



# IFRS Today

KPMG's podcast series on IFRS and financial reporting

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## EPISODE 10 TRANSCRIPT

### Preparing for the new leases standard – What should your priorities be?

#### Speakers

- Ruben Rog
- Dan Bealing
- Julianna Obal
- James Bowe (Host)



Dan Bealing  
Senior Manager  
Management Consulting  
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#### Host

Hi – and welcome to episode 10 of *IFRS Today*.

It's now just six weeks until the new leases standard becomes effective. In this podcast, we look at where realistically the average company should be with their preparations and what they should be prioritising.

Today I'm delighted to welcome three KPMG colleagues – here to offer some insights. First up, Ruben Rog – a partner in the Dutch firm who delivers technical accounting advice to companies globally on applying IFRS 16. And Dan Bealing and Julianna Obal from KPMG in the UK. They've both been helping companies implement the changes.

Thank you all for joining us on *IFRS Today*...

So, Ruben – to kick off, just how prepared are companies for IFRS 16?



Julianna Obal  
Manager  
Accounting Advisory Services

#### Ruben

Well, James, I see that a lot of companies still have a lot to do to get compliant by the end of the year.

A lot of the December year-end companies have realised that getting compliant is one thing but then embedding all of the systems and processes after that will take much more time.

So for those companies that are working under strict reporting deadlines, they will only have a few weeks to accomplish all of that in January – if they haven't done so already. Those not reporting on a monthly or quarterly basis can spend some more time in 2019 getting ready for 'business as usual'.

## James

Okay, thanks, Ruben. How would you summarise the main concerns that you're hearing from clients?

## Ruben

I would say I'm hearing three main concerns...

- The first one will not be a surprise. It has to do with having the correct and complete data to make necessary calculations for IFRS 16.
- And then secondly – once you have the data – you need the system to put the data in that makes the calculations for you for IFRS 16. And we have found that not all ERP systems have an 'out of the box', easy-to-implement solution. So some of the larger companies are actually looking at stand-alone systems that could take a number of months to implement.
- As a fall-back scenario some are also looking at spreadsheet-based work-arounds to get compliant by 1 January.
- Then there's a third point... Besides data and systems, there are obviously some technical points, as with any new standards, that have to be dealt with. And an important one for IFRS 16 is getting the discount rate right... The new standard doesn't say much about this but it is a big issue for lessees. So the accounting and treasury teams really need to sit down to determine the discount rate for the leases.

## James

Thanks, Ruben. Now, Dan and Julianna, what's your experience been in terms of data capture and systems implementation?

## Dan

Well, James, I'll start with data capture – because that's crucial to getting the initial lease accounting entries right. You could have a top-of-the-range system and solution set up but, without the complete and accurate lease data, your initial lease accounting entries will not be correct.

Some companies think they've already captured all of the data they need, but on closer inspection this is not always the case. IFRS 16 is asking organisations to collect new data, particularly for leases that were operating leases under the old standard.

## Julianna

I agree, Dan. So when I think about what the new lease accounting standard requires, for certain transition options, the data library needs to be capturing the history for every lease contract. And that's the full history, not just the most current version of the lease. We've seen some leases where this means finding contracts that date all the way back to the 1920s. And for companies that have international operations there's a few other things to consider: their contracts could be in multiple locations, formats or even languages!

## Dan

That's right, Julianna, so in order to tackle this, organisations really need to have a good view of what their contract landscape looks like as a first step and locate where all of the contracts are physically and electronically positioned. Once they've got this complete list of leases, then for each lease they are going to have to extract data points.

This should not be underestimated! On some projects I've seen, there are up to 100 data points being collected for each contract. So if you were going to do this process manually, this could take two to three hours per contract to collect that data. In addition, you need to make sure that data is collected accurately. So, for example, if you've got 100 contracts, then that could equate to 300 hours of work or just over eight weeks.

## Julianna

So remember, Dan, it's not just about pulling dates and payments from the lease contract. IFRS 16 is also asking us to make some really complex judgements, thinking about business and market factors that'll impact the lease. Companies need to be allocating these complex judgements to the people who have the right knowledge – and that's both centrally and in divisions.

