

**HOTEL OWNER / OPERATOR STRUCTURES: IMPLICATIONS FOR
CAPITAL BUDGETING PROCESS**

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ABSTRACT

The findings of a field study concerned with appraising capital budgeting process implications arising from different owner / operator structures employed in the hotel industry are reported. Dimensions of conflict that can arise between hotel operators and owners are examined. Consistent with expectations motivated by agency theory, data collected suggest that capital budgeting systems in hotels operating under a divorced owner / operator structure exhibit more formalisation and a greater propensity for investment proposal cash forecast biasing. These findings suggest a degree of dysfunctionality associated with the divorced / owner operator structure widely adopted in the hotel industry.

Key words: Hotel, Capital Budgeting, Ownership structure, Agency theory.

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1. Introduction

The degree of research endeavour that has been invested in surveying capital budgeting practice is apparent from studies attempting to synthesise and generalise findings to wider populations (e.g., Aggarwal, 1980; Pike, 1996; Sangster, 1993). While the survey method has predominated in capital budgeting research (e.g., Kester et al, 1999; Lamminmaki et al, 1996; Pike, 1996; Trahan and Gitman, 1995), there has been significant recent growth in the application of field methods (e.g., Carr and Tomkins, 1996; Harris, 1999; Van Cauwenbergh et al, 1996).

This study is concerned with capital budgeting in hotels. In terms of the considerable extant capital budgeting literature, it relates most closely to the work of Collier and Gregory (1995). Like Collier and Gregory, it employs a field study approach to investigate hotel capital budgeting practice. Unlike Collier and Gregory's study, which abstracted data at the corporate level of hotel companies, this study focuses on the hotel operating level. Collier and Gregory (1995) cite three factors motivating capital budgeting research in the hotel industry:

1. Hotel groups can be seen to be relatively unusual due to the dual nature of their activities involving property and management.
2. The hotel industry is characterised by high capital intensity, assets with a long life and negligible obsolescence if adequately maintained.
3. The hotel industry is a significant player in the large and expanding tourist industry.

There appears, however, to be another, and perhaps more significant factor motivating further capital budgeting research in the hotel sector. The industry is characterised by a somewhat idiosyncratic ownership / management structure, and it is this particular facet of the industry that is central to the focus of the study reported herein. In the hotel industry there is a subset of hotels where one party owns the physical assets of the hotel (the owner), and an independent second party manages the hotel (the operator). This schism between ownership and management signifies that unlike the context of most capital budgeting, where investment decisions are made within the confines of a single hierarchical organisation, two distinct organisations are frequently involved in hotel investment decision making processes.

It is surprising that the idiosyncrasy of this widely-used hotel owner / operator structure has not attracted more attention from management researchers.¹ Further, when the capital budgeting implications of the divorced owner / operator arrangement are recognised, it is even more surprising that it has not attracted the attention of capital budgeting research. The extent to which the divorced hotel owner / operator management structure poses a problem to capital budgeting process is noted by Beals (1995).²

¹ Field (1995) comments: "For an area which has provided the basis of such a great part of the development of the hotel industry over the past 30 years, and is performing an even more important role in the 1990s, there has been remarkably little published research into the impact of management contracting within the hotel sector." (p.261).

² Beals (1995) comments: "The distinctly different outlooks of the two entities all but ensure a clash

The primary theoretical framework informing this investigation of hotel capital budgeting practice is agency theory (Baiman, 1982; 1990). The agent is represented by the operating company, the principal is represented by the owning company and the two parties' relationship is mediated by a hotel management contract. It is customary in this type of relationship for the operating company to initiate investment proposals relating to the hotel's infrastructure, while the primary ratification onus rests with the owner. This distinction is apparent from the demarcation of responsibilities assumed by the two parties. Due to its proximity to the hotel's activities, the operating company can be expected to be more aware of what infrastructure refurbishment and replacement is needed. The owning company, however, finances all capital expenditure, as it is the party holding the equity stake in the hotel's assets.

The remainder of the paper is structured as follows. The next two sections provide theoretical context to the study by elaborating on typical ownership / operating structures employed in the hotel industry and also agency theory's application in management research. Subsequent sections address, in turn, the research method employed, the study's findings and a conclusion that elaborates on the significance and limitations of the work.

2. The ownership / management structure of hotels

The archetypal hotel management contract between owner and operator involves the owner retaining legal ownership of the site, the building, plant and equipment, furnishings and inventories, and an operator managing the day to day activities of the hotel.³ In Eyster's (1988) following description of the contrasting roles of the hotel owner and operator, the use of the word 'agent' is significant as it appears outside the context of any explicit acknowledgement of agency theory:

As an agent, the operator pays, in the name of the owner, all operating expenses from the cash flow generated from the property, retains management fees and remits the remaining cash flow, if any, to the owner. The owner supplies the lodging property, including any land, building, furniture, fixtures, equipment, and working capital, and assumes full legal and financial responsibility for the project. (1988; p. 4).

With the exception of the General Manager and sometimes the Financial Controller, it is normal for all hotel staff to be employees of the owner. This saves operating companies becoming involved in the legal obligations associated with being an employer. It also makes it easier for the owner to switch operators without a need to enter into new employment arrangements with staff. The usual arrangement of the General Managers and Financial Controllers serving as employees of the operating company underlines the significant role they may play in the agency relationship between the owning and operating company.

It is customary for the hotel operator to be remunerated by a fee based on the hotel's

between investors and hoteliers." (p. 281).

³ Comments made by this study's interviewees suggest that the typical duration of a negotiated contract is reducing. A decade ago, ten and fifteen year contracts were commonplace. Today, however, what is referred to as a "5 by 5" is becoming more popular. A "5 by 5" signifies an initial five year contract with the operator having an option to renew after five years if particular contractual covenants (e.g., achieving profit targets) are satisfied.

gross revenue and also profit before fixed charges such as depreciation, lease payments and interest charges (Field, 1995). Up to five percent of gross revenue plus around ten percent of profit before fixed charges are typical bases for the fee's calculation. While these bases predominate, Field notes the advent of some variations on these approaches, with some operators receiving no fee until a defined level of profit or cash flow is generated.

Beals (1995) sees several factors contributing to the growth of the divorced owner / operator structure in hotel management. These include:

1. The development of large professional management groups offering the benefits of international branding including enhanced buying power, an extensive referral system, advanced training capabilities, and career progression for talented staff.
2. The size of the capital investment needed to open a hotel signifies that segregation of ownership from management enables hotel operators to circumvent capital market imposed expansion constraints.
3. Some operating companies wish to expand without assuming the risks associated with international real estate investment.
4. Similarly, there is a motive for hotel owners to purchase hotel real estate without assuming the responsibility of hotel management.

