Top **6 Functional Requirements** for Day Two Compliance and a Lease Accounting Solution
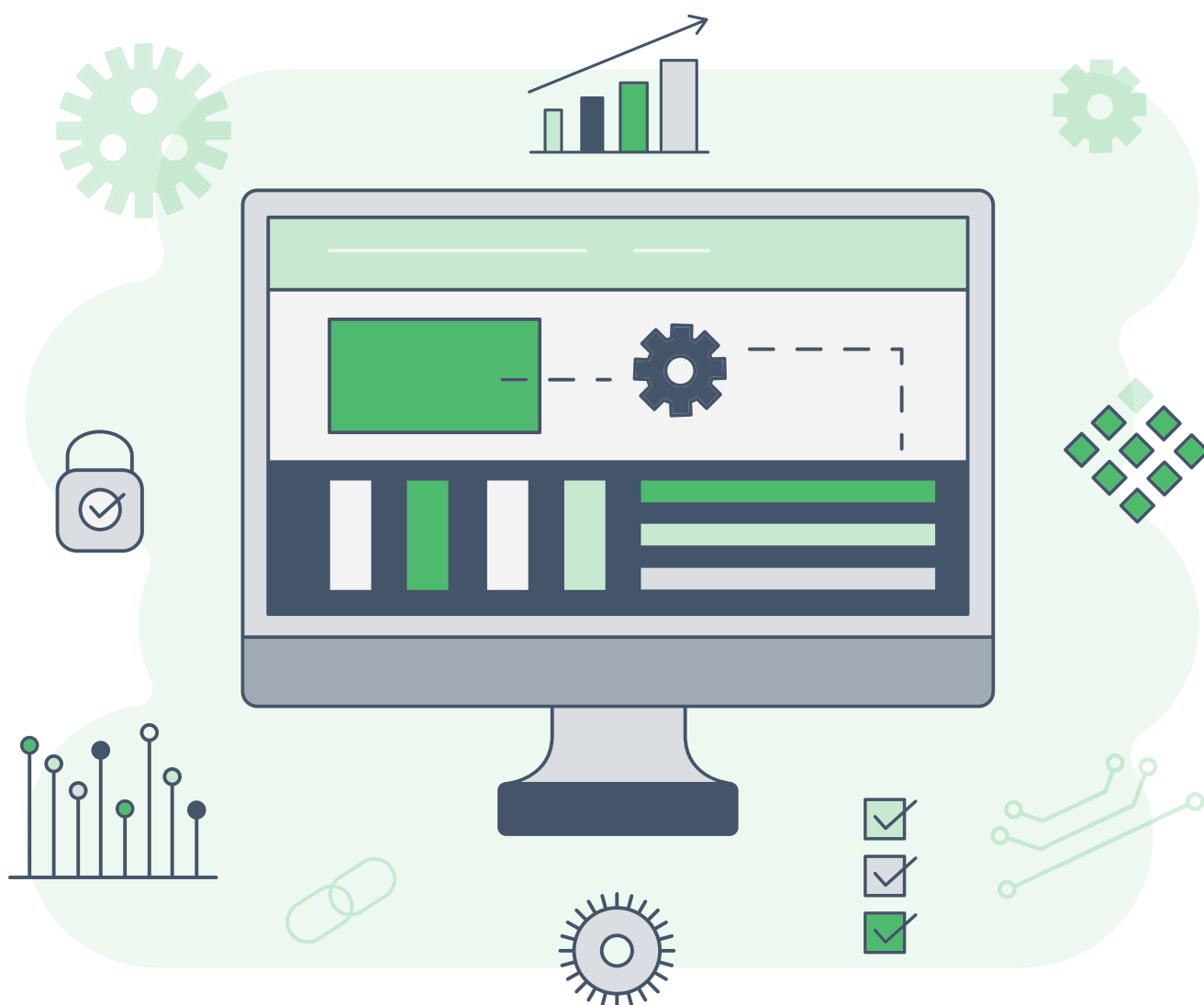
NAKISA®

Top 6 Functional Requirements for Day Two Compliance and a Lease Accounting Solution

In September/October of 2019, PricewaterhouseCoopers (PwC) conducted a lease accounting survey among over 900 finance professionals. The data resulting from this survey revealed significant insights regarding the road to compliance under both ASC 842 and IFRS 16 standards.

Of the professionals polled, 79% reported their title as CFO, controller, or finance/accounting director or manager, and disclosed a variety of business backgrounds which, together, painted a full picture of a pre- and post-adoption landscape populated by both private and public companies alike.

