



cutting through complexity

KPMG's CFO Financial Forum Webcast

Preparing for Organizational Impacts of
Proposed Lease Accounting Changes

August 26, 2013

Administrative

- CPE regulations require online participants to take part in online questions
- You must respond to a minimum of 4 questions in order to be eligible for CPE credit
- Polling questions will appear on your media player on top of the slides
- Send Questions via 'Ask a Question' Button
- Help Desk: 1-877-398-1471 or outside the U.S. at +1-954-969-3342
- You can print out presentation slides from the 'Supporting Material' icon
- Reference materials are available
 - Slides
 - Defining Issues
 - Issues In-Depth
 - Leasing Webcasts

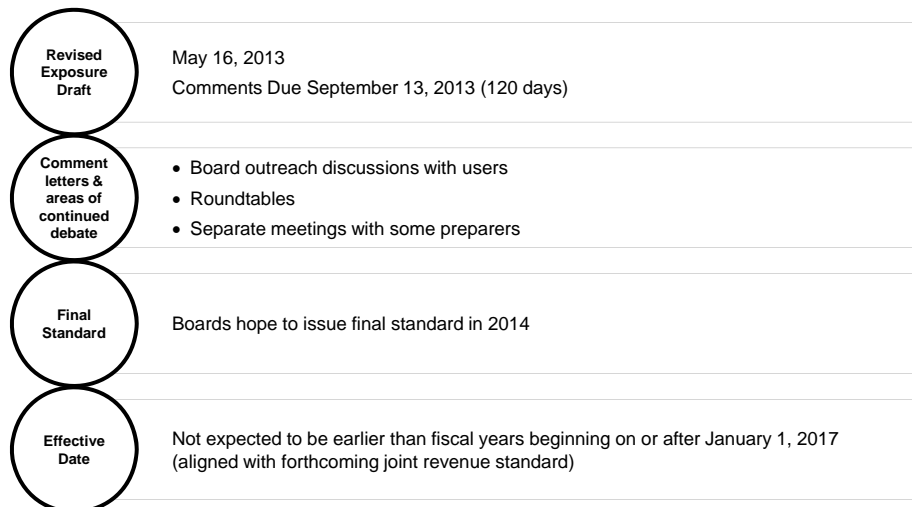
Webcast objectives

- Standard Setting Update
- Potential Impacts of Proposed Lease Standard
- Pre-final Standard Activities
- Share insights from Johnson & Johnson's ongoing leasing project

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Leases project update



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Polling question #1

What is the current status your leasing preparedness activities?

- A. Not started
- B. Selected a team and started identifying project objectives
- C. Determined our inventory of leases
- D. Catalogued leases and extracted salient lease terms for the proposed new standard
- E. In addition to the above, performed some level of financial statement modeling

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Judy Ryan and the Johnson & Johnson leasing project Drivers of the project

Who

- Judy Ryan
 - Global Lease Implementation Leader

Project Objectives

- Enhance leasing systems, process and data on a consistent basis throughout the organization

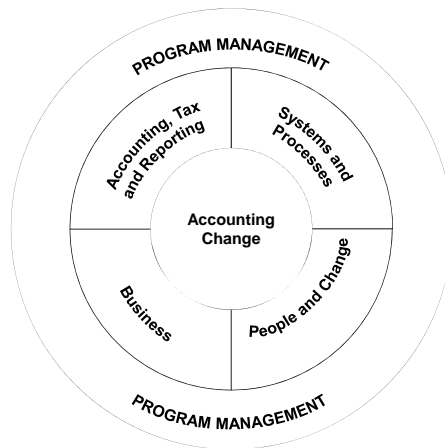
Why

- Preparedness
- Deeper insight into current leasing activities
- Opportunity

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Broad potential impacts of proposed lease accounting standards changes



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Polling question #2

If adopted, where does your organization see the greatest impact of the proposed standard?

