

Radu-Daniel LOGHIN
Academia de Studii Economice, București, Romania

FINANCIAL REPORTING IN THE TOURISM INDUSTRY

Empirical
study

Keywords

*Tourism,
Financial reporting,
Relevance,
Equity markets*

JEL Classification

L83, M41, M42

Abstract

In recent years the tourism industry has seen a rise in scope and influences both in the political and economic arenas. The industry has become exposed to risks such as money laundering and fraudulent reporting, demanding the use of International Financial Reporting Standards (IFRS) to reduce differences in financial reporting and increase the attractiveness of the sector for investors. For the purpose of this paper, a sample of 611 equities in the tourism and hospitality business was used in order to understand the state of financial reporting in the sector with an emphasis on the relevance of financial information and other issues such as timeliness and the adherence to a true and fair presentation. The research reveals the enhanced relevance obtained from the use of the IFRS as well as risks for the financial management of the companies.

Introduction

With the continuing technological progress going on in the transport industry, tourism is no longer a service for the privileged elite. As a result, more and more people are using the service and the industry is growing at a steady pace.

Tourism is no longer a business of small inns and gambling dens on the roadside, where a few merchants and adventurers gather, but a thriving multibillion industry which caters to a diverse audience.

The origins of the modern tourism industry is hard to pinpoint exactly, particularly because of the multitude of stakeholders and providers involved with the services offered to the tourists. While monasteries have been providing some sort of tourist service for the benefit of pilgrims for millennia, we could say that the 19th century has seen the development of the modern tourism infrastructure. The development of the railway had made pristine wilderness accessible to commoners, integrating industrial development with tourist attractions. Some of this integration could be seen in some American states (Little, 2009). Socialist systems have seen the rise of further co-integration between the tourism industry and its environment (Grandits, 2010).

With the rise of the international stock markets, tourist resorts are starting to consider listing on the stock exchanges as a means of securing finances. The globalization of the tourism industry has thus paved the way for specialized accounting services. While accounting can provide assistance for the users of financial statements, the tourism industry can provide a challenge for auditors and management alike. The multitude of recreational activities and services provided to tourists can provide an opportunity for unacceptable business practices and risks.

The concern for the protection of investors from these types of practices has seen the rise of a diverse body of scientific literature in the field of accounting and finance, especially in the field of management accounting (Adams, 2006) but thus far a comprehensive analysis of the accounting information provided by companies in the sector has not been achieved.

Our study tries to identify the dynamics for the behaviour of investors and management within the context financial reporting in the tourism industry for the latest financial period; in order to identify the strengths and weaknesses of a SME investor in the hospitality and tourism industry. For the first issue, we approach the problem employing the model developed by Feltham and Ohlson (1995). For the second issue, we use Pearson correlation coefficients and corresponding P-values to test the association between the variables.

1. Tourism from an accounting perspective

While both the tourism industry and accounting are ancient developments, the scientific literature dealing with both concepts seems to be a modern development.

Our first step in identifying the specific body of scientific literature is to address the scope of the tourism industry. While restaurants provide a tourist attraction and cater to travellers, for the purpose of this paper the tourism industry has been limited to three major GICS Sectors: Casinos & Gaming, Hotels, Resorts & Cruise Lines and Leisure Facilities.

After narrowing the field, the scientific literature begins to reveal a genuine interest in cross-disciplinary research covering accounting and the tourism industry.

For the hotel industry, which provides complex tourist services, Karagiorgos et al (2006) consider that accounting provides a „priceless support“. Further research from the Russian Federation reveals that accounting systems can provide a barrier to foreign investment (Annaraud, 2007), thus reducing the presence of foreign hospitality providers. One of the innovations developed in the context of the hotel industry due to the competitive nature of the sector is „strategic management accounting“ (Collier & Gregory, 1995).

In the „Casino and Gaming“ Sector, the most important scientific work would have to be Greenlees' textbook (Greenlees, 2008). One of the major assets of the book would be the introduction of the workflow chart to assist accountants in filling the record books. Further technical papers have been written in the field of casino loyalty programs (Gaynor, 2014) as well as the internal control systems deployed by casinos (DeFranco & Worhnan, 1997).

While no empirical paper has provided an insight into the relevance of financial accounting information presented in the context of the tourism and hospitality industry, papers have been written about the significance of management accounting in the tourism industry (Briciu & Scorte, 2012).

Thus we can state that the scientific literature which bridges the gap between accounting and the tourism industry does not cover in an appropriate manner the needs of the financial statement users.

The first issue facing accounting professionals working in the tourism industry is the threat of money laundering investigations launched by the authorities. Many popular tourist destinations are vulnerable to money laundering (Croes & Schmidt, 2007), and thus to special audit sessions.

Other issues which we might consider create a hazardous professional environment are tax evasion and fraudulent reporting through creative accounting practices with the purpose of misleading investors.

