Gold Coast Hospital and Health Service (GCHHS)

ITC 49 Sub 1

AASB 1059 Service Concession

Feedback on service concession standard AASB1059

Definition of Public Service

The scope of the standard is:

This Standard shall be applied to service concession arrangements, which involve an operator:

*(a) providing **public services** related to a service concession asset on behalf of a grantor; and*

(b) managing at least some of those services under its own discretion, rather than at the direction of the grantor.

Public services is not defined in Appendix A. Section B4 and B5 has a heading “Public Service” but B4 defines a service concession arrangement and B5 defines a service concession asset. Nether paragraph defines the meaning of public service.

Paragraphs B6-B9 provide guidance on assessing the public services provided by an asset. On example provided is:

As another example, a hospital car park constructed by an operator as part of the arrangement to construct a hospital that largely provides public services would be considered part of the hospital service concession arrangement. The car park may provide limited ancillary services without affecting the assessment that the car park is used to provide public services. However, if the car park was not constructed as part of the hospital service concession arrangement (eg subsequent to the construction of the hospital or with a different party) and is largely of a commercial nature (eg car parking is available to the general public, including hospital patrons), the car park would be regarded as an asset that does not provide public services, and therefore outside the scope of this Standard.

GCHHS owns land on which the Gold Coast Hospital Carpark was constructed by a private financier. The carpark is independently run as a commercial operation and provides services to the public, not exclusively hospital patrons or staff. Therefore, per scenario 2 of the above example, GCHHS took the position that the carpark was a commercial arrangement and not a public service.

However, the auditors took the position that by virtue of the carpark being constructed on GCHHS land, it inherited the primary purpose of GCHHS which is to provide public services (scenario 1 above). GCHHS were required to recognise the arrangement under the service concession standard or have an unadjusted audit difference reported for the life of the agreement.

A point of confusion in the above example is that it presumes there is a service concession arrangement in place over the main hospital and discusses whether to recognise an attached carpark that has either been constructed as part of that arrangement or subsequent to that arrangement. It does not address the scenario where the hospital construction was government funded, and only the carpark is part of a build-own-operate arrangement on government land.

We recommend clarity be provided by the board as to what constitutes a public service. Specific guidance around commercial operations collocated with public service buildings on government land would be beneficial.

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ACAG
AUSTRALASIAN COUNCIL OF AUDITORS GENERAL

Dr Keith Kendall
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Australian Accounting Standards Board
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23 February 2023

Dear Dr Kendall

AASB Invitation to Comment ITC 49 *Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors*

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to comment on AASB Invitation to Comment ITC 49 *Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors*. The views expressed in this submission represent those of all Australian members of ACAG, unless otherwise specified.

ACAG supports the Board's efforts to seek stakeholders' feedback about their implementation experience of AASB 1059.

In this letter, ACAG has raised numerous accounting and application issues, and auditing or assurance issues. The disparity of views and judgements on some areas were not only across the ACAG network but also arose from our audit experience where divergent interpretations were reached by consultants used by our clients. While ACAG has tried to provide a summary of the implementation experience of various jurisdictions, supported by examples where relevant, ACAG offices will be happy to engage directly with the AASB staff, should they need more information on any of the aspects covered in the letter.

ACAG has also included other suggestions and recommendations that we believe will help promote greater consistency and comparability of application across the public sector.

The attachment to this letter addresses the AASB's specific matters for comment outlined in the ITC.

ACAG appreciates the opportunity to comment and trusts you find the attached comments useful.

Yours sincerely

Margaret Crawford
Chair
ACAG Financial Reporting and Accounting Committee

Attachment

AASB Specific Matters for Comment

Topic 1: Public service

Question 1
Do you have comments regarding the application of the following requirements of AASB 1059: (a) the use of the term 'public service'; (b) the operator's involvement in providing public services on behalf of the grantor; (c) the operator managing at least some of the public services under its own discretion; and (d) the approach to secondary assets? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

(a) The use of the term 'public service'

As included in AASB 1059

ACAG found determining whether an arrangement provided 'public services' to be a key judgement area, that resulted in significant costs in some cases relative to applying the remainder of the standard. There is currently diversity in whether similar arrangements are classified as service concession arrangements. However, ACAG did not identify any situations where the public service test was not met, yet the other control criteria of AASB 1059 were met for arrangements where the assets were not already on balance sheet. For one jurisdiction, any arrangement (that was not already on-balance sheet) that failed the public services test (or agreed to disagree with client because of the diversity of views), but met the other control criteria, were recognised on-balance sheet under other accounting policies - accounting for PPPs that are not service concession arrangements.

When assessing whether an arrangement provides 'public services' it is not always clear whether the services provided by an asset:

- are necessary or essential to the general public as this is a judgement area and can vary depending on different perspectives and different subsets of the general public
- are generally expected to be provided by a public sector entity in accordance with government policy or regulation as what is generally expected to be provided by the public sector changes over time. For example: ports, ferries, electricity, prisons and detention centres were all government services and we note some of these may now be provided wholly or partially by private sector operators.

The following provides examples of a jurisdiction's reasoning for why particular services are a public service:

Student accommodation

When determining whether student accommodation provides public services as a secondary asset, it was important to first assess whether universities provide public services with their primary assets. Given most universities earn a significant portion of revenue from international students and international students pay significantly higher fees, it was a matter of significant judgement to assess whether universities provide public services. Overall, it was concluded that universities provide public services, because:

(a) With international education being a key contributor to Australia's exports and Gross Domestic Product, the level of international students' intake and fee-setting are largely matters of government policy for Australian public universities.

(b) Education (primary, secondary and tertiary) is essential to the public and there would be a general community expectation government provides tertiary education and makes it

accessible to the public even if a sub-set of the community uses those services (AASB 1059.B6).

Therefore, the jurisdiction considered it reasonable to conclude that Australian public universities provide public services (irrespective of the proportion of overseas exports vs local consumption).

Ports

There was significant debate whether only imports should be considered to be providing public services (such as motor vehicles and container cargo) rather than both exports and imports as providing public services.

There was a further discussion on dividing the port activities between imports and exports to determine to what extent ports provide public services. Within the jurisdiction, some had views that exports should not be considered as public services as exports primarily impact private corporations and more broadly the Australian economy.

Overall, the jurisdiction concluded that ports provide public services as:

(a) these are services that are necessary or essential to the general public and are generally expected to be provided by a public sector entity in accordance with government policy or regulation

(b) the services would be considered as accessible to the public, 'even if it is a subset of the community that uses the services'

(c) consumer industries rely heavily on the ports

(d) goods shipped are ultimately used by the public, and

(e) these services are also considered as essential services under the *Essential Services Commission Act 2001* (VIC).

ACAG considered whether the requirement for a service concession arrangement to provide a public service should be retained. Refer below to alternatives considered by ACAG. If the public service test is retained, ACAG believes that the AASB should provide more guidance and clarification on what factors should be considered when determining whether an asset or arrangement provides a public service.

Alternatives considered by ACAG

ACAG considered whether the public service test should be retained. The jurisdictions' views varied between:

- Removing the test – based on the view that the test of providing public services is not in the conceptual framework or any other asset recognition standard. Similarly, a comment was made that aren't all services provided by the public sector 'public services'. Another view to support removal is that the other 5 criteria in AASB 1059 in relation to control of the asset are sufficient to determine whether the grantor controls the asset or not.
- Retaining the test – as providing public services is the key feature of public private partnership (PPP) agreements that are meant to be scoped in AASB 1059. Furthermore, the test mirrors the requirements in AASB Interpretation 12 *Service Concession Arrangements.* However, jurisdictions that expressed this view requested additional guidance on what 'public services' means and clarification on what factors should be considered when determining whether an asset or arrangement provides a public service.

ACAG also considered whether the test could be changed to 'providing services to the public'. Similar diverse views to those mentioned above were expressed as to whether this would be effective. Additional views supporting the use of the term 'providing services to the public' considered that the change would assist in assessing outsourcing type arrangements (refer to examples in item (b) below). However, opposing views considered that the term 'providing services to the public' would not differentiate outsourcing arrangements as the ultimate service was provided to the public.

(b) The operator's involvement in providing public services on behalf of the grantor

Agency vs Consolidated

It is not clear in AASB 1059 whether a service concession arrangement can be recognised only in an agency's consolidated financial statements, at the sector level (general government sector or public non-financial corporations' sector) or whole of government financial statements. This has led to diverse opinions within ACAG as to whether a service concession arrangement needs to be recognised at an agency level (before it can be recognised at the consolidated level), or whether an arrangement can be recognised only at the consolidated level.

At least one jurisdiction believes that a service concession arrangement must first be recognised at an agency level before being recognised at the consolidated level. On the other hand, at least one other jurisdiction believes that a service concession arrangement can just be recognised at the consolidated level, for example, if the pricing (one of the recognition criteria) was set by Cabinet, and not by the individual agency – consistent with the proceeds being received at whole-of-government, and not by the agency. Further complications have arisen for arrangements that appear in an agency's administered activities, and different arrangements for implementing the Cabinet decision (for example is the agency part of the service concession arrangement with the state, and whether the agency does have ultimate decision making over price changes that need Cabinet approval).

ACAG requests that AASB provide guidance on this topic to reduce any future diversity in applying AASB 1059.

Applying 'on behalf of grantor' concept when multiple agencies are involved in the arrangement

- Identification of grantor:

  Some jurisdictions found it difficult to identify the grantor where multiple agencies were involved in the arrangement. The standard refers to 'grantor' however there is very little guidance on what a grantor means when there is more than one public sector entity entering into a contract, that is, more than one public sector entity with different roles and responsibilities. ACAG believes it would be beneficial for the AASB to provide guidance on how to identify a grantor when multiple parties with respective roles and responsibilities are involved.
- Interpreting 'on behalf of the grantor':

  Paragraph 2(a) of AASB 1059 refers to an operator 'providing public services related to a service concession asset on behalf of a grantor'. The concept 'on behalf of the grantor' is not currently defined in AASB 1059. ACAG believes additional guidance is required to apply this concept, particularly where multiple parties are involved in a public service or enter into a contract.

  This may help reduce interpretation issues between preparers and auditors in applying the requirements.

  Two jurisdictions encountered problems when applying the concept of 'on behalf of the grantor'. These primarily relate to situations where the potential grantor did not have the legislative ability to deliver the public service in its own right (that is, it can only contract the service out) or the potential grantor agency may not have the primary responsibility for providing the public service. An example of these has been included below.

  Examples encountered by one jurisdiction

  In this jurisdiction there are different agencies within the transport sector that have different roles in providing transport services to the public. Some of these transport agencies do not have the legislative ability to deliver the public service in their own right (that is, they can only contract the service out) or the agency may not have the primary responsibility for providing the public service. One or more of these agencies have entered into a service concession arrangement or are involved in a service concession arrangement.

Example 1

A transport asset manager entered into an agreement with a private sector operator to operate and maintain a certain number of stations on the rail network. While the transport asset manager had the legislative ability to deliver the public service in its own right, it was unable to exercise this function due to a restriction placed by the portfolio minister on operating and maintaining train stations. Instead, the operation and maintenance of these train stations was contracted to a private sector operator. Passenger railway services were also provided by a different government agency. The other requirements in AASB 1059 including retaining the residual interest were met by the transport asset manager.

The transport asset manager recognised this arrangement as a service concession arrangement on the basis that operating and maintaining train stations was consistent with its legislative functions and considered a public service (this is notwithstanding the fact it did not have the current ability to exercise that function it is own right, but only contract for the provision of the service due to the restriction placed by the portfolio minister).

Example 2

A coordinating transport entity has the ability to enter into contracts for the provision of a public passenger service, but does not have the legislative ability to provide that transport service directly. Legislation provides that another transport agency (agency A) may conduct these transport services.

The coordinating agency entered into a contract in its own accord with a private sector entity for them to provide public services for specific routes using the operator's own transport assets. The other requirements in AASB 1059 including retaining the residual interest were met by the coordinating agency as the assets reverted to the coordinating agency at the end of the arrangement.

Example 2 contrasts with another arrangement where the coordinating agency contracted with a private sector operator on behalf of agency A above (i.e as their agent). Agency A held the residual interest and met all of the other conditions for recognising a service concession arrangement. It was agreed that the arrangement should be recognised in the financial statements of agency A.

Application of criteria

While the combined factors (subject to the public services test discussed above) are useful for determining whether to include a service concession asset on-balance sheet – particularly where the private sector has paid for the construction of the asset and the operator is responsible for capital expenditure renewals, the tests are not conclusive in excluding other government arrangements.

One jurisdiction encountered the following government arrangements that have been argued to meet the definition of a service concession arrangement:

- Prisons – constructed by agency and maintained by agency
- Water treatment plant – constructed by agency and maintained by agency
- Social housing – housing constructed by agency and maintained by agency
- Grant for health services using grantor owned buildings
- Land required to be used for public space as part of property development arrangement.

In each of the above, the tests (i) the operator providing public services, (ii), the operator managing at least some of those services under its own discretion, and (iii) the grantor controls or regulates what services the operator must provide, to whom and at what price, were considered to be met (refer Appendix A), even though there was no private sector (or other) involvement in the construction or capital expenditure renewals of the asset. Essentially, no substantive operating provisions of the standard applied (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator) – apart from the mandated use of the cost approach to fair value, and additional disclosures.

However, some other jurisdictions with similar arrangements arrived at the conclusion that such arrangements were not service concession arrangements.

There is diversity in whether already on-balance sheet arrangements, where noted above, no substantive operating provisions of the standard apply are (or should be) accounted for under AASB 1059. Some, but not all, of the above arrangements were classified as service concession arrangements. This may be due to different facts and circumstances and/or different interpretations of the criteria.

