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IFRS in Tourism,
Hospitality and Leisure:
More Than Just Accounting

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IFRS in Tourism, Hospitality and Leisure: *More Than Just Accounting*

In today's competitive global marketplace, finance functions must find the optimum recipe for business success. This includes not only being a good steward of shareholder value, but also leading the strategic alignment of company objectives and operations. Not only could International Financial Reporting Standards (IFRS) have a significant impact on your company's accounting processes and procedures, but it may also provide a strategic opportunity for positive organizational change for those who understand the benefits of a reasoned and deliberate conversion process.

Of course like any significant business decision, determining the timing and pace of conversion to IFRS requires an understanding of the potential costs and benefits. It is important to make an informed choice based on a thorough analysis.

IFRS has been seldom used in the United States until recently. As of this writing, the U.S. Securities and Exchange Commission (SEC) announced proposed rules changes that would allow certain U.S. public companies the option to use IFRS in 2009, as part of a proposed roadmap that may lead to a requirement that U.S. public companies use IFRS beginning in 2014. By 2011, it is likely that virtually every country in the world will allow or require IFRS. As the topic appears with increasing frequency in print, on the Web, and in conversation, Tourism, Hospitality and Leisure (THL) executives are beginning to take notice.

Many of the challenges in adopting IFRS – as well as the opportunities – will be affected by specific, significant competitive realities of the industry:

- THL companies often have operations and assets that span countries and continents, and tap increasingly global capital markets.
- These companies face a variety of rules and regulations, tax jurisdictions, building and occupancy codes, lease and tenant issues, finance and accounting concerns, and much more.
- In a challenging economy and a highly competitive market, THL companies are continually looking for ways to stay ahead of their rivals, in addition to finding ways to secure funding from investors to continue to fund their expansions.

IFRS potentially offers companies increased transparency and consistency of financial information, streamlined, simplified and improved internal controls, greater access to capital, simplified cross-border M&A transactions, and opportunities to improve cash management and implement income tax strategies.

These potential benefits do not come without cost. Conversion to IFRS will require commitment of specialized resources in order to properly analyze, plan and execute the implementation.

The business case for IFRS

Certain players in your organization will find themselves on the front lines of any IFRS initiative — most notably the controller and the CFO. They will have the most to gain (and lose) and probably the most work to perform in any conversion project.

Thus, these parties may find themselves needing to convince other influential colleagues — such as the CEO, audit committee members, and perhaps even the Board of Directors — of the merits of getting ahead of the issue.

If you find yourself in that situation, consider some of these talking points around the benefits of early conversion:

- 1. Global positioning:** We do business globally; our brand is international; we are expanding into new markets. Our financial reporting should be a reflection of this operational reality.
- 2. Cost savings:** We are currently reporting under multiple standards —U.S. GAAP, local GAAPs, and IFRS. Consolidating to a single reporting standard and eliminating the large number of reconciliations will yield potentially significant savings.
- 3. Inevitability:** IFRS is coming. If we start soon, we can implement a phased, efficient, and orderly process and avoid the chaos that has typified other major projects.
- 4. Alignment:** We are already undergoing a major (ERP, finance transformation, systems, etc.) project. If we integrate our IFRS conversion effort with this project, we can make better use of our resources while ensuring that the two work harmoniously together.
- 5. Internal control:** Accounting policies and procedures will be refreshed during an IFRS conversion project; the number of financial reporting standards used and analyses required will likely drop dramatically. Net result: improved accuracy and timeliness of financial reporting.

Timing is everything

Chances are you or someone in your organization is already thinking about IFRS. That's a positive sign, because developments over the last year have shifted the discussion from the abstract and distant to the concrete and near-term. "If" is no longer part of the conversation; "when" is the relevant term.

In late August 2008, the SEC announced that it would issue a proposed IFRS "roadmap" that would include a timetable and appropriate milestones for mandatory transition to IFRS starting for fiscal years ending on or after December 15, 2014. Before evaluating whether to mandate adoption, specific proposed rule changes would provide a limited number of U.S. issuers the option of using IFRS as the accounting basis for their financial statements for fiscal years ending on or after December 15, 2009. (For the latest news and information on IFRS, visit www.deloitte.com/us/ifrs.)

But if 2014 seems a long way off, think again. A conversion effort that is both sane and successful (one that can stand up to the scrutiny of regulators, analysts, and your independent auditor) will require a lengthy runway. In mid-2008, the American Institute of Certified Public Accountants announced that it considered a 3-5 year timeline to be reasonable for transition to IFRS. Other organizations have made similar estimates.

Challenges and opportunities in tourism, hospitality and leisure

As is becoming increasingly apparent, an IFRS conversion is not primarily an exercise in reshuffling the chart of accounts, nor is it principally a technical accounting and financial reporting matter. Changing accounting principles means changing the language of your business: the impact of such a change is pervasive. In fact, your company is likely to spend a significant amount of time addressing concerns around tax, valuation, treasury, legal, people, technology, and communications.

Clearly, a great deal of work lies ahead. Yet, despite these challenges, you may find that the benefits of reporting under IFRS outweigh the costs.

Consider these factors:

Conversion provides a fresh look at current practices. If your close process includes reconciling multiple generally accepted accounting principles (GAAPs), and dealing with a variety of sub-ledgers, manual adjustments, data hand-offs, and accounting overrides, you may want to consider a fresh look at your accounting policies and procedures. IFRS provides the opportunity.

Conversion can be a catalyst for streamlining and consolidation.

As your company expands through growth and acquisitions, your information technology systems may become increasingly convoluted. Many companies operate a patchwork of legacy accounting and Enterprise Resource Planning (ERP) systems — systems that can't talk directly, leading to error-prone adjustments and reconciliations. Moving to IFRS provides a chance to streamline and consolidate these disparate systems.

IFRS offers an opportunity to use principles-based accounting.

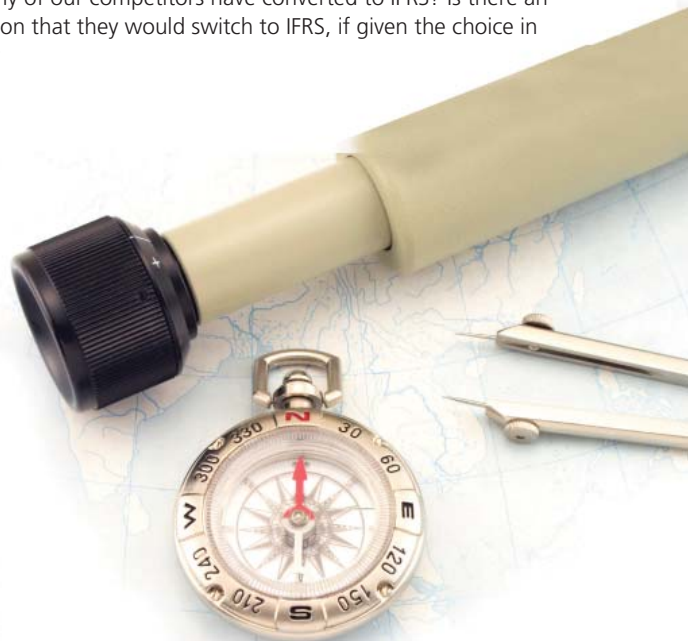
Many finance professionals have become increasingly frustrated with U.S. GAAP and its voluminous rules for dealing with virtually every accounting issue. For a decade or more, CFOs and other finance executives have openly pined for principles-based accounting to help improve the relevance and reliability of financial reporting. IFRS answers that wish.