Beals (1995) also notes problems in the owner / operator relationship, however. Several of these problems relate specifically to capital budgeting. He feels that a fundamental problem stems from the separation of wealth (real estate ownership) from operations, which is the source of the wealth and that this becomes a problem due to owners and operators having different perspectives on time. He claims that investors put an emphasis on immediacy and the discounting of future cash flows. The hotelier, however, has a culture that is more closely aligned to a longer time horizon, and building both their franchise and long-term customer relationships (Guilding et al, 2001). With respect to the capital budgeting process, Beals claims that:

Investors, to the frustration of operators, seek precision that goes beyond assembling cost estimates to forecasting concrete benefits in terms of increases in net operating income measured over a specific time line. Not surprisingly, operators frequently complain that investors fail to provide adequate capital to realize the full potential of the hotels they manage, and investors accuse hoteliers of mispending capital. (p. 282).

3. Agency theory and management research

Agency theory has proven to be a popular theoretical framework for researchers interested in exchanges where one party, the principal (frequently represented by the owner(s) of a business), assigns work to a second party, the agent (frequently represented by an employee of the business owned by the principal). It attempts to expose contractual problems arising when agents have scope to act in a self-interested manner that is not aligned with the interests of the principal (Berle and Means, 1962; Jensen and Meckling, 1976). Exacerbation of this problem occurs in the presence of information asymmetry favouring the agent.⁴

⁴ Information asymmetry arises when one party can access information that is unavailable to the second party.

Agency theory has been widely-used in research concerned with principal/agent conflicts of interest and mechanisms for managing incentive problems (Bohren, 1998; Eisenhardt, 1989; Lambert, 2001).⁵ Location of an organisational context where a potential for conflicting interests between one or more parties exists is a fundamental aspect of agency theory modeling. Lambert (2001) identifies four factors giving rise to principal-agent conflict. These are: (i) a differential in the principal and agents' perceived relevant time horizon (a principal may be seeking to hold their interest in the organisation for the long-term, while an agent may be seeking to resign in the short-term), (ii) a differential in the principal and agents' risk aversity, (iii) the agent may opportunistically use his work situation to divert resources for his own personal benefit, (iv) there is scope for effort aversion by the agent.

Agency theory recognises two distinct costs that a principal can incur when attempting to manage an agent: (1) costs of monitoring and (2) costs of metering (Sharma, 1997). Monitoring costs relate to costs incurred monitoring an agent's behaviour. Where these costs are prohibitively high (as will frequently be the case when a hotel is owned by an overseas-based institution), a principal can be expected to attach greater importance to metering the outcomes of the agent's actions. A significant distinguishing factor between behaviour monitoring and outcome metering is that the latter signifies a transference of risk from principal to agent. If importance is attached to outputs, the agent is exposed to the vagaries of uncontrollable events (e.g., economic downturns, equipment break-down, new competitors, etc.), affecting the measured performance.

4. Research Method

Field study research involving interviews with nine Financial Controllers (FCs) and five General Managers (GMs) in large three, four and five star hotels located in Australia's Gold Coast region were conducted in 2001. Three, four and five star hotels have a greater potential to be operated under a management contract due to their relatively large size and the fact that they are frequently internationally-branded complexes. The Gold Coast region was selected as it provided relative ease of access to the researcher and is a well-known Australian tourist destination with a high density of hotels.⁶ Relative to a broader cross-section of hotels, one distinguishing feature of the hotels serving as subjects in this study is their predominant focus on the tourist market. This characteristic appears unlikely, however, to carry implications for the phenomenon under study. Supporting the earlier comments concerning the benefits of international branding in the hotel industry, it has been found that a relatively high proportion of owning, and also managing, companies of large 3, 4 and 5 star Gold Coast hotels are based overseas. This characteristic provides further support for the sample of subjects selected, as it offers scope for capturing a range of agency relationships.

⁵ See Kakabadse and Kakabadse (2001), La Porta et al (1999), Letza and Smallman (2001), Stoney and Winstanley (2001) and Zingales (2000) for some recent critiques of this literature.

⁶ While international differences pertaining to taxation, legal constraints and employment rights should be borne in mind, it appears likely that this study's findings will be pertinent, and of interest, to the hotel sector in other Western economies where the divorced owner / operator organisational form is found. One cross-country difference that appears particularly worthy of note is that in large economies such as the US., one would expect to see a greater proportion of domestically-based hotel owning and operating companies. This might be a significant factor as, due to closer proximity, there would be greater opportunity for the owners to exercise closer behaviour monitoring controls (akin to what Merchant (1982) refers to as "action controls"), as opposed to formalised capital budgeting control and metering mechanisms.

As already noted, the unit of analysis is distinct from that evident in Collier and Gregory's (1995) study which focused on the corporate head office level of hotel groups.⁷ In the present study, the interviewees were at the individual hotel level. This point of abstraction was selected as it represents the most significant organisational node offering scope for uncovering any latent tension between the operating company and the owning company. In effect, the hotel represents the nexus between the operating and owning companies and is the locus of operating company initiated capital expenditure proposals that have to satisfy the investment criteria of senior management in the operating company as well as the owning company. The significant role played by GMs and FCs in the agency relationship between owners and operators underlines their appropriateness as subjects in the study. They appear well-placed to have an appreciation of the nature and extent of any conflicts of interest between the hotel owner and operating companies in capital budgeting.⁸

An overview of the subjects interviewed is provided in Table 1. The first column provides an alphabetical reference for each hotel and also the title of the interviewee. Subsequent columns provide, in turn, information on: the hotel's size (in terms of revenue as well as number of rooms), its main activities, the nature of the operating company, the nature of the owning company, and some general observations concerning each hotel's capital budgeting process. Two interviewees were drawn from the same hotel in one case only (Hotel B). This resulted from an expression of interest by the GM following the conduct of the interview with the FC in Hotel B. Two of the interviewees were female (FCs in Hotels E and H), the remainder were male.

Insert Table 1 about here

Ryan et al (1992) refer to five types of case and field study work, classifying them as: descriptive, illustrative, experimental, exploratory and explanatory. The primary orientation of the field study conducted here may be best characterised as exploratory, as the interviews were concerned with exploring agency issues arising in the context of different hotel owner / operator structures and the investment decision making process.

All interviews were tape recorded and the first eight interviews conducted were attended by two researchers. The second researcher had experience in the hotel industry and was employed to facilitate data collection and also to enable more enlightened reflection subsequent to each interview's completion. The interview schedule was designed with an open-ended initial question that asked the interviewee to comment on any shortcomings and / or problems they perceive in their hotel's investment decision making process. In several cases this resulted in interviewees making unprompted comments concerning capital budgeting implications arising from the owner / operator relationship. Subsequent questions were more directed, addressing the range of agency issues described in the next section.

