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# **GWSCPA Nonprofit Symposium Leases Deep Dive with Case Studies**

**Presenters:**

**Richard Cole, Partner, FORVIS**

**Paul Preziotti, Partner, Johnson Lambert**

# Presenter Bios



**Richard Cole, CPA, CGMA**  
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Rick is a partner with FORVIS (which is the result of a merger between BKD and DHG) with more than 25 years of experience serving not-for-profit organizations. He is based in the firm’s New York office and is a member of FORVIS’ Higher Education Center of Excellence, which is an internal committee focused on addressing issues important to the higher education industry. Rick focuses on audits and advisory services for not-for-profit and higher education organizations.

Prior to this role, he worked at the FASB, where he served as a supervising project manager for almost six years. In that role, he was the project manager on Accounting Standards Update (ASU) 2016-14, Presentation of Financial Statements of Not-for-Profit Entities; ASU 2018-08, Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made; and ASU 2019-03, Updating the Definition of Collections. He also was coordinator for FASB’s NFP Advisory Committee and Private Company Council. Before joining the FASB, Rick was vice president and controller at a large national museum in New York for seven years and a senior manager with a large international accounting firm where he worked for 14 years and specialized in audits of higher education institutions and other not-for-profit organizations.

Rick is a member of the AICPA Not-for-Profit Expert Panel. He is a lecturer at Columbia University’s School of Professional Studies in their Non-Profit Management program. He also has been a frequent speaker with NACUBO, the American Institute of CPAs (AICPA), and various state CPA societies.

He is a CPA in New York and New Jersey and is a member of the AICPA and New York State Society of Certified Public Accountants. Rick is a graduate of Montclair State University, New Jersey, with a B.S. degree and an M.B.A. degree.

# Presenter Bios



**Paul Preziotti, CPA**  
**Partner**

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Paul Preziotti, CPA, is a Partner for the multi-office CPA firm, Johnson Lambert LLP. He is responsible for providing audit and consulting services to not-for-profit entities and employee benefit plans. He has significant experience serving as an advisor for organizations on a variety of issues including risk assessment, governance, compliance and internal control considerations.

Paul received his Bachelor of Science in Accounting and Bachelor in International Business degrees from the University of Maryland, and he joined Johnson Lambert after graduating. He is a frequent speaker on audit and accounting topics at various industry conferences and seminars. He is an alumnus of the AICPA Leadership Academy, an honor for which less than 40 people are recognized nationally each year. He received the GWSCPA's 2018 Outstanding Member in Public Practice Award for his contributions to the growth and enhancement of the accounting profession. Furthermore, he is a current member of the AICPA's Not-for-Profit Advisory Council and a past chair for the GWSCPA's Nonprofit Finance & Accounting Symposium. Additionally, Paul serves as a board and audit committee member for St. John's Community Services and a member of the governance structure for the Radiation Effects Research Foundation.

# Today's Agenda

1

**Lease Examples, Calculations, & Journal Entries**

2

**Example Financial Statement Presentation & Disclosure**

**+**  
**Lease Examples, Calculation, &  
Journal Entries**

# Lessee Model — Initial Measurement

## Lease liability (obligation to make the lease payments)

- Measured at the present value of the future minimum lease payments

## Right-of-use asset

- Lease liability + initial direct cost + lease prepayments – lease incentives received

## Discount rate

- Use the rate charged by the lessor if known
- The incremental borrowing rate
- All private companies & NFPs **may elect** to use the risk-free rate rather than its borrowing rate (& can use both by class of underlying asset)
- Rate as of the implementation date for the remaining lease term (no need to go back in time)

# Lease Example #1 Details

## Finance Lease

- + Six-year lease
- + No renewal options
- + Lease payments \$40,000 paid EOY
- + Includes 9% interest rate
- + Lease classifies as a finance lease

In this simplified example, the lease liability & the right-of-use asset are both \$179,437 (present value of six payments of \$40,000 each, at a discount rate of 9%)

The journal entry would be

Dr. Right-of-use asset – finance lease	\$179,437
Cr. Lease liability – finance lease	(\$179,437)

# Lessee Model — Subsequent Accounting

Annual expense recognition & subsequent amortization of ROU asset depends on lease classification