Another jurisdiction encountered issues with local government (LG) entities contracting with private sector operators to manage existing LG facilities (such as an aquatic centre, recreational centre or landfill site) for a short period (for example, for 2 years), where the LG entity sets the prices to be charged to users. There was diversity in practice as to whether this was treated as a service concession arrangement or as an outsourcing arrangement.

Treated as a separate line-item class on face of balance sheet

Consistent with the guidance in AASB 1059 paragraph 29, at least one jurisdiction's Treasury department has mandated that service concession arrangement assets be classified as one class and as a separate line item on the face of the balance sheet.

This may lead to the loss of information as assets that would otherwise have been disclosed as land, buildings and infrastructure are classified as a separate class. In particular, service concession assets are not included in the building and infrastructure classes of PPE, even though they are of a similar nature as other PPE infrastructure assets. An example of the consequence of issues raised above is for arrangements that would otherwise have been considered outsourcing arrangements and included in PPE are reclassified as service concession arrangements in a different asset grouping and note to the financial statements.

(c) The operator managing at least some of the public services under its own discretion

Some jurisdictions believe it would be helpful if the AASB provides additional guidance on an operator managing at least some of the public services under its own discretion. The term 'at least some' is open to a significant amount of judgement. The current examples are very black and white on whether maintenance or other services are a significant component of the public service provided by the asset and the operator is responsible for at least some of the management of the public services. For example, while it is clear maintenance is not significant to a school but is significant for a road, it becomes less clear whether maintenance is significant for other public transport assets, such as buses and ferries especially when the grantor manages and sets the timetables.

A jurisdiction considered an operator's role to maintain the buses, trains etc as significant as proper maintenance is necessary for ensuring smooth running of such trains and buses and making sure these are hazard free for the health and safety of commuters.

Some jurisdictions also suggest adding guidance or an example on circumstances where the grantor has a right to / needs to review plans for providing services using the assets and considerations when these rights may be protective or substantive in nature. One jurisdiction has had circumstances where these rights were deemed only protective in nature and others where these rights were substantive, and the arrangement did not fall within the scope of AASB 1059. Example 5(a) of AASB 1059 implementation guidance only refers to protective rights in the context of determining whether services were provided on behalf of the grantor.

Application of criteria

As noted above, there is diversity in whether already on-balance sheet arrangements, where no substantive operating provisions of the standard apply (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator) are (or should be) accounted for under AASB 1059.

(d) The approach to secondary assets

There was considerable confusion, time, effort expended, and diversity in relation to considering secondary assets. These mainly related to student accommodation and hospital car parks.

In some situations, arrangements relating to secondary assets that are similar to toll roads (private sector entity constructs the asset and is responsible for capital expenditure renewals) were classified as service concession arrangements, and some were not.

The following are the problem areas encountered:

- built at a different time
- does the primary asset need to be a service concession asset?
- primary asset owned by a different agency
- largely of a commercial nature.

Built at a different time

AASB 1059 paragraph B7 introduces guidance that if the secondary asset is constructed at a different time to the primary asset, then the secondary asset may not be a service concession asset. The guidance does not explain how a different construction time affects the characteristics of a service concession asset, and the underlying control criteria of AASB 1059.

ACAG requests that the AASB explain how the time period from original construction affects the control criteria of AASB 1059 and explains how long a period it had in mind for the secondary asset to be a service concession asset.

ACAG jurisdictions have encountered various time periods involving toll road type arrangements for car parks being constructed after the initial buildings, varying from a few months to decades.

Does the primary asset need to be a service concession asset?

It is not clear whether the primary asset needs to be a service concession asset.

It is also not clear, in the circumstances that the primary asset is a service concession asset, whether the primary asset needs to be part of the same arrangement as the secondary asset.

ACAG jurisdictions have encountered student accommodation and hospital car parks where the primary asset (university PPE and hospital PPE) was not subject to a service concession arrangement (under AASB 1059) or a public-private partnership.

Primary asset owned by a different agency

It is not clear whether the primary asset needs to be owned or controlled by the same entity that is the grantor of the secondary asset.

Largely of a commercial nature

There is ambiguity in determining the term ‘largely’ to assess whether an arrangement is of a commercial nature. Jurisdictions considered various factors to determine whether the arrangement is of a largely commercial nature such as:

(a) the university's / grantor’s control in setting prices of student accommodation
(b) the ability of the operator to let out apartments to the general public when the demand of student accommodation is low from students
(c) the length of time the operator could let out the apartments (for example, where the apartments were required to be vacated prior to the start of the academic year).

Question 2
Do you have comments regarding the characteristics of an arrangement that would distinguish it as a service concession arrangement from other arrangements such as a privatisation or outsourcing arrangement, or a lease? If so, please provide your views on those characteristics.

Because of the various areas of uncertainty, and diversity in application described above, there were no clear characteristics to distinguish service concession arrangements from other arrangements such as a privatisation or outsourcing arrangement, or a lease in addition to those specified in paragraph IG 12 and IG 13. For example, in some jurisdictions, already on-balance sheet assets were considered to meet the criteria of a service concession arrangement (refer Question 1(b) *The operator's involvement in providing public services on behalf of the grantor* above, and Appendix A).

In another jurisdiction, similar arrangements were determined to be out of scope, because while the operator had the ability to make some decisions, the level of discretion was not sufficient (for example because the services were subject to strict requirements and/or changes had to be approved by the grantor – this was considered more than a protective right).

Possible characteristics that would be relevant to the provisions of the standard (GORTO liability and financial liability) are when the grantor pays the operator to construct the asset (or the operator constructs the asset for future user charges) and/or the operator is responsible for capital expenditure replacement.

Topic 2: Grantor's control of the asset

Question 3
Do you have comments regarding the application of the following requirements in AASB 1059 paragraph 5: (a) the grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them, and at what price; and (b) the grantor controls any significant residual interest in the asset at the end of the term of the arrangement? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

(a) the grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them, and at what price

Similar to Question 1(b), while the factors (apart from partly regulated assets) are useful for including a service concession asset on-balance sheet – particularly where the private sector has paid for the construction of the asset and/or the operator is responsible for capital expenditure renewals, the tests could be clearer in clarifying whether already on-balance sheet arrangements should be classified as service concession arrangements or outsourcing type arrangements.

Also similar to the response to Question 1(b) *The operator's involvement in providing public services on behalf of the grantor* above, and the analysis in Appendix A, there was diversity in the classification of already on-balance sheet arrangements as service concession arrangements.

<u>Partly Regulated Asset</u>

There were different views as to what 'enough of the service is regulated' (AASB 1059 paragraph B26) means, and consequently what level of regulation is sufficient for classification as a service concession arrangement. There is a lack of reference in the standard to what quantum 'enough' represents. One suggestion was to refer to the term 'significant', although that was acknowledged as having interpretation difficulties as well.

There were also different views as to how to assess whether 'enough of the service is regulated'. In particular, could enough of services be judged from the quantum of revenue generated from regulated and unregulated services, or whether it would be considered as one of the indicators that needed to be assessed with other factors of the arrangement. In this regard, there were also different views as to how to assess the amount of revenue. For example, revenue can vary from one year to another – so which year's revenue should be considered for assessing whether enough of services are regulated?

Controls the price

One jurisdiction suggested that the AASB clarify that an available Government subsidy (for example, aged care subsidy) does not result in the grantor (or a regulator) controlling the price, because the operator is still able to determine the price charged to customers.

(b) Residual Interest

Jurisdictions encountered practical issues in applying the residual interest test, with different approaches taken. Issues included:

- what rough quantitative % does 'significant' represent?
- assessing how remaining economic life was considered compared to relative fair values
- how to assess residual interest when replacements and lifecycle assets are included
- the criticality of the asset to the entity in delivering its objectives.

Often, the residual interest test is met, as the asset is on the grantor's land, and at the end of the arrangement, the grantor gains legal ownership and/or beneficial entitlement and so on, to whatever service concession asset remains on that land. Also, often it is an operating asset (for example, a toll road that has to meet a specific performance standard) and consequently will have a significant residual value. However, sometimes the residual interest is on the operator's land. In such circumstances, it is more important to determine how the residual interest is calculated in order to assess whether there is "significant residual interest in the asset at the end of the term of the arrangement".

AASB 1059 paragraph B35 appears contradictory. In the first part, it treats replacements and lifecycle costs as part of the asset. However, in the second part, it treats replacements and lifecycle costs as separate assets. Therefore, when assessing the estimated value of the asset (on arrangement expiry), is it the fair value of the original asset (of which major components will no longer exist), or will the fair value include the expiry value of the replaced components?

When assessing what level 'significant' represents, should reference be made to the 20% threshold under equity accounting, or the 20-30% some applied under the former IAS 39 / AASB 139 available for sale impairment testing, or did the AASB have another view of what quantitative level 'significant' should be? A dictionary definition of 'significant' is 'sufficiently great or important to be worthy of attention; noteworthy'.

ACAG suggests that the AASB provide additional guidance on the effect of common contractual alternatives at the end of the concession period including:

- the grantor acquires the assets – at a set operating performance standard (for example, a working toll road) for nil consideration
- the grantor acquires the assets – at a set operating performance standard for fair value consideration
- the operator is granted a second concession term
- a new operator is allowed to acquire the assets.

ACAG suggests the AASB include additional guidance when the grantor has the option to acquire the assets at fair value. For example, it can be argued that the grantor still controls the residual interest, as the operator cannot control the infrastructure until the grantor has decided what to do with the option.

Question 4

An arrangement is within the scope of AASB 1059 for recognition as a service concession arrangement if all of the following conditions are satisfied:

(a) the operator provides public services related to a service concession asset on behalf of the grantor;

(b) the operator manages at least some of the public services under its own discretion;

(c) the grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them and at what price; and

(d) the grantor controls any significant residual interest in the asset at the end of the term of the arrangement. This includes the grantor having substantive rights to prevent the operator from selling or pledging the asset during the service concession arrangement.

Do you consider it appropriate for an arrangement to be accounted for under AASB 1059 only when all of the above conditions are satisfied? Please provide reasons to support your view.

As discussed above, there is diversity in how service concession arrangements are assessed. In some situations, arrangements similar to toll roads (private sector entity constructs the asset and is responsible for capital expenditure renewals) were classified as service concession arrangements, and some were not, for example the arrangements with secondary assets discussed above.

Also, as noted in question 1(b) some arrangements where all the above tests were considered met were classified as service concession arrangements, even though there was no private sector (or other) involvement in the construction and/or capital expenditure renewals of the asset and essentially, no substantive operating provisions of the standard applied (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator) . ACAG requests additional implementation guidance and illustrative examples to clarify this issue.

Consequently, some ACAG jurisdictions do not consider it appropriate for an arrangement to be accounted for under AASB 1059 only when all of the above conditions are satisfied as the above criteria (based on current guidance) are not sufficiently discriminatory to result in consistent conclusions on whether certain arrangements should be classified as service concession arrangements. As noted above, there was a diversity of views within ACAG jurisdictions on the retention of the ‘public services’ test or a revision of that test. Some ACAG Jurisdictions support the use of the above conditions if guidance can be strengthened to ensure a more consistent classification of like arrangements.

ACAG believes the guidance needs to be strengthened to ensure a more consistent classification of like arrangements, that is, service concession arrangements or outsourcing arrangements. We discussed above suggestions to improve the requirements, including different views on whether the ‘public services’ test should be retained.

Question 5

In addition to the conditions in AASB 1059 paragraphs 2 and 5 (as set out in Question 4), are there other factors that you consider would assist in determining whether an arrangement is within the scope of AASB 1059? If so, please provide details of those factors and explain why you think they would be useful.

AASB 1059 is broadly the mirror accounting for AASB Interpretation 12 *Service Concession Arrangements*. Interpretation 12 was very helpful in determining whether infrastructure assets (plant and equipment) paid for and maintained by the private sector operator should be recognised as an asset of the operator, when under the arrangements the PPE was controlled by the grantor. Using a control-based approach, rather than a risks and rewards-based approach, also caused changes to the existing treatment.

Applying those concepts from the grantor perspective has meant that toll roads have been recognised on-balance sheet. However, as noted above, there has been diversity in treatment of similar arrangements for student accommodation and hospital car parking.

Some jurisdictions believe there appears little purpose in classifying an already on-balance sheet arrangement as a service concession arrangement. For these arrangements, none of the substantive operating provisions of AASB 1059 apply (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator), and yet requirements such as mandated cost approach fair valuation and disclosures apply.

Topic 3: Public sector operator

Question 6
Do you have comments regarding a public sector entity applying AASB 1059 as the grantor when the operator is another public sector entity? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting. If you propose excluding public-to-public arrangements from the scope of AASB 1059, what is the rationale for your view?

Most of the issues in relation to public sector grantor and public sector operator arrangements was determining whether the arrangement was a service concession arrangement or an outsourcing arrangement (refer to difficulties and application issues discussed above in Topic 1 and Topic 2).

The discussion in question 1(b) (regarding whether the service concession arrangement should be recognised in an agency's financial statements or only at the consolidated level) becomes more relevant when the arrangement is between two public sector entities. In this regard, some jurisdictions believe that the cost of undertaking service concession assessment and accounting may exceed the benefit if the arrangement is between two public sector entities as the arrangement gets eliminated at the consolidated level. Furthermore, there are not many instances of public-to-public service concession arrangements. Therefore, the AASB could consider scoping out public-to-public service concession arrangements by clarifying the definition of operator and amending AASB1059.BC129.

