THE ULTIMATE HANDBOOK

NEW FASB/IASB LEASE ACCOUNTING STANDARDS

(ASC-842/IFRS 16)

Version 5 | Release Date December 2018

ProLease
An MRI Software Company

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Welcome to the 5th version of our e-book on **the new "FASB/IASB Lease Accounting Standards."** This version was completed in December 2018 and includes valuable updated information about ASC-842 and IFRS 16. After doing a few hundred Lease Accounting training sessions since early 2016, we have a much better idea of the questions you have about the new lease accounting changes so we have updated this e-book to make it more informative and easier to read.

We hope you enjoy.

The information in this guide has been compiled over a period of over 8 years (2010-today). We began working on this project back in 2010 when FASB & the IASB released their first exposure draft, through 2013 when they released the second exposure draft and through the summer of 2015 through the fatal flaw document stage. We have been to London to meet with the IASB and we have met with FASB numerous times in Norwalk, CT to discuss the effects of the new lease accounting changes on commercial real estate. We have also worked very closely with FASB Working Committee members and auditors over the 8 year period to develop what is the most advanced, user-friendly lease accounting software available today.

> Stating that we have "the most advanced, user-friendly lease accounting software available today" is not just a line that our marketing department has come up with. This is what our clients are telling us. After looking at all the other applications that are touting the same capability, ProLease shines through as the program they want to use to become compatible with all the new lease accounting changes.

PROLEASE CAN:

- Manage your Real Estate and Equipment Leases
- Perform lease classification tests to determine if a lease is an Operating or Finance lease
- Capitalize both Operating & Finance leases (using either FASB or IASB rules)
- Dual reporting on one lease (FASB and IASB) for multinational companies
- Modify any capitalization schedule mid-term if the terms of the lease change
- Track subtenant income for disclosure reporting
- Transition existing leases from straight line rent to the new guidance regardless of whether you are a FASB or IASB company (they have different methods of transition)
- Set up one or multiple Chart of Accounts
- Generate Transition and Monthly Journal Entries which can be uploaded to your GL system
- Generate Disclosure Reports (quantitative and 5-year maturity) in accordance with the requirements of ASC-842 and IFRS 16

Call us today to schedule a demo.

We look forward to showing you the power of ProLease.

DISCLAIMER

This guide was written to introduce you to the concepts of capitalizing a real estate Operating lease under the new FASB standard ASC-842 for a FASB company. In the history of commercial real estate, nobody has ever capitalized an Operating lease. This is a complex process that requires you to track certain lease variables, understand the principles, make decisions about your real estate needs and do lots of complex calculations. This guide should not be used in place of discussions with your auditors. It should be used as a guide to introduce you to the capitalization process, educate you and help you to start an intelligent dialogue with your auditors to plan how to best to approach this huge task of putting all of your Operating leases on the balance sheet.

As a software vendor, it is not our job to tell you how to treat each and every scenario. It is up to your company to implement the rules/principles of the new standard, and your auditor's responsibility to audit/attest to whether they agree or not. It IS our job to create a software application that will easily allow you to create lease capitalization schedules, generate journal entries and run disclosure reports. This is the key functionality needed for public and private companies to comply with the new standard.

INTRODUCTION

On January 13, 2019 the IASB issued their new lease accounting standards (IFRS 16). On February 25, 2016 the FASB issued their new lease accounting standards ASU No. 2016-02 (aka ASC-842). The significance of these new standards cannot be overstated for both:

- The financial statement impact of lease transactions and
- The changes to systems, policies and procedures that will be needed to ensure compliance

You are hopefully aware by now that the biggest change is the requirement that almost all Operating leases will now need to be reported on the balance sheet. For US GAAP companies, the new standards will not have much of an impact on the P&L results of leasing activity, if at all. For IFRS reporters, the expense recognition pattern for Operating leases is changing from straight-line to interest amortization declining balance. As a result of these financial statement changes, many key financial metrics and ratios will be affected. So, how your company is viewed by the users of your financial statements including: investors, lenders and analysts will be seen through a whole new set of lenses. And your debt covenants could be affected too.

It will be a substantial challenge to keep track of all the required data points, perform new calculations and get the right numbers to roll up to your balance sheet. ProLease is here to make your job easier, which in turn will help you sleep better much better at night! Our integrated and scalable lease administration and lease accounting systems can take a lot of the heavy lifting off your shoulders.

ProLease calculates the monthly journal entries for your leases in a way that every dollar is verifiable and auditable. With all of your information in one database, your organization can make sure that the needs of all of your stakeholders are being met – from lease administration data entry to the audit committee of your Board, and everyone in between. Knowing that the Right of Use Asset and Lease Liability calculations are being done correctly, you can spend more time focusing on establishing the proper accounting policies and procedures and designing the new workflows and any related new internal controls. The end result of all of these new procedures and all of this collaboration among your stakeholders is that your organization can negotiate leases that will optimize the impact on the financial statements.

In ProLease language, creating the capitalization schedule for a lease is the process you perform to prepare the data to generate the transition and the monthly recurring journal entries for all leases that will need to appear on the balance sheet. We have written this guide to help you understand how to capitalize a lease. Once you understand all of the variables involved and their effect on the balance sheet, you will be better equipped to manage your lease portfolio. This better understanding should foster better communication with those in your organization responsible for establishing and implementing your leasing strategy. You cannot expect the terms of your leasing transactions to get better all of a sudden because of the new leasing standards; landlords and lessors are not going to negotiate for a penny less. But with the right data you will learn to identify the lease terms that will help you optimize the impact on your financial statements.

We cannot give out all of the work we have put into this project over the last 8 years for free so you should consider this e-book a getting started guide to capitalizing an Operating lease if you are a FASB company. This e-book will teach you how to create an "initial" capitalization schedule for an Operating lease for a FASB company.

THIS E-BOOK WILL NOT COVER:

- How to determine if a lease is an Operating or Finance lease
- The differences between FASB & IASB capitalization schedules
- How to capitalize Finance leases
- Transitioning existing leases to the new guidance
- How to modify initial capitalization schedule if the lease changes
- Journal Entries
- Disclosure Reporting

For ProLease clients, we have a 3 hour training session that will teach you EVERYTHING you need to know about putting leases on the balance sheet. We call it the "WHY, WHO, WHEN, WHAT & HOW of Putting Leases on the Balance Sheet."

- WHY are we putting leases on the balance sheet?
- WHO has to put leases on the balance sheet?
- WHEN do we start putting leases on the balance sheet?
- WHAT leases have to go on the balance sheet?

AND MOST IMPORTANTLY:

- HOW do you put a lease on the balance sheet?

If you would like to see a demo of ProLease software, or book a 3 hour training session, feel free to give us a call to schedule a demo.