## + Finance lease

- Unwind liability using the effective interest method
- Front-loaded expense pattern similar to capital leases under ASC 840 with interest & amortization recognized separately
- Interest determined on the lease liability in each period during the lease term as the amount that produces a constant periodic discount rate
- ROU asset generally amortized on a straight-line basis



# Lease Example #1 — Finance Lease

In this simplified example, if the arrangement is determined to be a *finance lease*, the lessee recognizes both amortization expense & interest expense, with higher expense in the initial years

	Finance Lease					
	Payments	Asset	Liability	Amort. Expense	Interest Expense	Total Expense
<b>Commencement</b>		179,437	179,437			
<b>Year 1</b>	40,000	149,531	155,586	29,906	16,149	46,055
<b>Year 2</b>	40,000	119,625	129,589	29,906	14,003	43,909
<b>Year 3</b>	40,000	89,719	101,252	29,906	11,663	41,569
<b>Year 4</b>	40,000	59,812	70,365	29,906	9,113	39,019
<b>Year 5</b>	40,000	29,906	36,698	29,906	6,333	36,239
<b>Year 6</b>	40,000	0	0	29,906	3,302	33,208
<b>Total</b>	240,000			179,437	60,563	240,000

# Journal Entries — Lease Example #1 Finance Lease

## Beginning Balances – Year 1 – Finance Lease

+ Right-of-use asset – finance lease	\$179,437
+ Lease liability – finance lease	(\$179,437)

## Year 1 Activity – Finance Lease

To record lease payment & year 1 journal entries

Dr. Lease liability – finance lease	\$23,851
Dr. Interest expense	\$16,149
Cr. Accounts Payable (or cash)	(\$40,000)
Dr. Amortization expense	\$29,906
Cr. Right-of-use asset – finance lease	(\$29,906)

## Ending Balances – Year 1 – Finance Lease

+ Right-of-use asset – finance lease	\$149,531
+ Lease liability – finance lease	(\$155,586)
+ Expense for the year	\$46,055

# Lease Example #2 Details

## Operating Lease

- + Six-year lease
- + No renewal options
- + Lease payments \$40,000 paid EOY
- + Includes 9% interest rate
- + Lease classifies as a finance lease

In this simplified example, the lease liability & the right-of-use asset are both \$179,437 (present value of six payments of \$40,000 each, at a discount rate of 9%)

The journal entry would be

Dr. Right-of-use asset – operating lease	\$179,437
Cr. Lease liability – operating lease (\$179,437)	

# Lessee Model — Subsequent Accounting

## Operating lease

- + Unwind liability using the effective interest method
- + Straight-line expense over term
- + ROU asset: Reduced by the difference between the annual straight-line lease expense & the annual interest cost on the lease liability, i.e., amortize the asset to achieve straight-line total lease expense

## Lease Example #2 — Operating Lease

In this simplified example, if the arrangement is determined to be an *operating lease*, there is only rent expense & the expense is straight-lined

	Operating Lease			Total Expense
	Payments	Asset	Liability	
<b>Commencement</b>		179,437	179,437	
<b>Year 1</b>	40,000	155,586	155,586	40,000
<b>Year 2</b>	40,000	129,589	129,589	40,000
<b>Year 3</b>	40,000	101,252	101,252	40,000
<b>Year 4</b>	40,000	70,365	70,365	40,000
<b>Year 5</b>	40,000	36,698	36,698	40,000
<b>Year 6</b>	40,000	0	0	40,000
<b>Total</b>	240,000			240,000

## Journal Entries — Lease Example #2

### Beginning Balances – Year 1 – Operating Lease

+ Right-of-use asset – operating lease	\$179,437
+ Lease liability – operating lease	(\$179,437)

### Year 1 Activity – Operating Lease

To record lease payment & year 1 journal entries

Dr. Lease expense	\$40,000	
Cr. Accounts Payable (or cash)		(\$40,000)
Dr. Lease liability – operating lease	\$23,851	
Cr. Right-of-use asset – operating lease		(\$23,851)