However, before AASB grants such an exemption:

- it will be important to understand the AASB's rationale for scoping in such arrangements in the standard in the first place and taking a different approach to AASB Interpretation 12 that only deals with public to private service concession arrangements
- a proper impact assessment will need to be conducted as some arrangements are between two public sector entities but in different sectors (that is, one public sector entity is in GGS and the other in the PNFC sector). Therefore, scoping out arrangements could mean an impact on the balance sheets of such sectors.

Another important point which we recommend the AASB to clarify is the interaction of AASB 1059 with AASB 10 (which is most relevant in case of public-to-public service concession arrangements). Generally, if the operator is controlled by the grantor under AASB 10, it will be difficult to meet the criteria 'whether the operator has discretion in managing some of the public services' because if any action of the operator is subject to the approval of the operator's Board and the operator's Board is controlled by the grantor, then AASB 10 will overrule AASB 1059.

One jurisdiction previously had a toll road operated by a public sector subsidiary, with the PPE of the roads accounted for on-balance sheet of the operator. This arrangement has now ceased.

Topic 4: Recognition and measurement of service concession assets and related liabilities

Topic 4A: Recognition and measurement of service concession assets

Question 7
Do you have any comments regarding: (a) initially measuring a service concession asset at its current replacement cost using the cost approach in AASB 13; and (b) subsequently measuring the service concession asset at current replacement cost under the revaluation model in AASB 116 or AASB 138 (if the revaluation model is adopted by the entity)? Where you do have comments on (a) and/or (b), please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Mandating the (replacement) cost model

ACAG believes that the mandated measurement at current replacement cost (CRC) should be reconsidered, and preferably removed, as it as an unnecessary modification to IFRS.

The majority of ACAG jurisdictions also disagree with the resultant accounting especially in case of an internally generated intangible asset recognised at nil, then revalued to millions of dollars (even though it is still controlled by the grantor), and then at the end of the service concession arrangement, it retains this revalued amount.

There should be less need for this requirement (based on the perception that some people previously interpreted AASB 13 as requiring a discounted cash flow approach for an asset held for its service potential) given the changes to AASB 13 by AASB 2022-10 *Amendments to Australian Accounting Standards – Fair Value Measurement of Non-Financial Assets of Not-for-Profit Public Sector Entities*.

The valuation of land registries using CRC has proved particularly challenging, specifically related to:

- what is the unit of account (the database or a record)?
- how new records should be treated (as a revaluation adjustment or asset addition)?
- to the extent the new record is an addition, how should they be accounted for? Also, how does the addition of new records to the database that increases the service concession asset value interact with the argument that the overall cash generating ability of the database has not changed and arguments that the land registry has an indefinite useful life?
- the anomalous situation (caused by being heavily reliant on the entity's own information about the costs of processing) that an inefficient approach, reliant on manual records and processing, results in a higher valuation than that of a more efficient approach assuming that the valuation is based on replacing the records in their current form in the current system.

The majority of ACAG jurisdictions believe that because of the high degree of estimation uncertainty, the valuation borders on not being relevant or reliable. Those who have revalued have disclosed the basis for that valuation given the degree of assumptions involved. For example, Attorney-General's Department.pdf (audit.sa.gov.au) Note 5.2. Another jurisdiction did not recognise this intangible service concession asset on the basis that the valuation could not be measured reliably.

The majority of ACAG jurisdictions do not consider the resulting information useful to users. Although acknowledging the valuation challenges, one jurisdiction considers the resulting information useful to users have considered the value it provides to the private sector who are willing to pay money for it.

Mandating the (replacement) cost model – construction work in progress

The examples are confusing in relation to revaluation of service concession assets under construction. The examples seem to indicate that the service concession asset is revalued to (replacement) cost even when not yet in use. Some jurisdictions ordinarily require the (historical) cost model to be used for PPE under construction.

Mandating a revaluation on change in use

ACAG believes that the mandated revaluation of service concession assets on change of use from non-service concession assets to service concession assets should be reconsidered, and preferably removed, as it as an unnecessary modification to IFRSs.

The main practical issue for this is the land registries – if an agency controlled the registry before the service concession arrangement, and controls it after the service concession arrangement commences, why does the AASB force a revaluation (especially of intangibles) not otherwise permitted by the standards?

No other standards require a forced revaluation for a change in use (unless after the change in use fair value is the new measurement model – for example, PPE to investment property at fair value).

Question 8
Do you have any comments regarding the recognition and measurement of a service concession asset under construction? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

ACAG believes that the AASB should provide clear guidance on how the progressive recognition of an asset during construction should be recorded, that is, at cost or fair value as the current guidance provided in AASB 1059, particularly examples 6, 7 and 8 is causing confusion. Two jurisdictions have adopted an interest accretion approach to determine a fair value uplift in order to continue to recognise assets under construction at fair value. The interest accrual on the financial liability from the State to the operator is used as a proxy for the increase in the value of work-in-progress (WIP) during the construction period.

A majority of ACAG jurisdictions believe that service concession assets under construction should not be mandated to be valued at fair value. This view relates both to the issues in the above response to Question 7 and to the objection of including borrowing / funding costs (refer to response below to Question 9).

One jurisdiction supports the fair value model during construction. This is because if the asset is not carried at fair value under-construction, entities will have an adjustment when the asset is reclassified from WIP and gets recognised as service concession assets.

Question 9
Do you have any comments regarding the calculation and treatment of borrowing costs or implied funding costs in measuring the current replacement cost of a service concession asset? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Illustrative examples 6, 7 and 8 include implied funding costs in the current replacement cost of the road (paragraphs IE18, IE 24 and IE34(a) and (c)), however there is no guidance or mention in the standard itself on implied funding costs. As these implementation examples only accompany, but do not form part of the standard it is not clear whether these implied funding costs need to be included in the current replacement cost of an asset when construction occurs over more than one year. It is also not clear what the purpose is of including the implied funding costs in the CRC. For example, is the purpose of implied funding costs to include borrowing costs while the asset is being constructed or an uplift on WIP assets in order to continue to recognise these at CRC? If the purpose is for WIP assets

to be valued at CRC then borrowing costs alone in a high inflationary environment will not necessarily result in the asset being recorded at its fair value and other indexation may be required.

If the AASB requires implied funding costs to be included in the CRC of a service concession asset under construction, then ACAG believes it is important for the AASB to add guidance on the purpose of implied funding costs and the circumstances when these costs should be included in the CRC of a service concession asset to ensure the requirements are consistently applied. ACAG notes that providing guidance would be inconsistent with the AASB's decision not to provide guidance on borrowing costs in the recent AASB 2022-10 amendments to AASB 13.

As noted above, the examples appear to revalue the service concession assets under construction and not yet in use. Some jurisdictions ordinarily require the (historical) cost model to be used for PPE under construction.

ACAG also has specific concerns with the examples that we have detailed below. ACAG therefore believes illustrative examples 6, 7 and 8 of AASB 1059 need to be revisited and revised.

Example 6

The example is confusing. For example, paragraph IE17 states "the asset is recognised as it is constructed (CU525 in year 1 and CU557 in year 2)." However, this does not appear to be aligned with the underlying accounting we expect in the example (and which is illustrated in Table 6.2) which is:

Dr	Asset		525	
Cr		Financial liability		525

Year 1 construction of the asset

Dr	Asset		525	
Cr		Financial liability		525

Year 2 construction of the asset

Dr	Finance expense		32	
Cr		Financial liability		32

Finance expense of 6.18% on financial liability of 525

Dr	Asset		32	
Cr		Asset revaluation reserve		32

Increase in fair value (current replacement cost) of the asset

This example is also confusing as the increase in the fair value (current replacement cost) uses the borrowing costs of the operator, and not the borrowing costs of the grantor or an assessment of the borrowing costs of a (usually non-existent) hypothetical market participant.

Example 7

This example is confusing and appears incorrect in its underlying reasoning. The example (paragraph IE24) includes an implied funding cost as part of the cost of the asset acquisition – being the second year of construction of the asset. No funding cost is included in the acquisition / construction of the asset in Year 1, or for the replacement surface layer in Year 8.

There is no indication that there is some sort of deferred payment or implied financing of the construction of the road in Year 2. The GORTO liability is broadly unearned revenue and not a financial liability, so including a financing expense for unearned revenue appears incorrect. Therefore, inclusion of an implied funding cost in Year 2 appears incorrect and should be removed.

Also, the treatment of the carrying value under fair value current replacement cost is not clear. Paragraph IE23 includes a cost of Year 2 of 557. In reality, it is a cost of 525. There is an additional 32 for the implied funding cost that is not part of the cost of the asset. Instead, it appears that there is an increase in current replacement cost of 32 – but no increase in the asset revaluation reserve. This accounting treatment is different from example 6, where the increase in fair value has been recognised in the asset revaluation reserve rather than in the financial liability.

Similar to our comments on Example 6 above, ACAG questions the use of the operator's funding costs in a current replacement cost valuation.

Example 8

This example should be updated for the above comments. The accounting treatment of the uplift in example 8 for a hybrid arrangement only applies the principles for the financial liability in example 6. It is not clear why different methods have been used for the financial liability and GORTO methods or why in the case of a hybrid arrangement the implied funding has not been calculated using the principles in both examples 6 and 7.

Question 10
Do you have any comments regarding the recognition and measurement of upgrades or replacement of major components of a service concession asset? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Upgrades

AASB 1059.B38 and B48 requires the grantor to recognise an upgrade (for example, an increase in capacity) or the replacement of a major component of an asset as a service concession asset and a corresponding liability, when the upgrade or replacement occurs, whereas paragraph B59 states that after initial recognition, a grantor applies AASB 116 or AASB 138 to subsequent costs incurred. It is currently unclear how minor capital additions to a service concession asset that are not an upgrade or major replacement should be accounted for e.g. should these be treated as lifecycle costs. The section below contains more details on lifecycle payments.

Paragraph IE7 is causing confusion, as it does not adequately explain how to account for upgrades. The paragraph's wording "then it would be appropriate to instead recognise revenue relevant to that improvement only once it has occurred" can be interpreted as meaning that revenue can be recognised immediately once the improvement upgrade has been completed. However, would this not be an upgrade captured by B48 and therefore require recognition of a corresponding liability? The inclusion of a new lane is not actually included in the implementation examples, and it is therefore difficult to understand the AASB's intent.

Lifecycle payments

Many service concession arrangements relating to the operator constructing the underlying asset also have provisions for the operator to maintain the underlying asset to a particular performance standard (for example toll roads). Arrangements involving the operator constructing an asset, that may not be considered as a service concession arrangement and were accounted for as a purchase, have similar arrangements for the operator to maintain the asset at a particular performance standard (e.g. school buildings). These payments relate to capital expenditure replacements, and are considered separate to ongoing facility maintenance payments.

Lifecycle payments might include categories such as building substructures, columns, roof, windows, doors, floor finishes, fitments, plumbing, mechanical services, fire protection, electric light and power, communications and hydraulics.

There is diversity in how lifecycle payments are accounted for, with the accounting treatment often being dependent upon the availability of information provided by the operator to the grantor. If the information is not available, the payments are generally expensed. In other instances, the replacements are accounted for similarly to capital expenditure replacements under AASB 116 as they can be tracked because monitoring of the asset management plan is sufficiently detailed, and/or there is cost sharing / gain sharing over set thresholds (that is, someone is monitoring the payments and what is being purchased).

A further complicating factor is that sometimes the lifecycle payments are paid based on expected timing and amounts (with the consequence that payments are lumpy), and sometimes they are 'straight-lined'. If the payments are 'straight-lined' (that is, having a consistent lifecycle payment in the quarterly service cash payment), then there is an element of a prepayment.

The operator effectively takes on the risk (including potential benefits) associated with the timing and quantum of lifecycle costs. There may be no contractual requirement for the operator to spend predetermined lifecycle payments on specific assets at a specific point in time. Further, there may not be any contractual obligation to substantiate actual expenditure incurred by the operator to the grantor. However, the lifecycle payments are based on an expected level of service from the assets – that is, if the underlying assets deteriorate earlier than expected, the operator is required to replace the assets without additional payment from the grantor.

Because of the diversity in accounting for lifecycle payments, ACAG requests the AASB to provide further guidance on the issue. As noted above, this issue also applies to arrangements that are not classified as service concessions.

Intangible assets – Land registries

There is a diversity of views in how to account for record 'additions' to the land registry databases. As noted above, there are related issues for the valuation of these databases. The divergence is in part due to differences in interpretation about what is actually providing the service potential of the asset, and what is the unit of account.

One argument is that new records should be accounted for as part of the overall revaluation of the asset. This is premised on the argument that the additional records would not seem to be 'upgrades or replacements' of major components of service concession assets and therefore those paragraphs of AASB 1059 which would require these to be treated as new service concession assets do not apply.

Under this argument, the requirements of AASB 138 should be applied. Broadly, if the database was accounted for as an owned asset, subsequent expenditure would not meet the capitalisation criteria (similar to other internally generated intangible assets like customer lists).

Further, this argument is based on a view that the service potential of the data assets is embodied in the state's statutory obligation to provide land titling and administrative services to the public and therefore is it those services as a whole that represent the service potential, not the number of records in the database. Rather, the entry of new records maintains the service potential of the asset.

The alternate view is that as components of the database, new records have service potential that increase the value of the land registry database (noting that for not-for-profit entities, future economic benefits are synonymous with the notion of service potential). Without these new records, the land registry database would not be current and complete. Therefore, new records increase the value of the service concession asset and the GORTO liability (paragraph 11).

Question 11
Do you have any comments regarding how contract modifications should be accounted for under AASB 1059? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Service concession arrangements are often subject to numerous changes from the Base Case Financial Model, for example differences between actual and expected CPI. However, these modifications are dealt with within the agreement.