We hope you enjoy this guide and *we look forward to hearing from you.*

CHAPTER 1 - THINGS YOU NEED TO KNOW

The goal of this guide book is to teach you the basic concepts of capitalizing an Operating lease for a FASB company (complicated procedure) in very easy to understand, user-friendly language so that even non-accounting people will be able to benefit greatly from this guide. We are not going to get "deep into the weeds" and we are not going to go into extremely detailed explanations of various topics. We are going to give you very precise, short explanations and teach you how to do this in the most minimum amount of pages possible. Our full 3 hour training session goes into a much greater depth of detail to explain all the ins & outs of capitalizing leases.

Before we get started, you need to understand a few basic concepts.

WHAT'S CHANGING IN THE WORLD OF LEASE ACCOUNTING?

In a nutshell, Finance leases (previously referred to as "Capital" leases) have always been on the balance sheet. They will remain on the balance sheet. Nothing new going on there other than the name "Capital Lease" has changed to "Finance Lease." Operating leases (most real estate leases) have never been on the balance sheet. We are now going to be putting Operating leases on the balance sheet. This is what is changing in the world of lease accounting.

It is important to mention that Operating leases appeared in the footnotes to financial statements. They were not on the balance sheet as assets & liabilities. They are now going on the balance sheet as assets & liabilities.

NOTE: If you think this guide is great, wait till you see our software and go through our full training session!

IMPORTANT: Understanding the variables and the calculations involved to capitalize a lease will get you to understand how you can manage your lease portfolio to optimize the impact on the financial statements.

WHAT IS A BALANCE SHEET?

The balance sheet lists all of a company's Assets & Liabilities, as of a specific date, where Assets = Liabilities + Equity.

HOW DO I PUT AN OPERATING LEASE ON THE BALANCE SHEET?

To put an Operating lease on the balance sheet you CAPITALIZE it. When you capitalize a lease, you create a liability and an asset that equal each other. When you sign a lease, you create an obligation (liability) to pay rent. This is your "Lease Liability." You also have an asset in your ability to use the space. This is known as your "Right of Use Asset" or "ROU Asset." You will hear these two terms a lot (Lease Liability and ROU Asset) so make sure you understand them.

Capitalizing a lease (creating a Lease Liability and ROU Asset) is a complicated set of calculations that requires a specific set of variables. This guide will teach you what those variables are and what the calculations are to create the schedule.

WHEN DO YOU HAVE TO START PUTTING LEASES ON THE BALANCE SHEET?

ASC-842 is effective for FASB public companies beginning in 2019. FASB private companies get an extra year so that ASC-842 is effective beginning in 2020. IFRS 16 is effective for IASB companies beginning in 2019. Early adoption is permitted by both FASB and IASB and is being contemplated by a number of companies we have been talking to.

TRANSITIONING EXISTING LEASES TO THE NEW GUIDANCE

FASB and the IASB have various methods of transitioning existing leases to the new guidance. It is expected that most companies will be utilizing a prospective-type approach whereby the new leasing standards are applied from the effective date forward and prior year financial statements are not restated. However, both FASB and IASB have transition methods that, if selected, would require that prior year financial statements be restated to reflect the new leasing standards for comparative reporting purposes. For FASB public companies 2017 and 2018 would need to be restated while for IASB companies 2018, at least, would need to be restated.

This book is solely focused on creating a capitalization schedule by a FASB company for a new Operating lease that commences after the new standards are effective, so we will NOT be showing any examples of transitioning existing leases in this guide.

IMPORTANT: ProLease software is fully FASB / IASB compatible to transition all existing leases to the new guidance. In addition, multi-national companies that will have to report under both FASB & IASB standards will love how easy ProLease makes the transition process.

OK, enough small talk. **Let's get started with HOW to capitalize a lease.**

CHAPTER 2 - WHAT INFORMATION DO YOU NEED TO HAVE BEFORE CREATING A CAPITALIZATION SCHEDULE?

There are 7 pieces of information you must have before you can create a capitalization schedule.

The good news is that with ProLease it doesn't make a difference. If you are:

- A FASB company or an IASB company
- Capitalizing a Finance lease or an Operating lease
- Creating an initial capitalization schedule or modifying an existing schedule mid term

To you the user, the data entry is the exact same in all of the above scenarios.

> **IMPORTANT:** Any time something changes your financial obligation mid-term, you will have to modify the capitalization schedule for that lease. You have to re-state from the date you "realize" the change, NOT the date of the change. For example, if your lease expires 12/31/2019 and you sign a lease extension on 7/2019 that starts on 1/1/2020, you will have to re-state your capitalization schedule as of 7/2019 to show the additional extension term and costs. The extension term does not begin until 1/1/2020 but you still have to re-state the schedule on 7/2019 because that is when you signed/realized the change in the obligation.
>
> Note: If the extension was the result of a renewal option, the capitalization schedule would need to be updated at the date your assessment changed to "Reasonably Certain" which likely would be before the renewal agreement execution date.

ProLease has whittled this data entry process down to the user entering 7 pieces of information.
They are:

1. Capitalization Term
2. Expenses to be capitalized
3. Discount Rate
4. Deductions you can take to reduce the rent to be capitalized
5. Landlord Allowances
6. Initial Direct Costs
7. Impairment Credits

Here is an explanation of each of those 7 items.

1) CAPITALIZATION TERM

There are 4 things that will affect your capitalization term:

A. The lease term

B. Is this a renewal or a new lease?

C. Renewal options

D. Cancellation options

The term of your capitalization schedule may be the same as your lease term or it may be a different term. If you are signing a new lease (as opposed to renewing a lease), the capitalization schedule will begin on the commencement date of the lease. If you are renewing a lease, you will have an existing capitalization schedule and you will have to re-state that schedule as of the renewal agreement execution date, or at the date your assessment changed to "Reasonably Certain." The schedule will NOT start on the renewal commencement date.

IMPORTANT: If you have a renewal option that is "Reasonably Certain" to be exercised, you will have to include the option period in your initial capitalization schedule. For example, you sign a 10 year lease with a 5 year renewal option and you deem that it is "Reasonably Certain" that you will exercise the option, you have to capitalize 15 years of rent.

If you have a cancellation option that is "Reasonably Certain" to be exercised, you only have to capitalize through the cancellation date. For example, you sign a 10 year lease but you have the right to cancel at the end of year 5. If you are "Reasonably Certain" that you will be exercising the cancellation option, you only have to capitalize 5 years of rent. However, if there is any cancellation penalty due (i.e. the unamortized portion of cash contribution, free rent and commission or 3 months of rent etc.) you will have to include the cancellation penalty in your rent to be capitalized at the start of the schedule.

IMPORTANT: So right about now I can hear you all saying "How do I know if I am 'Reasonably Certain' to exercise an option?" If there is an economic incentive or an economic compulsion to renew, it is going to be deemed likely that you will be renewing and therefore you will have to include the renewal term in your capitalization schedule. Remember how we were telling you earlier that the guidance is vague. Here is a great example. Defining economic incentive and economic compulsion can be tricky. You will need to work with management and your auditor to determine which business conditions and scenarios will cause you to identify if an option is "Reasonably Certain" to be exercised.

