

# Economics of Operating An Employee Food Service

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*The author, who has spent 30 years as an operations executive in the food service industry, seeks to acquaint management with some of the basic economics of operating an employee food service. The article is designed to assist the executive in understanding the basic philosophies and concepts of providing a food service to employees, as well as the cost factors involved in giving that service.*

Many corporations which operate an executive and employee food service have found themselves faced with rising operating costs for this service, and with company policy governing menu prices and other charge methods which preclude maintaining or lowering costs from their present level.

The basic principle in providing a food service for employees is as an employee benefit. As is the case with all employee benefits, its purpose is to foster and maintain good relations between employer and employee. Through this medium it is hoped that good will is created which will increase productivity, lessen employee turnover, and eventually provide profit to management.

As employees are of different categories, benefits are also for different categories. Two major categories of employees which receive different ratios of benefits to wages are the rank and file and supervisory and executive groups.

The food service provided by an employer quite naturally falls into these same two categories. The basic difference in the two is usually that supervisory and executive personnel are often offered more "service" than rank and file. This is in keeping with a general policy to allow this management group to occupy more office space per person, to have other special "perks" or incentives provided to motivate employees to want to become supervisors or executives, and to convince executives to remain with the corporation. Some companies such as IBM and Motorola do not differentiate between executive and employee food services; both groups utilize the company cafeteria.

## Company Policies Must Be Established

In order to provide a successful employee food service, an organization must clearly establish company policy in two areas: fiscal policy and basic personnel policy. It must be decided who will be allowed use of what company facilities, and the amount of cost the company is willing to invest to provide facilities and service to each group. Past history and past policies, whether actual or accepted, have a strong bearing on making these decisions. Management policy should not only be firmly established to allow for "financial" and "service" operational goals, but it should be reviewed from time to time to assure that the same goals are still desired.

There is one basic rule that governs the economics of any employee food service: to establish the degree of subsidy that is desired, if any. Keeping in mind that the food service is an employee benefit, this decision should be based on the relative cost of this service and its expected return in employee motivation, as compared to the cost of other employee benefits and their return. Since this motivation factor cannot be measured, it must be decided by management.

To establish the cost of the service and allow for a decision on the degree of subsidy, an operating budget must be prepared to project all costs to be incurred in providing a food service. To assist management in deciding on the degree of subsidy, a survey has been made of what major corporations do in operating their food services. These can be categorized into five basic methods:

- **Full Subsidy:** Free meals for all. This is still done in some industries (notably the insurance industry), but is becoming less and less utilized.
- **Subsidy: Recovery of food costs only.** Under this system employees are charged for 90 to 100 percent of the actual raw product cost of food. The employer subsidizes all other areas of cost; therefore, the employee receives a very low priced menu.
- **Subsidy: Recovery of food and labor costs.** Under this system, menu prices are geared to reflect the cost of raw foods and personnel costs necessary for preparation and service. All other areas of cost are subsidized, with the employee obtaining a moderately priced menu.
- **Subsidy: Recovery of all operating costs.** This involves recovery of all operational costs except space and, where a contract management company is utilized, its management fee. Under this system, menu prices are just below or equal to public restaurants of the same class as the employer-provided facility.
- **Subsidy: Profit and loss.** Under this system, management supplies the initial capital investment and the space. The contract company or the manager operates as he would in a public establishment. Menu prices are usually comparable to and sometimes above similar public cafeterias or restaurants. The food service has all the normal costs except rent and depreciation.

In all five methods, operational cost factors are influenced by the company locations, schedule and length of meal periods, space cost allocated, and many other factors which do not normally influence costs in a public eating place.

A review of a projection of costs (budget) and a decision on which cost factors, if any, will be subsidized will then establish the amount of money that must necessarily be recovered in sales. This in turn will be the key factor in establishing menu prices. In effect, in establishing a degree of subsidy, management will be establishing the menu prices to be charged its employees.

### **Subsidies Can Be Changed**

At any given time, management may wish to change the financial picture by changing the degree of subsidy. This can only be accomplished by a full knowledge of all operational cost factors of the employee food service and a decision as to which costs can be added to the menu prices without losing the benefits to employees that were originally planned.

Operational cost factors for all types of locations can be broken down into four basic categories:

- food costs
- labor costs
- other operating costs (laundry, paper goods and supplies, miscellaneous expenses)
- fixed charges (utilities, rent, etc.)

In many instances of providing an employee food service, labor costs and fixed charges are above those that would normally be encountered by a commercial food service. An interesting fact to be considered is that the average public restaurant today gains only 6 to 10 percent of sales as net profit before taxes. All areas of operating costs being comparable, an employer who wishes to operate a "no loss" employee food service could only eliminate the profit and offer food to his employees at 6 to 10 percent less than a restaurant of identical quality and style of service. This would not be much of an employee benefit.

### **Cost Factors Can Be Changed**

Should a decrease in operating subsidy be desired, some change must take place in one or more of the cost factors. Let us review what can be done to change the cost pattern in any of the four cost categories:

**Food Costs:** There are only three ways in which any food service operation, employee or commercial, can make a downward adjustment in its food cost to sales ratio once it reaches an optimum of efficiency in normal operations:

- lower food quality
- decrease portion size
- increase menu prices

Lowering the quality of food prepared or decreasing the size of portions served inevitably leads to a loss of customers and thus less gross sales and profits. This usually voids any savings gained by the change, especially in an employee food service.

Increasing menu prices will not always increase sales volume, but it will alter the food cost (percentage of raw food cost to sales ratio), thereby leaving a higher gross profit to pay for other areas of cost.

