Leases

A summary of IFRS 16 and its effects

May 2016

EY

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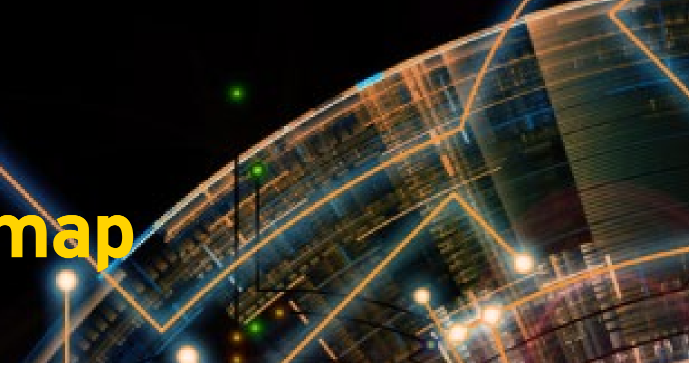
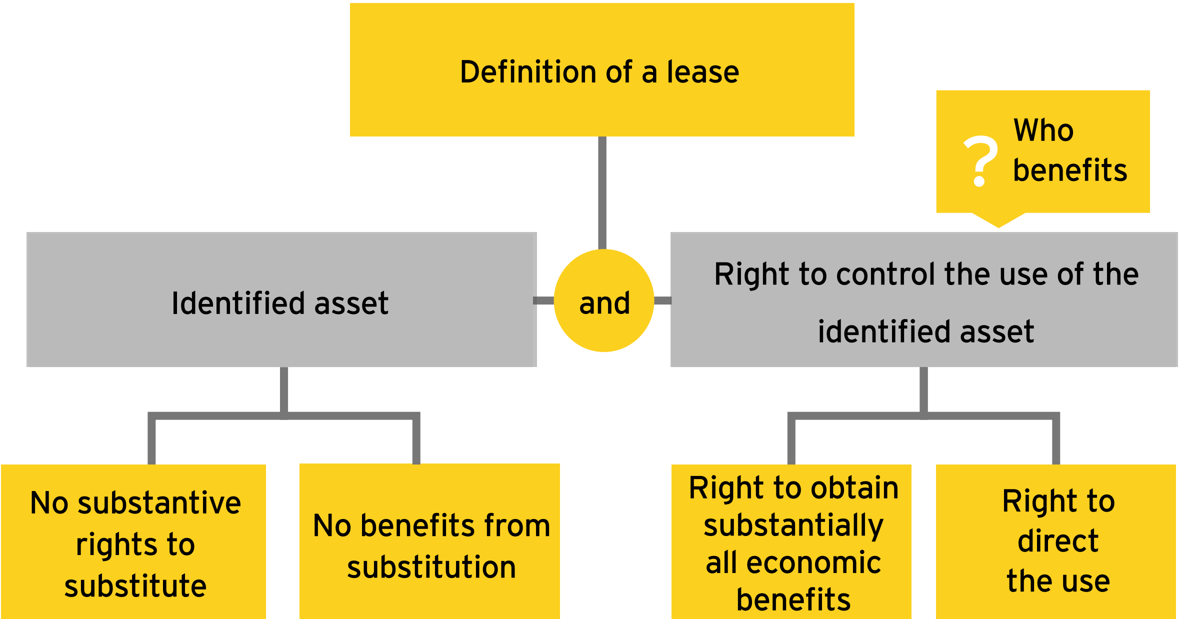
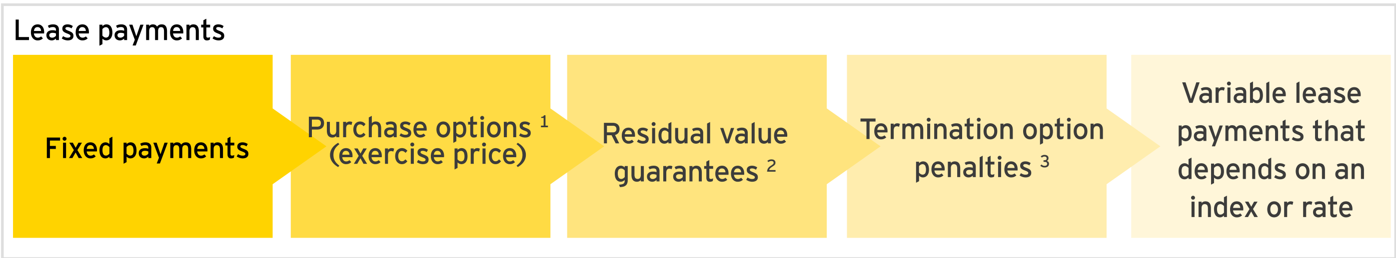
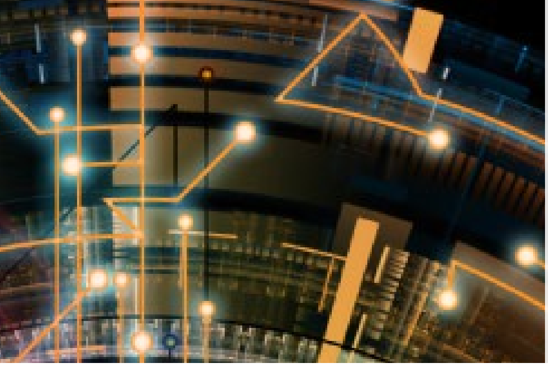


IFRS 16 Leases Roadmap



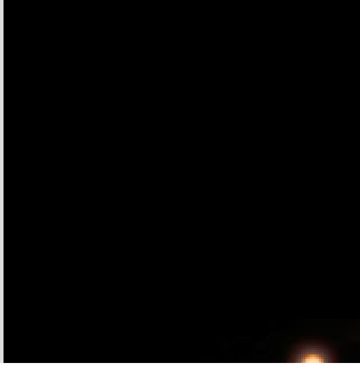


1. Include only if reasonably certain of exercise. 2. Lessees use the amounts they expect to pay. Lessors include any guarantee. 3. Include unless reasonably certain not to be exercised.



