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CBRE
REAL ESTATE INSIDER

QUARTERLY REAL ESTATE UPDATES FOR BUSINESSES AND CORPORATIONS

NEW LEASE ACCOUNTING STANDARDS: WHAT COMPANIES NEED TO KNOW

BACKGROUND

- Sweeping changes to lease accounting have been finalized. To varying degrees, these changes affect all global companies, across all industries.
- The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB), collectively the "Boards," have now separately issued new standards that will move virtually all leases onto the balance sheet

COMPANIES WILL NEED TO...

- Record ALL leases (including real estate) on their balance sheet, except leases of 12 months or less.
  Include rent to be paid in option periods "reasonably certain" of being exercised in the amount recorded on the balance sheet.
- Reassess over the term of the lease whether an option previously not "reasonably certain" of being exercised has become "reasonably certain" or vice versa.

TIMING

- 2019 for public companies and 2020 for private companies
- Companies can early adopt at any time.
- Existing leases will not be grandfathered and leases executed today will impact an occupier's financial statements because they must restate comparative periods in financial statements issued after the effective date.

CBRE/PWC SURVEY RESULTS: HOW DOES YOUR COMPANY COMPARE TO YOUR PEERS?

- 70% plan to begin implementing the new leasing standard in 2016, including 29% who have already started.
- 8% expect to change their lease vs. own strategy for real estate, while 68% see no change being made.
- 10% expect to reduce their average lease term.
- 2% anticipate reducing the amount of square footage leased.
- 50% plan no changes to their average lease term or square footage leased.
- 26% anticipate a longer process to obtain approval for a material lease, while 43% expect no change.
- 68% rely primarily on spreadsheets to track leasing data.
- 10% have selected a software solution to accommodate the new standard.

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FAQ:

Q: Occupied space will be on the balance sheet, so why not own?

A: While some companies may find ownership compelling for assets they fully occupy, for those occupying space in a multi-tenant facility, the possibility of "owning" the asset is usually not an option—even if it makes sense on paper. Condominiumizing (as it is known in the U.S.) multi-tenant buildings is not expected to widely occur as a result of the new standards because it is burdensome and costly to landlords. Additionally, the benefits to an occupier of taking an ownership position in a multi-tenant building will most likely be outweighed by the risks and limitations.

Q: What can Landlords expect leading up to and upon implementation of the new standard?

A: (1) Greater corporate scrutiny of real estate portfolios, (2) Occupiers requesting a greater number of lease scenarios, (3) Possible trend towards triple-net leases, (4) Increased interest in self-funding tenant improvements, (5) Increased interest in the prospect of owning rather than leasing space, (6) Possibility of occupiers considering shorter lease terms to minimize the impact to their balance sheet, (7) Greater spotlight on workplace strategies

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