

Technical Guide on Internal Audit of Hotel Industry

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Internal Audit Standards Board
The Institute of Chartered Accountants of India
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New Delhi

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Foreword

The hotel industry has emerged as one of the key drivers of growth of service sector in India. It is not only large employment generator but also a significant source of foreign exchange for the country. With ever increasing use of mobile devices, social media, advanced analytics, and online distribution channels, technology has created new opportunities for hotels to derive more business and operating efficiencies. In the emerging scenario, the industry also faces multiple risks like strategic risk, operational risk, economic risk, compliance risk, disaster risk, human capital risk, reputational risk, etc.

In this challenging environment, Chartered Accountants armed with sound domain knowledge, good analytical skills and in depth understanding of processes can play a critical role. As internal auditors, they can assist organizations operating in hotel industry in ensuring that objectives are achieved, risks are managed appropriately, resources are used responsibly and governance systems are strengthened. I am happy to note that the Internal Audit Standards Board of the Institute of Chartered Accountants of India (ICAI) has brought out this "*Technical Guide on Internal Audit of Hotel Industry*" which is aimed to equip the internal auditors with deeper understanding of this unique and complex industry. At this juncture, I would like to congratulate CA. Charanjot Singh Nanda, Chairman, CA. Sumantra Guha, Vice-Chairman and other members of Internal Audit Standards Board for issuance of this Technical Guide.

I am sure that this publication would further strengthen the skills of our members as internal auditors of hotel industry.

February 8, 2016
New Delhi

CA. Manoj Fadnis
President, ICAI

Preface

The hotel industry has emerged as one of the key industries driving growth of service sector in the country. With scale comes complexity, as the global industry and number of players are ever increasing, and so the hotel industry navigates a tough commercial, regulatory and governance environment. Taxation policies, debt-funding, licensing issues, human resource management, quality of guest services in the era of social media, safety, security, etc., are some of the major challenges faced by the hotel industry in the country.

In this scenario, the roles and responsibilities of the members working as internal auditors in hotel industry has assumed considerable significance. As the "third line of defense", internal audit plays a key role in organization's risk management, and assurance processes. Considering the above, the Internal Audit Standards Board of the Institute is issuing this "*Technical Guide on Internal Audit of Hotel Industry*". The Guide covers in detail all important aspects related to hotel industry. The first chapter provides a brief overview of tourism and hotel industry covering aspects, such as, financing and operating models, return on investments, revenue aspects, etc. The second chapter deals with the role of internal audit which includes managing stakeholder's expectations and internal auditors' viewpoint. The third chapter briefly discusses skill sets of internal auditors required in hotel industry like, behavioral, team management, legal and statutory, analytical, technical, etc. The fifth chapter throws light on areas of specialization which are projects, revenue management, information systems audits, risk control matrices, CAAT based auditing, etc. This Guide also contains Sample IT Application Map in Hotel, Audit Programme of Large Luxury Hotel Chains and also of Standalone Budget Hotels.

At this juncture, I wish to place on record my sincere thanks to CA. Kallol Kundu, convenor of the study group, and other members of the study group, viz., CA. Ranjit Khattar and CA. Praveen Verma for taking time out of their pressing preoccupations to develop this Guide.

I would like to thank to CA. Manoj Fadnis, President and CA. M. Devaraja Reddy, Vice President for their continuous support and encouragement to the initiatives of the Board. I must also thank my colleagues from the Council at the Internal Audit Standards Board, viz., CA. Sumantra Guha, Vice-Chairman, IASB, CA. Rajkumar S. Adukia, CA. Tarun Jamnadas Ghia,

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I am confident that this publication would prove to be immensely useful for the members.

February 9, 2016
New Delhi

CA. Charanjot Singh Nanda
Chairman, Internal Audit Standards Board

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Chapter 1

Objective and Scope of Guide

1.1 The objective of any industry specific technical guide, in general, is to help readers with an insight into aspects beyond a regular study guide. The basic premise is, therefore, that readers are already aware and acquainted with the basic subject matter, and are looking to further hone their skill sets with additional techniques.

1.2 Internal audit is a very dynamic function and has been continually evolving over the past few decades. Over the years, there has been a fundamental shift in perception of stakeholders whereby the internal auditor is no longer viewed as a fault finding machine but one who helps business process owners do their jobs better. In order to live up to the expectations of stakeholders, the internal auditor needs to be a true conscience-keeper, one who is capable and thoroughly passionate about the role and at the same time dispassionate and independent in approach.

1.3 With rapid growth and development in economic boom times, the hotel industry has come of age. Increased travel trade has raised the bar, both in quality of product and service delivery, as well as expectations of the discerning global traveller. The differentiating factor for the hotel industry vis-à-vis others has been its human interface, an environment where 'ladies and gentlemen' serve 'ladies and gentlemen'.

1.4 This Guide needs to factor in nuances of the soft-skill element that is very unlike traditional brick and mortar industries. It is the shades of grey in the blacks and whites of the hotel business that the internal auditor needs to look out for, which is more art than science in a commercial world, albeit within some kind of a line of control.

1.5 The aim of this guide is to help acquaint readers with such nuances of the hotel industry and help individuals equip themselves with skills that they can use to carve out a niche in their offerings of suggestions and advice as internal auditors. This guide is thus only an idea, and like any other idea, will be successful only to the extent it can be effectively deployed or modified to suit a practical situation.

Chapter 2

Tourism and Hotel Industry

Birds' Eye View

2.1 Tourism contributes directly to a nation's GDP, reflected in the total spending on travel and tourism by residents and non-residents for business and leisure. Typically, such spends correspond to the output of hotels, airlines, airports, travel agents and leisure/recreation services that deal directly with tourists, and is calculated from total internal spending by 'netting out' the purchases made by the different tourism industries¹.

2.2 Indirect contribution of tourism to GDP is by way of investment spending (e.g., purchase of aircrafts, construction of new hotels, etc.); Government initiatives, such as, tourism promotions, etc.; spending on goods and services by sectors dealing directly with tourists which includes suppliers to hotels, fuel and catering services in airlines, IT infrastructure services and many more.

2.3 Worldwide, the tourism industry contributed 3.1% to GDP directly in 2014 and 9.8% along with indirect contribution. India, with respective figures of 2.2% and 6.7% lagged in the Asian subset behind most other countries including Thailand, Cambodia, Sri Lanka, Vietnam, Malaysia, Indonesia, China and Pakistan.²

2.4 The silver lining for India appears to be in the projection for the upcoming decade 2015-2025, where the country is poised for the highest year-on-year average growth of 7.2% among all the nations in the world³.

2.5 The existing rooms supply in the organized hotel market in India grew by 11% in 2014-15 over the previous year totaling to 1,12,284 rooms as of 31 March, 2015⁴. On a nationwide basis, branded and/or organized supply

¹2008 Tourism Satellite Account: Recommended Methodological Framework (TSA: RMF 2008)

²WTTC report 'Travel & Tourism Economic Impact 2015'

³ibid.

⁴HVS report '2015 Hotels in India Trends & Opportunities'

grew at a CAGR of 15.3% over the past five years and demand for these rooms grew at a similar rate of 15.5% over the same period. Occupancy moved from 57.8% in 2012-13 to 58.4% in 2013-14 and closed at 60.3% in 2014-15

Hotel Chains – Financing and Operating Models

Financing Models

2.6 The hotel industry is capital intensive, especially, in the Indian context. The funding structure critically determines the sustainability of a hotel project and plays an important role in determining the credit risk profile of the company.

Broad elements in hotel projects

2.7 Typically, a hotel project includes the following elements, all of which can be fairly well defined and would vary depending on the category of the hotel project:

- Land and Site Development
- Building, including interiors
- Plant and Machinery
- Miscellaneous Fixed Assets
- Contingencies
- Margin for Working Capital.

Indicative project cost per room

2.8 As per industry norms, an indicative cost of project per room could be as follows:

- Budget hotels (Three Star) ₹ 30-40 lacs
- Four Star hotels ₹ 60-70 lacs
- Five-Star/ Five-Star Delux hotels ₹ 1 crore and more.

The cost of land is one area, which cannot be specified as a standard and can vary significantly from location to location. In contemporary times, the cost of land has been the single biggest contributor to spiraling hotel project costs.

Various Models of Hotel Projects

2.9 Today hotel projects being set up are of various kinds and, therefore, special financing techniques have to be evolved. Some instances of the evolving types are Hotel-cum-Malls, Hotel-cum-Office Complex or Service Apartments and Hotel-cum-Golf Course, etc., all of which would require separate project financing plans.

Different financing patterns

- Promoters Contribution
- In case the mall is sold, advances from customers would be taken, normally, on a construction-linked pattern and advances would be received based on the progress of construction.
- Term Loans from Bank
- Club memberships in case of Golf courses.

Financing Structure and Consideration – An overview

2.10 The financing structure in the Indian context normally comprises Promoters Contribution by way of Equity and Unsecured Loans, and funding from Financial Institutions and Banks by way of debt or term loans.

Sources of Equity

2.11 This, normally, comprises of promoters own contribution in equity, venture capital funds from investors, public issues or unsecured loans from promoters, relatives and friends. Venture Capital Funds are, generally, available in case of very large hotel projects or in case of large groups having chains of hotels. Unsecured loans from promoters, relatives and friends, normally, comprise around 20% to 30% of the Equity Capital in the company and Banks, generally, stipulate that these unsecured loans cannot be taken out till the loan is repaid to the bank/FIs.

Bank lending considerations

2.12 Financial Institutions, normally, insist on a Debt Equity Ratio of 2:1, implying that 1/3rd of the project cost is to be brought in by the promoter. In respect of purchase of land for the hotel, Reserve Bank of India provides that the promoter has to bring in the cost of land from his own funds as part of promoters' contribution and only there after the Bank/ Financial Institutions can then take it as part of the project cost.

Debt Equity Ratio

2.13 Although a 2:1 Debt–Equity Ratio is acceptable but banks, generally, insist this should not be more than 1.5: 1. In fact, the lower the leverage the better it is for the hotel to service the interest and repayment of principal. It is also important to consider factors relevant under present scenarios, such as, low ARR/ Rev Par on account of competition; low tourist arrivals; increased expenditure in food cost, employee salary; heat, light power and high interest rates.

Debt Service Coverage Ratio

2.14 Another key ratio looked at by the Financial Institutions and also the owners while examining the quantum of funding/ time frame for repayment is the Debt Service Coverage Ratio in the project. The Debt Service Coverage Ratio (DSCR) is explained as the amount of assessable cash flow to congregate the annual interest and principal payments on debt. This is calculated as a ratio of Net Operating Income to Total Debt Service.

Debt service coverage ratio is a benchmark used to measure the cash producing ability of a business entity to cover its debt payments, and a ratio below one indicates a negative cash flow, which is, generally, frowned upon by lenders and allowed, only if, the borrower has sound outside income.

Interest Coverage Ratio

2.15 The interest coverage ratio measures how many times over a company could pay its current interest payment with its available earnings and indicates the margin of safety a company has for paying interest during a given period, which a company needs in order to survive future (and perhaps unforeseeable) financial hardship should it arise. Interest coverage ratio below one indicates the non-sufficient revenues to satisfy its interest expenses.

It may, however, be noted that even though it creates debt and interest, borrowing has the potential to positively affect a company's profitability through the development of capital assets according to the cost-benefit analysis.

Non-conventional debt instruments

External Commercial Borrowing

2.16 External Commercial Borrowing (ECB) is a loan or debt funding raised

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from a foreign entity, and could be commercial loans, buyers credit, suppliers credit and/ or other forms of funding provided by a foreign financial institution or supplier or investor in the company.

ECBs can be raised by hotel businesses in India for a wide range of application including import of capital goods, new projects, modernization of existing projects, etc. ECB in India are approved under the automatic route or approval route, similar to Foreign Direct Investment in India.

A number of hotels corporations are using Buyers Credit for importing equipment from China and other countries, such as, lifts, furniture and fixtures, kitchen equipment, bathroom fittings, etc.

FCNR (B) Loans

2.17 Indian firms are allowed to raise funds through foreign currency loans within the prevailing policy guidelines of RBI. FCNR (B) loans are beneficial to a borrowing company as it may entail lesser interest cost vis-à-vis Rupee borrowings, and borrowers are not required to go to the International market for raising funds as these are available in India reducing the cost of raising funds.

Foreign Currency Convertible Bond (FCCB)

2.18 FCCB is a type of convertible bond issued in a currency different than the issuer's domestic currency. A convertible bond is a mix of debt and equity instrument. It acts like a bond by making regular coupon and principal payments, but these bonds also give the bondholder the option to convert the bond into stock.

Operating Models

2.19 Hotels are typically operated in one or more of the following models:

- (i) Independent hotels
- (ii) Managed hotels
- (iii) Hotel chains and conglomerates.

Independent Hotels

2.20 This is the classical model where an independent or standalone hotel is owned as well as operated by the same person or entity. Such hotels are, typically, family owned and operated, often operating popularly as 'bed and

breakfast' or B&B models, but could also be owned by a proprietor, a partnership firm or corporation.

As a single business, the obvious advantages of this model is the possible autonomy and flexibility of management in defining its policies, procedures, marketing schemes, etc. Such models can quite easily adapt to changing market conditions, but may find it difficult to achieve advantages that conglomerates would enjoy in terms of economies of scale, multinational presence and a globalized branding.

Changing business trends

2.21 Till a few years back, the focus of independent hotels may have been more local than global, or at best 'global' only to the extent of personal contacts or goodwill spread by the word of mouth. The past decade or two has, however, dramatically changed the trend of business and brought independent owned-cum-operated hotels back in limelight. If any single factor is to be credited for this trend, it is the world wide web.

Impact of Online Travel Portals

2.22 With the advent of travel portal 'aggregators', online travel agents (OTAs), Third Party Websites (TPA) and Travel Review Portals, the dynamics for businesses of independent hotels have completely changed with suddenly accessibility from all across the globe. It may not at all be surprising today to find individual standalone hotels garnering business from various corners of the globe through the effective reach of internet portals despite very little marketing activity of its own.

2.23 Internal audits of such independent standalone hotels, therefore, require such businesses to be viewed from a very different standpoint than what was the case pre-internet and pre-globalization.

However, the capital intensive nature of the hotel industry has over the last few decades propelled a change towards segregating the ownership and management or operation of hotels, as discussed in the following section.

Management Contracts

Features and trends

2.24 As mentioned earlier, the ownership and operation of hotels is segregated under this arrangement, whereby, typically, the owner is

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expected to finance, construct and fully furnish the hotel with or without the help of the operating partner.

On its part the operating partner is, generally, a hotel planning and operating expert with the requisite skill sets, competence and experience in managing and operating hotels.

