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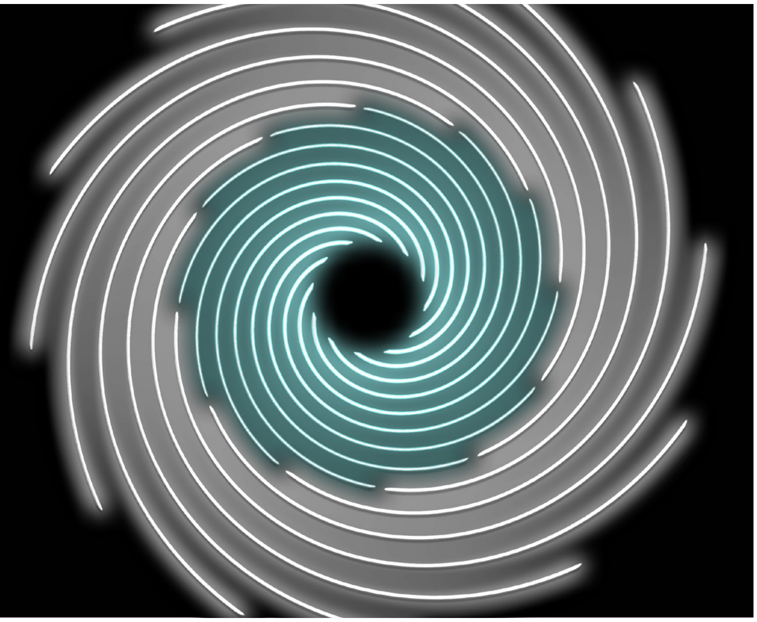
Private

Gearing up for the new lease accounting standard

Choosing an approach and technology platform to meet the new requirements for private companies



For private companies, the new lease accounting standard ASC 842 goes into effect for the calendar year starting January 1, 2021, and time to prepare is quickly running out. Based on the experiences of many public companies implementing lease accounting technology solutions to comply with the new requirements, it often takes longer than anticipated for a new tool to be fully operational. Achieving compliance could be a complex challenge that may require major changes to systems and processes. It's not too soon to act now.

Implementing lease accounting technology to comply with the updated lease accounting requirements may require more work than anticipated. Private companies likely need to revise their internal controls and related business processes for capturing, calculating, and accounting for lease agreements. Depending on the nature and complexity of a lease agreement, up to 100 data elements may need to be captured (some of which are not contained within the lease contract).

Today, many private companies do not have systems or technology solutions to effectively manage lease agreements. Even among those that do, leases are often not administered centrally. In addition, in many cases lease contracts exist only in hard copy—in multiple languages, locations, and currencies—making it difficult to ensure all agreements have been identified and to extract the information necessary for the accounting and reporting requirements under the new standard.

ASC 842 will likely dramatically affect how private companies account for lease arrangements, requiring systems and processes to capture relevant lease data, integrate lease data with business processes, and generate accurate and actionable lease-related information for financial reporting. Doing so means overcoming some obstacles that have emerged as key operational challenges related to implementation:

- Data challenges
- IT systems
- Timeline for adoption

Today, many private companies do not have systems or technology solutions to effectively manage lease agreements.

Potential challenges associated with implementing the new lease standard

1. **Data challenges:** Consolidating and organizing a high volume of data—which may be maintained on a decentralized basis in a variety of systems, formats, currencies, and languages—can be manually intensive, time consuming, and result in errors.
   - Number of new data elements
   - Data housed in various systems
   - Information isn't all in one agreement
   - High volume of data fields
   - Multiple languages/ contracting practices
   - Multiple currencies
   - Lack of resources
   - New analytics or metrics needs
   - Agreements aren't electronic

2. **IT systems:** Current/legacy lease systems may need modifications to address new reporting and disclosure requirements, or completely new systems may be required.

3. **Adoption timeline:** Data abstraction and migration and system implementation are commonly the most challenging and time-intensive aspects of implementation.

