

## Unit- I      **TARIFF STRUCTURE**

### **BASIS OF CHARGING**

Different hotels follow different policies while charging tariff from their customers. Following are the common basis on which tariff is charged:

1. **12 noon / Check-in, check out basis-**

It is the most common & convenient for both hotel and guest to fix a check-in and check- out time.

Most commonly hotels fix 12 noon as the check-in & check-out time.

If a guest checks in at the check-in time decided by the hotel and checks out next day at the same time, then he will be charged for one day. But if he exceeds the check- out time, he may be charged for two days.

2. **24 Hour Basis –**

There are some hotels that charge according to 24 hour basis. The time when the guest checks-in becomes the check-out time for guest.

The guests are charged one day rent only when they have spent 24 hours or a part of 24 hours in the hotel.

3. **Number of Night basis –**

There are some hotels that charge the room rent on the basis of nights spent in the hotel.

If a guest spends one night, then he is charged for a day and if he spends two nights, then he is charged for two days.

4. **Day Use –**

Sometimes a guest wants to stay in a hotel for few hours only (maximum 6 hours). These guests are charged room rent on day basis irrespective of the check-in and check-out time.

## ESTABLISHING ROOM RATES or ROOM TARIFF FIXATION

### 1. **Market Based Pricing** –

Market based pricing is setting a price based on the value of the product in the perception of the customer. The concept is based on an idea of what the ultimate consumer /guest is prepared to pay and then use it as a starting point. In this case, a hotel work backwards as it first makes an accommodation product available at a price that a guest is willing to pay, then it tries to cut down on the cost to achieve a reasonable rate of return on that basis.

Some common methods of market-based pricing are:

- a. **As per competition**: Arriving at a price based on competing hotel's rates.
- b. **Market tolerance**: Checking competing hotels' Best Available Rates (BAR) for a room. These rates can be found out by hotels by calling up the competing hotels without disclosing their identity.
- c. **Rate cutting**: Lowering of rates to increase occupancy levels, specially during off-seasons.
- d. **Inclusive and non-inclusive rates**: Charging room rates on the basis of meals, provided on CP/ MAP/ AP basis.

### 2. **Cost Based Pricing** –

Cost based pricing is a room rate/rent determination technique that covers the basic cost of operations at a given level of service, plus the predetermined percentage of return on investment. It involves the determination of total costs (fixed costs + variable costs) associated with a hotel. Managers add a desired profit margin to each unit, such as 5 or 10 percent mark-up. The goal of the cost-oriented approach is to cover all costs incurred in producing or delivering the products or services and to achieve a targeted level of profit.

Selling Price = Total cost + Fixed profit percentage

Merits –

- Simple method
- Does not involve examining the market or considering the competition and other factors that might have an impact on pricing.
- Popular method as it uses internal information that managers can easily obtain.

The following are the two widely used cost-based pricing techniques –

- A. Rule of Thumb Approach
- B. Hubbart Formula

#### **A. Rule of Thumb Approach –**

- Oldest/Traditional method of determining room rate of a hotel.
- The Rule of Thumb Approach sets the rate of room at \$ 1 for each \$1000 of construction and furnishing costs per room, assuming a 70% occupancy.
- For example – Hotel ABC incurs a total expenditure of Rs.15,00,000 on a room, the room rate will be Rs. 15,000.
- This approach fails to consider the effects of inflation.
- It also fails to consider the contribution of other facilities and services towards the hotel's desired profitability.

#### **Consumer's Profile:**

- It is important to keep in mind the social & financial status of the guest i.e. paying capacity of the guest in mind.

#### **Standards of service:**

- While deciding the tariff of the room, standards of service should be kept in mind as the standards of service is the USP of the hotel and contributes towards the profitability of the hotel.
- Higher the standards of service, higher is the room rate.

#### **B. Hubbart's Formula –**

This is a scientific way of determining the room rent, was developed by **Roy Hubbart in America in the 1940s**. It resolves all the problems of the Rule of Thumb Approach, as Rule of Thumb Approach is an old traditional and unscientific way of determining the room rate of a hotel.

The steps involved in calculating the room rent/rate according to Hubbart formula:

#### **Step 1:**

- Calculate total investment.

Total investment = Owner's capital + Loans

- Calculate return on investment. Return on Investment is the percentage of return that would have been generated had the amount been invested in the open market.

$$\text{ROI} = \text{Total investment} \times \text{Return percentage}$$

**Step 2:**

Calculate total expenses.

Total expenses = Operating expenses + Taxes and Insurance + Interest paid on loans + Depreciation on book value

**Step 3:**

Calculate gross operating revenue.

Gross Operating Revenue = Total expenses + ROI

**Step 4:**

Find revenue generation from room sales only, by subtracting revenue generated by all sources other than rooms from the gross operating revenue.

Revenue to be generated by room sales to cover cost and fair ROI =  
Gross Operating Revenue – Revenue generated from other sources

**Step 5:**

- Calculate total number of rooms available during the year.

Total no. of rooms available during the year =

Total no. of rooms in the hotel x Number of days in the year

- Make the provision for expected average occupancy that is expected during the year. This step will provide the total number of rooms available for sale.

Total no. of rooms available after making the provision for average occupancy =

Total no. of rooms in the year x Occupancy percentage

**Step 6:**

Calculate Average Daily Rate (ADR). This will cover the cost of operations and fair return on investments.

ADR =  $\frac{\text{Revenue to be generated by room sales (Step 4)}}{\text{Total no. of \#s available (Step 5)}}$

## Cost Based Pricing versus Market Based Pricing

As compared to market-based pricing, cost-based pricing is more scientific and practical as it takes into account factors like the rate of return on investment, operating cost, overheads, fair profit, etc. In market-based pricing, one can get the advantage of selling the same product over a range of prices.