- A. Accounting and reporting
- B. Systems and processes
- C. Data and abstracting
- D. People and change
- E. Business practices

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Broad potential impacts of proposed lease accounting standards changes

Accounting and Reporting Impacts

- Increased management judgment (e.g., definition of a lease, lease term, service components, lease classification, etc.)
- Potential for increased level of effort and financial reporting volatility due to ongoing remeasurement for certain items (e.g., lease term)
- New right-of-use asset subject to impairment
- Added complexity in calculating book vs. tax differences
- Need to significantly amend accounting policies and procedures
- Increased disclosure requirements
- Initial valuation of opening balance sheet and preparation of comparative periods
- Need to support transition and ongoing external audit requirements

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Polling question #3

Our company's underlying leasing "systems" are best described as:

- A. Spreadsheet/homegrown and will remain that way
- B. Spreadsheet/homegrown and we expect to upgrade to a larger third-party leasing system
- C. Third-party leasing system and we are in ongoing discussions with our vendor about their expected solution
- D. Third-party leasing system and we have not yet discussed their expected solution

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Broad potential impacts of proposed lease accounting standards changes

Systems & Processes Impacts

- Existing lease systems likely do not have sufficient functionality to handle new requirements including remeasurement
- Transition will require an inventorying of all leases across an organization, potentially including contracts not previously accounted for as leases and contracts previously accounted for as leases that no longer will be (e.g., some contract manufacturing, IT outsourcing arrangements)
- Once leases are inventoried, physical lease documents will likely need to be obtained so that salient lease terms for every lease can be captured in a database
- Expanded data needs may necessitate a need for forecasting and other systems
- Increased management judgment will elevate financial reporting risk, and will require changes to process documentation and SOX 404 testing

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Polling question #4

In what state is your company's current inventory of real estate leases?

- A. Additional work is required to obtain a complete inventory of leasing arrangements
- B. Inventory is complete, but additional lease contract items will need to be abstracted
- C. Inventory is complete, including any additional lease contract items
- D. Not applicable as we have little to no real estate leases.

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Broad potential impacts of proposed lease accounting standards changes

Business Impacts

- Potential for moderate to significant financial statement changes for lessees:
 - Increase in assets impact ROA calculations and increase in liabilities impact capitalization and debt to equity calculations
 - Interest expense impact (I&A method leases) will accelerate expense recognition
 - Elimination of rent expense and reflection as amortization and interest expense (I&A Method leases) result in an increase to EBITDA
- Potential for significant financial statement changes primarily for equipment lessors:
 - Deferred timing of profit recognition on current sales type leases
 - Accelerated timing of profit recognition on most current operating leases
- Management may choose to review buy versus lease decisions and evaluate the need to renegotiate current lease terms
- Potentially could impact state and local taxes paid

Polling question #5

In what state is your company's current inventory of non-real estate (i.e., equipment) leases?

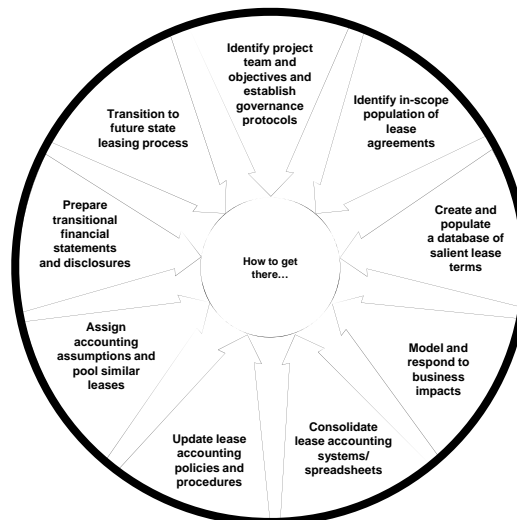
- A. Additional work is required to obtain a complete inventory of leasing arrangements
- B. Inventory is complete, but additional lease contract items will need to be abstracted
- C. Inventory is complete, including any additional lease contract items
- D. Not applicable as we have little to no real estate leases.

Broad potential impacts of proposed lease accounting standards changes

People & Change Impacts

- Due to pervasive organizational change there is a need for a strong project management office with an effective governance structure and communication protocols
- Impacted departments will need appropriate communication and training to understand their role, the impact to their job responsibilities and their level of involvement in the ongoing support of the conversion project and ongoing accounting
- Departments impacted outside of General Accounting and Financial Reporting will likely include Legal, Real Estate, Treasury, Internal Audit, IT, Tax, Budgeting, Regulatory, Contract Management, and Forecasting

Implementing change...



