



## 2022 AICPA & CIMA CFO CONFERENCE

# SUCCESSFUL IMPLEMENTATION OF THE NEW FASB LEASE ACCOUNTING STANDARD... "LAST LAPS"

— April 2022 —

PRESENTED BY:



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# Interactive Polling Session

## CFO2207: Successful Implementation of the New FASB Lease Accounting Standards . . . the "Last Laps"



7. Successful Implementation of  
the New FASB Lease Accounting  
Standards . . . the "Last Laps"

Wed, 4/27, 3:55 PM - 4:45 PM PT  
50 minutes

Concurrent Session Onsite and Online

Add session

To ask a question or participate in polling, [click here](#).

This session will focus on the remaining timetable  
to implement Topic 842...the FASB's New Lease  
Accounting standards.

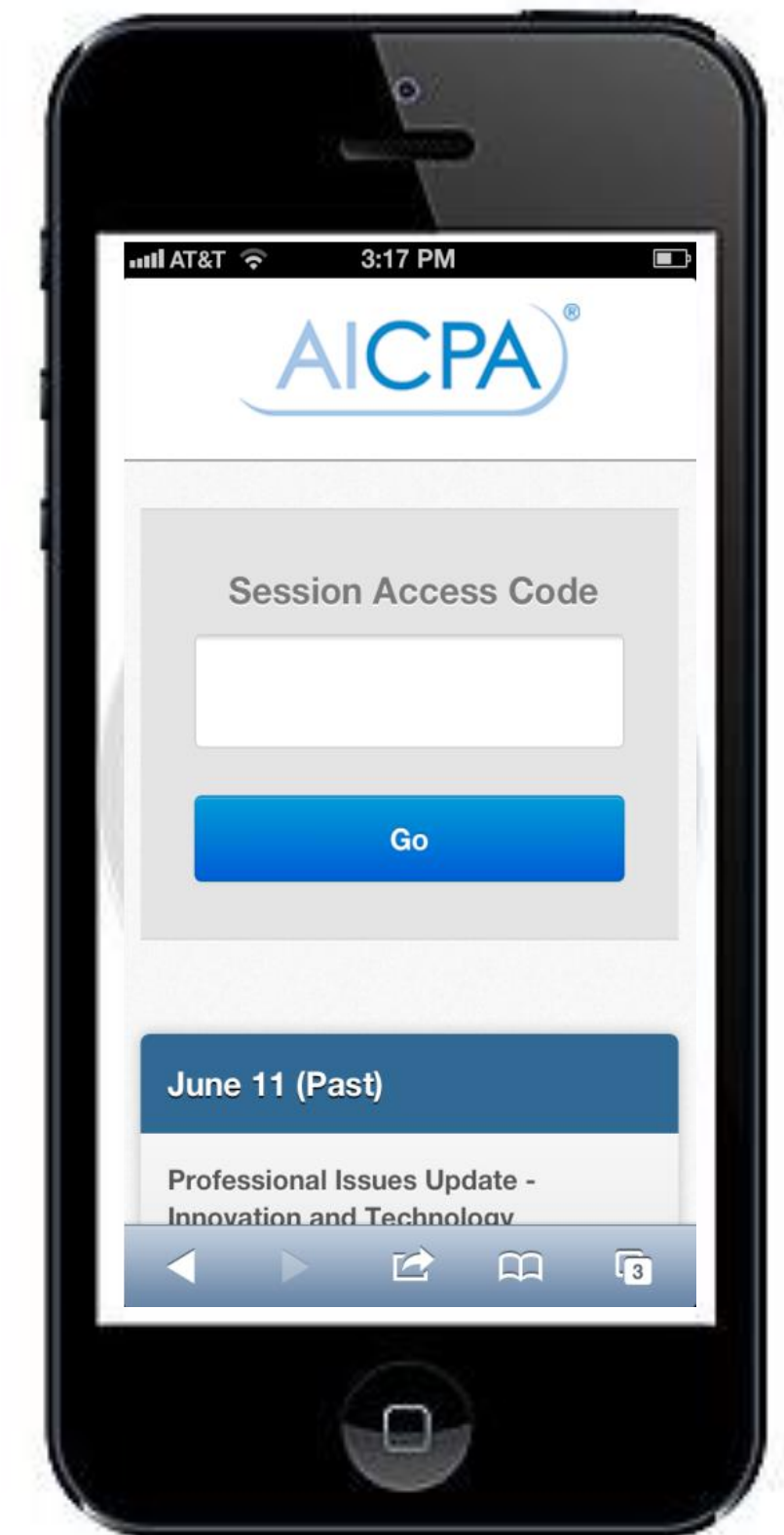
As a co-author of six publications in the Journal of  
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# INTRODUCTIONS