Organizations expressed a mixture of preparedness and lack thereof, with a few respondents reporting having selected a software vendor to help them over the finish line. A theme of "struggling to meet the deadline" emerged from those surveyed in the private sector—a trend that was also observed with public sector behavior a few years ago.
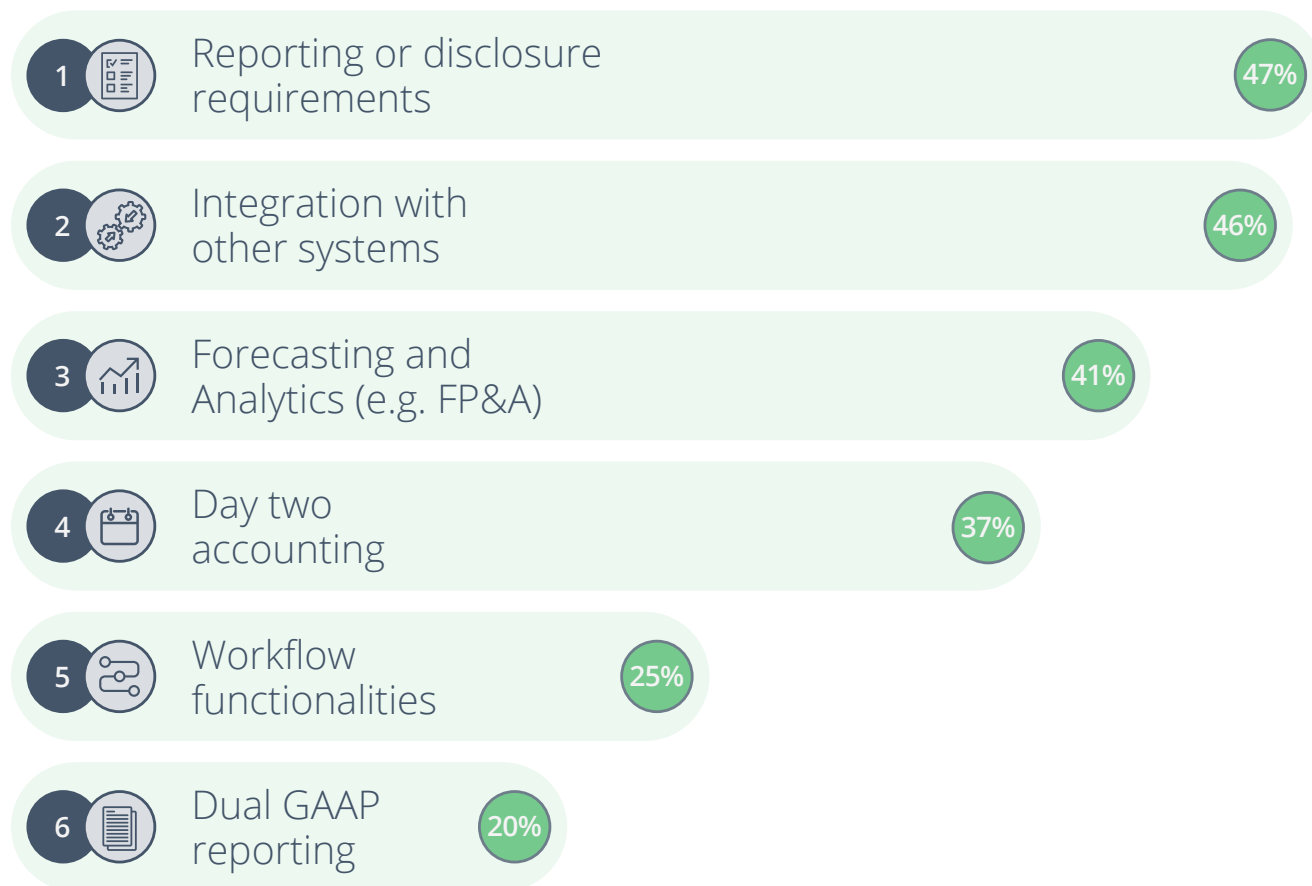
The Never-Ending Battle for Compliance

For public companies, of course, the rush to meet the compliance deadline is over. While many have already been "live" under the new standards for a few quarters, it's interesting to note that according to the PwC survey, as many as 54% of public companies are still working on lease accounting system implementations, while 31% are seeking alternatives in the hope of enhancing their existing system.

The 2019 PwC survey revealed that while some companies reported relying heavily on manual processes alongside limited desktop applications (such as Excel) to compile their leasing data and begin reporting, alternatively, many organizations chose to work with software vendors. Surprisingly, the PwC survey reported that 70% of those companies who adopted software for their lease accounting purposes still required some manual workarounds when using the tool, and only 18% reaped the benefits of a turnkey reporting solution. The PwC survey identified the top six gaps in IT lease accounting solution functionalities:

Top missing functionalities in lease accounting IT solutions:

1. Reporting or disclosure requirements — 47%
2. Integration with other systems — 46%
3. Forecasting and Analytics (e.g. FP&A) — 41%
4. Day two accounting — 37%
5. Workflow functionalities — 25%
6. Dual GAAP reporting — 20%

Source: PwC, "IFRS 16 — Beyond the Implementation"

The "Biggest Ever Accounting Change"

The seemingly simple addition of leased assets in the financials was much more complex than initially perceived. It was estimated that some trillions in debt would be making an appearance on the books with devastating downstream accounting effects across several industries, particularly for decentralized organizations.

As accountants around the world came to terms with the reality of the new standards, many multinational corporations were met with a new hurdle: the sheer volume of assets to manage combined with the unique reporting requirements by region. The challenges, including each standard's different reporting requirements (a problem for companies reporting under both IFRS and GAAP as well as local GAAP), the disbursement of leasing data, the lack of talent and knowledge in the lease accounting spectrum, and the inadequate

processes to manage the transition began to compound.

A company navigating such challenges might at first have had the impulse to lean heavily into manpower or existing software tools. While this might have been feasible for organizations with small equipment lease portfolios, organizations with more vast portfolios realized they needed a dedicated solution. One, described by Shawn Husband, Senior Director, Global Lease Center of Expertise at Walmart, that "does everything you want."

Lease Accounting Solution Fit/Gap Analysis: Nakisa Lease Administration

There are many lease accounting solutions on the market and making the right choice has been a challenge for many organizations. Nakisa Lease Administration is one such solution, that more unusually fulfills the six missing functionalities of software vendors described above. Through a thorough examination of the missing functionalities of lease accounting software vendors as listed below, we will examine the value of solution support in these areas.

① Dual GAAP Reporting

One of the most basic functionalities of a lease accounting solution is supporting the two main reporting regimes, IFRS and US GAAP. An ideal lease accounting solution should offer the same functionality and accounting capabilities for both standards in parallel.

