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ASC 842 Leases: Is Your Software Up to the Challenge?

PRESENTED BY

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Quick Recap

- **Issued:** February 2016
- **Effective Date:** Annual reporting periods beginning after December 15, 2021
- **Summary:** Under the new guidance, lessees are required to recognize a right-of-use asset and a lease liability for all leases. The new guidance classifies leases as either financing or operating, with classification affecting the pattern of expense recognition.

Practical Expedients

- The "package" of practical expedients: An entity can elect not to reassess lease classification, embedded leases and initial direct costs.
 - › All or nothing
 - › Does not waive completeness
- Short term lease exemption.
- Non-lease components can be combined with the associated lease component in certain situations.
- Land easements can continue to be recorded in a manner consistent with prior accounting.
- Prior periods do not need to be restated under the new guidance when following the modified retrospective adoption approach.
- Non-public companies only:
 - Ability to use the risk-free rate, rather than the incremental borrowing rate, to determine the lease liability (and the corresponding right of use asset) to be recorded on the balance sheet.
- While some of these may appear to ease the burden related to implementation and the resulting audit implications, it is important to consider the current and future impacts of these practical expedients.

Resources

- [Lease Landing Page](#)

- › Full description of services, which include, but are not limited to:
 - Implementation of lease accounting standard
 - Incremental borrowing rate (IBR) analysis
 - Training and education
 - Lease tool selection and implementation
- › Technical guidance
 - 2021 Summer CPE webinar replay
 - Implementation and transition resources
 - Technical resources
 - Industry specific resources
- › [Lease Accounting Guide for Private Companies](#)

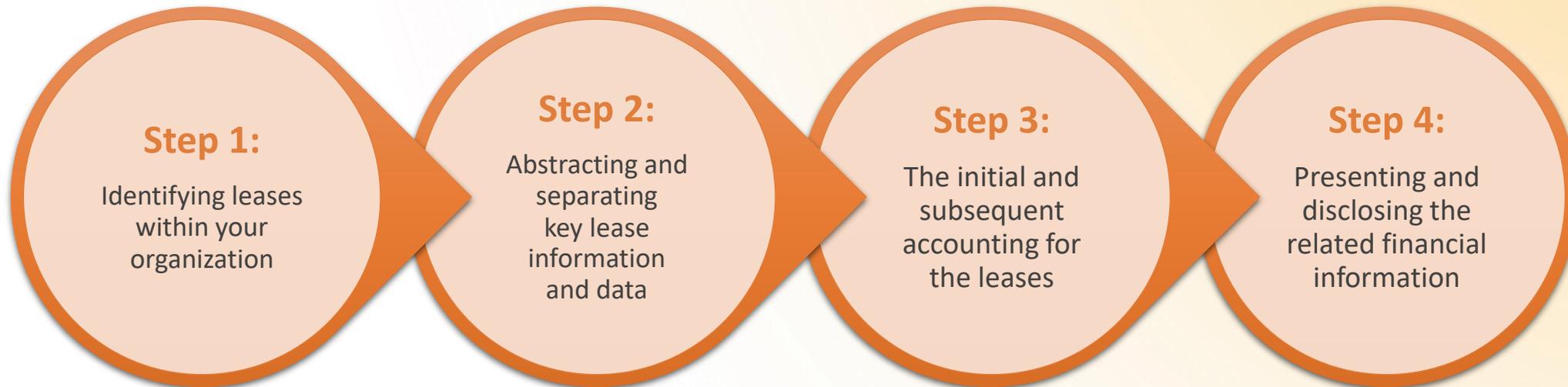
Polling Question #1

How do you currently track and maintain your leases?

- A. No tracking
- B. Excel
- C. Some other method
- D. Third party software

Transition

- To adequately prepare for the transition to ASC 842, there are numerous steps a company must go through, including, among others:



Polling Question #2

What is your best estimate of where you are in the transition process?

- A. Identifying leases within your organization
- B. Abstracting and separating key lease information and data
- C. The initial and subsequent accounting for the leases
- D. Presenting and disclosing the related financial information
- E. Prefer not to say