**Stephen G. Austin, CPA, MBA**

*Firm Managing Partner*  
Swenson Advisors, LLP



Steve is a Certified Public Accountant in the states of California and Georgia. Steve manages audit, SEC, Sarbanes-Oxley, and business consulting engagements with a focus on technology, manufacturing, service, real estate, social media, and non-profit organizations. He is the author of the book *Rise of the New Ethics Class*. Steve is a national thought leader on adopting the new lease accounting standards and speaks worldwide on lease accounting, governance, Sarbanes-Oxley, and IFRS matters. Among his many articles published by the AICPA are six articles on lease accounting. Prior to joining Swenson Advisors, Steve held Partner positions with McGladrey & Pullen, LLP and Price Waterhouse, LLP. Steve earned a BS in Accounting and Finance from Bob Jones University and an MBA from the University of Georgia, Terry College of Business. Steve serves on numerous community boards and audit committees — including Santa Fe Christian School, Summit Ministries, and Integra International®.



# ACCOUNTLEASE™ BY THE NUMBERS



**\$25 BILLION**

Estimated present value  
of the lease liabilities



**110,000**

Number of leases accounted  
for by AccountLease™ team



**150**

Number of articles in Journal of  
Accounting, webinars, presentations  
since 2016 on Topic 842



**15,000**

Number of hours spent by  
AccountLease™ professionals



**27**

Number of 842 trained  
professionals at AccountLease™

\*As of March 2022.



# JOURNAL OF ACCOUNTANCY ARTICLES

## Lease Accounting: Private Companies On the Clock After Delay

**September 9, 2021** *Joel C. Colbourn, CPA, MBA; Stephen G. Austin, CPA, MBA; and Jim LoPresti, MBA*

## Pandemic Alters Lease Accounting Landscape

**April 16, 2020** *Stephen G. Austin, CPA, MBA; Joel C. Colbourn, CPA, MBA; Ane Ohm, CPA; and Don Mitchell*

## Lease Accounting Standard Requires New Auditor Judgments

**March 1, 2020** *Stephen G. Austin, CPA, MBA; Joel C. Colbourn, CPA, MBA;*

*Phillip Doolittle; and Doug Renner*

## Hidden in Plain Sight: Accounting for Embedded Leases

**September 19, 2019** *Stephen G. Austin, CPA, MBA; Joel C. Colbourn, CPA, MBA;*

*and Kristen Gibbons*

## Lease Accounting: A Private Company Perspective

**July 1, 2019** *Stephen G. Austin, CPA, MBA; Michael G. Fraunces, J.D.;*

*and Alisia Scudder, CPA*

## Practical Considerations for Lease Accounting

**November 21, 2017** *Stephen Austin, CPA, MBA*





# TOPIC 842

## FASB issued a new standard Topic 842, Leases February 25, 2016

### Effective

- » For public companies, fiscal years beginning after **December 15, 2018**.

### With COVID-19 delays, effective

- » For private not-for-profit (NFP) entities that have issued or are conduit bond obligors for securities that are traded, listed or quoted on an exchange or an over-the-counter market and which have not yet issued financial statements, fiscal years beginning after **December 15, 2019**.
- » For private companies and private NFP entities, fiscal years starting after **December 15, 2021**.