### Ending Balances – Year 1 – Operating Lease

+ Right-of-use asset – operating lease	\$155,589
+ Lease liability – operating lease	(\$155,586)
+ Expense for the year	\$40,000

# Journal Entries — Comparison of Journal Entries

## Lease Examples #1 & #2

Beginning Balances - Year 1	Finance Lease		Operating Lease	
	Dr.	Cr.	Dr.	Cr.
Right-of-use asset	\$ 179,437		\$ 179,437	
Lease liability		\$ (179,437)		\$ (179,437)
<b>Year 1 Activity</b>				
	Finance Lease		Operating Lease	
	Dr.	Cr.	Dr.	Cr.
Lease liability	\$ 23,851		\$ 23,851	
Interest expense	\$ 16,149		\$ -	
Lease expense	\$ -		\$ 40,000	
Accounts Payable		\$ (40,000)		\$ (40,000)
Amortization expense	\$ 29,906		\$ -	
Right-of-use asset		\$ (29,906)		\$ (23,851)
<b>Ending Balances - Year 1</b>				
	Finance Lease		Operating Lease	
	Dr.	Cr.	Dr.	Cr.
Right-of-use asset	\$ 149,531		\$ 155,586	
Lease liability		\$ (155,586)		\$ (155,586)
Expense for the year	\$ 46,055		\$ 40,000	

# Lease Example #3 Details

## Finance Lease

- + Six-year lease
- + No renewal options
- + Lease payments at \$30,000 escalating \$10,000 every other year, paid EOY
- + Includes 9% interest rate
- + Lease classifies as a finance lease

In this example, the lease liability & the right-of-use asset are both \$174,306 (present value of six payments escalating by \$10,000 every second year from \$30,000 to \$50,000 each, at a discount rate of 9%)

The journal entry would be

Dr. Right-of-use asset – finance lease	\$174,306
Cr. Lease liability – finance lease	(\$174,306)



## Lease Example #3 — Finance Lease

In this example for *a finance lease*, the lessee recognizes both amortization expense & interest expense, with higher expense in the initial years

	Finance Lease					
	Payments	Asset	Liability	Amort. Expense	Interest Expense	Total Expense
<b>Commencement</b>		174,306	174,306			
<b>Year 1</b>	30,000	145,255	159,994	29,051	15,688	44,739
<b>Year 2</b>	30,000	116,204	144,394	29,051	14,400	43,451
<b>Year 3</b>	40,000	87,153	117,390	29,051	12,996	42,047
<b>Year 4</b>	40,000	58,102	87,955	29,051	10,565	39,616
<b>Year 5</b>	50,000	29,051	45,871	29,051	7,916	36,967
<b>Year 6</b>	50,000	0	0	29,051	4,129	33,180
<b>Total</b>	240,000			174,306	65,694	240,000

# Journal Entries — Lease Example #3 Finance Lease

## Beginning Balances – Year 1 – Finance Lease

+ Right-of-use asset – finance lease	\$174,306	
+ Lease liability – finance lease		(\$174,306)

## Year 1 Activity – Finance Lease

To record lease payment & year 1 journal entries

Dr. Lease liability – finance lease	\$14,312	
Dr. Interest expense	\$15,688	
Cr. Accounts Payable (or cash)		(\$30,000)
Dr. Amortization expense	\$29,051	
Cr. Right-of-use asset – finance lease	(\$29,051)	

## Ending Balances – Year 1 – Finance Lease

+ Right-of-use asset – finance lease	\$145,255	
+ Lease liability – finance lease		(\$159,994)
+ Expense for the year	\$44,739	

# Lease Example #4 Details

## Operating Lease

- + Six-year lease
- + No renewal options
- + Lease payments \$30,000, escalating \$10,000 every other year, paid EOY
- + Includes 9% interest rate
- + Lease classifies as an operating lease

In this example, the lease liability & the right-of-use asset are both \$174,306 (present value of six payments escalating by \$10,000 every second year from \$30,000 to \$50,000 each, at a discount rate of 9%)

The journal entry would be

Dr. Right-of-use asset – operating lease	\$174,306
Cr. Lease liability – operating lease	(\$174,306)