The software should also be able to understand the divergences between the two standards, such as dual classification under ASC 842 versus single classification under IFRS 16. Similarly, the solution needs to treat the lease event scenarios such as the index (e.g. CPI)/rate changes, decreasing lease term etc. differently under ASC 842 and IFRS 16.

In addition to the two main regulatory standards, many companies are required to adhere to local/statutory GAAP standards as well, such as the UK, French, and German GAAP. As a result, many may become ensnared in the complicated and diverse reporting structures of various jurisdictions.

Subsequently, for organizations that have not gone live under the new standards yet, it's important for the software vendor to support the full retrospective method under IFRS 16 or the modified retrospective method under ASC 842 without the transition relief. In doing so, the solution needs to keep track of the comparative numbers, track their changes and report in parallel by producing the comparative reports.

How Nakisa Helps:

Nakisa easily supports multiple reporting with the same input and pushes out accurate accounting calculations to ERPs thanks to its integration capabilities with SAP, Oracle, and more.

② Workflow Functionalities

Prior to the lease accounting deadline, Deloitte's Lease Accounting Services Leader, Sean Torr, stated that, "compliance [would] likely require input from multiple stakeholders from different parts of the organization." Consequently, in order to expedite cross-team collaboration, an easy-to-use interface is an essential functionality in leasing software.

In the years preceding compliance, leasing data was largely siloed into individual teams within corporations, a system that led to crippling bottlenecks when gathering leasing data. A practical solution to collecting the required information from these siloes was for leasing software vendors to put together a checklist of data that needed to be collected prior to implementing the solution.

In a post-IFRS 16 and-ASC 842 regulations world, there is growing attention being paid to internal control systems, auditors, and lease software users looking for audit logs that document changes to lease agreements.

While supporting various roles and users, the final requirement for larger organizations is often strict security controls to easily keep control of the workflow.
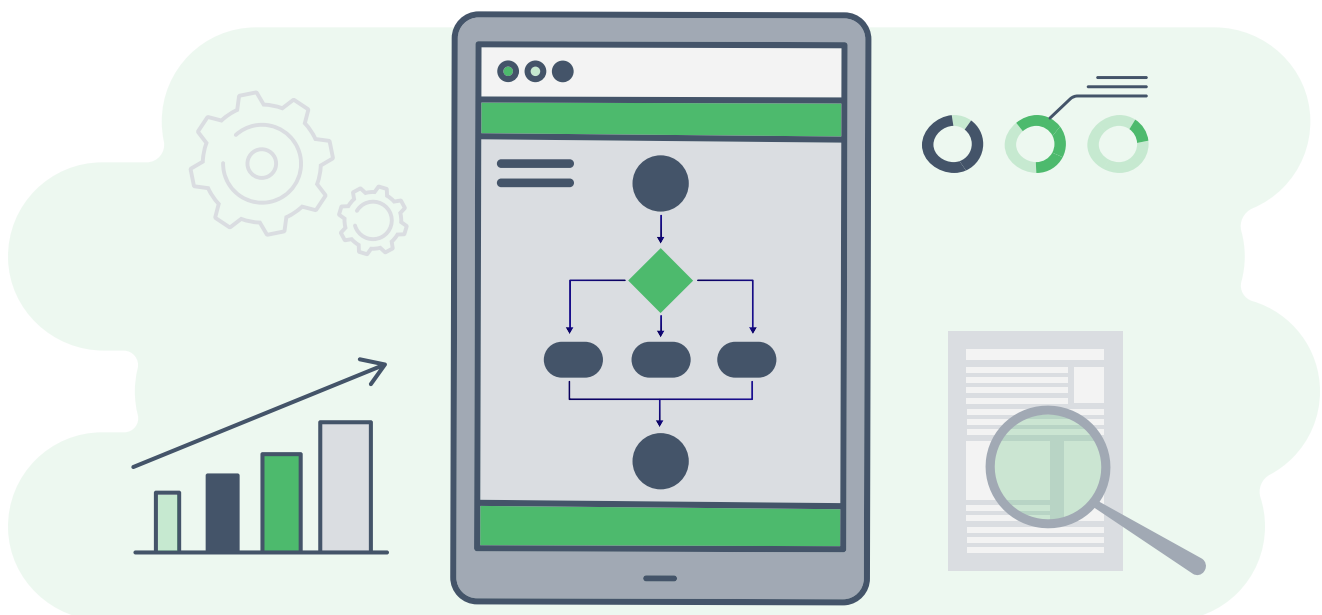
How Nakisa Helps:

Nakisa Lease Administration provides a data dictionary outlining all the fields in the solution, making it easier to identify what information is required from various stakeholders. The solution embeds an approval process that can be tailored based on requirements and internal control policies, within its workflow to align with various security roles and positions within organizations. This allows for an efficient segregation of duties and a stronger control environment.