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

Choosing an approach

Lease accounting or lease administration?

The first strategic question you may want to consider is whether to limit the scope of the technology solution to *lease accounting* or to pursue a solution that covers the broader scope of *lease administration*. The latter option can offer more benefits and enhancement opportunities; however, it likely will require more time, effort, and investment.

Centralized or decentralized?

Another strategic question to consider is whether to *centralize* or *decentralize* the systems and processes related to leases. A decentralized approach is typically more flexible and responsive to local needs. It tends to be less efficient and consistent, however, and it may require more time and effort to implement due to the increased challenges of coordinating and driving multiple initiatives across organizational and geographic boundaries.

It is important to find a technology solution that fits each company's unique needs and operating model. For example, a centralized model requires a platform that can effectively support a *single global instance*, while a decentralized model might favor a platform designed around a *distributed architecture*.

In-house or outsourced?

A third strategic question to consider is whether to handle lease accounting and related activities *in-house* or to *outsource* some (or many) to a third party. Outsourcing can allow a private company to capitalize on a vendor's deep experience and economies of scale. Insourcing provides more direct, hands-on control, but it requires dedicated resources as well as technical and lease accounting experience.

Choosing a platform/vendor

Another important consideration is whether to use a cloud-based platform (e.g., Software-as-a-Service) or to build and maintain an on-premise solution. The pros and cons are similar to those associated with the outsourcing/insourcing decision. One potential advantage of the cloud in this situation is that software updates tend to be more timely and efficient, making it easier for a company to stay compliant. Many platforms have the ability to support the broader scope of lease administration, not just lease accounting; however, some platforms are more capable and broad than others, so it is important to choose wisely.

It is also critical not to ignore fundamental vendor-selection criteria such as:

- **Financial and technical resources.** Does the vendor have sufficient financial and technical resources to keep its platform and features up to date and viable?
- **Testing and certification.** Has the platform been tested and certified? The requirements of the new lease standard are detailed and highly complex, so it is important to know that the underlying accounting rules are being applied correctly.
- **Total cost.** What will be the platform cost to implement and operate on an ongoing basis? To make a more informed decision, all expected costs should be considered, including first-year implementation expenses, annual licenses, and maintenance fees.

Other factors to consider include ease of integration with current systems, the implementation timeline, anticipated release of required functionality, and the ability to customize the technology solution to your private company's needs.

If a vendor is gaining popularity in your industry, it may be a sign that its platform is a good fit; however, that does not replace the need to conduct your own careful selection process.

Choosing an interim solution

Companies may benefit most from a comprehensive, fully integrated platform for lease accounting (or lease administration, which is even broader). However, depending on the complexity of a company's needs—and in which stage of the decision process it is—there might not be enough time to fully implement such a platform before the new lease accounting standard adoption deadline. As such, some companies may need to implement a temporary technology solution that can promptly satisfy the new standard's minimum reporting requirements by layering on top of existing systems and processes.

When implementing an interim solution, it is recommended companies strive to reduce duplication and rework. Thus, data portability should be a top priority. Cleansing and extracting lease data from existing systems and processes is typically the most time- and resource-intensive step of achieving compliance; therefore, it is a good idea to attempt to do it only once. That means extracting all the information necessary for the long-term technology solution, not just satisfying the immediate needs of the interim solution. It also means choosing an interim solution that allows data to be promptly and efficiently transferred to other platforms.

Taking action now

The time available to achieve compliance with the new lease accounting standard is less than many people realize. For private companies, the new standard goes into effect for the calendar year starting January 1, 2021; however, the required systems and processes should be up and running well before that date to allow sufficient time for testing, training, and debugging.

Private companies should consider promptly developing a clear strategy and timeline for achieving compliance—and then aggressively managing their efforts against that timeline.

The clock is ticking, and there's no time to lose.

Trends come and go, but nothing should matter more than how well a platform fits a private company's unique needs.

Let's talk

For additional information regarding the above and other interpretative guidance related to the new lease standard, contact:

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