

## Lease accounting changes are coming. **Are you ready?**



After nearly a decade of planning and debate, in February 2016 the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) issued an Accounting Standards Update (ASU) that will change how leases are recognized on the balance sheet.

### What's Changing?

The new standards are designed to shed light on financial commitments that were previously not recognized. According to the FASB, "Organizations that lease assets, referred to as 'lessees', will now be required to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases." Specifically for lessee accounting, organizations will be required to make a liability entry for the lease obligation and an asset entry to recognize the right to use that underlying asset. The new standards will affect all tangible assets, but with regard to the real estate market, these changes will primarily impact corporate real estate lessees.

#### DOMESTIC LEASE CLASSIFICATION

While current GAAP principles only require the recognition of finance leases on the balance sheet, the new FASB standards will now require that both finance and operating leases be reported. Essentially, changes will be required regardless of whether leases are classified as finance or operating leases.

#### INTERNATIONAL LEASE CLASSIFICATION

For those with international portfolios, the IASB has also issued similar changes in the form of IFRS 16. Similar to the new FASB lease accounting standards, the lease obligation and right-to-use the leased asset will need to be reported on the balance sheet; however, the IASB does not make a distinction between a finance and operating lease. The IFRS lessee accounting model will require that all leases are treated in a manner consistent with the FASB approach to finance leases. To read more about these and other differences between the new FASB regulations and IFRS, visit [www.ifrs.org](http://www.ifrs.org).

#### TRANSITION PERIOD RESTATEMENT TRANSACTIONS & REPORTING

During the transition period, "lessees and lessors will be required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach," as stated in the FASB Accounting Standards Update for Leases (Topic 842). Restated financials will be required for comparative periods, and for many companies, this will require tracking current leases with a term starting prior to the comparative periods.

#### RE-MEASUREMENT & RE-ASSESSMENT SCENARIOS

Companies will need to reassess asset management performance, recognize asset value and liability, and review the language used in contracts to evaluate if they will be affected. Additionally, companies should understand the rate used in Net Present Value (NPV) calculations for both current and future leases and determine the impact across all areas of the portfolio. The complexities of the new leasing standards will drive organizations to transition from a spreadsheet-based approach to a purpose-built system.

## When do these changes take affect?

According to FASB.org, the new standards will generally take effect in December 2019 for public companies and 2020 for private companies. However, for certain types of businesses, the changes will take effect in December 2018. To determine the effective dates for your organization, read the full details outlined in the FASB Accounting Standards Update for Leases (Topic 842) on the FASB.org website.

## How MRI can help

The recent FASB and IASB lease accounting updates highlight the importance of utilizing flexible software that can adapt to support proposed changes. By integrating financials with CRE management tools, organizations are empowered to streamline compliance processes and analyze the impact of these changes. Companies that leverage business intelligence and analytics software tools will be well positioned to model new scenarios quickly and make informed decisions that impact the future of the business.

MRI Software is collaborating with industry experts and accounting professionals to ensure that our software enables our clients to adopt these new standards.

## Lease Accounting Checklist

A few guidelines to help prepare for the changes:

- ☑ How are your leases currently classified? Understand the difference between a finance and operating lease and apply lease classification tests.
- ☑ Track operating leases and identify all multi-year contracts.
- ☑ Understand the assets that are included in your lease, if any.
- ☑ Understand your current and future lease terms and how they will be affected by the new standards.
- ☑ Implement a consistent process to track expenses and record data associated with your leases.
- ☑ Evaluate how the new standards will affect your company's approach to leasing situations.