Nakisa also pays utmost attention to security controls, through the provisioning of read-only, read-and-write, as well as admin-level accesses in the system. Subsequently, its simple user interface invites cross-functional collaboration.
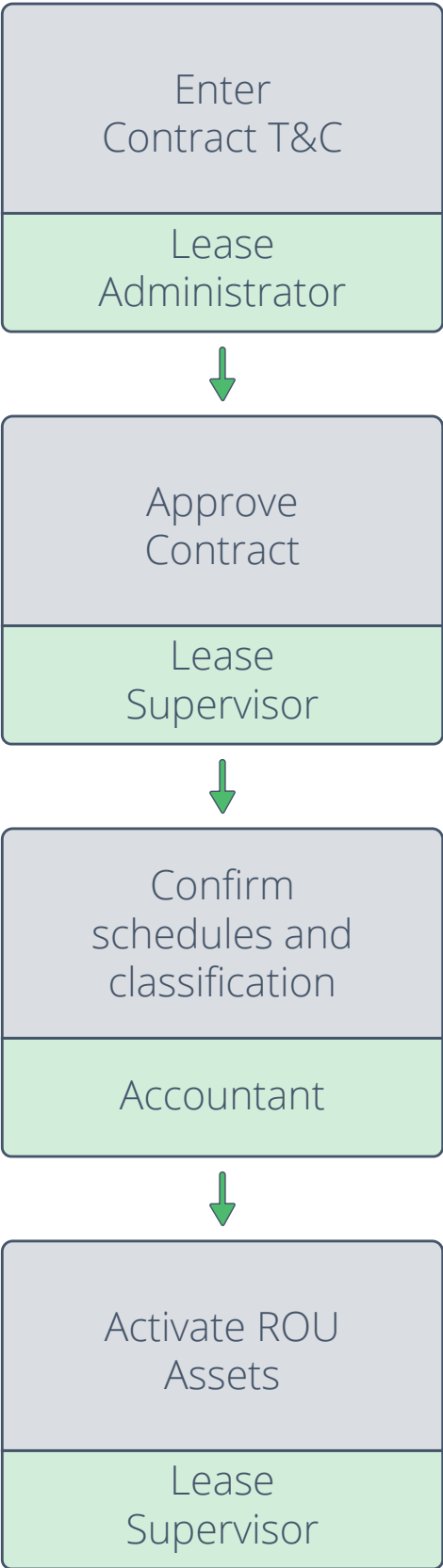
For example, after a lease administrator enters lease terms and conditions, a notification is pushed to an accountant that a new lease contract is ready for approval.

Nakisa Lease Administration also enables end-users to extract multiple reports from the system which can grant Internal Control System assurances. Additionally, the software supports IT general controls (ITGC) with audit logs that track the changes made in the terms and conditions, master data and configurations. The software also offers an easily configurable approval workflow aligned with various security roles and approval matrices within organizations.

A Use Case example of this in action is that, using Nakisa Lease Administration, Air France-KLM was able to build a central repository of their leasing contracts—a step towards sustainably maintaining their compliance endeavors and gain insight into their leasing situation. Moving forward, the airline hopes to use the data to inform their leasing decisions, reduce the complexities of managing lease events, and simplify their accounting processes.

Assist audit procedures through an audit trail

Since a degree of applied knowledge must be enforced when interpreting the newly implemented accounting standards, it is important for organizations to be able to justify their accounting choices and then to keep track of changes to their data. The ideal lease accounting solution should have an embedded audit trail.