IFRS helps open the doors of the global marketplace. Adopting IFRS may improve access to foreign capital markets by giving foreign investors greater insight into a company's financial performance. Such investors may be more comfortable with or have more confidence in a globally accepted set of accounting standards. Companies themselves can also benefit from improved ability to benchmark with peers and competitors. Many THL companies operate on a worldwide scale: growing markets, international customer base, escalating cross-border merger and acquisition activity. The fact is, your company already does business globally. Shouldn't you be reporting under a global standard?

Chart the course

If you take only one action after reading this document, we suggest it be this: develop an IFRS implementation roadmap. To kick off this effort, ask yourself and your team a few preliminary questions to gauge the potential impact of IFRS on your company.

- Have we inventoried our current IFRS reporting requirements, if any?
- How many local GAAPs do we currently report under?
- How many of our business units already prepare IFRS financial statements?
- How might our access to capital be impacted by an IFRS conversion?
- What are the expectations regarding IFRS of users of our financial information (including major shareholders, analysts who cover our company, as well as banks and other financial stakeholders)?
- How many of our competitors have converted to IFRS? Is there an expectation that they would switch to IFRS, if given the choice in the U.S.?



- Do we have a major ERP or finance transformation project in the works?
- Are we involved in or considering a major merger or acquisition?
- What is the level of IFRS knowledge within the company, both domestically and globally?
- What would be the impact on our company of a possible IFRS requirement in the U.S.?
- Have we assessed the costs and benefits of adopting IFRS?

Of course, your IFRS implementation roadmap will likely contain significantly more detail than shown above. Given the far-reaching scope of IFRS, your map-making process may assess the potential impact on each department in your organization, including finance, human resources, tax, legal, information technology, and investor

relations. Other stakeholders should also be involved, including the board, audit committee, and your external auditor.

By determining your costs, benefits, and timing up front, you can avoid the rushed approach (and unnecessary expense) that some companies experienced through initiatives such as the Sarbanes-Oxley Act and the Year 2000 computer issue.

A carefully designed roadmap will empower your company to convert on its own terms. By taking a measured and informed approach, you increase the likelihood of identifying value in an exercise that otherwise may be reactive and solely compliance driven. The value may show itself in the form of reduced costs of implementation, standardization and centralization of statutory reporting activities and related controls, greater consistency of accounting policy application, and possibly core finance transformation.

Competitive Landscape: Tourism, Hospitality and Leisure Companies by Accounting Standard

Company	Subsector	Country of Origin	Revenues (millions)*	Accounting Standard	International Operations
Harrah's Entertainment, Inc.	Gaming	U.S.A.	\$10,825.20	U.S. GAAP	•
MGM MIRAGE	Gaming	U.S.A.	7,691.60	U.S. GAAP	•
Las Vegas Sands Corp.	Gaming	U.S.A.	2,950.60	U.S. GAAP	•
Wynn Resorts, Limited	Gaming	U.S.A.	2,687.50	U.S. GAAP	•
Penn National Gaming, Inc.	Gaming	U.S.A.	2,436.80	U.S. GAAP	•
Boyd Gaming Corporation	Gaming	U.S.A.	1,997.10	U.S. GAAP	
Isle of Capri Casinos, Inc.	Gaming	U.S.A.	1,125.40	U.S. GAAP	•
Marriott International, Inc.	Hospitality	U.S.A.	12,990.00	U.S. GAAP	•
Accor	Hospitality	France	11,961.00	IFRS	•
Starwood Hotels & Resorts Worldwide, Inc.	Hospitality	U.S.A.	6,153.00	U.S. GAAP	•
Wyndham Worldwide Corporation	Hospitality	U.S.A.	4,360.00	U.S. GAAP	•
InterContinental Hotels Group PLC	Hospitality	U.K.	1,763.60	IFRS	•
Millennium & Copthorne Hotels PLC	Hospitality	U.K.	1,337.40	IFRS	•
Orient-Express Hotels, Ltd.	Hospitality	U.S.A.	578.40	U.S. GAAP	•
Avis Budget Group, Inc.	Leisure	U.S.A.	5,986.00	U.S. GAAP	•
Travelport Limited	Leisure	U.S.A.	2,780.00	U.S. GAAP	•
AMC Entertainment Inc.	Leisure	U.S.A.	2,504.30	U.S. GAAP	•
Six Flags, Inc.	Leisure	U.S.A.	972.80	U.S. GAAP	
Speedway Motorsports, Inc.	Leisure	U.S.A.	561.60	U.S. GAAP	
Groupe Casino Guichard-Perrachon	Restaurant	France	36,780.00	IFRS	•
McDonald's Corporation	Restaurant	U.S.A.	22,786.60	U.S. GAAP	•
YUM! Brands, Inc.	Restaurant	U.S.A.	10,416.00	U.S. GAAP	•
Darden Restaurants, Inc.	Restaurant	U.S.A.	6,626.50	U.S. GAAP	•
CKE Restaurants, Inc.	Restaurant	U.S.A.	1,534.60	U.S. GAAP	•
P.F. Chang's China Bistro, Inc.	Restaurant	U.S.A.	1,092.70	U.S. GAAP	•

*Revenues of the public filers listed represent the fiscal year revenues based on the company's latest filing. All amounts have been converted to U.S. dollars using the Euro or Sterling exchange rate (as applicable) as of December 31, 2007.
Source: corporate websites, SEC filings

Which approach will work for you?

Generally speaking, two approaches to IFRS conversion predominate: all-in and tiered. The former is characterized by a relatively short timeframe; simultaneous conversion of all reporting entities; dedicated project teams; and devotion of significant resources. The latter is conducted over a more extended period; with phased conversion of reporting entities; with at least some personnel retaining their “day job” duties; and with a spreading out of project costs.