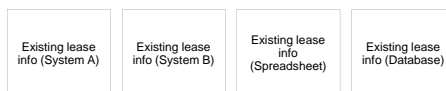
Judy Ryan and the Johnson & Johnson leasing project

Experience

- Pilot program
- Project timeline
 - Phased approach
 - Data Integrity phase
- Substantial undertaking
- Existing information
- Training
 - Language

Illustrative system requirements

Existing database(s) and/or leasing system(s) (e.g., 10 lease terms)



Illustrative system requirements (continued)

Existing database(s) and/or leasing system(s) (e.g., 10 lease terms)

Existing lease
info (System A)

Existing lease
info (System B)

Existing lease
info
(Spreadsheet)

Existing lease
info (Database)

Future state leasing system
(e.g., 20 terms and 3 assumptions)
that would support accounting, leased
asset management and cash
distribution

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Illustrative system requirements (continued)

Existing database(s) and/or leasing system(s) (e.g., 10 lease terms)

Existing lease
info (System A)

Existing lease
info (System B)

Existing lease
info
(Spreadsheet)

Existing lease
info (Database)

KPMG Leasing Tool

Manual input

Future state leasing system
(e.g., 20 terms and 3 assumptions)
that would support accounting, leased
asset management and cash
distribution

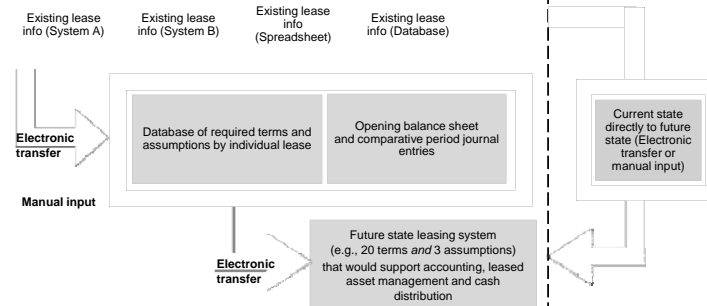
Current state
directly to future
state (Electronic
transfer or
manual input)

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Illustrative system requirements (continued)

Existing database(s) and/or leasing system(s) (e.g., 10 lease terms)



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Polling question #6

What is the most robust level of pre-final standard activities will your company likely perform? (A. being the least, E. being most)

- A. None, we will wait until the final standard
- B. Assign team members and set project objectives
- C. Selected a lease accounting system
- D. Implemented a lease accounting system
- E. Inventory leases
- F. Abstract the inventory of leases, including new salient contract items
- G. Including the above, performing financial statement modeling

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Judy Ryan and the Johnson & Johnson project

Benefits of the project

Experience

- Basic modeling
- Transparency

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Other companies – benefits

- Enhanced observations to provide in comment letters and other Board outreach
- Greater understanding of level of effort required to adopt the standard
- Better understanding of company-wide user requirements for a lease administration system
- Enhanced insight to leasing activities to enable company specific accounting policies
- Elevated outreach and organizational observations

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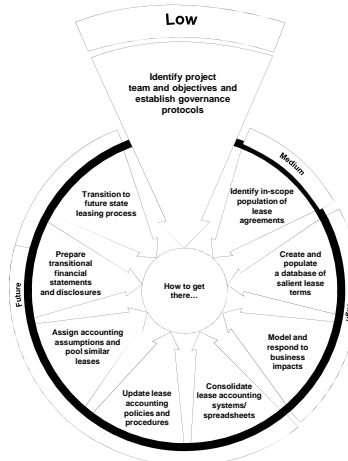
Judy Ryan and the Johnson & Johnson project

What we plan to do next

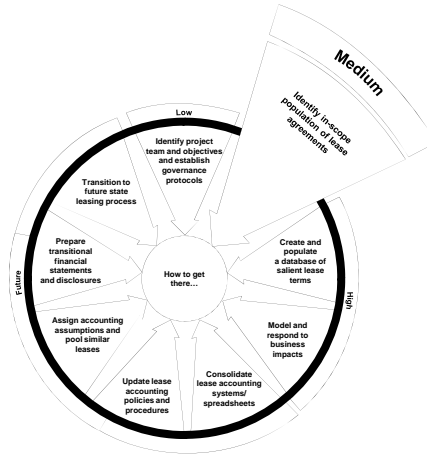
Experience

- Comparative modeling
- Ongoing maintenance

Implementing change...