Accordingly, the operator renders technical assistance services in areas of planning, furnishing, equipping and decorating the hotel and further provides technical services to operate the hotel upon its completion. In lieu of such services, the operator charges a fixed technical assistance services fee for its services during planning and construction, and a management fee, generally, in industry parlance, as a percentage of the hotels' Gross Operating Profits.

In terms of rights and obligations, the owner is, generally, responsible to procure all licenses and permissions, albeit with the help and co-operation of the operator. Furthermore, all project related repayments and interest costs are borne by the owner, as also all related rents, taxes, levies, assessments, etc. Accordingly, as the hotel is financed by the owner, all capital assets are to be found in the books of such owner.

2.25 On the operators' part, as a hotel management expert, it has absolute discretion in course of managing the hotel, from recruitment on behalf of the owner, to formulating all operating policies, reporting and control systems, operational procurement, repairs and sales. In all these matters, the operator acts solely as an agent of the owner. In addition, again in the capacity of a hotel management expert, an operating partner may provide group sales and marketing facilities including promotion and publicity. It is often the case that the operating partner may charge a separate fee, generally, as a percentage of sales over and above the management fee mentioned earlier.

Finally, in addition to the above, there may be an element of royalty, again generally, payable by a hotel as a percentage of sales, for use of the brand name. The brand owner may of course be an entirely different entity from both the owner and the operator.

Internal Audit of Managed Hotels

2.26 As evident from the above context, internal auditor has different responsibilities depending on whether his assignment is on behalf of the owner or the operator. If the internal auditor were responsible for the audit of the owning partner, the duty would encompass controls over capital assets of

the company, revenues/ costs/ margins (depending upon the type of arrangement with the operator), project loans, etc. and ensuring its share of profits from the hotel is in line with the terms of agreement and appropriate at the operators' optimum efficiency. On the operators' side, however, the Internal Auditors' role would cover the entire operational gamut of the hotel, from sales and revenue management of a hotel to management of its expenses, internal controls and other facets of operations.

Hotel Chains and Conglomerates

2.27 Large hotel chains and conglomerates, typically, follow a hybrid structure of ownership and management. This means that whilst some of the hotels in the repertoire of a large hotel chain or conglomerate are owned by the entity, there would be others in its bouquet which would simply be managed and operated by them.

Internal auditor of this kind of an organization will be called upon to look at both sides of the coin and will, typically, be one with extensive understanding of the industry as a whole.

(a) Time Share Models

In this business, timeshares are sold at a present date with a right to use 12 months later, hence, financially the timeshare business model requires low capital.

(b) Aggregator/ online market place model

The aggregator partners with hotels/ individuals these are willing to lend their properties to his brand. Once the partnership has been finalized, the aggregator team performs an audit of the hotel and standardize the property as per their standards and finally lists the property under it's brand name. The business model is technology driven.

Hotel Organizations as Auditable Entities

2.28 Creating a structured internal audit programme for an entire hotel organization would entail segregating the same into various auditable entities. The idea is to modularize the entire gamut into manageable units.

Corporate

2.29 The various corporate functions (not necessarily in any order of importance) of a typical hotel corporation and a brief overview of each from

an internal auditor's viewpoint follows. Generic functions that are not unique to the hotel industry are only mentioned here without any elaboration. The structure indicated here is illustrative and the internal auditor would need to review the specific areas where the roles in each of the functions mentioned herein are actually performed in the context of the specific organization which is audited.

Corporate Sales and Marketing

2.30 This is the function that is responsible for preparing the organization's 'marketing and business plan'. From a management review standpoint, it is important to be able to validate that the plan is in accordance with the overall organizational philosophy and risk appetite. On one side is the task of positioning of a hotel in the targeted market segment and on the other is the task of directing the efforts of the sales force towards the stated objective.

2.31 A starting point could be a review of the efficacy of marketing campaigns, advertising campaigns, relevance of participation in travel marts and fairs, and such other marketing efforts. Other reviewable marketing initiatives includes (as applicable) web designing activities, structuring of loyalty programs and sales schemes launched from time to time.

One important financial aspect to be reviewed is the accuracy and appropriateness of allocation of group corporate sales and marketing expenditure across various hotels within an entity and also amongst various legal entities, if any, of the group. Related party transactions as well as domestic and international transfer pricing aspects may be kept in mind during the course of this exercise.

Corporate Engineering

2.32 This function is responsible for two crucial segments of a hotel corporation's expenditure bill, repairs and maintenance (R&M) and energy (also referred as heat, light and power in industry parlance).

From a management review standpoint, one may need to ensure that the function has been able to fairly balance the R&M budget of the organization across hotels depending on priorities, positioning and urgency of requirements. Often, but not always, it is also the responsibility of the Corporate Engineering function to negotiate or help hotels in negotiations of large job or work contracts. If applicable, review of decisions on selection of contractors and vendors and the respective price points will need to be audited here.

The other important role of this function is to set forth the policies and norms of the organization towards energy management. Review of this will need to take into consideration factors, such as, incorporation of industry best practices on energy conservation, use of renewable sources of energy from an environmental perspective and implementing rigorous energy audits. Internal auditors should be equipped or if necessary, obtain technical help to evaluate the efficacy of energy audits undertaken and ensure implementation of suggested measures.

Corporate Information Technology

2.33 This function is responsible for creating the policies around the Information Technology architecture in the organization.

From an internal auditors' standpoint, reviews would, generally, encompass policies and procedures around information security. Typically, this includes review of network and application security, vulnerability and penetration tests, application of organization wide IT security policies through 'Active Directory' (if applicable), robustness of firewalls and gateways, data security measures, mobile device policies. This has been discussed in Chapter 6 of this Guide.

Corporate Finance

Corporate Human Resources

Corporate Security

Devising the security strategy for each of the hotels depending upon the location and threat perception.

Corporate Secretarial and Compliance

Other Policy Making Corporate Functions

Operations

2.34 In contrast with corporate functions indicated above, operations are meant to signify where the actions lie, i.e., hotels. The various functions of hotel operations include Rooms Division, including Front Office and Housekeeping, Food and Beverage Division, Hotel Engineering, Hotel Sales, Finance, Human Resources, Hotel Information Technology and Administration, which is, generally, the General Manager's office.

Each operational function is a subject of internal audit and is extensively

covered throughout the guide. As mentioned earlier, and in greater detail in later parts of the guide, the formulation of an internal audit plan for a specific assignment to ensure coverage of the length and breadth of a hotel organization will require a thorough understanding of the organizational architecture, in accordance to which the resource allocation and internal audit effort should be planned out. Internal audit techniques for various aspects of hotel operations may accordingly be chosen and applied from among the repertoire of subjects covered in various parts of this guide.

Hotels: 360° Business View

2.35 The need for the internal auditor to go to depths of business insights is high, if one has to raise the quality of internal audit assignments from controls and compliance audits to incisive analytical management audits on business performance.

Return on Investment (ROI)

2.36 As highlighted in the opening paragraphs of this Guide, a flourishing or indeed, even a sustainable hotel business model would need to address the needs of the modern customer who is not only a discerning contemporary global traveller but is also up-to-date with the best hospitality practices be it technology, health and wellness, cuisine, amenities or value add-ons. Interpreted in common terms, this would translate as having a direct correlation to the extent of lavish spending on infrastructure creation.

At the same time, equity investors, generally, look at cash-on-cash average return of 10%-15% and an Equity Yield somewhere in the region of 18% to 24% when considering to invest in hotel projects, besides the benefits of tax shelters, etc., for specific projects.

Strategic Planning, Business Architecture and Layout

2.37 In order to deliver the twin objectives of adequate return on investments as well as create a product capable of delivering value for money to the guest, a fine balance ought to be achieved at the strategic planning stage itself.

Decisions need to be taken upfront on whether the objectives are to be achieved by building, for example, a spread out high-end, high-paying, low-volume boutique property or a mid-segment high-volume functional one. Similarly, while building a business hotel for instance, decisions need to be taken at the outset on factors, such as, room size, banqueting and

conference spaces or shopping arcade, business centers, etc. Or for that matter, while creating a restaurant, decisions on whether to go for a niche high-paying, low-cover fine dining specialty versus settling for high-volume all-day dining coffee shop.

Management reviews of the rationale of various strategic plans are not within the scope of this limited technical guide, but the idea is to trigger the thought process within the Internal Auditing fraternity who are called upon to review hotel business and operations. For instance, in order to review the reason for Fine Dining restaurant not doing good business, there may be a need to analyze if a five-course menu (say, as an example) is suited to the ambience of the restaurant.

Renovations

2.38 Renovation decisions depend on the age of buildings, standard of construction and current fit-outs, level of on-going maintenance and strength or competitiveness of the operating market. Refurbishment triggers can also include technology upgrades coupled with an increased desire by hotel owners to focus on the key touch points for hotel guests. Typically, operators and investors work on seven year cycles for room refurbishments and five-year cycles for food, beverage and public areas but this can be extended with well-designed, high-quality fit-out and rolling maintenance programs. With increasingly discerning customers and frequent technological advancement the acceptable time between refurbishments appears to be shortening. To maintain market position, there is often the need to regularly enhance the product to create the perception of a 'new' environment. Renovations may involve one or more of the following:

- Redecoration
- Replacement of furniture, fittings and equipment
- Minor works to improve ease of operation, such as changing door sizes to accommodate larger room-service trolleys.
- Remodeling or rebranding aims to move the hotel into a different market sector, increasing room rates and overall yield. Such a refurbishment involves major works on guest floors, including creating new guest rooms from redundant space, replacement of bathrooms and services, changing room layouts and sizes, adding comfort cooling, introducing new guest facilities, including IT and in-room entertainment, complete replacement of finishes, furniture, fittings and equipment.

Environment

2.39 In the face of growing concerns about borrowing consumption from future generations, and increasing corporate social responsibility, the hotel sector is also under increasing pressure to prove it is driving down its environmental footprint and developing truly sustainable operations. Hotel buildings have significant opportunities to reduce their energy and water consumption and greenhouse gas emissions and the best opportunity to address this is during refurbishment programs and annual capex planning. An efficient hotel can reduce its impact on the environment, and save operating costs for the owner and manager.

2.40 Progressive hotel owners and investors are already aggressively implementing sophisticated building monitoring and control systems to be able to capture energy use, and drive efficiencies and cost savings, positively impacting the bottom line. A number of hotels are undertaking environmental benchmarking. National Australian Built Environment Rating System (NABERS) is the industry standard for measuring and benchmarking the environmental performance of existing Australian buildings. NABERS provides a suite of tools to measure and rate a range of environmental impacts of hotel, office and residential buildings, with retail tools under development.

Some illustrations of specific works could include:

- Solar Panels installation on roof tops - high one time cost but cost effective in the long run.
- Appropriate window systems, glazing and finishes to maximise natural light.
- Smart floor finishes, such as, lighter grade (eco) carpet to boost lighting levels and reduce energy consumption for artificial lighting.
- Selecting more light reflective and harder wall finishes adjacent to windows to improve light penetration and bring light deeper into the room.
- Opening the internal bathroom envelope to obtain natural daylight.
- Replacing electrical heating and cooling plant where possible with gas equipment.

Capex Allocation - Business Prudence

2.41 With tight capital expenditure budgets now par for the course for many hotel operators and owners, a strategic approach is needed to ensure investment is maximized to positively impact on both operational performance and capital value. There are a number of considerations including:

- Age of asset;
- Legislative changes;
- Emerging consumer preferences;
- Energy saving techniques, i.e., green practices; and
- Competitive positioning in the market that will influence the way in which capital expenditure budgets are directed.

2.42 All hotel capital investments should be tested with life cycle analysis, taking into account energy usage now and in the future. Operational costs can come down dramatically by implementing:

- Efficient air conditioning;
- Heating and lighting systems using LED lights and automatic sensor lighting;
- Using eco-friendly products;
- Reducing water consumption;
- Rain water harvesting;
- Recycling STP treated water.

Revenue Concepts

2.43 Hospitality as an industry, particularly, in the luxury segment has in the past decade metamorphosed dramatically from a static, predictive revenue model to a highly dynamic one effectively harnessing the economic arbitrage of market driven demand and supply conditions.

Rate Strategies

2.44 Yield management or popularly called Revenue management is quite aptly captured in the definition: *'...selling the right product at the right time to the right customer at the right price...'*

Here the product is not just a room in the hotel or a dish prepared by Chef in the restaurant, rather it is a whole package of tangibles and intangibles, including the flexibility and refundability of a reservation.

Marketing and Business Plan

2.45 This involves careful planning and is based on the 'marketing and business plan' of the organization. A robust marketing and business plan would first decide on the positioning of a hotel, analyze the market supply and zero in on its possible competitive set. Decisions on specific markets and market segments to target would follow as a result, and would entail deciding if occupancy strategies or rate strategies or a combination of both would work best, depending on the targeted market or segment. Furthering this analysis, the plan should be able to project the market occupancies based on its market penetration analysis and finally project the hotels occupancy levels for a given period of time. Today, a number of software applications are deployed by hotel chains to carry out this simulation.

Pricing Plans

2.46 Based on the overall Marketing and Business Plan, actual pricing strategies are determined. Various types of pricing plans are as follows:

- (i) Long term business at lower rates, but made available for limited room inventory. These kind of businesses are procured typically on corporate RFPs (Request for Proposals) and have a fair deal of permanency, and generally used to fill in a part of the 'base-category' rooms.
- (ii) High-rates for short-term bookings unless the expected occupancy is low and discounts are appropriate.
- (iii) Rate structures even for contracts are defined by room types, to ensure availability of lower rate room-types are limited and the revenue manager can quickly shift gears to sell only higher room type rates on a high demand scenario (such as, corporate deals, events).

Price drivers and current trends

Business Intelligence / City Demand

2.47 For the purpose of effective revenue management, the demand-supply scenario for a given set of business dates need to be available. Specialized consulting businesses have sophisticated data mining and data intelligence

setups that provide comprehensive hospitality industry trends and 'actionable information' on city demand positions including competition landscape. Contemporary hotel organizations often choose to use such data intelligence services to supplement their pricing strategies. Data from such sources could be useful for revenue management analysis from internal audit perspectives as well, and depending on the scale and mandate of assignment, may be deployed by the internal audit function.

Brand Positioning

2.48 The pricing strategy of a hotel depends to a large extent on its brand positioning, especially, in the luxury segment as short term low rate strategies may be market penetrative but may erode the brand equity of the hotel.

Seasonality

2.49 The hotel industry, especially, leisure locations are, generally, seasonal and pricing is factored accordingly. Similarly, business or 'city hotels', generally, have 'weekend' and 'weekday' rates.

'Rate of the Day'

2.50 Another feature of dynamic pricing is the concept of 'Rate of the Day'. This is based on rate slabs worked out by Revenue Managers as various demand points for a hotel. Thereafter depending on the projected occupancy, i.e., demand level based on its 'business on books', the pre-decided rate slab is quoted across the various channels. Most formidable hotel organizations use software to predict occupancy levels for given dates of stay. Such software have their own algorithm for projecting demand based on past trends and a host of complex iterations is built into the system.