When the European Union converted to IFRS in 2005, it was, for most companies, an all-in effort driven by the tight timelines imposed by the European regulators. Without the luxury of time to convert on a tiered basis, most companies were forced to rush through the process, leading to inevitable inefficiencies and ineffectiveness. (See sidebar, “The European Experience,” on page 13.)

A tiered approach – staged, rational and measured – to IFRS conversion will likely provide better results. This comes with a seemingly self-contradictory caveat: you’ll have to act fast if you want to go slow. That is, if you want to reap the benefits of phasing in your conversion, you’ll need to start planning soon.

Companies that choose a tiered strategy should consider staggering their conversion on a country-by-country or region-by-region basis. As each group moves through the stages (see graphic, “A Tiered Approach to IFRS Conversion” below), the processes developed and lessons learned are applied to the next group.

More than accounting

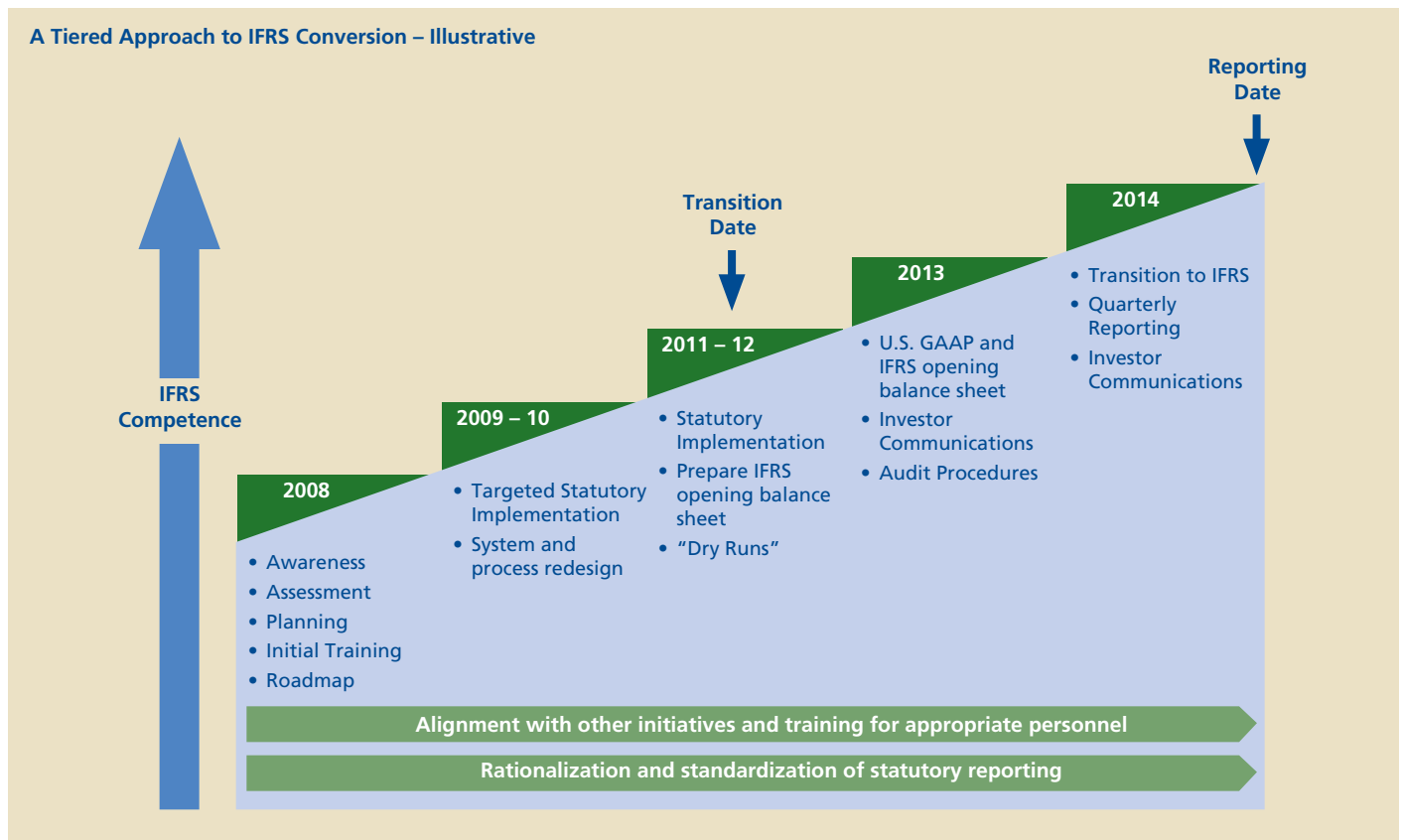
Without question, the impact of IFRS on the general ledger and the financials will be substantial. But in a relative sense, the accounting may be the easy part. How you handle the nonfinancial aspects of the conversion may be a far more accurate indicator of your success. Among the areas warranting your attention are human resources, legal, M&A, valuation, tax, treasury and information technology.

Human Resources: As noted, IFRS involves much more than reorganizing the chart of accounts. It represents a fundamental change that cascades well beyond the finance department

Consequently, human resources issues may be a major concern. A conversion project will place increased demands on your personnel, which may come at a time when you are least able to handle it. Finance organizations have streamlined in recent years, downsizing accounting functions through reduced hiring, layoffs, and attrition, as well as outsourcing or offshoring key functions. Unfortunately, these personnel reductions may mean that the people who could best help with your IFRS efforts are no longer available.

Recruiting may pose another challenge, particularly in the United States. College accounting programs across the country represent an important pipeline for keeping finance functions staffed and operating. Yet, most U.S. university accounting programs are only now beginning to develop comprehensive instruction on IFRS.

This issue can be addressed through training programs in the U.S. and internationally, to help key personnel become proficient in both IFRS and U.S. GAAP.



Legal: The ripple effects of conversion to IFRS will surely be felt by your legal department. Many contracts will need to be examined for possible impact, and some agreements, including debt compliance covenants, will need to be renegotiated and restructured.

The THL industry has a propensity for joint ventures, licensing, royalty and other profit-sharing agreements, as well as other collaborative arrangements. The contractual underpinnings of all these relationships will need to be revisited to recast key terms in a new reporting language.

Education and retraining will also come into play for the legal team. IFRS principles and associated guidance from the Securities and Exchange Commission will need to be analyzed and understood from a legal perspective.

Regulatory: The opportunity to reduce local GAAP reporting and coalesce around a single standard will be appealing to many THL companies. The change may be dramatic. For example, until recently, companies doing business in Western Europe had to track financial information using up to 21 different GAAPs. The EU's 2005 conversion to a single standard harmonized and simplified compliance, and today there is more cross-border consistency in the application of rules and standards.