**Labor Costs:** Labor costs are directly controlled by management's decision as to what hours meals are to be served, what type of service (cafeteria, dining room, vending, etc.) is to be provided, and who will be serviced. Many of these decisions are influenced by past industrial relations decisions that have given employees a service in the past when it was felt desirable. Union contracts are often a part of those decisions. Although changes in the cost picture now make the service less desirable, past policy has a way of placing permanent cost burdens on future decisions.

Should a change in labor costs now be desired, the only methods by which management can decrease labor costs in its operations are:

- **Change type of service:** Make basic changes in the format of service given to allow for less service personnel. Such things as consolidation of dining rooms or changing the layout of the cafeteria line to utilize more self-service usually involve some capital investment in new layout or equipment. This should be carefully analyzed and have a definite "payout" period before instituting any change.
- **Decrease amount of service given:** Such changes as effecting a "self-busing" program and eliminating bus personnel, decreasing menu variety to lighten the production load and reduce production personnel, using more convenient type foods, utilizing vending machines to replace coffee carts or cafeteria service, and raising the requirements to eat in "supervisory" or "executive" dining rooms to lighten the attendance and reduce service personnel.
- **Eliminate previous services:** Elimination of guest dining room facilities to reduce service personnel, elimination of coffee runs in the afternoon or at all times, elimination of an on-premises bake shop, or other similar changes.

No matter which of the three categories is used to effect a labor savings, management must weigh all factors in the corporation to ensure that a change in service will not result in a decrease in attendance or disruption of labor relations. Either circumstance can prove any economy to be a false economy.

**Other Costs:** Very little can be done to reduce costs in the area of paper goods, cleaning supplies, and laundry once maximum efficiency of handling materials has been attained.

An exception to this rule is laundry. Any reductions in operating

personnel effected as a labor savings have the side benefit of also saving on laundry. Similarly, any reduction in dining room services utilizing laundry, etc., also provides a savings.

**Fixed Charges:** Fixed charges are usually imposed on the area occupied by the food service by central accounting or by other management decisions. These can be lowered or raised by the same management decisions. It is not unusual to find the space being charged to the food service completely out of line with its worth. Further, space charges allotted to food service are often well above what a profit and loss restaurateur could, or would, pay for the premises.

Cost of utilities can be lowered, in some instances. Often the replacement of a piece of faulty equipment or a better maintenance program can have a "payout" in utility bills. Many older facilities can lower costs by an effective energy savings survey by an expert. Older locations have a potential for energy cost savings; newer locations have less potential.

### **Management Method May Be Changed**

One area that has been adopted by many companies in recent years to reduce management subsidy requirements has been to change the management method from self-operation to a contract management company operation. A survey made by a trade magazine 20 years ago indicated that less than 50 percent of all locations which provided an employee food service were operated by contract management companies. A recent survey indicated that over 80 percent are now operated by the professional management companies. The reasons for this are many. Primary among them is the ability of the contract companies to pay a lower wage scale for food service employees than a manufacturing or business enterprise. Another is the ability of the management companies to supervise and direct the food service effort with a greater degree of management expertise which results in manhours and operating costs savings. Where a company is having difficulty maintaining or lowering food service operating costs, the choice of subcontracting out to a professional management company has a high degree of merit.

### **Assignment of Cost Varies**

In assigning the cost of subsidy of the food service to the various departments, different companies employ different methods. Some of the more popular ones are:

- **Rental on a square foot basis:** Division of the cost of food service subsidy by the number of square feet occupied by all other departments. Each department is then charged an additional service cost per square foot occupied, the same as it is for cleaning service, window washing, electricity, etc. One advantage of this system is that departments which allow their people more space per person (such as executive areas) pick up their fair share of this side benefit.

- **Charge by population:** Division of the cost of subsidizing the food service and charge back to each department on a per capita basis. This can be a less than equitable assessment when departments with many employees eligible to use facilities are charged no more per capita for the use of expensive executive and guest dining rooms than departments with just a few people in that category.
- **Employee benefits:** Charging of the subsidy cost of the food service to payroll on a ratio basis. Under this method an equal spread of this employee benefit is made the same as pension plans and other benefit costs, based on income, are made.
- **Assessment on an as-used basis:** Although this does not fully qualify for discussion at this point, it should be considered. Many companies wisely charge for service at the point of service, reducing the overall losses in the case of service dining rooms and guest dining rooms. Under this system, all company guest dining that is a departmental or company charge pays full costs for all meals served. In this manner the most expensive burden on a company-operated food service is deployed on a direct pro rata basis to the departments utilizing the service and incurring the cost to the company.

In light of the facts presented, the suggestion is made that the corporate executive responsible for policy decisions governing the employee food service reflect on his own situation. Thought should be given to past policy, present costs, and desired costs. This should lead to management decisions on future costs and service goals.

These decisions can be translated into new company policy to change the type of service, make a capital investment in new equipment, change the policy of management to a contract operation, or make other potential changes.

The employee food service is an employee benefit. It is important to compare it to the cost of other employee benefits (FICA, etc.), measuring both costs and benefit to the employee and the company with that thought in mind.

Executive and employee food services cost money. How much they are worth is a value judgment that each business enterprise must make. Once that decision is made and it is translated into sound operating policy, and effected through good management practices in the food service operation, each company can continue to provide itself with an executive and employee food service program that will both meet its needs and remain within the desired cost boundaries.

### **Footnote**

The main portion of this article was written over 20 years ago and presented to participants of an American Management Association Seminar in New York City. Those participants were all corporate executive personnel responsible for the operation of the executive and employee food services of their respective companies. The problems of that day were the same as the problems of today. Some minor updating of figures and material has been made to that original presentation, but by and large the concepts presented here were originally prepared 20 years ago.