Value Add-ons

2.51 Hotels often play on value add-ons to hold on to the rate-strategy of the organization. For instance, it may be prudent to offer varying complimentary services to customers of different market segments whilst still charging the desired rate from each segment. For instance, whilst crew rates may be inclusive of complimentary laundry, business travelers may prefer an internet-inclusive rates. Some hotels earn equal or more amount of revenue from F&B and value added services, hence the strategy is made considering the overall revenue expected based on these rates.

Chapter 3

Role of Internal Audit

Managing Stakeholder Expectations

Board of Directors

3.1 The Companies Act, 2013 and SEBI Guidelines, 2015 has placed onerous responsibilities on the Board of Directors and more, specifically, on the Audit Committee under various sections of the Act, to ensure that an appropriate system of Internal Financial Controls and Risk Management systems has been implemented in an organization.

Practically, in many organizations directors seek independent assurance from the Internal Audit department that the Internal Financial Controls have been properly laid out and that the same are operating effectively. In addition, formation of internal audit function has been made mandatory for prescribed class of companies under the Companies Act, 2013.

Corporate Management

3.2 Managing the expectations of the Corporate Management is like a double-edged sword. Whether under the direct employment or a contract, Corporate Management has an inevitable say in the appointment and remuneration of the Internal Auditor, subject of course to the approval of the Compensation Committee of the Board of Directors. The independence of the Internal Auditor as a conscience keeper is, thus, under a constant spotlight and limited only to the professional integrity and competence of the individual.

On another plane, the intangible subtlety of hospitality service demands a nuanced audit approach as compared to a more straight jacket classical approach that can be adopted in a purely process driven or manufacturing organization. In line with the theme of this guide, it is important to remember yet again that hotel corporate managements today are looking up to Internal Auditors to add value to their businesses, much beyond the scope of just pointing out inadequacy of controls and processes, though no doubt, those objectives are no less important.

Operational Departments

3.3 Operational departments in hotels are, generally, geared to provide exceptional service to guests. Their nature of work requires substantial amount of flexibility, and exceptions to rigid rules of policy are not rare. It is true that operational departments, generally, view Internal Auditors as a policing authority as it sometimes creates impediments for them to exercise such flexibility. It is here that the maturity of Internal Auditors are the most required, as this helps not only to create their perception as business enablers but also helps win their confidence which in turn helps implementation of controls easier.

The Internal Auditor's Viewpoint

Conscience Keeper and Business Enabler

3.4 Internal Audit has, traditionally, been perceived as an orthodox function, often viewed with suspicion, fear or even contempt, and if not anything, at least with a tendency of being avoided. It is important to recognize and appreciate the perception rather than push it under the carpet, lest the momentum the function seems to be gathering with changing times fades away. A comparative view of the contrasting positions of how internal audits were conducted in the past vis-à-vis some of the transforming philosophy, attitude and techniques of modern times is useful, more so in the backdrop of the hotel industry.

3.5 In the early days of Internal Audit as a function in the hotel industry, there was this concept of 'pre-audit', whereby every transaction before completion would be routed through and approved by the internal auditor. This obviously must have given the auditor a sense of 'power' if without his/her approval a transaction could not be completed.

With the advent of information computer systems, one assumes, this practice may have started giving way, as the 'approval' mechanism got incorporated as an extension into the processes themselves. For example, all transactions at the end of the day pertaining to guest stays started getting checked by a 'night auditor' which really speaking dispensed the need of a separate internal auditor again to check and approve every transaction. Similarly with the 'income auditor' or the 'F&B Controller' and so on. Naturally, and again one may only assume, that if each transaction was already checked by an independent person in every process, the internal auditor would have had very little to contribute at the end of the day.

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3.6 Evolution, therefore, must have been a natural outcome for the Internal Audit function. With globalization and increased focus on corporate governance following a spate of earth-shaking scams in the early part of the new millennium, the Internal Auditor regained prominence in an unenviable capacity as a conscience keeper for the organization and was recognized as an important cog in the wheel of corporate governance. Being privy on one hand, to organizational intricacies and nuances, and with the enormous wealth of professional knowledge and competence on the other, the Internal Auditor was in the driver's seat in the capacity of conscience keeper for the organization. In the hotel industry, in particular, transactions points increased manifold times, necessarily to enhance and personalize the experience of the guest with changing times. At the same time, with multi-dimensional compliance requirements, business stakeholders began viewing Internal Audit reviews, not as policing but as assurance that all is well.

With the advent of management and business audits, the Internal Audit function has come a full circle, and is now the 'one-stop-assurance-shop' for all stakeholders in an organization, one that does not impede business but enables it by helping to identify and remove the thorns in its way of progression.

Independent Assurance

3.7 As a logical extension of the role defined above, an internal auditor may also be involved in responsibilities requiring participation in business decisions.

As an example, typically in hotel operations, an internal auditor is often called upon to participate as observers in contracting processes.

Similarly, many organizations seek the internal auditors' participation in 'morning meetings', essentially, as the name suggests, operations management meetings prior to start of a day for planning and prioritizing the events of the day.

As the human conscience provides direction to the mind as to what is right and what is wrong but does not either do something or prevent it being done, so also an internal auditor ought not to lose sight of the fact that despite being a cog in the wheel of business governance, its role is advisory, hence should ensure that independence is not compromised at any cost.

Chapter 4

Managing the Internal Audit Function

General Techniques

4.1 As in case of any internal audit, it is imperative for the auditor to gain a thorough understanding of the business first. It is, therefore, advisable for the internal auditor to spend adequate time in each department before commencement of assignments, *viz.* Front Office, Food and Beverage, i.e., restaurants, bars and banquet halls, Kitchen, Engineering, Sales, Materials, Stores, Health Club/ Spa and other Minor Operating Departments, Procurement/ Inventory Management, Security, Finance & Compliance, Information Technology and Human Resources. Whilst in each department, a process walkthrough for a few transactions from beginning to end would give a fair idea of the activities involved in the process.

Simultaneously, it would be important to understand the data flow across processes and from one process to another including use of technology. This ought to be correlated to the observations from the walkthrough mentioned earlier.

Finally, a good internal auditor would make it a point to spend quality and quantity time with the head of each department to understand the nuances of the trade in each function.

Techniques Specific to the Hotel Industry

4.2 Whilst every internal auditor formulates her own technique of audit depending on the circumstances of each assignment, and it is virtually impossible to compile an exhaustive list of 'techniques', some tips are described here that gives an idea of how to look at new angles to identify the nuances in hotel audits.

Compartmentalization

4.3 The various areas of internal audit of a hotel may to be compartmentalized for better manageability.

For instance, while evaluating say the electricity expenditure of a hotel, it is important to segregate first between guest areas/ rooms, common areas and

office, then further into common (for fixed consumption) and specific areas (for variable consumption), and further mapping of all electricity sub-meters for each area. Once this matrix is ready, the process of evaluation becomes simpler and scientific. The same exercise may then be repeated for every auditable component.

IT Application Map

4.4 A sample IT application map of a hotel is provided in **Appendix 1** for reference. It is advisable for an internal auditor to create a similar map and update the same for any changes from time to time. This will not only help in proper scoping of internal audit assignments depending on the vulnerabilities but will also ensure that the auditor has a birds' eye view of the data flow.

Data Collation and Data Mining

4.5 A lot of management review observations in the hotel business emanates from analysis of trends, and thus, it is important to pre-decide the exercise of data collation for a substantial period of time to be able to use the same for evaluation in future. Further, it is very important for the internal auditor to review the Business MIS (monthly/ daily) to understand the performance parameters (cost variations, revenue variations) and type of exceptions (cancellations, complementary rooms/ services, upgrades, waivers, debtors ageing, inventory, etc.). This will help them in identifying the focus areas of audit and to validate the processes/ controls in place for preventing any leakages around these areas. Additionally, data analytics plays a significant role in identifying potential gaps in the central environment (e.g., procurement of same material at different prices, re-prints at banquets, exceptions from specific user IDs, waivers post checkout, variations in front office and housekeeping data, etc.)

A classic example is evaluation of the application of 'Rate of the Day' in Revenue Management. Analyzing if the application of 'rate of the day' has been judicious is impossible without having an idea of what was the business-on-books for a given stay date on the day when the Revenue Manager was applying the rate slab for that particular stay date. For example for a given date, say, the 17th October, the books may be showing only a 40% occupancy for say, 12th December when the Revenue Manager decided to apply a low rate slab of say ₹ X for reservations coming in on 17th October for the 12th December. However, later if business picks up and occupancy

reaches close to 100% on 12th December, one cannot possibly blame the Revenue Manager for the decision that he had taken based on the business-on-books on the 17th October.

Tracking Multiple Transfer Entries

4.6 The hotel industry, typically, has a high volume of relatively small transactions adding up to large recoverable amounts from customers, unlike say in a consumer durable industry where one purchase is a single large value transaction.

Typically, therefore irregularities tend to remain camouflaged within a maze of transactions. It has often been seen that cases of irregularities are found mostly where a number of entries have been transferred to and fro amongst various accounts so that the audit trail is either lost or it becomes very difficult to untie the transactions to their source. The internal auditor must pay special attention if volumes of unrelated transfer of entries is high.

Audit Programme

4.7 Perspectives, scope and dimensions of Internal Audits could be substantially varying depending on the size, class, category and type of hotels.

Representative audit programme of two different types (a) Large luxury hotel chains and (b) Standalone Budget hotels may illustrate the dimensions of difference, and are provided herewith.

Audit Programme for Large Luxury Hotel Chains

4.8 It is imperative for internal auditors to document an audit programme based on risk assessment of the concerned auditable entity, and assign risk weights before undertaking every assignment.

A typical risk-based audit programme⁵ for large luxury hotel chains may need a plan of audit activities that are relevant to address various risk parameters typical of large hotel chains. Broad classes and categories of risk-based audit parameters provided in the following section may be considered as

⁵ *Internal auditors are advised to use this framework only as a base starting point and add or modify parameters based on the scope of specific assignments*

guiding principles :

Risk-Based Audit Parameters

4.9 Following are Risk-based Audit Parameters

(a) Risk Class: Operational

- Cost Efficiency
- Waste Avoidance
- Work Efficiency
- Adherence to Standards
- Statutory Compliances
- Safety/ Security
- Customer Service/ Delight

(b) Risk Class: Financial

- Accuracy
- Appropriateness
- Occupational Frauds
- Control Weaknesses
- Losses and Pilferage

(c) Risk Class: Strategic

- Revenue Optimization
- Policy Inputs
- Contracting
- Pricing
- IT Security

(d) Risk Class: Other Consideration

- Management mandate
- Non-monitored areas
- Repetitive Issues

4.10 Having reviewed the applicable risk class and respective components, the internal audit programme for specific assignments may then be drawn up and correlated with the respective risk class to ensure all impending risks are covered.

The various facets of typical audit activities covered in audit programmes are provided below. Readers may like to select sections from, or add to the sample below, depending on the circumstances and scope of each audit assignment.

A sample audit programme for Large Luxury Hotel Chains is provided in **Appendix 2**.

Audit Programme for Standalone Budget Hotels

Budget Hotels – A brief

4.11 In India, hotels that are classified 3-star or below with room tariff ranging INR 1000-3500 is, generally, understood to be categorized as budget hotels.

Such hotels cater to both corporate and leisure travellers, though some hotels in this category have become attractive choices for various big corporates to house their trainees or have corporate events and big gatherings as well, as these hotels, generally, have the wherewithal to cater to the basic demands of these segments.

Facilities include clean and well furnished rooms, Wifi, vending machines, air-conditioning, parking, breakfast and lunch arrangements, separate restaurants, 24-hours power backup, fitness centers, gaming and small conference facilities.

A sample audit programme for standalone branded 'budget' hotels is provided in **Appendix 3**.

Chapter 5

Skillsets for Internal Auditor in Hotel Industry

Team Management

5.1 The internal audit teams can be organized on the following lines:

- Central audit team based out of the corporate office which visits various hotels on a periodic basis, either by rotation or based on risk-assessment: While this method may be helpful where reports can be extracted in a central location, there is a risk of dilution of audit effort since presence on the ground is very important for internal audit teams.
- Having a decentralized audit team where the audit team is based out of different locations, reporting periodically to the Central audit team: This helps in better local business intelligence and quicker response to various issues.
- Internal audit performed by an external agency based on agreed scope.

5.2 Operations in a hotel industry are more dynamic compared to, say, a manufacturing or information technology set up since most activities occur on a real time basis with very short turnaround time. Irrespective of how the team is organized, it is important that the internal audit team is dynamic enough to monitor this environment, by closely interacting with different departments.

The internal auditor should obtain sufficient, appropriate information prior to commencement of audit, specifically, on the following aspects: relevant industry and competitive environment, regulatory, and other external factors, applicable financial reporting framework, supplier and customer relationships, and technological developments and relevant regulatory factors.

Apart from the usual methods of obtaining information like review of websites, past audit reports, interviews of key personnel, review of control framework, etc., which are normally used in planning the audit, internal

Skillsets for Internal Auditor in Hotel Industry

auditors can look at the following as well, for managing the audit in the hotel industry:

- Participation in various meetings normally conducted at the hotel, *viz.*, daily operations meetings of departmental heads, customer credit review meeting, purchase committees, etc., to gain insight into the operations.
- Planning of staff deployment in advance so that audits are not intrusive during busy timings, e.g., It may not be prudent to perform stock verification at a restaurant during lunch hours. It may be rescheduled to a lean period.
- Evaluation of team size and mix, including having required specialists for big data analysis/ IT, forensics, etc.
- Reading reports from various external agencies on the sector performance and challenges faced.
- Mystery visit to the hotel to experience the process compliance and identify gaps.

5.3 Managing the audits of hotels, especially, those which are multi-location in nature, involve early planning, deployment of resources and timely communication of findings. The audit plan is generally based on the scope as agreed upon with the audit committee/ governing body, and would be required to cover all the locations/ departments on a rotation basis over a period of time, depending on the relative risk identified.

Certain department/ activities can also be chosen and audited simultaneously at different locations to compare processes. In these cases, adequate care should be taken to ensure that preliminary audit findings are not shared with other locations so that those units resort to covering their tracks intentionally.

While planning, sufficient time and resources should also be budgeted for surprise audits, unscheduled investigations based on fraud, etc.

Technical

5.4 As per The Companies Act, 2013, certain companies shall be required to appoint an internal auditor as may be decided by the Board to conduct internal audit of the functions and activities of the company.

