Examining the Perceived Impact of Proposed Leasing Rules in Lodging Industry

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SUMMARY

The current paper reviews the history of lease accounting and will assess the perceived impact that proposed changes in lease accounting will have on the lodging industry. A questionnaire is distributed to 500 members of the lodging section of the Hospitality Financial and Technology Professionals association (HFTP); and a model will be proposed to examine the relationship between property characteristics and the perceived impact that proposed changes in lease accounting will have on the lodging industry.

From the results, this study can make valuable contributions to both industry and academia. First, management can not only get a sense of what equipment are usually being leased and how long the lease terms are, but also understand the financial impact brought from the proposed change of lease accounting and the extent of each impact to the property. Furthermore, understanding the changes being proposed to lease accounting is helpful for controllers to make decision in leasing properties. Lastly, the significance test results would provide future research ideas to scholars interested in lease accounting in hospitality industry.

BACKGROUND

Lease Accounting has a long history in United States. In 1949, the Committee on Accounting Procedure of the American Institute of Accountants issued ARB No. 38, in which the Committee posited that long-term leases were often nothing more than substitutes for ownership and mortgage borrowing. (IASB/FASB, 2007) In 1976, the FASB issued Statement No. 13, *Accounting for Leases*, which provides current guidance for lessees. Noncancelable leases that meet any one of four general criteria (1.transfer of ownership; 2. bargain purchase option; 3. lease term ≥75 percent useful life; 4. present value of commitments ≥90 percent of asset's fair value) must be capitalized. (Robert, 2001) In 1996, the G4+1 Group issued a special report in which it proposed a single method of lease accounting, eliminating the distinction between operating and capital leases. (McGregor, 1996)

In March 2009 the IASB and FASB issued a discussion paper on the future of lease accounting. This paper proposes a significant change in the accounting model for lessees. If implemented, all the rights and obligations arising from lease agreements will be recognized as assets and liabilities on the Balance Sheet. The carrying value of these assets and liabilities will need to be reassessed at each Balance Sheet date. (PWC, 2010) According to PWC, this proposal will impact all companies that have significant lease agreements in place (irrespective of whether these are classified as operating lease or finance lease today).

According to Ray Schmidgall and Arun Upneja's research, the majority of hospitality firms' leases are accounted as operating leases. They evaluated the relative importance to the lodging industry of leasing's impact, such as lower down payment, tax advantage, protection from obsolescence, and so on. (Schmidgall and Upneja, 2001) Therefore, it is likely to have some potential financial impacts to the lodging industry if the new leasing rules are implemented, and the impacts under current rules may also be different from those impacts around ten years ago.

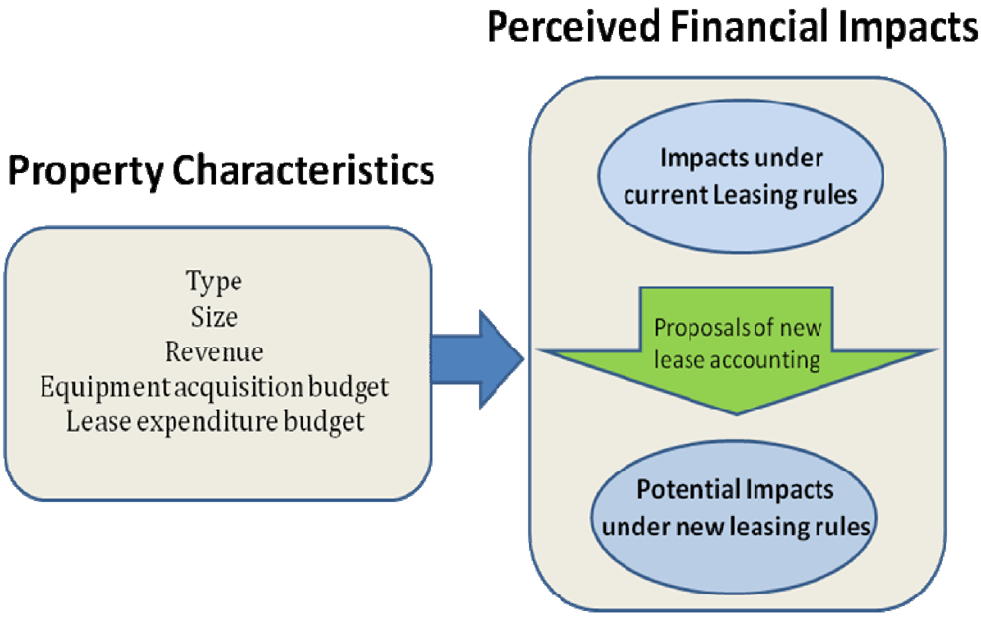
OBJECTIVES

The study contains three major objectives. First objective is to collect statistical data on the magnitude of leasing in the hotel industry. The second one is to evaluate the perceived financial impact of leasing to the lodging industry by now, which is, what the controllers of lodging industry may think, under the current rules, the impact of leasing will be. The last one, also the most important objective, is to examine the perceived financial impact the proposed changes (new rules towards lease accounting) will bring to the lodging industry. The difference that the third objective from the second one is, it examines the impact on the assumption that the new rules implement, while the second one just evaluate the current situation.

CONCEPTUAL MODEL

Based on Schmidgall and Upneja's research, controllers will have different perception on lease accounting according to the characteristics of property that they are managing. Such as the room size (how many rooms the property has), revenue (how much the annual revenue is), lease expenditure budget (how much the lease expenditure budget is), and so on. These characteristics would influence the perceived impact of controllers of lodging industry. (Schmidgall and Upneja, 2001)

This study presents an impact extent model (IEM) that was developed to investigate the perceived financial impact to different property based on size, revenue, type of property, and lease expenditure budget. For those property characteristics, except for type of property (independent, chain owned, Chain affiliated-franchise, multi-properties, and other types), all the other characteristics will be examined by using ordinal scale.



Conceptual framework: IEM

METHODS

A lease accounting questionnaire is distributed to 500 members of the lodging section of the Hospitality Financial and Technology Professionals association (IT related members is purposely excluded).

The survey contains three sections:

1. Current situation of lease accounting, which includes property characteristics, leased equipment, and the extent of current perceived financial impact of leasing on a five point scale. The scale was anchored by 1 = "not important" and 5 = "very important"
2. The awareness of the changes being proposed in lease accounting and the extent of potential perceived financial impact to the property (also on a five point scale from 1 = "not important" to 5 = "very important).
3. Information of respondent (position, major area, professional certification, year of experience).

Multivariate Analysis of Variance (MANOVA) will be used in the study. The independent variables (IVs) are property characteristics (type, size, revenue, budget), and the dependent variables (DVs) are current perceived impact of leasing (Ex: Lower down payments) and perceived impact after proposal of new leasing rules to the property (Ex: Businesses will have to analyze the service components that are part of lease contracts.). The hypothesis is:

H: There is important relationship between property characteristics and impact of leasing

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