Overview of IFRS 16 Leases

- Lessees will have a single accounting model for all leases, two exemptions ('low-value assets' and short-term leases)
- Lessor accounting is substantially unchanged
- Additional disclosure requirements



Lessee accounting – Recognition and measurement

Initial recognition and measurement		Measure right of use (ROU) asset[1] and lease liability at present value of lease payments
Subsequent measurement	**ROU Asset**	Depreciate ROU asset based on IAS 16, or use alternative measurement basis under IAS 16 and IAS 40
	Liability	Accrete liability based on the interest method, using a discount rate determined at lease commencement[2]. Reduce the liability by payments made
Profit and loss		Generally front loaded expense for an individual lease. Interest and depreciation are separated.

Lessor accounting – Recognition and measurement

Many aspects of lessor accounting will remain the same.

Effects on the income statement	Effects on the balance sheet	Effects on the cash flow statement
↑ ↑ EBITDA[3]	↑ Lease assets	↑ Cash from operating activities
↑ Operating profit and finance costs	↑ Financial liabilities	↓ Cash from financing activities
↔ Profit before tax	↓ Equity	↔ Total cash flow

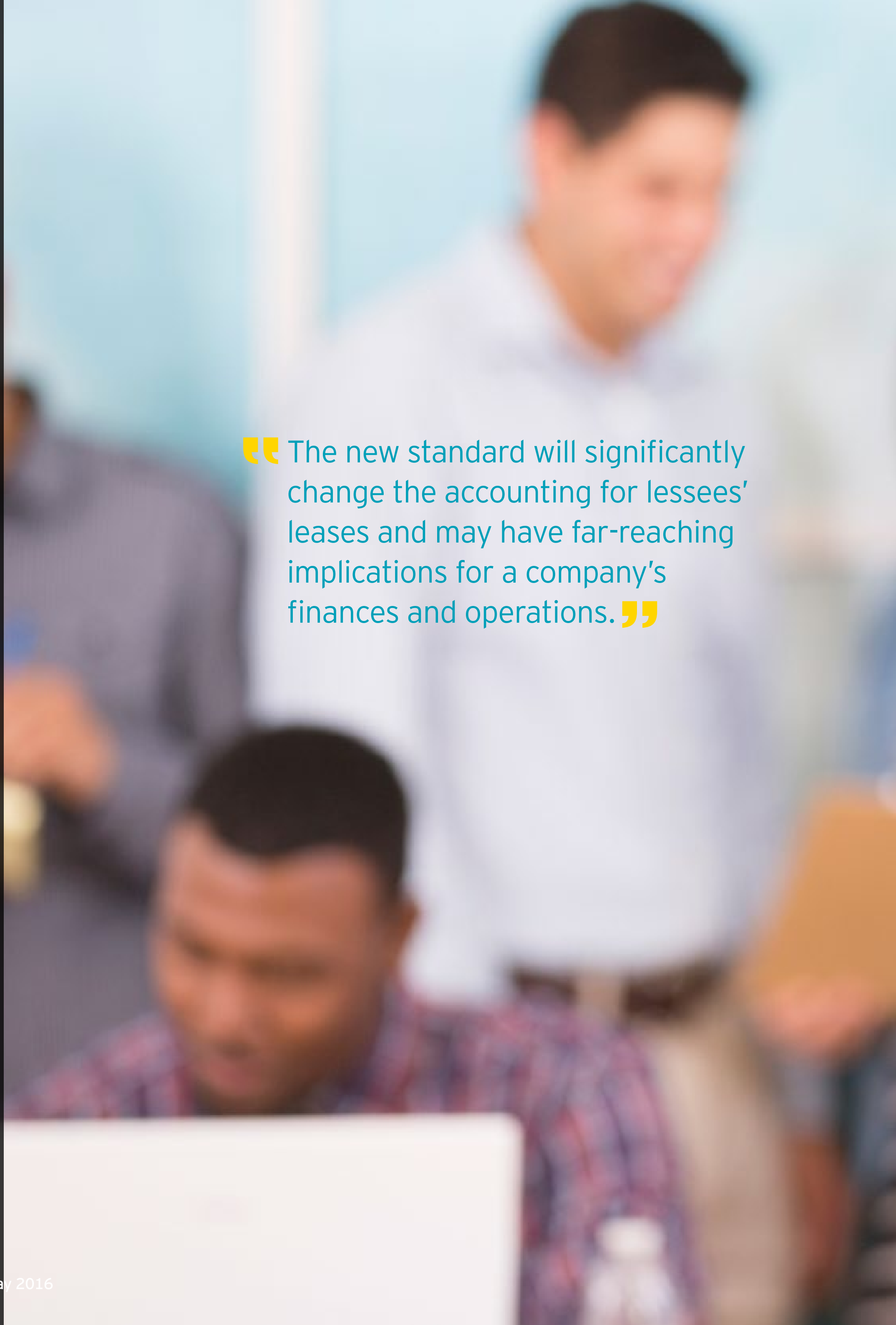
1. Initial measurement of the ROU asset would also include the lessee's initial direct costs; prepayments made to the lessor, less any lease incentives received from the lessor; and restoration, removal and dismantling costs. 2. As long as a reassessment and a change in the discount rate have not occurred. 3. Earnings before Interest, tax, depreciation and amortisation.

Background

The International Accounting Standards Board (IASB or Board) issued IFRS 16 *Leases* (IFRS 16 or the new standard), which requires lessees to recognise assets and liabilities for most leases. For lessors, there is little change to the existing accounting in IAS 17 *Leases*.

The IASB issued its standard as part of a joint project with the Financial Accounting Standards Board (FASB). The FASB has not yet issued its new standard, but it is also expected to require lessees to recognise most leases on their balance sheets. However, the IASB and FASB made different decisions during deliberations, and differences between the two standards will exist (e.g., there would be a classification test for lessees under the FASB's standard).

The new standard will be effective for annual periods beginning on or after 1 January 2019. Early application is permitted, provided the new revenue standard, IFRS 15 *Revenue from Contracts with Customers* has been applied, or is applied at the same date as IFRS 16.



"The new standard will significantly change the accounting for lessees' leases and may have far-reaching implications for a company's finances and operations."

“IFRS 16 requires lessees to recognise most leases on their balance sheets, regardless of the industry that the entity operates in.”