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Having the right mix of different professionals in an internal audit team can ensure that all pertinent risks are addressed. Where the team does not possess the required skills expertise or experience needed to perform all or part of the internal audit, the internal auditor may also either themselves acquire the knowledge or evaluate obtaining technical advice and assistance from competent experts, namely:

- Information technology specialists for analyzing network related issues, including vulnerability and threats (including customer data security);
- Data analysis specialists who can analyse big data for unusual variances;
- Specialists like engineers for energy and safety related audits or marketing review specialists;
- Civil engineers/ architects for project audits;
- Legal experts to assess the regulatory compliance related aspect;
- Forensic specialists who can identify and prevent fraud conditions; and
- Restaurateurs who are proficient in all aspects of the restaurant business (F&B, Banquets).

Legal and Statutory Compliance

5.5 The internal auditor should obtain knowledge of the economy, the entity's business and its operating environment, including its regulatory environment and the industry in which it operates, sufficient to enable him to review the key risks and entity-wide processes, systems, procedures and controls. The internal auditor may evaluate on the following lines :

- Hotels have numerous licenses and statutory regulations (International/ Central/ State/ local authorities, etc.) to be complied with on a regular basis. While some are recurring in nature (excise licenses/ pollution clearance, etc.), some are event based (public performance license/ police clearance, etc.).
- It is, therefore, important that the audit team is aware of the entire gamut of applicable licenses and clearances during the course of audit. An eye for detail is required since there are various conditions

Skillsets for Internal Auditor in Hotel Industry

given in the fine print, the result of non-compliance of which may even result in cancellation of hotel's permit/ imprisonment of key officials.

- It is a good practice for any Internal Auditor to prepare an exhaustive list of all applicable laws and regulations before commencement of audits. A guide of various areas that the auditor is likely to encounter whilst preparing the list is provided in **Appendix 4**.

Behavioral

5.6 The hotel industry stands out from many others in that it involves extensive soft skills and adept human capital management.

Operations facing people are generally good communicators and exude a high level of confidence in their respective roles. It is imperative for Internal Auditors to be able to demonstrate their understanding of hotel operations to cut the ice and encourage the auditee to speak. Data analysis is important but human resource management skills are paramount for this people driven industry.

Finally, unlike strict process-driven industries, the hotel industry demands a lot of flexibility on the part of its employees to service guest specific needs and may often lead to more exceptions than the rule. Here the Internal Auditor must be able to demonstrate maturity in assessment of situations balancing both business and controls to form a fair view for reporting.

Needless, to say, the requirement of any audit team would be to have dynamic individuals, having inter-personal skills who are effective communicators, capable of out-of-the-box thinking and challenging the status quo.

Analytical

Differentiating Analytical Skillset of the Internal Auditor

5.7 The internal auditor needs to have a hotel business oriented analytical aptitude to be able to analyze the performance of a hotel or the chain. Business analytics for the hotel business comprise the following broad statistical parameters. The most significant parameters that are specific to the hotel industry are explained in some detail and those that are generic, i.e., commonly applicable across industries have just been listed here for comprehensiveness.

(i) Financial Parameters

- **Growth**

Compounded Annual Growth Rate (CAGR)

- **Performance**

PBT, PAT and EBITDA

(ii) Statistical Parameters

- **Average Room Rate (ARR)**

Average Room Rate (ARR) is a hotel KPI, which measures the average room rate per occupied room. ARR is calculated as 'Total Room Revenue/ Total Rooms Occupied' and can be used to measure the average rate for a day, week, month or year, or for that matter any period for which the analysis is done.

5.8 The following are nuances and interpretation of ARR :

- ARR is, typically, a performance evaluation of rooms department and is, therefore, an important customary parameter for every manager responsible for hotel room sales. Commonly, the sales and marketing department's efforts are evaluated by a combination of occupancy and average room rate that has been achieved. It is not rare, therefore, to expect various stakeholders in hotels to make adjustments to the figure of ARR and project figures that suit respective performance appraisals.
- Whilst comparing ARR of a hotel vis-à-vis its competition set, it must be ensured that the assumptions of the comparable set are similar. For instance, whilst calculation ARR, some hotel organizations exclude the component of breakfast included in a composite room rate, whilst many hotel organizations do not.
- Room revenue, as noted in a subsequent paragraph is a combination of various market segments all of which may be sold at varying divergent rates. It is also a function of different room types from standard room to exclusive suites, all differently priced products. It may be necessary to segregate these components to evaluate performances of specific sales responsibilities.
- As ARR includes all 'occupied rooms', and not necessarily all 'paid

rooms', it may be worthwhile to separate complimentary and house use rooms. Similarly, it may be useful also to segregate the element of 'retention' charges forming part of the total room revenue for no-shows and/or late cancellations, as these kinds of revenue are typically the outcome of policy and not necessarily attributable to performances of hotel managers.

- A manager may want to increase the occupancy at the cost of the room rate or vice-versa depending on what his performance is likely to be evaluated based on. On one hand, where lowering rates may be detrimental to the market standing of a hotel (besides potential loss of revenue), refusal to sell a room below unreasonable fixed rates may turn away a potential guest, and by norm many further potential guests that the other satisfied guest would have brought in.

RevPar (Revenue per available room)

5.9 RevPar addresses some of the pitfalls of the ARR based performance measurement. RevPar is calculated by dividing the hotel's total room revenue by the total number of rooms 'available for sale' in a given period. RevPar is more a reliable tool in measuring the efficiency of the management in selling rooms than ARR as all out of order, complimentary and house use rooms are deducted from the total inventory of rooms to calculate rooms available for sale.

RevPar Index

5.10 RevPar Index measures a hotel's fair market share of their competitive set's revenue per available room. If a hotel is capturing its fair market share, the index will be 100; if capturing less than its fair market share, a hotel's index will be less than 100; and if capturing more than its fair market share, a hotel's index will be greater than 100. Fair share can be thought of as the subject hotel's "piece of the pie" in the market

RevPar index is calculated as:

$(\text{Hotel RevPar} / \text{Competitive Set RevPar}) \times 100.$

Productivity Parameters

Segment wise business analysis

5.11 The various market segments relevant for the hotel industry comprises

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of Corporates, MICE (Meetings, Incentives, Conferences and Exhibitions), Packages, Public Rates, Rack Rates, Long Stays, Travel Trade, FIT (Free Individual Traveller) and Adhoc.

Segment wise business analysis entails review of productivity, both in terms of room nights and rates in each segment as compared to the 'Marketing and Business Plan' referred earlier this guide. Reasons of variances need to be analyzed and a constructive view ought to be taken if any conscious change in market-mix has been beneficial or detrimental to the interests of the organization.

Channel wise business distribution analysis

5.12 Channels refers to sources through business is garnered in hotels. The various channels of business are Direct Reservations, Voice and Walk-ins, Brand or Hotel websites, and third party channels, such as, OTAs and Global Distribution Systems or GDS.

Each distribution channel plays a different role in the hotel's marketing program. The hotel website reflects the hotel's image and competitive edge; OTAs can boost occupancy in the short term and often helps diversify a hotel's client base; GDS connects hotels with consortia, which are global associations of travel agents that provide hotels primarily with major sources of corporate business.

As in case of segment wise analysis, review of channel wise business distribution must be done against the Marketing and Business plan and variances if any, ought to be analyzed for reasons.

Chapter 6

Areas of Specialization

Projects

6.1 Internal Audit of hotel projects is a technical job and involves understanding of engineering and project management aspects besides the functional areas of contracting, tendering, procurement, costing, quality assurance, etc. Contrary to common perception, it is imperative for internal auditors to gain understanding of the technical aspects even for the most basic job of verifying running bills for contractor payments.

Hotel Project Components

6.2 Typically, a hotel construction project comprises of following illustrative sections and sub-sections (as an example, some figs are cited in case of Civil and Structural works in brackets to illustrate the proportion of the type of specific activity to total cost):

(i) Civil and Structural Works

- (a) Site Development and Earthwork (1-2%)
- (b) Plain and Reinforced Cement Concrete (75-80%)
- (c) Masonry (5-6%)
- (d) Waterproofing (5-6%)
- (e) Flooring (4-5%)
- (f) Painting and Finishing (4-5%)
- (g) Miscellaneous (balance %)

(ii) Plumbing Works

- (a) Internal and External Water Supply system
- (b) Soil, Waste and Rain Water System
- (c) External Sewage and Drainage System
- (d) Water Supply, Drainage, Pumps and Equipment
- (e) Water Treatment Plant

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- (f) Plumbing Panel
- (g) Rain Harvesting Pits / Borewell
- (h) Sanitary Fixtures

(iii) HVAC Works

(iv) Electrical Works

- (a) Circuit cum Point Wiring and Conduiting
- (b) Conduiting and Wiring for Telephone, Intercom, TV and Data cabling
- (c) Sub main wiring
- (d) Conduits for Sub main
- (e) Low tension cables, sub mains cabling and cable trays
- (f) Distribution Boards and Panels
- (g) Installation of Low Tension Panels
- (h) High Tension cabling
- (i) Step Down Transformer (if applicable)
- (j) High Tension Panels
- (k) Installation of Sub-Station equipment
- (l) Rising Mains and Bus Ducts
- (m) Supply of Light Fittings
- (n) Installation of Light Fittings
- (o) Lightning Protection System
- (p) Cost of approvals

(v) Fire fighting

- (a) Fire Pump and Equipment
- (b) Fire Hydrant System
- (c) Sprinklers, Piping and Accessories
- (d) Portable Fire Extinguishers
- (e) Electrical Installation for Fire Fighting System

- (vi) **Sewage Treatment and Disposal**
 - (a) Sewage Treatment Plant
 - (b) Electrical Installation for Sewage Treatment Plant
- (vii) **Interiors (including painting, furnishing items)**
- (viii) **Purchase of Equipment and Fixed Assets**
- (ix) **Purchase of Current Assets**

Conducting the Internal Audit of Projects

6.3 Specialized skillsets required for internal auditors are to be contextualized with respect to three primary documents: (i) BOQ (Bill of Quantities) for a given project, (ii) Technical Specifications and (iii) Contract terms and conditions. The internal auditor should also have some basic training of studying building plans and drawings, and ensure access to the Quantity Surveyor's reports.

6.4 A comprehensive study of the three documents before embarking on the audit will provide the auditor with a birds' eye view of the project activities. Study of the sanctioned building plan will give an overview of the project contours and facilities planned.

6.5 Internal auditing, typically, involves following aspects:

- (a) **The BOQ overview:** Correlating the activities in quantity surveyor reports with the building plans.
- (b) **Assessing BOQ quantities:** Assessing the BOQ quantities planned vis-à-vis quantity surveyors' reports.
- (c) **Analyzing BOQ rates:** One of the best and time-tested reference points is to compare* the BOQ rates is an official 'Schedule of Rates', for example, the Govt. of India's CPWD Delhi Schedule of Rates. For non-comparable rates of comparative significance, time and motion studies may be carried out by the internal auditor.
- (d) **Running Bills:** Quantities billed in running bills should be compared with Engineers' measurement sheets and overall totals tallied with the budgeted BOQ quantities.

* *Necessary adjustments should be made to the quoted rates to discount in special factors such as location, urgency, availability, etc.*

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(e) Building Plans and Technical Drawings: It is also important to correlate the sanctioned building plan with 'as-built' drawings to ensure that deviations are properly accounted for and necessarily reconciled with the revised BOQs, and subsequently in the contractors' running bills.

(f) Understanding BOQ activities: One of the most important but often underestimated requirement is to ensure that the activities billed for by contractors in running bills corresponds accurately to the intended activity listed in the BOQ. It must be remembered that minor variations in language are often likely to be overlooked, say, for instance 'Superstructure RCC Vs. Substructure RCC'.

(g) Extra Items: One of the most important aspects of a project is 'Extra Items'. These are activities planned outside the scope of the original BOQ and negotiated separately, often at very short notices or practically even sometimes after a job has been executed. Care must be taken to ensure that extraneous factors, such as, urgency and imperativeness are not misused to pay higher costs than warranted. Adequate justification and approval should be available for the extra items, including amendment in the budget and impact on overall business plan of the hotel.

(h) Validating measurements: Internal audits may be commissioned at any stage within the project time frame. If the auditor is physically present during the tenure of a project, it may be possible to accompany the engineering team for physical measurements, else one may have to rely on as-built drawings to logically derive the dimensions of various jobs in order to validate the measurements billed in running bills.

(i) Procurements: The internal audit of procurement of capital assets during projects would follow a similar trajectory for internal audit of the procurement function, in general, that is elaborated elsewhere in this Guide. However, in some cases the contracts are awarded on fixed price or item rate basis, in such cases assessment of cost of procurement during the award of contract is very critical. Special attention should be given to the escalation clauses agreed in the contract and the basis of such escalation should be clearly defined.

(j) Project schedule: Auditors should assess the project timelines/ schedule, critical path analysis and process of monitoring/reassessment of project completion timelines. This has direct impact on the revenue as well as the cost of project. Overall project schedule should be available with defined critical paths, regular monitoring mechanism and corrective measures to control the delays. Additionally, the key contracts should include liquidated damages for delays in completion of project.

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(k) Quality control: The quality plans/ parameters are clearly defined in the contractors' scope (including the reporting requirements and adherence to the statutory guidelines/ building code). Internal auditor should look at the timeliness and availability of relevant quality records to review the compliance with quality standards.

(l) Statutory Compliances

(m) Compliances with Labour Laws

(n) Tax Compliance

(o) Capitalization: Involvement of internal audit during the course of, or immediately post capitalization is of paramount importance. Appropriate and accurate capitalization goes a long way in the life of a company to ensure correctness of the Fixed Assets Register (FAR). This in turn ensures proper identification during the life of an asset and at the time of disposal.

(p) Pre-Opening: Shortly after completion of the project stage is the 'Pre-Opening' stage whereby the hotel is handed over to operations for commencement of business.

At this stage, the Internal Auditor plays an important role to ensure that all balances, including assets and liabilities, are properly transferred from the project to operations books, pre-opening expenses are properly categorized and accounted for amortization, and Internal Control Systems of the organization as evidenced by the Risk Control Matrices are properly set up. It is also important to ensure at this stage that all licenses and permissions required to operate the hotel are in place.

Revenue Management

6.6 Some of the auditable facets of the Revenue Management function involves evaluating the following revenue optimization options:

(a) Room-type/ revenue type management– A room type is a class of rooms for which a hotel needs to track availability. Typically, room types are classified as Regular, Pseudo (used for e.g., for posting transactions to non-guest accounts) and Generic. Ability of a hotel to sell out the base room types and then maximize sale of higher room types without resorting to upgrades is the hallmark of good revenue management. This is a technical area requiring specialized audit skillsets such as predictive analytics*.

* Predictive Analysis involves use of data, statistical algorithms and machine-learning techniques to identify the likelihood of future outcomes based on historical data

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Additionally, there are several other areas of revenue maximization which are driven through policies (such as, day use, early check-in/ late checkout, barter, upsetting contracts with corporate, crew, etc.)