2) EXPENSES TO BE CAPITALIZED

As a general rule of thumb, fixed expenses get capitalized while variable expenses do not (very similar to calculating straight line rent). There are two exceptions to this variable expense rule. Read on.

When we say variable expenses, we mean things like future increases in operating expenses, real estate taxes, CAM charges, electric costs, utility costs etc. These costs will never be capitalized.

Some examples of fixed costs that will get capitalized are:

- Base Rent after any free rent
- Fixed $ bumps in Base Rent (i.e. $.50 per sq ft annual bumps / $2.00 bump in year 5)
- Fixed % increases in Base Rent (i.e. 3% per annum annual increases)
- Designated parking spaces
- Cancellation penalties (only if you are "Reasonably Certain" to exercise the cancellation option)

[The two exceptions to the variable expense rule are: CPI & % Rents for Retailers]

CPI – The FASB and IASB could not agree on how to handle variable index increases like CPI, so they diverged and they handle it differently.

IASB – You must capitalize CPI costs when they are incurred. This means that each year when you receive your CPI increase, you will have to re-state your lease obligation assuming the new escalated rent will be the rent you pay from the increase date till the end of the term.

FASB – You do not have to capitalize CPI unless you are re-stating your capitalization schedule for some other reason. For example, you sign a 5 year lease with a CPI escalation. Your rent is $30.00 per sq ft and each year on the anniversary of the lease, your rent will go up by the CPI increase from last year.

On day 1 you will capitalize 5 years at $30.00 per sq ft. You will NOT capitalize any CPI increase. In year 2 you get a CPI increase and your rent goes up to $30.90. You pay the escalated additional rent but under FASB you do not touch your capitalization schedule. You are still capitalizing $30.00 per sq ft. Beginning of year 3 you get another CPI increase and your rent goes up to $31.80 per sq ft. You pay the escalated rent but you do not change your capitalization schedule. In the middle of year 3 you downsize and give back some space. This is a definite change to your financial obligation so now you have to restate your lease in the middle of year 3. You will use $31.80 (the then escalated rent) as your rent from the date you are re-stating till the end of the term.

IMPORTANT:

- From a balance sheet perspective, the worst Base Rent increases you can negotiate are either fixed $ bumps ($.50 per sq ft per year) or fixed % increases (3% per annum increases). When you negotiate these types of increases, they are included in the initial present value calculation and the Base Rent increases for the entire lease term go on your balance sheet day 1. If you negotiate CPI increases you are deferring the capitalization of rent increases to a later date. This means the initial amount added to your balance sheet as an asset and a liability will be smaller.
- If you are a FASB company and you get through your lease without ever having to re-state your lease obligation, you will never capitalize any CPI increases.
- % Rents for Retailers – This is the second exception to the variable rent rule. If a retailer is paying a market Base Rent, they do not have to capitalize any % rent amounts owed. If a retailer is paying a below market Base Rent, they will have to capitalize some or all of their % rent amount. This is to insure that retailers will not sign below market rents and give the landlord a higher % of sales in order to improve their balance sheet.
- You do not continuously test throughout the lease term to see if you are paying above or below market. This test is performed once at the onset of the lease and never looked at again unless there is a modification to the lease.

3) DISCOUNT RATE

The discount rate is used in two calculations:

- To calculate the Present Value
- To calculate the interest on the Lease Liability

The guidance says a lessee should use the lessor's implicit rate if it is available (FYI – it's almost never available in a real estate lease). If the lessor's rate is not available, the lessee should use its incremental borrowing rate at the commencement date of the lease. The incremental borrowing rate is defined as the rate at which you can borrow money at, for a sum that is approximately the same as the value of the lease payments, for a similar term as the lease, for a collateralized loan.

For private companies that do not have a borrowing rate, you can use a "risk free" discount rate (US Treasury Bills, Notes and Bonds) but this will yield a lower discount rate which means a higher PV which means a higher amount going on your balance sheet. Check with your finance department for what discount rates you should be using.

Calculating Present Value – There are 4 common ways to calculate present value:

- **MONTHLY** assuming a BEGINNING of month payment
- **MONTHLY** assuming an END of month payment
- **ANNUALLY** assuming a BEGINNING of year payment
- **ANNUALLY** assuming an END of year payment

All 4 calculations will yield a different PV amount. Remember, the goal is to capitalize the least amount of rent possible and the amount you are capitalizing is the PV of the rent payments that are subject to being capitalized. Hence, you want the PV to be the lowest amount possible.

The calculation that will yield the lowest PV is **ANNUALLY** assuming an **END** of year payment.

The calculation that will yield the highest PV is **MONTHLY** assuming a **BEGINNING** of month payment. Even though **MONTHLY** assuming a **BEGINNING** of month payment yields the highest PV amount, we recommend using that method because rent is most often paid **MONTHLY** at the **BEGINNING** of every month.

4) DEDUCTIONS YOU CAN TAKE

As previously stated, the goal is to capitalize the least amount of rent possible. Therefore it is critical that you understand all of the deductions you can take to lower the amount of rent to be capitalized. The guidance says that you are allowed to deduct any rent that you receive a "service" for. Let's look at a few examples.

4A) Operating Expense Base Amount – In a Gross Deal, you can deduct the operating expense base amount from the Base Rent in each year.

> **IMPORTANT: You cannot deduct future operating expense increases. You can only deduct the operating expense base amount in a "Gross" lease.**

Suppose you are negotiating a deal that commences in 2017. The rent is $30.00 per sq ft. It is a Gross deal and you negotiate a 2017 base year for operating expenses. The landlord tells you that the operating expense base amount in 2017 is $6.00 per sq ft. You are certainly receiving a service for the $6.00 of operating expenses you are paying. That is how the landlord runs the building. Hence, you can deduct $6.00 from the $30.00 per sq ft Base Rent. You have just reduced the rent to be capitalized from $30.00 to $24.00 (20% decrease in rent to be capitalized).

> **IMPORTANT: You cannot back out the operating expenses in a Net deal because they are not a part of the Base Rent. They are already separate so you will not capitalize operating expenses in a Net deal.**

4B) Real Estate Tax Base Amount – So you are all probably thinking that if we can back out operating expenses in a Gross deal, then you should also be able to back out the real estate tax base amount as well. You are definitely receiving a service for the real estate taxes you are paying. That's how the city runs. They use it to pay policemen, firemen, teachers, government employees etc. This would be a logical assumption except the boards have decided that the services you are receiving for your real estate tax dollars are NOT directly related to the space you are leasing, therefore you are really just reimbursing the landlord for their expenses hence it is considered rent and in a Gross deal, you must capitalize the real estate tax base amount.