What you need to know

IFRS 16 requires **lessees** to **recognise most leases on their balance sheets.** The new standard is a **significant change in approach** from current IFRS and will **affect many entities across various industries.**

- Lessees will have a **single accounting model for all leases,** with **two exemptions** (low value assets and short term leases).
- **Lessor accounting** is substantially **unchanged.**
- There will be **additional disclosure** requirements.
- The new standard will be **effective** from **1 January 2019** with limited early application permitted.

What is in the scope or affected by the standard?

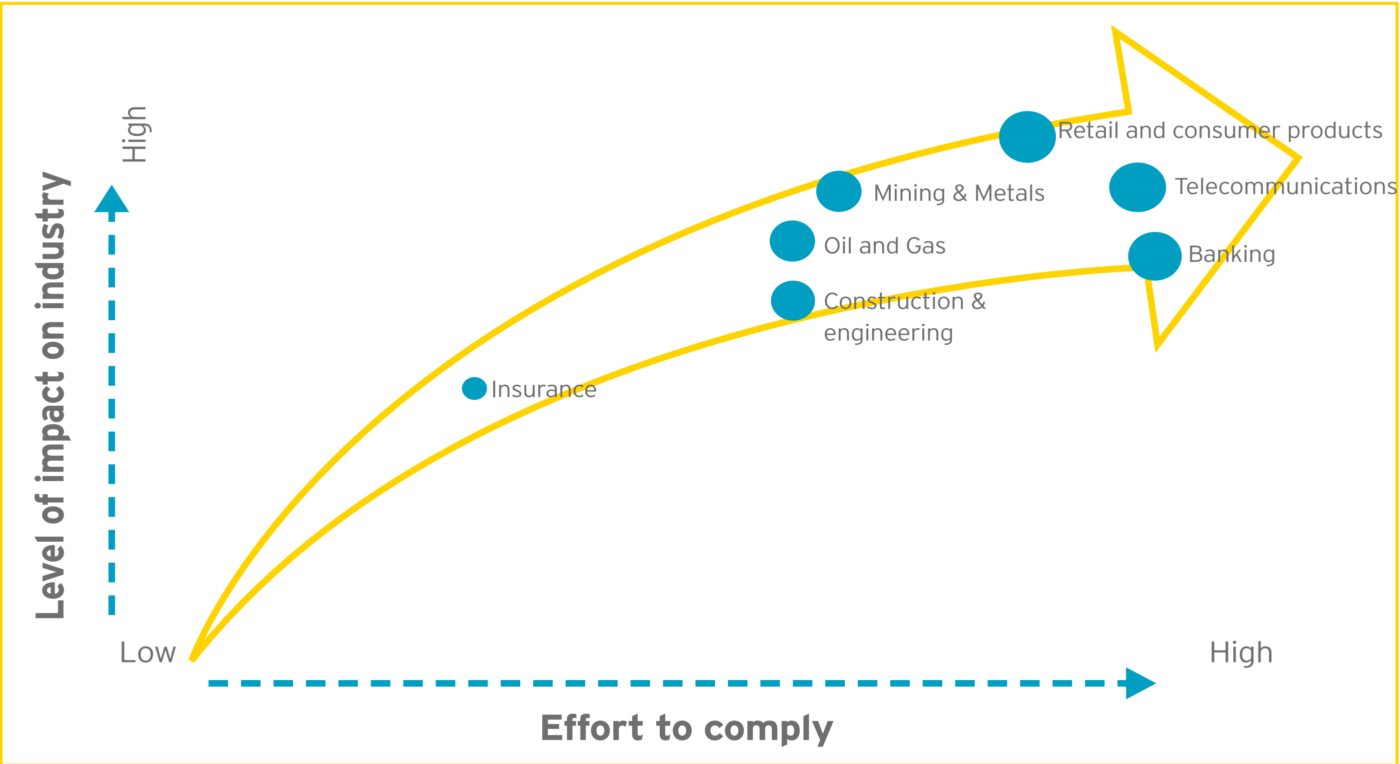
Leases of all assets, except for:

- Leases of non-regenerative resources
- Leases of biological assets
- Service concession arrangements
- Licences of intellectual property granted by lessor
- Rights held by a lessee under certain licensing agreements (e.g. films)

Impact of the adoption of IFRS 16

Industry impact

The following diagram illustrates the potential impact of the adoption of IFRS 16 on specific industries:



Entities most likely to be affected by the changes

The effects of IFRS 16 will need to be assessed on the facts and circumstances relevant to each entity. This will further be impacted by the different capital structures that entities have adopted, for example an entity that typically rents office space, which is being accounted for as an operating lease, will be more significantly impacted than an entity that has purchased office space.

It is expected that certain industries will be more significantly impacted than others. Some of the types of contracts that entities would need to consider include:

Retail and consumer product entities are expected to be most significantly impacted by the changes in the new lease requirements. This is especially the case where leased retail space forms a significant part of the entity's business model. In addition, manufacturing entities will need to consider all the major contracts that they have entered into, such as the rental of manufacturing plants and equipment, distribution centres as well as fleet arrangements that form part of their distribution networks.

Telecommunications entities are expected to be significantly impacted by the new lease requirements. Careful consideration would need to be given to the new definition of a lease to identify arrangements that contain a lease (previously IFRIC 4). Telecommunications will need to consider tower arrangements, signal transmission devices as well as data and fixed line agreements (for example indefeasible right of use (IRU) on fibre lines). Some of these entities have extensive retail outlets, which will require consideration.

In addition, telecommunication entities will need to analyse contracts where equipment is provided to their customers. In such instances, consideration would need to be given to whether the contract contains a lease and if so, how the lease payments should be allocated to products and services provided.

Banking and other financial services entities that have extensive branch networks as well as large administration and call centres will need to consider any lease arrangements carefully. In addition, contracts over ATMs and the related space occupied by such machines will need to be assessed under the new lease standard's requirements. Financial services entities may also make use of data storage facilities and these arrangements with providers could potentially fall within the scope of IFRS 16. Financial service entities will need to monitor how right-of-use assets will be treated for regulatory capital requirements.

Metals and mining entities will need to carefully consider all major arrangements that they have entered into that may give rise to on balance sheet lease accounting under the new leases standard, such as mining equipment, vehicles as well as land and buildings. Mining entities often enter into arrangements that contain a lease (previously IFRIC 4) that falls within the scope of the new standard.