(b) Rate Management– This refers to selective acceptance or refusal of reservations based on whether or not certain rate codes are marked as being *available* for the selected dates and number of rooms. This strategy is applied where rate is a more predominant selling criteria vis-à-vis room types. This involves evaluating the revenue managers' rate strategizing abilities, more specifically, how accurate has been the timing of 'opening' and 'closing' rate codes for various reservation dates.

Information System Audits

6.7 Internal auditors have over a period of time developed adequate specialized skills to conduct at least preliminary, if not advanced Information System Audits. Detailed procedures of 'Vulnerability Assessment and Penetration testing' is beyond the scope of this technical guide. A general summary of the auditable areas is provided below:

- Review of acceptable use of internet/ e-mail usage.
- Review of password protection standards.
- Review of Data handling, retention, storage and 'disposal of media' policy
- Review of anti-virus and patch management policy.
- Review of data backup and recovery policy. This helps prevention of data loss due to system failure, disaster, etc.
- Reviewing reports of Technical vulnerability assessment carried out by experts and ensure that valid suggestions are properly implemented to ensure risk of attacks by exploitable vulnerabilities are reduced.
- Review of access controls. Internal audit departments in some hotel organizations are also custodians of the policy of access controls. This ensures that users have access to data and information only on a 'need to know' basis.
- Review of equipment configuration policy. This includes policies implemented to protect internet gateways, firewall and router configurations.
- Review of information classification policy and ensuring that protection measures are commensurate to the risk level of classification.

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- Review remote access policy of the organization which prevents unauthorized access by remote users.
- Review and implementation of organizational policy in respect of personal communication devices allowed in organizational premises.
- Review of asset criticality policy, and ensuring assets are classified according to applicable criticality.
- Ensure IT infrastructure and configuration is uniformly implemented across hotels.
- Review of measures taken to secure risks related to information leaks over wireless networks.
- Review of Internet policy to ensure controls are exercised to prevent inaccurate data and/or misleading information to be passed onto the world wide web.
- Review of Active Directory (AD) (if implemented) or any other network policy mechanism. Active Directory is used in many hotels organizations to implement system protection across the organization through enforcement of group policies. It also ensures that user accounts are adequately protected through uniform password management, account lockouts, etc. AD also helps implement data protection through use of USB and external data transfer devices.

Risk Control Matrices

6.8 The Risk-Internal Control Framework is the mechanism for evaluating the Internal Controls architecture of the organization. **This must be differentiated from, and not confused with 'Risk-based Audit Parameters' discussed earlier.**

6.9 The current regulatory framework has placed onerous responsibilities on the Audit Committee and the Board as a whole to ensure that the Internal Control environment of the organization is in place and working. Some of the important references are as given below:

- Section 134 (5)(e) of the Companies Act, 2013
- Section 177 (4)(vii) of the Companies Act, 2013
- Rule 8(5)(viii) of the Companies (Accounts) Rules, 2014
- Schedule II: Corporate Governance of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 — Part C: Role of the Audit Committee and Review of Information by Audit Committee

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6.10 Whilst the regulatory mechanism places the responsibility on Directors to ensure proper Internal Controls have been laid down in the company, it is often the case that the Directors typically tend to seek an independent assurance from the Internal Audit function.

Where such services are sought of Internal Audit, it becomes an onerous responsibility for the function to deliver, and it calls for specialized skill sets to evaluate the Risk-Internal Control Framework.

6.11 The two principal guiding documents for the Internal Auditor, are: (a) ICAI Guidance Note on Audit of Internal Financial Controls over Financial Reporting, and (b) Appendix 1 of Standard on Auditing (SA) 315, "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entry and its Environment". Essentially, the exercise entails evaluation of the framework in the foreground of the following control components:

(a) Control Environment

- Integrity and Ethics
- Commitment to Competence
- Organization Structure
- Authority and Responsibility

(b) Control Risk Assessment

- Standard Operating Procedures (SOP)
- Risk and Control Matrices (RACM)
- Information Technology (IT) Policies
- Internal and Information Security Audits

(c) Control Activities

- Physical Controls
- Logical Controls
- Business Controls

(d) Information Systems

- Nature of IT Systems

(e) Monitoring Controls

- In-Line Monitoring mechanisms
- Systems and Application logs
- Physical Surveillance
- Control Self Assessment
- Internal Assurance Audits

Management Audit of Business Areas

Marketing

6.12 The marketing activities in a hotel organization determines the positioning of its hotels, and creates the necessary base in a market for sales departments to capitalize on. The facts of this important function from an auditable viewpoint is as follows:

(i) Target Audience

Without a clear target audience marketing cannot achieve the desired results. The target audience determines the mode and place of marketing. Management reviews by Internal Auditor helps determine if marketing activities are (a) aligned to the hotels' business and (b) aligned to reach the intended target audience. For instance, promotion of foreign currency packages cannot be ensured by advertising in domestic newspapers or magazines. As per the latest trends, organizations are moving towards digital marketing/ social media to increase the presence of brand and outcome from marketing activities. Such a real time access to enquiries/ searches done by the guests on a particular hotel, assessment of guests interests through thus social profile. Effective market ensures higher revenue and reduced costs of operations.

(ii) Promotional Packages

A significant marketing activity involves creation of new promotional packages that are then marketed through e-mailers, advertisements, online through social media or through other websites. It is important for Internal Audit to review the cost benefit analysis of such promotional activities, and review if they are aligned with the cost incurred to promote such packages. For instance, expenses incurred on print advertisements should be supported by readership numbers of the magazine or newspaper.

(iii) Website Maintenance

Websites are now an indispensable element of marketing activities. Among other things the look and feel of the websites along with the ease of navigation needs special attention. Website content should be reviewed on a periodic basis by Internal Audit to ensure the correctness of information, rates, inventory position, facilities and also rate parity among different websites selling a hotel. The concept applicable to websites are now extended to mobile apps also, where applicable.

(iv) Marketing Tie-ups

Another important component is various tie-ups done with corporates, online travel agents, credit card companies to promote or co-brand hotels and/or the brand. Productivity of marketing tie-ups ought to be reviewed from time to time to validate continuance of such arrangements.

(v) Road shows/ Stalls in travel fairs

Marketing divisions often organize road shows or put up stalls in travel fairs aimed at promoting awareness about the brand. The effectiveness of such spends are a subject of review in addition to tracking if the objectives of such initiatives are actually achieved.

Managing Travel Review Portals

6.13 Travel review portals are today some of the key influencers of online travel business. Most portals support first hand reviews by guests and, therefore, are able to demonstrate a perception of honest and first-hand information to potential travellers. Indeed, some of the current travel review portals have robust internal controls mechanisms to ensure transparency and lack of bias when reporting such reviews.

6.14 In most cases, such portals allow creation of a plain vanilla 'profile' of hotels free of cost, through which the hotels can have access to guest reviews and also post their comments on such reviews. Depending on the standing of a hotel, it can choose to either avail of the free services or go for a business listing agreement which would allow increased content on such portals including promotion of packages, display of contact details, links of website, etc. Most review portals also have a system of ranking hotels and/or restaurants within a city. Readers will recall the advantage discussed earlier that independent and standalone hotels now have as a result of the changing dynamics and influence of the world wide web.

6.15 There are today third party organizations which provide subscription-based statistical analysis of various facets of hotel business influence of these portals. It is possible for management auditors to form independent views of guest perception of hotels based on guest reviews on these portals, the findings of which can be viewed alongside the hotels' internal guest questionnaire system to gain perception of the quality of service delivery.

The auditor should assess the process followed by company to review the feedback available on leading online portals and measures taken by them to improve the hotel ranking/ rating. Additionally, it is important to review the response given by the hotel management to the negative comments on the website/ social media.

Loyalty Programs

Aims and Objectives

6.16 The primary aim of loyalty programs in hotels is to retain customers by virtue of their loyalty to specific hotel brands. This is sought to be achieved by providing incentives to guests so that they return to the brand and use its hotels time and again.

Structure of the Programs

6.17 Typically, loyalty programs are structured for their members to receive 'points' when they stay at a participating hotel, which they can accumulate and later redeem in a variety of ways. In hotel parlance, crediting members with points is termed 'earning' and redemption by members is termed 'burning'. With increase in popularity, Loyalty programs are increasingly becoming customer centric by providing for cross-industry or cross-branding earning and burning options. What this means is for instance, a member may choose to obtain airline points when staying in a hotel and vice-versa with similar redeeming options.

The programs also offer different tiers to members, with each higher tier providing additional soft perks and benefits, such as, early check-ins and late checkouts, free upgrades, bonus points, toll-free concierge services, etc.

Costs of Running Loyalty Programs

6.18 Generally, the costs of running loyalty programs are segregated into two categories:

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- (a) Marketing and Administrative costs, such as, marketing, customer service and database and web management services and
- (b) Incentive costs, which are basically the bulk, comprising that incurred for the points, opportunity costs of reward room nights and other redemption facilities as applicable, such as Spa, Food and Beverage coupons, etc.

The costs are primarily funded by charging fees from participating hotels as also revenues generated from agreements for third-party partnerships.

Internal Audit of Loyalty programs

Management Reviews

6.19 The primary aim of Internal Audit includes analyzing and identifying contribution of the loyalty programs to a hotel's business and to provide an independent review of their effectiveness. It is not easy to directly relate the contribution of loyalty programs to a participating hotel's business, although it may be possible to derive indirect correlation by analyzing patterns of earning, accumulation and burning of loyalty points. Some pointers for analysis are as follows:

- Ratio of high-income, high-frequency guests to total guests. It is this profile of guest that loyalty programs typically hope to attract and retain by developing their loyalty and preference towards its hotels. Thus repeated returns of this profile of guests is valid justification of the cost of the program (repeat business).
- Conversely, a high ratio of low-income, low-frequency guests would indicate a relatively insignificant influence of a hotel brand's loyalty programs.
- Another trait worth analyzing are trends of members moving from lower to higher tiers. Typically, as members move up tiers, they tend to consolidate their spending within a particular brand or group of brands.
- In order to assess the effectiveness of hotels in leveraging the benefits of loyalty programs, it is worthwhile to assess whether participating hotels are effectively able to use the detailed insight and personalized guest information available through loyalty programs to personalize guest service delivery, or create effective and profile-focused marketing campaigns. Loyalty programs should be able to increase the

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repeat guests ratio to the total business, in addition to attracting more guests due to effectiveness of loyalty program. This is also a fraud prone area and a special focus should be given on the process to redeem the loyalty parts (specially misuse of expired points/ points lying in guest accounts for long duration).

Financial Reviews

6.20 Besides management reviews, there are several financial aspects that the Internal Auditor needs to review in respect of loyalty programs, such as, the following:

- Appropriateness and accuracy of business logic for calculation of earning and burning of loyalty points.
- Reconciliation of eligible reservations / activities vs. actuals for credit of loyalty points to members.
- Authorization process and accuracy of manual and often retrospectively credited points to members.
- Accuracy of invoicing by hotels for points credited on accruals.
- Reconciliation of redemptions with points consumed and balance amounts paid.
- Review of processes related to purchase, use, issue and dispatch of vouchers for redemption.
- Accounting for liability and reconciliation of points earned vs. points burned.

Reservations and Call Center Management

6.21 Call centers are, usually, the first point of contact for potential guests. Usually, all major hotels chains have centralized call centers for handling reservations, although the concept of shared centralized reservation centers is also gaining ground, those which provides services to multiple hotel organizations.

Access to centralized reservation systems are generally through toll free numbers. From a hotel organization's point of view, centralized call center operations help in reducing overall costs in addition to ensuring call standards. Centralized call centers may also handle e-mails made by guests for reservations.

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6.22 Following points may be considered by the internal auditor while auditing call centers:

- Ascertain if the toll free numbers are accessible from regions that they are meant to service. Volume of calls received on those numbers are also useful indicators for the same.
- Call quality review — Random selection of calls are made and heard to judge if call quality is in sync with service standards. The quality can be judged on various parameters, such as, attentiveness, knowledge, etc.
- The internal auditor may also like to carry out mystery calls to judge the call quality based on various scenarios, including analysis of customer complaints related to call center/ reservation.
- Calls abandoned are analyzed to review if the reasons are disproportionate call volume or technical glitches. Appropriate call back facility for all calls abandoned can be reviewed.
- E-mail Quality Check — Process checks are done to ensure all e-mails are adequately answered within the time as mandated by policy. This would include scrutiny of spam mails.
- Ensure PCI compliances for all reservations through Credit Cards.
- Reservation centers may also have a reconfirmation process with guests. It is important to ensure robustness of the process to proactively ensure minimum no-shows or late cancellations.
- Handling of group reservations where apart from rates special attention/ follow-up may be required for ensuring materialization of businesses.
- Review of waitlisted or turned away reservations, especially due to reasons other than a sold-out status.

CAAT Based Auditing

6.23 Extracting meaningful information from multiple oceans of mass data is a formidable challenge for any analyst, and is no different for the contemporary internal auditor. The hotel business, by nature, involves vast number of transactions.

To give an indication, one could easily expect to encounter at least 25,000 to 30,000 transactions in a month whilst auditing, say, a typical 100-room

business hotel in an Indian metropolitan city averaging at a 70% annual occupancy. Given that even mid-sized hotels can be expected to operate on some sort of structured IT system with at least basic RDBMS* (Relational Database Management Systems) in action, it is quite reasonable to assume that various segments of a transaction would be spread across a vast majority of inter-related tables and data structures.

Logically, therefore it is most unlikely that an internal auditor will, from the maze of data, be able to chance upon the proverbial needle in the haystack in the absence of any structured analysis. Rather, it is imperative to follow a method in order to be able to decipher patterns, trends and aberrations, and be guided to structured information that are most likely to yield results close to the assignment objective. CAAT-based audit mechanisms have over the past two decades responded quite formidably to the needs of Internal Audit in general, and quite admirably to users in the hotel industry specifically.

Creating CAAT-based Auditing Mechanism

6.24 Before even embarking on an assignment, it is a pre-requisite to understand the transactional data-flow within the data systems, and how they mirror the execution of any particular process from one mile-post to another. For example, in most Front Office IT applications, transactional data post check-in of a guest resides in transient tables in the database.

6.25 These tables can be uploaded on CAAT tool using a database connector. This data can then be used for performing detailed analysis, detecting inconsistencies and for forensic audits.

Using analytical procedures through CAAT, auditors can facilitate granular analysis of data to determine the accuracy and irregularities.

“Analytical procedures” means the analysis of significant ratios and trends, including the resulting investigation of fluctuations and relationships in both financial and non-financial data that are inconsistent with other relevant information or which deviate significantly from predicted amounts.

Generally, much of the same information is requested and analyzed as in a traditional audit. However, internal audit functions hitherto performed manually are now automated. Customized reports are generated using computers and a standard audit trail is maintained.

* Conceptually, any RDBMS will record data across tables with minimum repetition to ensure least redundancy.

