



FASB's new lease standard: Accounting and implementation insights

2017 Engineering and Construction Conference

Agenda

Module/Topic

Identifying a lease

Key ingredients of the leases model

Overview of the core accounting models

Other provisions, effective date, and transition

Tax implications

Areas of potential challenge

Components of implementation effort

Implementation tools

Q&A

Understanding the journey

-
- 2005** SEC targets off-balance-sheet financing
 - 2006** FASB and IASB initiate joint project on leases
 - 2009** FASB and IASB issue Leases: Preliminary Views (March)
 - 2010** FASB and IASB issue the first lease standard exposure draft (August)
 - 2013** FASB and IASB issue the second lease standard exposure draft (May)
 - 2016** IASB issues its final standard IFRS 16, Leases (January 13)
FASB issues its final standard ASU 2016-02, Leases (February 25)

*After more than 10 years in the making...
Let's discuss how to navigate the new leasing standard*

Overview

The “Big Picture”

Key takeaways from this presentation

Most leases on balance sheet for lessees

→ *Classification will drive expense profile*

Lessor model largely unchanged

→ *Most changes result from alignment with ASC 606*

→ *Separate lease & non-lease components and disclosures*

FASB tried to make things easy

→ *Classification, reassessment, transition*

Effective 2019 (2020 nonpublic), but don't wait to assess impact

→ *Process and systems changes may be required*

→ *Potential impact on debt covenants*

Understanding the implications

Individuals throughout an entire organization will need to understand the new lease accounting rules under ASC 842 because it represents a wholesale change when compared to the current guidance



Lease characterization for tax purposes has not changed as a result of the new standard. However, since ASC 842 results in the recognition of more assets and liabilities, entities may be required to record new or adjust existing DTAs and DTLs



Identification of the lease population, data abstraction, and developing a platform for ongoing reporting are all key steps in implementing the new standard



Identifying a lease

Introducing the new standard¹

What's in and what's out?

Scope

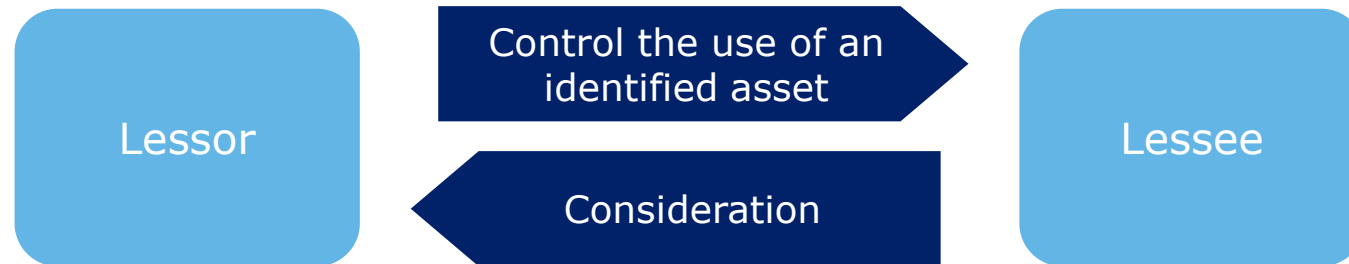
- Applies to leases of property, plant, and equipment
 - Does **not** apply to:
 - Leases of intangible assets
 - Leases to explore for or use nonregenerative resources
 - Leases of biological assets
 - Leases of inventory
 - Leases of assets under construction
-

¹ Refers to Accounting Standards Codification Topic 842, *Leases* (ASC 842, the new leases standard)

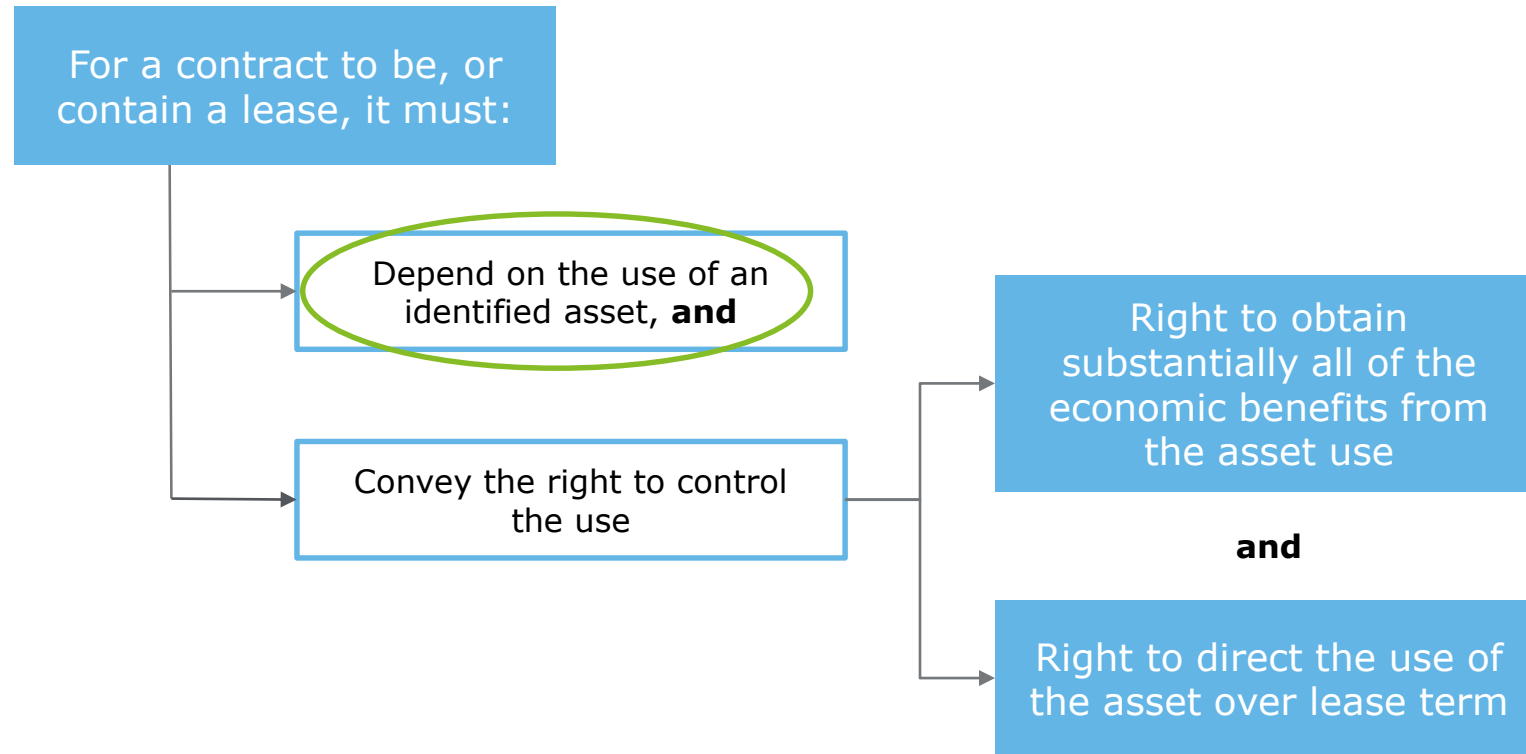
Definition of a lease

What does the new definition look like under ASC 842?

A lease is a contract, or part of a contract, that conveys the right to control the use of identified property, plant, or equipment for a period of time in exchange for consideration



Definition of a lease (cont.)