### EARLY ADOPTION IS PERMITTED







# POLLING QUESTION #1

In what year was the first lease accounting standard, **FASB Statement No. 13**, issued?

a. 1974

b. 1976

c. 1980

d. 1984



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**Poll: In what year was the first lease accounting standard, FASB Statement No. 13, issued?**



# HIGH-LEVEL OVERVIEW OF TOPIC 842



- » All leases will now be reflected on the balance sheet.
- » The new lease accounting standard is principles-based rather than rules-based, and is applicable to both lessees and lessors.
- » Still two lease classifications – operating leases and finance (previously capital) leases – and the classification criteria has been updated.
- » Leases are recorded as of the implementation date at the present value of future rent payments/collections.
  - Lessees record right-of-use (ROU) asset and lease liability.
  - Lessors record lease receivable and deferred revenue.
- » Determining applicable discount rate may take some analysis.
- » Embedded leases may present challenges.
- » With the recording of the current portion of the lease liability, working capital decreases affecting financial ratios which may impact covenants for bank and other credit-related arrangements.



# LEASE DEFINITION AND TYPES OF LEASES

## WHAT IS A LEASE?

A **LEASE** is a contract that conveys the “right to use” an underlying asset for a period of time in exchange for consideration.

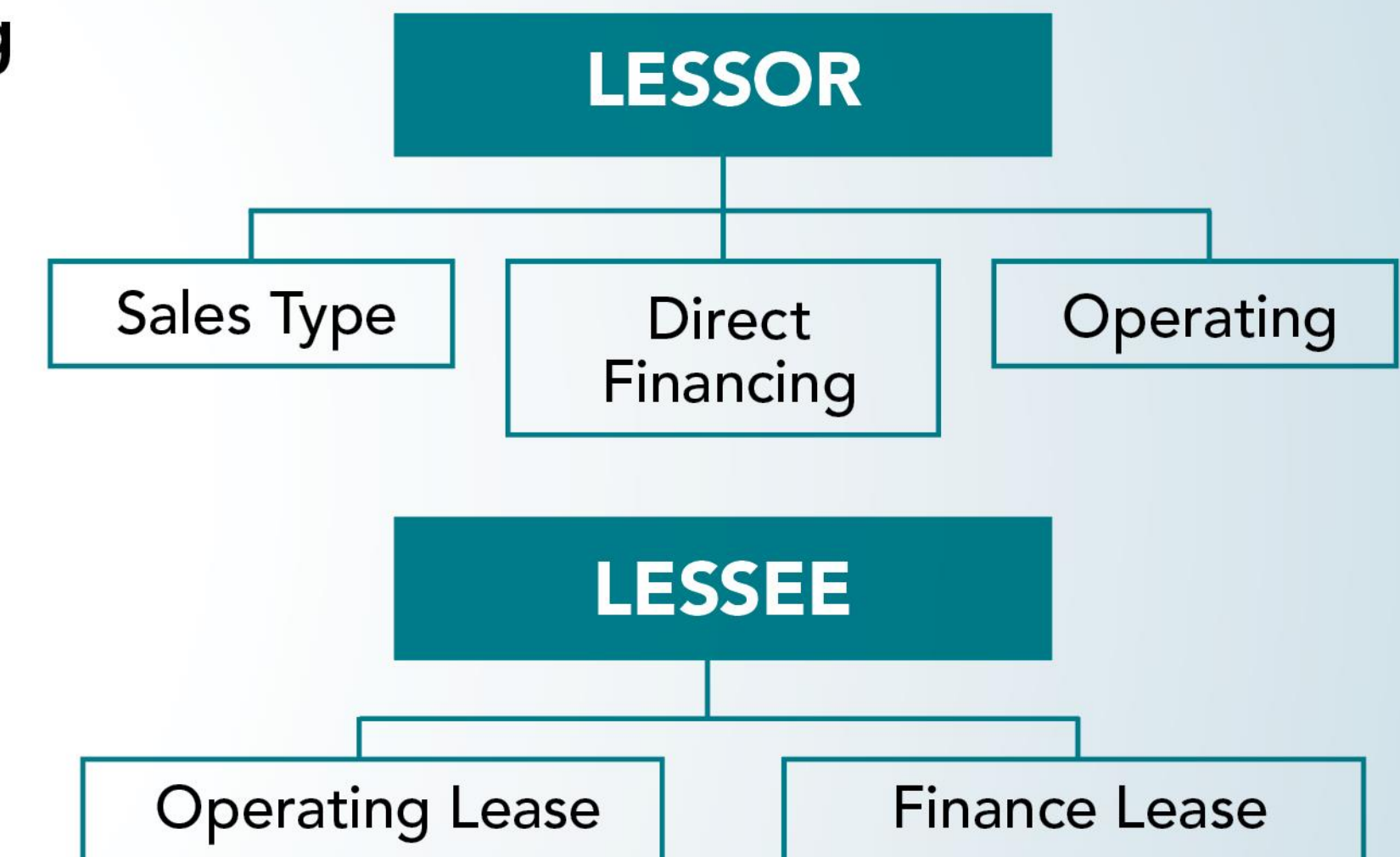
## A CONTRACT IS (OR CONTAINS) A LEASE IF:

- » The use of an identified asset is explicitly or implicitly specified **(842-10-15-3)**.
- » The customer controls the use of the identified asset for a period of time **(842-10-15-4)**.

**CONTROL** means that the customer has the right to:

- » Direct the use of the identified assets and
- » Obtain substantially all of the economic benefits during the lease term from directing the use of the identified asset.

## TYPES OF LEASES



### Scope Exception:

Lessees may make an accounting policy election to use the current accounting model for operating leases with an initial lease term of **12 months or less**.



# LEASE CLASSIFICATION



## FINANCE LEASE

When **ANY** of the following criteria are met at lease commencement **(842-10-25-2)**:

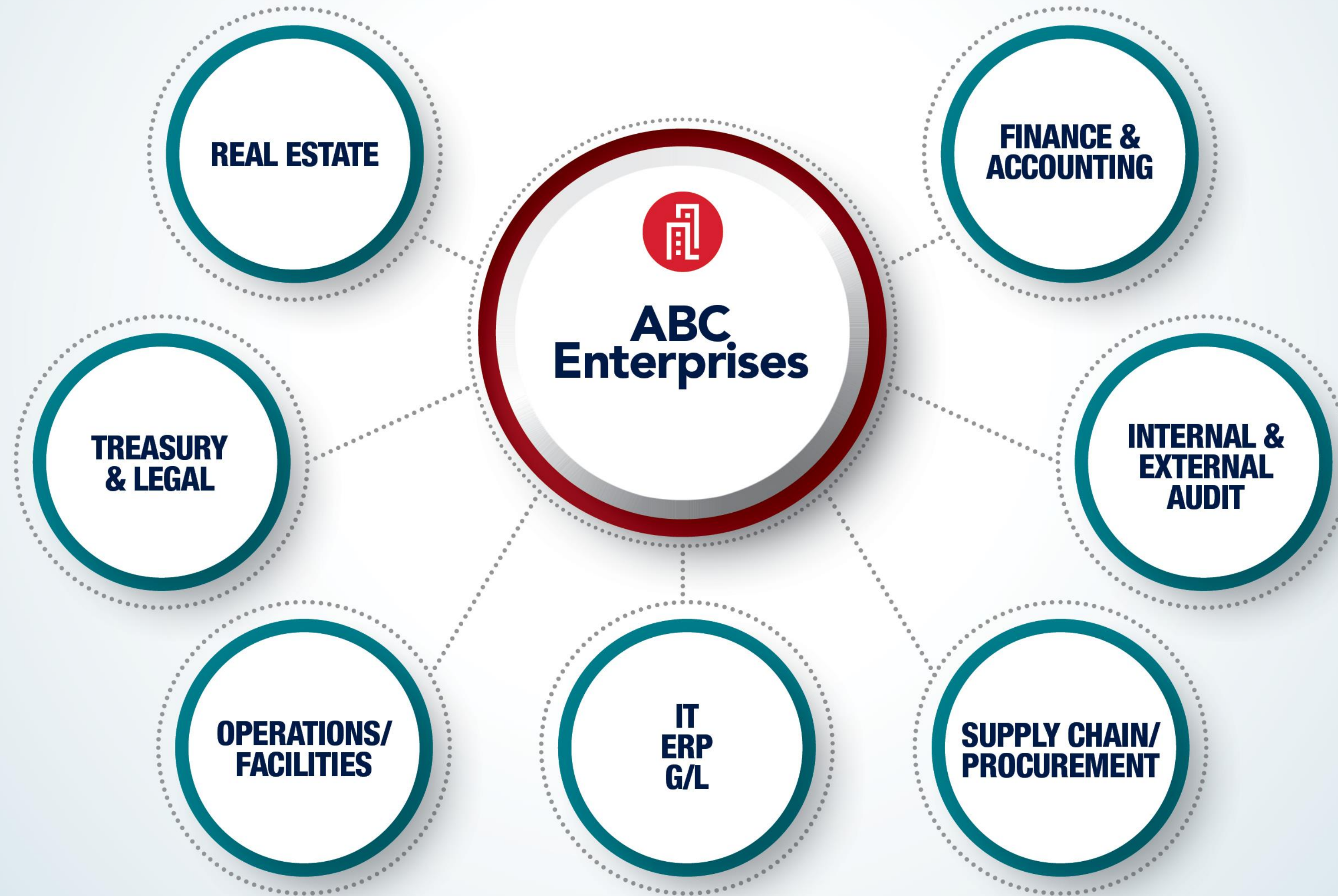
- » The lease transfers ownership of the underlying asset,
- » The lessee is reasonably certain to exercise an option to purchase the asset,
- » The lease term is for the major part of the remaining economic life of the asset,
- » The present value of the sum of the lease payments equals or exceeds substantially all of the fair value of the underlying asset,
- » **NEW** – The underlying asset is of such a specialized nature that it is expected to have no alternative use to the lessor at the end of the lease term.

## OPERATING LEASE

When **ANY** lease does not meet the criteria above.



# LEASE ACCOUNTING STAKEHOLDERS







## POLLING QUESTION #2

How many **ASC 842 criteria** are there to determine if a lease is classified as a **finance lease**?

a. 3

b. 4

c. 5

d. 10