2. Overview of the tourism industry equities

The tourism sector is not a prominent feature of the global equity markets. Worldwide, there are around 848 primary equities (retrieved at 10.06.2016 from the Thomson Reuters database) which cover the tourism GICS sectors (i.e. Casinos & Gaming, Hotels, Resorts & Cruise Lines and Leisure Facilities).

However, many of those fillers of financial data either are inactive (no financial reporting filled for the financial period ending in 2016 and 2015) or have small reporting cycles (<52 weeks).

Thus, the industry narrows to 611 unique equities, which also provide full financial disclosure (i.e. audited financial statements). This sample consists of 376 equities from „Hotels, Resorts and Cruise Lines”; 149 equities from „Casino and Gaming” and 86 from „Leisure facilities”. The sample origins are diverse, coming from about 73 accounting jurisdictions (countries and autonomous subdivisions/ overseas territories).

About half the sample uses International Financial Reporting Standards for their financial statements (50%), followed by US GAAP (12%) and other national standards (38%). The diversity of reporting practices can lead to information asymmetry for international investors (Annaraud, 2007), even though there are standardization efforts being made through the use of uniform accounts. The Herfindahl–Hirschman Index reveals a large concentration of the sample (0.28) based on the reporting standards employed by the financial management, meaning that to a large extent the tourism sector has converted to a single set of financial statements.

From an auditing viewpoint the opinions expressed on the reliability of the financial statements are for the most part unqualified (89.52% unqualified opinions).

Lastly, the distribution of the financial period end dates and reporting dates, as seen in Figure 1, reveals that the optimum period for ending the financial period in the the tourism industry is still December, while the optimum reporting period ranges from February to April. The results are easily explained by the fact that the inventory period has to coincide with the period that is least likely to require a significant use of resources and the period between Christmas and the New Year would require the least amount of resources businesswise.

Prior to the New Year celebrations there is a lull in business for three days between Christmas and the New Year when there are few reservations being made because of the increased prices during the New Year celebrations. This could explain the reason for selecting this period. Also, bias towards Northern equity markets such as LSE and NYSE might also further shift the financial period end date for December.

3. Methodology, sample and results

The current paper deals with both issues affecting the financial management in the tourism industry who are responsible for the financial statements of their entities and the users of the said financial information.

In the first case we deal with one issue across the entire sample, respectively the size of the companies, the prevalence of qualified audit opinions and the lag between the financial period end date and the reporting date.

In practice the size of the company can be inferred from the natural logarithm of the total assets of that company. Since the current sample is large and the size varies across markets with different purchasing power and currencies, a dichotomous variable referring to the above average size of the company was selected as the item for analysis. This was obtained from comparing the natural logarithm of the total assets for a company against the average size of the sample. The values were 1 for companies above the average size of the sample and 0 otherwise.

The second variable which was considered for analysis in the first part of the study is the above average lag between the financial period end date and the reporting date. This variable was also deemed to fit the profile of a dichotomous variable with 1 for the companies with a larger lag than the average and 0 for other cases.

Lastly the prevalence of the qualified audit opinions was analysed by deploying a dichotomous variable where 1 signals a qualified audit opinion and 0 other opinions.

The association between the three variables was tested by a Pearson correlation matrix generated in Matlab 2011b, using the `corrcoef()` function. The two statistically-significant associations were found between the size of the company and the lag between the financial period end date and the reporting date (Pearson coefficient: -0.15 with a p-value of <1%) and between size and the prevalence of qualified audit opinions (Pearson coefficient: -0.10 with a p-value of <1%). The negative associations, while still preliminary, might reflect the need for more attention to the operations of small and medium tourism operations as well as the need to simplify the accounting standards to facilitate the financial reporting of smaller enterprises so that they may benefit from the faster review of their financial operations by shareholders and major stakeholders.

After considering the issues facing the preparers of the financial statements in the tourism business, we develop a simple model for assessing the relevance of financial information in the tourism business, based on the theoretical boundaries drawn by Feltham & Ohlson (1995).

There are many value relevance studies conducted through the world but these studies have rarely

been performed on an international sample and none thus far from the ISI Web of Knowledge (as of 10.06.2016) have been performed in the context of the tourism sector.

While done for the purpose of detecting the relevance of a specific financial indicator such as goodwill, these studies are mostly concerned with individual stock exchanges or groups of stock exchanges. Among the relevant studies in the field would have to be Damash et al (2009), Craig et al (2010), Beisland & Hamberg (2014). However for the purpose of this study we selected the „barebones model” since an understanding of the industry would require interviews and other qualitative techniques to extract the relevant specific financial information solicited by investors.