Similarly, construction and engineering entities will need to consider all major arrangements that they have entered into such as leases over construction equipment, vehicles as well as land and buildings, which may give rise to on balance sheet lease accounting under the new leases standard.

Oil and gas entities may be impacted by arrangements in respect of land and buildings, vehicles and equipment as well as arrangements that contain a lease (previously IFRIC 4).

Insurance entities will need to consider all major arrangements entered into in respect of land and buildings, vehicles and equipment that are not currently accounted for on balance sheet.

Determining when a customer has the right to direct the use of an identified asset may require judgment, particularly for arrangements that include significant services. While the new standard provides new criteria for determining whether an arrangement meets the definition of a lease, we expect that entities will generally reach similar conclusions as they do today.

Lessees with existing finance leases and lessors carry over existing balances at the date of the initial application of the new standard (see transition guidance).

Financial statement impact - Before and after IFRS 16

Balance sheet impact*

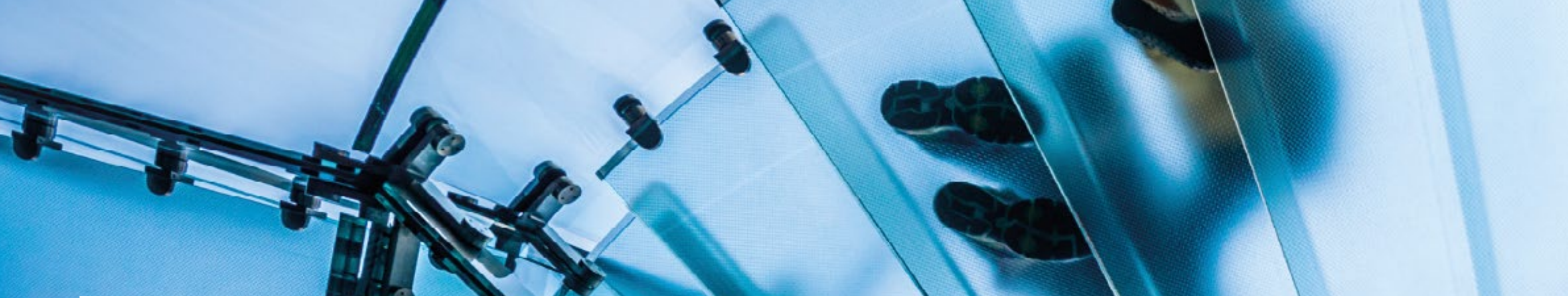
	IAS 17		IFRS 16
	Finance leases	Operating leases	All leases
Assets		—	
Liabilities	$$$$	—	$$$$
Off balance sheet rights / obligations	—	 $$$$	—

* IASB - IFRS 16 Effects analysis

Income statement impact*

	IAS 17		IFRS16
	Finance leases	Operating leases	All leases
Revenue	$$$$	$$$$	$$$$
Operating costs (excluding depreciation and amortisation)	—	Single lease expense	—
EBITDA		—	▲▲
Depreciation and amortisation	Depreciation	—	Depreciation
Operating profit			▲
Finance costs	Interest		Interest
Profit before tax			↔

* IASB - IFRS 16 Effects analysis



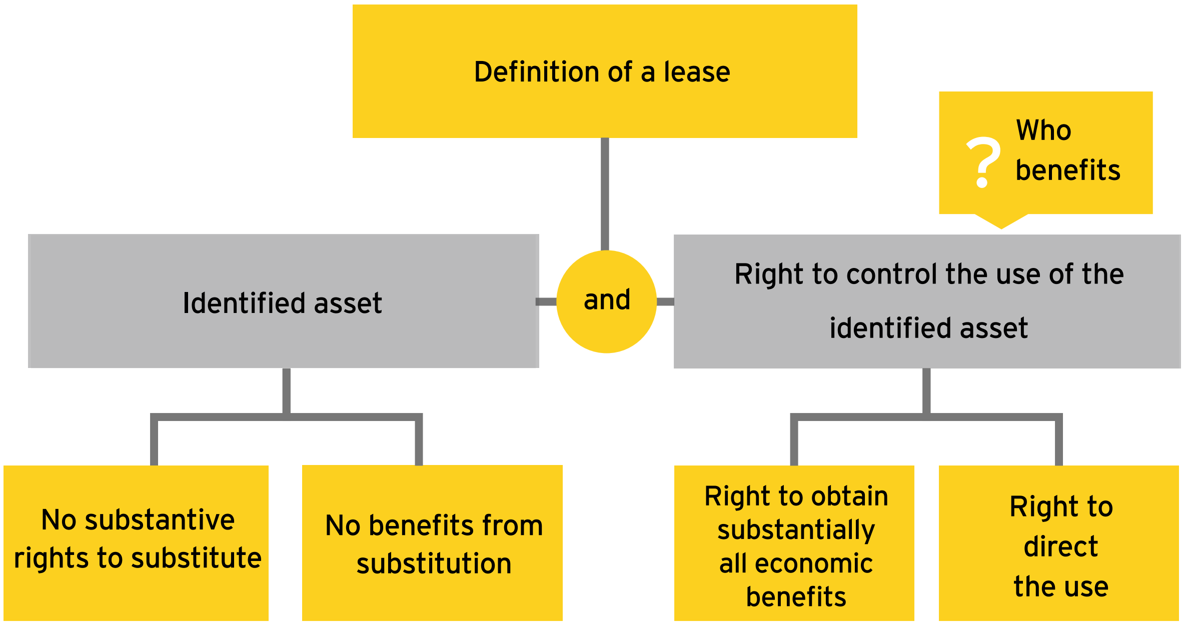
Key principles of IFRS 16

Determining whether an arrangement contains a lease

Under the new standard, a lease is a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration. To be a lease, a contract must convey the right to control the use of an identified asset, which could be a physically distinct portion of an asset such as a floor of a building.

A contract conveys the right to control the use of an identified asset if, throughout the period of use, the customer has the right to:

- obtain substantially all of the economic benefits from the use of the identified asset; and
- direct the use of the identified asset (i.e., direct how and for what purpose the asset is used).