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**Poll: How many ASC 842 criteria are there to determine if a lease is classified as a finance lease?**



# ASC 842: KEY DECISIONS AND IMPLEMENTATION ISSUES



- » Assess current status of lease accounting practices (ASC 840)
  - Current accounting practices
    - » Identifying lease arrangements
    - » Accounting for leases (capital and operating)
    - » Reviewing/authorizing/approving changes to leases
    - » Reviewing/authorizing/recording lease payments
    - » Updates for lease changes – maturity, extension, termination
    - » Physical inventory of leased assets
    - » Financial statement reporting and disclosures





- Profile of leases portfolio

- » Lease classification – capital (now finance) vs. operating

- » Types of leases

- Real estate leases
- IT leases
- Embedded leases
- Equipment leases
- Fleet leases

- Accounting policy elections:

- » Transition methods

- Apply prospectively – as of the beginning of the period of adoption, or
- Apply retrospectively – as the earliest period presented in the financial statements with cumulative effect recognized in equity

- » Reassessment practical expedient “package of 3” (existence of lease, lease classification, initial direct costs)

- » Exclude short-term leases (12 months or less)

- » Do not use hindsight





- » Election to not separate non-lease components (and treat as one combined lease component)
  - ROU asset and lease liability amounts determined using both lease and non-lease components
  - Need to separate between fixed and variable payments
  - Election can be made by asset type
  