The code used to extract the variables from the Thomson Reuters database were TR.NetIncomeAfterTaxes, TR.TotalEquity, TR.TtlCmnSharesOut and TR.CompanyMarketCap. The period in question was the last fiscal year, with Euro as the selected reporting currency. Three variables were selected to represent the basic Ohlson model: KB (TR.CompanyMarketCap/ TR.TtlCmnSharesOut), KP (TR.TotalEquity/ TR.TtlCmnSharesOut) and PR (TR.NetIncomeAfterTaxes/ TR.TtlCmnSharesOut)

Of the 611 equities, nine had no trading activity during the time of the publishing of their financial statements according to the Thomson Reuters database and thus could not be included in the final sample. The structure of the subsample subtracted from the second model included 2 US equities, 1 Australian equity, 1 Jamaican equity, 1 Swedish equity, 1 Vietnamese equity, 1 Spanish equity and 1 Thai equity.

A further twenty-three equities were subtracted from the sample due to size issues (had a market cap larger than 100 euro/share or a market cap smaller than nine times the minimum market cap) due to the large influence on the regression model.

In order to test the influence of the International Accounting Standards on the relevance of the financial information presented in the reports coming from the tourism sector two models were constructed (one for the entire sample or 579 equities and one for the subsample of entities which report using the IFRS framework or 289 equities). The reason for such a choice was a significant association (Pearson p-value <0.1) between the above average size of the company and the preference for International Financial Reporting Standards (IFRS).

The two samples were tested in Matlab 2011b using the `regstats` () function for a linear model with intercept.

For the first model we can observe that there is no autocorrelation between the residuals (Durbin-Watson test is close to 2) and that the Fisher test

also validates the model (~0.01%). Also, the variables included have corresponding p-values. We can observe that financial users are more focused on the latest financial performance of the company than its financial position, since the coefficients for PR are greater than those for KP.

As with the first model, the second model lacks autocorrelation between the residuals (Durbin-Watson test is close to 2) and likewise the Fisher test also validates the model (~0.01%). As with the first model the second model possesses a significant adjusted R-squared. However, the coefficient is significantly higher, meaning the financial information is more relevant for the users than in the case of the first sample. In no model was there a Simpson's effect detected.

The data provided in Table 1 reveals that the financial information is relevant to users of financial information who operate in the tourism sector. However, based upon the statistics we can say that the information provided by respondents who reported based upon the IFRS framework convinced the users to rely more on the financial information disclosed in their annual reports.

Entities below average size are more likely to fill financial statements using the IFRS framework (Pearson negative association of -0.07 with a p-value of 0.057), meaning that more relevant financial information can increase the market capitalization of those entities and thus ensure their growth in the very competitive tourism business.

Conclusions

Unless a shift takes place globally in which the financial users shift towards the IFRS framework, it is likely that undercapitalized fillers of financial information are going to benefit from adopting the IFRS framework, and thus deploy their accounting system as a competitive advantage.

However, adoption of the IFRS framework would likely lead to qualified audit opinions and delays in the financial reporting cycle which would only reduce the chances of an increase in the equity's market capitalization and value.

The limits of the study refer to the sampling technique used as well as the sampling period for the variables. Future models should focus on a single equity market and deploy robust regressions to limit the leverage of significant observations.

Also, qualitative data should be deployed for the benefit of quantitative models which would appropriately identify specific financial indicators relevant for the industry at large. Lastly future research could better identify the entities which are dedicated to the tourism industry, as the restaurants were excluded from the sample because of issues regarding the economic role of such establishments in the industry at large.