Identifying and separating lease and non-lease components of a contract and allocating contract consideration

Many contracts contain a lease coupled with an agreement to purchase or sell other goods or services (i.e., non-lease components such as maintenance). For these contracts, the non-lease components are identified and accounted for separately from the lease component, except lessees can make an accounting policy election, by class of underlying asset, to account for both components as a single lease component. Lessees that do not make this policy election are required to allocate the consideration in the contract to the lease and non-lease components on a relative standalone price basis. Lessors are required to apply IFRS 15 to allocate the consideration in the contract.

Lessee accounting

Initial recognition and measurement

Lessees are required to initially recognise a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term.

The lease liability is measured at the present value of the lease payments to be made over the lease term.

Lease payments

Fixed payments → Purchase options [1] (exercise price) → Residual value guarantees [2] → Termination option penalties [3] → Variable lease payments that depends on an index or rate

The right-of-use asset is initially measured at the amount of the lease liability, adjusted for lease prepayments, lease incentives received, the lessee's initial direct costs (e.g., commissions) and an estimate of restoration, removal and dismantling costs.

Lessees are permitted to make an accounting policy election, by class of underlying asset, to apply a method like IAS 17's operating lease accounting and not recognise lease assets and lease liabilities for leases with a lease term of 12 months or less (i.e., short-term leases). Lessees also are permitted to make an election, on a lease-by-lease basis, to apply a method similar to current operating lease accounting to leases for which the underlying asset is of low value (i.e. low-value assets).

1.Include only if reasonably certain of exercise. 2. Lessees use the amounts they expect to pay. Lessors include any guarantee. 3. Include unless reasonably certain not to be exercised.

Subsequent measurement

Lessees accrete the lease liability to reflect interest and reduce the liability to reflect lease payments made. The related right-of-use asset is depreciated in accordance with the depreciation requirements of IAS 16 *Property, Plant and Equipment*. For lessees that depreciate the right-of-use asset on a straight-line basis, the aggregate of interest expense on the lease liability and depreciation of the right-of-use asset generally results in higher total periodic expense in the earlier periods of a lease. Lessees remeasure the lease liability upon the occurrence of certain events (e.g., change in the lease term, change in variable rents based on an index or rate), which is generally recognised as an adjustment to the right-of-use asset.

Lessees apply alternative subsequent measurement bases for the right-of-use asset under certain circumstances in accordance with IAS 16 and IAS 40 *Investment Property*. Right-of-use assets are subject to impairment testing under IAS 36 *Impairment of Assets*.

Presentation

Right-of-use assets are either presented separately from other assets on the balance sheet or disclosed separately in the notes. Similarly, lease liabilities are either presented separately from other liabilities on the balance sheet or disclosed separately in the notes. Depreciation expense and interest expense cannot be combined in the income statement. In the cash flow statement, principal payments on the lease liability are presented within financing activities; interest payments are presented based on an accounting policy election in accordance with IAS 7 *Statement of Cash Flows*.

Lessor accounting

Initial recognition and measurement

The accounting by lessors under the new standard is substantially unchanged from today's accounting in IAS 17. Lessors classify all leases using the same classification principle as in IAS 17 and distinguish between two types of leases: operating and finance leases.

For operating leases, lessors continue to recognise the underlying asset.

For finance leases, lessors derecognise the underlying asset and recognise a net investment in the lease similar to today's requirements. Any selling profit or loss is recognised at lease commencement.

Subsequent measurement

For operating leases, lessors recognise lease income on either a straight-line basis or another systematic basis that is more representative of the pattern in which benefit from the use of the underlying asset is diminished.

For finance leases, lessors recognise interest income for the accretion of the net investment in the lease and reduce that investment for payments received. The net investment in the lease is subject to the derecognition and impairment requirements in IFRS 9 *Financial Instruments*.

Factors that impact the complexity of implementation

Less complexity

- Majority of current leases classified as financing
- Contracts <1 year and leases of small assets
- Lease contract data readily available
- Highly centralised operations/ processes
- Contracts do not contain service components
- Lease portfolio contains similar assets, terms and conditions

More complexity

- Majority of current leases classified as operating
- Long-term contracts, such as commercial property
- Lease contract data available manually
- Decentralized operations/processes
- Lease contracts contain both lease and service
- Lease portfolio contains dissimilar assets, terms and conditions

Sale and leaseback transactions

A seller-lessee and a buyer-lessor use the definition of a sale from IFRS 15 to determine whether a sale has occurred in a sale and leaseback transaction. If the transfer of the underlying asset satisfies the requirements of IFRS 15 to be accounted for as a sale, the transaction will be accounted for as a sale and a lease by both the lessee and the lessor. If not, the transaction will be accounted for as a financing by both the seller-lessee and the buyer-lessor.

How we see it

The new determination of whether a sale has occurred in a sale and leaseback transaction is a significant change from current practice. For example, IAS 17 focuses on whether the leaseback is an operating or finance lease, and does not explicitly require the seller-lessee to determine whether the sale and leaseback transaction meets the condition for the sale of the asset. We generally expect fewer transactions to be accounted for as sales and leasebacks under the new standard.

Sale and leaseback - recognition and measurement

Determine whether the transfer of the asset is a sale

- **Apply IFRS 15**
- **Presence of a leaseback does not preclude a sale**

Transfer of the asset is a sale

Seller-lessee will:

- Derecognise the underlying asset
- Recognise the sale at fair value
- Recognise only the gain/loss that relates to the rights transferred to buyer-lessor
- Recognise a ROU asset as proportion of previous carrying amount of underlying asset
- Recognise a lease liability

Failed sale

Seller-lessee will:

- Not derecognise the underlying asset.
- Recognise a financial liability - IFRS 9/IAS 39

Buyer-lessee will:

- Not recognise the transferred asset.
- Recognise a financial asset - IFRS 9/IAS 39