# Lease Example #4 — Operating Lease

For leases with escalating payments in *operating lease*, lessee recognizes only rent expense on straight-line basis. Difference in asset amortization & liability is cumulative difference of payments & expense

Operating Lease						
	Payments	Asset	Liability	Straightline Adjustment to Expense	Cumulative Adjustment in ROU Asset	Total Straightlined Expense
<b>Commencement</b>		174,306	174,306			
<b>Year 1</b>	30,000	149,994	159,994	10,000	10,000	40,000
<b>Year 2</b>	30,000	124,394	144,394	10,000	20,000	40,000
<b>Year 3</b>	40,000	97,390	117,390	0	20,000	40,000
<b>Year 4</b>	40,000	67,955	87,955	0	20,000	40,000
<b>Year 5</b>	50,000	35,871	45,871	(10,000)	10,000	40,000
<b>Year 6</b>	50,000	0	0	(10,000)	0	40,000
<b>Total</b>	240,000			0		240,000

# Journal Entries — Lease Examples #4 Operating Lease

## Beginning Balances – Year 1 – Operating Lease

+ Right-of-use asset – operating lease	\$174,306
+ Lease liability – operating lease	(\$174,306)

## Year 1 Activity – Operating Lease

To record lease payment & year 1 journal entries

Dr. Lease expense	\$40,000	
Cr. Accounts payable (or cash)		(\$30,000)
Cr. Right-of-use asset – operating lease		(\$10,000)
Dr. Lease liability – operating lease	\$14,312	
Cr. Right-of-use asset – operating lease		(\$14,312)

## Ending Balances – Year 1 – Operating Lease

+ Right-of-use asset – operating lease	\$149,994	
+ Lease liability – operating lease	(\$159,994)	
+ Expense for the year		\$40,000

# Journal Entries — Comparison of Journal Entries

## Lease Examples #3 & #4

### Beginning Balances - Year 1

	Finance Lease		Operating Lease	
	Dr.	Cr.	Dr.	Cr.
Right-of-use asset	\$ 174,306		\$ 174,306	
Lease liability		\$ (174,306)		\$ (174,306)

### Year 1 Activity

	Finance Lease		Operating Lease	
	Dr.	Cr.	Dr.	Cr.
Lease liability	\$ 14,312		\$ 14,312	
Interest expense	\$ 15,688		\$ -	
Lease expense	\$ -		\$ 40,000	
Accounts Payable		\$ (30,000)		\$ (30,000)
Amortization expense	\$ 29,051		\$ -	
Right-of-use asset		\$ (29,051)		\$ (24,312)

### Ending Balances - Year 1

	Finance Lease		Operating Lease	
	Dr.	Cr.	Dr.	Cr.
Right-of-use asset	\$ 145,255		\$ 149,994	
Lease liability		\$ (159,994)		\$ (159,994)
Expense for the year	\$ 44,739		\$ 40,000	

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# Example Financial Statement Presentation & Disclosure

# Lessee Balance Sheet Presentation

The below table shows acceptable and unacceptable ways to present these balances on the lessee's balance sheet (note that for simplicity this is an unclassified balance sheet).

<b>Separate Presentation</b> <i>Acceptable</i>  Balance Sheet Period Ended December 31, 20X1	<b>Presentation with Other Assets and Liabilities and Disclosed Separately</b> <i>Acceptable</i>  Balance Sheet Period Ended December 31, 20X1	<b>Combined Presentation</b> <i>Not Acceptable</i>  Balance Sheet Period Ended December 31, 20X1
ROU assets – operating leases 25,000 ROU assets – finance leases 900 Property, plant and equipment 1,100  Operating lease liabilities 25,150 Finance lease liabilities 850 Other liabilities 1,000	ROU assets – operating leases 25,000 Property, plant and equipment 2,000  Operating lease liabilities 25,150 Other liabilities 1,850  <u>Disclosure</u>  For the period ended December 31, 20X1, right-of-use assets from finance leases of \$900 are included as part of property, plant and equipment.  For the period ended December 31, 20X1, lease liabilities from finance leases of \$850 are included as part of other liabilities.	ROU assets 25,900 Property, plant and equipment 1,100  Lease liabilities 26,000 Other liabilities 1,000