⁷ Collier and Gregory (1995) acknowledged the distinction between owner and operator that can arise in a subset of hotels, however they did not make it a central feature in their empirical enquiry.

⁸ The FC in Hotel K (see Table 1) commented "I sit in between the owner and the management company. So I'm kind of the meat in the sandwich".

5. Findings

This section presents the study's findings and is ordered according to the following sub-headings: 1) general comments concerning the potential for conflict in the hotel owner / operator relationship; 2) formalisation of the capital budgeting process; 3) cash flow data biasing.

General comments on the potential for conflict in the hotel owner / operator relationship

Findings in this sub-section are structured according to Lambert's (2001) four point classification of factors accounting for principal / agent conflict that was noted above. Lambert's classification has been augmented by "bureaucratic tension", a dimension of conflict found to be present in the context of this study but not delineated as a separate category in Lambert's typology.

(a) Differential in the principal and agents' perceived relevant time horizon

An awareness of the potential for capital budgeting conflict in divorced owner / operator management structures was particularly apparent to the GM in Hotel F. Following the initial open-ended interview question, i.e., prior to even raising the issue of different owner / operator structures, he provided the following commentary:

(Names a competing hotel and its operating company) have a management contract on that property for probably another 5-10 years. The owner of the hotel has just bought that building and wants to maximise their ROI, not only their capital gain in the future. They want the building maintained properly and they want their share of short term profits. That is what the owner wants. (The operating company) on the other hand says we have five years left in this contract to wring every cent out of it we can. So they will be saying to themselves 'Let us look for another (names a hotel chain) on the Gold Coast'. So instantly you have an owner and an operator who have totally different agendas.

These comments contradict the direction of Beals' (1995) view of a potential time-based conflict between owner and operator. As noted earlier, Beals suggests that, relative to operators, owners are more short-termist in their approach to investment appraisal. In the scenario outlined by the GM in Hotel F, however, an incentive for the operating company adopting a relatively short-termist perspective on hotel profits is apparent. Short-termist actions that the operating company might take which could be contrary to the longer-term interests of the owning company include reduced training and asset maintenance expenditure and the promotion of investment expenditure that might result in relatively high short-term returns but low long-term returns.

This owner / operator goal incongruity results from different owner / operator time horizons arising when the operator is considering non-renewal of the management contract or when an owner is considering selling the hotel. This rationale can be seen as providing a reconciliation of the seemingly inconsistent views of Beals (1995) and Hotel F's GM. If either the principal or agent is considering ending its involvement in the relationship, then a time-based goal misalignment can arise. The party seeking to terminate the relationship can be expected to heavily discount long-term implications of the hotel's management, maintenance and investment.

While the comments made by the GM in Hotel F appear pertinent as they underline a potential for a time-based goal misalignment resulting from an operator's intention to forego contract renewal, they should be put in the context of observations suggesting that such a situation is not commonplace. Based on the sample of interviews conducted, it appears that the industry is not characterised by a change in capital budgeting behaviour over the lifetime of the management contract. When asked to comment on why this is the case, the FC in Hotel E noted that in the vast majority of instances hotel operators are seeking renewal of their contract and stated:

If (you are) hoping to get a new contract, absolutely you would not be seeking to change your capital budgeting behaviour. Why would you if you are seeking renewal?⁹

(b) Differential in the principal and agents' risk aversity

As any investment in hotel assets and infrastructure is financed by the owner, it is readily apparent that in the context of capital budget decisions the owner is exposed to more absolute risk than the agent. The agent's downside risk is limited to reduced profit and revenue, the owner, however has an equity as well as a profit and revenue stake in the business. The operator stands to gain from further hotel capital expenditure (enhanced profitability and brand image) without carrying the risk and burden of financing the investment.

The two contracting parties' incongruity with respect to risk aversity can be also linked to the time-based conflict just commented upon. Firstly, Beals' perspective may relate to risk as, relative to an operator, an owner has a greater incentive to exercise caution in investment appraisal. Secondly, the risk aversion misalignment can be expected to grow as the concluding date of a management contract approaches and if the operator is not planning to seek contract renewal. In this circumstance, the closer to a contract's termination date, the less concerned the operator will be with the riskiness of asset expenditure. If profit predictions are not met, the operator's loss is limited to the time remaining in the contract.

One strategy owners may adopt to reduce a potential differential in risk aversity is to only contract with strongly branded hotel operating companies. The strongly branded hotel operating company's need to protect its brand reputation would appear to represent a constraint to any propensity to pursuit of risky operating and management practices. This is because the operator also has an asset, i.e., its brand value, to protect.

Despite this view, it is also apparent that the strength of a hotel operator's brand can also be a potential source of conflict between owner and operator. A GM in a hotel with a strong brand will be motivated to seek investment not only to increase hotel revenue and profitability but also to uphold the hotel operating company's brand name. One can conceive of a situation where an owner is willing to let the physical standing of a property decline if this is consistent with increased profitability (e.g., due to reduced refurbishment and maintenance expenditure). Such a development can be expected to be heavily resisted by a strongly branded hotel operator as although the hotel's profits might increase, poor customer experience in the hotel will adversely impact on the operator's

⁹ The view of "no change in capital budgeting behaviour" over the life of the management contract should be qualified by the assumption that both parties are seeking to renew the contract.

revenues in other hotels bearing the same brand name. This brand related dimension of conflict is apparent in the following comments provided by the GM in Hotel M:

In terms of capital expenditure in regards to refurbishment of the hotel, the management company would want to refurbish the hotel to maintain the standard of the brand. So, if they want this hotel to look like any other (names the hotel brand) and they don't want it to look worse than any other (names the brand), we try to give them that brand and they don't really care whether or not they make the hotel more profitable. The owner, on the other hand, doesn't give a damn what the hotel looks like, he wants to know where I'm going to get the dollars. So there is always a conflict.

This need to protect a brand name is also evident in comments made by the FC in Hotel H. In connection with a particular hotel that is part of a strongly-branded international chain she elaborated on the propensity of some owners to defer investing in hotel refurbishment. Such deferment can be particularly damaging to a strongly branded hotel operator. She noted:

This is where you have conflict between owner and manager. It's the owner that approves the change, irrelevant of what the manager wants. They (an operating company the interviewee used to work for) had to be firm with the owners because the hotel required some major refurbishment work and they had to argue quite strongly about it. Its going through some refurbishment now, but there are some very difficult things between owner and manager that come up; unresolvable in many cases.

(c) Opportunistic diversion of resources by agent

The following two interviewee comments are believed to be significant as they both highlight the importance of the assets to the owner when distinguishing between the interests of the two contracting parties.