> **IMPORTANT: You are NOT allowed to deduct the real estate tax base amount from the rent to be capitalized in a Gross lease. Our recommendation is that you negotiate Net real estate tax escalations. This way the tax base amount will be outside the rent, it will be considered a variable expense and it will not be subject to capitalization.**

> **IMPORTANT: So let's look at the deal we have been discussing above. We have a $30.00 per sq ft gross Base Rent. We have negotiated current base years for operating expense & taxes and the base amount for operating expense is $6.00 per sq ft and the real estate tax base amount is $4.00 per sq ft. Some people would say the net rent is $20.00 ($30.00 gross rent - $6.00 operating - $4.00 taxes = $20.00).**

In this scenario, we will end up capitalizing $24.00 per sq ft ($30.00 Base Rent - $6.00 operating expense base amount = $24.00). **A better way to negotiate this deal would be as a modified Gross deal:**

- $26.00 Base Rent
- Current Base Year for operating expense
- Net real estate tax escalation ($4.00 per sq ft)

By structuring the deal this way your total rent is still the same $30.00 per sq ft ($26.00 Base Rent + $4.00 real estate taxes) but you do not have to capitalize the real estate taxes because they are outside of the Base Rent and they are a variable expense. We can back the $6.00 operating expense base amount out of the $26.00 Base Rent which reduces the amount to be capitalized down to $20.00 per sq ft. We have now reduced the rent to be capitalized from $30.00 to $20.00 (33% decrease in rent to be capitalized). ***We are still paying the exact same rent ($30.00) but by structuring this deal differently we are able to "optimize the real estate lease to minimize the impact on the balance sheet."***

There are other ways to structure a real estate lease that will help to minimize the impact on the balance sheet. For purposes of keeping this document short & sweet we are only going to use these two examples. We go through other scenarios in depth in our 3 hour lease capitalization training session.

5) LANDLORD ALLOWANCES

The guidance says that you can deduct any cash payments made from the landlord to the tenant. Examples would be a TI Allowance, Moving Allowance, Architectural Allowance, Cable & Wiring Allowance etc.

Previously (before the new guidance), when you were creating straight line rent schedules, if you negotiated a deal where the total rent was $1,000,000 and the landlord agreed that upon paid receipts and waivers of liens from you, they would reimburse you up to $250,000 for your construction costs, most tenants (NOT all, but most tenants) would take the total rent ($1,000,000) and subtract the total Landlord TI ($250,000) on day 1 and straight line $750,000 over the term. Even though they had not yet received the $250,000 payment from the landlord, they would deduct the total amount up front. Each time you receive a payment from the landlord you will have to re-state your lease obligation and reduce the ROU Asset by the amount of the contribution.

> **IMPORTANT: Any cash payment received from the landlord can definitely be deducted from your ROU Asset.**

Here's an important concept you need to discuss with your auditor. Below are two scenarios where backing out Landlord TI's gets complicated. The guidance does not address these specific situations and our clients are telling us what their auditors are telling them to do and it is contradicting from one company to another.

SCENARIO 1) The landlord builds the space out turn-key for you. They pay for the entire installation. No cash trades hands. Do you, the lessee, have the right to deduct the cost of the installation from your ROU Asset?

SCENARIO 2) The total cost of the installation is $60.00 per sq ft. The landlord has contributed $40.00 per sq ft and the tenant pays the additional $20.00 per sq ft. From an accounting perspective, only one person can own the asset. You must determine who owns it and what amount can be used as a deduction to the ROU Asset.

The flip side of scenario 2 above is if the landlord only pays $20.00 per sq ft and the tenant pays $40.00 per sq ft of the installation cost.

> **IMPORTANT: Check with your auditors to see how these two scenarios should be handled. Should make for a great conversation.**

6) INITIAL DIRECT COSTS (IDC)

Initial Direct Costs (IDC) are defined as costs that are paid by the lessee, to a third party (NOT the landlord) that are directly attributable to the negotiation and arranging of a lease and are only paid if the deal goes through.

> **IMPORTANT: IDC costs are not deductions. They are costs to the lessee of doing the deal which means they increase the ROU Asset. They have no effect on the Lease Liability.**

Two examples of IDC Costs would be:

- Commissions paid by the lessee (NOT commissions paid by the lessor).
- Money paid by the lessee to an existing tenant to get them out of the space you are trying to lease.

> **IMPORTANT: Brokerage commissions paid by the lessee are considered IDC costs. Legal fees paid by the lessee are not considered IDC. The reason legal fees are not considered IDC is because they get paid regardless of whether the deal goes through or not. Brokerage commissions paid by the lessee are IDC because they are only paid if the deal goes through.**

> **IMPORTANT: From a real estate perspective, we believe it will be very rare that you have any IDC costs in a real estate lease other than in the two examples mentioned above.**

7) IMPAIRMENT CREDITS

Impairment is defined as when the asset is no longer worth what you are carrying it for on your books.

The actual impairment calculation is quite a bit more complicated. However, the important point to note is that after the effective date of ASC-842 and IFRS-16 the ROU Asset is tested for impairment following the same accounting rules as for owned Property, Plant, and Equipment.

> **IMPORTANT: Impairment credits have no effect on the Lease Liability. They are reductions to the ROU Asset only.**

CHAPTER 2 REVIEW

There are 7 pieces of information you must have to create a capitalization schedule.
They are:

1. Capitalization Term*
2. Expenses to be capitalized*
3. Discount Rate*
4. Deductions you can take to reduce the rent to be capitalized
5. Landlord Allowances
6. Initial Direct Costs
7. Impairment Credits

* 1, 2 & 3 are mandatory. You cannot have a capitalization schedule without a finite term, at least one expense and a discount rate.

4, 5, 6 & 7 – You may or may not have any of these items in your lease. When you sign the lease, look for these items. If they are present, you must include them in the capitalization schedule. If they are not present, we will leave them out.

CHAPTER 3 - CREATING A CAPITALIZATION SCHEDULE

Today, when you sign a lease, you create a straight line rent schedule (ASC-840). In the very near future, when you sign a lease, you will need to create a capitalization schedule. Let's discuss how to create a capitalization schedule.

In the previous chapter, we told you that you need 7 pieces of information to create a capitalization schedule. Let's start off by creating a new lease and identifying those 7 pieces of information.

> **IMPORTANT: We are going to keep this to a 3 year term so we can show you all of the monthly calculations on a single page.**

Lease Term	7/1/2019 – 6/30/2022 (3 Years 0 Months – 36 months)	
Rentable Area	10,000 SF	
Free Rent	3 Months Free (7/1/2019 – 9/30/2019)	
Base Rent	10/1/2019 – 6/30/2020	$25,000.00 per month ($30.00 Per year)
	7/1/2020 – 6/30/2021	$25,833.33 per month ($31.00 per year)
	7/1/2021 – 6/30/2022	$26,666.67 per month ($32.00 per year)
Landlord TI	The landlord has agreed that upon paid receipts and waivers of liens, they will reimburse the tenant up to $250,000 for their construction costs. However, notwithstanding any other clause in the lease, the landlord agrees to give the tenant a check for $50,000 upon signing the lease.	