A fringe benefit of conversion may be the promise of collaboration among various regulatory bodies. The model for this was provided by the Committee of European Securities Regulators (CESR), an independent body that works to improve coordination among EU securities regulators. This group, formed in 2001, played an important role in the IFRS conversion effort by bringing together regulators from across the EU to discuss issues, smooth over differences, and reconcile complex points of view.

As other countries across the globe adopt IFRS, the prospect of additional regulatory bodies (such as the SEC) interacting with their counterparts increases. Thus, the movement toward IFRS is changing the regulatory dynamic, forcing regulators to think globally, instead of nationally, in how they treat these issues.

Tax: The tax considerations associated with a conversion to IFRS, like the other aspects of a conversion, are multifaceted. The tax analysis will likely include an assessment of key tax accounting differences between FAS 109 and IAS 12, the impact of pre-tax accounting changes on tax methods, the impact on global planning strategies that are already in place and those still contemplated, and the information systems in place to capture all the necessary data. A conversion to IFRS will require an understanding of the impact of IFRS on tax matters and processes.

One area for a THL company to consider is its involvement in IP migration strategies where it shares high value intangibles such as trade-names, processes and systems across borders. When such an arrangement is entered into with a related party, the transaction is typically eliminated in consolidation for financial reporting purposes. For certain arrangements, historically under FAS 109, paragraph 9(e), no current tax or deferred tax was required to be recorded. IAS 12 does not have a similar exception; therefore, such an arrangement could have a substantial impact on the effective tax rate as the book income will continue to be deferred while the tax consequences are recognized.

Share-based payments are commonly used as an incentive for THL employees. Some advantage may be gained from an IFRS conversion by having a standard principle across entities and countries. However, this benefit may also come with an unanticipated consequence, since the deferred tax asset associated with share-based payment arrangements under FAS 123R is recorded based upon the book expense recognized. Under IFRS, the deferred tax asset is based upon the expected tax deduction as of the reporting date (i.e., the difference between the fair market value of the stock on the reporting date and the exercise price). Therefore, the fluctuation of the stock price will directly impact the deferred tax asset recorded, and since the compensation expense under IFRS is not based on the same expected tax deduction amount, the effective tax rate may become more volatile.

Other differences between IFRS and U.S. GAAP may also have an impact on the calculation of book-to-tax differences. For differences that impact pre-tax accounting methods, a THL company will need to consider the following questions:

- Is the new financial reporting standard a permissible tax accounting method?
- Is the new book method preferable for tax reporting purposes?
- Is it necessary to file changes in methods of accounting?
- Will there be modifications in the computation of permanent and temporary differences?
- Do planning opportunities exist?

Further examples of differences a THL company may be faced with are the requirement to book assets using a component approach and the option to revalue assets. The company will have to address the questions above in order to fully understand the impact of accounting choices and requirements. These differences may also have systems implications. Though companies are accustomed to having book-to-tax differences related to fixed assets, most systems are not designed to track revaluation of existing assets. Other areas of pre-tax difference that may be of particular interest to THL companies include the treatment of lease transactions and business combinations.

The issues associated with componentization and revaluation of fixed assets may have broader impact than just tax methods. And it isn't all down side. One unexpected outcome of addressing the componentized assets approach relates to cost segregation studies. Historically these studies were of value only to the tax department in order to maximize accelerated depreciation deductions by identifying shorter lived assets. These studies identify assets at the component level. Therefore, the benefit to having such a study on large projects will increase as it will be of use to the financial accounting department as well; therefore, organizations may be more likely to have such studies performed, and as a result, maximizing tax benefits.

Additionally, real estate investment trusts ("REITs") often invest in THL assets and may need to consider whether this component approach to accounting for fixed assets could impact the determination of their requisite holdings of real estate assets. Having component level fixed asset records will more clearly identify the asset makeup of real and personal property and potentially highlight any exposure for non-compliance with the asset test.

The key to an effective conversion to IFRS is advanced planning. Tax issues such as those discussed above need to be addressed in the planning stages of a conversion. If a company waits until a conversion is complete to address these matters, the process will likely be very difficult and the potential benefits in accounting choices, systems enhancements and planning opportunities may not be maximized.

Treasury: Moving to a global financial reporting model may open up access to new sources of capital. Many global lenders, global private equity firms, and international exchanges require or prefer IFRS reporting due, in part, to its increased transparency, use of fair value, which improves comparability to other investments or companies. Thus, these sources potentially become new avenues for capital funding, particularly in the current U.S. dollar environment.

Note, however, that greater use of fair value may create more volatility in your company's access to capital. That is, not only can reporting under IFRS potentially open up access to additional capital in a favorable fair value environment, but it can also serve to limit additional capital in an unfavorable fair value environment.

Furthermore, with reporting or disclosure under fair value, management will certainly need to understand, evaluate, and manage the expected market reactions to reported volatility of values. This will represent new territory for most U.S.-headquartered THL companies.

Additional impacts of IFRS on the treasury function may include the following:

- Companies that choose to present fair value may consider the need to lower their leverage models to ensure that market fluctuations can be adequately absorbed by equity.
- Companies may need to consider and revise debt terms for covenants previously based on U.S. GAAP metrics or financial results which don't make sense or are no longer attainable under IFRS.
- The clearer view that lenders get of the fair value of collateral (whether presented on the balance sheet or disclosed in the footnotes) may alter their evaluation of creditworthiness and may impact the terms of new debt instruments (e.g., more stringent collateral and covenants requirements).

Contract Management: An IFRS conversion will potentially impact your existing contracts. Consider involving your legal team as part of the assessment and implementation process. Issues may include the following:

- Many contracts may need to be reviewed to make sure the proper accounting treatment is followed under IFRS. To improve the efficiency of this process, a contract database could be created (if not already in place) to better monitor the IFRS conversion and tracking of effects.
- Many THL companies participate in joint ventures that they don't directly control. Thus, it can be difficult for the company to obtain all the necessary information to accurately convert to IFRS. For example, trying to identify the components of a hotel that was funded – but not built or managed – by your company may prove vexing. In such instances, you may want to reassess (and potentially revise) your requirements for financial and accounting information from the joint venture.

- The IFRS conversion may trigger the need to amend contracts with financial institutions and joint venture partners in regards to financial accounting information to be supplied by your company. You may have to reword certain sections to address regulatory or third-party requirements to replace U.S. GAAP with IFRS information.

Technology Issues: IFRS is expected to have wide-ranging impacts at different levels of the IT systems architecture. The realignment of the company information systems will pose a real challenge for IT (along with the rest of the organization). Virtually all applications and interfaces in the system architecture can be affected, from the upstream or source of data to the farthest end of the reporting tools. As such, time and resource needs may be significant.