The GM in Hotel F commented:

(In) most of the hotels that you interview, the owner and the operator will be separate. So if you are talking to the operator all they are really interested in is wringing as much money out of their management contract as possible, and the owner of course wants an on-going profit but also sustainability and integrity of his assets.

The FC in Hotel K also highlighted the competing interests of the two companies party to a management contract. He commented:

Each of the companies' preferences are there you know. I mean, the management earns its income by managing a hotel successfully and therefore generating revenue. The owner makes it from a profit base which includes considerations to cash flow capital. At the end of the day, it's the owner's assets you know. So I guess there is a lot of conflict that exists between them.

As already noted, under the typical hotel management contract the hotel operator is remunerated based on profit and revenue levels achieved. In this study, no operator was found to be remunerated on a basis that recognised profit as a function of investment. All operators were remunerated based on a percentage of profit and percentage of sales basis (this finding is consistent with Beals' (1995) commentary pertaining to owner operator

contractual arrangements in the U.S.).

To use a remuneration basis that recognises the value of assets involved (e.g., ROI) would appear to lessen the potential for owner / operator goal incongruity that can become particularly evident in the context of capital budgeting. When ranking two mutually exclusive projects where project A has a higher NPV than project B, the operators of the hotel will have an incentive to promote project B if it is the option that generates higher absolute levels of sales and profit. This incentive underlines the degree to which under the conventional hotel management contract there is scope for the agent to opportunistically divert resources in the long-term context of investment decision making. In the context of capital budgeting this was the only mode of agent opportunistic diversion of resources noted, although the discussion below concerned with agent cash flow data biasing could also be interpreted as a form of opportunistic diversion of resources.

(d) Scope for effort aversion by the agent

The interviews yielded negligible evidence of effort aversion by the agent. *Prima facie*, the incentive for such effort aversion would appear to be negligible given the operator's remuneration-based incentive to maximise profit and revenue.

Mediating factors limiting the scope for agent effort aversion relate to the hotel operator's desire to uphold its brand name and also loyalty felt by the operator to the owner. The potential of loyalty to constrain any tendency for hotel operator effort aversion is evident in the following comments made by the FC in Hotel L:

There is a duty of care too. When you accept a management contract on behalf of an owner, we are basically operating his or her assets. So therefore, when we present a proposal to an owner, we as the operator have to be totally committed that it's good for the owner as well, so there is certainly a duty of care when it comes to submitting this stuff to an owner. You've got to be pretty committed and also make sure that you know whatever is in it for him or her.

(e) Bureaucratic tension

Observations relating to bureaucratic tension between owners and operators were noted and as these are not easily accommodated by Lambert's (2001) four point typology, they have been afforded separate classification in this study. Parallels can be drawn between this notion of bureaucratic tension (which can be interpreted as representing bureaucratic costs) and the Transaction Cost Economics theorem (Coase, 1937; Williamson, 1979; 1988).

Two issues raised by the FC in Hotel H are elaborated upon here. Firstly, by citing bureaucratic control problems that she had previously experienced in divorced owner / operator hotel structures, she elaborated on her preference for the unified owner / operator structure which existed in the hotel where she worked at the time of the interview. With respect to these structures she commented:

The minute you put something down in writing they (the owners) hold you to it. Its like having a noose around your neck all the time in hotels, and that is the problem with management / owner relations. If they ask you to document something you don't completely believe in they will hold you to it and drive you

crazy with it. You spend so much of your time dealing with their questions, you're not focussing on the most important thing which is the operation and how to get more people into the hotel.

A second issue she commented on concerned frustration that can be experienced when owners elect not to release capital reserves for expenditure. In many owner / operator agreements it is common practice for three percent of profit to be set aside as a capital reserve. While this reserve is identified for future capital expenditure, there is no requirement placed on the owner to expend the amount accumulated in the reserve. With respect to this capital reserve arrangement the FC in Hotel H commented:

From our point of view as a management company, we've been told that three percent of revenue will be held for capital needs of the property in the future. This is the sad thing, we have the fund, we believe that what we are asking for is important for the property. I'm not suggesting for a moment that we believe that we are wasting the owner's money, but usually we are not looking into the cash side of it. That's the owner's responsibility.

Formalisation of the capital budgeting process

A particular dimension of capital budgeting appraised in the interviews concerns the degree to which each hotel employed formalised capital budgeting procedures. Capital budgeting processes have been interpreted as formalised where there is high "systematic study of issues" (Langley, 1990; p. 17) and importance attached to formal financial analysis using methods such as net present value, internal rate of return, payback, and return on investment (Van Cauwenbergh (1996). While the entirety of each interview facilitated greatest appreciation of each subject company's degree of capital budgeting formalisation, particular insight was sought by posing the following question: "How formalised is the investment decision making process in your organisation?"

Agency theory motivates an expectation that greater capital budgeting formalisation will be present in divorced owner / operator structures. Baiman (1990) notes that, based on the principal-agent model,

..... one would expect to find a managerial accounting procedure only in contexts in which individuals would benefit from its use - by mitigating motivational problems within firms made up of self-interested individuals. (p.344).

For the reasons outlined above, there would appear to be potential for agency problems in those hotels adopting a divorced owner / operator structure, and especially in those hotels where the hotel operating company reports to an overseas hotel owner. In these situations, there is significant potential for information asymmetry (Baiman and Evans, 1983; Penno, 1984). Also, the potential of a significant departure from goal congruence between the two contracting parties is present. The owner can be expected to be interested in securing a satisfactory rate of return from investments, while the operator has an incentive to focus more narrowly on simply increasing absolute levels of revenue and profit.

In light of this potential agency problem, one might expect more formalised capital budgeting justification procedures in the presence of divorced owner / operator structures and especially in those situations where the owner has little involvement in the day to day workings of the hotel. It is in these situations that the potential for capital budgeting information asymmetry between the two contracting parties appears to be greatest, and

greater formalisation of procedures might be used to combat the greater potential of goal incongruency.

Further motivation for an expectation that hotel owner / operator divorce will result in greater capital budgeting formalisation derives from Brunsson (1989) and Langley (1990; 1991) who both questioned the real significance of formal analysis in investment appraisal. Brunsson (1989) concluded that the primary role of formal analysis is symbolic. He felt the rational organisation to be an illusion, but that it is valuable for an organisation to present itself in this light. This view appears to have some support from Collier and Gregory's hotel industry study, as one of their interviewee's noted "there is a need to have a bankable document" (1995: 33). The additional dynamics of a divorced owner / operator structure, may well signify greater capital budgeting formalisation due to the owner and the operator both sensing a need to present themselves as rational to the other party.