The following were examples of some of the modifications encountered by jurisdictions that involved amendments to agreements (some details slightly changed for explanatory purposes):

Hospital Car Park lease:

- Commenced 1999, original term 20 years.
- Amended 2005 to include expansion for additional floors. Original term extended 6 years (so remaining term is 20 years from amendment date).

Toll road

- Initial agreement for Toll Road A, original term 40 years (from 1996 – completion 2000) (terminating 2034).
- Expansion of Toll Road A (additional lanes) – Concession was increased by one year, minimum toll increase of 4.5% retained for an additional year (that affects all future tolls) and truck tolls increases.
- Additional agreement for Toll Road B – Construction commenced in 2018 (still under construction). Consideration by operator was for tolls on this Toll Road B until 2045 and for an extension of the Toll Road A concession (as expanded) for another 10 years (terminating in 2045) and a higher annual minimum toll increase.

Difficulty was encountered with the toll road example particularly in relation to the amortisation of the GORTO liability and revenue recognition (refer Question 16).

In NSW, there have been various contract modifications to toll road arrangements prior to implementation of AASB 1059. For information on these, the AASB can refer to note 14 of Transport for NSW's publicly available financial statements.

Modifications to existing service concession arrangements are likely in the future. The AASB should consider the above examples in providing guidance on contract modifications.

Question 12
Are there any other comments regarding the AASB 1059 recognition and measurement requirements for service concession assets that you think the AASB should consider?

The Queensland Audit Office, in March 2017, advised the AASB of issues relating to variable consideration for service concession arrangements in its response to *AASB 10XY Service Concession Arrangements: Grantors – Fatal-Flaw Review*.

> https://www.aasb.gov.au/admin/file/content106/c2/QAO%20Response%20-%20Fatal%20Flaw%20Review%20-%20AASB10XY%20SCA%20for%20Grantors_24-03-2017_153439.pdf

While there are no further variable consideration payments for the identified arrangement, the accounting for such payments has not been resolved for future service concession arrangements.

Topic 4B: Recognition and measurement of liabilities in service concession arrangements

Question 13
Do you have comments regarding the application of the requirements in paragraphs 11 and 12 of AASB 1059 to initially measure the liability at the same amount as the service concession asset, subject to certain adjustments? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

The statement 'initially measure the liability at the same amount as the service concession asset' is causing confusion, as there are potential differences in the accounting for the service concession asset and related liability (financial liability and/or GORTO liability) at the different times of asset construction, during construction of the asset and at construction completion.

ACAG has highlighted above under Question 9 issues related to:

- Example 6 (financial liability) where the service concession asset and liability appear to be the same during the construction period as we have concerns as to why and how that was achieved.
- Example 7 (GORTO liability) where we have highlighted that the example appears incorrect by capitalising a financing cost on unearned revenue – that results in the service concession asset and liability appearing to be the same on completion.

In these examples, it is not clear whether the asset is the same as the service concession liability during construction because it is required, or it is the impact of recognising interest accretion using different methods i.e. through revaluation surplus (under the financial liability model and hybrid models example 6 and 8) and as an addition to the unearned revenue liability (under the GORTO model in example 7) or just a coincidence.

To ensure that the standard is being applied consistently, ACAG suggests the AASB clarify whether a liability needs to be measured at the same amount as the service concession asset as the asset is being constructed, on completion or both.

Question 14
In addition, do you have comments regarding the application of AASB 1059 requirements to initially recognise a partly completed service concession asset (or asset under construction) and associated liabilities? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Jurisdictions have also had difficulties in certain instances when validating costs related to service concession assets under construction as:

- details provided by the operator are not detailed enough
- there is difficulty validating the costs provided by the operator when the grantor is not necessarily approving the invoices for costs incurred during construction by the operator
- there is difficulty in segregating values of plant and equipment and land and buildings at the WIP stage.

Further, current replacement cost (fair value) is expected to include amounts such as share of overheads, profit margin on the construction amount etc. (per IVS 105). It is difficult for an auditor to obtain assurance over these amounts as these will not be included in invoices.

Question 15
Do you have comments regarding the subsequent measurement requirements for financial liabilities? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Issues related to variable consideration raised previously by the Queensland Audit Office are included above under Question 12.

One jurisdiction encountered a divergent interpretation in applying the standard for an otherwise GORTO arrangement (operator takes risk for volume), but there were potential minimum guarantee payments, where the grantor pays any shortfall between the amounts received by the operator from users and the contracted minimum consideration for the operator. The divergent interpretation was that the entity recognised a GORTO liability (equal to the service concession asset constructed), plus a provision for the grantor's best estimate of the expected shortfalls. However, the Audit Office in that jurisdiction enforced the view that the entity should instead recognise:

- a gross financial liability for the present value of the minimum guaranteed amounts over the term of the arrangement using the contractually specified interest rate;
- a GORTO liability for the difference between the service concession asset and the financial liability (thus resulting in a hybrid arrangement); and
- the revenue received from the users.

Question 16
Do you have comments regarding the initial and subsequent measurement, including amortisation, of GORTO liabilities? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Question 11 includes an example from one jurisdiction where an operator manages multiple service concession projects for the grantor and the operator's right to charge tolls are intertwined amongst various projects. In that example, the grantor entered into a GORTO arrangement with the operator to construct Toll Road B, and as part of the consideration the operator was able to charge tolls on Toll Road B, and was also given the right to charge tolls on Toll Road A for an additional 10 years (after the original termination of the Toll Road A agreement) and the operator was given a higher annual minimum toll increase for Toll Road A.

The provisions in AASB 1059 on the amortisation of the GORTO liability caused confusion. AASB 1059 paragraph 22 states that the grantor shall reduce the GORTO liability and recognise revenue according to the economic substance of the arrangement.

On one hand AASB1059 paragraph B71 states revenue is usually recognised as access to 'the service concession asset' is provided to the operator over the term of the service concession arrangement. In most cases, access to the subject service concession asset is uniformly provided to the operator over the term of the arrangement (as the arrangement involves one asset). Similarly, from a grantor's perspective it has received the service concession asset 'free of charge' uniformly over the agreement period. Therefore, revenue should be recognised on a straight-line basis. Furthermore, Toll Road B is available for use by toll users equally over the service concession period, therefore the straight-line method is justified.

On the other hand, for GORTO arrangements, the grantor recognises a liability 'for granting the operator the right to collect tolls' (AASB 1059 paragraph IE24). Therefore, if the right to collect tolls is not uniform over the term of the arrangement as in the example above, it can be argued that the GORTO liability should not be amortised on a straight-line basis. In this example, the receipt of tolls by the operator is back-ended in the later years (the extension of the tolling arrangement on Toll Road A from 2035 to 2045). AASB 1059 paragraphs BC78 to BC80 states that the liability is analogous to a contract liability under AASB 15 that should represent remaining performance obligations under the contract at any time. Therefore, if the grantor has granted the right to the

operator to charge tolls on multiple arrangements as a consideration for the service concession arrangement (which could be considered as a performance obligation), then the GORTO liability should not be amortised on a straight-line method basis.

Therefore, based on the above, it is not clear which notion should be followed i.e. having uniform access to the service concession asset (asset side notion) or granting right to the operator to charge toll revenues (liability side notion) which may not be uniform.

Question 17
Are there any other comments regarding the AASB 1059 recognition and measurement requirements for liabilities of a service concession arrangement that you think the AASB should consider?

No additional items identified.

Topic 5: Other matters

Question 18
Do you have any comments regarding the disclosure requirements in AASB 1059 (paragraphs 28 and 29), which cover both qualitative and quantitative information about a grantor's service concession arrangements? If so, please provide your views on those requirements and their significance.

Treated as a separate line-item class on face of balance sheet

As noted above under Question 1(b), at least one jurisdiction's Treasury department has mandated that service concession arrangement assets be disclosed as a separate line item on the face of the balance sheet, even though the assets are a similar nature as other PPE infrastructure assets. We noted that this may lead to the loss of information as assets that would otherwise have been disclosed as land, buildings and infrastructure are classified as a different asset grouping and note to the financial statements.

Question 19
Do you have any comments regarding the Implementation Guidance and Illustrative Examples that accompany AASB 1059? If so, please provide your views and any suggested amendments.

The illustrative examples appear simplistic. Based on the comments provided in the sections above and areas highlighted, we recommend the AASB to include more guidance and illustrative examples for achieving consistent application of the standard. Following are ACAG's specific comments on some examples:

Previous comments on examples

ACAG has highlighted above under Question 9 issues related to Examples 6 (financial liability), 7 (GORTO liability) and 8 (combination).

Borrowing costs

ACAG believes that given the AASB's decision not to provide guidance on the treatment of borrowing costs for fair value under the modifications to AASB 13 by AASB 2022-10, the AASB should be consistent with that decision and not provide guidance in AASB 1059. This would require amendments to examples 6, 7 and 8 on the inclusion of implied funding costs.

Already on-balance sheet assets

As noted above, (in particular Questions 1 and 4) there is diversity in whether already on-balance sheet arrangements, where no substantive operating provisions of the standard apply (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator) are (or should be) accounted for under AASB 1059.

ACAG requests additional implementation guidance and illustrative examples to clarify, and if necessary, revise the criteria, so that the AASB 1059 criteria are suitably discriminatory.

Land under service concession assets

One jurisdiction suggested that the AASB should clarify in the Implementation Guidance and the Illustrative Examples that the existing land owned by the grantor on which a service concession asset is constructed by the operator should also be reclassified by the grantor as a service concession asset.

Question 20
Are there any other matters that the AASB should consider as part of this PIR? If so, please explain those matters and why they should be considered, and provide examples to illustrate your response. For example, in your view are there new or emerging arrangements for which it is difficult to determine whether they are within the scope of AASB 1059 or for which service concession accounting might not be suitable? .

As discussed above under Question 10, there is diversity in how lifecycle payments are accounted for.

The diversity relates to service concession arrangements, and arrangements that fail the AASB 1059 criteria (for example public-private partnerships where the construction of the asset is considered a purchase).

AASB General Matters for Comment

Question 21
Does the application of AASB 1059 adversely affect any regulatory requirements for grantors?

One jurisdiction noted that a local government's statutory reporting ratios were affected by AASB 1059 – this being the only local government with material service concession arrangements, that were not already on-balance sheet.

Question 22
Does the application of AASB 1059 result in major auditing or assurance challenges?

Yes, the major auditing or assurance challenges include those areas where there is significant amount of judgement and those where there is a lack of guidance. Those that have been discussed above include:

- determining whether an asset provides public services (Question 1)
- applying the term 'on behalf of the grantor' (Question 1)
- applying the term 'on behalf of the grantor' when the agency may not have the primary responsibility for providing the public service (Question 1)
- whether an arrangement can be accounted for as a service concession arrangement at a consolidated whole of government level, when this has not been accounted for as a service concession arrangement at the individual agency level (Question 1)
- determining whether the operator provides at least some of the management of the public service at its own discretion (Question 1)

- whether a secondary asset provides public services, particularly when it was constructed after the initial asset (which may or may not have itself been the subject of a service concession arrangement) (Question 1)
- whether a service concession arrangement granted over a secondary asset can be within the scope of AASB 1059 where the primary asset is controlled by a different public sector entity (Question 1)
- partly-regulated assets (Question 3)
- residual interest (Question 3)
- diversity in applying the control criteria (Question 4)
- valuing land registries using current replacement cost – note this will be an on-going issue for these arrangements and involve additional costs every year (Question 7)
- applying the concept of implied funding costs (Question 9)
- lifecycle payments (Question 10)
- variable consideration (Question 12)
- accounting for assets under construction (Question 14)
- minimum guarantee payments (Question 15)
- upgrades, including linking to other service concession assets (Question 16).

Question 23
Overall, does AASB 1059 result in financial statements that are more useful to users of public sector grantors' financial statements?

ACAG generally agrees that putting on-balance sheet arrangements that the grantor controls makes public sector grantors' financial statements more useful.

As noted above, there is less agreement amongst ACAG offices about the treatment of already on-balance sheet arrangements, and as noted above, whether these are actually service concession arrangements – particularly if the operator is not involved in construction or capital expenditure renewal. It is also noted that such already on-balance sheet arrangements are often encountered in local government short-term management arrangements with the private sector.

Also as noted above, ACAG believes that there is scope to increase the consistency in accounting for service concession arrangements by providing additional guidance in the key areas we have mentioned.

As noted above under Question 7, ACAG believes that the following AASB 1059 provisions should be reconsidered, and preferably removed, as there are an unnecessary modification to IFRSs:

- the mandated revaluation of service concession assets on change of use from not being used as service concession assets to being used as service concession assets
- the mandated use of CRC.

The majority of ACAG jurisdictions believe that revaluing land registries (which would not otherwise be recognised under AASB 138) does not provide useful information.

Question 24
In your view, do the benefits of applying the requirements of AASB 1059 exceed the implementation and ongoing application costs?

ACAG is not able to comment generally on the costs and benefits of the proposals.

However, the majority of ACAG jurisdictions believes that the valuation and audit of the valuation of previously unrecognised intangible assets (in particular, land registries) has resulted in the costs exceeding the benefits.

ACAG believes that if the AASB clarifies the issues above, and provides more guidance where relevant, this will reduce the costs of applying AASB 1059.

Appendix A – On-Balance sheet arrangements

The following are examples provided by one jurisdiction in applying the service concession criteria to already on-balance sheet arrangements, and where the substantive provisions of the standard did not apply (i.e. there was no GORTO liability, and no financial liability). Some, but not all, of the arrangements were classified as service concession arrangements.