Some lease accounting choices are best made at the top level, so that you get consistency of application across the group. In this category, you might include decisions like whether to apply the short-term and low-value lease exemptions, or practical expedients.

## Ruben

Julianna – I think this also would refer to my earlier point on discount rates. Would you agree? I mean, if you have a central group treasury function, I would clearly expect them to be involved in this?

## Julianna

Yes, absolutely. But I would remind everyone to think about incorporating accounting teams in that decision. While treasury functions would have a great position to calculate discount rates, they would need help from the accounting team to understand the specific risks that are included in the discount rate under IFRS 16.

Now that brings out a great point that some accounting judgements will need to be made on a lease-by-lease basis. Particularly tricky judgements here will include: spotting leases that are embedded in service contracts, determining the lease term and separating components of a contract.

So let's take the lease term, for example. The lease term is often determined based on both terms of the contract and market- and asset-specific factors. This means the process of extracting data needs to be a team effort and it should include people with a technical accounting background but also people with an operational background. It's also really important that those tasked with data collection are properly supported and trained.

## James

Right. Thanks, Julianna! So, Dan – once all this data is captured and those key judgements have been made, what would you say the next step is for companies?

## Dan

So, James, companies will have all the data but then it needs processing and calculations for the accounting postings need to be done. So companies will need to figure out what solution they're going to use to actually do this.

Some have already decided on what solution they are going to use. But for those who haven't, there are many options on the market. These fall into two main areas, which are:

- you can have your lease management system which manages the whole end-to-end lease lifecycle and also does the postings that are required for IFRS 16; or
- just an accounting engine that doesn't do the lease management but just calculates the postings that should be made.

Whilst all this is going on – data collection and systems implementation – companies need to keep in mind their project timelines. From what I've seen, implementation can take three to six months to complete. So, if there's not enough time to complete, a Plan B should be considered to make sure that the organisation remains compliant in time.

## Julianna

That's a great point, Dan. And I think it really highlights the importance of project management being a part of accounting change projects. Having a clear transition plan with detailed steps, responsibilities and timelines is going to be really important and can really speed up progress. It's also a great way to flag potential risks.

## James

Okay, so it sounds like getting the right data into a system has to be the main focus for companies before 1 January. But for those companies that are further along the road, is there anything else they should be thinking about?

## Dan

Yes, there certainly is, James. They need to consider all the processes that need to be set up to support that data and system solution that is going to be implemented.

Many new processes will need to be designed and maintained on an ongoing basis and these will be to support the data entry into the solution and then the data that comes out of the solution that are posted into ERP systems.

Organisations should primarily focus on setting up a compliant process first and then aim to make this more sustainable and efficient later.

## Julianna

Yes, that's right, Dan. So this might mean that at first, you've got manual workarounds for processes that could be made more efficient or automated later.

## James

Thanks, Julianna and Dan. Now, Ruben – what would you say companies need to be thinking about in terms of managing stakeholder and market expectations?

## Ruben

Yes, the point on expectations of stakeholders is an important one – internal and external stakeholders. So the leases standard brings some significant changes – in terms of balance sheet reporting but also EBITDA reporting, and a big part of the challenge for companies will be to keep all stakeholders in the loop during the transition so there are no surprises.

We also know that regulators are expecting all companies to disclose the impact of IFRS 16 in 2018 financial statements and this is based on the requirements in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. So for example ESMA, one of the European regulators, has made this pretty clear in one of the [enforcement priorities](#) it issued this year.

So whatever the impact is, it makes sense to think hard about the needs of your outside stakeholders – such as investors, banks and lease providers – who may all have expectations that are impacted by IFRS 16.

I would therefore strongly encourage everyone who hasn't started yet to make this a priority, because we see the timeline for a successful implementation easily taking up to six months.

## James

Excellent, thank you, Ruben, Julianna and Dan...

Now, there's a lot to consider here... And if you're looking for more insight on this and other leases issues, take a look at the [topic page](#) on our website or follow [KPMG IFRS on LinkedIn](#).

Finally, thank you all very much for taking the time to listen to our podcast. And look out for our next episode, which will be released in the coming weeks.

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