From Table 1 it is apparent that Hotels A, B, E, G, J, K, L and M operate with a divorced owner / operator structure, and of these, A, G, J, K, L and M are owned by overseas companies (Hotel B is jointly owned by an overseas and a domestic company). From the agency perspective outlined above, we would expect the capital budgeting processes in these hotels to be relatively formalised. With the exception of Hotel B, support for this expectation has been found. The FC in Hotel G commented:

Cash flow is very, very important here. Our owners do require a lot of cash flow information.

Further comments made by this FC highlight the degree to which owners dictate the capital budgeting system applied in hotels operating under a divorced owner / operator structure. He commented:

We tend to fit into what the owners want in the presentation and the sorts of figures they want, the sorts of statistics they want to see, the sorts of projections, that sort of thing. I mean (the operating company) have their own guidelines and format but at the end of the day it's the owner's money, so we need to give them exactly how they want it.....

While these comments suggest pre-eminence attached to the owner's needs, other comments made underline the degree to which a multi-tiered ratification process also applies. The same FC commented:

We provide a lot of the figures. We provide the forecasts. We provide all that sort of information that goes to (the operating company's) divisional office in Hong Kong and then the U.S. headquarters for big projects. They then model and present direct to the owner. Its not done by ourselves. we don't even see what they present to the owners.

This multi-tiered ratification process retards the speed of capital budget decision making. Slowness in capital budget decision making (which could be interpreted as a further source of bureaucratic tension) appeared to represent a significant problem to the GM in Hotel A. Geographically remote owners did not represent the cause of the problem, however, as the owners were represented by very involved local agents. It was the GM's view that the owners frequently became too involved. He cited the length of time and number of meetings involved with the owners to be a major shortcoming in the capital budgeting process he confronted. He felt this problem was exacerbated in his hotel due to what he perceived to be a conservative management culture in the owning company.

Further problems that can arise in a highly formalised capital budgeting environment when combined with a divorced owner / operator structure were outlined by the FC in Hotel H. The first problem concerns the number of times a project can be turned down and the difficulties this presents when attempting to obtain repeat quotes from sub-contractors. The FC in Hotel H had experienced this problem in a hotel that she had previously worked for (a divorced owner / operator structure with large owner and operator). She described the system and the problem that it had led to as follows:

You had to prepare a rationale. You had to prepare three quotes minimum. You would have to then prepare a form which was a capital expenditure approval form which had all the details in it and then that actually went to the department head, to the financial controller, to the general manager, to the regional manager (in the operating company) before it went to the owning company. Each year in the budget process we do a capital plan for (the operating company). First (the operating company) approves it, and then the owner. To do that plan you actually have to go out and source quotes to get an indication of the type of money you are going to spend. The plan is then approved as part of the business plan, but still in most cases they want to see it project by project and re-approve it. In that particular case, then, you can prepare for a project six times and the owners could decide they don't want to do it now. Then what you have is a local problem where the suppliers don't want to quote anymore. It's a common problem across the country; (the owners) constantly are changing their mind and local suppliers just stopped quoting because it's wasting their time.

Again, with respect to an earlier experience in her hotel career, the FC in Hotel H, also commented on the problem that a split owner / operator structure presents due to the additional ratification step required. With respect to the problem, she commented:

An extra level of information is required which is more draining on resources, and, at times, I'd be honest at saying it's just a waste of time. preparing data in different fashions for different people.

The "slow-moving, conservative and bureaucratic" approach to capital budgeting evident in most of the divorced owner / operator hotels lies in stark contrast to the procedures in place in Hotels B and D. Hotel D had a unified owner / operator structure and although Hotel B had a divorced owner / operator structure, it displayed characteristics that were more consistent with a unified owner operator structure. The normal relative levels of involvement in the hotel's day to day affairs by the owning company and the operating company appeared to be reversed in the case of Hotel B. The operating company (which had a partial ownership stake) was based overseas, while the owning company that did not have an operating stake was a relatively small operating company, located in the same city as the hotel. It also had a highly charismatic CEO who liked to maintain close involvement with the hotel. So much so that on one occasion the CEO entered the hotel's foyer at a time that there was a large number of suitcases around the porter's desk. The following extract from the interview with Hotel B's Financial Controller highlights both the steps taken by the owner and the degree to which these steps highlight an unusual owner / operator relationship:

Financial Controller: This place, compared to where I have worked before, is surprisingly liberal in so far that we have owners who have a head office that is just around the corner. (With respect to the luggage in the foyer incident), he said you should change that, so there's an easy way for luggage to pass through,

and the next day, about 7 in the morning or something, work men rocked up, nobody had any idea, sheets went up, covered everything up, they started to work, and I think it took them all up a week. The whole porter's desk was completely re-vamped, the back of the porter's desk and luggage area was increased, etc. Not very often do you get that."

Researcher: "It does seem that there is quite a good relationship between the owners and management?"

Financial Controller: "Well, I've never seen something like that or operation of that nature in any company I've worked in. Very unique".

Referring to this same incident, the GM of Hotel B commented:

I've never had that scenario before. I suppose it comes with being a smaller company and someone like (names the owner) being in such close contact and having such a feel for the property and really taking ownership of it.

The relatively non-formalised nature of Hotel B's capital budgeting process is apparent from the fact that in its brief three year history the FC had been involved in the preparation of only one or two small payback calculations, and no NPV, IRR or accounting rate of return calculations.

Hotel D, which was owner-managed by a small owner, appeared to have the least formalised capital budgeting process. The process was conducted in a somewhat ad hoc and reactionary manner with capital expenditures triggered by cash availability. The financial controller commented:

We don't at the beginning of the financial year say this is what we've got for capital expenditure, this is what we've got for refurbishment, this is what we want to spend on on-going maintenance. Basically, we tend to do it in reverse. We tend to do it on cash flow, like if we've got a good cash flow period coming up, we might go through and do selective bedding, painting, etc.

When asked to comment on the most important phase of the capital budgeting process, the GM in Hotel D ranked financial analysis as relatively unimportant and felt managerial intuition to be the most significant factor.

In addition to Hotel D, four other hotels have been classified as operating under a unified owner / operator structure, i.e, Hotels C, F, H and I. Of these, C operated a highly formalised capital budgeting process that appeared fairly typical of any operating division of a large multi-national company. Hotel H had some standardised procedures, however, the flair and close involvement of the owning company signified that the process was not bureaucratic. In addition, the nature of the owner appeared to result in some capital investment decisions being taken in a relatively impulsive manner as they did not pass through the conventional decision-making process.

Hotel I used to have a relatively distinct owner / operator structure that involved two companies operating the hotel as a joint venture. The FC in Hotel I noted that he was now accountable to one large company that was both owner and operator and that this resulted in little flexibility in procedures. He compared this situation to the earlier joint venture arrangement:

Because we were almost a cross between a management company and a franchise, we were able to get away with a lot. We didn't use to go to the nth degree as far as adherence to corporate capital expenditures outlines.