Lease accounting software—implication by roles:

```
┌─────────────────────────┐
│         Enter           │
│      Contract T&C       │
├─────────────────────────┤
│         Lease           │
│      Administrator      │
└─────────────────────────┘
            │
            ▼
┌─────────────────────────┐
│        Approve          │
│        Contract         │
├─────────────────────────┤
│         Lease           │
│       Supervisor        │
└─────────────────────────┘
            │
            ▼
┌─────────────────────────┐
│        Confirm          │
│      schedules and      │
│     classification      │
├─────────────────────────┤
│       Accountant        │
└─────────────────────────┘
            │
            ▼
┌─────────────────────────┐
│      Activate ROU       │
│        Assets           │
├─────────────────────────┤
│         Lease           │
│       Supervisor        │
└─────────────────────────┘
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③ Day Two Accounting

It goes without saying that the ideal lease accounting solution needs to compute and support the accounting that pertains to leases.

Data capture of new leases

As the popular tech phrase, "garbage in, garbage out" indicates, for any given software to perform to its full potential, accurate and verified data must be correctly entered into the system. Supporting large volumes of leasing data, with complete accuracy is therefore, a highly desirable quality in a premier lease accounting solution.

How Nakisa Helps:

To help add new leases to existing leasing portfolios with ease, Nakisa introduced a validation framework into Nakisa Lease Administration which begins this validation as soon as data is uploaded into the system. This validation step allows large volumes of leasing data to be processed error-free.

In this environment, data is uploaded to a staging area and checked for accuracy and completeness. Nakisa shares an excel report for each completed job detailing the tasks completed, i.e. a list of entries posted with the assigned document ID.

Support batch processing

One of the main benefits of software solutions is the automation of processes. The ideal lease accounting solution therefore must support large lease portfolios and the scheduling of recurring tasks, such as periodic postings.

Not only does Nakisa Lease Administration support large lease portfolios and mass postings, the solution also provides plenty of flexibility with its job scheduler tool to perform periodic amortization, accruals, and payment postings based on the preference set for every entity within the organization.

This feature also permits the scheduling of new jobs or the alteration of existing jobs with specific parameters. Moreover, users may schedule posting jobs based on plus or minus the number of days from the last day of the month.

Batches of records may be filtered based on master agreement, contract and/ or activation group for added flexibility. Meanwhile, users can slice through contract data choosing only the terms and conditions elected as likely to exercise through a checkbox selection (otherwise all default terms and conditions are applied) in daily operations.

Incremental Borrowing Rate (IBR) selection and global CPI-based remeasurements

In such instances when the implicit borrowing rate is missing from the lease contract, lessees must use their own incremental borrowing rates (IBR) when discounting lease payments. For IBR estimation purposes, accounting software must factor in the economic environment (that the lessee operates in), the lease term, asset class of the contract, etc. for a specific period (as IBRs have a limited validity period).

Since maintaining IBRs and CPIs for each individual lease can be both time-consuming and prone to errors, IBR tables should ideally be actively maintained and updated in the backend of a leasing solution. This relieves users from tedious manual entry of IBRs whenever any change to the lease occurs. For example, if a reassessment is due to change within the lease term, the onus is on the lessee to remeasure the lease liability by discounting the revised lease payments using the IBR at the effective date of remeasurement.

Similarly, if lease payments hinge on an economically volatile rate such as the consumer price index (CPI), then a hefty lease accounting solution should be able to access the latest CPIs in the region and apply it to the necessary calculations.

The diagram below highlights certain facets of a lease that need to be changed, per identified events. This demonstrates how imperative it is to have a complete and adaptable solution for optimized effectiveness.

Noting changes per lease events:

	Event				
What needs to be updated	**Change in Lease Term**	**Change in purchase option assumption**	**Change in Guaranteed Residual Value (GRV) estimate**	**Resolution of a contingency**	**Index/rate changes (IFRS 16 only)***
Lease Payments	✓	✓	✓	✓	✓
Contract consideration and allocation	✓	✓	✓	✓	✗
Discount rate	✓	✓	✗	✗	✗
Lease Classification (ASC 842 only)	✓	✓	✗	✗	✗

***Index/rate changes (IFRS 16 only):** If the change in lease payments results from a change in floating interest rates, the lessee shall use a revised discount rate that reflects changes in the interest rate.

How Nakisa Helps:

Not only does Nakisa Lease Administration maintain an IBR table in its back end, during the various lease reassessment/modification processes, the updated IBR is used and pulled from the table to revise the lease effectively on the date of the event. This is also useful during lease input and reassessment/ modification processes as it automatically picks up the right IBR based on the terms and conditions in the contract.

Nakisa very easily also supports the CPI calculations across the globe. To simplify and streamline index-based remeasurements, users can use Nakisa Lease Administration's CPI global functionality so that multiple contracts tied to the same CPI can be changed simultaneously whenever there is a change in the CPI.

Support mass modifications of lease events

Under the new standards, each lease event—early termination, lease extension, CPI/indexation changes and lease payment adjustments—must be treated differently. For vast lease portfolios, this means that multiple events will impact current values and future postings.

How Nakisa Helps:

With Nakisa Lease Administration, users can tackle lease event modifications in bulk by identifying leases that require modifications such as extension and termination, and then they can systematically remeasure the ROU Asset and Lease Liability.

Using Nakisa Lease Administration, users can tackle lease event modifications (in bulk) in four easy steps:

1. Identify leases that require modification

2. Download a template for mass modification (if needed)

3. Enter the desired changes in the template and upload into the system

4. The system automatically makes the necessary adjustments to the ROU Asset and Lease Liability calculations for all leases

Additionally, Nakisa users are afforded the enhanced ability to add their own supplemental, reduction, termination option and/or base rent as a lease modification to multiple contracts via an excel upload template.

Nakisa's solution also provides full audit trails during lease modification events by saving pre- and post-modification schedules as well as a summary report to show the impact on ROU asset and lease liability.

How Nakisa Helps:

Nakisa Lease Administration supports IT general controls (ITGCs) with audit logs that track the changes made in both the front and back-end of the application. The logs track the old and new values, the users that made the changes as well as the transaction dates. This functionality is easily accessible in the UI.

Similarly, the Nakisa solution also keeps track of the changes made to its Master Data Configuration settings.

Navigate the complex currency infrastructure through currency translation

As organizations around the world become ever more globalized, a robust lease accounting solution must support the multiple currencies their lease transactions are conducted in.

Global businesses have requirements to extract data from a lease accounting solution in different currencies. For example, disclosure reports need to be translated when taking rates applicable for non-monetary asset and monetary liability.

How Nakisa Helps:

First, Nakisa Lease Accounting supports the full gambit of currencies: group, functional, and transactional currencies. Next, the solution also accounts for the correct postings with the necessary currency and the most relevant exchange rate.

Walmart's Shawn Husband grappled with the fact that most accounting systems struggle with maneuvering the infinite complexities of currency transactions, which may affect the precision of both general entries and reports. Husband surmised that other systems may jumble the calculations of the ROU asset with dated or expired exchange rates. These systems would then send the wrong information to the ERPs, further compounding the problem.

Nakisa's solution very easily mimics the remeasurement of the leasing currency to a company's functional currency as well as to its reporting currency. All these calculations are then rightfully sent out to the General Ledger and GL Reports.

Calculate month-end closing reports

Most accounting software users require month-end reconciliation between what has been reported for IFRS16 and ASC842 in the leasing subledger and what has been booked in their ERP. The ideal lease accounting solution needs to be able to support the following month-end closing reports:

- Trial Balance Report (GL Balance Report)
- Transaction Report showing all postings
- Activity Analysis and Control Reports (ex. Activity Analysis by Amount & Activity Analysis by Count)
- Monthly Financial Reports (Balance Sheet, Income Statement and cash flow reports)

How Nakisa Helps:

Not only does Nakisa Lease Administration produce the above-mentioned reports, but the solution also ensures that the balances in the ERPs reconcile seamlessly.

④ Financial Planning and Analytics (FP&A)

Every organization has varying business requirements for financial planning and analysis purposes. Some users might need to see expenses or payments aggregated by company, while others by cost centers. These data requirements can be specific, and are based on many factors, such as geographic region or market, asset classes, etc.