As you plan changes to your IT systems, you will need to take into account external factors such as local and international regulations, financial consolidation of subsidiaries, stock markets, and external auditors. This business transformation should not be considered a one-step project. It may be necessary to implement short-term initiatives strategically designed to institute an effective long-term solution for the organization.



Potential Technology Impacts

Upstream Source Systems and Transformation Layer	General Ledger and Financial Applications	Reporting Data Warehouse Planning and Calculation Engines	Downstream Reporting Capabilities
Differences in the accounting treatment between current accounting standards and IFRS will create a need for new input data.	Differences in the accounting treatment between current accounting standards and IFRS will likely drive changes to general ledger design, chart of accounts, as well as sub-ledgers and feeds.	IFRS has much more extensive disclosure requirements, requiring regular reporting and usage of financial data that may not be standardized in current data models.	The differences that arise in the accounting treatment between current accounting standards and IFRS will create a need for changes in reporting.
Data and transactions that are captured, stored and ultimately sent to the financial systems may not have all the needed attributes or qualities.	Multinational companies may ultimately realize a need to re-develop general ledger platforms or additional sets of books to ensure compliance with multiple financial reporting requirements.	Increased need for documented assumptions, sensitivity analyses; potential factors that could affect future development may expand the scope of information managed by financial systems.	Assumption changes from period to period can introduce significant volatility and require detailed support for derivation and rationale for changes, requiring design of additional reports.
Sub-ledgers within the ERP may have additional functionality to support IFRS that is currently not being utilized but could be implemented.	Multi-ledger accounting functionality within newer releases of ERP's may be considered for long-term solutions.	Reporting warehouse feeds to calculation engines may need to be adjusted in a standardized way to support reporting processes.	External reporting templates will likely require revisions to reflect IFRS requirements.
Transformation layer not likely to have been designed with IFRS in mind; data sender/receiver structures may need to be adjusted.	Changes to IFRS will likely necessitate redesigned accounting, reporting, consolidation, and reconciliation processes, which may impact configurations of the financial applications.	Data governance functions and meta data repositories (potentially including data dictionary, ETL & business intelligence tools) may need to be adjusted to reflect revised data models.	Increased disclosures such as sensitivity tests and roll-forwards may require additional ad hoc query capabilities.
Over time the potential for acquisitions of companies using IFRS will increase; altering source systems and Extract, Transform and Load (ETL) tools to provide all needed data elements will make integrations significantly more efficient.	Differences that arise in accounting treatment between current accounting standards and IFRS may create a need for new expense allocations and other calculations.	Current valuation systems may not have functionality to handle IFRS requirements.	



Technical accounting issues for THL companies

In September 2008, the FASB and the International Accounting Standards Board ("IASB") issued an updated memorandum of understanding ("MOU") describing the milestones related to their completion of major joint projects by 2011. In updating the MOU, the boards noted that the major joint projects will take into consideration their ongoing efforts to improve and converge their conceptual frameworks. THL companies and executives are encouraged to contribute to the standard setting process by providing comments when the exposure drafts are issued. Refer to the table below for the IASB's structure and refer to the side table for the IASB's process.

U.S. GAAP and IFRS differ in key ways, including their fundamental premise. Overall U.S. GAAP is more of a rules-based system, whereas IFRS is more principles-based. This distinction may prove more vexing than it initially appears, because most accounting and finance professionals in the U.S. have been schooled in the rules of U.S. GAAP. The overriding lesson from their years of study and work was this: If you have an issue, look it up. Under U.S. GAAP, voluminous guidance attempts to address nearly every conceivable accounting problem that might arise. And if that guidance doesn't exist, it generally is created. On the other hand, IFRS is a far shorter volume of principles-based standards, and consequently requires more judgment than U.S. GAAP practitioners are accustomed to.

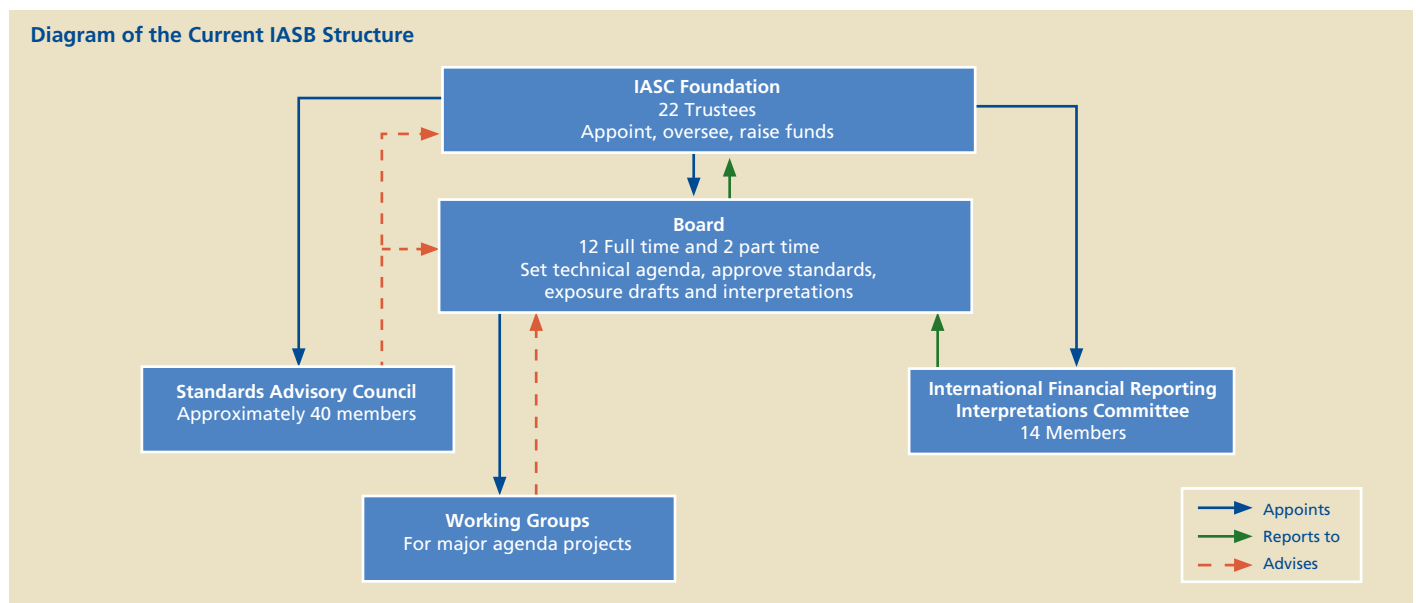
Several key accounting differences that may have a significant impact on THL companies are (1) accounting for property, plant and equipment; (2) accounting for impairment of long-lived and indefinite-lived assets; (3) accounting for customer loyalty programs; and (4) accounting for leases. The section that follows provides an overview of these key differences and the impact that each may have on THL companies. For more information on these topics, as well as other differences between U.S. GAAP and IFRS, please visit www.iasplus.com.