This appears as an interesting observation as it counters the view that involvement of more than one contracting party results in more formalised capital expenditure systems. In this particular case, it appears that involvement of more than one party as a joint venture operating the hotel might blur conventional system requirements with the result that the hotel GM operated with greater autonomy.

The above discussion has been largely predicated on the view that owner / operator structure may be a significant determinant of the degree of formalisation in a hotel's capital budgeting process. Further consideration of the data collected suggests a second contingency factor affecting the degree of capital budget formalisation. This factor is size of the owning company. Closely related to the notion of capital budgeting formalisation is the use of financial analysis (Butler et al, 1993) and several prior studies have noted a positive relationship between company size and use of sophisticated financial analysis in investment appraisal (Lamminmaki et al, 1996; Patterson, 1989; Pike, 1996). While a positive relationship between size of the hotel operating company and capital budgeting formalisation might be anticipated, due to the equity stake taken by the owning company in any asset acquired, it is expected that size of the owner would be the more significant determinant of capital budget formalisation.

The view that owner size as well as the owner / operator structure may constitute significant determinants of capital budgeting formalisation can be diagrammatically synthesised in the manner depicted in Figure 1. In this figure, the vertical vector concerns type of hotel operating structure and the horizontal vector concerns the size of the owning company. Within each of the four quadrants defined by the dichotomous vectors, an entry has been made outlining the degree of capital budgeting formalisation expected and also the degree of capital budgeting process formalisation observed in each of the hotels under study. In the following discussion, it will be noted that the findings are largely consistent with the model's expectations.

Insert Figure 1 about here

Following the rationale and findings outlined above, the implications for capital budgeting formalisation in those hotels characterised by quadrant 1 (north-west) and quadrant 4 (south-east) of Figure 1 are fairly obvious. Quadrant 1 hotels are expected to employ highly formalised capital budgeting practices, while quadrant 4 hotels are expected to employ relatively non-formalised capital budgeting practices. Hotels A, E, G, J, K and L fall into the quadrant 1 category. All apply highly formalised capital budgeting procedures. In three of these six hotels (A, E and J) some dysfunctionality associated with the highly formalised capital budgeting processes was noted. In Hotel A the length of time involved was seen as a problem, in Hotel E there were political manoeuvrings resulting from capital expenditure recommendations being cut back by as much as a third, and in Hotel J a bargaining process prevailed. Consistent with the expectations of the model, Hotel D, which is a quadrant 4 archetype, had the least formalised capital budgeting process of the hotels under study. Hotel H, which also falls into quadrant 4 showed some formalisation, however, there was no sense of the system being bureaucratic and in fact it was characterised by occasional impulsive investments made by the owner.

Hotels in quadrants 2 (north east) and 3 (south west) can be seen to be subject to competing factors with respect to capital budgeting process formalisation. With respect to these competing factors, it is believed that size of the owning company will tend to be the predominant influence. With respect to quadrant 2, it is believed that the small size of the owning company will enable the owner to employ more of a hands-on approach to the operating company (low formalisation) by maintaining relatively close working relations with the hotel's GM. Hotels B and M are categorised in quadrant 2. The findings of low formalisation in B and a degree of formalisation but not excessive bureaucracy in M are largely supportive of the model. With respect to quadrant 3, while the unified nature of the owner / operator can be expected to limit the degree to which capital budgeting formalisation may become burdensome, it is believed that the large size of the owner will tend to dictate relatively high formalisation in the capital budget process. Hotels C, F and I are classified in quadrant 3. All three applied fairly formalised procedures. It is noteworthy that none of the interviewees in these hotels related any frustrations felt as a result of the system appearing to be too bureaucratic.

Cash flow data biasing

Two factors suggest an incentive for hotel operators in divorced owner / operator structures being relatively "bullish" when initiating capital expenditure proposals (i.e., inflating projected revenues and deflating projected expenditures). Firstly, as noted by Field (1995), the owner shoulders the main burden of the downside risk associated with capital expenditure failure. Secondly, as the formula used to remunerate the operator recognises absolute revenue and profit but not investment, there would appear to be an incentive for the operator attempting to stimulate investment that will increase revenue and profit, with muted concern attached to return as a function of investment.¹⁰

Findings with respect to this expectation are mixed, however. Comments by some of the interviewees are supportive of an optimistic data biasing effect, comments made by others suggest an incentive to negatively bias cash inflow estimates. The propensity to negatively bias cash inflow estimates would appear to be greater when the owner attaches significant importance to metering outputs rather than monitoring behaviour (Sharma, 1997). A "metering" approach to performance appraisal appears consistent with the owning company seeking to benchmark the operating company's performance against investment proposal forecasts. The presence of divorced owner / operator structures signifies that capital expenditure proposals are submitted by one contracting party to another. This appears to result in them assuming an ex-post control significance greater than that normally found in more conventional organisational contexts.¹¹

This incentive to negatively bias cash inflow projections in a divorced hotel owner / operator structure signifies that the concept of budgetary slack, which has been the

¹⁰ The project with the highest ROI is not necessarily the project with the highest absolute profit. From an ROI perspective, consider projects A and B. Assume project A requires an initial investment of \$250,000 and will provide net cash inflows of \$50,000 per annum for five years (i.e., an ROI of 20%), and project B requires an initial investment \$1,500,000 and has projected net cash inflows of \$60,000 per annum for five years (i.e., an ROI of 4%). A hotel operator might be tempted to inflate the cash inflow estimates for project B as it is the project providing the highest net annual cash flows yet it is the project that an owner is unlikely to favour due to its low projected ROI.

¹¹ Use of projected cash flow data in this manner can be seen to resemble the conduct of investment post-audits (see Mills and Kennedy, 1993; Neale, 1989).

subject of extensive empirical investigation in the context of annualised budgeting (Dunk, 1993; Lukka, 1988; Merchant, 1985), can be extended to capital budgets. The combination of high participation by the operating company in formulating capital expenditure proposals, high information asymmetry (Baiman and Evans, 1983; Penno, 1984) that is characteristic of many hotel owner / operator relationships, and also the use of budgeted data as a performance measurement vehicle, signify that all the ingredients Dunk (1993) sees as conducive for high budgetary slack are frequently present in divorced owner / operator capital budgeting processes.

The FC in Hotel B felt there was a greater propensity for investment proposal cash flow forecasts to be biased in the direction of the interests of the hotel operator in those situations where the owner did not have a close working relationship with the hotel. Such situations would appear to present an opportunity for the operating company capitalising on greater degrees of information asymmetry. The FC in Hotel B elaborated on one example suggestive of such information asymmetry capitalisation. He noted a tendency for operating companies knowingly using flawed logic as part of a justification for capital expenditure:

Where it is more difficult to squeeze money out of owners then you whip up all these different stages, then you say well if we do this then our occupancy increases by 'x' or we can start to charge more on the room rate. Which generally is rubbish anyway. The room rate is determined by the market that's there.