## Disclosure Objective

### Enable users of financial statements to assess amount, timing & uncertainty of cash flows arising from leases

- Policies & nature of leases
- Significant assumptions
- Quantitative disclosure examples
  - Finance lease costs, operating lease costs, short-term lease costs, & variable lease costs
  - Weighted average remaining lease term, weighted average discount rate, & supplemental noncash transaction information
  - More info: Sublease income, sale-leaseback gains, & others

	<b>2022</b>	<b>2021</b>
Lease cost		
Finance lease cost		
Amortization of right-of-use asset	\$ -	\$ -
Interest on lease liabilities	-	-
Operating lease cost	-	-
Short-term lease cost	-	-
Variable lease cost	-	-
Sublease income	-	-
(Gains) and losses on sale and leaseback transactions, net	-	-
	<hr/>	<hr/>
Total lease cost	<u>\$ -</u>	<u>\$ -</u>
	<hr/>	<hr/>
	<b>2022</b>	<b>2021</b>
Other information		
Cash paid for amounts included in the measurement of lease liabilities		
Operating cash flows from finance leases	\$ -	\$ -
Financing cash flows from finance leases	-	-
Operating cash flows from operating leases	-	-
Right-of-use assets obtained in exchange for new finance lease liabilities	-	-
Right-of-use assets obtained in exchange for new operating lease liabilities	-	-
Weighted-average remaining lease term		
Finance leases	x.x years	x.x years
Operating leases	x.x years	x.x years
Weighted-average discount rate		
Finance leases	0.0%	0.0%
Operating leases	0.0%	0.0%

# Example Lessee Balance Sheet Presentation

	2022	2021
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 4,640,000	\$ 5,590,000
Accounts receivable	1,450,000	1,000,000
Other receivables	450,000	500,000
Prepaid expenses and other assets	145,000	200,000
Total current assets	<u>6,685,000</u>	<u>7,290,000</u>
<b>Property and Equipment, Net</b>	3,930,000	3,400,000
<b>Right-Of-Use Assets - Operating</b>	<u>305,580</u>	<u>-</u>
Total assets	<u>\$ 10,920,580</u>	<u>\$ 10,690,000</u>
<b>Liabilities and Net Assets</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued expenses	\$ 625,000	\$ 582,000
Current maturities of long-term debt	1,455,000	1,525,000
Current portion of finance lease liabilities	70,000	-
Current portion of operating lease liabilities	70,000	-
Total current liabilities	<u>2,220,000</u>	<u>2,107,000</u>
<b>Finance Lease Liabilities, Net of Current Portion</b>	245,580	-
<b>Operating Lease Liabilities, Net of Current Portion</b>	245,580	-
<b>Long-Term Debt, Net of Current Portion</b>	<u>5,020,000</u>	<u>6,475,000</u>
Total liabilities	<u>7,731,160</u>	<u>8,582,000</u>
<b>Equity / Net Assets Without Donor Restrictions</b>	<u>3,189,420</u>	<u>2,108,000</u>
Total liabilities and equity / net assets	<u>\$ 10,920,580</u>	<u>\$ 10,690,000</u>

## Note \_\_: Leases

### Accounting Policies (can be here in a standalone lease footnote or separate accounting policies section)

The Company determines if an arrangement is a lease or contains a lease at inception of a contract. A contract is determined to be or contain a lease if the contract conveys the right to control the use of identified property, plant, or equipment (an identified asset) in exchange for consideration. The Company determines these assets are leased because the Company has the right to obtain substantially all of the economic benefit from and the right to direct the use of the identified asset. Assets in which the supplier or lessor has the practical ability and right to substitute alternative assets for the identified asset and would benefit economically from the exercise of its right to substitute the asset are not considered to be or contain a lease because the Company determines it does not have the right to control and direct the use of the identified asset. The Company's lease agreements do not contain any material residual value guarantees or material restrictive covenants.

In evaluating its contracts, the Company separately identifies lease and nonlease components, such as common area and other maintenance costs, in calculating the ROU assets and lease liabilities for its office buildings, apartments and vehicles. The Company has elected the practical expedient to not separate lease and nonlease components and classifies the contract as a lease if consideration in the contract allocated to the lease component is greater than the consideration allocated to the nonlease component.