- Prisons – Constructed by agency and maintained by agency
- Water treatment plant – Constructed by agency and maintained by agency
- Social housing – Housing constructed by agency and maintained by agency
- Grant for health services using grantor owned buildings
- Land required to be used for public space as part of property development arrangement

Prisons – Constructed by agency and maintained by agency	
AASB 1059 criteria	**Analysis**
Operator providing public services	Yes – Prisons are managed by the public sector
Operator managing at least some of those services under its own discretion	Yes – Operator has discretion in how prisoners and prisons are managed, and are subject to key performance indicators
Grantor controls or regulates what services the operator must provide	Yes – Operator must provide prison and prisoner services
Grantor controls to whom the operator must provide services	Yes – Operator must provide services to prisoners as determined (by the courts) and the grantor
Grantor controls what prices the operator charges	Yes – Grantor requires that no fees be charged to prisoners
Grantor controls any significant residual interest	Yes -–Buildings are already owned by the grantor

Another jurisdiction, with similar arrangements, concluded that the operator did not have sufficient discretion because of the detailed requirements, including restrictions on reducing staff numbers, transferring key personnel, the number of shifts required, the number of hours per shift and expected annual hours per position.

Water treatment plant – Constructed by agency and maintained by agency	
AASB 1059 criteria	**Analysis**
Operator providing public services	Yes – Providing potable water is a public service
Operator managing at least some of those services under its own discretion	Yes – Operator must ‘operate the facility so that it can provide the Services to at least the Performance Standards at its own cost and risk’
Grantor controls or regulates what services the operator must provide	Yes – Water treatment plant can only be used for water treatment
Grantor controls to whom the operator must provide services	Yes – Services must be provided to the public
Grantor controls what prices the operator charges	Yes – Operator cannot charge any additional fees
Grantor controls any significant residual interest	Yes – PPE already owned by the grantor

Another jurisdiction, with BOOT arrangements for similar assets, concluded that the operator was not providing a public service, as the service was used internally by the grantor.

Social housing – Housing constructed by agency and maintained by agency	
AASB 1059 criteria	**Analysis**
Operator providing public services	Yes – Social housing is a public service
Operator managing at least some of those services under its own discretion	Yes – Operator has discretion in managing and selecting tenants.
Grantor controls or regulates what services the operator must provide	Yes – The social housing must be used for social housing
Grantor controls to whom the operator must provide services	Yes – The social housing must be provided (subject to capacity) to those that meet grantor determined eligibility
Grantor controls what prices the operator charges	Yes – Grantor determines rent, or discount to market
Grantor controls any significant residual interest	Yes – PPE already owned by the grantor

Grant for health services using grantor owned buildings	
AASB 1059 criteria	**Analysis**
Operator providing public services	Yes – Health services a public service
Operator managing at least some of those services under its own discretion	Yes – Operator has discretion in managing and selecting patients
Grantor controls or regulates what services the operator must provide	Yes – The grantor owned buildings must be used for the designated health services
Grantor controls to whom the operator must provide services	Yes – The grantor refers selected patients to the operator
Grantor controls what prices the operator charges	Yes – The operator is not permitted to charge any additional fees to the patient
Grantor controls any significant residual interest	Yes – PPE already owned by the grantor

Land required to be used for public space as part of property development arrangement. Operator / property developer permitted to use major parts of land for retail. Hotel and carpark usage, but must use some of the land for public space	
AASB 1059 criteria	**Analysis**
Operator providing public services	Yes – Providing land as public space is a public service
Operator managing at least some of those services under its own discretion	Yes – Operator permitted to hold events, at its discretion, on public space – as long as access to public space not unreasonably restricted
Grantor controls or regulates what services the operator must provide	Yes – public space must be provided for public space
Grantor controls to whom the operator must provide services	Yes – the public space must be open to the public
Grantor controls what prices the operator charges	Yes – the public space must be open to the public for free
Grantor controls any significant residual interest	Yes – The property / land is already owned by the grantor

Dr. Keith Kendall
Chair
Australian Accounting Standards Board
PO Box 204
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via submission portal: https://www.aasb.gov.au/current-projects/open-for-comment/

27 February 2023

Dear Sirs,

RE: AASB Invitation to Comment ITC 49 *Post-implementation Review of AASB 1059* Service Concession Arrangements: Grantors *(ITC 49)*

I am responding to your invitation to comment on the Post-implementation Review of AASB 1059 on behalf of PwC.

We welcome the Board seeking feedback in relation to the application of AASB 1059 *Service Concession Arrangements: Grantors*. Having worked with a number of clients in this area, we highlight the following key areas where enhancements may be made to enable more consistent application:

- providing further indicators to support preparers in identifying whether the arrangement is in scope of AASB 1059 and
- clarifying the measurement of the GORTO liability for service concession assets under construction.

We also consider that the requirement to use current replacement cost to measure the fair value of service concession assets (SCA) should be a presumption that could be rebutted in certain situations.

Detailed feedback on these issues and recommendations of how they might be addressed are in the Appendix to this letter.

While we have just highlighted our more significant observations in this letter, we will organise a call to discuss our more detailed comments and further explain any questions you may have.

Yours sincerely,

Erin Craike
Partner

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Appendix

Is an arrangement in the scope of AASB 1059?

Topic 1: Public Service

We do see diversity in practice in relation to assessing whether a transaction is in the scope of the standard in the following areas:

- Operator involvement in the management of the asset -- An example of where we see challenges in this assessment is where maintenance for an asset is essential to the provision of a service (such as, for trains). Preparers may take analogy to Example 2(a) where facility maintenance is not considered to represent a significant component of the provision of the public service. We do not consider this to always be appropriate.

- Identifying whether an asset provides public service -- We have also seen diversity arise in this assessment where assets subject to the arrangement have a commingled public service (i.e., provision of cultural experiences that provide benefits to the local economy) and commercial purpose. Examples may include stadiums, assets related to the arts, universities, zoos, convention centres, and student accommodation. In practice, many consider these are not public services. However, we do not consider this to always be appropriate, depending on the circumstances.

We acknowledge that it is difficult to strictly define a public service and that there will often be significant judgement involved in making assessment. However, additional indicators may be provided to encourage more consistent application. Indicators are often more helpful than examples to ensure that inappropriate analogies are not made (i.e., always considering maintenance to be an ancillary service even where it is essential, always considering student accommodation to be a public service even though there are cases where it may be largely used by foreign fee paying students). As in other areas of Australian Accounting standards, we would expect the indicators to be considered collectively with no single indicator necessarily leading one to conclude that an arrangement is either within or out of scope of AASB 1059.

Collective indicators are used in the public sector specific guidance for AASB 17 to help assess whether an arrangement gives rise to insurance contracts that fall within the scope of AASB 17. This approach is quite helpful in providing direction to preparers in assessing their facts and circumstances. If particular indicators are considered more or less important, a ranking such as that used in Appendix E of AASB 2022-9, which distinguishes between pre-requisites, indicators and other considerations, could also be introduced. Primary and secondary indicators in AASB 121 are also useful to help preparers prioritise those indicators that are most important.

While the application guidance in Appendix B of AASB 1059 provides features of a service concession arrangement, we consider this guidance could be compiled into a list of indicators to be assessed collectively. Using the existing discussion in Appendix B as a starting point, potential indicators to assess whether the service provided is a 'public service' could include:

- Are the services provided by the asset necessary or essential to the general public? (AASB 1059, par. B6)
- Are the services generally expected to be provided by a public sector entity? (AASB 1059, par. B6)
- Would the government be required to step in if the services were not provided by private sector entities?
- Does the asset provide other (eg, unrelated) services, and, if yes, how significant are these services to the arrangement? (AASB 1059, par. B6)
- In the case of a secondary asset, is the asset constructed at the same time and will the asset be mainly used to complement the primary asset, i.e., to provide ancillary services? (AASB 1059, par. B7) Are the profits of the secondary asset being used to subsidise the cost of the public service provided by the primary asset?
- Are the services used wholly internally by a public sector entity for the purpose of assisting the public sector in delivering public services to domestic residents/citizens? (AASB 1059, par B8)
- To what extent is the asset used for commercial purposes (for example, would it be uneconomic for a private sector to provide those services at the prices that can be charged to the public)?
- Does the grantor subsidise the running cost of the asset in any form (for example, via the provision of land or other assets at no charge) and why?

Similarly, indicators could also be used to assess whether the operator manages at least some of the services at their own discretion. We consider that the following indicators may be useful:

- Do the operator's actions directly affect the public service that is being provided by the asset (for example, the actual running and/or scheduling of a hospital where the public service is the provision of hospital services, the scheduling of maintenance of transport or roads which directly impacts when the public service may be disrupted) or is there only an indirect impact (for example, providing building maintenance and security services to the hospital)? (AASB 1059, par. B10)
- How much discretion does the operator have over the services they provide and how many of the services to be provided are predetermined in the arrangement? For example, if the agreement specifies how often and when the operator must undertake specific maintenance activities, regardless of the state of the asset, the operator has little or no discretion to manage the relevant activities.
- What is the estimated cost/magnitude of the service being provided by the operator as compared to the total costs/magnitude of operating the asset?

Topic 3: Public sector operator

ITC 49 seeks feedback as to whether AASB 1059 should apply to public-to-public arrangements and acknowledge this issue has come up in practice. We agree that this is an area of diversity and are of the view that if sound indicators are provided, AASB 1059 should apply to public-to-public arrangements. In particular, we consider that application in public-to-public arrangements is important where the entities involved in the arrangement operate in different sectors or are GGS entities.

Requirement to use Current Replacement Cost (CRC)

Topic 4A: Recognition and measurement of service concession assets

While CRC generally leads to an appropriate outcome (in particular for new construction), there are instances where other valuation methodologies may be equally appropriate and of lower cost to preparers. For example, for-profit public sector entities more commonly use income-based valuation techniques to measure the value of assets (particularly in regulated utility businesses where a service concession asset forms part of a cash generating unit that is measured using the income approach). Because income-based valuation techniques are acceptable under AASB 13, we consider that this approach should also be acceptable under AASB 1059. As such, we would recommend a presumption that CRC is most appropriate, but acknowledges that other methodologies may be acceptable either generally, or at least in certain circumstances.

Measurement of Gorto Liabilities for Assets under Construction

Topic 4B: Recognition and measurement of liabilities in service concession arrangements

Based on our experience, service concession assets (SCA) under construction are generally revalued to fair value which results in borrowing costs (or implied funding costs) being included in the measurement of the current replacement cost (as accepted under AASB 13). Following the guidance in AASB 116, this revaluation is recognised in a revaluation reserve in equity. However, there is diversity in practice with respect to the measurement of the GORTO liability.

In some cases, preparers have interpreted AASB 1059, par. 12 to mean that the GORTO liability should be measured at the initial fair value of the SCA but that the GORTO liability should not be subsequently remeasured for changes in the fair value of the SCA during the construction phase. Neither the core guidance in the standard in paragraphs 11-12 nor paragraphs B70-B72 refer to such a remeasurement. In other cases, preparers have looked to Illustrative Example 7 to remeasure the GORTO liability during construction for capital expenditure and imputed funding cost. This remeasurement is also recognised in the asset revaluation reserve, offsetting that recognised for the SCA. Remeasurement of the GORTO liability ensures that it equates to the CRC of the SCA at the end of the construction period.

We understand the principle of the standard to be that the operator provides the fair value of the SCA to the grantor in exchange for the right to construct/operate/maintain the asset. The grantor's liability is to be measured at the fair value of the SCA, as that is the asset being received by the grantor in exchange for providing the rights to the operator per paragraph 12. As such, in our view, at the end of construction, the SCA should equal the liability. We also consider that AASB 116 should be followed with respect to remeasurement of the asset. As such, the standard should be clarified to be clear as to how the GORTO liability should be measured subsequent to initial recognition during the construction period.

SW
Accountants & Advisors

Take the lead

27 February 2023

Australian Accounting Standards Board
Podium Level 14,
530 Collins Street,
Melbourne VIC 3000

Dear Board Members

RESPONSE TO AASB – PIR OF AASB 1059

We would like to take the opportunity to comment on some of the technical issues that we encountered in implementation of AASB 1059 as part of this post-implementation review by AASB.

Issue 1: Accounting for occupancy guarantees.

In practice, a lot of service concession agreements that we review, provide for an 'occupancy guarantee' by the grantor to the operator in relation to the service concession asset involved. Typically, the occupancy guarantee takes the form of a promise to pay a deficiency in revenue in a certain period of the arrangement. The deficiency is determined as difference between a certain % of return from the asset and the actual return to the operator.

The issue we face here is the interpretation of paragraphs 15-16 read along with the related guidance in paragraphs B75-B78 in AASB 1059.

- Paragraphs 15-16 require that shortfall, if any, between amounts received by the operator from users of the service concession asset and any other specified or determinable amounts payable by the grantor **is to be accounted as a financial liability** since it represents a contractual obligation to deliver cash. Further, paragraph B63 appears to assert that any contractual obligation that cannot be discretionarily avoided is to be recognised as a financial liability.
- However, the impression we get from paragraphs B75-B76 (which term such commitments to pay revenue shortfall as a performance guarantee) is that the entity should assess **whether such guarantees are financial guarantees to be accounted as per AASB 9 or insurance contract (AASB 17) or provision as per AASB 137**.
- Adding an element of confusion is paragraph BC20 which states as below:
  "*The Board considered that compensation of revenue shortfalls in the context of AASB 1059 paragraph 16(b)* ***would not meet the definition of a financial guarantee*** *under AASB 9 for the grantor where the grantor is guaranteeing payments to the operator to cover lower usage of service concession assets than expected. Therefore,* ***insurance accounting would not be appropriate*** *in measuring the liability to the operator in the case of such revenue shortfalls.*"

Prima facie, the relatively straightforward requirement set out by paragraph 15 to recognise a financial liability appears to be contradicted by the requirement in paragraphs B75-B76 to recognise a financial guarantee or provision or as an insurance contract. We are at times made to suspect, whether the term 'financial liability' used in paragraph 15 is a generic term including 'financial guarantee' as well. But as we already know that AASB 9 and AASB 132 uses different definitions for these two terms, that view is not supported.