Reference list

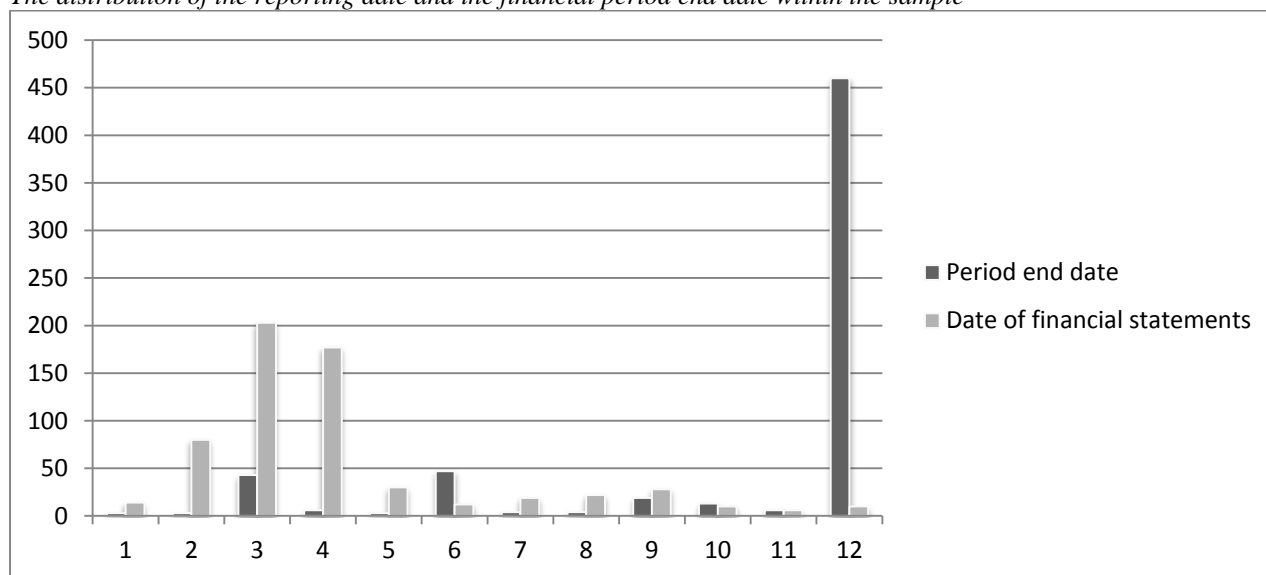
- [1] Adams, D. (2006). *Management Accounting for the Hospitality, Tourism and Leisure Industries: A Strategic Approach*. London: Thomson Learning.
- [2] Annaraud, K. (2007). Accounting in Russia: Challenges for the Hospitality Stakeholders. *Journal of Hospitality Financial Management*, 1-20.
- [3] Briciu, S., & Scorte, C. (2012). The Relevance Of Management Accounting For The Hospitality Industry. *The Annals of the University of Oradea Economic Sciences*, 886-893.
- [4] Collier, P., & Gregory, A. (1995). Strategic management accounting : a UK hotel sector case study. *International Journal of Contemporary Hospitality Management*, 16-21 .
- [5] Craig, R., Rodrigues, L., & Oliveira, L. (2010). Intangible assets and value relevance: Evidence from the Portuguese stock exchange. *The British Accounting Review*, 241-252.
- [6] Croes, R., & Schmidt, P. (2007). Promoting Tourism As U.S. Foreign Aid: Building On The Promise Of The Caribbean Basin Initiative . Retrieved on 05 25, 2016, from *Journal of Multidisciplinary Research*: <http://www.scientificjournals.org/journals2007/articles/1071.htm>
- [7] Dahmash, F., Durand, R., & Watson, J. (2009). The value relevance and reliability of reported goodwill and identifiable intangible assets. *The British Accounting Review*, 41(2), 120-137.
- [8] DeFranco, A., & Worhnan, J. (1997). Internal Control Practices in Casino Gaming. *Journal of Hospitality Financial Management*, 33-48.
- [9] Feltham, G., & Ohlson, J. (1995). Valuation and clean surplus accounting for operating and financial activities. *Contemporary Accounting Research*, 689-731.
- [10] Gaynor, G. (2014). Accounting Techniques for Loyalty Programs and Promotional Allowances in the Gaming Industry. Retrieved 06 10, 2016, from <https://www.questia.com/read/1G1-370031051/accounting-techniques-for-loyalty-programs-and-promotional>
- [11] Grandits, H. (2010). *Yugoslavia's Sunny Side: A History of Tourism in Socialism (1950-1980)*. Budapest: Central European University Press.
- [12] Greenlees, E. (2008). *Casino Accounting and Financial Management*. Reno & Las Vegas: University of Nevada Press.
- [13] Hamberg, M., & Beisland, L.-A. (2014). Changes in the value relevance of goodwill accounting following the adoption of IFRS 3. *Journal of International Accounting, Auditing and Taxation*, 59-73.
- [14] Karagiorgos, T., Drogalas, G., Christodoulou, P., & Pazarskis, M. (2006). The crucial importance of accounting in tourism business. *Management of International Business & Economic Systems (mibes) Conference Proceedings* (pg. 1-8). Larissa: Dpt. of Business Administration of the TEI of Larissa.
- [15] Little, J. (2009). Scenic tourism on the northeastern borderland: Lake Memphremagog's steamboat excursions and resort hotels, 1850–1900. *Journal of Historical Geography*, 716-742.

Appendices

Appendix A

Figure No.1

The distribution of the reporting date and the financial period end date within the sample



Source (own research based on the Thomson Reuters database)

Appendix B

Table No.1

The metrics relating to the relevance of the financial information in the two samples

Statistics	F-test	Adjusted R ²	Durbin-Watson Test	Intercept	KP (t-stat/p/coeff)	PR (t-stat/p/coeff)
Sample 1	0.01%	18.9%	2.0172	4.53	(10.45/0.01/0.376)	(2.27/0.01/1.207)
Sample 2	0.01%	40.4%	2.0098	3.32	(13.26/0.01/0.412)	(7.69/0.01/2.755)

Source (own research based on the Thomson Reuters database)