How Software Can Help

Step #3: The initial and subsequent accounting for the leases

Step #4: Presenting and disclosing the related financial information



Difficulties of Manually Tracking in Excel

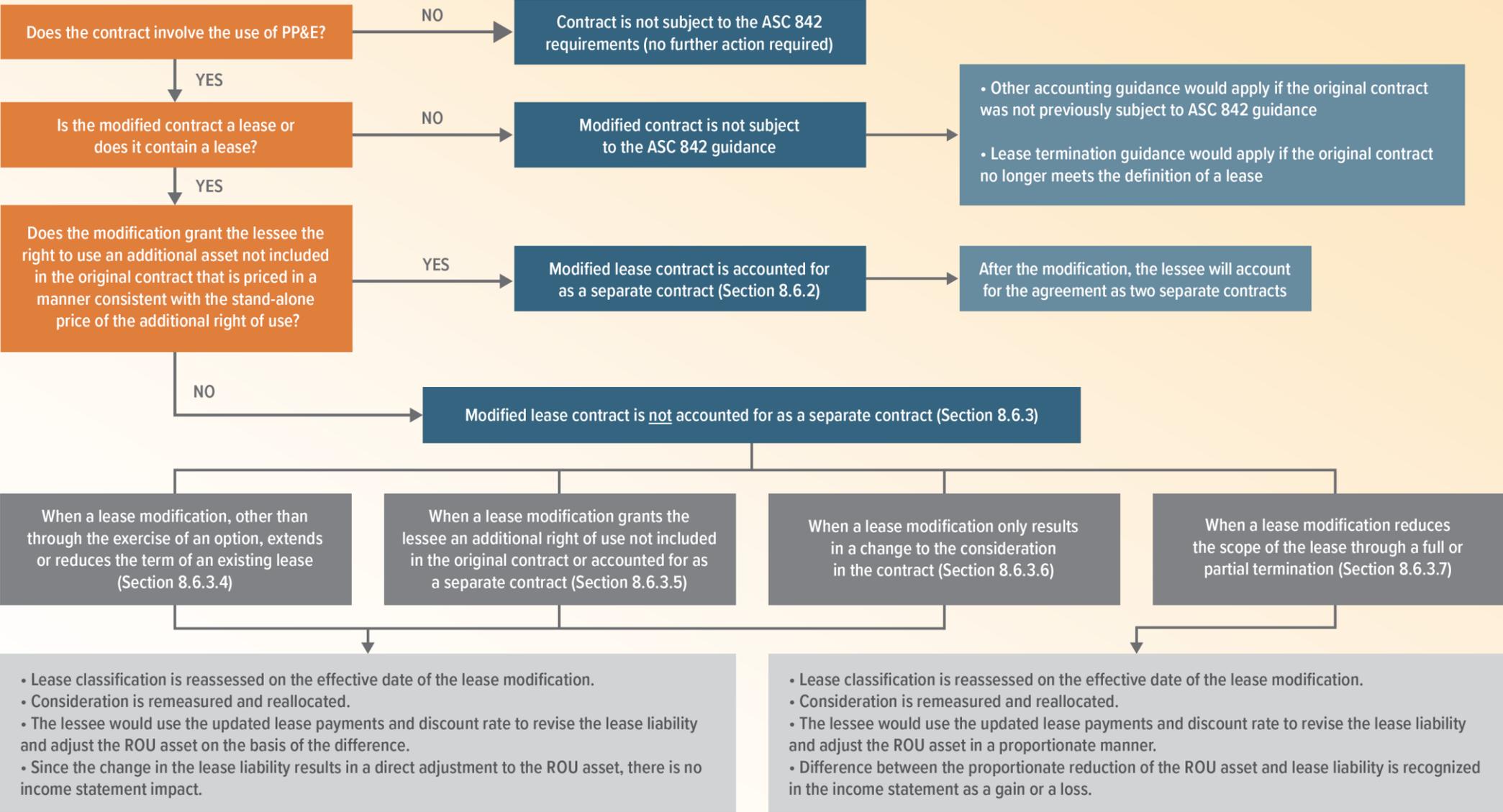
Step #3: The initial and subsequent accounting for the leases

- Lease calculations are complex.
- Summarizing data to post journal entries can be difficult.
- Manual calculations are time consuming and can lead to errors.
- Lease modification calculations are complex.

Step #4: Presenting and disclosing the related financial information

Gathering data for disclosures can be time consuming. Currently 35 questions in the disclosure checklist for non-public companies.

Decision Tree on Accounting for Modifications



Source: Deloitte’s “A Roadmap to Applying the New Lease Standard”

Polling Question #3

What do you feel like the biggest challenge to implementing is?

- A. Time/bandwidth
- B. Interpretation of the standard
- C. Completeness of records
- D. Access to software solution

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Are You Ready for the New Lease Accounting Standard?

Joe Pink, LeaseCrunch

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What is the Best ASC 842 Software?