Many users hoped that using a lease accounting solution would allow them to be able to make better-informed leasing decisions. And indeed, an ideal solution should give users access to reports to do exactly that. Users hoped to be able to easily review upcoming lease payments, compare lease terms and negotiate better deals. They also hoped to set up alerts surrounding evergreen leases to tackle their management better.

How Nakisa Helps:

Nakisa Lease Accounting gives users a chance to review upcoming lease payments in a variety of ways. Users can view balances for a selected period by GL account and ensure that movement for each account is as expected. This helps facilitate reporting for month-end or other reporting periods.

Through its Activity Analysis and Contract Expiration Reports features, Nakisa allows users to track and maintain the events and activities that have occurred within the application on a roll-forward basis. Through an IFRS/GAAP-compliance report, Nakisa users can also glean information about the status of their compliance efforts.

Lastly, Nakisa's Dashboard Reporting Tool allows users to create dynamic, real-time custom reports by slicing and dicing data into exactly what they need. The system allows users to drill down into different year-ends and into different company codes—going so far as running hierarchies of company codes and legal entities.

Native integration with the market's leading ERP systems is highly desirable in an ideal lease accounting software solution, as direct integration with an ERP system streamlines the payment process and makes it less prone to errors.

To comply sustainably and report according to the complex new lease accounting standards, it's crucial for accountants to establish as much automation as possible in their solution.

Many advisory boards, prior to the public companies' compliance deadline, advised that it was best to avoid third-party integrations as they often require highly complex customization projects. Standalone solutions, on the other hand, involve significant near-term and long-term risks in addition the upfront and recurring costs for customization hours.

Integration with SAP Systems

SAP General Ledger

·A complete record of financial transactions
·Internal/external reporting

SAP Asset Accounting

·Track, capitalize, and manage ROU/Asset accounting

SAP Accounts Payable

·Execute Payments
·Internal AP reporting

SAP Material Management

·Link Lease Contract to PO

How Nakisa Helps:

Nakisa Lease Administration is designed to leverage core master data from the source SAP ERP system in real time. Nakisa's bi-directional integration with ERP systems allows the solution to pull the correct master data and push back accounting transactions. Furthermore, Nakisa leverages ERP user roles and security infrastructure to support a set-and-forget rollout. The Nakisa solution also handles volume with ease and automatically posts journal entries.

Not only does Nakisa natively integrate with SAP, but it also connects to Oracle through the Nakisa Cloud Connector.

Furthermore, a more recent version of Nakisa Lease Administration released several API Connectors to extend the solution's reach and extensibility.

Additionally, Nakisa's solution supports the capitalization of leased assets and liabilities in different batches at different points in time, within the same contract—a feature that may be particularly suitable for handling fleet leases. Tracking by individual assets allows for unit-specific amortization schedules and streamlines accounting for the casualty of a specific unit.
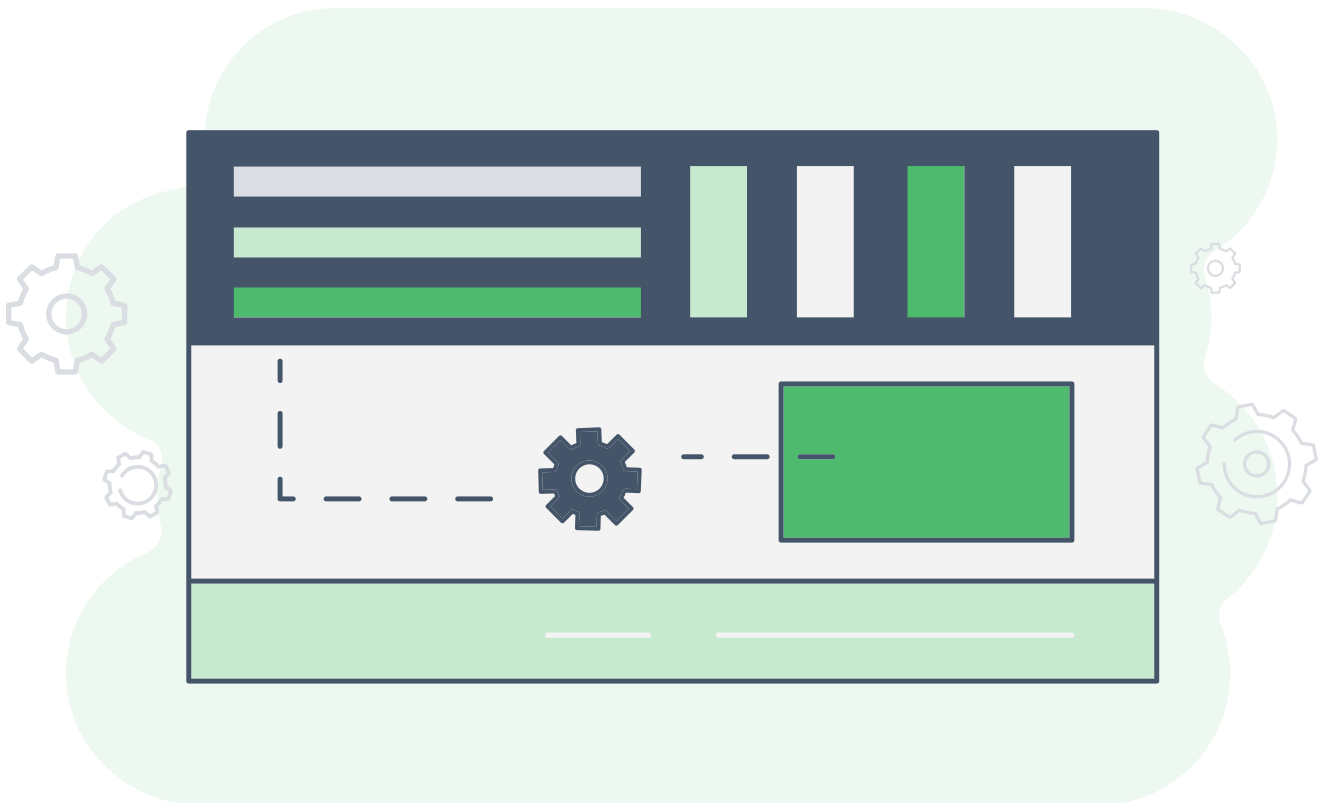
API Connectors

Financial Transaction API Set

Ease business processes by automating postings from Nakisa Lease Administration to one or several different ERP general ledgers. Posting data will be tracked and flagged when posted to eliminate the risk of duplicate or missing journal entries.

Configuration and Lookup API Set

System configuration is essential for defining integration with external environments. Nakisa's integration tools will allow users to easily change configuration data and extract data from external lookup tables.

Lease Management API Set

Streamline Integration and replace manual data entry by leveraging existing master data. Integration with ERP systems is very important as lease liabilities and ROU assets go through frequent remeasurements.

Business Entity API Set

Nakisa's Integration tools will allow users to leverage financial data in ERPs and other financial systems. This delivers a streamlined experience to end-users, reduces manual work, and ensures data consistency across systems.

⑥ Reporting or Disclosure Requirements

Prior to the new regulations, only a few sentences and a table in the annex of the financial statements were enough to report on leases, but IFRS 16 and ASC 842 were brought into place after a call for transparency. Companies were asked to provide detailed reports and tables of their leasing portfolios in order to accurately portray their debt obligations.