Transition

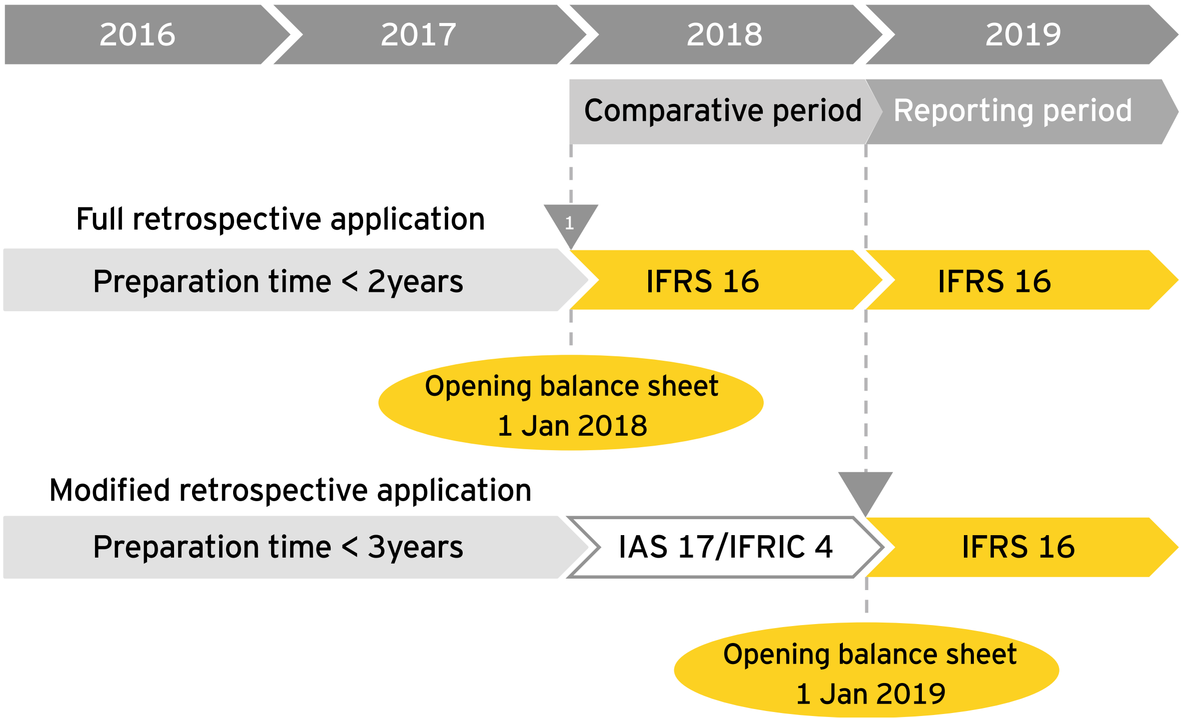
The new standard is effective for annual periods beginning on or after 1 January 2019. Early application is permitted if IFRS 15 has already been applied or is applied at the same date as the new leases standard.

Lessees with existing finance leases and lessors carry over existing balances at the date of initial application of the new standard (except for intermediate lessors in a sublease).

Lessees are permitted to choose either a full or a modified retrospective transition approach for leases existing at the date of transition. Certain transition relief is available under the modified approach.

Disclosures are required in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, with certain revisions.

Early preparation is recommended due to complexity of challenges



1. Assumes one comparative period. Some jurisdictions or regulatory environments may require two comparative periods.

How will your business be affected?

What is the impact for lessees?

For many companies, leases play a critical role in their business operations. However, because most lease transactions (e.g., operating leases) are off-balance sheet today, accounting for leases under current lease standards often does not require a significant effort.

The new standard will require a company to do more than simply convert its existing operating lease commitments disclosure to reflect lease assets and liabilities. Its implementation could result in changes to the policies, processes, controls and IT systems that support lease accounting and possibly lease procurement, lease administration and tax. Companies may also wish to consider the implications for financial statements and metrics as they negotiate contracts that are, or may contain, leases. These activities will require involvement from a variety of departments across the company.

Data collection and ongoing data management

In order to determine what changes are necessary to apply the new standard, much of the preliminary work will revolve around assessing the state of a company's current lease contract data management (i.e., its systems, policies, processes and controls), including the data required for financial reporting purposes.

Companies that already have well-organised lease administration and accounting functions may simply need to evaluate whether their existing systems, policies, processes and controls require adjustments to accommodate the changes in the new standard. However, while existing systems (e.g., spreadsheets and software) may include some lease information, they may not have all of the information required to make the calculations, judgements (including on-going assessments) and information for disclosures necessary to comply with the new standard. As such, significant effort could be required to manually gather missing lease information.

Other companies (e.g., those with lease procurement, lease administration and lease accounting functions that are decentralised depending on the business unit, geographic location, or type of leased asset) could have a challenging journey ahead. For such companies, determining the completeness of the lease portfolio, as well as the accuracy and completeness of the lease data, may require considerable effort.

One example of how the new standard will drive the need for changes in a company's lease data management is the treatment of lease and non-lease components within a contract. For contracts with multiple components, a company is required to identify and separate non-lease components (e.g., operations, maintenance services) from the lease component. Today, many companies may not focus on identifying the distinct components because their accounting treatment (i.e., the accounting for an operating lease and a service contract) is often the same. The new standard does permit, as an accounting policy election, lessees to recognise the lease and non-lease components as a single lease component on the balance sheet, but that would have the effect of increasing the lease obligation on the balance sheet. We expect lessees may find that policy attractive when the non-lease components are not a significant aspect of the arrangement. Therefore, lessees that do not elect to combine lease and non-lease components may need to put robust processes in place to identify and account for the separate components if they wish to minimise the impact of the new standard on their balance sheets.

IT systems, processes and controls

Today's lease-related IT systems are often designed primarily to assist with lease administration, and many are focused on real estate leasing or a lessor's investment in leased assets. However, lessees commonly use spreadsheets to supplement requirements for current lease accounting and reporting because today's lease-related IT systems often lack the capabilities to perform the calculations required for accounting.

To satisfy the new financial statement presentation and disclosure requirements, companies will need to evaluate whether to update their existing systems or to implement a new system. Selecting or updating a lease IT system will probably require input, not only from accounting, but also from the lease administration and IT functions, depending on the company's enterprise resource planning (ERP) environment. When implementing any IT system, it is important to define system requirements and the expectations of relevant stakeholders prior to selecting a vendor.

If a company chooses to apply the new standard on a full retrospective basis, upon initial application, it will be required to restate comparative reporting periods. Furthermore, companies may need to keep separate books for external reporting, local statutory requirements and tax purposes. This will increase the IT system requirements, and may also further complicate processes and controls. Identifying, developing and implementing changes to IT systems are not easy exercises, and the amount of time necessary would depend on the legacy systems in place.