Identified asset

Understanding the criteria under ASC 842

Contract must depend on use of identified asset

- Asset must be explicitly or implicitly identified
- Physically distinct portion of a larger asset may be an identified asset
- Capacity portion of a larger asset is generally not an identified asset

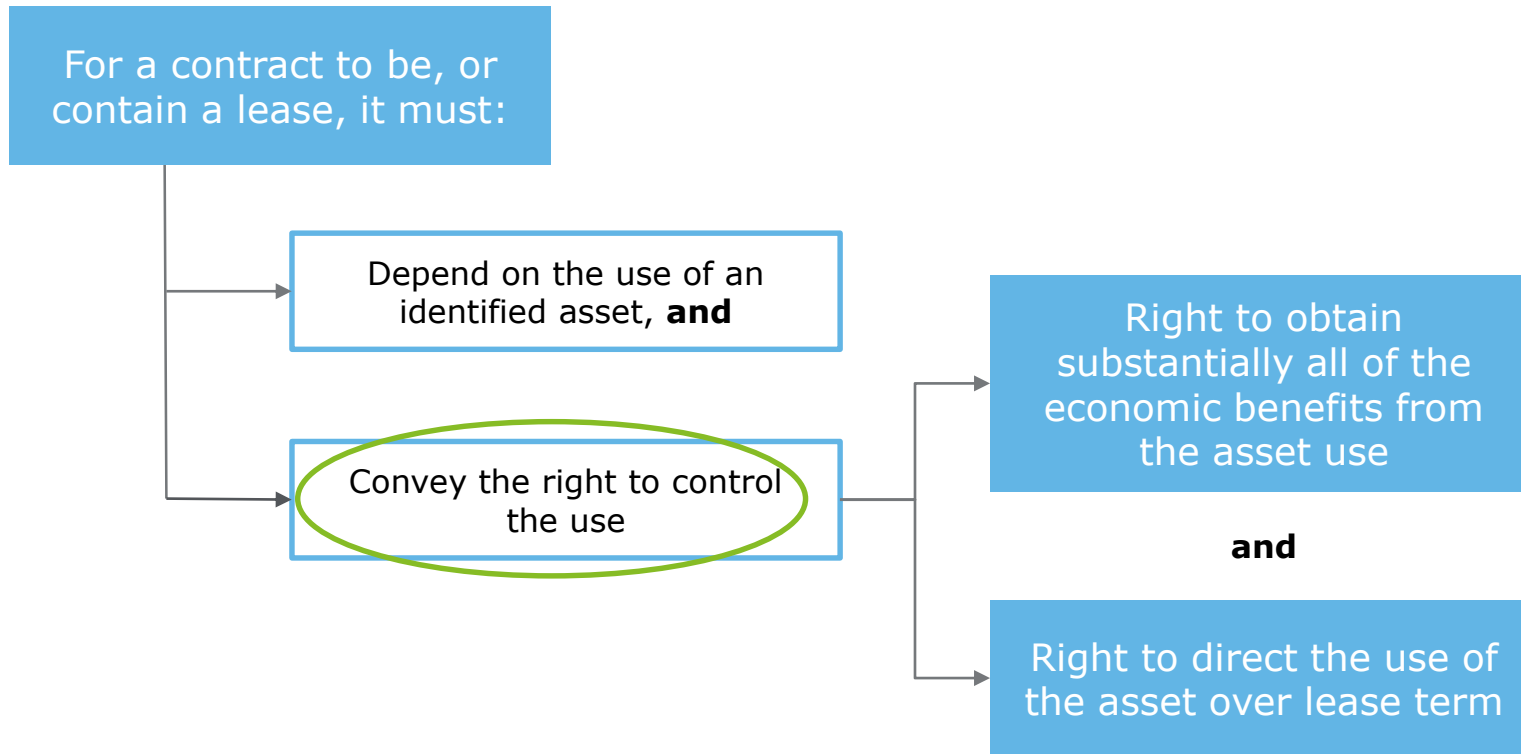
Right of substitution

- Would result in the asset not being deemed a specified asset
- Substitution would be considered substantive if:
 - Lessor has the practical ability to substitute the asset
 - Lessor would benefit from exercising its right of substitution

Warranty or upgrade considerations

- Supplier's right or obligation to substitute an alternative asset due to operational failure does not mean the asset is not an identified asset
- Supplier's right or obligation to upgrade the asset similarly does not mean the asset is not an identified asset

Definition of a lease (cont.)



Right to control the use

Obtain substantially all of the economic benefits from use

Right to obtain substantially all of the economic benefits from use



Can obtain economic benefits from the use of an asset directly or indirectly in many ways



Economic benefits from the use of an asset include its primary output and by-products, including potential cash flows derived from these items

Benefits related to the ownership of an asset should not be included in the assessment of whether an arrangement contains a lease

Right to control the use (cont.)

Right to direct the use

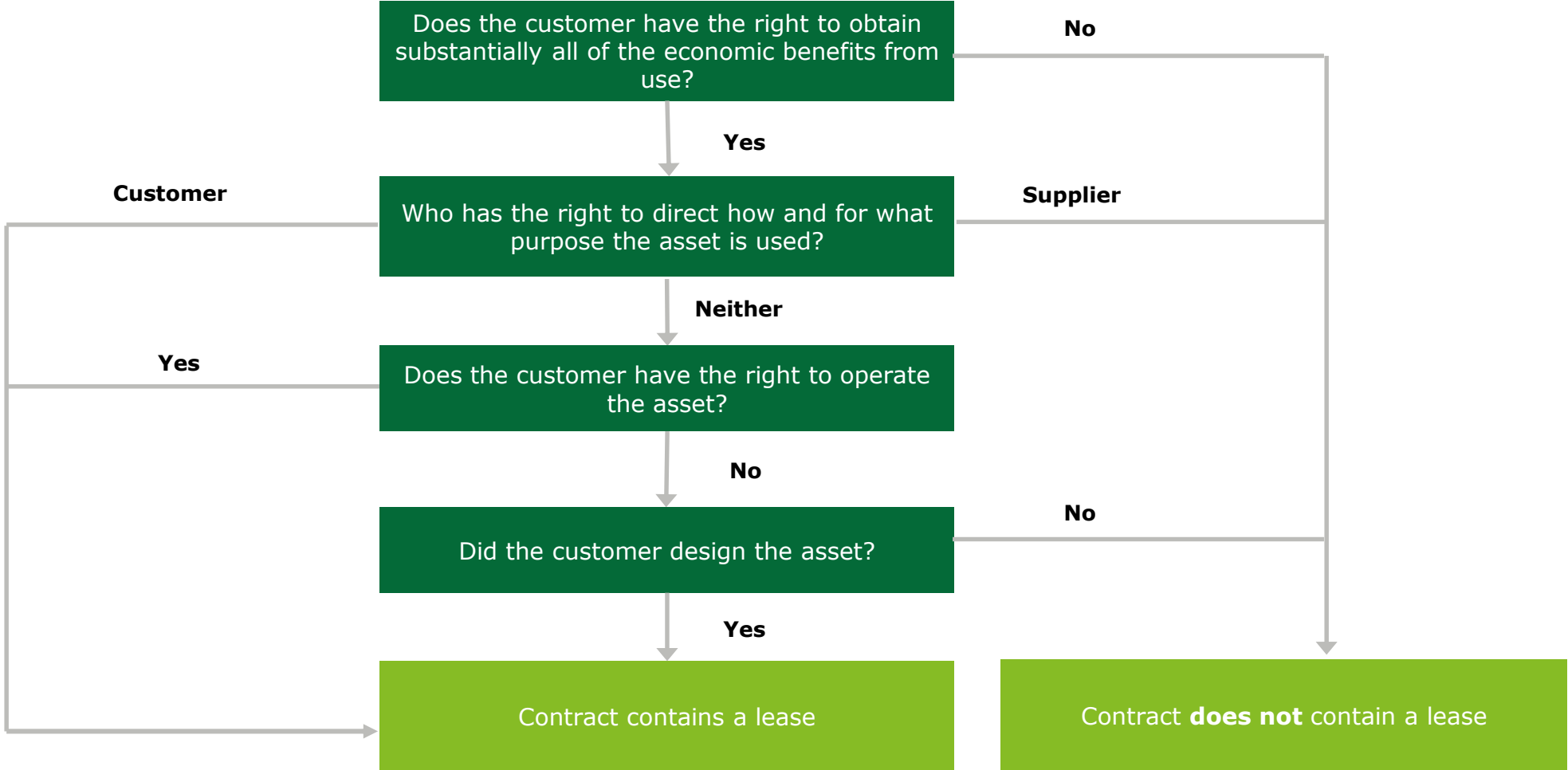
Right to direct the use of the asset

- Right to direct “how and for what purpose” the asset is used throughout the period of use; or
- Relevant decisions about “how and for what purpose” asset is used are predetermined before the period of use, and:
 - Customer has the right to operate asset without supplier having the right to change operating instructions; or
 - Customer designed the asset in a way that predetermines the most relevant decisions about how and for what purpose