Modern CAAT tools are user-friendly. Large raw data is converted into statistical and analytical data at the click of a button, thereby, saving the auditors a lot of time. After selecting the right data, import that to the CAAT tool and the tool will automatically generate the analytical data. This tool really contributes to the audit efficiency and is generally used to:

- Capture, cleanse, and normalize data to ensure consistency and accuracy irrespective of the quantum or geographical differences;
- Identify trends, pinpoint exceptions and highlight potential areas of concern through automated routines or simple scripts;
- Help in forensic audits by locating errors and potential frauds;
- Based on pre-defined fraud schemes/ scenarios;
- Facilitate structured sampling by employing scientific sampling techniques. It considers all transactions that occurred during the audit period.

Inbuilt Features in CAAT

6.26 CAATs perform statistical analysis by using data mining techniques. Data mining is the process of discovering meaningful correlations, patterns, and trends by sifting through large amounts of data, using statistical and pattern recognition techniques. Some of the inbuilt features in CAAT are:

- Filter/ Display data sorted by expressions and equations;
- Detect gaps and duplicates;
- Merge data in worksheets;
- Create new datasets through queries;
- Summarizing data by groups;
- Perform regression analysis;
- Performs ageing analysis;
- Quickly finds statistical information;
- Split out data by dates or groups;
- Execute complex data stratifications;
- Perform trend analysis;
- Combination of the above.

Selection of CAAT

6.27 The important criteria that are followed in selection of any software are also applicable in selection of CAAT. Since the key requirement is that the results should be of high reliability and accuracy, internal audit teams may either go in for well-established product or self-developed audit software. The following pointers may be considered while selecting a CAAT tool for the organization:

- Determine the enterprise's audit plan, objectives and priorities;
- Determine the scope of the audits;
- Consider the enterprise's technology environment;
- Evaluate the compatibility with existing systems;
- Understand the volume of transactions;
- Choose a user-friendly tool that can access a wide variety of data files on different platforms;
- Check if data confidentiality features are satisfactory.

Learning to Use CAAT

6.28 Some useful ways to learn use of CAAT are as follows:

- The CAAT tools available off-the-shelf come with guide books and CD's. These would be very helpful in learning the basics of the tool.
- If data analysis and audit procedures are fixed, query running can be automated to generate exception reports periodically.
- CAAT user groups are pretty common and can be found all over the Internet. Social networking groups are also in full-swing where problems and solutions are shared within a matter of minutes.
- Subject experts write blogs on each feature covering various concepts and possibilities. Following good blogs would help increase the learning by leaps and bounds.
- ICAI conducts online and direct sessions on using CAAT and some specific CAAT tools.

Limitations of CAAT

6.29 Following are some limitations of CAAT:

- CAATs can be expensive and time consuming to set up, the software must either be purchased or designed;

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- Client permission and co-operation may be difficult to obtain for running CAAT, especially by external internal audit teams;
- Potential incompatibility with the client's computer system;
- The internal audit team may not have sufficient IT skills and knowledge to create the complex data extracts and programming required;
- The internal audit team may not have the knowledge or training needed to understand the results of the CAATs;
- Data may be corrupted or lost during the application of CAATs.

6.30 By using CAAT along with guest details and financial reports, an illustrative list of possibilities is as follows:

- Abnormally low or high room rates;
- Repetitive cases of guests being offered discounts;
- High in-house rooms usage;
- Unoccupied rooms;
- Inconsistencies in guest master data;
- Entries made post office hours/ weekends/ near the Balance sheet date;
- Entries with special attributes – round sums/ reversing entries at period end;
- Stocks with negative value and issues made without inventory;
- Abnormal power consumption;
- Employees with attendance in multiple departments/ with similar PAN number or date of birth;
- Wrong application of payments to debtors;
- Employees with no leaves taken for several months;
- Entries made directly by CFO/ CEO;
- Delays in posting entries/ inventory receipts and issues;
- High discounts offered by same waiter/ POS;
- Different rates for same item;

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- Differences in valuation of inventory among different hotels;
- Inconsistencies in master data;
- Lost Interface transactions;
- Consistent application of taxes;
- Regular areas of guest complaints.

The list is expandable infinitum, subject only to the limits of imagination and creativity of individual internal auditors.

Power and Electricity

6.31 Generally, electricity cost is a major contributor to the total operating cost of any hotel. This cost is incurred in different locations all across the organization and different strategies may need to be adopted for each to maintain optimality. The word 'optimal' is used instead of 'cheapest' on account of factors, such as, reliability and stability of the supply.

Internal auditor needs to acquire the knowledge of various factors contributing to the build up of electricity cost coupled with business perspectives of the hotel in order to do justice towards his roles and responsibilities. Few nuances are illustrated below:

- A major aspect is to ascertain the proper sourcing of the electricity where alternatives are available.
- In order to ascertain alternatives as also for future budget planning, the Electricity Regulatory Commission Order of the to be/present supplier is often very handy. This deals with details and salient features of the electricity tariff, the variability of tariff depending on the type of connection, details of benefit available to a consumer, penalties applicable due to non fulfillment of duty as a consumer, probability of rate fluctuations due to other prevailing factors like, oil and fuel, etc.
- Tariff elements to be looked into are the power consumptions slabs, and sanctioned and peak loads. This would help determine possibilities of reducing consumption and applicability of lower slabs, which considerably reduce the power cost due to lower cost of units.
- Majority of the supplies now a days come with Time of the Day (TOD) factor embedded in the electricity rate, whereby surcharges are levied on peak-period consumption and rebate allowed in lean periods. This

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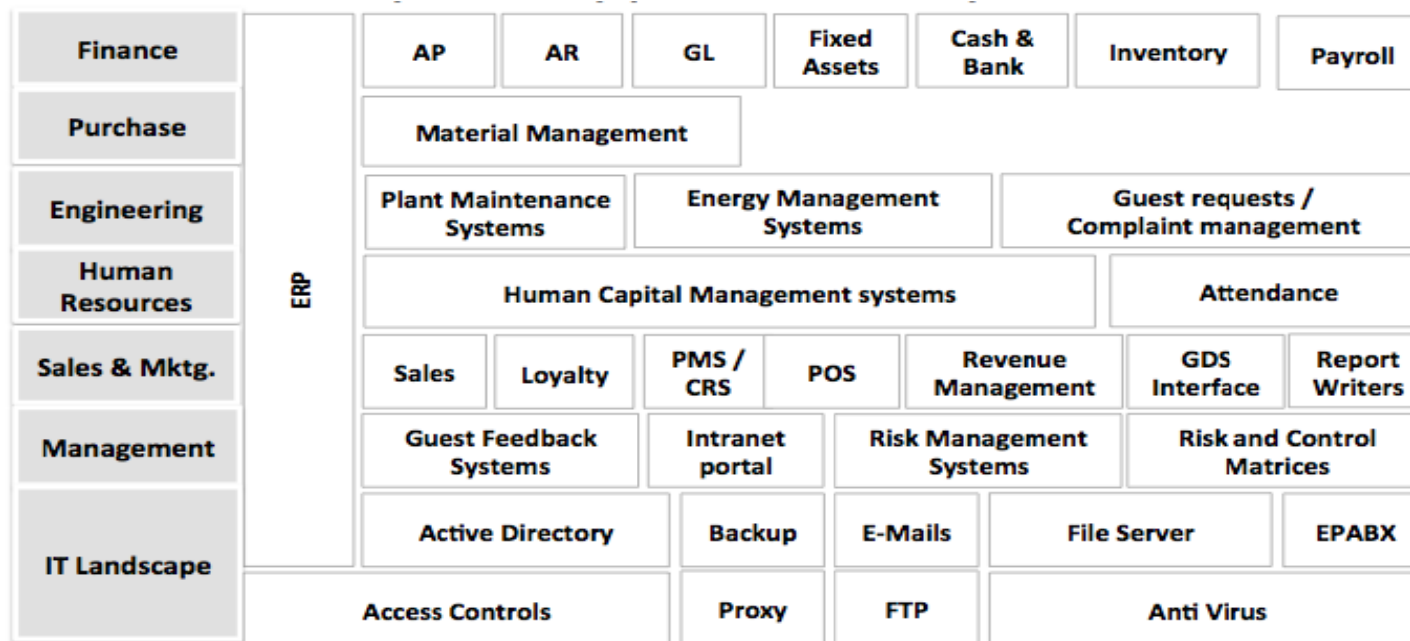
presents a major scope to Internal Auditors in their consulting activity to suggest major shifts in the pattern of production or any other activity which may turn out to be a major cost saver for a hotel.

- Another important aspect to be looked into is the fixation and management of Power Factor level. This accounts for two major benefits, i.e., Power Factor discount and Load Factor discounts which can contribute to savings of around 10 to 12 percent of the total electricity cost. Conversely, improper fixation and handling may result in penalties over and above the normal electricity cost.
- With respect to technical aspects of electricity consumption of various equipment, such as, air conditioning requirements, heating apparatus, steam generation, lighting arrangements and asset procurement, Internal Audit may play an important role.
- Internal Audit may facilitate the organization in management of Energy Audits at regular intervals and ensure proper implementation of measures suggested.
- Apart from the above, Internal Audit should also look into aspects of meter testing, suggest implementations of sub-meters for high consuming areas or equipment, look for suitable cheaper alternatives like PNG etc., play an active role during feasibility and planning to ensure due consideration is given to aspects of energy saving.
- Internal audit can play a key role even in broader aspects, such as, scope of availment of carbon credits.
- Finally, the audit plan or program should include verification of agreement with the electricity supplier, regular checking of availment of prompt payment discounts, determining if there is unnecessary payment of late charges, proper receipt of interest on Security Deposits parked with the Electric Companies, checking of electricity bills at fixed intervals, regular payments towards electricity irrespective of non receipt of bills as otherwise the organization will land up paying penalties due to non payments in time.

Appendices

Appendix 1

A Sample IT Application Map in Hotel



Appendix 2

Sample Internal Audit Programme for Large Luxury Hotel Chains

(A) Central Reservations

- Checking of working of Domestic Toll free number from different cities/ places.
- Checking of working of International Toll free number through different sources. (a) Country-wise call received from different cities/places vs. calls received last year (b) Calls abandoned country wise.
- Listening to calls.
- Carrying out mystery calls.
- Review of quality audit procedure prevalent.
- Check availability of International Toll free numbers in countries with good business potential.
- Comparison of toll free number facility vs. other hotels/ co facility.
- Call back facility for abandonment calls checking.
- Call volume analysis by comparison with respect to previous year growth, etc.
- Reading sample e-mails and ensuring the mail is properly closed.
- Completeness, comprehensiveness, through reply to the satisfaction of guest, follow up, if any, deletion or diversion of mails, if any, non reply/ delay in reply of mails, etc.
- Mystery e-mails.
- Spam mail scrutiny.
- Possibility of mails bouncing back from server and not received/ viewed by Associates.
- Reply to mails received in language other than English.

Appendices

- Solicitation of credit/ debit card details over phone or e-mail. Security of card details stored.
- Marketing tie ups and special promotions.
- Completeness of guest profiles.
- Accuracy of rates offered.
- Checking rate parity at third party website *vs.* brand website.
- Ensuring correct information across third party websites and brand website as regard to facilities, awards, etc.
- Ensuring display of all toll free numbers on website.
- Checking of reservation system from brand website.
- Checking of social media websites, like, twitter, facebook, etc.
- Checking of comment updation by hotels on tripadvisor.com.
- Checking accuracy of data for hotels.
- Reconfirmation checking.
- Ensuring receipt of guarantee for every reservation, especially, for sold out dates.
- Turnaway analysis.
- Review of revenue management process.
- Reconciliation between telephone bills and call actually received.
- Review of Loyalty programmes offered by the group.
- Checking of point's credit under loyalty programmes.
- Checking redemption of points.
- Accounting of liability and reconciliation between points earned and burned.

(B) Front Office

(i) Reservation (Other than those handled by central reservations)

- Review of the reservation process.

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- Accuracy of room rates charged by the hotel reservation team.
- Correctness of rate codes applied.
- Profile checking.
- Appropriateness of value add-ons.
- Appropriateness of room upgrades.
- Unauthorized/ unapproved discounts offered.
- Unauthorized credit extended to guests.
- Correctness of market segments/ channel/ source applied.
- Review of revenue management processes.
- Block management processes.
- Reconfirmation processes including waitlisted procedures.
- Appropriateness of Complimentary and House Use rooms.
- Checking of retentions charged for no-shows/ late cancellations and review of reasons for waiver of retention.
- Mailing of reservation confirmation letter. Adequacy of the terms and conditions in the confirmation letter and mention of requirement of Govt. Issued ID proof.
- Online Rate Management.
- Weekly/ Periodic review and updation of rates on brand website and on third party sites.
- Independent verification of the correctness of the rates updated on brand website and third party websites.
- Ensuring consistency in rates offered in various websites.
- Access for updation of rates on brand websites and third party websites restricted to Revenue/ Reservation Manager or Front Office Manager.
- Comparison of the rates on brand websites/ Third Party websites with the competition hotels.

(ii) Guest Registration and ID Proofs

- Non-collection of valid Government approved ID proof.

- Collection of single guest ID card in 'multi-occupancy rooms'.
- Incomplete/ Inadequacy of Guest ID proof.
- Incomplete information in guest registration cards.
- Registration card not available for the complementary rooms.
- Copies of Passport and Visa documents for foreign guests.
- Room rates incorrectly captured in guest registration card.
- Non-sequential/ haphazard maintenance of Registration cards.
- Lost registration cards due to improper storage.
- Non-recording of guest details in front office software.
- Incorrect details in the front office software.
- Recording of guest details with delay.

(iii) Attending Guest Requests/ Hot Log Sheet

- Non-recording of guests requests/ calls and resolution tracking.
- Inadequate resolution of guest requests/ calls.
- Guest calls not attended or transferred to concerned department.

(iv) Handling guest supplies

- Inventory register not maintained for receipts and issuance of guest supplies.
- Absence of physical verification of guest supply inventory in defined frequency.
- Pilferage in supplies.
- High stocks of supplies.
- Poor upkeep of the stores and spoilage of guest supplies.
- Supplies sold to guests not billed/ invoiced.
- Frequency of surprise checks.

(v) Guest Comment Card/ Feedback Process/ Online Reviews

- Review of the guest comment cards to identify major reasons for guest dissatisfaction.

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- Review of the ratings and guest comments on Trip Advisor and other third party websites.
- Checking if negative guest comments on third party websites are timely responded.
- Checking whether appropriate action is taken based on the guest complaints/ suggestions.

(vi) Early Check-In and Late Check Out

- Early Check-in/ Late check outs waived off without the General Manager/ Operations Manager Approval.
- Early Check-in/ Late not charged as per the hotel policy.
- Reasons for waiver of the early check in/late checkout not recorded.