- » Determining lease term for accounting purposes
  - Generally stated lease term
  - May reflect exercise of renewal/extension option(s) if “reasonably certain”
  - May reflect exercise of early termination option if “reasonably certain” after consideration of penalties
  - Lease term may be redetermined
  - “Reasonably certain” considered high threshold
  - “Reasonably certain” corresponds to “reasonably assured” under ASC 840





- » **Determining discount rate:**
  - **Rate implicit in the lease**
    - » Specific definition
    - » Should be used when known or determinable
    - » Rate known only by lessor (based on definition)
  - **Incremental borrowing rate**
    - » Used if rate implicit in the lease is not available
    - » Rate reflects secured borrowing for the same term
    - » Should be determined by identified process updated regularly
  - **Risk-free rate**
    - » Can be elected if not a Public Business Entity
    - » Can be applied by asset type
    - » Based on published rates for U.S. Treasury securities



# ASC 842 IMPLEMENTATION PROGRAM



The Implementation Program presented includes five phases which are summarized below. While the timing of some of the steps in each phase may overlap, the phases provide a framework for making decisions that are most appropriate in the circumstances.

## PHASE 1 - PREPARATION

- » The focus is to identify the resources needed, implementation team stakeholders and get the needed training.

## PHASE 2 - READINESS ASSESSMENT

- » The focus is to gather/centralize lease accounting documentation and information, establish the completeness of the lease documentation and information, and determine the reasonableness of previous lease accounting.





## PHASE 3 - PRELIMINARY PORTFOLIO REVIEW AND IMPLEMENTATION PLAN DEVELOPMENT

- » The focus is to review the possible portfolio of leases based on the information gathered, determine the appropriate lease accounting policy elections and draft documentation, select the provider of the lease accounting software solution, and develop the implementation plan.

## PHASE 4 - IMPLEMENTATION PLAN EXECUTION

- » The focus is to review the documentation to determine contracts that are or contain a lease, abstract lease information and input into lease accounting software solution, quality control review of abstract and input data, record accounting entries and perform reconciliations, and roll forward lease information to the end of the reporting period.

## PHASE 5 - COMPLETION

- » The focus is to reconcile activity through the end of the reporting period, complete financial statement disclosures, and complete documentation.





## POLLING QUESTION #3

Was there such a thing as an **embedded lease** under **ASC 840**?

a. Yes

b. No

c. Maybe

d. Don't Know



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**Poll: Was there such a thing as an embedded lease under ASC 840?**



# OBSERVATIONS FROM THE TRENCHES



- » Identifying all leases and gathering documentation needed for lease accounting should be an early objective, often involves Stakeholders across the organization, may include identification of persons authorized to execute certain types of agreement and actions taken, may involve documents that no longer exist requiring judgement, and will take longer than expected – arrangements may become known after implementation  
*(Journal of Accountancy article, July 1, 2019)*
- » Finding all the embedded leases generally requires some strategizing and focused effort with Stakeholder participation *(Journal of Accountancy article, September 19, 2019)*
- » Appropriate accounting policy elections can be important in reducing the complexity of the lease accounting process *(Journal of Accountancy article, September 9, 2021)*





- » Most organizations apply ASC 842 prospectively from the implementation date rather than restating prior periods, elect the “package of three” practical expedients, and have made the accounting policy election to not separate lease and nonlease components, and treat both as a single lease component, for at least one asset class
- » Calculating payments for lease accounting purposes involves determining what costs are lease components, what costs are nonlease components, and what costs are lease non-components, and may include determining how costs will be allocated – note that lease accounting is performed for lease components only unless an accounting policy election is made by asset class to not separate
- » Tenant allowances is an area of focus since how they are structured in the agreement affects accounting treatment; reimbursement of improvement costs that benefit the landlord may be treated as pass-through of funds while reimbursement allowances without accountability may represent an adjustment to required payments





