Eight years since it was first floated, the International Accounting Standards Board (IASB) has announced that it will issue its definitive guide to the new lease accounting standards in Q1 2016. **Come 2019, all companies reporting under IASB will need to comply.**

The US accounting standards board FASB will be issuing their own lease standard in Q1 2016 and although there is agreement between the Boards on a number of issues, there is a significant divergence on the income statement treatment of new leases – so there will be two different standards. Find out more on the FASB standards update [here](#).

**Will your company be impacted?**

The IASB revisions will impact all companies that have leases (for real estate or equipment) and that file financial statements.

This includes public companies, private entities, and non-profit organisations. The changes will most dramatically increase the obligations that must be reported by retailers, leisure operators, banks and other companies that rely heavily on leasing for their operations.

The changes will not create new financial obligations for companies, but they could impact financial ratios, such as return on assets.

**For real estate occupiers under IASB the impact is potentially huge**

Leases will become a key feature on company balance sheets. Given the decisions made by the IASB to date, we know:

- All leases will come on to balance sheets, effectively **inflating assets and liabilities**
- The **income statement treatment** of a lease will be different to the actual cash rent being paid
- The income statement impact in the early years of any lease will be higher than currently – **depressing profits**
- It will be a **significant administrative burden** for companies to collect the data and calculate the impact

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### Items Requiring Balance Sheet Inclusion (in 2019)

**Include:**

- Rent Payments
- Non-cancellable term
- Fixed Rental Uplifts
- Based on Rate or Index
- Residual Value Guarantees
- Term Penalties
- Initial Direct Costs
- Decommissioning Costs

**Exclude:**

- Performance/Turnover Rent
- Operating Expense
What will businesses need to do?

We should see business seeking:

- **Shorter term leases** – to reduce the balance sheet and profit impact on their financial statement

- **More turnover rents** – to the extent the rent is uncertain then it will not need to be recognised on balance sheet so rents that are a percentage of turnover could be very attractive to retailers

- A move towards ownership of property – given there is no off balance sheet advantage of leasing

Given long-established funding and investment structures we are unlikely to see changes overnight. Many companies may take the view that their cash position doesn’t change. Private companies, for example, who do not have the pressure of shareholders or analysts to contend with, may be indifferent to the changes.

But JLL advises most companies to begin to take action by:

- Analysing the impact of their leased property portfolio on their financial statements

- Evaluating alternative strategies to reshape their portfolio

- Identifying how they are going to collect the information and prepare for implementation

What is the impact on Investors?

The most forward thinking investors may change their approach to try and capitalise on the changes and create leasing deals that are more appealing under the new standard.

We may potentially see:

- A growth in serviced offices and co-working – not only does it create greater flexibility but its initial balance sheet impact is limited

- An end to rents with fixed uplifts – they represent the worst of all worlds under the new standard

- The development of a suite of sale and leaseback offers including strip income, ground rent and turnover rent products – since leases are all on balance sheet, a range of structures may be developed to meet occupiers’ objectives

**Own versus Lease**

The criteria for deciding whether to lease or own property may be re-examined by several large corporations. With the new standards, balance sheets will grow for most companies, and the changes will eliminate some of the financial benefits of leasing.

Of course, decisions to own or lease properties are based on many more variables than accounting rules alone. Economics, portfolio flexibility, and operational requirements should still be the primary drivers. However, the new changes could potentially shift the balance toward ownership.

JLL will continue to produce reports on the IASB standards as more information becomes public. We also have teams available for more detailed analysis of the new accounting standards and their impact on your real estate portfolio.

For more information contact:

- **Michael Evans**
  Head of UK Corporate Capital Markets
  +44 (0)20 7399 5575
  Michael.Evans@eu.jll.com

- **Nick Compton**
  Head of EMEA Corporate Capital Markets
  +44 (0)20 7087 5340
  Nick.Compton@eu.jll.com

- **Daniel Miller**
  Director of Corporate Capital Markets
  +44 (0)20 7399 5368
  Daniel.Miller@eu.jll.com

For more information please see the JLL Lease accounting changes website