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## ACCOUNTING

# 5 Steps to Compliance with New Lease Accounting Standards

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**Kristin Jones** • Sep. 28, 2018



The compliance countdown is on for ASC 842. The new lease accounting standard published by the Financial Accounting Standards Board in 2016 will require companies to report most operating leases on their balance sheets starting in 2019. According to some estimates, trillions of dollars in leased assets will soon appear on corporate balance sheets due to this new guidance. This is not surprising given that lease arrangements offer businesses a cost-effective strategy to access costly expenditures such as equipment, vehicles, or distribution centers at a fraction of the cost of purchasing. Businesses across all industries, especially asset heavy industries like retail, restaurants, manufacturing and construction, are scrambling to meet these new financial reporting mandates.

According to a recent [Bloomberg Tax survey](#) of 500 professionals who are responsible for tracking, accounting, or expensing leased assets for their organizations, over 80% have leases that need to be accounted for under ASC 842, most of which are material to financial reporting.

At its core, ASC 842 seeks to improve transparency, comparability, and financial reporting, but achieving compliance puts heavy demands on companies. Tax and accounting teams responsible for tracking, accounting, or expensing leased assets for

their organizations will now have new tasks and workflows to carry out to ensure their company is ASC 842 compliant. Consequently, having a solid plan and effective tools is not only crucial to complying, but also to avoiding risks of material misstatements, material weakness, or in the case of a CPA, potential malpractice lawsuits. Conversely, accurate compliance with ASC 842 offers the opportunity to provide more value by streamlining processes, empowering better decision-making, and realizing cost savings. Leveraging best practices already implemented by leading companies, here is a five-step process to tackling ASC 842's time-consuming calculation and reporting requirements.

### **Step 1: Build a Cross-Functional Team**

ASC 842 touches the entire organization. Therefore, the ASC 842 team should reflect the many functions that are impacted, such as accounting, IT, legal, procurement, treasury, and possibly others.

### **Step 2: Collect and Organize Contracts**

Remember to collect all contracts, including master lease agreements and addendums. Again, technology will be a critical role in keeping these key documents in one place saving precious time and ultimately money. Some studies suggest that employees spend 50% of their time searching for documents manually or sifting through spreadsheets, taking an average of 18 minutes to locate each document. Best practices indicate that choosing a leased asset software product that includes document management results in time savings, improves financial controls, and streamlines accounting and audit efforts downstream.

### **Step 3: Determine Whether the Contract is or Contains a Lease**

Each contract will need to be analyzed to determine whether the contract contains/includes a lease for ASC 842 purposes. Companies should be on the lookout for embedded leases. Contracts that include the outsourcing of services, as well as arrangements involving data centers, hosting and other IT arrangements are common examples of embedded leases.

Another key step in transitioning from the old ASC 840 rules to the new ASC 842 rules is to see if the lease can be grandfathered in as part of the practical expedients election that prevents companies from having to reassess old contracts. They can simply say it wasn't a lease before and based on prior conclusions it's not a lease now. While this sounds simple at first glance, there are certain guidelines

surrounding the application of the package of three practical expedient that must be considered.

From a systems perspective, be sure to select a leased asset system that allows you to separate out and properly classify each embedded lease as an operating or finance lease.

#### **Step 4: Capture Lease Data**

Leases contain many data elements that are required for ASC 842 calculation purposes. For example, dates are key to properly accounting for a lease, such as when the lease begins, ends, optional termination dates, and option to purchase date, just to name a few. Be sure to look for a leased asset system that includes a bulk import option in addition to an intuitive manual data entry user interface. As mentioned in step 2, integrated document management that allows you to apply data tags by lease type, entity, is also useful for organizing, searching and sorting leases and source documents by lease/entity.

#### **Step 5: Automate with Software**

New GAAP rules, like new tax rules, break existing processes. In the case of ASC 842, companies in many cases have no prior process and are starting from scratch. This is a great time to review and automate workflows. Advanced leased asset systems provide you with web services (API's) and rules engines to export, transform, and load data. Look for a software vendor who has experience automating workflows to/from ERP systems to subledgers such as for fixed or leased assets. The right software can make a dramatic difference in productivity. For example, a Fortune 100 transportation company was able to use automation software to transform a 100-step manual process to 12 steps, freeing up staff to perform higher-value tasks.

#### **Examine Processes and Systems to Ensure Compliance**

At first blush, tackling the time-consuming calculation and reporting requirements needed to successfully achieve ASC 842 compliance can seem daunting and nearly impossible. However, with the right processes, systems, and expertise in place, the road to ASC 842 compliance can be made much easier and well worth the effort.

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