Protective rights, while defining the scope of the asset use, generally do not, in isolation, prevent the customer from being able to direct the use of the asset

Right to control the use (cont.)

Decision tree



Right to control the use (cont.)

Illustrative example

Contract for the use of a crane—Facts

Customer A enters into a contract with Supplier B for the use of a specific crane for a two-year period

- Supplier B is not permitted to substitute the crane during the contract term
- During the lease term, Customer A is required to provide a properly trained operator for the crane
- Customer A decides what and when the crane will lift during the contract period, subject to certain limitations
- Customer A is prohibited from moving the crane or using it unsafely (e.g. lifting anything in excess of 20 tons)
- During the contract period, Supplier B is required to maintain the crane



Right to control the use (cont.)

Illustrative example

Contract for the use of a crane—analysis

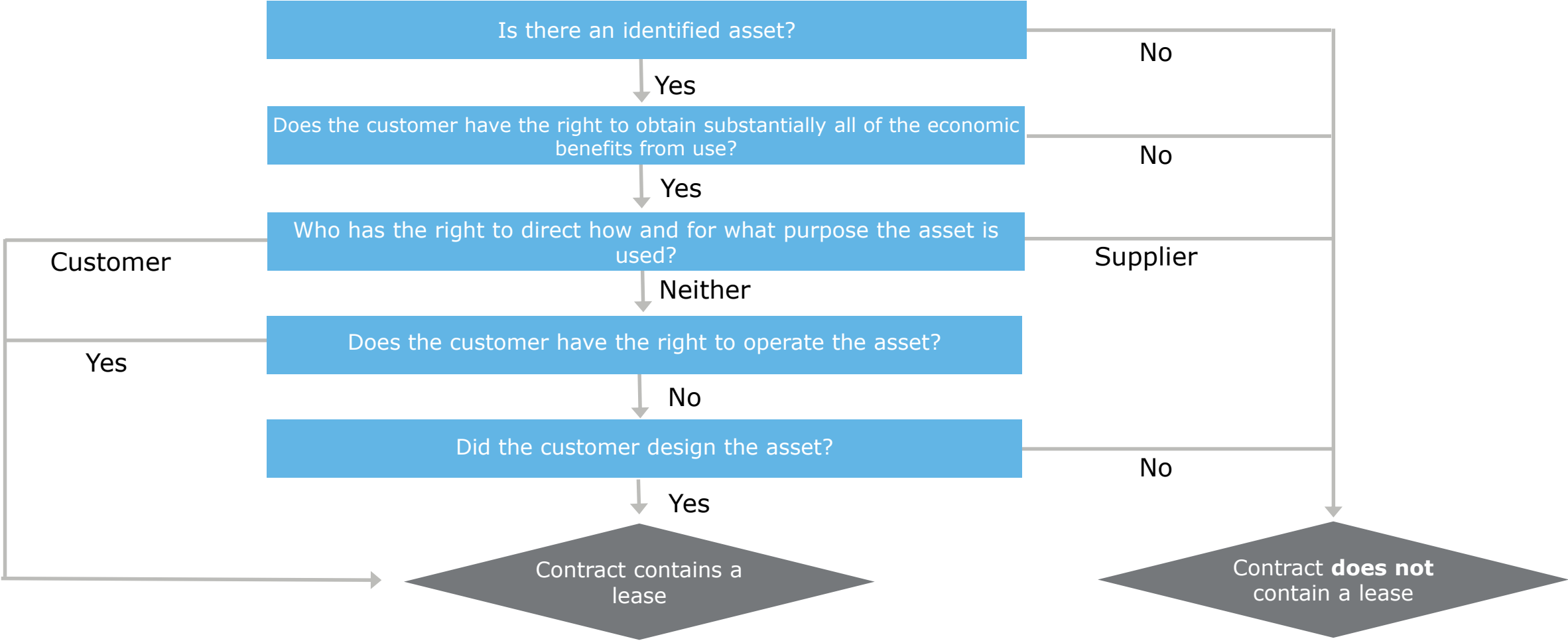
In this scenario, Customer A has the right to control the use of the crane throughout the two-year contract period

- Customer A has the right to obtain substantially all of the economic benefits from the use of the crane during the contract period through its exclusive use of the crane
- Customer A has the right to direct activities related to the use of the crane because it decides where and what the crane will lift
- While there are contractual restrictions about moving the crane or using it unsafely, these are protective rights and do not prevent Customer A from having the right to direct the use of the asset
- Since Customer A has an identified asset (crane) and the right to control the use of the crane, this contract would meet the definition of a lease
- since Customer has an identified asset and the right to control the use of the crane, it would meet the definition of lease.



Identifying a lease

Decision tree



Contracts with multiple components

Contracts that contain multiple components

Separating lease and nonlease components

Contracts with multiple lease components for different underlying assets

An asset will be considered a separate lease component if:

- Lessee can benefit from the use of the underlying asset either on its own or using other resources that are readily available
- The underlying asset is not highly dependent on or highly interrelated with other assets in the arrangement

NOTE: Land and other elements evaluated separately unless the accounting for the land element would not be significantly different

Contracts with lease and nonlease components (i.e., separate services)

An activity is a nonlease component if it transfers a good or service to the lessee:

- Common area maintenance (CAM) and utilities would likely be separate, nonlease components
- Property taxes and insurance would likely not be considered a component of the contract, and any consideration received should be allocated across the lease and nonlease components in the contract

NOTE: Consideration in the contract is only allocated to the contract components

Standard provides specific lessee and lessor guidance on how consideration should be allocated to each contract component

Contracts that contain multiple components

Allocating consideration in the contract

The basic process is similar for lessees and lessors

Step 1

Determine the consideration in the contract

Lessees:

- Fixed and in-substance fixed payments, less incentives
- Variable lease payments that depend on an index or rate

Lessors:

- Same as above, plus
- Variable consideration in accordance with ASC 606, for which variability does not relate to the lease component

Step 2

Determine the basis for allocation

Lessees, for each component:

- Stand-alone price using observable stand-alone price, if readily available
- If not, estimate stand-alone price maximizing the use of observable information
- Residual estimation may be appropriate

Lessors, for each component:

- Stand-alone selling price, in accordance with ASC 606

Step 3

Allocate consideration in the contract to each component

Lessees:

- Relative stand-alone price basis

Lessors:

- Relative stand-alone selling price basis, in accordance with ASC 606

Example: Lessee allocation

- Lessee X enters into a five-year lease of equipment from Lessor Y
- Fixed annual lease payments are \$25,000, which includes both rental payments and payment for maintenance of the equipment that are detailed within the contract as follows:

Items	Contractual payment
Rent	\$20,000
Maintenance	5,000
Total	\$25,000

Question 1: How many components are there in the contract?