Formal due process for IASB projects normally involves the following steps:

- Asks staff to identify and review the issues associated with the topic and to consider the application of the Framework to the issues;
- Study national accounting requirements and practice and exchange views about the issues with national standard-setters;
- Consult the Standards Advisory Council about the advisability of adding the topic to the IASB's agenda;
- Form an advisory group (generally called a 'working group') to advise the IASB and its staff on the project;
- Publish for public comment a discussion document;
- Publish for public comment an exposure draft approved by vote of at least nine IASB members, including any dissenting opinions held by IASB members (in exposure drafts, dissenting opinions are referred to as 'alternative views');
- Publish within an exposure draft a basis for conclusions;
- Consider all comments received within the comment period on discussion documents and exposure drafts;
- Consider the desirability of holding a public hearing and the desirability of conducting field tests and, if considered desirable, holding such hearings and conducting such tests;
- Approve a standard by votes of at least nine IASB members and include in the published standard any dissenting opinions; and
- Publish within a standard a basis for conclusions, explaining, among other things, the steps in the IASB's due process and how the IASB dealt with public comments on the exposure draft.

Source: IAS Plus, <http://www.iasplus.com/restruct/restruct.htm#board>

Diagram of the Current IASB Structure



Property, Plant, and Equipment (IAS 16 (Revised))

Property, plant, and equipment (PP&E), one of the most significant line items on a THL company's balance sheet, represents a key area of difference between IFRS and U.S. GAAP.

Measurement after Recognition

Under IFRS, an entity may elect to value PP&E using either the cost or revaluation model. Under the revaluation model, an entire class of PP&E is revalued at fair value regularly, if fair value can be measured reliably. The revalued amount is the fair value of the asset at the revaluation date less any accumulated depreciation and accumulated impairment charges. Revaluation increases are credited to equity and labeled revaluation surplus. However, if a revaluation decrease has been previously charged to income, then the revaluation increase would be charged to income to the extent of the previous revaluation loss and any additional amount would be credited to equity and labeled revaluation surplus. Revaluation losses are charged first against any revaluation surplus in equity related to the specific asset, and any excess charged to income.

This is significant to THL companies, since companies may choose to value certain asset groups (e.g., land and buildings), but not revalue other groups (e.g., machinery and furniture and fixtures) using the revaluation model. Consequently, THL companies will also need to determine the impact this will have on their accounting systems. Systems will need to be able to track these changes and re-compute the related depreciation. Similarly, the decrease in fair value of the asset will trigger a decrease in the annual depreciation.

Depreciation

IFRS requires a component approach for depreciation where assets must be separated into individual components and depreciated over their useful lives. For example, components of a THL company's building may include the building structure, roof, flooring, furnishings, pools and parking lot, etc. Each of these components could represent a separate depreciable asset with different useful life or depreciation method. Subsidiary ledgers will need to be set up to ensure that asset components are properly recorded as individual components.

Estimates of useful life and residual value, and the method of depreciation are reviewed at least annually. The residual value may be adjusted up or down, and any changes that result in differences in expectations from previous estimates, shall be accounted for as a change in an accounting estimate under IFRS. These changes also have a direct affect on the depreciation taken on the asset, as the higher values would result in higher depreciation and vice versa. Additionally, IFRS requires that the depreciation method applied to an asset be reviewed at each financial year-end. If there is a significant change in the expected pattern of consumption of the future economic benefits of the assets, the method shall be changed to reflect the changed pattern.

Impairment of Long-lived and Indefinite-lived Assets (IAS 36 (Revised))

Management agreements, franchise agreements, license agreements, customer lists, trademarks, and goodwill represent some of the long-lived and indefinite-lived assets held by THL companies.

IFRS requires that goodwill and other indefinite-lived intangibles be tested for impairment at least annually, or more frequently if an indicator is present. Other long-lived assets are reviewed at the end of each reporting period for any indication of impairment, and tested for impairment if necessary. IFRS requires impairment testing at the "cash-generating unit" (CGU) level, which is generally similar to the U.S. GAAP "asset group" level, but may result in a lower level of testing.

However, IFRS differs from U.S. GAAP in the method and valuation for calculating impairment, and allows for reversal of impairment with the exception of goodwill. Long-lived asset impairment is a one-step approach under IFRS and is assessed on the basis of recoverable amount, which is calculated as the higher of fair value less costs to sell or value in use (e.g., discounted cash flows). If impairment is indicated, assets are written down to the higher recoverable amount.

The ultimate effect of IFRS is that impairment will likely occur sooner than under U.S. GAAP, but may not be as high. For example, assume a resort's undiscounted cash flow exceeds the asset carrying value, but its fair value (in use, determined through a discounted cash flow model) is less than the asset carrying value. No impairment charge would be recorded under U.S. GAAP as the step 2 test would not be performed. An impairment charge would be recorded under IFRS.

Comparison of Impairment Approaches

	U.S. GAAP		IFRS
	Goodwill	Fixed Assets	All Finite & Indefinite-Lived Assets
Step 1	Determine if impairment exists by comparing the total carrying value of the reporting unit to its fair value. If the carrying value exceeds the fair value, go to step 2.	Determine whether impairment exists by comparing the carrying value of the asset group to the undiscounted cash flows. If the carrying value exceeds the undiscounted cash flows, go to step 2.	Determine if impairment exists by comparing the carrying value of the CGU or asset to its recoverable amount as defined above. If the carrying value exceeds the recoverable amount, impairment is recognized for the difference.
Step 2	Calculate and assign fair value of all other assets and liabilities of reporting unit, remainder equals implied goodwill. Impairment charge is measured as the difference between the carrying value and implied fair value of goodwill.	An impairment charge is recognized by reducing the carrying value of the asset group to its estimated fair value.	Not applicable.

After the recognition of an impairment charge, the depreciation or amortization charge for the asset shall be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value, on a systematic basis over its remaining useful life. An impairment charge shall be recognized immediately in profit or charge, unless the asset is carried at revalued amount. Any impairment charge of a revalued asset shall be treated as a revaluation decrease.

Reversal of Impairment Charge

Except for goodwill, IFRS allows the reversal of impairment charges if the recoverable amount of an asset has increased since the impairment charge was recognized. An entity should increase the value of the asset to its current recoverable amount and the prior impairment charge recorded is therefore reversed, not above the carrying amount of the asset that would have existed if no impairment charge had been recognized (i.e., the otherwise net carrying amount after regular depreciation expense is deducted). A reversal of an impairment charge for an asset other than goodwill shall be recognized immediately in profit or loss, unless the asset is carried at revalued amount. Any reversal of an impairment charge of a revalued asset shall be treated as a revaluation increase.