7 ITEMS YOU NEED TO CREATE A CAPITALIZATION SCHEDULE

Here are the 7 pieces of information you need to create a capitalization schedule, based on the terms outlined on the previous page.

1. Capitalization Term	7/1/2019 – 6/30/2022 This is a new lease (NOT a renewal lease) and there are no renewal or cancellation options.
2. Expenses to be capitalized	Base Rent only
3. Discount Rate	5%
4. Deductions to the rent	Tenant received a 2016 base year for operating expenses. The 2016 operating base amount is $7.20 per sq ft $7.20 x 10,000 SF = $72,000 annually $72,000 divided by 12 = $6,000 per month
5. Landlord Allowance	$50,000 on signing
6. Initial Direct Costs (IDC)	None in this example
7. Impairment Credit	None in this example

> **IMPORTANT: Do not even attempt to create a capitalization schedule if you do not have these 7 items.**

Now that we have defined the 7 items, we are ready to create the capitalization schedule.

STEP #1

Calculate the term and expenses to be capitalized (see monthly rent schedule on next page). Based on the above information, you can see the 36 month term, 3 months of free rent and 27 months of rent.

> **IMPORTANT: The total rent amount subject to being capitalized is $657,000.**

		Total Rent to be Capitalized		
		$855,000.00	**($198,000.00)**	**$657,000.00**
Month #	Date	A) Rent	B) Monthly Service Deductions	Total Rent to be Capitalized (A+B)
1	7/1/2019			
2	8/1/2019			
3	9/1/2019			
4	10/1/2019	$25,000.00	($6,000.00)	$19,000.00
5	11/1/2019	$25,000.00	($6,000.00)	$19,000.00
6	12/1/2019	$25,000.00	($6,000.00)	$19,000.00
7	1/1/2020	$25,000.00	($6,000.00)	$19,000.00
8	2/1/2020	$25,000.00	($6,000.00)	$19,000.00
9	3/1/2020	$25,000.00	($6,000.00)	$19,000.00
10	4/1/2020	$25,000.00	($6,000.00)	$19,000.00
11	5/1/2020	$25,000.00	($6,000.00)	$19,000.00
12	6/1/2020	$25,000.00	($6,000.00)	$19,000.00
13	7/1/2020	$25,833.33	($6,000.00)	$19,833.33
14	8/1/2020	$25,833.33	($6,000.00)	$19,833.33
15	9/1/2020	$25,833.33	($6,000.00)	$19,833.33
16	10/1/2020	$25,833.33	($6,000.00)	$19,833.33
17	11/1/2020	$25,833.33	($6,000.00)	$19,833.33
18	12/1/2020	$25,833.33	($6,000.00)	$19,833.33
19	1/1/2021	$25,833.33	($6,000.00)	$19,833.33
20	2/1/2021	$25,833.33	($6,000.00)	$19,833.33
21	3/1/2021	$25,833.33	($6,000.00)	$19,833.33
22	4/1/2021	$25,833.33	($6,000.00)	$19,833.33
23	5/1/2021	$25,833.33	($6,000.00)	$19,833.33
24	6/1/2021	$25,833.33	($6,000.00)	$19,833.33
25	7/1/2021	$26,666.67	($6,000.00)	$20,666.67
26	8/1/2021	$26,666.67	($6,000.00)	$20,666.67
27	9/1/2021	$26,666.67	($6,000.00)	$20,666.67
28	10/1/2021	$26,666.67	($6,000.00)	$20,666.67
29	11/1/2021	$26,666.67	($6,000.00)	$20,666.67
30	12/1/2021	$26,666.67	($6,000.00)	$20,666.67
31	1/1/2022	$26,666.67	($6,000.00)	$20,666.67
32	2/1/2022	$26,666.67	($6,000.00)	$20,666.67
33	3/1/2022	$26,666.67	($6,000.00)	$20,666.67
34	4/1/2022	$26,666.67	($6,000.00)	$20,666.67
35	5/1/2022	$26,666.67	($6,000.00)	$20,666.67
36	6/1/2022	$26,666.67	($6,000.00)	$20,666.67

STEP #2 : IMPORTANT

Now that we know the rent amount that is subject to being capitalized ($657,000), we need to calculate the PV of this cash flow. We will use a 5% discount rate and we will calculate the PV MONTHLY assuming a BEGINNING of month payment (because that is when rent is due).

On the next page is a sample calculation of the Lease Liability. You will see it starts with $606,818.20. That is the PV of the rent to be capitalized ($657,000).

Now that we have the starting point for the Lease Liability, we need to amortize that amount down to $0 over the 36 month term. The amortization of the Lease Liability is done using a combination of interest and the actual cash rent paid. The schedule on the next page shows each month's calculations (opening balance, monthly amortization and closing balance). Notice how in month 36 the closing balance goes down to $0. Everything must go down to $0 at the end of the term.

Below is an explanation of each of the columns:

REMAINING PRESENT VALUE AT 5%

This column shows the opening Lease Liability balance in each month. It is the PV of the remaining rent payments.

INTEREST ((PV – TOTAL RENT) * 5.00%)/12

To calculate the interest on the Lease Liability you take each month's PV subtract the total rent in that month, multiply by the discount rate and divide by 12. Month #1 is showing interest of $2,528.41. Here is how that amount is calculated:

$606,818.20 - $0 = $606,818.20

$606,818.20 x .05 = $30,340.91

$30,340.91 divided by 12 = $2,528.41

LEASE LIABILITY CLOSING BALANCE (REMAINING PV + INTEREST – CASH RENT)

To calculate the closing Lease Liability balance each month we will start with the PV, add the interest in that month and subtract the cash rent paid in that month. Month #1 is showing a closing balance of $609,346.61. Here is how that amount is calculated:

$606,818.20 + $2,528.41 - $0 = $609,346.61

IMPORTANT: In the first 3 months, the closing balance is higher than the opening balance because we have 3 months of free rent. When there is not enough rent paid to overcome the interest charged you have negative amortization. Once you start paying rent (Month #4), your closing balance will start going down and continue down to $0 at the end of the term.