- When in the market for ASC 842 lease accounting software, it's important to look for a solution that hits several main areas of focus:
 - › **Efficiency:** Manual calculations take time, especially with more intricate lease accounting standards. Software can crunch numbers and save you money and time.
 - › **Ease of use:** Software should simplify implementing the new standard, not make it more confusing. Look for a platform that has a user-friendly interface for ease of use and integration.
 - › **Customization and control:** Look for a software solution that scales to your organization and is modifiable based on the features you want.
 - › **Security:** Choosing a technology that is secure is just as important as choosing one that is fast and accurate.
 - › **Expertise:** Select software created by a team of accounting experts, not just software engineers.

Polling Question #4

**How many leases
do you have/do you
think you have?**

- A. 0
- B. 1-9
- C. 10-49
- D. 50 or greater

ASC 842 Implementation Checklist

- Implementing the new lease standard is not just a one-time exercise; it requires changes to accounting processes and financial reporting controls.
- Accounting policy elections and practical expedients will affect the overall process and timeline, so be sure to assess them early.
- Effective implementations require a thorough evaluation of resources, and your organization should identify someone to take the lead for all of this work.

The checklist on the following slides will help you get started and walk you through key steps in the implementation process.

☐ Identify the Entire Lease Portfolio and Gather Lease Documents

- ☐ Consider all locations
 - ☐ Review recurring expenses to look for lease payments
 - ☐ Review GL expense accounts with key words that could indicate a lease, *e.g., rent, lease, subscription, contractor*
 - ☐ Leases may include office space rental, vehicles, photocopiers, equipment and embedded lease (*equipment or other assets included in a service contract*)
- ☐ **Be certain to exclude the following contracts that do not fall under the new lease standard:**
 - ☐ Leases of 12 months or less, if this is an elected policy
 - ☐ Intangible assets like SaaS software, although IFRS 16 has some scope limitations
 - ☐ Exploration of non-generative resources, e.g., minerals
 - ☐ Biological assets, e.g., crops
 - ☐ Inventory is excluded by ASC 842 but included under IFRS 16
 - ☐ Assets under construction are excluded by ASC 842 but included under IFRS 16
 - ☐ Low-dollar leases, if this is an elected policy under IFRS 16

□ Review Lease Data in All Lease Contracts

- Key dates: commencement, termination
 - Lease term, early termination and renewal provisions
 - Asset details: type, description and location
 - Payment terms, termination penalties, bargain purchase options, renewal term payments, residual value guarantees
 - Lease incentives and initial direct costs
 - Useful life of the asset to determine amortization period, e.g., right-of-use (ROU) asset life
 - Other important data to track, such as taxable vs. nontaxable leases
- **Variable lease payments tied to sales or an index receive special treatment:**
 - Variable payments tied to sales are expensed
 - If payments are tied to an index, organizations following ASC 842 use the index at lease start date or initial application date (whichever is later) to calculate the lease payments. Changes in the index are expensed. Organizations following IFRS 16 will modify their lease liability with every change in the index.
 - Useful life of the asset to determine amortization period, e.g., right-of-use (ROU) asset life
 - Other important data to track, such as taxable vs. nontaxable leases

Evaluate Existing Lease Business Processes

- Who is responsible? Are current resources sufficient?
- Are areas other than Accounting involved (Procurement, Legal, Treasury)?
- Is lease processing and record retention centralized or decentralized?

Assess Current Systems and Use of Technology for Lease Processing

- Are spreadsheets and manual tracking used?
- Is separate lease accounting software (not part of ERP, G/L) in place?
- Does the accounting software include all of the required general ledger accounts?
 - *ROU assets*
 - *Short-term lease liabilities*
 - *Long-term lease liabilities*
 - *Operating lease expense*
 - *Variable lease expense*
 - *Short-term lease expense, and*
 - *Finance lease expenses, such as amortization expense and interest expense*
- Is there a lease module in the ERP, and does it have future capabilities?

❑ Review New Accounting and Disclosure Requirements, including Judgment Areas

- ❑ Accounting policy elections and practical expedients, including lease vs. non-lease components, short-term leases, leasehold improvements and lease accounting during the transition period
- ❑ Accounting for leases created after implementation using the new standard
- ❑ Process for determining classification criteria, including the fair market value and economic life of the lease asset
- ❑ Determine how ROU Assets and Lease Liabilities will be disclosed on the financial statements — separately in a footnote, or within the balance sheet and income statement itself. For new disclosures, consider data location and whether it is reliable and auditable.
- ❑ How will discount rates be determined and applied by Accounting? ASC 842 provides a policy election to use a risk-free rate.

Discuss the New Standard With:

- The board or owners
- The audit committee
- Investors
- Lenders

Please join us at our next session:

STOP: Tax Law Changes Ahead

Are you ready?

Wednesday, August 17, 2022

Register at cohencpa.com

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