Leases result in the recognition of ROU assets and lease liabilities on the balance sheet. ROU assets represent the right to use an underlying asset for the lease term, and lease liabilities represent the obligation to make lease payments arising from the lease, measured on a discounted basis. The Company determines lease classification as operating or finance at the lease commencement date. ROU assets for finance leases are included in property and equipment in our balance sheet.

At lease inception, the lease liability is measured at the present value of the lease payments over the lease term. The ROU asset equals the lease liability adjusted for any initial direct costs, prepaid or deferred rent, and lease incentives. The Company uses the implicit rate when readily determinable. As most of the leases do not provide an implicit rate, the Company uses its incremental borrowing rate based on the information available at the commencement date to determine the present value of lease payments. Incremental borrowing rates used to determine the present value of lease payments were derived by reference to the secured-debt yields the Company would receive to finance each lease transaction or needed to borrow the amount of the undiscounted future payments over the term of the lease.

The lease term may include options to extend or to terminate the lease that the Company is reasonably certain to exercise. Lease expense is generally recognized on a straight-line basis over the lease term.

The Company has elected not to record leases with an initial term of 12 months or less on the balance sheet. Lease expense on such leases is recognized on a straight-line basis over the lease term.

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## Nature of Leases

The Company has entered into the following lease arrangements:

### Finance Leases

These leases mainly consist of equipment for the use of operations. One finance lease includes an escalating fee schedule, which range from a 25 to 33 percent increase for specific years. Termination of the leases generally are prohibited unless there is a violation under the lease agreement.

### Operating Leases

The Company has two leases for office space that expire in 2027. These leases generally contain renewal options for periods ranging from 2 years to 5 years and require the Company to pay all executory costs (property taxes, maintenance and insurance). One operating lease includes an escalating fee schedule, which range from a 25 to 33 percent increase for specific years. Termination of the leases is generally prohibited unless there is a violation under the lease agreement.

### Short-Term Leases

The Company has certain leases that are for a period of 12 months or less or contain renewals for periods of 12 months or less. The Company does not include short-term leases within the statements of financial position since it has elected the practical expedient to included these leases within the operating right of use asset and lease liabilities. The Company did not have any short-term leases during the years ending December 31, 2022 and 2021.

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# Completed Lessee Quantitative Disclosure Based on Lease Examples

The lease cost & other required information for the year ended December 31, 2022, are

	<b>2022</b>
Lease cost	
Finance lease cost	
Amortization of right-of-use asset	\$ 58,957
Interest on lease liabilities	31,837
Operating lease cost	80,000
	<hr/>
Total lease cost	\$ 170,794
	<hr/>
	<b>2022</b>
Other information	
Cash paid for amounts included in the measurement of lease liabilities	
Operating cash flows from finance leases	\$ 31,837
Financing cash flows from finance leases	38,163
Operating cash flows from operating leases	70,000
Right-of-use assets obtained in exchange for new finance lease liabilities	353,743
Right-of-use assets obtained in exchange for new operating lease liabilities	353,743
Weighted-average remaining lease term	
Finance leases	5.0 years
Operating leases	5.0 years
Weighted-average discount rate	
Finance leases	9.0%
Operating leases	9.0%

# Completed Lessee Quantitative Disclosure Based on Lease Examples

Future minimum lease payments & reconciliation to the balance sheet at December 31, 2022, are as follows.

	<b>Finance Leases</b>	<b>Operating Leases</b>
2023	\$ 70,000	\$ 70,000
2024	80,000	80,000
2025	80,000	80,000
2026	90,000	90,000
2027	90,000	90,000
Thereafter	-	-
Total future undiscounted lease payments	410,000	410,000
Less present value discount	(94,420)	(94,420)
Lease liabilities	<u>\$ 315,580</u>	<u>\$ 315,580</u>

# Presentation and Disclosure Reminders

Supplemental cash flow information for ROU assets obtained for new lease liabilities (operating leases separate from finance leases)

Prior-year disclosures under ASC 840 required when not using the transition method to adopt for prior period presentation (including prior year maturity footnote schedule)



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# Thank You

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