			Lease Liability		
		$657,000.00		$50,181.80	
Month #	Date	Total Rent to Be Capitalized	Remaining Present Value @ 5.00%	Interest ((PV-Total Rent) x 5.00%)/12	Lease Liability Closing Balance (Remaining PV + Interest - Cash Rent)
1	7/1/2019		$606,818.20	$2,528.41	$609,346.61
2	8/1/2019		$609,346.61	$2,538.94	$611,885.55
3	9/1/2019		$611,885.55	$2,549.52	$614,435.07
4	10/1/2019	$19,000.00	$614,435.07	$2,480.98	$597,916.05
5	11/1/2019	$19,000.00	$597,916.05	$2,412.15	$581,328.20
6	12/1/2019	$19,000.00	$581,328.20	$2,343.03	$564,671.23
7	1/1/2020	$19,000.00	$564,671.21	$2,273.63	$547,944.86
8	2/1/2020	$19,000.00	$547,944.86	$2,203.94	$531,148.80
9	3/1/2020	$19,000.00	$531,148.80	$2,133.95	$514,282.75
10	4/1/2020	$19,000.00	$514,282.75	$2,063.68	$497,346.43
11	5/1/2020	$19,000.00	$497,346.43	$1,993.11	$480,339.54
12	6/1/2020	$19,000.00	$480,339.54	$1,922.25	$463,261.79
13	7/1/2020	$19,833.33	$463,261.79	$1,847.62	$445,276.08
14	8/1/2020	$19,833.33	$445,276.08	$1,772.68	$427,215.43
15	9/1/2020	$19,833.33	$427,215.43	$1,697.43	$409,079.53
16	10/1/2020	$19,833.33	$409,079.53	$1,621.86	$390,868.06
17	11/1/2020	$19,833.33	$390,868.06	$1,545.98	$372,580.71
18	12/1/2020	$19,833.33	$372,580.71	$1,469.78	$354,217.16
19	1/1/2021	$19,833.33	$354,217.16	$1,393.27	$335,777.10
20	2/1/2021	$19,833.33	$335,777.10	$1,316.43	$317,260.20
21	3/1/2021	$19,833.33	$317,260.20	$1,239.28	$298,666.15
22	4/1/2021	$19,833.33	$298,666.15	$1,161.80	$279,994.62
23	5/1/2021	$19,833.33	$279,994.62	$1,084.01	$261,245.30
24	6/1/2021	$19,833.33	$261,245.30	$1,005.88	$242,417.85
25	7/1/2021	$20,666.67	$242,417.85	$923.96	$222,675.14
26	8/1/2021	$20,666.67	$222,675.14	$841.70	$202,850.17
27	9/1/2021	$20,666.67	$202,850.17	$759.10	$182,942.60
28	10/1/2021	$20,666.67	$182,942.60	$676.15	$162,952.08
29	11/1/2021	$20,666.67	$162,952.08	$592.86	$142,878.27
30	12/1/2021	$20,666.67	$142,878.27	$509.22	$122,720.82
31	1/1/2022	$20,666.67	$122,720.82	$425.23	$102,479.38
32	2/1/2022	$20,666.67	$102,479.38	$340.89	$82,153.60
33	3/1/2022	$20,666.67	$82,153.60	$256.20	$61,743.13
34	4/1/2022	$20,666.67	$61,743.13	$171.15	$41,247.61
35	5/1/2022	$20,666.67	$41,247.61	$85.73	$20,666.67
36	6/1/2022	$20,666.67	$20,666.67		

STEP #3

The Lease Liability is done. We need to calculate the ROU Asset.

IMPORTANT: When you sign a 3 year lease, you are creating an obligation to pay rent for 3 years. That is what your Lease Liability is all about...the obligation to pay rent. In addition to rent, we have all of these other components:

- Landlord Allowances
- Initial Direct Costs
- Impairment Credits

These components have no effect on the rent you are liable for so they have no effect on the Lease Liability. The above components will get rolled into the ROU Asset. The ROU Asset by itself is one calculation but the "total" ROU Asset must include the above components. To get the "Total ROU Asset" we will add together the Landlord Allowance Closing Balance, IDC Closing Balance, Impairment Closing Balance and the ROU Asset Closing Balance. Let's look at each component individually.

LANDLORD ALLOWANCE

In any month where you receive a Landlord Allowance, you should see the total allowance appear in that month. In our example, we have a $50,000 allowance in month 1.

In the example on the next page you can see the column labeled "Landlord Allowance" and you can see the $50,000 allowance appears as a negative amount in month 1. This is a deduction.

LANDLORD ALLOWANCE AMORTIZATION

We will amortize the Landlord Allowance on a straight line basis over the remaining term. The amortization in each month is $1,388.89.

LANDLORD ALLOWANCE CLOSING BALANCE

In each month we will take the opening balance and subtract the monthly amortization to get a monthly closing balance. At the end of the term the Landlord Allowance gets amortized down to $0.

IMPORTANT: Because our example does not include any IDC costs or Impairment credits we will leave the explanation of those items out of this guide.

		LL Allowance for ROU Asset Only		
		($50,000.00)	($50,000.00)	
Month #	Date	Landlord Allowance	Landlord Allowance Amortization	Landlord Allowance Closing Balance
1	7/1/2019	($50,000.00)	($1,388.89)	($48,611.11)
2	8/1/2019		($1,388.89)	($47,222.22)
3	9/1/2019		($1,388.89)	($45,833.33)
4	10/1/2019		($1,388.89)	($44,444.44)
5	11/1/2019		($1,388.89)	($43,055.55)
6	12/1/2019		($1,388.89)	($41,666.66)
7	1/1/2020		($1,388.89)	($40,277.77)
8	2/1/2020		($1,388.89)	($38,888.88)
9	3/1/2020		($1,388.89)	($37,499.99)
10	4/1/2020		($1,388.89)	($36,111.10)
11	5/1/2020		($1,388.89)	($34,722.21)
12	6/1/2020		($1,388.89)	($33,333.32)
13	7/1/2020		($1,388.89)	($31,944.43)
14	8/1/2020		($1,388.89)	($30,555.55)
15	9/1/2020		($1,388.89)	($29,166.65)
16	10/1/2020		($1,388.89)	($27,777.76)
17	11/1/2020		($1,388.89)	($26,388.87)
18	12/1/2020		($1,388.89)	($24,999.98)
19	1/1/2021		($1,388.89)	($23,611.09)
20	2/1/2021		($1,388.89)	($22,222.20)
21	3/1/2021		($1,388.89)	($20,833.31)
22	4/1/2021		($1,388.89)	($19,444.42)
23	5/1/2021		($1,388.89)	($18,055.53)
24	6/1/2021		($1,388.89)	($16,666.64)
25	7/1/2021		($1,388.89)	($15,277.75)
26	8/1/2021		($1,388.89)	($13,888.86)
27	9/1/2021		($1,388.89)	($12,499.97)
28	10/1/2021		($1,388.89)	($11,111.08)
29	11/1/2021		($1,388.89)	($9,722.19)
30	12/1/2021		($1,388.89)	($8,333.30)
31	1/1/2022		($1,388.89)	($6,944.41)
32	2/1/2022		($1,388.89)	($5,555.52)
33	3/1/2022		($1,388.89)	($4,166.63)
34	4/1/2022		($1,388.89)	($2,777.74)
35	5/1/2022		($1,388.89)	($1,388.85)
36	6/1/2022		($1,388.85)	

STEP #4

We are now ready to calculate the ROU Asset. Remember, on the balance sheet our Assets = Liabilities + Equity, hence the Lease Liability and the ROU Asset have to start with the same amount. That amount is the PV of the rent that is subject to being capitalized. If you go back and look at the Lease Liability, you will see the starting PV amount is $606,818.20.