Companies that are presently designing or upgrading IT financial reporting systems would be well advised to consider the new standard as part of their current IT development efforts. This could reduce the risk of costly re-work and redesign at a later date. Companies also should be mindful that although IT programs can help accumulate data and perform calculations required by the new standard, they are not a complete solution; no program can make the critical estimates or judgements required by the new standard.

Accounting policies and manuals

The new standard requires the application of judgement and estimates. For example, evaluating whether an arrangement meets the definition of a lease could require judgement for certain arrangements such as those with a significant service component. The revised definition of a lease could result in some arrangements receiving different accounting treatment compared to current standards. Other key decisions requiring judgement include lease payments and the lease term, including the ongoing evaluations of the lease term and the accounting for lease modifications. While the IASB expects many of the conclusions to be the same under the new standard, many of the judgements and estimates may receive increased scrutiny because lease assets and liabilities will be reported on the balance sheet for most leases.

Also, there are a number of accounting policy elections that may be made, both at transition and for the accounting post-transition, including whether to apply the recognition exemptions for short-term leases and leases of low-value assets. In addition, the new standard allows for certain transition reliefs that, if elected, can help minimise the implementation burden. Companies will need to understand the impact of these options to help them make informed choices as to which elections to make.

Companies will also need to update their policies and manuals, as well as provide education and guidance on the new standard across the organisation, in order to ensure accurate and consistent policies and processes around areas of judgement and estimates.

Lease procurement and negotiation

Under the new standard, lessees will recognise the present value of lease payments over the lease term as a lease liability on the balance sheet. Similar to current accounting, the definition of lease payments excludes certain variable payments, and the lease term includes only those lease term options that are reasonably

certain of being exercised. As such, lessees may reassess their needs when negotiating their lease terms and payments. A higher proportion of variable payments compared to fixed payments or shorter initial lease terms may result in smaller lease liabilities. Some lessees may reassess whether buying an asset would be more advantageous than leasing it. At a minimum, companies entering into new leases today should be aware of the potential impact of the new standard on their financial statements.

Although some of these approaches to minimising the lease liability appear advantageous from a financial statement presentation perspective, lessees should understand that there are certain economic and business risks associated with such approaches. Therefore, companies should consider any changes to their approach to lease contracts in the context of their underlying commercial requirements. For example, a company may consider balancing a lower lease liability from a shorter lease term for a property against the security of longer-term access to the premises. Further, lessors may be hesitant to take on the additional risk associated with variable payments and shorter initial lease terms. While companies should not make economic decisions based on accounting results, they should be aware of the accounting consequences associated with their business decisions.

Financial statements and metrics

For most lessees, the new standard will result in a gross-up of the balance sheet. This could cause a deterioration of debt ratios and return on assets compared with current accounting. Certain regulatory ratios may also be impacted.

A company should assess the potential impact on its financial statements and metrics and evaluate how this may affect the way stakeholders view its financial position and performance. Companies will likely need to educate internal and external stakeholders on the financial statement implications of the new standard. Some companies anticipate the need to better manage the communication of key performance indicators to stakeholders under both current lease accounting and the new standard during the transition period.

In addition, companies should identify whether compensation (e.g., employee bonuses) and debt arrangements should change in light of the new standard. However, renegotiating these arrangements may not be straightforward. For instance, companies may need to evaluate their existing debt arrangements and, if necessary, negotiate with their creditors either to allow for more headroom in covenants or to allow for the continued use of current lease accounting in the covenant calculations. While the continued use of current lease accounting may seem like a good idea, it would require the ongoing burden of maintaining a separate set of books for covenant calculation purposes. Similar considerations should be evaluated if key metrics underlying compensation arrangements are impacted.

Tax considerations

Adoption of the new standard will result in additional tax related considerations. These include understanding the impact of the lease accounting changes on existing tax positions, initial adjustments to deferred taxes and tracking book/tax differences. Companies will need to determine necessary changes to tax-related processes and controls required to identify and track tax adjustments. The impact on taxes will, of course, depend upon the requirements of the specific tax jurisdiction and whether and how they are changed to reflect the requirements of the new standard.

What are the practical implications for lessors?

Although the accounting by lessors is substantially unchanged from current accounting, lessors will have new disclosure requirements.

However, lessors should understand how the new standard could affect their lessee-customers' behaviour. This would help lessors negotiate lease arrangements that meet the needs of their customers. For example, certain lessees may desire shorter lease terms or a larger portion of variable payments in an effort to minimise their financial statement impact. However, shorter leases and variable payments could result in unpredictable revenue for lessors and drive up costs to lessees. Lessees may request that lessors assist them by separately pricing non-lease components to help them to evaluate and minimise the financial statement impact. However, lessors may be reluctant to disclose this information for proprietary reasons. Although a contractually stated price may be the stand-alone price for a good or service, it is not presumed to be for accounting purposes.

Lessons learned

1 **Project structure**

Break the project into manageable stages with clear responsibilities, roles and time lines.

2 **Details are crucial**

Make sure all types of lease are fully understood to give a complete picture of the issues

3 **Beyond finance**

Ensure there is engagement of all stakeholders across the organisation, as this is not just a finance function exercise.

4 **Act early**

Plan for engagement early on, initially with key internal stakeholders, minimising surprises to/from the business later and building a consensus.

5 **Training and awareness**

Develop a clear plan for communication to all stakeholders, including briefing analysts, media and investors, on the impact of the new standard.

6 **Amount of effort**

Do not underestimate the amount of work and resources that will be involved. Systems and data gathering impacts may be significant.

How should companies prepare?

Education

An initial step in preparing for implementation of any new accounting standard is developing an understanding of what's changing. Companies should review the new standard and understand the implications of the changes, including the areas within the company that will experience the greatest impact. It is also important to stay updated for potential changes in interpretation of the new standard that may emerge.