(vii) Submission of C forms to FRRO

- Adherence to Rule 14 of the Registration of Foreigners rules, 1992, which requires hotels to upload details of foreign nationals in the FRRO website within 24 hours of arrival of the guest.
- Non-filing/ delays in uploading of C-forms.
- Non-capturing of arrival and departure information in the register.
- Incomplete information such as guest confirmation number, guest name, nationality, date and time of arrival, etc.

(C) Housekeeping Management

(i) Linen Inventory Management

- Identify untagged linen.
- Deficiencies in process of discarding the linen.
- Missing linen passed off as discard.
- Necessary approvals for missing/ discard linen.
- Parameters for declaring the linen as discard not mentioned in the hotel policy.
- Linen inventory maintenance at stores and sub-stores not proper.

- Linen register not maintained date wise but based on the month end inventory physical verification.
- Accounting impact of the discarded/ missing linen not properly taken care of based on frequency based physical verification.

(ii) Linen Laundry

- Linen laundry given without presence of hotel housekeeping supervisors, non-acknowledgement on laundry challans by housekeeping.
- Laundry not verified for cleanliness by housekeeping.
- Missing signatures of housekeeping/ laundry partner on challans.
- Over-writings in the laundry challan.

(iii) Guest Laundry

- Guest laundry challans not maintained.
- Acknowledgement on laundry slips not taken by the housekeeping team.
- Delay in delivering laundry.
- Controls missing on complimentary laundry.
- Correctness of laundry rates in line with hotel tariffs.

(iv) Housekeeping Consumables Consumption and Inventory Management

- Controls on inventory of housekeeping consumables.
- Reasons for high/ erratic consumption of consumables.
- Physical verification of housekeeping consumables not done.
- Improper storage of the consumables.

(v) Room Making

- Checklist for room making was not followed.
- No process of confirmation of "room made" by supervisor.
- Physical verification of rooms to confirm the compliance of checklist.

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- Delay in room making causing increase in guest wait time.
- Reasons of out of order rooms.

(vi) Lost and Found

- Lost and found register not maintained.
- Serial number control over lost and found slips.
- Lost and found slips not issued to founder of the goods.
- No records maintained for the timely intimation of lost and found to guest.
- Guest ID proof was not seen/ taken at the time of handing over the goods to guest.
- Process of unclaimed items not defined.

(vii) Packaged Mineral Water

- Water bottles consumption analysis and examining the reasons for upward movement.
- Extra water bottles other than complimentary not billed to customer.
- Control over Issuance of water bottles at front office.

(D) Food and Beverage

(i) Pricing

- Review of Pricing policies and frequency of price revision.
- Ensuring that only systems manager has the rights to change F&B price in the billing software which is subsequently verified by Chef and F&B Manager.
- Ensuring accuracy of F&B rates charged.
- Checking of the Menu rates vs. billing software rates (mismatch multiple rates for same item).
- Comparing of rates with competitive hotels/ restaurants (process of menu re-engineering)
- Access controls to modify menu masters.

- Analysis of open items to assess the need for standard pricing in the menu.
- Open checks/ delay in settlement.

(ii) Process Related Control Aspects

- Appropriateness of discounts given to guests to ensure discounts is approved by appropriate authority and reasons for the same are recorded.
- Reconciliation of the actual count of complimentary breakfasts/meal plans vs. count as per reservation details.
- Ensuring no food is prepared unless a KOT (Kitchen Order Ticket) is received from the restaurant.
- Ensuring void KOTs is signed by the restaurant manager and the chef.
- Verifying the appropriateness of void items and/ or checks.
- Ensuring all restaurant checks are received and verify, if any, hard copy check is missing, by referring to the sequence of check numbers.
- Checking if all the KOTs are billed.
- Ensuring daily sales is tallied with the settlements in cash, credit cards and billed to rooms.
- Accuracy/ appropriateness of food, beverage and tobacco cost.
- Review of reasons for high food cost.
- Monitoring spoilage/ wastage.

(iii) Banquets

- Review of booking process, payment terms and cancellation policy.
- Control over PAX count.
- Billing for flower decoration, rentals for electrical equipment and other items.
- Control over quantity of food prepared and wastage.
- Correctness of banquet food costing.
- Compliance of Luxury tax, Amusement Tax, Public Performance License, if applicable.

(iv) Compliances

- Reconciliation of VAT, Excise and/ or Service Tax charged and deposited.
- Verification of Licenses/ Excise records.
- Ensuring compliance of hygiene and food safety standards as per FSSAI.

(v) Guest Reviews/ Social Media

- Review of the guest comment cards of the restaurants to identify major reasons for guest dissatisfaction.
- Review of the ratings and guest comments on Trip Advisor, Zomato and other third party websites.
- Checking if negative guest comments on third party websites are timely responded by F&B Manager.
- Checking whether appropriate action is taken based on the guest complaints/ suggestions.
- Verifying the correctness of restaurant details such as restaurant timings, type of cuisines, seating capacity, etc. on third party websites.
- Verifying correct and latest menu is updated on review websites.

(vi) Internet/ Telephones

- Automatic posting of Internet/ Telephone costs to guest room folios from the internet/ telephone billing server.
- Reconciliation of internet usage/ calls billed to guests vs. charges paid for internet and calls.
- Review of call quality and internet speed and connectivity.
- Access to update rate master restricted to system manager.
- Review of guest complaints and the measure adopted for resolution.

(vii) In-House Car Rental

- Process of making reservations.
- Process of confirmation of the reservations.

Appendices

- Process of cancellation of reservations.
- Minimum billing in case of cancellation by guest.
- Process of generation of agreement/ duty slip.
- Process of Signing of duty slips by guest.
- Car utilization report to review car wise revenue report.
- Analysis of upgrades and downgrades.
- Appropriateness of Non Revenue KMs (Fueling, Maintenance).
- Review instances of Did Not Use and Did Not Avail, its approval, reasonability.
- Controls over cash sale-daily banking, cash receipts, etc.
- Vouching of duty slip.
- Control over KMs-Revenue/ Non revenue.
- Checking of car log books vis-a-vis duty slips.
- Control over Package KM, e.g., airport pick up/ drop, etc.
- Rate master checking.
- Physical inspection to check whether the car accessories include first aid box, fire extinguisher, newspaper, water bottles, car, magazine, etc. are available in the car.
- Fleet Master checking-correctness of car description, etc.
- Surprise physical verification of Odometer for correctness of logbook recording.
- Drivers Inventory Management - Drivers antecedent verification, License, Badge, movement order and identity proof, etc.
- Drivers Utilization vs. Cars Utilization.
- Expense Reimbursement Process to Drivers - Parking, toll taxes, emergency fueling, conveyance, etc.
- Drivers Cost-Salary, OT, telephone reimbursement, Uniforms, etc.
- Review of attendance system of drivers.
- Car Financing process - Selection of best financier, monthly Interest payment, composition of various financier, closure of loan.

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- Benefits accrued being a commercial user of cars in excise, import rules, ST.VAT and also in price from vendors being bulk buyer, etc.
- Review of car sale process and sales of scarp, such as, tyres, other spare parts.
- Insurance-renewal and expiry of car insurance policies.
- Review of process of insurance claim and status of insurance claims made.

(E) Procurement/ Service Contracts/ AMC

- Process of procurement planning (central and unit/ hotel level procurement, tender vs. non-tender items).
- Checking of Rate Contracting - negotiation process, renewal.
- Checking of Annual Maintenance Contracts - negotiation process, renewal (inclusion of critical clauses, such as, recovery of different cost from vendor due to his inability to supply contracted material services on time and hence, material services sourced from another vendor at higher rates).
- Review of market survey reports.
- Items covered in AMCs vs. Requirement as per the hotels (additional cost incurred for items covered in AMC — reasons and approvals).
- Purchase Orders verification.
- Review of Import procedure, Vendor selection, Negotiation, Approval, Freight forwarder appointment, clearing process, etc.
- Vouching of bills for freight, clearing agent, warehouse charges.
- Advance to vendors.
- Foreign remittance related statutory liability.
- VAT/CST compliance in stock transfer to between hotels, adequacy of insurance, process of warehousing, physical verification of old stocks, etc.
- Reconciliation of pending C & F Forms.
- Physical verification of SFIS licenses in hand. Acknowledgement for licenses with hotels/ units/ bonders/ CHA & Vendors.

- Checking of SFIS licenses utilization.
- EPCG License Master Details, including details of licenses for which export obligation is yet to be fulfilled.
- EPCG Utilization details.
- Export obligations Fulfilled but Bonds not yet cancelled.
- Foreign exchange earnings reporting for the group.
- Emergency purchases (reasons, cost impact and control measures for future).

(F) Engineering

- Review the major energy consumption points in hotel property.
- Verification of the bills of the energy provider.
- Rates charged by the energy provider and its tariff plan.
- Security deposits with energy provider and interest condition.
- Compare the per room consumption and deliberation on identification of unusual trends in such consumption.
- DG performance through the DG log book.
- Diesel procurement and re-order level and pricing of diesel.
- Verification of meters/ sub-meters recordings.
- Condition around DG set, i.e., water logging, seepage, etc.
- Energy conservation measures to be examined.
- Water expenses trends and per room consumption analysis of water on average.
- Raw water delivery from municipality and water quality, i.e., Hardness, TDS, etc.
- Water treatment related items and its cost to hotel.
- Availability of water in the adequate quantity for the guests in hotel.
- Efficiency of machines.
- STP related issues.
- Scrutiny of test reports.

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- Review of research reports conducted.
- Evaluating efficacy of work done vs. work orders.
- Vouching of rates for standard job items.
- Evaluating efficacy of work done for standard job items.
- Work order/ AMC verification.

(G) Accounting

(i) Accounts Payable

- Scrutiny of payment of statutory dues.
- Payment/ settlement process review.
- Scrutiny of vendor database.
- Scrutiny of ageing summary.
- Scrutiny of suppliers' advances/ prepaid expenses vs. adjustments.
- Tax deductions and reconciliation – TDS/WCT.
- Vouching for PJV/ payment processing.
- Balance Confirmations.

(ii) Accounts Receivables

- Examine the credit application moved by the sales team and primary credentials and market knowledge about prospective customer.
- Credit evaluation of the customer by the finance team based on financials.
- Credit review approval checking.
- Examine whether the credit terms offered by the hotel is beyond the corporate guidelines/ SOP.
- Verify if credit has been offered to clients which have been blacklisted or having long pending dues in other group hotels.
- Agreement with the customer and agreeing on terms and conditions.
- Authorized signatory/ connect from clients end to be notified with agreement.

- Credit limit and credit days were not observed during the business with client.
- Credit ageing review and high aging debtors.
- Examine follow up procedures by the sales team.
- Control over payments received through credit cards, correctness of settlements and control over chargeback.
- Correctness in settlement of payments received in bank. Copies of payment advices and mails to be maintained.
- Examine the TDS receivable outstanding from clients.

(iii) Inventory Management

- Physical verification of current assets / inventory.
- Ensuring FIFO valuation.
- Loading of incidental costs to current assets.
- Correct stock depletion of Beverage inventory.
- Correct valuation of circulating stock.
- Checking of issues vs. requisitions.
- Storage facilities and controls.
- Opening-Receipts-Issues-Closing stock reconciliation store-wise.
- Review of par stocks.
- Review of re-ordering levels.
- In-circulation inventory controls.

(iv) General Ledger

- Scrutiny of JVs for all account heads.
- Review of Provisions.
- Inter-Co./ Inter-Unit balances.
- Financial Statements Review
- MIS/ Reporting accuracy.

(v) General Cashiering

- Physical Cash verification.

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- Bank/ Cash Reconciliation statements.
- Banking of cash and cheques.
- IOUs.
- Vouching of reimbursements to and from other departments.
- Petty Cash vouching.
- Night audit/ income audit.

(vi) Fixed Assets

- Review of physical verification process at unit.
- Audit verification on a sample basis for countable items.
- Vouching of purchases and disposal.
- Checking of Depreciation calculation.
- Capitalization and Accounting.
- CWIP.
- Insurance of assets.
- Maintenance of assets (Preventive/ corrective).

(H) HR and Payroll

- Review of attendance systems.
- Master level checking in payroll and attendance software vs. source documents.
- Checking of leave records.
- Income tax computations.
- PF and ESI deductions for employees.
- Review of Manpower Contract terms and conditions.
- Adherence to terms of contract vs. corporate policy and statutory requirements.
- Statutory obligations for manpower contracts.
- Bonus, gratuity and leave encashment calculations.

- Staff advances.
- Full and final settlements.
- Overtime calculations.
- Controls in Salary Processing.
- Training programs.
- Mediclaims.

(I) Statutory Compliances

- Police License/ Registration.
- License under Shops and Establishments Act.
- Registration under the Luxury Tax Act.
- Registration under the Sales Tax Act.
- Registration under Service Tax
- Registration under the Contract Labour Act.
- Registration under the Pollution Control Act.
- Registration under the Provident Fund Act.
- Registration under the ESI Act.
- License for storage of Diesel Oil.
- Sign Board Directions, Neon Signs.
- License to deal in Foreign Exchange under FEMA.
- Building Completion Certificate.
- Copy Right License for Playing of Music.

(J) Hotel Safety and Security

- Screening of guest profile.
- Proper procedure while screening of guest/ baggage will be followed.
- Liaise with local police for the placement of an Armed Police Vehicle for a specific critical period
- Outer periphery needs to be under active surveillance.

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- Strict movement control at Staff gate will be ensured.
- Staff to report any suspicious object/ unusual behaviour within the premises.
- Check the internal controls as to the access to lifts and access to each floor through lifts.
- Check the controls on each exit point from where a possible entry is possible by some intruders. Especially when the property is attached to some mall/ property with other commercial space.
- Fire extinguisher and fire hydrant system in the property.
- Employees background verification/ screening before recruitment.
- Use of CCTV to be examined at some critical points for safety and security of guest and property respectively.
- Emergency plan to handle instances of fire/ power outage/ robbery/ death or severe injury to any guest/ any local threat, etc.

Appendix 3

Sample Internal Audit Programme for Standalone Branded Budget Hotels

(A) Front Office

(i) Reservation

- Review of the Reservation process.
- Accuracy of room rates charged.
- Unauthorized/ unapproved discounts offered.
- Checking of retentions charged for no-shows/ late cancellations and review of reasons for waiver of retention.

(ii) Guest registration and ID proofs

- Non-collection of valid Government approved ID proof.
- Collection of single guest ID card in 'multi-occupancy rooms'.
- Guest ID proof not matching the guest details.
- Incomplete information in guest registration cards.
- No registration card made for the complementary rooms hence no guest ID collected.
- Non-preparation of fresh registration cards for extended stays.
- Unreadable copies of ID proof.
- Copies of Passport and Visa documents for foreign guests.
- Room rates are incorrectly captured in guest registration card resulting in disputes later.
- Non-sequential/ haphazard maintenance of Registration cards.
- Lost registration cards due to improper storage.