This will be the starting amount for the ROU Asset as well. We need to amortize the ROU Asset down to $0 using a different method of amortization than the Lease Liability. On the next page is an example of the ROU Asset amortization schedule.

ROU ASSET ONLY OPENING BALANCE (PV ONLY)

This is the starting value of the ROU Asset. Notice it is the exact same amount as the starting value of the Lease Liability. It is the PV of the rent ($606,818.20).

ROU ASSET ONLY AMORTIZATION (STRAIGHT LINE – INTEREST)

This column represents the monthly amortization of the ROU Asset. It is a calculated field. As you can see at the top of the column, it tells you it is the “Straight Line Rent – the Interest from the Lease Liability.” The 3rd column shows the straight line of the total rent to be capitalized. If you remember, that was $657,000. When we straight line that amount over the term it comes out to $18,250 per month. The 4th column is a duplicate of the Lease Liability interest column.

To calculate the monthly amortization of the ROU Asset, you take the straight line amount and subtract the interest from the Lease Liability and that is the monthly amortization of the ROU Asset.

ROU ASSET CLOSING BALANCE (Current Balance – Amortization)

To calculate the closing balance of the ROU Asset each month you take this month's opening balance and subtract the monthly amortization.

> **IMPORTANT: Notice how the ROU Asset closing balance goes down to $0 at the end of the term. In most cases, everything will go down to $0 at the end of the term.**

		ROU Asset				
		$657,000.00	$50,181.80		$606,818.20	
Month #	Date	Straight Line of Total Rent to be Capitalized	Interest ((PV-Total Rent) x 5.00%)/12	ROU Asset Only Opening Balance (PV Only)	ROU Asset Only Amortization (Straight Line - Interest)	ROU Asset Closing Balance (Current Balance - Amortization)
1	7/1/2019	$18,250.00	$2,528.41	$606,818.20	$15,721.59	$591,096.61
2	8/1/2019	$18,250.00	$2,538.94		$15,711.06	$575,385.55
3	9/1/2019	$18,250.00	$2,549.52		$15,700.48	$559,685.07
4	10/1/2019	$18,250.00	$2,480.98		$15,769.02	$543,916.05
5	11/1/2019	$18,250.00	$2,412.15		$15,837.85	$528,078.20
6	12/1/2019	$18,250.00	$2,343.03		$15,906.97	$512,171.23
7	1/1/2020	$18,250.00	$2,273.63		$15,976.37	$496,194.86
8	2/1/2020	$18,250.00	$2,203.94		$16,046.06	$480,148.80
9	3/1/2020	$18,250.00	$2,133.95		$16,116.05	$464,032.75
10	4/1/2020	$18,250.00	$2,063.68		$16,186.32	$447,846.43
11	5/1/2020	$18,250.00	$1,993.11		$16,256.89	$431,589.54
12	6/1/2020	$18,250.00	$1,922.25		$16,327.75	$415,261.79
13	7/1/2020	$18,250.00	$1,847.62		$16,402.38	$398,859.41
14	8/1/2020	$18,250.00	$1,772.68		$16,477.32	$382,382.09
15	9/1/2020	$18,250.00	$1,697.43		$16,552.57	$365,829.52
16	10/1/2020	$18,250.00	$1,621.86		$16,628.14	$349,201.38
17	11/1/2020	$18,250.00	$1,545.98		$16,704.02	$332,497.36
18	12/1/2020	$18,250.00	$1,469.78		$16,780.22	$315,717.14
19	1/1/2021	$18,250.00	$1,393.27		$16,856.73	$298,860.41
20	2/1/2021	$18,250.00	$1,316.43		$16,933.57	$281,926.84
21	3/1/2021	$18,250.00	$1,239.28		$17,010.72	$264,916.12
22	4/1/2021	$18,250.00	$1,161.80		$17,088.20	$247,827.92
23	5/1/2021	$18,250.00	$1,084.01		$17,165.99	$230,661.93
24	6/1/2021	$18,250.00	$1,005.88		$17,244.12	$213,417.81
25	7/1/2021	$18,250.00	$923.96		$17,326.04	$196,091.77
26	8/1/2021	$18,250.00	$841.70		$17,408.30	$178,683.47
27	9/1/2021	$18,250.00	$759.10		$17,490.90	$161,192.57
28	10/1/2021	$18,250.00	$676.15		$17,573.85	$143,618.72
29	11/1/2021	$18,250.00	$592.86		$17,657.14	$125,961.58
30	12/1/2021	$18,250.00	$509.22		$17,740.78	$108,220.80
31	1/1/2022	$18,250.00	$425.23		$17,824.77	$90,396.03
32	2/1/2022	$18,250.00	$340.89		$17,909.11	$72,486.92
33	3/1/2022	$18,250.00	$256.20		$17,993.80	$54,493.12
34	4/1/2022	$18,250.00	$171.15		$18,078.85	$36,414.27
35	5/1/2022	$18,250.00	$85.73		$18,164.27	$18,250.00
36	6/1/2022	$18,250.00			$18,250.00	

STEP #5

Now that we have calculated the ROU Asset, we need to calculate the total ROU Asset Closing balance in each month.

THIS IS THE SUM OF THE:

LL Allowance Closing Balance

+

Initial Direct Cost Closing Balance

+

Impairment Credit Closing Balance

+

ROU Asset Closing Balance

The sum of all of these columns will give you the "Total ROU Asset Closing Balance." In our example, we only have a Landlord Allowance. **We do not have any IDC costs or Impairment credits so our "Total ROU Asset Closing Balance" would look like this:**