Now that organizations are required to calculate future debt payment tables as well as weighted average lease term and weighted average discount rate reports, they need their lease accounting solution to provide a full set of quantitative disclosure reports that can be easily reconciled with contract-level information as well as provide a currency translation perspective.

Furthermore, many companies adopt dual reporting, especially companies with a global presence. This is a significant change to adopt, given that there are compliance divergences between IFRS 16 and ASC 842 that public companies need to ensure are properly disclosed as notes to the financial statements.

How Nakisa Helps:

When building Nakisa Lease Administration, significant emphasis was put on supporting quantitative reporting, which means the Nakisa solution can generate disclosure reports as required by IFRS 16 and ASC 842, and ensures that the currency translation for these reports is done in accordance with IAS 21 and ASC 830 respectively. The reports include liability balances, payment commitment, ROU asset roll forward, lease cost, cash flow, weighted average discount rate, and weighted average lease term.

Nakisa also provides a complete list of contracts with the amounts in contract currency along with the used exchange rates so that the aggregate values can be reconciled against the contract level data. The solution offers a full dual reporting for financial schedules and disclosure reports, for companies that have entities requiring both reporting standards.
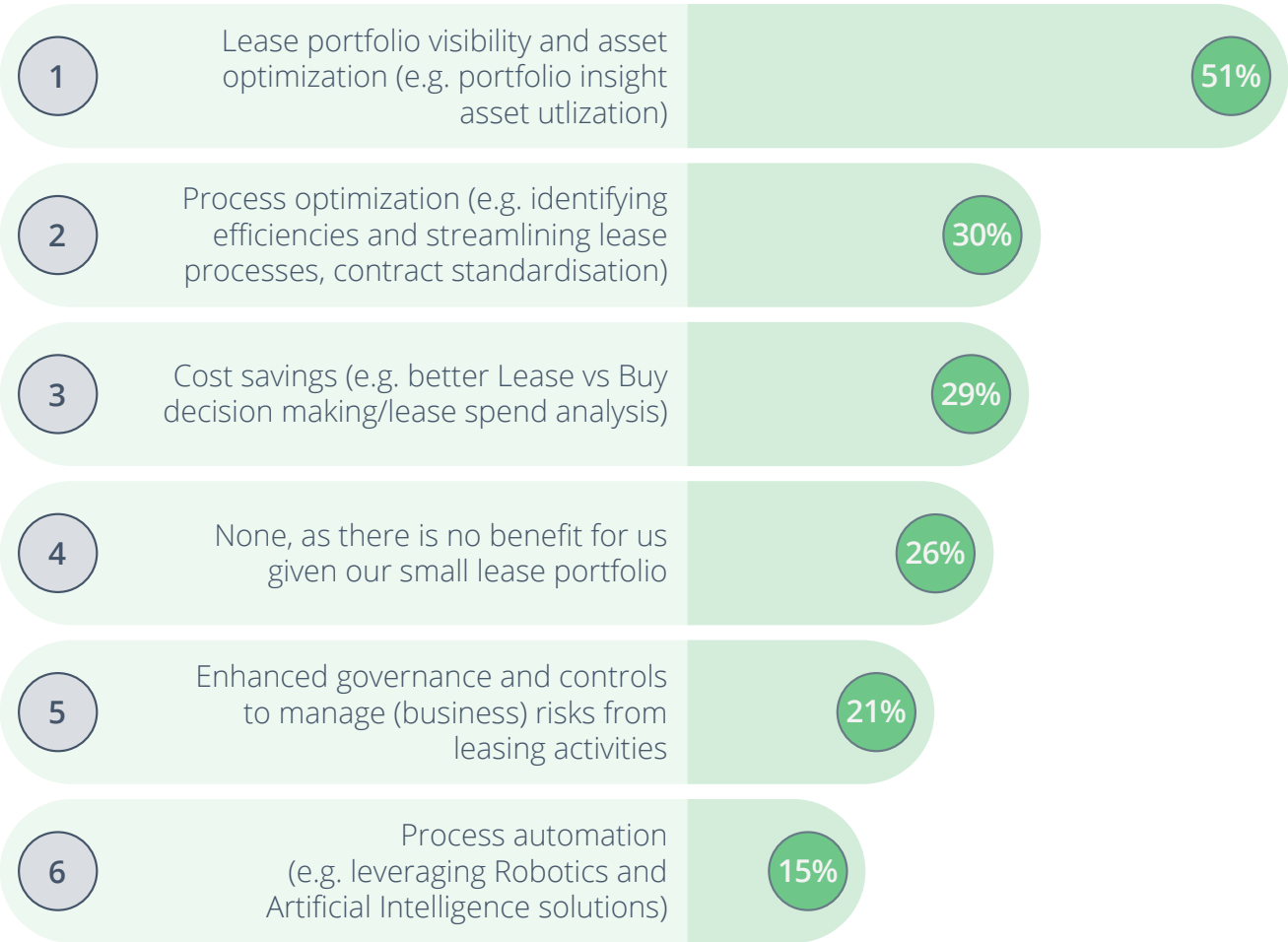
Untapped Benefits

One full year since adoption of the new accounting standards, it appears that companies have yet to realize the benefits of having completed the legwork to bring their leased assets into their year-end financials.

The 2019 PwC report on lease accounting states that as much as 51% of the companies polled still seek to benefit from lease portfolio visibility, while smaller percentages of companies seek to benefit from process optimization surrounding their leases and from cost savings through better decisions around leases. Most of these benefits can be realized through the right lease accounting software vendor.

Benefits most desired from lease accounting implementation IT solution by percentage of respondants who answered that benefit is desired

1	Lease portfolio visibility and asset optimization (e.g. portfolio insight asset utlization)	51%
2	Process optimization (e.g. identifying efficiencies and streamlining lease processes, contract standardisation)	30%
3	Cost savings (e.g. better Lease vs Buy decision making/lease spend analysis)	29%
4	None, as there is no benefit for us given our small lease portfolio	26%
5	Enhanced governance and controls to manage (business) risks from leasing activities	21%
6	Process automation (e.g. leveraging Robotics and Artificial Intelligence solutions)	15%

Source: PwC, "IFRS 16 — Beyond the Implementation"

Nakisa Lease Administration: End-to-End Lease Accounting

Richard van der Laan, Director, Accounting and Reporting at Air France-KLM says that when his company opted for early adoption of IFRS 16 one year before the deadline, they found the Nakisa solution to be the only software capable of capturing and identifying the totality of their leasing contracts (estimated at some $8B in aircraft leases, etc.) as well as seamlessly and accurately performing the accounting behind it.

Van der Laan adds that his organization required a solution capable of providing integration synergies. Likewise, Bancolombia, one of the premier financial institutions in Latin America, had about 2,900 leasing contracts to sort through, and, similarly, required a solution able to natively integrate with their existing SAP ERP systems.

Nakisa Lease Administration readily delivered (and continues to deliver) on such organizations' integration mandates.

Moreover, Nakisa's robust software also offers a wealth of other winning features, positioning the software as the premier lease accounting solution capable of interpreting, tackling, and rolling out the accounting jargon hidden behind the regulations.

Nakisa's ability to handle both behemoth organizations, such as the likes of Walmart—one of the world's largest retail corporations—proved that a specialized solution was required to account for both real estate and equipment leases, and the existing real estate only solutions couldn't fill that gap.

Several other clients have cited that Nakisa's team, comprised of implementation experts, client success, training and accounting excellence thought leaders, as reasons behind their choice.

That's why corporations choose Nakisa Lease Administration—a robust solution that allows organizations to automate parts of their lease accounting process and ensures post-compliance efficiencies are achieved.
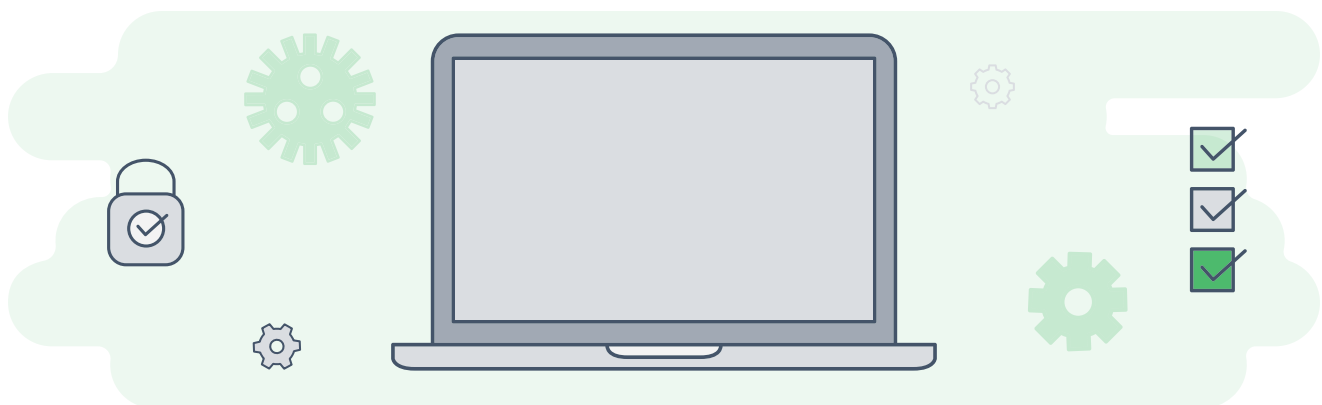
About Us

A global leader in cloud business solutions for Organization Design and Accounting & Compliance, Nakisa delivers innovative, forward-thinking and robust human resource and financial management solutions that advance your business strategies.

If you are interested in learning more about Nakisa Lease Administration, contact us today on info@nakisa.com or visit our website www.nakisa.com/finance.

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