We would therefore request a clarification as to what is the exact expectation of AASB with regard to recognising such occupancy guarantees and if required make editorial corrections to ensure consistency. We feel, if AASB does not believe such revenue shortfalls are financial guarantee contracts or insurance contracts, then it would be better to be more explicit on the accounting requirement rather than directing the entity to assess further as per B75-B76 which prolongs the accounting process.

Issue 2: Explanation of the phrase 'contractual obligation to pay cash' – paragraph 15 and 16.

Paragraph 16 categorically states "*The grantor has a contractual obligation to pay cash* ***if it has agreed to pay the operator specified or determinable amounts***....."

We faced a couple of interpretational issues as below:

- Firstly, it is not clear what the paragraph means by the term 'determinable'. Is there a limitation to this determinability? For e.g., if a clause states that the shortfall is determined with reference to a market rate which is only derived by valuation techniques using unobservable inputs (as in AASB 13) or independent valuation by an expert, can these amounts be regarded as 'determinable' or should such rates be readily available/observable from externally published data. Some examples in this regard would be helpful to implement the standard in future.
- Secondly, as a matter of academic interest to us professionals, is AASB 1059 carving out a slightly different definition of financial liability from what we see in AASB 132? This is because AASB 132 contains no such additional phrase as '*if it is agreed to pay a specified or determinable amounts*'; it only requires determining whether there is a contractual obligation to deliver cash. Also, paragraph B63 does not contain the phrase "*if it is agreed to pay a specified or determinable amounts"* but instead uses the phrase "*to make a* ***predetermined*** *series of payments to the operator"* rather than 'determinable' amounts. Thus, apparently there is an inconsistency in the use of language across these paragraphs which requires clarification.
- If AASB does clarify what 'determinable' means in the context, it would be a relevant question as to what should be the accounting treatment of amounts that **are not 'determinable'**.

Issue 3: Insurance accounting of performance guarantees under AASB 17.

Clearly, the insurance accounting requirements were relatively primitive when AASB 1059 was first implemented. With AASB 17 becoming effective, the accounting requirements for insurance contracts are more detailed and disclosure requirements are significantly high. With that being the case, can there be an exemption for service concession arrangements from applying AASB 17 or perhaps more simpler requirements if they include a component of performance guarantee that meet the definition of an insurance contract. This is because we are of the following views:

- The core objective of the contract is to provide a service concession asset to an operator while providing insurance to the operator from specific uncertain event is only incidental. Requiring the grantor to recognise various components of insurance accounting may potentially obscure the main components recognised through the service concession arrangement and complicated for user who tend to be focussed on the economics of the service concession.

- The quid pro quo arrangement in these agreements can be unstructured and entirely different from typical insurance contracts where a premium is collected by the insurer as a compensation. This makes it onerous to apply AASB 17 in general.
- Being the simplest approach under AASB 17, the premium allocation method cannot be used in these arrangements since invariably all the service concession arrangements are for a term more than one year (one of the qualifying criteria for applying this method).

Thanking hereby for this opportunity, we would request AASB to take cognizance of some of the issues raised by us above and make suitable amendments and clarifications for a smoother implementation of AASB 1059 in future.

Kind Regards

Hayley Underwood

Heads of Treasuries Accounting and Reporting Advisory Committee
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Contact Member for Submission: Jeanne Vandenbroek
Jeanne.Vandenbroek@treasury.nsw.gov.au

6 March 2023

Dr Keith Kendall
Chair
Australian Accounting Standards Board
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Collins Street West
VIC 8007 Australia

Dear Dr Kendall

ITC49 Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to respond to AASB Invitation to Comment *ITC 49 Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors* (ITC 49). HoTARAC is an intergovernmental committee that advises Australian Heads of Treasuries on accounting and reporting issues. The Committee comprises senior accounting policy representatives from all Australian states and territories and the Australian Government.

HoTARAC members have experienced challenges of judgement in accounting and auditing of service concession arrangements. In general, HoTARAC members agree that AASB 1059 has resulted in financial statements that are more useful to users, though one member's dissenting view is explained in Appendix 1. To address the challenges in applying the standard, this submission requests further and stronger guidance in some areas and recommends the AASB reconsider the requirements to others.

If you have any queries regarding HoTARAC's comments, please contact Jeanne Vandenbroek from New South Wales Treasury on (02) 9228 5233 or by email to Jeanne.vandenbroek@treasury.nsw.gov.au.

Yours sincerely

Heads of Treasuries Accounting and Reporting Advisory Committee

ITC49 Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors

Topic 1: Public service

1. Do you have comments regarding the application of the following requirements of AASB 1059:
(a) the use of the term 'public service';
(b) the operator's involvement in providing public services on behalf of the grantor;
(c) the operator managing at least some of the public services under its own discretion; and
(d) the approach to secondary assets?
If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

ITC49:
"Some stakeholders have commented that: (a) determining whether an arrangement is within the scope of AASB 1059 involves significant judgement and can be challenging;
(b) it is unclear which services are considered 'public services' in order to determine whether an arrangement is within the scope of AASB 1059, particularly when an arrangement might also provide some commercial services;
(c) it is sometimes difficult to determine whether an entity is providing services 'on behalf of the grantor'. For example, if enabling legislation permits a public sector entity to hold an asset but prohibits it from using the asset to provide services in its own right, the entity would need to contract another party for the provision of services. In this situation, is the party that is providing the services using the asset considered to be providing services 'on behalf of the grantor'? Some stakeholders query whether the requirement to provide services on behalf of the grantor is necessary;
(d) there are instances where multiple entities are involved with the delivery of the public services with varying degrees of responsibilities, in which case it may be unclear which entity is the grantor, or the operator, of the arrangement and whether the provision of services is considered to be 'on behalf of the grantor';
(e) more guidance is needed to determine whether the operator is managing at least some of the services at its own discretion. For example, is an operator managing railway workers' rosters considered to be "managing some of the public services" when the operator has no control over the timing of the railway services?; and
(f) it is unclear whether an arrangement with a private sector entity to manage an existing local government facility (e.g. an aquatic centre, recreational centre or landfill site) for a short period (e.g. 2 years), where the local government entity sets the prices to be charged to users, should be considered a service concession arrangement.

In respect of secondary assets – an asset used or mainly used to complement the primary asset through which the public services are principally provided – some stakeholders commented that:
(a) more guidance is needed to determine whether a secondary asset is "largely providing public services" for the purpose of determining whether it should be accounted for under AASB 1059; and
(b) it is unclear whether a secondary asset should be recognised as a service concession asset under AASB 1059 where:

(i) the primary asset is controlled by a different entity;
(ii) the provision of the secondary asset is not part of the same arrangement as the provision of the primary asset; or
(iii) the secondary asset is constructed some time after the primary asset – AASB 1059 paragraph B7 does not specify the period between the construction of the primary asset and the secondary asset that would affect whether the secondary asset is considered to be part of the arrangement for the primary asset."

Public service

Under the existing standard, a lot of effort and judgement goes into assessing whether an arrangement involves provision of a 'public service'. Where the public service test is failed otherwise economically similar arrangements are accounted for differently.

Given the lack of a recognised definition of 'public service' globally and the tendency of public expectations to change over time, HoTARAC continues to believe that seeking to define a public service for the purposes of AASB 1059 would be problematic and may create further issues or unintended consequences.

HoTARAC acknowledges that the AASB may reassess whether the 'public service' concept needs to be retained as one of the conditions for an arrangement to be classified as a service concession arrangement. At this stage, HoTARAC would not support removing 'public service' as one of the conditions for an arrangement to be a service concession because the accounting implications of such a change need to be evaluated. It may result in arrangements that are not currently in scope being considered in scope.

Instead, HoTARAC would support more guidance on assessing whether an arrangement involves provision of a 'public service'.

In our view, whether something is a 'public service' should follow from the government policy that is specific to the relevant jurisdiction and considers changes in this policy over time. A good example would be banking and aviation services that were, for many years, government owned and operated prior to deregulation and privatisation. Deregulation and privatisation of certain markets may indicate that the respective services crossed the 'fine line', ceasing to be a public service and moving to a regulated market. HoTARAC notes this may result in different outcomes across jurisdictions, but believe this is consistent with the substance of each arrangement.

When providing examples to assess whether a service is a public service, the standard implies that the public services are expected to be 'necessary or essential to the general public and are generally expected to be provided by a public sector entity in accordance with government policy or regulation' (AASB 1059.B6). In our view, in the context of a particular jurisdiction, public services should not normally include services in the industries that have effectively been privatised in this jurisdiction. This is because in most cases privatisation represents government policy change where the relevant service ceased to be expected to be provided by a public sector entity in accordance with government policy or regulation.

Further, useful guidance could include indicators of a 'public service. Such a list of 'public service' indicators could include, for example, subsidised provision of goods or services, public regulatory and legislative activities/services (i.e. expected to be provided by a public sector entity in accordance with government policy or regulation), public ownership of associated assets. This could be supported with various examples (and contrasted with examples that are not public services).

The list of indicators could be similar to the list of factors (primary and secondary) considered in determining the functional currency in AASB 121 *The Effects of Changes in Foreign Exchange Rates* or the list of indicators to identify arrangements that fall within the scope of AASB 17 *Insurance contracts* in a public sector context.

Some jurisdictions may adopt, as a practical expedient, a rebuttable presumption that service provision arrangements a government enters into are arrangements to provide public services. This would align AASB 1059 with Interpretation 12 *Service Concession Arrangements* applicable to operators. While this would, in some cases, simplify scoping assessments, we do not recommend this presumption be included in the standard or guidance because applying such a presumption would result in more prescriptive outcomes based on form rather than the substance of the arrangement. As such it could result in certain arrangements that are not intended to be captured by AASB 1059 as falling in scope. Such a presumption would also not be appropriate to apply to arrangements that exist between two entities within the same jurisdiction.

A single asset providing multiple services

Assessing whether an asset provides public services requires judgement, taking into account the nature and relative significance of each of the services provided (AASB 1059.B6).

Guidance is requested on how to assess whether an arrangement/asset is fully or partially in scope of AASB 1059 or not in cases where the asset is used not exclusively for a service concession arrangement. Currently the examples in AASB 1059.B6 assume that the entire asset is subject to the same arrangement. Refer to the example scenarios below:

- An asset (e.g. a residential property) providing more than one public service with all the services significant and none of them ancillary (e.g. social housing services and medical support services), but only one of the services (social housing) is provided by the operator. The other one (medical support) is outsourced or provided by the grantor.
- An asset (e.g. a database) that is used partially as a service concession asset (SCA) and partially – for own government needs.

'On behalf of' concept

HoTARAC members have experienced challenges applying the "on behalf of" concept when determining whether an arrangement or asset is within the scope of AASB 1059. The concept appears to be a critical part of the definition of a service concession arrangement, and therefore key in terms of scoping. However, the Implementation Guidance does not deal with this concept in any detail, the standard does not provide any definition of 'on

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behalf of'. We find it clear 'on behalf of' is closely linked to 'public service' however the standard also does not provide a definition of public service (see discussion above).

We believe that the standard should have more guidance to help identify who the grantor is in situations where there is more than one government agency involved in the arrangement, for example:

- When one public sector agency (Agency 1) enters into an arrangement with another public sector agency (Agency 2), it can be challenging to identify whether Agency 2 is operating on behalf of Agency 1 or vice versa
- When one public sector agency (Agency 1) has primary responsibility for providing a public service and another public sector agency (Agency 2) is signatory to the contract with the operator (acting as agent for Agency 1) who is considered the grantor?
- When more than one public sector agency is a party to the arrangement with the private sector – such as when different public sector entities are responsible for the design, construction and operation phases - it can be challenging to identify which agency should be the grantor.
- In some jurisdictions, the State itself enters into arrangements on behalf of an agency and it is challenging to identify who the grantor is in those arrangements. Some jurisdiction received advice that such arrangements should dbe treated as administered at the agency level.

In our view, for a service to be provided "on behalf of" an agency, the agency should have the legislative function and primary responsibility for the service. Some examples of how this may look in practice include:

- When a public sector entity is established with certain legislative functions (e.g. holding and maintaining some public assets) but does not have the legislative or policy ability to *provide* a public service (with the use of the assets), then an operator cannot be seen to operate 'on behalf of' an entity which does not have the legislative function and primary responsibility for that service.
- where there is *more* than one government agency involved in an arrangement and each of them has their own legislative functions and primary responsibilities, in order for services to be provided "on behalf of" the grantor, the grantor should have the legislative function and primary responsibility for that service.
- One government entity (Agency 1) has entered into a contract with the operator to provide public services, however, another government entity (Agency 2) is primarily responsible for that public service and the relevant legislative function. Our view is that Agency 1 is facilitating the transaction on behalf of Agency 2. This could be due to certain legislative functions vested on Agency 1 e.g. contracting for services on behalf of the State. As noted above, an operator cannot be seen to operate 'on behalf of' an entity which does not have the legislative function and primary responsibility for that service. Therefore, Agency 1 is not a grantor under the arrangement and is only facilitating the transaction on behalf of Agency 2.
- Similarly, if a contract with an operator is co-signed by two government agencies, the agency that holds the legislative function and primary responsibility for that service should be considered the grantor.