Question 2: What is Lessee X's consideration in the contract?

Example: Lessee allocation (cont.)

Answer 1: Two

- Lease component, for the right to use the equipment
- Nonlease component, for the maintenance services

Answer 2: \$25,000

Accordingly, Lessee X would allocate its \$25,000 total consideration in the contract on the basis of stand-alone selling price (SASP) for two components. Assume that the SASP for the rent of the equipment is \$21,500. Further, assume that the stand-alone selling price for the maintenance services is \$3,000

Component	SASP	% of Total SASP	Allocation
Rent	\$21,500	87.8%	$87.8\% \times \$25,000 = \$21,950$
Maintenance	\$3,000	12.2%	$12.2\% \times \$25,000 = \$3,050$
Total	\$24,500	100.0%	\$25,000

Key ingredients of the leases model

Lease classification

Overview of the criteria

Classification criteria

Lease would be classified as a finance lease (lessee) or a sales-type lease (lessor) when:

- Lease transfers ownership of the underlying asset to lessee by the end of the lease term
 - Lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise
 - **Lease term** is for a major part of the remaining economic life of the underlying asset
 - Present value of the **lease payments** and any residual value guaranteed by the lessee equals or exceeds substantially all of the fair value of the underlying asset
 - Leased asset is so specialized in nature that it is expected to have no alternative use to the lessor at the end of the lease term
-

The standard states that the bright-line thresholds that exist under ASC 840 could be a reasonable approach to evaluate whether a lease would be classified as a finance lease

Lease term

Initial determination and reassessment

Lease term

Noncancelable period, plus:

- Renewal options that are reasonably certain to be exercised by a lessee
 - Termination options that are reasonably certain not to be exercised by a lessee
 - Options to extend (or not to terminate) that are controlled by the lessor
-

Reassessment requirements

Lessees are required to reassess lease term when:

- A significant event or change in circumstances occurs that is in the control of the lessee
- A contract term obliges the lessee to exercise (or not exercise) a renewal or termination option
- Lessee elects to exercise or not exercise a renewal or termination option that was not previously deemed reasonably certain of being or not being exercised
- Would reassess when there is a modification that does not result in a separate contract

Lessors would not be required to reassess lease term, unless there is a modification that does not result in a separate contract

Lease payments

What amounts are included in lease payments?

Fixed lease payments



- Payments specified in the lease agreement
- In-substance fixed payments

Variable payments



- Payments that depend on an index or a rate
- Excludes payments based on usage or performance
- Reassessment required under certain circumstances

Residual value guarantees



- **Lessees**—amount that it is probable will be owed under the RVG at the end of the lease term
- **Lessors**—the full amount at which the residual asset is guaranteed by the lessee or third party

Purchase and termination options



- Treated in a manner consistent with the accounting for renewal options
- Include options that a lessee is reasonably certain to exercise

Discount rate

What discount rate should be used?

- Lessee must use the rate the lessor charges in the lease if readily determinable or, alternatively, its incremental borrowing rate
- Lessor would use the rate it charges the lessee, which is known as the rate implicit in the lease

Reassessment requirements

- Would generally be updated when there is a remeasurement of the lease obligation
- Would reassess when there is a modification that does not result in a separate contract

- Would reassess, in certain instances, when there is a modification that does not result in a separate contract

Nonpublic business entities are permitted to make an accounting policy election to use the risk-free rate when measuring their lease obligations

Overview of the core accounting models

Lessee accounting model

What does the lessee model look like?

Most* leases are recorded on the balance sheet using a right-of-use asset approach

Initial measurement

- **Lease obligation**—PV of lease payments not yet paid
- **ROU asset**—lease obligation + initial direct costs – lease incentives + prepaid lease payments

Subsequent measurement

- **Lease obligation**—amortized using the effective interest method
- **ROU asset**—depends upon lease classification
- Expense recognition pattern:
 - Finance lease—front-loaded
 - Operating lease—generally straight-line

** Short-term leases: A lessee can elect, by asset class, not to record on its balance sheet a lease with a lease term of 12 months or less and that does not include a purchase option that the lessee is reasonably certain to exercise*

Lessee accounting model

Illustrative example

A lessee enters into a three-year lease and agrees to make the following annual payments at the end of each year: \$10,000 in year 1, \$15,000 in year 2, and \$20,000 in year 3. The initial measurement of the right-of-use (ROU) asset and liability to make lease payments is \$38,000 at a discount rate of 8%.

This table highlights the differences in accounting for the lease under the finance lease and operating lease models.

Year	Both methods		Finance lease			Operating lease (straight-line approach)		
	Lease liability	Interest expense <X>	Amortization expense <Y>	Total lease expense <X + Y>	ROU asset	Lease expense <Z>	Reduction in ROU asset <Z - X>	ROU asset
0	\$38,000				\$38,000			\$38,000
1	31,038	\$3,038	\$12,666	\$15,704	25,334	\$15,000	\$11,962	26,038
2	18,520	2,481	12,667	15,148	12,667	15,000	12,519	13,519
3	-	1,481	12,667	14,148	-	15,000	13,519	-
Total		\$7,000	\$38,000	\$45,000		\$45,000	\$38,000	

Lessee accounting-let's do the journal entries!

Lessee enters into a three-year lease with payments of \$10,000 at the end of year one, \$15,000 at the end of year two and \$20,000 at the end of year three, for a total of \$45,000. Assume an interest rate of 8%.

Journal Entry at lease inception:

Right of use asset	\$38,000 (assumes no initial direct costs)
Lease liability	\$38,000 (PV of lease payments @8%)

Lessee accounting-let's do the journal entries!

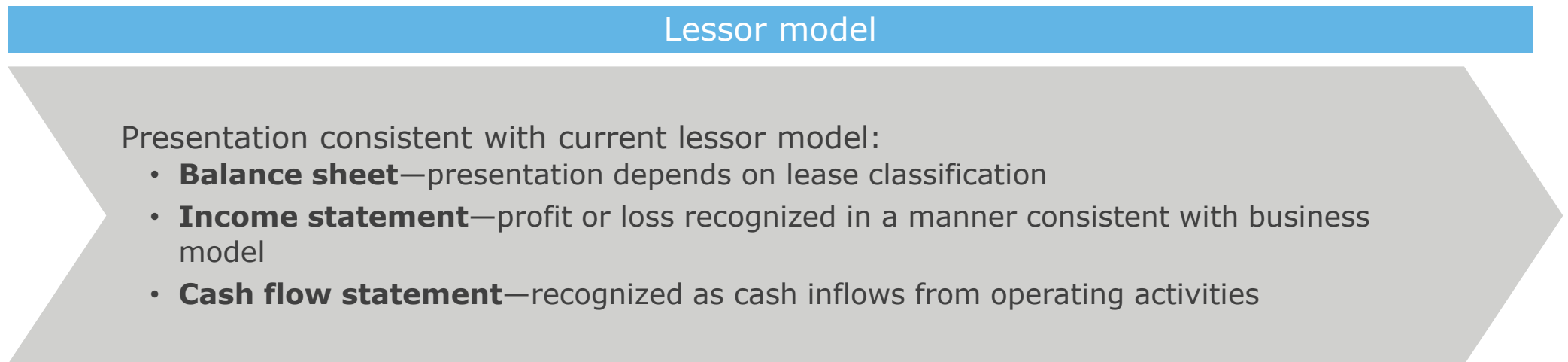
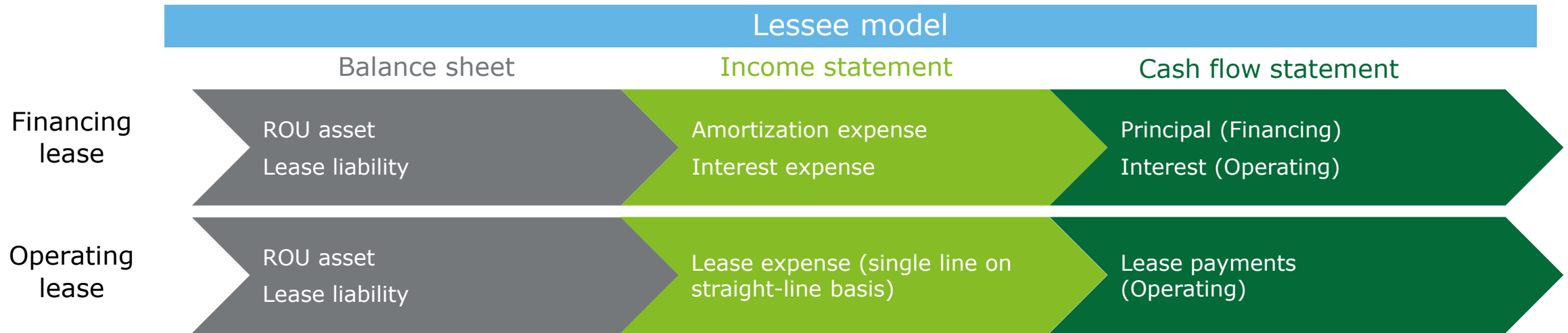
Finance lease: entry at end of year one:

Amortization expense	\$12,667 ($\$38,000/3$)
Interest expense	\$3,038 ($\$38,000 \times .08$)
Lease liability	\$6,962 ($\$10,000 - \$3,038$)
Right of use asset-accumulated amortization	\$12,667
Cash	\$10,000

Operating lease: entry at end of year one:

Rent expense	\$15,000 ($\$45,000/3$)
Lease liability	\$6,962 ($\$10,000 - \$3,038$)
Right of use asset-accumulated amortization	\$11,962 (PLUG)
Cash	\$10,000

Presentation requirements



Disclosure requirements

Disclosure objective—Enable financial statement users to assess the amount, timing, and uncertainty of cash flows arising from leases

Lessee disclosures

- Nature of its leases
 - Information about leases that have not yet commenced
 - Related-party lease transactions
 - Accounting policy election regarding short-term leases
 - Finance and operating lease costs
 - Short-term and variable lease costs
 - Sublease income
 - Gain or loss from sale-and-leaseback
 - Maturity analysis for lease obligations
 - Weighted-average remaining lease term
 - Weighted-average discount rate
-

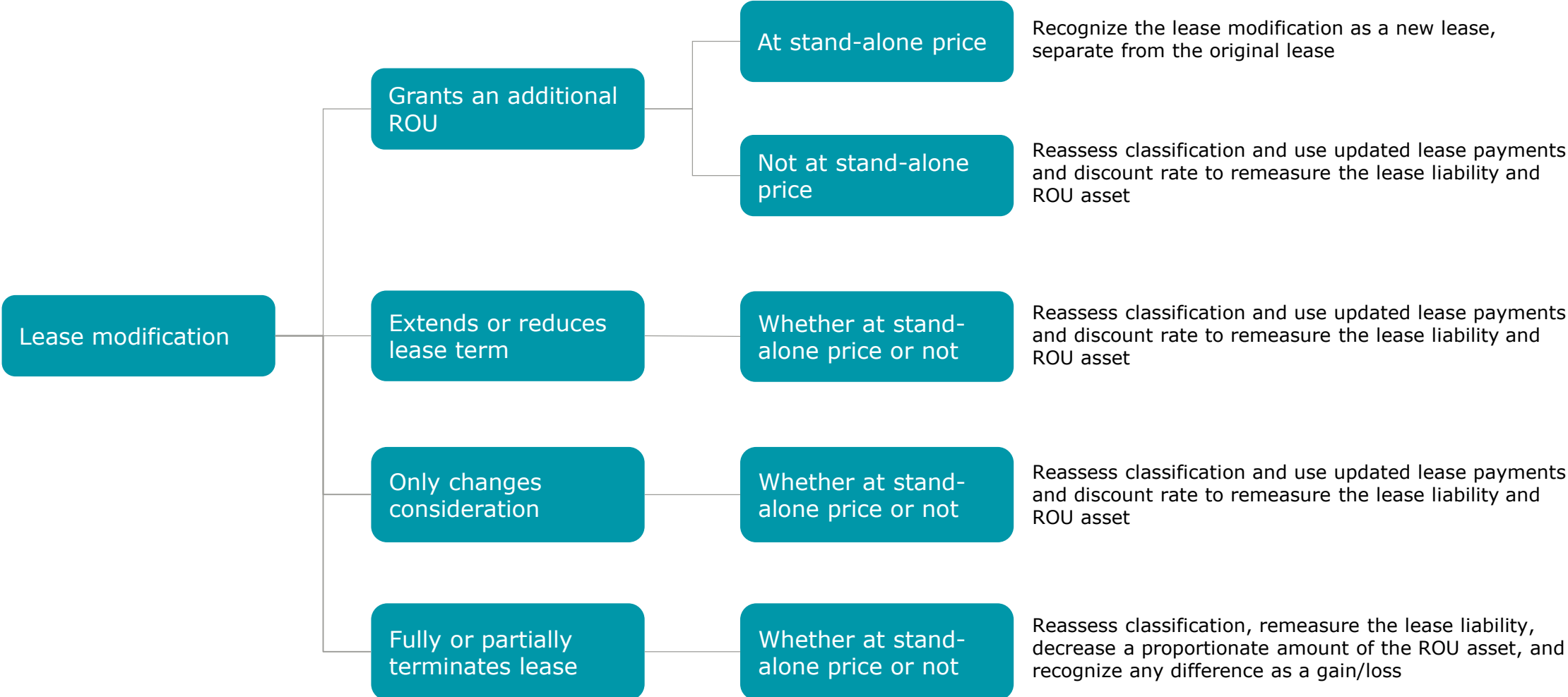
Lessor disclosures

- Nature of its leases
 - Significant assumptions and judgments used
 - Related-party leases transactions
 - Tabular disclosure of lease-related income
 - Components of the net investment in a lease
 - Information on the management of risk associated with residual asset
 - Maturity analysis of operating lease payments and lease receivable
 - Information required by ASC 360
-

Other provisions, effective date, and transition

Lease modifications

Lessee



Other key provisions

Lessee disclosures

- Head lease and sublease accounted for as two separate leases
- Sublease classification based on underlying asset
- Offsetting generally prohibited

Related-party leases

- Accounted for on the basis of legally enforceable terms and conditions (versus substance)
- Subject to ASC Topic 850 disclosure requirements

Leasehold improvements

- Generally capitalized and amortized over the shorter of their useful life or remaining lease term unless:
 - Lease transfers ownership at the end of lease term or
 - It is reasonably certain that lessee will exercise purchase option
-

Effective date and transition

Effective date

- Public business entities—effective for calendar periods beginning on January 1, 2019 and interim periods therein
- All other entities—effective for calendar periods beginning on January 1, 2020, and interim periods thereafter
- Early adoption will be permitted

Transition

- Lessees and lessors are required to use a modified retrospective transition method for all existing leases
- Would apply the new model for the earliest year presented in the financial statements
- Application of approach linked to current lease classification and new lease classification
- An entity can use hindsight when evaluating lease term

Transition relief package:

Lessees and lessors are not required to reassess the following upon transition:

- Whether any expired or existing contracts are leases or contain leases
- The lease classification for any expired or existing leases
- Initial direct costs for any existing leases

ASC 205: Retrospective reporting compliance

Insight to required financial statements to be presented on the reporting date for all entities

Public business entities (SEC)	
Balance sheet	
FY 2018	FY 2019
Restate under ASC 842	

Income statement (P&L)		
FY 2017	FY 2018	FY 2019
Restate under ASC 842		

Public business entities: effective for calendar periods beginning after December 15, 2018 and interim periods **therein**. The Q1 2019 will be the first publication to be presented in compliance

All other entities	
Balance sheet	
FY 2019*	FY 2020
Restate under ASC 842	

Income statement (P&L)	
FY 2019*	FY 2020
Restate under ASC 842	

All other entities: effective for calendar periods beginning after December 15, 2019 and interim periods **thereafter**

*Topic 205 encourages a **comparative presentation** as ordinarily desirable, but requirements may differ

SEC and ASC 250 reporting rules require earlier comparative results restated (as early as 2017)

Shall provide the transition disclosures required by Topic 250 on accounting changes and error corrections, except for the requirements related to effect of changes in the statements

Early adoption is permitted

Other key provisions and resources

But wait, there's more...

- Contract combinations
- Leveraged lease accounting
- Accounting for leases at a portfolio level
- Leases in a business combination
- Impairment considerations
- U.S. GAAP to IFRS comparison

Deloitte.

March 1, 2016
Updated July 12, 2016
Volume 23, Issue 5

Heads Up

Bring It On!
FASB's New Standard Brings Most Leases Onto the Balance Sheet


In This Issue

- A Snapshot of the New Guidance
- Scope
- Short-Term Leases
- Definition of a Lease
- Lease Classification
- Lease Term
- Lease Payments
- Discount Rate
- Lessee Accounting
- Lessor Accounting
- Effective Date
- Appendix A — Evaluating Whether an Arrangement Is or Contains a Lease
- Appendix B — Other Significant Provisions
- Appendix C — Presentation Requirements
- Appendix D — Disclosure Requirements
- Appendix E — Transition
- Appendix F — Implementation Considerations

Join us on March 15 at 2:00 p.m. EDT for a **Webcast** on the new standard.

Deloitte.

Heads Up | Volume 24, Issue 12
April 25, 2017



Frequently Asked Questions About the FASB's New Leases Standard

by Deloitte & Touche LLP's National Office, Accounting Services

Introduction

It's been over a year since the FASB issued ASU 2016-02,¹ its new standard on accounting for leases (codified in ASC 842).² Although the standard will not be effective until 2019,³ entities have already begun raising implementation issues.⁴ In addition, many questions have arisen about the standard's fundamental concepts, including the definition of a lease, lease payments, and presentation and disclosure.

In this *Heads Up*, we share our perspectives on such topics and address FAQs about the standard. We have also included several Driving Discussions to highlight certain key issues related to the new guidance, some of which remain unresolved as of the issuance date of this publication.

For a comprehensive overview of ASU 2016-02, see Deloitte's March 1, 2016, *Heads Up*.

¹ For full titles of standards, regulations, and other literature, see Appendix A. For definitions of abbreviations, see Appendix B.
² ASU 2016-02 was issued on February 25, 2016. ASU 16-01, the IASB's new leases standard, was issued on January 13, 2016.
³ For public business entities, certain not-for-profit entities, and certain employee benefit plans, ASU 2016-02 is effective for annual periods beginning after December 15, 2018, and interim periods therein. For all other entities, the ASU is effective for annual periods beginning after December 15, 2019, and interim periods within annual periods beginning after December 15, 2020. Early adoption is permitted.
⁴ On November 30, 2016, for the first time since issuing ASU 2016-02, the FASB discussed implementation issues related to the new leases standard. The Board indicated that it will address implementation issues raised by stakeholders in future FASB meetings instead of forming a transition resource group (TRG) similar to the TRG created to address transition issues related to the new revenue recognition and credit losses guidance.

In This Issue

- Introduction
- Scope
- Definition of a Lease
- Lessee Model
- Lessor Model
- Lease Classification
- Ingredients of the Lessee Model
- Presentation and Disclosure
- Transition
- Other Key Provisions
- Appendix A — Glossary of Standards and Other Literature
- Appendix B — Abbreviations

Tax implications

Overview of income tax implications

Lease characterization for federal income tax purposes has not changed (e.g., true lease vs. sale) as a result of ASC 842. For tax, the focus remains on which party bears the benefits and burdens of ownership

ASC 842 **does not contain tax accounting guidance** and only includes minor, conforming amendments to ASC 740, *Accounting for Income Taxes*, that do not change the basic requirements of current accounting

ASC 842 will create book/tax differences consistent with current GAAP. However, since the new standard may result in the recognition of more assets and liabilities, ASC 842 **may require entities to record new or adjust existing DTAs and DTLs**

ASC 842 **may also impact the computation of state and local income-based taxes** as a result of changes to the apportionment formula

Common book/tax differences

Tenant construction allowances

	Book	Tax
Lessee Lessee-owned	<ul style="list-style-type: none">• Lessee records allowance as an incentive that reduces the ROU asset that is recorded• Resulting asset is generally amortized over the lesser of the life of the asset or the lease term	<ul style="list-style-type: none">• Lessee includes allowance into income on receipt; depreciates property over applicable recovery period
Lessor Lessor-owned	<ul style="list-style-type: none">• Lessor depreciates property on a straight-line basis over the useful life	<ul style="list-style-type: none">• Lessor depreciates property over applicable recovery period

Common book/tax differences

Operating lease (book)/true lease (tax)

	Book	Tax
Lessee Lessee-owned	<ul style="list-style-type: none">• Lessee expenses rent on a straight-line basis over lease term	<ul style="list-style-type: none">• Lessee expenses rent as payments are made (subject to section 467)
Lessor Lessor-owned	<ul style="list-style-type: none">• Lessor depreciates property on a straight-line basis over the useful life	<ul style="list-style-type: none">• Lessor depreciates property over applicable recovery period

Common book/tax differences

Finance lease (book)/asset sale (tax)

	Book	Tax
Lessee only	<ul style="list-style-type: none"> • Lessee expenses interest component of payment as payments are made • Lessee uses lessor's implicit rate, if readily determinable, or incremental borrowing rate • Lessee depreciates ROU asset on a straight-line basis or using another systematic basis, if appropriate 	<ul style="list-style-type: none"> • Lessee expenses interest component of payment as payments are made • Interest imputed using AFR under OID rules • Lessee depreciates property over applicable recovery period