(iii) Attending Guest Requests/ Hot Log Sheet

- Non-recording of guests requests/ calls and resolution tracking.
- Inadequate resolution of guest requests/ calls.
- Guest calls not attended or transferred to the concerned department.
- Non-recording of staff member taking the request and call.

(iv) Handling Guest Supplies

- Inventory register not maintained for receipts and issuance of guest supplies.
- No physical verification of guest supply inventory in defined frequency or manner.
- Pilferage in supplies.
- High inventory of supplies in the stores.
- Poor upkeep of the stores and items getting soiled/ spoilt.
- Supplies sold to guests not billed/ invoiced.
- No surprise checks.

(v) Updating Registration Cards in Systems

- Non-recording of guest details in front office software.
- Incorrect details in the front office software.
- Incomplete details in front office software or details captured only for few guests.
- Recording of guest details with delay.

(vi) Maintaining Guest Complaint Register

- Guest complaint register not maintained.
- Guest complaints/ feedback not worked upon.
- Frequency based review of complaint register was not done.

(vii) Cash Handover Booklet

- Excessive cash float.

- Signature of the handover giver and/or receiver signature missing.
- Incomplete details filling in the suggested format, i.e., date, total amount, handover details.
- Release of cash even after sufficient float is maintained.

(viii) Arrival and Departure Register

- Non-capturing of arrival and departure information in the register.
- Incomplete information, such as, guest confirmation number, guest name, nationality, date and time of arrival, etc.

(ix) Submission of C forms to FRRO

- Adherence to Rule 14 of the Registration of Foreigners rules, 1992, which requires hotels to upload details of foreign nationals in the FRRO website within 24 hours of arrival of the guest.
- Non-filing / delays in uploading of C-forms.

(x) Late Checkouts

- Late checkouts are waived off without the General Manager/ Operations Manager Approval.
- Late checkout not charged as per the hotel policy.
- Late checkout had been wrongly charged, i.e., short or excess charge to customer.
- Reasons for waiver of the late checkout was not recorded.

(B) Housekeeping Management

(i) Linen Inventory Management

- Identify untagged linen.
- Deficiencies in process of discarding the linen.
- Missing linen passed off as discard.
- Necessary approvals for missing/ discard linen.
- Parameters for declaring the linen as discard not mentioned in the policy.

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- Linen inventory maintenance at stores and sub-stores not proper.
- Linen register not maintained date wise but based on the month end inventory physical verification.
- Accounting impact of the discarded/ missing linen not properly taken care of based on frequency based physical verification.

(ii) Linen Laundry

- Linen counting process at the time of giving laundry was not proper or deficient, i.e., laundry given without presence of hotel housekeeping supervisors, non-acknowledgement on laundry challans by housekeeping.
- Laundry was not verified for cleanliness by housekeeping.
- Missing signatures of the either of housekeeping or laundry partner on challans.
- Over-writings in the laundry challan.

(iii) Guest Laundry

- Guest laundry challans were not maintained.
- Acknowledgement on laundry slips was not taken by the housekeeping team.
- Delay in delivering laundry.
- Controls missing on complimentary laundry.
- To check the laundry rates in line with hotel tariffs, i.e., effective daily cost impact of laundry on overall cost to guest.

(iv) Housekeeping Consumables Consumption and Inventory Management

- Housekeeping consumables include cleaning agents, cleaning instruments, dusters, wipes, brooms, etc.
- Controls on inventory of housekeeping consumables, i.e., high inventory of certain items, stock out for others, consumption is irregular, etc.

- Understand each type of consumable and accordingly analyse the consumption trends.
- Reasons for high consumption and low consumptions to be examined for possible adverse impact.
- Physical verification of housekeeping consumables was not done in a frequency based manner or method was not correct.
- Storage conditions of the consumables was improper or not on storage principals, such as, 5S.

(v) Room Making

- Examine whether the room making checklist exists or not.
- Checklist for room making was not followed.
- No process of confirmation of “room made” by supervisor.
- Physical verification of rooms to be conducted by internal auditors to confirm the checklist.
- Out of order rooms and since when to be checked.

(vi) Lost and Found

- Lost and found register not maintained.
- Lost and found slips not having pre-printed serial numbers.
- Lost and found slips not issued to finder of the goods.
- No records maintained for the timely intimation of lost and found to guest.
- Guest ID proof was not seen/ taken at the time of handing over the goods to guest.
- Process of unclaimed items not defined.

(vii) Vending Machines

- Understand that how many vending machine are there with the hotel
- Vending machines are not working properly, i.e., premixes inventory in machine not maintained, not accepting money, not releasing the drink/ item bought.

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- Re-order levels are not maintained for the premixes and other required items.
- AMC of the machines not taken.

(viii) Packaged mineral water

- The water bottles consumption analysis and examining the reasons for upward movement.
- Examine that extra water bottles other than complimentary was billed to customer or not.
- Issuance of water bottles at front office is controlled.
- Consumption of water bottles to be linked with the room nights sold in a month.

(C) Food and Beverage

(i) Pricing

- Review of Pricing policies and frequency of price revision.
- Ensuring accuracy of F&B rates charged.
- Checking of the menu rates *vs.* billing software rates.

(ii) Process Related/ Control Aspects

- Appropriateness of discounts given to guests to ensure discounts is approved by appropriate authority and reasons for the same are recorded.
- Reconciliation of the actual count of complimentary breakfasts/ meal plans *vs.* count as per reservation details.
- Ensuring no food is prepared unless a KOT (Kitchen Order Ticket) is received from the restaurant.
- Ensuring void KOTs is signed by the restaurant manager and the chef.
- Verifying the appropriateness of void items and/ or checks.
- Accuracy/ appropriateness of Food, Beverage and Tobacco Cost.
- Review of reasons for high food cost.
- Monitoring spoilage/ wastage.

(iii) Compliances

- Reconciliation of VAT, Excise and/or Service Tax charged and deposited.
- Verification of Licenses/ Excise records.
- Ensuring compliance of hygiene and food safety standards as per FSSAI.

(iv) Guest Reviews

- Review of the ratings and guest comments on Trip Advisor, Zomato and other third party websites.
- Checking whether appropriate action is taken based on the guest complaints/ suggestions.
- Verifying the correctness of restaurant details, such as, restaurant timings, type of cuisines, seating capacity, etc., on third party websites.
- Verifying that correct and latest menu is updated on websites like, Zomato.

(v) Internet/ Telephones

- Correct billing of Internet/Telephone charges to guests.
- Reconciliation of internet usage/calls billed to guests vs. charges paid for internet and calls.
- Review of call quality and internet speed and connectivity.
- Review of guest complaints and the measure adopted for resolution.

(vi) Accounts Payable/ Procurement/ Service Contracts

In line with the size of hotel and nature of operations, there are various areas in which various kind of service are taken from outside vendors:

- Laundry services
- Pest control service
- Cab service contract
- Cable/DTH contract

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- Food services
- Lift's AMC & GENSET AMC.

(vii) Laundry Services

- Rates of the laundry service are competitive.
- Agreement validity.
- Terms and conditions of laundry service were adhered to, i.e., timely pick up, timely delivery, complete documentation, rates charged as per agreement, use of its own vehicle for delivery, counting in presence of housekeeping supervisor, cleaning standards adhered, etc.
- Bills submission on timely basis and checking of quantities from laundry challans.
- Bills approval by housekeeping and internal check by accounts.

(viii) Pest Control Service

- Daily pest control on the unoccupied rooms not done.
- Pest controls are not effective so as to control cockroaches, rodents, spiders, etc.
- Pest control resource(s) was not present in hotel property on daily basis.
- Pest control not done in rooms which are on longer occupancy.
- No process of feedback to pest control agency based on guest complaints.
- Bills submission with attendance and confirmation of service deliverables.
- Register of attendance of pest control resource not maintained.

(ix) Cab Service Contract

- High or low number of cabs were hired.
- Cabs were underutilized vis-à-vis agreed monthly Kilometres.
- Rates of the cab services not negotiated properly.

- Latest developments in cab services, i.e., on-line cab services corporate solutions were not examined.
- Safety standards of the cabs not confirmed.
- Cleanliness of the cab was not checked by the hotel.
- Drivers were not trained in line with hospitality standards.
- Billing by vendor and its recovery procedure from guests.

(x) Cable/ DTH contract

- The quality of TV channels through DTH was not good.
- Best pricing had not been obtained from vendor.
- Free channels by vendor.
- Examine time of contract, i.e., annual/ two years/ three years as the pricing has impact of longevity.
- Continuous focus on the DTH plans to suit the customer preferences.

(xi) Food Services

- Agreement with the food service outsourced agency not entered.
- Food related controls not examined or not made part of the contract. Microbiological reports may be done for food in a surprise manner.
- Rates of the food were not decided in a competitive manner.
- Compliances to applicable laws by the food service vendor.
- Billing by vendor and its recovery procedure from guests.

(xii) Lifts' and GENSET AMC

- Verify the warranty records of Genset and lifts.
- Verify the service reports during the service warranty.
- Paid service reports and type of records to be checked.
- Cost of service paid are as per AMC agreement.

(xiii) Other Significant Expenses

Besides the service contracts, there are certain more expenses which are significant and seen in this category of hotels which includes:

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- Utility bills and fuel expenses,
- Advertising expenses,
- Management fees under Hotel Management Agreements (HMA).

(xiv) Utility Bills

- These expenses include electricity bills, GENSET management, water and water treatment plant related expenses, water tanker bills, etc.

(xv) Electricity and GENSET Expenses

- Electricity and GENSET expenses are inversely proportional to each other and hence to be seen in an integrated manner.
- Understand the infrastructure of hotel in relation to electrical fittings and energy concept, i.e., concept of LED lighting is from the project stage or after construction hotel is shifting to these energy conservation measures.
- Understand the major energy consumption points in hotel property in each of the season.
- Verification of the bills of the energy provider as it could be a Govt. Utility or Mall authority. Rates charged by the energy provider and its agreement/ tariff plan to be confirmed.
- Security deposits with energy provider and interest condition, if any, on such deposit.
- Compare the per room consumption and deliberation on identification of unusual trends in such consumption.
- DG set primary checks procedures are essential to check to ensure proactive controls on DG function.
- DG performance through the DG log book and comparing the no. of units generated per unit of diesel.
- Diesel procurement and re-order level and pricing of diesel should be consistent with market rates.
- Decision as to selection of the size of DG should be documented and approved by hotels technical team.

- Verification of meters/ sub-meters recordings on daily basis to ensure correct number of units billed to hotel. Any variance to be reported and discussed with management.
- Agreement with the Mall/ Property owner to be reviewed for electricity and DG related conditions.
- Condition around DG set, i.e., water logging, seepage, etc. could be observed minutely.
- Energy conservation measures could be examined across the property.

(xvi) Water and water treatment plant

- Water expenses trends and per room consumption analysis of water on average.
- Understand the raw water delivery from municipality and water quality, i.e., Hardness, TDS, etc.
- Water treatment related items and its cost to hotel.
- Ways to ensure that water is always available in adequate quantity for the guests in hotel.
- Water tankers need determination and approvals to be checked specifically and quality of the water to be tested before release to hotels tank.

(xvii) Advertising Expenses

- The advertising expense, in general, involves the outdoor home media as it is reasonable and reach is up to masses.
- The timing of the advertisement is selected to optimize the cost, i.e., high times of Indian festivals and events in any nearby place.
- Other brand building measures, i.e., listing of properties on the various websites, gifting, etc.
- As the target market is clear and concept of selling is strong, the advertising expense is done to a reasonable extent.
- Keeping above background in mind, the internal auditor should approach on this expense review.

(xviii) Hotel Management Agreements

- Hotel management fees are paid based on the agreement between the owner and the operator.
- Agreement conditions are to be minutely checked and fees calculations are to be checked so that there is no future calculation issues in various kind of management fees, i.e., base management fee, Incentive management fees and sales contribution.
- Monthly reconciliations may be checked to ensure the correctness as the calculation may have certain underlying figures which may change slightly.

(xix) Accounts Receivables

- Examine the credit application moved by the sales team, primary credentials and market knowledge about prospective customer.
- Credit evaluation of the customer by the finance team based on financials.
- Credit review approval checking.
- Agreement with the customer and agreeing on terms and conditions.
- Authorized signatory/ connect from clients end to be notified with agreement.
- Credit limit and credit days were not observed during the business with client.
- Credit ageing review and high aging debtors.
- Examine follow up procedures by the sales team.

(xx) HR and Payroll

- Review of attendance systems.
- Master level checking in payroll and attendance software vs. source documents.
- Checking of leave records.
- Income tax computations.
- PF and ESI deductions for employees.

- Bonus, gratuity and Leave encashment calculations.
- Staff advances.
- Full and final settlements.
- Overtime calculations.
- Controls in Salary Processing.

(xxi) Statutory Compliances

- Police License/ Registration.
- License under Shops and Establishments Act.
- Registration under the Luxury Tax Act.
- Registration under the Sales Tax Act.
- Registration under Service Tax.
- Registration under the Contract Labour Act.
- Registration under the Pollution Control Act.
- Registration under the Provident Fund Act.
- Registration under the ESI Act.
- License for storage of Diesel Oil.
- Sign Board Directions, Neon Signs.
- License to deal in Foreign Exchange under FEMA.
- Building Completion Certificate.
- Copy Right License for Playing of Music.

(xxii) Hotel Safety and Security

- Check the internal controls as to the access to lifts and access to each floor through lifts.
- Check the controls on each exit point from where a possible entry is possible by some intruders. Especially, when the property is attached to some mall/ property with other commercial space.
- Fire extinguisher and fire hydrant system in the property.
- Employees background verification/screening before recruitment.

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- Use of CCTV to be examined at some critical points for safety and security of guest and property, respectively.
- Emergency plan w.r.t any fire/ power outage/ robbery/ death or severe injury to any guest/ any local threat, etc.

Appendix 4

Applicable Laws and Regulations – Illustrative Areas to look for

(i) Front Office

- Acts relating to Foreign guests, currency
- Star categorization
- Smoking zones

(ii) Food and Beverage / Kitchen

- Liquor and restaurant licenses
- Food safety standards
- Event specific clearances
- Metrology
- Excise – Local and Central

(iii) Housekeeping

- Use of permitted chemicals
- Garbage disposal

(iv) Engineering

- Electricity related laws
- Water and Sewerage
- Pollution Control
- Approvals for use of equipment like, elevators, boilers, DG sets, etc.
- Sewage treatment
- Fire and property
- Water bodies related laws

(v) Human resources

- Shops and catering establishment related laws
- Retirement dues
- Apprentice rules
- All Labour Laws
- Harassment regulations
- Statutory holidays
- Security laws
- Contracting laws

(vi) Finance

- All direct and indirect taxes
- Customs clearances
- Export benefits
- Licenses management

(vii) IT Systems

- Software licenses
- Internet services
- Mobile towers and Communication devices