



Steps to Prepare for New Lease Standards

ASC 842 AND GASB 87

WEALTH ADVISORY | OUTSOURCING | AUDIT, TAX, AND CONSULTING



Previous lease standards allowed operating leases to be reported in a way that did not clearly reflect commitments made by the lessee. In accordance with those standards, only capital leases were recognized as assets and liabilities in the financial statements, and liabilities associated with operating leases were only disclosed in the notes to the financial statements.

Now, Financial Accounting Standards Board (FASB) ASC 842 and Governmental Accounting Standards Board (GASB) 87 both require entities to evaluate all contracts relating to the right-to-use assets for recognition in financial statements. **For those contracts that qualify, entities are required to report a lease asset and liability.**

ASC 842 also requires that leases be classified as either operating or financing, which impacts their presentation on income and cash flow statements. GASB 87 requires that all leases be reported as financing activities — significantly changing how entities report expenditures in governmental funds.

Impact to financial reporting

Understand how these changes will impact your financial reporting and how those changes will be interpreted by third parties that rely on financial statements to make business decisions. Quick ratios, debt ratios, and earnings before interest, taxes, depreciation, and amortization (EBITDA) can all be affected and may impact future compliance with current loan covenants or in securing new financing.

Both standards require additional disclosure.

For governmental entities, it will impact the same ratios and change the way governmental fund budgets are prepared. In addition, government lessors will be required to mirror the lessee entries and recognize a lease receivable and corresponding deferred inflow.

Stay ahead and stay compliant

Implementation will take more time and money than most entities realize, and there is no substitute for education and planning. Since leases exist in a variety of different forms and formats and may not be obvious or easily identified, entities that seemingly have minimal leases or complexities may be unexpectedly impacted.



In fact, this is likely the most time-consuming and complex portion of the implementation process. While timing may vary, plan on the process taking months, not weeks. Consider three of the most common factors affecting timeline and effort:

- The size and complexity of the leasing and service contract portfolio
- The structure and availability of the leasing and service contracts and data
- The availability of internal resources and knowledge to assist with the process

As with any project, the more time spent on planning and preparation, the better the chance of successful execution. As a first step, identify a lease champion within your entity and establish a plan. To create a path to success, thoughtfully prepare in the five areas shown on the right.

Be proactive when entering into new leases. Your knowledge and understanding of how each contract is structured, and the words therein, directly impact financial reporting. Consider modifying historical language when entering into future contracts to make sure the accounting properly reflects the circumstance. For contracts that have both fixed and variable payments, you may opt to have lower fixed payments — as variable payments are excluded from the lease liability and asset.

New lease standard deadlines

Start designing and implementing lease accounting processes that meet the requirements of the new standards now to better prepare for the following accounting standards reporting.

ASC 842 — private companies	Years beginning after December 15, 2021
-----------------------------	---

GASB 87	Years beginning after June 15, 2021
---------	-------------------------------------

CLA can help navigate you through the standards and provide support along the way.

1 Planning

Develop a high-level project plan and establish a steering committee to provide project oversight and make an achievable timeline.

2 Current state assessment

Understand your lease environment, inventory your leases, and validate the completeness of your lease population. Create a detailed project plan and develop a tailored training program for your designated staff.

3 Lease accounting software

Evaluate various lease management tools and software for future accounting of the new lease standard.

4 Lease analysis and implementation

Analyze existing leases, service arrangements, and other contracts to determine if they meet the definition of a lease under the new standards. Extra time and knowledge may be necessary to perform an embedded lease analysis, collect the required data, and document key attributes, accounting, and management's elections.

5 Functional area analysis and execution

Learn how the new standards impact internal controls and each functional area of the entity and consider changes.





CLAcconnect.com

WEALTH ADVISORY | OUTSOURCING | AUDIT, TAX, AND CONSULTING

Investment advisory services are offered through CliftonLarsonAllen Wealth Advisors, LLC, an SEC-registered investment advisor. CLA is an independent member of Nexia International, a leading, global network of independent accounting and consulting firms. See [nexia.com/member-firm-disclaimer](https://www.nexia.com/member-firm-disclaimer) for details. CliftonLarsonAllen LLP