Impaired assets must be tracked at original value in order to calculate the amount of impairment reversal. The reversal of the impairment is only allowed to the extent of the impairment previously recognized. After the reversal of an impairment charge, the amortization amount for the asset should be adjusted on the basis of the new value of the asset, its residual value, and its remaining useful life.

Customer Loyalty Programs (IFRIC 13)

Another difference between IFRS and U.S. GAAP, which will likely have a significant impact on THL companies, is the accounting for customer loyalty programs. Many hotels, travel agencies, rental car agencies, restaurants, etc. have loyalty programs. Under U.S. GAAP, there is no specific accounting guidance surrounding the accounting for customer loyalty programs. In fact, the scope of EITF 00-14 *Accounting for Certain Sales Incentives* and EITF 00-22 *Accounting for Points and Certain Other Time-Based or Volume-Based Sales Incentive Offers, and Offers for Free Products or Services to Be Delivered in the Future* specifically excludes these types of arrangements. As a result of the lack of specific guidance, there is diversity in practice where some entities have applied the 'accrual' or 'incremental cost' approach, while others have applied other methods.

IFRIC 13, "Customer Loyalty Programs," provides guidance for when customers can redeem goods or services for free or at a discount. IFRIC 13 specifies that such awards are 'multiple element revenue transactions' and the fair value of any consideration received or receivable should be allocated between the award credits granted and the other components of the transactions. This treatment applies irrespective of whether the entity supplies the awards or whether a third party supplies them. IFRS does not permit the application of the 'accrual' approach where the full consideration received is recognized with a separate liability for the cost of supplying the awards.

IFRIC 13 requires entities to account for the award credits as a separately identifiable component of the sales transactions in which they are granted. The fair value of the consideration received or receivable is allocated between the award credits and the other components of the sale. The consideration allocated to the award credits is measured by reference to their fair value, i.e. the amount for which the award credits could be sold separately. In addition, IFRIC 13 explains that some of the consideration received in respect to the initial sale should be allocated to the award credits and recorded as deferred revenue until the entity fulfills its obligations to deliver awards to customers.

Leases (IAS 17 & IFRIC 4)

The scope of IFRS lease guidance includes the right to use other assets in addition to property, plant, and equipment (e.g., certain intangible assets). Intangible assets are within the scope of IAS 17 if they establish rights for the exclusive use of the intangible asset. For example, brands and trademarks often are licensed exclusively and therefore are intangible assets that are included in the scope of IAS 17.

Lease Classification

Under IFRS, lease classification (e.g., operating or finance - IFRS term for capital lease) depends on similar criteria as U.S. GAAP, but without the bright-line guidance. For example, IAS 17 states that the lease term is for the "major part" of the economic life (not a strict 75 percent) or the present value of the minimum lease payments at lease inception is for "substantially all" of the fair value (not 90 percent). The basic IFRS principle is, if it is clear from other features that the lease does not transfer substantially all risks and rewards incidental to ownership, the lease is classified as an operating lease. In calculating the amounts above, THL companies must use the interest rate implicit in the lease. These changes could result in potentially more capital leases. Furthermore, a company's systems may be impacted to account for changes in lease classifications.

Leases of Land and Buildings

U.S. GAAP generally requires the lease of land and building elements to be accounted for as a single unit in all but limited circumstances. IAS 17 requires the lease of land and building elements to be accounted for separately for a lease classification unless the land element is not material. The present value of the minimum lease payments, including any lump-sum upfront payments, are allocated between the land and building elements in proportion to their relative fair values at the inception of the lease. This can significantly impact THL companies that lease both the land and the building. THL companies will need to re-assess their lease classifications and may need to break out the land and the building into separate leases.

Lease Expense

Similar to U.S. GAAP, lease expense should be recognized on a straight-line basis over the lease term, unless another systematic basis is more representative of the pattern of benefit. Lease incentives (such as free rent periods) are recognized as a reduction of expense over the lease term.

Membership Fees (IAS 18)

Many THL companies offer lifetime or other ongoing membership services to their health clubs, premier clubs, golf clubs, etc. for a fee. The nature of the membership fees are a key factor in determining the revenue recognition of those fees. For example, a company sells a lifetime membership in a health club to its customer. After paying a nonrefundable “initiation fee,” the customer is permitted to use the health club indefinitely, so long as the customer also pays an additional usage fee each month. The monthly usage fees collected from all customers are adequate to cover the operating costs of the health club. Although, the initiation fee is a non-refundable fee, under U.S. GAAP, the initiation fee is not deemed to constitute a discrete earnings event and as a result this up-front fee is recognized pro-rata over a period of time. In some cases, the period of time may not be readily available and thus the revenue may be deferred and recognized ratably over the estimated life of the facilities or some other determinable period.

As stated in IAS 18, “Revenue recognition depends on the nature of the services provided. If the fee permits only membership, and

all other services or products are paid for separately, or if there is a separate annual subscription, the fee is recognized as revenue when no significant uncertainty as to its collectability exists. If the fee entitles the member to services or publications to be provided during the membership period or to purchase goods or services at prices lower than those charged to non-members, it is recognized on a basis that reflects the timing, nature and value of the benefits provided.”

This is a significant change for companies that offer a one-time membership fee and subsequently receive monthly fees that cover the costs of operating the facilities. IFRS may allow companies to recognize the initial fee once collectability is assured; if the fee is non-refundable, companies may be able to recognize the revenue once the initial fee is received.

Other accounting differences

In addition to the detailed differences outlined above, IFRS may pose other accounting challenges to THL companies. A chart showing several U.S. GAAP/IFRS differences follows:

Technical Accounting Issues			
Additional Differences	Potential Implications		
	Differences	Financial Statements	Process/IT
Asset retirement	Under U.S. GAAP, an entity shall capitalize an asset retirement cost by increasing the carrying amount of the related long-lived asset by the same amount as the liability. IFRS allows asset retirement obligation costs to be added to the carrying amount of the inventory in the period in which they are incurred.	May result in different recorded values.	Systems modifications may be necessary to track components.
Advertising costs	Advertising costs are expensed as incurred or capitalized and then expensed the first time the advertisement runs under U.S. GAAP. Those costs are generally expensed as incurred under IFRS.	May result in different disclosure requirements.	Systems modifications may be necessary to track components.
Classification of discontinued operations	Under IFRS, a component may be a reportable business or geographical segment; U.S. GAAP is less restrictive where it can be an operating segment, a reporting unit, a subsidiary, or an asset group. Under U.S. GAAP, disposing entity should have no significant continuing cash flows or continuing involvement; IFRS does not specify any such condition	Different classification criteria for discontinued operations.	Current systems might require modifications to accommodate different classification criteria.
Presentation of discontinued operations	Unlike U.S. GAAP which requires both pre-tax and post-tax income/ loss, only post-tax income/loss is required on the face of the income statement under IFRS.	Different presentation requirements.	Current systems might require modifications to accommodate different classification criteria.
Cumulative exchange differences inclusion in carrying amount of asset (or disposal group)	Not included under IFRS; Included under U.S. GAAP.	May result in a different carrying value.	System modification to adjust the carrying values.