Areas of potential challenges

Operational challenges

Key challenges associated with the proposed lease standard

1

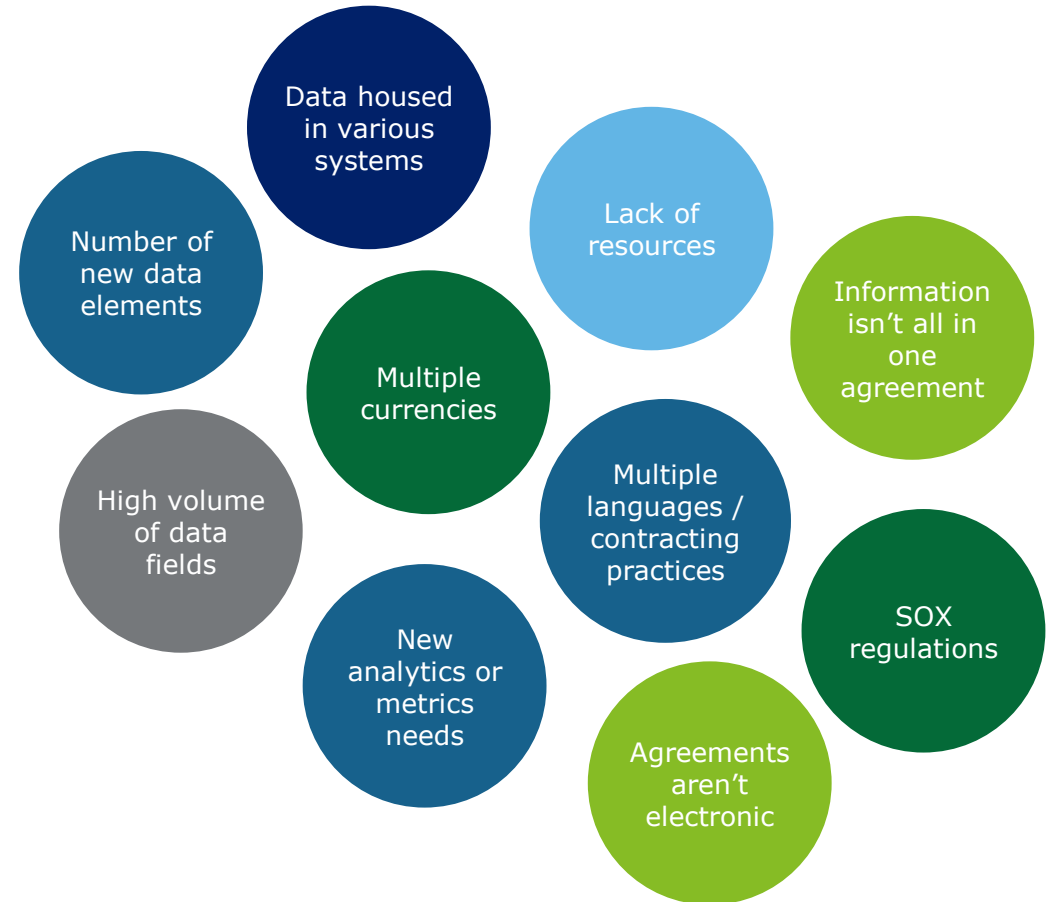
Data Challenges: High volume of lease agreements across multiple decentralized locations, in different business and operating units.

2

IT systems: Need to store lease data and perform calculations. Consider modifying existing system or moving to new system. Given the long lead times of system initiatives, may need bridge system.

3

Timeline for adoption: It can be a challenge to anticipate the data gaps and overcome the data abstraction hurdle. A typical timeline from planning to implementation is 18-24+ months.



The data being collected may be in a variety of formats, thus increasing the complexity and cost of organizing the data.

Operational challenges (cont.)

The system change efforts are often given primary consideration, however you must also consider the vital component of data maintenance.



During this period, your operations do not cease. New leases are entered into and existing leases are modified and terminated.

Operational challenges (cont.)

The following challenges should be considered in the transition period:

Application of Judgment and Estimation



Apply judgment and make estimates under a number of the new lease requirements:

- Judgment is often required in the assessment of a lease's term, which would affect whether the lease qualifies for the short-term exemption and therefore for off-balance-sheet treatment
- Since almost all leases will be recognized on the balance sheet, an entity's judgment in distinguishing between leases and services becomes more critical under the new guidance
- Lease classification without bright line classification tests
- Determine whether the customer has the right or not to direct the use of the identified asset

Data Management



- Third-party data may be needed to ensure a high level of operational quality and efficiency
- Numerous lease agreements at multiple decentralized locations, lease data in spreadsheets or physical documents. Consequently, collecting and abstracting may be time-consuming and resource-intensive
- Entities may need to gather information that may not be contained in lease agreements (e.g.: the fair value of an asset, the asset's estimated useful life, incremental borrowing rate, etc.)
- Distinct data between the new requirements and to accomplish with the transition period data

Operational challenges (cont.)

Internal Controls and Business Process Environment



- Increased relevance of new leasing to the financial statements, entities may face additional scrutiny from auditors and regulators regarding the design and effectiveness of associated controls under Sarbanes-Oxley
- Examine internal controls related to their processes for capturing, calculating, and accounting for their leases
- Internal controls or processes are needed, entities may also need to issue organizational communications and establish change management and employee training programs

Covenants



- Careful examination of the effects of increased leverage and potential debt covenant violations will be required
- This may depend in part on how various debt agreements define and limit indebtedness as well as on whether the debt agreements use “frozen Generally Accepted Accounting Principals (GAAP)” covenants.
- The ASC requires entities to present operating lease liabilities outside of traditional debt, which may provide relief to some entities. Nevertheless, it will be critical for all entities to determine the ASC’s potential effects on debt covenants.

Income Taxes



- Potential tax implications are situational requiring involvement of entities’ tax department

Internal control considerations

Lease accounting is naturally an area of significant complexity both from an operational and accounting perspective.

The new lease standard introduces additional considerations around a company's internal control structure:

- Increased focus around internal controls by regulators and other stakeholders
- New balances and disclosures subject to internal controls
- Complexity of requirements of the New Lease Accounting Standard

- Other internal control considerations
- Data and access management
 - Workflow management with approvals/reviews
 - Audit trails
 - Segregation of duties
- Technology/processing
 - Version control
 - Re-assessment for lease modifications
- Service organization
 - Internal controls performed by service organization
 - Consideration of new Committee of Sponsoring Organizations (COSO) integrated framework



Control considerations during the lease cycle (part 1 of 2)



Reporting and Disclosures

- Control Environment
 - Building in the appropriate structure and accountability to handle the changes including Steering Committee and Project Management Office (PMO)
 - Approach to areas where judgment is required
- Risk assessment
 - Change creates risk
 - Consider risks related to financial reporting change
 - Monitoring controls implemented
 - System change controls in place
 - Appropriately trained personnel
 - Coordination between various key stakeholders (e.g. technical accounting, tax, real estate, IT)
- Completeness of initial opening balance sheet
 - Challenge of getting the lease data into an electronic repository
 - Potential decentralization of the data gathering efforts
 - Existing lease data used for operational purposes and may not be subject to internal controls
 - Reconciliation to current ASC 840 footnote disclosures
- Controls during comparative reporting period



Information Technology Controls

- Controls around classification – operating vs. financing leases
- Embedded leases
- Short Term lease scope exception
- Portfolio approach



Controls around Outsourced Service Providers

- Leases commonly are modified, renewed, extended, cancelled
 - Challenge around frequency
 - Completeness and timely identification of modifications as they occur
 - Process for tracking and review / approvals for changes
- Version controls



Control considerations during the lease cycle (part 2 of 2)



Reporting and Disclosures

- Significantly increased disclosure requirements – increased visibility to judgments used and nature of the lease portfolio
- Many of the disclosure requirements are data Intensive
 - Weighted average calculations, variable lease payments, etc.
 - Consider source and controls over the data



Information Technology Controls

- Controls over source data and interfaces / data transfers
- General IT controls including access controls, Segregation of Duties
- Change management controls related to lease calculations
- Appropriate user acceptance testing
- Reviews/approvals and workflow management
 - Especially important when decentralization exists
- Audit trails