## TYPES OF RATE

### **Room Tariff Card –**

It is a document published by the hotel for use by prospective guests. It includes prices of various rooms and meal plans.

### Different rates for a hotel guestrooms include –

1. **Rack Rate:**  
This is the rate printed on the room tariff card. This rate is usually negotiable as it is the highest published rate of rooms. It is a rate before any discount.
2. **Crib Rate:**  
It is a special rate charged for children above 5 years and below 12 years of age who are accompanying their parents. The hotel provides a crib (baby bed) in room for infants.
3. **Corporate Rate:**  
This is a promotional rate to attract the corporate market segment. This rate is generally 10 to 20 percent lower than the rack rate.
4. **Seasonal Rate:**  
Hotels may offer different rates for different seasons. Destinations may have high, low, and shoulder seasons. The duration when the tourist traffic at a particular place is high is known as the peak season; when the demand for hotel rooms drops down, it is known as off-season rate. Hotels in these locations mention their seasonal rate and off-season (discounted) rate.
5. **Advance Purchase Rate:**  
Though popular in the airlines industry, it is a new concept in the hospitality industry. It entails heavy discounts on room rates when room bookings are done in advance. The rate of discount depends upon the advance period and the number of rooms available for the time of booking. For instance, a hotel may offer more discount for a room that is booked two months in advance as compared to a room that is booked fifteen days in advance.
6. **Week Day/ Weekend Rate:**

The demand for hotel rooms may be more on certain days in a week. Hotels analyse their demand levels over a period of time and fix a higher rate during high demand periods and a lower room rate during low demand periods.

**7. Day and Half Day Rate:**

The day rate, charged from guests not staying overnight at a hotel, is lower than the rack rate. Sometimes, a guest may wish to stay for a very short duration of time, not exceeding six hours. In these cases, the half day rate, which is a bit higher than the numerical half of the rack rate, is charged from guests.

**8. Group Rate:**

As a large group (15 and more than 15 persons) provide bulk business to a hotel, hotels offer discounted rates to groups.

**9. Travel Agent Rate:**

Travel agents sell travel products like hotel rooms, airlines bookings, etc., on a commission basis to the guests. They provide a substantial amount of business to hotels, hence hotels offer them special discounts.

E.g. Of travel agencies – Thomas Cook, Cox & King, SITA Travels etc.

**10. Company Volume Guaranteed Rate: (CVGR/CGVR)**

Hotels may offer a special rate (lower than the rack rate) in order to attract high volume of business from special market segments like Companies. A hotel may have a contractual agreement with a company, according to which the company's representatives are entitled to a special discounted rate when they reserve a room in the hotel. The percentage of discount will depend upon the volume of business promised and the mutual understanding between the hotel and the company at the time of making agreement.

**11. Airlines and Crew Rate:**

A special discounted rate for the crew of one or more airlines that offer certain volume of business throughout the year on a consistent and continuous basis.

**12. Government Rate:**

Some hotels offer special discounted rates to Government Officials when they are on an official tour and staying in a hotel.

**13. Educational Rate:**

These are special rates offered by hotels to students and educationists, as they are a significant source of business because of their large numbers and frequency of travel.

**14. Membership Rate:**

These rates are offered to guests who are members of influential organizations like FHRAI, United Nations etc. The rates are much

lower than the rack rate and may also include discounts on food and beverage.

**15. Introductory Rate:**

This rate is offered by the hotel on the opening of a new property in the town. This rate is generally offered to attract guests and is offered till the hotel is established in the market.

**16. Complimentary Rate:**

When a hotel does not charge the room rent from a guest, it is called complimentary rate or Comp. rate/ room rate. Hotels generally offer such rates to tour/group leader, tour operators, travel agencies, and local dignitaries who are vital to the public relations programme of the hotel.

**17. Package Rate:**

A package rate is quoted for the bouquet of products or services. The rate is generally lower than the sum total of the prices of individual products or services offered in the bouquet. It is a market strategy to sell the slow moving items along with hot selling products.

Hotels may offer the following packages-

a. Meeting package

(May include residential arrangement of delegates, meeting room, meals, tea/coffee, snacks, audio visual equipment etc.)

b. Meal package

(Includes room rent and meals)

c. Marriage package

(Includes all the necessary arrangements for marriage, like mandap, priest, party hall/lawn, accommodation for the marriage party, arrangement of reception buffet, and even a complimentary room/suite for the newly wedded couple)

d. Holiday package

(Includes transportation, accommodation, meals, guide, and sight-seeing at the destination)

**18. Tour Group (Series Group) Wholesale Rate:**

These are heavily discounted rates for wholesalers who operate a series of tours for groups arriving and departing together.

For example, a tour operator may conduct a week's tour of the Golden Triangle (Delhi-Agra-Jaipur-Delhi) on the 2<sup>nd</sup>, 12<sup>th</sup>, and 22<sup>nd</sup> of every month for group of 20 persons.

The tour operator guarantees the hotel that it would provide this series of business every month for a period of one year. In return, the hotel offers a heavy discount to the operator and allocates or 'blocks' rooms for the series for the entire year.

### **Assignment – (Room Tariff)**

1. Explain the various meal plans in detail.
  2. Define/ explain the following key terms:
    - i. Hubbart formula
    - ii. Rule of Thumb Approach
    - iii. Market-based pricing
    - iv. Occupancy rate
    - v. Room tariff card
    - vi. Room tariff/ rate
  3. Why should a hotel have different types of room rates and room categories? Write your answer in points.
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### **Bibliography**

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