The FC in Hotel I believed biasing of capital expenditure proposal data to be rife in the industry. He saw a key role of the FC to be the "policing" of this problem. He commented:

At the end of the day the Financial Controller is left holding the baby. I mean, we've got to find the cash to pay the bills. So, you know, if we are to keep the operational management people and the owning company, we are left holding the bag. There's no advantage for the finance people to play the game.

Although Hotel A experienced close owner involvement (low information asymmetry), its capital budgeting process nevertheless manifested budgetary slack in a manner typifying several of the hotels investigated. The GM in Hotel A felt that the operating company he worked for erred on the side of negatively biasing estimates when preparing cash inflow projections. When asked what drove this bias in estimates he provided to the owners, he replied:

Just the management contract. We want to make sure, as a management company that we exceed beyond the customers' expectations and the owner's expectation.

Although Hotel C was an owner-operated hotel, it exhibited several traits more consistent with hotels operating under a divorced owner / operator structure. This appears to be because the owning company is a very large overseas company with a specialism in property investment and ownership. The hotel used to be run by an operating company until the early 1990's. At that time the owning company did not renew the hotel management contract and instead assumed management responsibility. The management responsibility appears to be highly decentralised, however, with the hotel's GM operating in a manner similar to a small overseas subsidiary company. The capital budgeting system in this hotel is highly formalised and characterised by a significant degree of budgetary slack. The FC in this hotel noted that due to experience derived from dealing with the owners, the hotel's executive management preferred to negatively bias cash

inflow projections when submitting capital expenditure proposals to management. He commented:

Its just from dealing with our owners that we have learnt to be conservative because being optimistic doesn't pay off for you in the long run. Someone is going to come down on you when you don't achieve it".

This quotation is believed to be quite significant. Not only does it reveal slack in the hotel's capital budgeting process, it also highlights the degree to which the owner is viewed as a distinct organisation, despite the fact that the hotel's formal structure falls within the single owner / operator archetype.

A similar observation was made in Hotel K. The FC commented:

You know there is a high degree of accountability. So, from an operator's point of view, you know, I'm very cautious about what I put in these numbers because I recognise that they have to be achievable, unless I know I've got an imminent transfer coming up.

A propensity for capital budgeting budgetary slack was also apparent at the "within operating company" level. When asked whether a Food and Beverage manager might inflate profits estimated to result from a restaurant's proposed refurbishment, the FC in Hotel E commented:

(The estimated cash flows) go in his budget, that's his target. His bonus is based on it at the end of the year. So its going to come back and bite him if it doesn't work. They're in this quandary. They really want to spend this money, but that has to go in their budget too. So they can't have it both ways. So in fact you probably end up with a reasonable proposal between those two goals that they've got.

Evidence of optimistically biasing cash inflow projections was apparent in Hotel G. In this hotel the FC felt that due to the operating company's desire to increase profits, there was a real tendency for the development of optimistic cash flow data when submitting proposed capital expenditures to the owner. He felt that the owner's were wise to this propensity and that there was extensive scrutiny made of the projections submitted.

Returning to Lambert's (2001) four dimensions of agent-principal conflict, it appears the time horizon issue is significantly implicated as a contingent factor affecting the propensity to bias cash flow projections. In those situations where a long-term relationship is sought, it is expected that factors such as the desire to instill and maintain trust, combined with the need to avoid disappointing the owner will be more evident (i.e., there will be a greater tendency to negatively bias cash inflow projections when submitting forecasts). As noted earlier, where the perceived relationship horizon is relatively short-term, there would appear to be heightened potential for goal incongruency, i.e., the operator can be expected to be increasingly concerned with maximising cash flow from the hotel, without due regard to the owner's interests which include maintaining the value of the property (see earlier cited comments made by the GM in Hotel F). In addition, in owner / operator relationships with a short time horizon, the operating company can be expected to discount control implications that give rise to a budgetary slack effect. This rationale suggests that short time horizon owner / operator relationships will tend to result in optimistic investment proposal cash flow biasing. A second factor likely to mediate whether an operator adopts an optimistic stance when compiling investment proposals, is the degree to which the owning company uses

investment proposal forecasts as a basis for controlling the operating company. In the presence of low use of forecast data as a basis for ex-post monitoring, more optimistic forecasting in capital expenditure proposals is to be expected.

6. Conclusion and discussion

This study has investigated the somewhat idiosyncratic nature of the divorced owner / operator structure adopted by many hotels. It was the idiosyncrasy of this structure that motivated the investigation into capital budgeting processes applied in the hotel industry. Agency theory has been drawn upon as the theoretical framework underpinning the investigation.

Lambert's (2001) classification of factors accounting for principal / agent conflict has been used to structure an appraisal of the nature of potential hotel owner / operator conflict. It has been noted that if either the owner or operator adopts a relatively short-term planning horizon with respect to a hotel, then a time-based goal misalignment can arise that sees the party seeking to terminate the relationship heavily discounting long-term implications of the hotel's management. If the hotel operator is not planning to renew the contract, and if it is strongly branded, the potential for owner / operator conflict will be constrained by its need to uphold the brand's value. It has also been noted, however, that an operator's need to maintain brand image can also represent a source of owner / operator conflict, as brand image maintenance may compete with profit maximisation. A potential motivation for long-term diversion of resources by the operator is evident due to the operator's remuneration basis which is linked to revenue and profit, but no algorithm capturing return as a function of investment. The recent attention afforded to Economic Value Added (EVA[®]) (Stewart, 1994), heightens the extent to which this is a somewhat perplexing finding that appears worthy of further research enquiry. The notion of "bureaucratic tension" has been introduced as an augmentation to Lambert's four point classification. This broadening of Lambert's typology was necessitated by observations concerned with the additional administrative demands arising in the context of a divorced owner / operator structure.

In addition to this general appraisal of the potential for agent / principal conflict, two particular dimensions of capital budgeting have been appraised: formalisation and cash flow biasing. With respect to formalisation, some support for the view that more formalised capital budgeting procedures are applied in divorced owner / operator hotel structures has been provided. This finding appears consistent with agency theory which holds that greater use of formalised procedures will occur in situations where individuals can be expected to derive benefit from their use. More formalisation tends to signify greater bureaucracy and several interviewees noted adverse implications arising from greater formalisation, e.g., slow investment decision making, the need to prepare forecast data in more than one format, and problems of securing sub-contractor quotations where the same proposal has been compiled several times.