Controls around Outsourced Service Providers

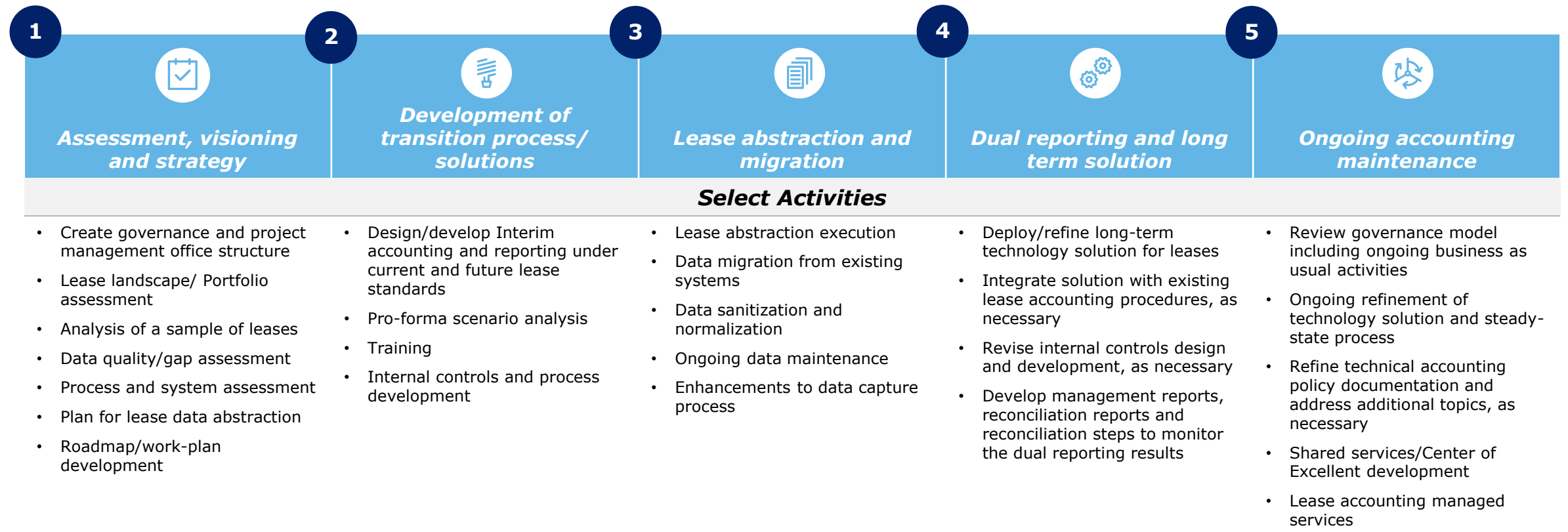
- Many organizations use Outsourced Service Providers to assist in the management of parts or all of their lease portfolio
 - Consider internal controls performed by the Service Provider
 - Appropriate monitoring mechanisms over reporting from the Service Provider



Components of an Implementation Effort

An Approach to Implementation

Implementation is typically made up of five phases, beginning with a phase 1 assessment, visioning and strategy.



Implementation tools

A variety of technologies are available

These technology accelerators and solutions may be customized to meet specific lease accounting and lease administration needs.

Analysing and abstracting lease contracts

Abstraction software



- Software that automates the process of reading and extracting critical data from documents and contracts
- Combines machine learning algorithm with human knowledge (contract provisions “trained” by Deloitte domain specialists)
- Increases productivity and delivery speed making it faster, easier, and cheaper to abstract required lease data

Solution for lease accounting calculations to facilitate ASC 842 adoption

LeaseController™



- LeaseController is focused primarily on the new lease accounting standard
- LeaseController comes bundled with Deloitte services
- Flexible and customizable for all industries
- Covers real estate leases in addition to other lease types (e.g., equipment, vehicles, etc.)
- Use LeaseController for reporting under current and future rules

Rethinking workspace management and lease accounting and administration

LeasePoint™

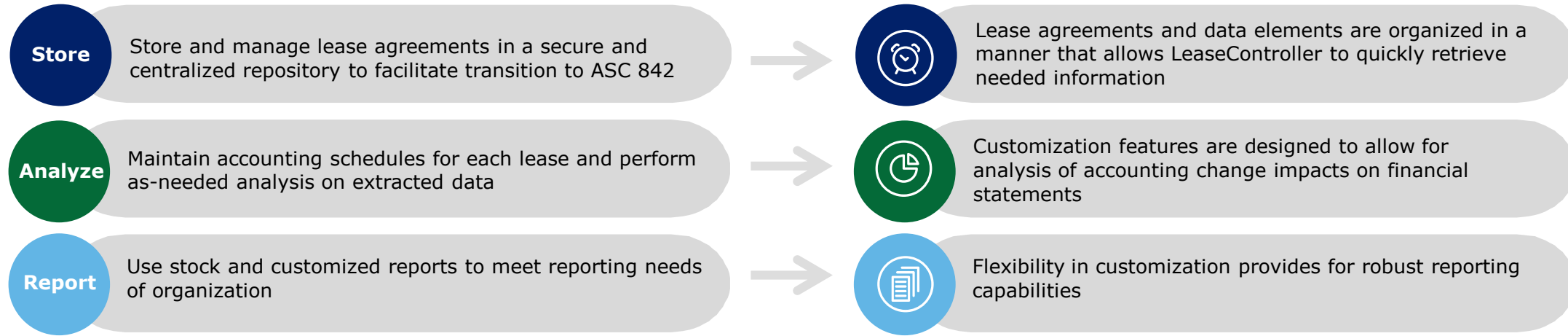


- LeasePoint is a cloud-based solution powered by IBM TRIRIGA®
- The solution is focused on real estate and equipment lease administration, payment and accounting functionality
- LeasePoint transmits relevant lease data to a client’s ERP solution for financial reporting and generates information needed for footnotes
- Robust, secure, scalable hosting and application support managed by Deloitte; may also be bundled with Deloitte accounting support services

As used in this document, “Deloitte” means Deloitte & Touche LLP, a subsidiary of Deloitte LLP. Please see www.deloitte.com/us/about for a detailed description of the legal structure of Deloitte USA LLP, Deloitte LLP and their respective subsidiaries. Certain services may not be available to attest clients under the rules and regulations of public accounting.

Deloitte LeaseController™

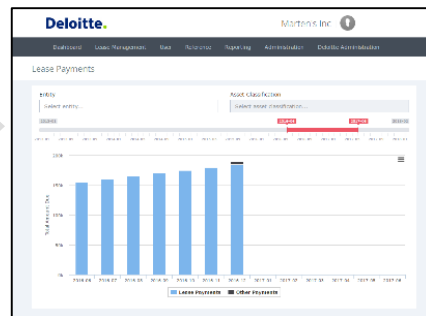
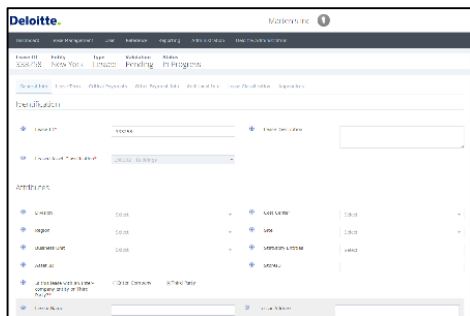
LeaseController facilitates data gathering, analytical reviews and reporting under current and future rules. LeaseController can assist with implementation efforts by providing a centralized repository to store lease documentation and analyze and report on the information critical to your organization.



Store

Analyze

Report



Lease ID	Party	Type	Maturity	Status	Lease Type	...
1000000001	ABC Corp	Operating	2025-12-31	Active	Operating	...
1000000002	DEF Inc	Finance	2026-06-30	Active	Finance	...

Q&A



Jim Brant, Partner

jbrant@Deloitte.com

Clif Mathews, Partner

clmathews@Deloitte.com



Official Professional Services Sponsor

Professional Services means audit, tax, consulting, and advisory.

About Deloitte

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. In the United States, Deloitte refers to one or more of the US member firms of DTTL, their related entities that operate using the "Deloitte" name in the United States and their respective affiliates. Certain services may not be available to attest clients under the rules and regulations of public accounting. Please see www.deloitte.com/about to learn more about our global network of member firms.