

A Case Study of the Effects of the New Lease Rules on Financial Reporting under IFRS and US GAAP

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Abstract

After decades of continuous controversy of allowing most lease transactions to be reflected as off balance sheet accounts under both; rules based US GAAP and principles based IFRS, both regimes in a joint convergence project have finally decided to treat all long term non-cancellable leases as balance sheet assets and liabilities effective for periods beginning on or after January 1, 2019. The length of time for this inevitable change is very surprising given that lease accounting is often cited as the single major culprit of financial statement misstatement and fraud. It should also be noted that the SOX regulations in the USA effectively eliminated all other off balance sheet debt which begs the question as to how lease accounting continued without change for more than a decade after SOX. This change however will have significant negative effects on business entities, particularly on their debt related ratios which will translate into higher interest costs and a higher company cost of capital. This case study presents a Balance Sheet, Income Statement, and Cash Flow Statement along with a set of facts relating to the company's lease agreements. The student will first be required to prepare a complete set of financial statements per the new lease rules under IFRS and US GAAP. The student is then required to calculate a set of debt related ratios and compare these ratios between the new and current lease rules. The student will then comment on the effects of these ratios and the resulting consequences. The student will complete the project by discussing the differences in lease accounting under IFRS and US GAAP. This case study is recommended as a group project for an undergraduate Advanced Intermediate Accounting course, as well for graduate Intermediate Accounting, Financial Statement Analysis, International Accounting, and Financial Accounting theory courses. A good working knowledge of both IFRS and US GAAP accounting rules are required for the satisfactory completion of this case study.