Collier and Gregory (1995) concluded that a narrow span of influence in the investment decision making procedure (they refer to situations "where the chief executive is essentially the decision maker") is positively related to less formalised approaches and more simplistic methods of investment appraisal. This conclusion appears to be largely borne out by the findings noted in this study. From Figure 1 it is apparent that in addition to the ownership structure, size of the owner represents a determinant of capital budgeting formalisation. It appears that small owner size is positively related to less capital budgeting formalisation, and this would seem consistent with Collier and Gregory's "narrow span of influence" conclusion.

With respect to cash flow biasing, it appears that information asymmetry arising in the context of divorced owner / operator structures might increase the propensity for capital expenditure cash flow estimate biasing. Two competing effects are apparent. As a result of cash flow forecasts being used as the basis for ex-post monitoring of the operator's performance, there is an incentive to negatively bias cash inflow projections (the budgetary slack effect). As a result of the operator's remuneration being based on profit and revenue (but not linked to capital employed), there is an incentive to stimulate further owner investment by submitting optimistic cash flow forecasts (the optimistic effect). While data collected lends support to the view that the divorced owner / operator structure provides greater scope and incentive for bias in investment proposal cash flow forecasts, the results are mixed with respect to the direction of the bias. While information asymmetry is seen as a prerequisite of bias, it appears likely that the direction of the bias is mediated by the degree to which owners use forecast capital expenditure data as a basis for monitoring the operator's performance and also the time horizon perceived by the operating company. In the presence of low use of investment proposals as a basis for ex-post monitoring, there is a greater propensity for optimistic biasing of capital expenditure proposals. Where the operator perceives a relatively short-term time horizon in the owner / operator relationship there will also be an incentive to prepare optimistic investment proposal cash flow forecasts.

The findings claimed for this study need to be considered in the context of all the limitations normally associated with field study qualitative research. In addition to these limitations, it should be noted that the decision to interview general managers and financial controllers, which was motivated by a desire to seek representation of the experiences of both of these "gatekeepers" of capital investment projects submitted to hotel owning companies, signifies that the findings may be skewed towards the hotel operators' perspective. In subsequent research concerned with the hotel owner / operator interface, further useful insights might well derive from conducting interviews with representatives of the owning companies as well as the operating companies.

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Table 1

Overview of the subject companies

Hotel reference / Interviewee function^a	Size: 1) Revenue p.a. (\$m); 2) Number of rooms.	Main activities	Operating company	Owning company	Comments on the capital budgeting system
A / G.M.	1) \$15m.; 2) 298.	Accommod'n, F&B ^b , banqueting, gaming.	Publicly traded, large international hotel management company.	Publicly traded, overseas-based owning company	Highly formalised, slow and sometimes problems securing repeat quotes from potential sub-contractors / suppliers experienced.
B / G.M. & F.C.	1) \$12m; 2) 403	Accommod'n, F&B, hosting functions.	Small overseas company (also has ownership stake).	Jointly owned by 2 companies: a) the operating company, b) a small, high-growth, domestic company.	Relatively "liberal" approach. Close involvement of owner resulted in controls akin to "personnel" controls.
C / F.C.	1) \$20m; 2) 296.	Accommod'n, F&B, hosting functions.	Same as owning company, although most of the company's hotels are managed by separate operating companies.	Publicly-traded overseas company.	Thorough and formalised. Room refurbishment expenditure includes preparation of a "mock up" room for inspection by owners.
D / G.M.	1) 2.5m ; 2) 150.	Accommod'n, F&B.	Same as owning company.	Small sole trader, owns three properties.	Simplistic. Minimal use of formal appraisal models.
E / F.C	1) N.A. 2) 609.	Accommod'n, F&B, conferences, gaming.	Overseas publicly traded company.	Domestic publicly traded company.	Highly formalised. Investments classified according to \$ size and nature (e.g., workplace health and safety, operational replacement, etc.)
F / G.M.	1) N.A. 2) 329	Accommod'n, F&B, golf, residential, conferences.	Wholly owned subsidiary of owning company.	Large overseas publicly traded company.	Relatively formalised. Conducted in context of well-defined long-term strategic plan. High use of financial modeling (NPV, payback, etc.). Minimal bureaucracy or politicality evident.

Table 1 (cont'd)

Overview of the subject companies

G / F.C.	1) \$16m; 2) 405.	Accommod'n, F&B.	Large overseas publicly traded company.	Large overseas publicly traded company	Highly formalised. Investment proposals considered at divisional and head office of operating company prior to submission to owners.
H / F.C.	1) N.A.; 2) 205 hotel rooms + 72 condo's.	Hotel accommod'n, residential accommod', F&B.	Subsidiary of the owning company.	Small domestic company	Formalised aspects, however very close owner involvement results in some impulsive investment decision making.
I / F.C.	1) \$30m; 2) 330.	Accommod'n, F&B, conferences.	Large overseas publicly traded company.	Same as operating company.	Highly formalised procedure
J / F.C.	1) N.A.; 2) 317.	Accommod'n, F&B, functions, gaming.	Large overseas company.	Large overseas company.	Formalised procedure. General Manager puts forward more projects than actually required, due to the expectations of a bargaining process.
K / F.C.	1) \$40m; 2) 300	Accommod'n, F&B, recreation, conferences.	Large overseas company.	Medium / large overseas-based consortium.	Formalised. Some politicality, although "not overwhelming and not degrading the owner / operator relationship". Financial modeling used with particular importance attached to payback period.
L / F.C.	1) \$15m; 2) 380	Accommod'n, F&B, conferences.	Rooms individually owned under separate titles; owners represented through a body corporate.	Large overseas company.	Formalised process. Good working relations with owners in evidence.
M / G.M.	1) \$12m; 2) 302	Accommod'n, F&B.	Large overseas company.	Small overseas investment company	Relatively formalised process with emphasis attached to financial modeling. Can become political.

^a F.C.: Financial Controller; G.M. General Manager.

^b F&B: Food and Beverage

Figure 1

Owner / operator structure and owning company size: implications for capital budgeting formalisation.

	Large owning company	Small owning company
Divorced owner/operator structure	<p>1) Expectation: Highly formalised capital budgeting procedures.</p> <p>Finding: A, E, J (All highly formalised, some dysfunctional implications); G, K, L (Highly formalised, no specific dysfunctionality observed)</p>	<p>2) Expectation: Relatively low formalisation of capital budgeting procedures.</p> <p>Finding: B (Relatively low formalisation); M: (Some formalisation; no suggestion of an overly bureaucratic approach).</p>
Unified owner/operator structure	<p>3) Expectation: Relatively formalised capital budgeting procedures.</p> <p>Finding: C & F (Relatively formalised); I: (Highly formalised)</p>	<p>4) Expectation: Low formalisation of capital budgeting procedures.</p> <p>Finding: H (Some formalisation, however scope for “impulsive investments”), D (Highly non-formalised)</p>