- » Determining previous accounting under ASC 840 has been performed correctly is important since many of the existing balances as of the implementation date are carried forward (capital lease asset and liability, deferred rent, prepaid rent), correctly calculating deferred rent for arrangements with scheduled rent increases is a common error, and since ASC 842 does not “grandfather” accounting errors, calculating the aggregate amount of accounting errors should be performed to determine whether a prior period adjustment is needed
- » Materiality is often an area of focus, and many establish guidance consistent with asset capitalization policy; however, some adopt an approach to determine an aggregate payments criteria as to what is meaningful to asset/liability measurement – this is an area where auditor feedback can be useful ([Journal of Accountancy article, March 1, 2020](#))
- » Determining the Incremental Borrowing Rate (IBR) can be more difficult than anticipated as it may involve obtaining credit profile-specific indicative secured borrowing rates from financial institutions across various maturity dates ([Journal of Accountancy article, March 1, 2020](#))





- » Spreadsheets alone may not work; perform an analysis to understand your needs before selecting a lease accounting system to ensure your requirements will be met in a cost-effective manner; some systems (LeaseCrunch and others) are easier to implement and maintain  
*(Journal of Accountancy article, September 9, 2021)*
- » Only about half of public companies that have implemented ASC 842 have integrated their lease accounting system with their ERP system  
*(EY/LeaseAccelerator 2022 Global Lease Accounting Survey)*
- » Documentation is needed both to memorialize implementation decisions and accounting policy elections and to provide continuing guidance to that established processes and controls will continue ensuring the completeness of the lease accounting and recording/reconciliation activities





- » Following implementation there must be specific efforts to verify the established procedures are in place for timely Stakeholder communication to the Finance Staff of all changes affecting leasing arrangements including additions, terminations, and modifications
- » While training Finance Staff and Stakeholders about ASC 842 and their future roles is a key part of the implementation process, continuing that training will need to be an area of focus due to changes in personnel and duties





## POLLING QUESTION #4

What is the **total number of pages** for the **ASC 842 Lease Accounting Guides** for the Big 4?

a. 1,724 pages

b. 2,445 pages

c. 2,996 pages

d. 7,842 pages



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**Poll: What is the total number of pages for the ASC 842 Lease Accounting Guides for the Big 4?**



# TOP 10 LESSONS LEARNED TO HELP EXPEDITE THE IMPLEMENTATION PROCESS



1. Identifying all the leases and finding needed documentation can be a challenge
2. Ensure executive support and designate a lease accounting champion who will lead the project and become the subject matter expert
3. Approach lease accounting implementation like any other project with adequate allocated resources, reasonable timeline, regular progress monitoring and status meetings, and open communication with your auditors – **start early as it will take longer than you think**
4. Lease accounting process will require participation of “Stakeholders” outside the Finance Staff; ensure “Stakeholders” receive adequate training as to lease accounting requirements as they may play an important role in identifying arrangements that could include embedded leases
5. Lease accounting software solution will be needed – spreadsheets alone will not suffice



# TOP 10 LESSONS LEARNED TO HELP EXPEDITE THE IMPLEMENTATION PROCESS CONT.



- 6. Appropriate lease accounting policy elections are critical in ensuring costs are properly identified and correctly reflected in the lease accounting system**
- 7. Ensure adequate training for persons abstracting critical information from lease documentation consistent with the accounting policy elections, and ensure appropriate QC of the information entered into the lease accounting system**
- 8. Establish adequate processes and controls for the recording of entries from the lease accounting system including reconciliation of actual lease payments with scheduled payments from the lease accounting system**
- 9. Successful post-implementation compliance depends on establishment of adequate processes and controls to communicate/monitor new leases and changes to existing leases**
- 10. Auditor focus will be on reasonable application of the standard, appropriate determination of lease terms and discount rates, and completeness of the lease portfolio including changes and updates ([Journal of Accountancy article, March 1, 2020](#))**



# CLOSING THOUGHTS/QUESTIONS



- » **Making appropriate accounting policy elections can result in an easier implementation.**
- » **Assessing your needs should be done BEFORE selecting a lease accounting system.**
- » **Implementing ASC 842 will be a learn, analyze, and refine process until it ultimately becomes just another recurring accounting activity.**





# CONTACT INFORMATION



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