		Total ROU Asset Closing Balance		
Month #	Date	A) Landlord Allowance Closing Balance	B) ROU Asset Closing Balance	Total ROU Asset Closing Balance (A+B)
1	7/1/2019	($48,611.11)	$591,096.61	$542,485.50
2	8/1/2019	($47,222.22)	$575,385.55	$528,163.33
3	9/1/2019	($45,833.33)	$559,685.07	$513,851.74
4	10/1/2019	($44,444.44)	$543,916.05	$499,471.61
5	11/1/2019	($43,055.55)	$528,078.20	$485,022.65
6	12/1/2019	($41,666.66)	$512,171.23	$470,504.57
7	1/1/2020	($40,277.77)	$496,194.86	$455,917.09
8	2/1/2020	($38,888.88)	$480,148.80	$441,259.92
9	3/1/2020	($37,499.99)	$464,032.75	$426,532.76
10	4/1/2020	($36,111.10)	$447,846.43	$411,735.33
11	5/1/2020	($34,722.21)	$431,589.54	$396,867.33
12	6/1/2020	($33,333.32)	$415,261.79	$381,928.47
13	7/1/2020	($31,944.43)	$398,859.41	$366,914.98
14	8/1/2020	($30,555.54)	$382,382.09	$351,826.55
15	9/1/2020	($29,166.65)	$365,829.52	$336,662.87
16	10/1/2020	($27,777.76)	$349,201.38	$321,423.62
17	11/1/2020	($26,388.87)	$332,497.36	$306,108.49
18	12/1/2020	($24,999.98)	$315,717.14	$290,717.16
19	1/1/2021	($23,611.09)	$298,860.41	$275,249.32
20	2/1/2021	($22,222.20)	$281,926.84	$259,704.64
21	3/1/2021	($20,833.31)	$264,916.12	$244,082.81
22	4/1/2021	($19,444.42)	$247,827.92	$228,383.50
23	5/1/2021	($18,055.53)	$230,661.93	$212,606.40
24	6/1/2021	($16,666.64)	$213,417.81	$196,751.17
25	7/1/2021	($15,277.75)	$196,091.77	$180,814.02
26	8/1/2021	($13,888.86)	$178,683.47	$164,794.61
27	9/1/2021	($12,499.97)	$161,192.57	$148,692.60
28	10/1/2021	($11,111.08)	$143,618.72	$132,501.64
29	11/1/2021	($9,722.19)	$125,961.58	$116,239.39
30	12/1/2021	($8,333.30)	$108,220.80	$99,887.50
31	1/1/2022	($6,944.41)	$90,396.03	$83,451.62
32	2/1/2022	($5,555.52)	$72,486.92	$66,931.40
33	3/1/2022	($4,166.63)	$54,492.12	$50,326.49
34	4/1/2022	($2,777.74)	$36,414.27	$33,636.53
35	5/1/2022	($1,388.85)	$18,250.00	$16,861.15
36	6/1/2022			

STEP #6

Now that we have our Lease Liability & ROU Asset calculated in every month, we can now calculate the rent expense going to the P & L.

> **IMPORTANT: If you are a FASB company and you are capitalizing an Operating lease, the rent expense going to your P & L will be a straight line rent very similar (if not the same) as your current straight line rent amount however, the calculation to get this amount is very different than calculating straight line rent.**

The calculation to get the P & L expense in an Operating lease for a FASB company is as follows:

Interest on the Lease Liability

+

Amortization of Landlord Allowance

+

Amortization of Initial Direct Costs

+

Amortization of Impairment

+

Amortization of ROU Asset

In our example it would look like this:

		P & L Expense			
		$50,181.80	($50,000.00)	$606,818.20	$607,000.00
Month #	Date	A) Lease Liability Interest	B) Landlord Allowance Amortization	C) ROU Asset Only Amortization	P & L – Reported Lease Expense/ Operating Lease (A+B+C)
1	7/1/2019	$2,528.41	($1,388.89)	$15,721.59	$16,861.11
2	8/1/2019	$2,538.94	($1,388.89)	$15,711.06	$16,861.11
3	9/1/2019	$2,549.52	($1,388.89)	$15,700.48	$16,861.11
4	10/1/2019	$2,480.98	($1,388.89)	$15,769.02	$16,861.11
5	11/1/2019	$2,412.15	($1,388.89)	$15,837.85	$16,861.11
6	12/1/2019	$2,343.03	($1,388.89)	$15,906.97	$16,861.11
7	1/1/2020	$2,273.63	($1,388.89)	$15,976.37	$16,861.11
8	2/1/2020	$2,203.94	($1,388.89)	$16,046.06	$16,861.11
9	3/1/2020	$2,133.95	($1,388.89)	$16,116.05	$16,861.11
10	4/1/2020	$2,063.68	($1,388.89)	$16,186.32	$16,861.11
11	5/1/2020	$1,993.11	($1,388.89)	$16,256.89	$16,861.11
12	6/1/2020	$1,922.25	($1,388.89)	$16,327.75	$16,861.11
13	7/1/2020	$1,847.62	($1,388.89)	$16,402.38	$16,861.11
14	8/1/2020	$1,772.68	($1,388.89)	$16,477.32	$16,861.11
15	9/1/2020	$1,697.43	($1,388.89)	$16,552.57	$16,861.11
16	10/1/2020	$1,621.86	($1,388.89)	$16,628.14	$16,861.11
17	11/1/2020	$1,545.98	($1,388.89)	$16,704.02	$16,861.11
18	12/1/2020	$1,469.78	($1,388.89)	$16,780.22	$16,861.11
19	1/1/2021	$1,393.27	($1,388.89)	$16,856.73	$16,861.11
20	2/1/2021	$1,316.43	($1,388.89)	$16,933.57	$16,861.11
21	3/1/2021	$1,239.28	($1,388.89)	$17,010.72	$16,861.11
22	4/1/2021	$1,161.80	($1,388.89)	$17,088.20	$16,861.11
23	5/1/2021	$1,084.01	($1,388.89)	$17,165.99	$16,861.11
24	6/1/2021	$1,005.88	($1,388.89)	$17,244.12	$16,861.11
25	7/1/2021	$923.96	($1,388.89)	$17,326.04	$16,861.11
26	8/1/2021	$841.70	($1,388.89)	$17,408.30	$16,861.11
27	9/1/2021	$759.10	($1,388.89)	$17,490.90	$16,861.11
28	10/1/2021	$676.15	($1,388.89)	$17,573.85	$16,861.11
29	11/1/2021	$592.86	($1,388.89)	$17,657.14	$16,861.11
30	12/1/2021	$509.22	($1,388.89)	$17,740.78	$16,861.11
31	1/1/2022	$425.23	($1,388.89)	$17,824.77	$16,861.11
32	2/1/2022	$340.89	($1,388.89)	$17,909.11	$16,861.11
33	3/1/2022	$256.20	($1,388.89)	$17,993.80	$16,861.11
34	4/1/2022	$171.15	($1,388.89)	$18,078.85	$16,861.11
35	5/1/2022	$85.73	($1,388.89)	$18,164.27	$16,861.11
36	6/1/2022		($1,388.85)	$18,250.00	$16,861.15

Notice the P & L Expense is a straight line rent in every month. For a FASB company, capitalizing an Operating lease, the rent expense going to your P&L will be a straight line rent.

Congratulations, you have now capitalized your first lease. There is a lot more to it than this simple example. As previously mentioned, we have a 3 hour training session that is geared towards teaching you everything you need to know to capitalize operating leases.

We hope you have enjoyed this guide and got a lot out of it. If you are interested in seeing a demo of ProLease, please contact us.

We look forward to hearing from you.

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