

A photograph of a modern operating room with surgical lights, monitors, and medical equipment.

Lease Standards Accounting

In an effort to reduce off-balance sheet accounting of operating leases, the accounting standards boards issued new accounting guidance for how organizations are required to evaluate and recognize leases. The new guidance will require measurement and recognition of all leases with a term of greater than twelve months on the balance sheet.

With the incorporation of operating leases on the balance sheet, organizations will have to be much more diligent in evaluating components of each contract to determine whether or not they meet the new definition of a lease. Depending on the volume, complexity of contracts, availability of data, and so forth, this process could be time consuming and labor intensive. A review of current and potential future debt arrangements will also need to be evaluated.

Lessees will be required to disclose qualitative and quantitative information about its leases including general description of the lease, terms and conditions of options to extend or terminate the lease, any restrictions or covenants imposed by the lease, and significant judgments made by management like lease discount rates or lease classifications. Lessors will also have disclosures and lease recognition considerations.

As part of this process, healthcare organizations need to complete the following:

- > Consider current processes and reports to evaluate areas for data gathering.
- > Assess lease information already available (i.e. capital and operating leases.)
- > Check transactional details, contracts, agreements, et al. to identify potential leases.
- > Examine all agreements potentially impacted by the new standard.
- > Prepare summaries of contract terms to assess lease types.
- > Review current lease identification practices and develop a process for new leases.

Be on the lookout for the following types of contracts and agreements which may include a lease component which needs to be reviewed:

- > Automated medication dispensing machines
- > Related party and intercompany real estate agreements
- > Usage-based agreements (radiology equipment, copiers, etc.)
- > "Free assets" with requirement to use vendor disposables
- > Bio-medical and environmental equipment and supplies
- > Physician office buildings and clinics
- > Marketing and advertising activities
- > Technology, data storage, and license arrangements
- > Outside contracted services
- > Other intercompany agreements