We acknowledge that there may be scenarios where one government agency (Agency 1) engages another government agency (Agency 2) to provide a public service and Agency 2 does not have any legislative function/primarily responsibility assigned by the government to provide the service. In this case, it is possible to argue that Agency 2 is providing the

public service on behalf of Agency 1. This would be especially true where Agency 1 is also entering into similar arrangements for the same or similar services with private sector operators.

HoTARAC would not support the concept 'on behalf of' being interpreted in a way that the public sector agency that signed the contract with the operator is automatically seen to be the grantor even though a second public sector agency is primary responsible for providing the public service. This could result in arbitrary choice of the grantor for a particular arrangement, and would represent a form over substance approach. This would be especially challenging to apply in circumstances where "the Crown" or "the State" itself enters into the contract, represented by an agency.

To determine who a service is being provided "on behalf of", and therefore who is the grantor (where there is more than one government agency involved in the arrangement, either directly or indirectly), we think it is necessary to consider the following:

- Who would be responsible for replacing the asset, if the asset ceased to be fit for purpose? Even if an agency is the owner, holder, or deemed to have control of the asset(s) that is subject to the arrangement, would it continue to have the responsibility to source replacement assets if the asset were no longer fit for the purposes of providing those services?
- Who would be responsible for providing the service or finding/appointing another operator if the service ceased to be provided by the operator?

To determine which party has primary responsibility for the public service provided with an asset, the following sources would be relevant:

- Regulation
- Legislation establishing the agency
- The stated purpose of the agency, which may be found in their organisational strategy and/or on their website.
- Governance structure
- Contract e.g. the agreement may state the respective obligations of the parties, including who would be responsible for providing the service if the operator ceased to provide the service.
- Constitution

Operator's discretion

More guidance is requested on how to determine whether the operator is managing at least some of the services at its own discretion. Significant judgement is required to determine whether:

- the service provided by the operator are sufficiently significant to the public service provided using the asset to be "at least some"; and
- the degree of discretion able to be exercised by the operator is sufficient for the operator to be considered a principal and not an agent of the grantor.

Operator Discretion: "at least some"

We believe that entities must first determine what the significant activities are of a particular public service. In order to satisfy the "managing at least some" criteria, the operator would need to be managing an activity that is significant to the public service. The standard could be amended such that references to "managing at least some" is replaced by "managing at least some of the significant components" of the public services. In addition to

making the requirements consistent with the guidance in paragraph B10, it makes it much clearer what the intention of the standard is.

It would be helpful if the AASB provided more guidance in the standard on how to assess what types of services are significant for what types of public services.

An example is social housing (i.e. an arrangement providing housing services and housing support services) under the following scenario. The responsibility of the operator is restricted to repair damage, cleaning and gardening, while the asset management responsibility is retained by the State. We believe that in this scenario services provided by the operator are not significant to the provision of housing services and housing support services. In this scenario the operator will not be considered "managing at least some" of the public service at its discretion.

We believe that the factors such as the following should be considered, individually or in combination, in determining whether a service is significant or not:

- Compensation to the operator for the service compared to other services provided under the arrangement;
- Resource requirements (e.g. direct labour, service costs etc.) for the provision of the service relative to others provided under the arrangement;
- Impact on agreed outcomes, performance and/or KPIs under the arrangement;
- Senior management time and resources committed to the service relative to others provided under the arrangement and
- Physical apportionment of the asset between different services etc.

Operator's discretion: assessing sufficient discretion - distinguishing between protective and substantive rights of the grantor

We suggest that guidance is added to the standard to help make assessment whether operator has discretion over managing of the services under a contract with the grantor depending on whether the grantor has protective or substantive rights over provision of the services. This guidance could be similar to that applied in AASB 10 *Consolidated Financial Statements*.

The guidance could cover a scenario where the grantor has ultimate approval right over the way the services are delivered. For example, the operator prepares a detailed asset management plan, timetabling etc. but the grantor has the right to approve/reject these documents. How should stakeholders distinguish when the grantor's right of approval is protective or substantive? For example, a grantor may typically approve the operations and maintenance manual. However, the operator has discretion and flexibility in preparing the O&M manual, subject to the grantor's minimum standards. Where the grantor's right to reject must be substantiated and for all practical purposes will be exercised only if the minimum standards are not met, we believe this should be viewed as a 'protective' right.

Another example, a grantor in an arrangement may specify specific KPIs which must be met by the operator, but it may be completely at the operator's discretion on how it manages and achieves these requirements. If the operator has flexibility and managerial decision-making in terms of day-to-day functioning, making granular decisions while still remining compliant with the broader KPIs, this may demonstrate the operator is managing at least some of the services under its own discretion.

Secondary assets

HoTARAC members request the AASB either clarify or remove the concept of 'secondary assets' from AASB 1059 because we find guidance on this concept limited and confusing.

HoTARAC's preferred option is to remove the concept of secondary asset. Most of the assets the jurisdictions hold, to which this concept could possibly apply, e.g. car parks, have been determined to be providing a public service in their own right. So, in many instances, entities would achieve the same accounting outcome with and without applying the secondary asset concept in the standard.

If the AASB decides to retain the 'secondary assets' concept, it would be beneficial if the AASB provides clarification on the application of secondary assets concept (including the requirements in AASB 1059.B7) preferably with some real-life examples. HoTARAC members have found the concept and examples in B7 both confusing and contradictory – does "secondary" mean secondary within the context of the arrangement, or secondary in the context of the public service? For example:

- AABS 1059.B7 refers to the "*arrangement* provides public services principally through a primary asset, and a secondary asset is used or mainly used to compliment the primary asset, such as student accommodation …" however student accommodation and a university is rarely, if ever, seen as part of the same *arrangement*. Do we therefore interpret this example to mean that the student accommodation services are a secondary service to provision of university education and research services, rather than the student accommodation asset being secondary in the *arrangement*?
- AASB 1059.B7 also refers to an example of a hospital car park, however using a hospital service concession arrangement example is problematic because hospitals generally fall outside the scope of AASB 1059 as the operators do not have responsibility for management of hospital public service. In the example, the car park is assessed as not providing a public service because it was not constructed as part of the arrangement *and* the car park is largely of a commercial nature. Do we infer from this example that the car park is not providing public services because it is not part of the arrangement? Or that the car park is not providing public services because it is largely commercial? What would the outcome be if the car park was built at the same time, as part of the same arrangement, and largely of a commercial nature? What would the outcome be if the car park was built separately but not largely of a commercial nature?

Clarity is requested as to how the secondary asset's assessment under AASB 1059 takes into account the assessment for the primary asset? In particular, can a secondary asset be part of arrangements where the primary asset is concluded to be out of scope of AASB 1059 or should the secondary asset be treated as out of scope of AASB 1059 in every case where the primary asset is out of scope of AASB 1059? One of the interpretations of AASB 1059.B7 is that secondary assets concept can only relate to arrangements where primary assets are assessed to be in scope of AASB 1059.

However, using the AASB's example, if a public hospital car park built and operated by the private sector is largely of a commercial nature (e.g. car parking is available to the general public, including hospital patrons and the car park charges commercial rates), would the car park be regarded as an asset that provides public services?

Another example of a scoping situation where one of the HoTARAC members encountered practical difficulties was in assessing whether a hospital car park is a secondary asset and whether the hospital car parking services are 'public services' under the following scenario:

- The public hospital car park is ancillary to the primary public health service being delivered
- The car park is operated by a third party under the arrangement with the State
- The parking services are provided outside an arrangement related to the hospital itself
- The car park operation is not 'largely of a commercial nature'
- The State did not have any public policy, service delivery or regulatory regime around providing public car parking services as a primary, standalone service
- Hospital staff uses a physical separate portion of the car park; the other part is used by the public
- Hospital arrangement is not a service concession.

Regarding the interaction between paragraphs AASB 1059.B7 about secondary assets and AASB 1059.B8 about assets used wholly internally: some more examples would be helpful in distinguishing between primary and secondary assets. For instance, in an arrangement between a grantor and an operator for a hospital car park that is largely for staff use, or where there is a physically distinct section of the car park reserved for staff use, would the car park or the staff section be considered a secondary asset according to AASB 1059.B7 or an outsourcing arrangement according to AASB 1059.B8? Our view is that staff car parking assists the agency to deliver public services and should be treated under AASB 1059.B8.

2. Do you have comments regarding the characteristics of an arrangement that would distinguish it as a service concession arrangement from other arrangements such as a privatisation or outsourcing arrangement, or a lease? If so, please provide your views on those characteristics.

Distinguishing a service concession from privatisation

In our view, whether something is a 'public service' should follow from the government policy that is specific to the relevant jurisdiction and considers changes in this policy over time. See comments for topic 'public service' above regarding the historical transition of banking and aviation services away from public ownership and 'public service' to private ownership in deregulated markets.

Existing assets of the grantor

AASB 1059.8 requires existing assets of the grantor to be reclassified as SCAs where they meet the control criteria in AASB 1059.5 and AASB 1059.6. Generally, HoTARAC members agree with this approach.

Minority view

Two HoTARAC member's view is that the arrangements where a public agency provides its existing asset to external parties to provide public services should be explicitly excluded

from service concession definition unless the operator is required or expected to build on or expand the asset as part of the arrangement.

The reasons for this suggestion are as follows:

1. It would make AASB 1059 more consistent:
   - paragraph IG12 of AASB 1059 states that it is the operator rather than the grantor who should be responsible for capital investment.
   - Para B2 of AASB 1059 states that: "An arrangement within the scope of this Standard typically involves an operator constructing the assets used to provide the public services or upgrading the assets (for example, by increasing their capacity) and operating and maintaining the assets for a specified period of time".

2. When a public sector agency transfers its asset to an external party to provide public services on the agency's behalf, these HoTARAC members have found it is often an outsourcing arrangement because the state normally does not intend to share management of provision of the services with the external party. This is not the experience of all HoTARAC members.

3. From a cost/benefit perspective, this would be a favourable change as there is often little actual impact on the financial statements, however the reclassification requires effort related to determining whether there is a service concession arrangement and revaluation of existing assets using Current Replacement Cost method (many, but not all, existing assets are already measured at CRC, but where they are not, they are costly to revalue e.g. internally generated intangibles and assets measured using the income approach as part of a broader CGU).

Topic 2: Grantor's control of the asset

3. Do you have comments regarding the application of the following requirements in AASB 1059 paragraph 5: (a) the grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them, and at what price; and (b) the grantor controls any significant residual interest in the asset at the end of the term of the arrangement? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting. ITC 49: *"Some stakeholders have commented that too much judgement is involved in determining whether a grantor controls a service concession asset. They requested more guidance to assist in identifying how much 'control' the grantor needs to have over the services and/or pricing of the services to determine whether an arrangement is within the scope of AASB 1059.* *Some stakeholders also commented that it may be difficult to determine whether the grantor has control of any significant residual interest in the asset at the end of the term of the arrangement."*

4. An arrangement is within the scope of AASB 1059 for recognition as a service concession arrangement if all of the following conditions are satisfied: (a) the operator provides public services related to a service concession asset on behalf of the grantor; (b) the operator manages at least some of the public services under its own discretion; (c) the grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them and at what price; and (d) the grantor controls any significant residual interest in the asset at the end of the term of the arrangement. This includes the grantor having substantive rights to prevent the operator from selling or pledging the asset during the service concession arrangement. Do you consider it appropriate for an arrangement to be accounted for under AASB 1059 only when all of the above conditions are satisfied? Please provide reasons to support your view.

5. In addition to the conditions in AASB 1059 paragraphs 2 and 5 (as set out in Question 4), are there other factors that you consider would assist in determining whether an arrangement is within the scope of AASB 1059? If so, please provide details of those factors and explain why you think they would be useful.

Partly Regulated Assets

More guidance is sought on partly regulated assets such as transport assets, ports, car parks – how to determine whether enough of the service is regulated in order to demonstrate that the grantor has control of the asset. In making the assessment of the relative quantitative significance of regulated and unregulated services, it is essential to apply an appropriate metric. What indicators should be considered to make such an assessment (volume of the services, value of the services, etc)?

Significant residual interest

Assessment over whether the grantor controls any significant residual interest in the asset can be challenging, for example, where two or more assets are involved in the service provision. HoTARAC suggests adding real-life examples to the guidance on significant residual interest.

Third party regulator

As set out in AASB1059.B20-B22 where a third party regulates what services the operator must provide with the asset, to whom it must provide them, and/or at what price, the grantor is taken to be regulating them “implicitly” or “passively”. The reason for this is that such regulation removes the ability of the operator to determine these things. While HoTARAC members generally do not agree with the AASB’s rationale that third party regulation results in control by the grantor, HoTARAC members do not believe this concept has been overly problematic in terms of being able to apply the standard.

HoTARAC recommends that paragraphs B19-B22 be amended to be clearer. Wording similar to that used in the basis for conclusions, paragraph BC29 could make the intention of the standard clearer. There is also an inconsistency – at least in wording - between paragraph 5(a) of the standard and B19-22 (and BC29). Paragraph 5(a) is written in such a way that the grantor must control/regulate all of the price, the services and access. B19-B22 and BC 29 are written in such a way that the grantor only has to have one of these.

Comments on grantor's control of the asset generally

Refer to Appendix A for alternate view.

