lease accounting

Market Readiness Two Years after the Publication of ASC 842

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LEASE ACCOUNTING PROGRESS REPORT 2018
EXECUTIVE SUMMARY

Two years have passed since the initial publication of the new ASC 842 Leases standard by the Financial Accounting Standards Board (FASB). In an effort to provide a quantitative progress report on the status of compliance efforts, LeaseAccelerator conducted a research study in late January 2018. Over 300 finance and accounting leaders from large US-based public and private companies were surveyed. A summary of the findings is outlined below:

KEY FINDINGS

Most Companies are On Track, but Prefer a One Year Extension

Two thirds of companies are on schedule or ahead of schedule with their lease accounting project, which is encouraging as the first implementation deadlines are approaching at the end of 2018. Only 6% indicated that they had completed the project. Approximately 60% of companies think that FASB should extend the compliance deadline with the majority seeking only a one-year delay. It seems the desire for additional time is not solely driven by the complexity of the ASC 842 standard, but rather the combined work effort required to comply with both the new leasing and revenue recognition standards in such close proximity.

Leasing Project More Complex than Revenue Recognition

As compared to the new revenue recognition accounting standards, 75% are finding the new leasing standards to be just as complex or more challenging. The top implementation challenge with leasing projects, cited by 50% of respondents, is finding and collecting the necessary data. Respondents also indicated that modifying business processes, policies, and controls; upgrading software applications; and project managing the overall work effort were also key implementation hurdles. Only 30% cited that the application of the accounting standards was proving to be a significant challenge. However, many suggested simplification or implementation relief for areas such as embedded leases, separating non-lease components, comparative reporting, and financial disclosures.

Embedded Leases are the Most Challenging to Analyze

Accounting organizations are finding embedded leases contained in service agreements with contract manufacturing, third party logistics, and data center outsourcing vendors to be the most challenging to find and analyze. Non-real estate leases such as IT, fleet, material handling, rail car, transportation, and other equipment leases are also proving challenging. More than half of companies have taken an inventory of their enterprise-wide lease portfolio. And 30% of companies are more than half way done with the data collection process.

Best of Breed Lease Accounting Software Applications Rising

More than one third of companies have now selected a software vendor to support the new lease accounting standards. For most companies, the historically-used, spreadsheet-based accounting approach will be replaced with a true enterprise application. Significant work remains for systems implementation as less than one third of companies have issued an RFP for lease accounting software. New, best-of-breed lease accounting vendors are the most popular option being considered. ERP and real estate administration vendors are also being widely considered.

Accounting is Taking a Formal Cross-Enterprise Role

Approximately, 80% have assigned a formal project manager from the accounting or financial reporting team to lead the initiative, which for many companies will be one of the largest accounting change initiatives in the past 50 years. Corporate Real Estate and IT are playing a strategic role in more than half of the projects. Almost two thirds of companies are planning to leverage in-house resources to complete the project. Less than 30% plan to utilize consultants from the Big Four, IT, or Business Process outsourcing organizations.

RECOMMENDATIONS

Hidden Challenges Remain for Many Project Teams

While companies are demonstrating meaningful progress in their lease accounting compliance efforts, many project teams have yet to reach the more challenging activities of the initiative. The data collection effort, not the accounting, will be the most time-consuming aspect of the project. In most cases, data will need to be collected manually by studying leasing contracts, reviewing purchase orders, and interviewing asset users. Even data sourced from enterprise systems, such as real estate administration, will need to be cleansed, reconciled, and enriched to perform the accounting. Evaluating and selecting a software application will present new challenges. Only a few vendors have mature applications that have been tested in real-world scenarios. As a result, many companies may have to undertake manual workarounds to complete the accounting until vendor product roadmaps are completed.

Take a Formal Project Management Approach

ASC 842 is more complex than most accounting change projects. The scope cannot be limited to within the four walls of the controller's organization. Participation from the day-to-day users of the leased assets, including Real Estate, Corporate IT, Fleet, Operations, and Logistics, will be required along with support from corporate functions such as Treasury, Procurement, and Accounts Payable. To mitigate the risk of project delays, we encourage accounting organizations to appoint a formal executive sponsor who will seek out budget and resource commitments across the business. We also encourage companies to assign a dedicated project manager who manages activities from a formal project plan.

Plan for Day Two and Beyond

Most project teams are focused on simply complying with the new implementation deadlines. However, another set of challenges await accounting organizations on day two and beyond. Success with lease accounting will demand that companies get visibility into all new leases being signed across the business as well as the many different events that can occur within the term of a contract. Variable rent changes, equipment location changes, cost center changes, mid-term buyouts, and end-of-term renewals are just a few examples. Project teams should implement long-term business processes, policies, and controls to ensure that their lease accounting remains accurate after day one. Success will require commitment and partnerships with functions such as Procurement, Treasury, Real Estate, Corporate IT, and Operations.

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