Global companies that report under both IFRS and US GAAP will also need to understand the changes in US GAAP. While a long-standing objective of the project was a single converged leases standard, the IASB and the FASB reached different decisions in some key areas. One of the main expected differences between IFRS and the expected US GAAP standard is lease classification and subsequent measurement. As it relates to lessees, the IASB decided that lessees will treat most leases similar to today's finance leases, resulting in the recognition of depreciation expense and interest expense for those leases. In contrast, the FASB decided to require lessees to classify most leases into two types: finance leases and operating leases. While both types of leases will be recognised on lessees' balance sheets, the expense recognition will be similar to today's finance and operating leases based on the lease classification. Another key difference is that the IASB’s new standard includes a recognition exemption for lessees’ leases of low-value assets (e.g., personal computers, tablets and telephones but not vehicles).

As such, companies that are required to apply both IFRS and US GAAP may be subject to additional costs and complexities arising from maintaining multiple processes and systems to comply with the requirements under each respective standard and to identify the differences when comparing one set of financial statements to the other.

Project team and planning

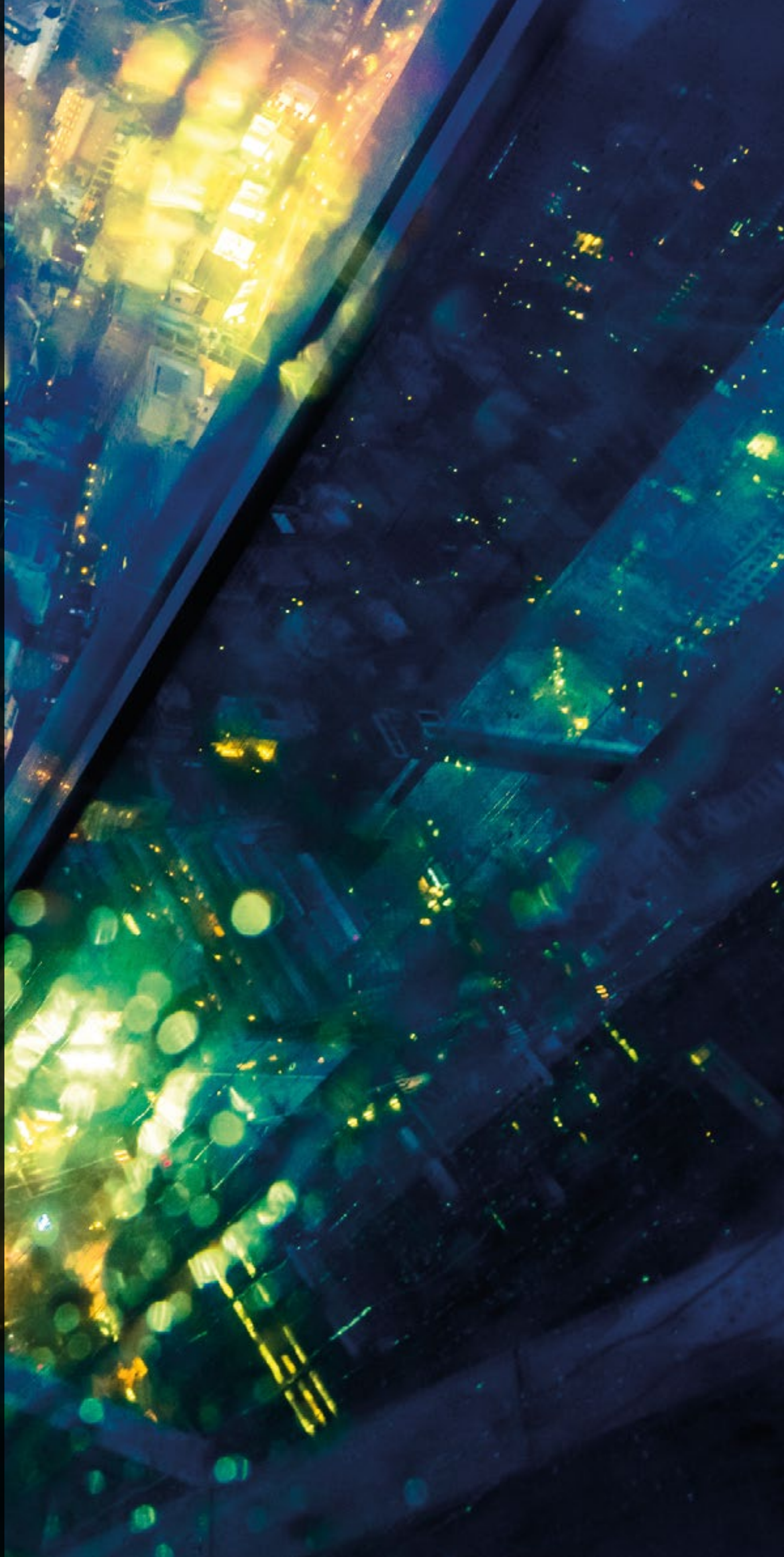
After obtaining an understanding of the new standard, companies should identify a cross-functional team and develop a project plan with effective project management to tackle its implementation. This is unlikely to be a ‘one size fits all’ approach as the nature of leasing activities (i.e., the underlying assets, value and volume of leases), existing policies and processes, financial reporting requirements, and strategic business decisions vary across companies.

Another critical element of planning is ensuring appropriate governance, including seeking input from relevant stakeholders and obtaining an understanding of whether a company wants simply to comply with the new standard or to use this as an opportunity to drive organisational improvements and savings in its leasing activities.

Diagnostic: understand current state and identify changes

Not all aspects of current lease accounting are changing under the new standard. Therefore, companies should assess what lease arrangements exist and the lease procurement, lease administration and lease accounting functions that support these arrangements in comparison with the requirements of the new standard. This will allow companies to determine the extent of the changes that will be required and appropriately design and plan the transition.

As part of the review, companies should consider the policies and systems in place within other departments, including treasury, legal, IT and tax, and understand how processes involving leasing may vary depending on geographies or other differences within the company.



Design, implementation and transition

Implementing the new standard will require companies to determine when to transition. Companies may decide to early adopt the leases standard to align with the transition to the new revenue recognition standard. Once the transition decisions are made and there is a clear understanding of what changes will be necessary based on current state diagnostics, companies can then design the implementation and transition plan.

Preparing for an accounting change of this magnitude presents a considerable challenge. Understanding how the new standard will affect your company is critical. All companies with significant leasing activities should review the new standard and begin thinking about the implications now, as we believe that starting early is the best way to reduce the overall cost of implementation and to avoid unwanted surprises and costly mistakes.

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