USALI Treatment of Preopening Expenses

The 11th revised edition of the Uniform System of Accounts for the Lodging Industry (USALI) was published in the spring of 2014, with an implementation date of January 1, 2015. The responsibility for revising the USALI lies with the Financial Management Committee (FMC) of the American Hotel & Lodging Association (AH&LA).

Throughout the implementation process, the FMC has received several questions from the worldwide lodging industry. To answer these questions, the FMC has created a Frequently Asked Questions (FAQ) document on the USALI resource portal page of the AH&LA Education Institute's (AHLEI) website (www.ahlei.org/usali).

In an effort to assist hotel owners and operators with their implementation, the FMC is presenting a series of monthly articles that address some of the most frequently asked questions. Some of the topics to be discussed include the expanded labor cost reporting, gross versus net revenue reporting, service charges, the change from cover to customer counts, mixed-ownership facilities, and operating metrics.

For this month we discuss pre-opening expenses. The article was prepared by FMC committee member Gordon Potter, Ph.D.

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USALI Treatment of Preopening Expenses

By Gordon Potter Ph.D.

There have been numerous inquiries regarding the USALI treatment of preopening expenses. These costs are generally associated with the opening of new business unit, and they should be expensed as incurred.

Preopening costs have been a source of confusion since 1996 when the 9th edition of USALI was published. The 9th edition stated " *this edition has deleted all references to preopening expenses. This action was taken because it has become common practice to write off preopening expenses as incurred or to amortize them over a period of no more than one year." **[1]*** Beginning in 1999, AICPA issued Statement of Position 98-5 [2] that required nongovernmental entities to expense the costs of start-up activities as they are incurred. In the United States, the accounting for start-up costs is now codified in FASB ASC 720-15.

Preopening activities are considered a type of start-up activity. Examples of start-up activities include opening a new facility, introducing a new product or service, conducting business in a new territory, and conducting business with a new class of customer. They also include activities related to organizing a new entity (often described as organization costs). In the lodging industry preopening activities are primarily associated with the opening of a new property. As displayed in Exhibit One, preopening expenses include salary-related expenses for new employees, as well as the training costs and meals for these new employees. Other preopening expenses include salaries and all-travel costs for the property opening team, and all property carrying costs, such as property taxes, utilities, and insurance, once the facility is complete. Costs related to advertising, furniture, fixtures and equipment, coupons, and licenses are not considered preopening expenses and are addressed elsewhere in the USALI.

Exhibit One

Types of Preopening Expenses

Considered Preopening Expenses

- Salary-related expenses for new employees
- Salary-related expenses for the management property opening team
- Training costs and meals for newly hired employees
- Staff recruiting costs
- Hotel charges, meals, and transportation for the opening team
- Security, property taxes, insurance, and utilities costs incurred after construction is completed
- Depreciation of assets placed into service, such as computers and other communication devices
- Consulting costs related to feasibility studies, accounting, legal, tax, and governmental affairs
- Nonrecurring operating losses

Not Considered Preopening Expenses

- Property advertising costs
- Coupon giveaways
- Costs of furniture, fixtures and equipme
- Costs to obtain licenses
- Security, property taxes, insurance, and costs related to construction activities

Source: AICPA SOP 98-5 and FASB ASC 720-15-55

Following generally accepted accounting principles, preopening costs are recognized as an expense when incurred. For purposes of the USALI, these amounts are recorded in the department that incurred the expense. For example, the training cost and compensation of personnel in the rooms department would be included in room's department expense. Start-up consulting costs, unless directly related to a specific department operation, would be recognized when incurred in administrative and general under professional fees.

Even though the accounting treatment seems clear, it is understandable that we continue to receive questions on preopening expenses. One reason for this is that, because preopening costs are not specifically mentioned in the USALI, it is difficult to find explicit guidance. Perhaps future editions should provide more clarity by specifically mentioning the accounting procedures for these expenses. Another source of confusion is that during the preopening period these expenses may be incurred by both the owner and the future operator. As a result, questions may surface regarding which party is tracking the cost and who is ultimately responsible for these costs. Finally, uncertainty over the accounting for these expenses may result because these costs often have a different treatment for tax reporting. In the United States the tax treatment for start-up costs, which includes preopening expenses such as salaries and wages for employees who are being trained and their instructors and fees for other professionals, is covered in Section 195 of the Internal Revenue Code. In many instances, for the purposes of tax accounting, the majority of these costs must be capitalized and amortized to expense over a 180 month period. [3] Therefore, it is very possible to have a temporary difference in preopening expense recognition between USALI and tax.

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To purchase a copy of the 11 th edition of the USALI, and access the nearly 100 questions and answers on the FAQ, or submit your own question for the FMC, please visitwww.ahlei.org/usali .

[1] Page vii, *Uniform System of Accounts for the Lodging Industry* , Ninth Revised Edition (1996), Educational Institute of the AH&MA, East Lansing, MI.

[2] *Reporting on the Costs of Start-Up Activities* , Statement of Position 98-5, AICPA, 1998. The Statement of Position was superseded by FASB Accounting Standards Codification (ASC) 720-15. International accounting standards treat start-up costs similarly (IAS 38.69).

[3] For more details on what constitutes a start-up for tax purposes and tax treatment of start-up costs in the United States please refer to Section 195 of the Internal Revenue Code, Treasury Regulations, and IRS Publication 535. Currently, a small amount of these expenses can be expense immediately, and a taxpayer can elect not to amortize these costs.