common restaurant ratios that restaurant owners and management should be concerned with are:

- Food sales and beverage sales as a percentage of total sales
- Food costs as a percentage of food sales
- Beverage costs, including liquor, beer and wine, as a percentage of the related beverage sales
- Labor costs as a percentage of total sales
- Prime costs (food, beverage and labor costs) as a percentage of total sales
- Controllable and non-controllable expenses as a percentage of total sales
- Net profit margin (net income divided by total sales)

In order to calculate these on a timely basis, it is important that the restaurant maintains its accounting records in a sufficient level of detail, primarily as it relates to sales, cost of goods sold and the various costs of the restaurant. The Uniform System of Accounts for Restaurants published by the National Restaurant Association is a useful guide for this. Having this information included as part of your financial reporting allows these ratios to be calculated easily.

Once these ratios are calculated, they must be properly evaluated. This includes comparing the ratios to prior months, comparing to restaurant norms and comparing to other similar restaurants under common ownership. By evaluating the ratios in all these manners, you can identify any negative trends that must be addressed. For example, increased food costs as a percentage of food sales over a large period of time may lead to the need to review food pricing with vendors, an increase in menu prices or unusual levels of food waste. Increasing labor costs as a percentage of net sales may necessitate the scaling back of shifts and hours for certain front-of-the-house and back-of-the-house staff. Finally, decreases in net profit margin, though net sales and net income has increased, may necessitate a further look at all costs of the restaurant to see why an increase in net sales is not flowing down to the bottom line.

Keep track of historical ratios for your restaurant to monitor these trends. If your accounting software is able to track and report these items, this will be your best bet. However, you may find that you need to track these in Excel after exporting financial information during the monthly close process.

With 2017 here, now is a good time to evaluate how you measure and evaluate your restaurant financial performance. Making any necessary changes and developing an approach for the New Year can set you in the right direction to better managing your restaurant.

If you have any questions, Jonathan can be reached at (480) 839-4900 or JonathanP@hhcpa.com.

Tappas

The U.S. Department of Agriculture released new food labeling guidelines in hopes of cutting down the amount of good food thrown out. They now want just one date label – "best if used by" – and are asking egg, meat and dairy manufacturers to use it.

The National Restaurant Association is out with 2017's hottest industry trends: hyper-local sourcing; chef-driven fast-casual concepts; natural ingredients/clean menus; environmental sustainability; locally sourced produce, meat and seafood; food waste reduction; meal kits; simplicity/back to basics; and nutrition.