Technical Accounting Issues, cont.

Additional Differences	Potential Implications		
	Differences	Financial Statements	Process/IT
Employee benefits: pension costs – actuarial gains & losses	Unlike IFRS, the actuarial gains & losses cannot be deferred under U.S. GAAP.	May result in potential changes to employee cost. Further, valuation of pension asset/liability may also differ.	Current systems might require modifications to perform calculations.
Employee benefit-valuation date	Both IFRS and U.S. GAAP permit different dates for measurement of the fair value of the plan assets and benefit obligation.	May result in potential changes in the value of the asset/liability.	Current systems might require modifications to perform calculations.
Re-structuring liability	Under IFRS, recognition can be made based on announcement/ implementation of detailed formal plan. However, recognition solely based on commitment to plan is prohibited under U.S. GAAP.	Difference in basis of valuation may impact valuation of liability.	Current systems might require modifications to perform calculations.



Smoothing the transition

If you decide an accelerated IFRS conversion is desirable, here are a few considerations for smoothing implementation:

Leverage existing projects: If you are already going through — or recently completed — an enterprise resource planning (ERP) or finance transformation project, now may be the time to consider IFRS adoption. Recent versions of major ERP systems are designed to accommodate IFRS, which can be mapped in, usually with significant cost savings.

Conduct a trial run: Implementation might be easier if you take a bite-sized approach starting with a single country or reporting entity. Use existing reporting requirements and local country IFRS requirements to your advantage. For example, subsidiaries in countries adopting IFRS over the next three years may be good candidates for your trial run. Learn from this initial conversion exercise, and apply the lessons learned to your global rollout down the road.

Consider shared services centers: IFRS might provide a compelling reason to establish shared services centers and to consolidate dozens of local GAAPs down to a single reporting standard. Geographically-dispersed finance offices could be drastically reduced or even eliminated in favor of a central finance function, strategically located to take advantage of tax incentives, payroll savings, and facilities cost reductions. In many cases, this concept is already aligned with the strategic direction THL companies have taken or are currently considering relative to their finance function.

Time for leadership

You are in an enviable position, because you possess knowledge that many others in your organization may not: the movement toward IFRS is inexorable; and the initiative involves multiple corporate functions, not solely finance.

So you have a choice: either sit back and wait for it to happen (with all the attendant uncertainty and risk), or mobilize your company to attempt to extract every possible benefit and dodge every avoidable obstacle.

In other words, it's time for leadership.

By starting now, you will likely spread out your costs, get the jump on your competition, and reel in scarce talent before it vanishes. You can avoid the fire-drill atmosphere that characterizes most last-minute projects. You can improve your processes and systems. You can integrate with other initiatives, such as an ERP upgrade or a merger or acquisition. Most important, you can do it on your own terms, at a pace that suits your company and its circumstances.

THL companies are characterized by intensive activity that places major demands on financial and human resources. An IFRS project cannot be a distraction from the primary activities of your business. It must be integrated, coordinated, and aligned. It starts now with some preliminary questions and a carefully drawn roadmap. And it ends somewhere in the next decade when you report for the first time under a single unified standard. Whether the journey from here to there is rocky or smooth may be entirely up to you.

The European experience

In July 2002, the European Parliament passed legislation requiring listed companies to convert to IFRS by 2005. The short timeframe and extensive reach of the directive had many companies scrambling to comply. Anecdotal reports from the field suggest that the conversion placed significant resource pressure — human and financial — on finance teams and their companies at large.

A more tangible measurement of the effort can be found by comparing European companies' 2004 (local GAAP) and 2005 (IFRS) financial statements. The latter averaged more than 50 percent longer than the former; in some instances, reports doubled in length. Much of the increase can be attributed to an increased level of disclosure in the financial statements in areas such as judgments made and assumptions used.

Certain accounting issues proved especially vexing during the transition, including asset impairments, financial instruments, and lease accounting.

Among the lessons learned from the European experience were the following:

- **The effort was often underestimated.** The original perception that conversion was solely an accounting issue was replaced with a growing realization that the initiative was much larger and more complex.

- **Projects often lacked a holistic approach.** Because of the limited view cited above, companies frequently did not take the collateral effects into consideration, such as the impacts on IT, HR, and tax.
- **A late start often resulted in escalation of costs.** Those few companies that anticipated conversion and took steps to prepare for it were in much better shape than those that did not. Companies that delayed their response paid a price for it, in terms of higher costs and greater diversion of resources.
- **Many companies did not achieve “business as usual” state for IFRS reporting.** The highest quality financial data is obtained when companies fully integrate IFRS into their systems and processes. The compressed timeframes precluded this possibility; instead, first-year financials were often produced using extraordinary, labor-intensive, and unsustainable measures.

Several European companies are only now starting to explore benefits from IFRS implementation. Due to multiple constraints, the first-year effort in the EU was focused more on “getting it done.” Potential benefits in terms of reducing complexity, increasing efficiency, and decreasing costs had to be deferred.

Resources

Deloitte has extensive IFRS experience in THL. With thousands of IFRS-experienced professionals in our global network, we provide a comprehensive array of services related to IFRS. As a multidisciplinary organization, we can help companies address a wide range of IFRS issues.

Deloitte offers companies assistance with:

- Evaluating the potential impacts of IFRS
- Assessing readiness for IFRS conversions
- Implementing IFRS conversions, providing support with technical research, project management, and training
- Addressing the implications of IFRS in such areas as tax, finance operations, technology, and valuation

Deloitte's THL Practice:

To learn more about our practice, visit us online at www.deloitte.com/us/thl. Here you can access our complimentary Dbriefs webcast series, Deloitte Insights podcast program, innovative and practical industry research, and a lot more about the issues facing THL businesses from some of the industry's most experienced minds.

Deloitte's Online Resources

For a wealth of online resources related to IFRS, visit www.deloitte.com/us/ifrs. Available materials include newsletters, whitepapers, pocket guides, timelines, webcasts, podcasts, and more.

International Accounting Resources

The International Accounting Standards Board (IASB) provides additional guidance. Visit the IFRS section of www.iasb.org for additional details and copies of the standards.

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