



## **Top 6 Tip for Lessors to Prepare for New Lease Accounting Rules**

New lease accounting rules passed by the U.S. Financial Accounting Standards Board (FASB) will become effective starting after December 15, 2018 for public companies and after December 15, 2019 for private companies. Companies should use the time wisely to prepare for the transition. Read below for tips for what equipment finance companies should be doing now to prepare.

### **1. Get up to speed on the new rules.**

The more knowledgeable you are about the new rules, the stronger position you'll be in to prepare for the change and educate your stakeholders about what's coming. Your ELFA membership provides access to the most current information and updates on the final rules. Take advantage of the latest resources from the association, including:

- [Recording of one-day workshop on March 2, 2016](#)
- [FAQs and other tip sheets on the ELFA website](#)
- Informational resources for your customers on ELFA's [Equipment Finance Advantage website](#)
- Information about the new rules at [ELFA events](#)
- [Recording of February 2016 webinar](#)

### **2. Educate your dealers and vendors about the new standard.**

Emphasize the fact that there is no revenue recognition impact for Operating Leases, regardless of the finance provider. Get talking points for your dealers and vendors from the ELFA whitepaper, "Changes in Lease Accounting: The Benefits of Equipment Lease Financing Remain."

### **3. Educate your sales team about the rules.**

Make sure your sales people know key points about the new rules, so they may converse with customers about the changes. The most important point for lessees to understand is that the many business benefits to leasing will remain intact under the new rules, including flexible terms and structures, cash flow and tax benefits, and avoiding ownership of obsolete equipment. Your customers may not realize that the financial impact of capitalizing operating leases is minimal and that it is still important that the lease is classified as an operating lease. The impact of the new rules should be minor and may in fact lead to new product opportunities. Get talking points for your sales team from the ELFA whitepaper, "Changes in Lease Accounting: The Benefits of Equipment Lease Financing Remain."

### **4. Educate your end-user customers about the rules.**

Maintain a dialogue with your customers to help them prepare for the new rules. Start by suggesting they make an inventory list of all equipment lease and rental contracts, and provide the following guidance:

- **Bank relationships:** We expect no change to credit lines and minimal impact to covenants, but they should review their covenants under the new rules and talk to their lenders if there are issues.
  - **Auditors:** Suggest they get advice and guidance about the support they can expect and how the new rules will impact their P&L and balance sheet.
  - **IT systems and software providers:** They can help your customer understand the consequences for both proprietary and third-party systems and software.
- Get more tips for educating end-users from the ELFA whitepaper, “Changes in Lease Accounting: The Benefits of Equipment Lease Financing Remain.”

## 5. Address internal consideration

The FASB made few changes to lessor accounting. The key ones are:

- The definition of initial direct costs was changed to eliminate internal costs.
- Full-service lessors must bifurcate the lease and service components of bundled billed leases.
- Sale leasebacks with fixed purchase options will need to be carefully structured to avoid “failed” sale leaseback accounting (basically a financing).
- Sales type leases needing third-party residual insurance will not be afforded up front gross profit recognition.
- Leveraged leases are eliminated but existing deals are grandfathered.

You should understand the new rules and consider how the new rules will impact your company internally (including operations, staffing, accounting policies, education and underwriting). Understanding the proposed rules and their application will support compliance across the enterprise, from sales generation to internal and external reporting. Here is a suggested timeline:

- **2016: Phase 1 – Planning** During this phase lessors should assess the overall impact of the project and develop an implementation strategy.
- **2017: Phase 2 – Conversion** This includes evaluating the impact of new rules, developing new policies, revising contracts and marketing materials, determining accounting and servicing system changes and executing on those changes, modifying work streams and processes, training staff, etc. You may find opportunities for new products or product modifications.
- **2018: Phase 3 – Implementation** This is the “go live” phase when all changes are incorporated into day-to-day operating activities

Collaborate with your internal accounting standards groups, internal and external auditors, regulators and software providers up front on how the new rules will be applied in order to mitigate costs in the future. In addition to accountants, underwriters and businesses will need to revise contracts, adjust projections, monitor covenants and manage internal budgets accordingly. Costs to support estimates need to be considered in the pricing of transactions along with staff time to document the technical accounting decisions made to support these transactions.

**6. If needed, engage professional help**

You may need to hire consultants with specialized skills for technical knowledge, process documentation, control compliance and system development, etc., as well as temporary help to research lease documentation and perform restatement analyses. Resources to evaluate transition decisions will be needed, due to the short time frame to gather historical data. Also, changes in lease contracts will need to be addressed early for legal compliance jurisdictionally. For more on this topic, read “Considerations for the Implementation of the New Lease-Accounting Standard: Internal Preparation for Lessors: Part One of a Three-Part Series,” from the Jan/Feb 2016 Equipment Leasing & Finance Magazine.

**More information:**

To learn more about this topic, visit the Equipment Leasing and Finance Association’s Lease Accounting webpage at [www.elfaonline.org/industry-topics/lease-accounting](http://www.elfaonline.org/industry-topics/lease-accounting).

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