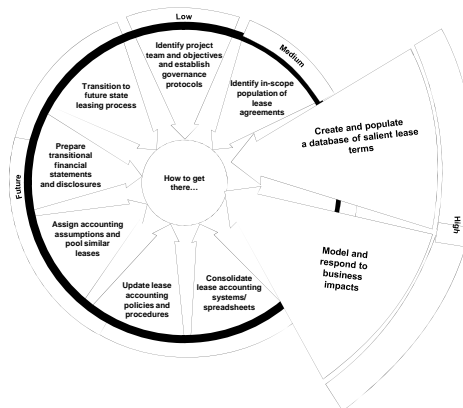
Implementing change...



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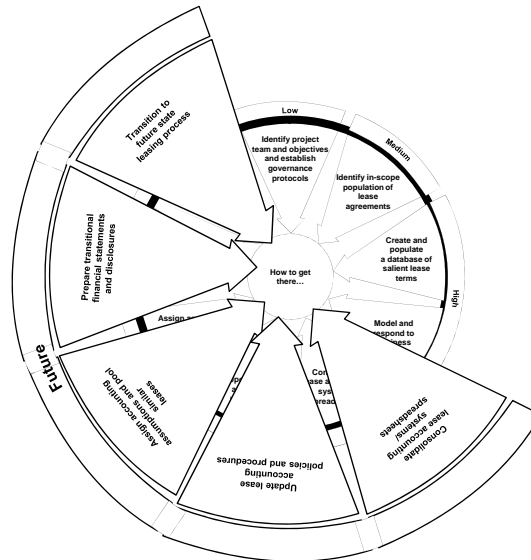
Implementing change...



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Implementing change...



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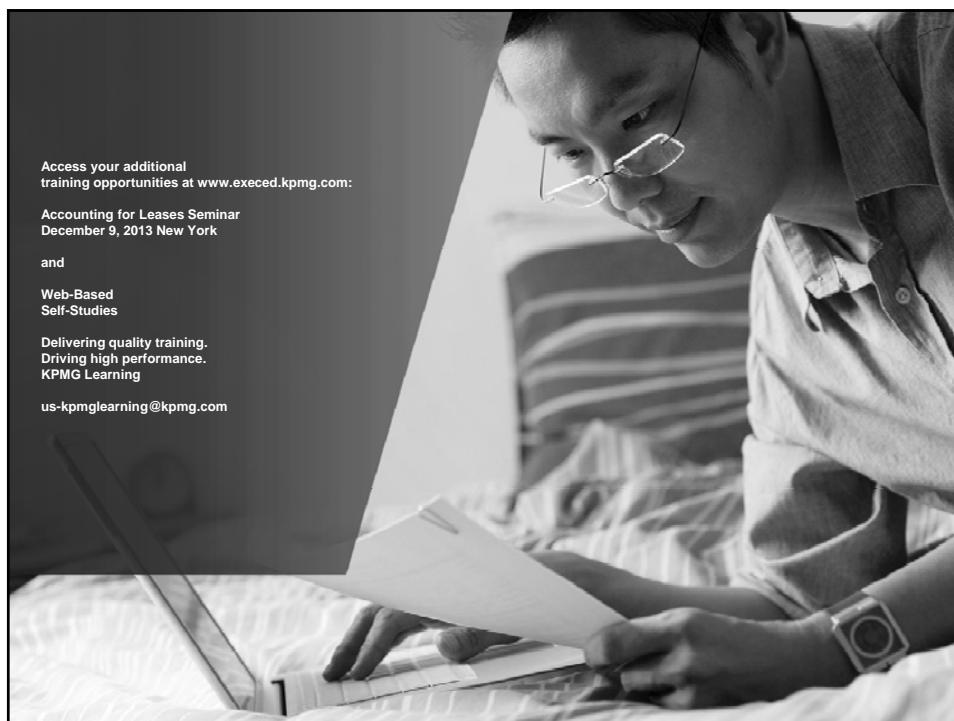
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