Topic 3: Public sector operator

6. Do you have comments regarding a public sector entity applying AASB 1059 as the grantor when the operator is another public sector entity? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting. If you propose excluding public-to-public arrangements from the scope of AASB 1059, what is the rationale for your view? ITC49: *"Some stakeholders have commented there are many "public-to-public" service concession arrangements, which involve an operator that is a public sector entity. These arrangements are within the scope of AASB 1059 since the Standard does not exclude arrangements where the operator is a public sector entity. Many such public-to-public arrangements are within the same department or jurisdiction. Some stakeholders have suggested that the benefits of requiring intra-group transactions to be accounted for under AASB 1059 would not outweigh the costs of that accounting when it is to be reversed on consolidation for the controlling entity or the whole of government financial statements."*

AASB 1059 does not exclude a possibility for public-to-public service concession arrangements. HoTARAC agrees that, although rare, public to public service concession arrangements are possible and should not be specifically scoped out of the scope of AASB 1059.

As mentioned above, there could be rare scenarios where one government agency (Agency 1) engages another government agency (Agency 2) to provide a public service. Agency 1 has the legislative function / primary responsibility assigned by the government to provide that service and Agency 2 does not. In this case, it is possible to argue that Agency 2 provides the service on behalf of Agency 1, and the arrangement could potentially be a public-to-public service concession.

However, taking into account the legislative context public-to-public service concessions may be less common than expected upon looking at which party has the primary responsibility and legislative remit (refer to our response to Question 1 above).

HoTARAC reiterates its request for the AASB to provide more guidance on how to apply the "on behalf of" concept. In doing so, the AASB should include consideration of a public-to-public arrangement (including providing examples).

The reason that HoTARAC believes that the appropriate application of the "on behalf of" concept would result in public-to-public service concession arrangements being rare are listed below:

- We believe that 'on behalf of' concept should be interpreted in a way that a public agency is a grantor only when that agency's primary responsibilities and legislative

functions are provide the respective public service. Public sector agencies are normally unable to act on behalf of other public agencies as each agency usually has its own primary responsibilities and legislative functions. This makes the concept of public-to-public service concessions redundant in most cases. However, we acknowledge that there may be rare cases where the primary responsibilities for provision of a public service are not clearly assigned to particular agencies, in which case a public entity may be considered acting on behalf of another when there is a service contract between them.

- As stated above in response to Question 1, if the concept 'on behalf of' were to be interpreted in such a way that in all cases the public sector agency that signed the contract with the operator is the grantor (even if a second public sector agency is primarily responsible for providing the public service), it could result in arbitrary choice of the grantor for a particular arrangement.

Topic 4: Recognition and measurement of service concession assets and related liabilities

Service concession assets

7. Do you have any comments regarding: (a) initially measuring a service concession asset at its current replacement cost using the cost approach in AASB 13; and (b) subsequently measuring the service concession asset at current replacement cost under the revaluation model in AASB 116 or AASB 138 (if the revaluation model is adopted by the entity)? Where you do have comments on (a) and/or (b), please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

ITC49:
"In respect of the recognition and measurement of service concession assets, some stakeholders have commented that:
(a) other valuation techniques in AASB 13 should be permitted to be applied in measuring a service concession asset, given that AASB 13 paragraph 61 states that an entity "shall use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs". In addition, applying the market approach seems to be more appropriate than applying the cost approach in measuring the fair value of land included in a service concession arrangement;
(b) anomalous outcomes could arise when measuring the fair value of a previously unrecognised internally generated intangible asset at CRC, compared with the income approach. They question the appropriateness of recognising assets that had not previously met the recognition criteria in AASB 138 and measuring them at fair value when fair value would not otherwise be permitted under AASB 138 because an active market is unlikely to exist for those intangible assets;
(c) because the operator is responsible for the construction and any upgrades, replacement or renewal of the service concession asset, in some cases the grantor has limited access to information about the asset. This creates challenges for initial and subsequent measurement, depreciation calculations and derecognition of components of the service concession asset when relevant;

(d) it is unclear whether service concession assets under construction should be measured at cost or at fair value;
(e) it is unclear whether borrowing costs or implied funding costs are required to be included in the current replacement cost of a service concession asset. The nonmandatory Illustrative Examples that accompany AASB 1059 illustrate how implied funding costs are calculated but there appear to be inconsistencies across Examples 6, 7 and 8;
(f) it is unclear whether, after initially recognising a service concession asset, any improvements to that asset should be recognised and measured in accordance with: • the subsequent measurement requirements in AASB 116 or AASB 138 as additions to the service concession asset; or • AASB 1059 paragraph B48, as a separate service concession asset with a corresponding liability; and
(g) AASB 1059 does not specify how contract modifications should be accounted for, such as when the operator provides an additional asset or service or carries out a major upgrade or replacement that was not part of the original arrangement."

Initial and subsequent measurement at Current Replacement Cost

HoTARAC believes that the AASB may want to reconsider whether mandating the use of current replacement cost (CRC) for initial and subsequent measurement of SCAs is sufficiently justified. Mandating CRC is inconsistent with AASB 13 *Fair Value Measurement* (AASB 13) (even though we note that CRC is expected to be the appropriate method under AASB 13 in most cases).

We suggest reconsidering whether SCAs should be recognised and measured as other assets in accordance with the relevant accounting standards such as AASB 116 *Property, Plant and Equipment* (AASB 116) and AASB 138 *Intangible Assets (AASB 138)*.

Some issues related to application of CRC under AASB 1059:

- It is unclear on how to value land that is part of SCA at CRC as land is normally valued using the market approach.
- In the case of for-profit public sector agencies where the service concession assets comprise a component of a larger cash generating unit valued using the income approach, the requirement to value SCAs at CRC results in (1) inconsistent valuation of otherwise similar assets – usually overvalued SCAs comparing to other assets (which can be particularly significant in an environment of rising inflation and rising interest rates) and (2) extra costs on valuing SCAs at CRC in comparison to valuing all assets, including SCAs under the income approach based on the enterprise value. If assets move back and forth between SCA and other categories of PPE, this results in unjustified fluctuation of the assets' carrying amount.
- Where a service concession arrangement has involved an internally generated intangible, such as a database with an indefinite useful life, the price paid by the private sector operator for use of the asset is significantly different to the cost of regenerating the database. This results in a very asymmetrical outcome, with a large GORTO liability and large revenue compared to a relatively low value asset and zero depreciation.

HoTARAC remains unconvinced that recognition and measurement of assets should depend on whether an asset is part of a service concession arrangement or built and owned by the grantor under the respective accounting standard - AASB 116 or AASB 138. However,

HoTARAC also acknowledges that it may be challenging to determine what the appropriate valuation approach under AASB 13 would be where the income generated by an asset accrues to the operator – for example, what would the appropriate valuation approach be for a toll road. Additional guidance would be required on how to approach identifying the appropriate valuation approach..

Recognition of internally generated intangible assets

HoTARAC is of the view that internally generated intangible assets which do not qualify for recognition as an intangible asset under AASB 138 *Intangible Assets*should not be recognised as SCAs. Provision of intangible assets to a service concession does not necessarily result in crystallisation of their value for the government in the same way as a business combination even though there may be more clarity about cash inflows associated with use of the assets by the public or cash outflows related to operation of the assets (AASB 1059.BC40).

Further, there is uncertainty around the treatment of subsequent capitalisation of such intangible assets under AASB 1059. It is unclear how the increase in an asset interacts with the GORTO liability. For example, where a database is recognised as an intangible asset under AASB 1059 in a GORTO arrangement. As new records are recognised in this database, these may be viewed as necessary to maintain the service capacity of the database, or may be viewed as increasing the service capacity of the database – in reality addition of new records do both. If the former, the new records are considered a revaluation i.e. increase in the CRC of the database with corresponding increase in the ARR. If the latter, these new records (contributed by the private sector operator) may instead increase the GORTO liability. Given these internally generated intangible assets are required to be recognised and measured because of AASB 1059 guidance is necessary.

8. Do you have any comments regarding the recognition and measurement of a service concession asset under construction? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

9. Do you have any comments regarding the calculation and treatment of borrowing costs or implied funding costs in measuring the current replacement cost of a service concession asset? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Interest accretion (i.e. adjustment of CRC to include implied funding cost in measuring a SCA)

HoTARAC members have had significant challenges understanding how to apply the recognition and measurement requirements to service concession arrangements where the service concession asset and corresponding liability are built / incurred over a number of years. AASB 1059 seems to mostly assume that a service concession arrangement is entered into, and the asset commences operating, on the same date or at least in the same reporting period. Given a majority of service concession arrangements relate to large and complex infrastructure projects, this is an overly simplistic assumption.

AASB 1059 requires the service concession asset and service concession liability to be initially measured at the CRC of the service concession asset adjusted for any other consideration (AASB 1059.7 and AASB 1059.12). It is not clear if the value of the asset and liability should be equal at the beginning of construction, at the end of construction or both. Given the asset is subsequently measured at CRC, and a financial liability measured in accordance with AASB 9 *Financial Instruments* it is inevitable that the values of the asset and liability diverge after initial recognition. Similarly, the GORTO liability is reduced based on the economic substance of the arrangement, such that subsequent to initial measurement it is likely the value of the GORTO liability will not match the value of the service concession asset.

Examples 6 and 7 in AASB 1059 implementation guidance assume that the value of an asset constructed over a number of years will match the value of a financial or GORTO liability at the end of each year of construction, however it is not clear on what basis the examples come to this conclusion. Inconsistencies arise in interpreting the examples:

- The uplift in the CRC of the asset under construction (AUC) appears to represent "funding costs" related to construction costs in the previous year (AASB 1059.IE17, AASB 1059.IE23).
- If the uplift in CRC for "funding costs" is intended to represent a part of the SCA revaluation related to borrowing costs, there is an inconsistency between valuing SCA and similar non-SCA assets for general government sector agencies. Borrowing costs are normally expensed by such entities because of the GFS rules, but SCA assets appear to include these costs through interest accretion.
- If, however, the uplift in CRC for "funding costs" is intended to be a proxy for the fair value increase, what aspects of the revaluation increment is it intended to cover? Is this uplift in CRC intended to cover all AUC revaluation increments or only part of them? If it is just a part of total revaluation increment/decrement, what fair value increments it is supposed to cover? Should an uplift for "funding costs" not be posted if an entity revalues the AUC based on construction indices, physical inspection and other inputs with involvement of external valuers? Or should "funding costs" and AUC revaluation increments related to indexation of construction costs and revaluation increments related to other factors be added together? How should agencies avoid double counting?
- If the uplift in CRC for "funding costs" is intended to be a revaluation adjustment, why then is the uplift adjusted to the GORTO liability in Example 7 directly, and not adjusted to the asset revaluation reserve? We would expect that the accounting for the SCA should be the same regardless of whether it is a financial or GORTO liability.

Assets under construction (AUC)

HoTARAC requests that the guidance and worked examples in relation to service concession assets constructed over several years be improved and clarified, including:

- Setting out what each of the examples is intended to demonstrate or achieve, as this will help preparers interpret the examples & apply them in practice.

- Explaining the purpose and meaning of each of the entries in the examples, because this will help when preparers are applying judgements to real life examples which differ from the exact fact pattern in the examples
- unbundling the calculation of finance expenses and calculation of SCA revaluation increments during the construction phase, because even though finance expenses may serve as a proxy for fair value adjustments in limited circumstances, SCA revaluation increment should include all movements in fair value of AUC, including construction indices increase, physical condition of AUC and other factors.
- adding more years to the construction period in the examples 6-8 and assume the time value of money is not negligible. This would ensure the examples take into account compounded interest.
- Remove or explain the inconsistencies between examples 6,7 and 8 in the implementation guidance:
    - In Example 6, the adjustment to CRC for interest costs is taken to asset revaluation reserve. In Example 7, this was adjusted to the GORTO liability directly and there was no adjustment to asset revaluation reserve. We would expect that the accounting for the SCA should be the same regardless of whether it is a financial or GORTO liability.
    - For hybrid arrangements, example 8 ignores the GORTO element. It is unclear if under a hybrid arrangement, an uplift should be recognised on the GORTO element in line with example 7. If an uplift is required, it is unclear how the implied effective interest rate on the GORTO element in a hybrid arrangement is determined as example 8 ignores this.

10. Do you have any comments regarding the recognition and measurement of upgrades or replacement of major components of a service concession asset? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Refer also to response to question 16

11. Do you have any comments regarding how contract modifications should be accounted for under AASB 1059? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Contract modifications

We recommend that AASB 1059 includes guidance on how modifications of service concession arrangements should be accounted for.

AASB 1059 Example 6 sets out how to account for the replacement of a major component of a SCA (road resurfacing) where it is contemplated as part of the original arrangement and the compensation to the operator for this service is included in the predetermined series of payments the operator has the right to earn. Under Example 6, the grantor recognises a SCA

and related liability when the resurfacing occurs. This financial liability is subsequently measured at amortised cost using the original effective interest rate (EIR) calculated using the predetermined series of payments that already included the payment for resurfacing.

AASB 1059 is silent on how major upgrades or replacements of assets should be accounted for when they are not contemplated as part of the original arrangement. It also does not address situations where the contract between the operator and grantor are modified such that an additional asset or service is provided by the operator or such that the period of the concession is increased or decreased.

Sometimes, grantors have difficulty obtaining information from operators about costs of SCAs upgrades not covered by original arrangements. We would recommend allowing use of a pragmatic simplified approach considering these data constrains to determine increases in fair value of SCAs.

Under the financial liability model, AASB 1059 prescribes the application of AASB 9 to the subsequent measurement of the financial liability. Therefore, where there are contract modifications that result in changes to cash flows under the arrangement the grantor will need assess the modification under AASB 9. This can result in a reset of the EIR and recognition of gains/losses that are not reflective of the economics of the arrangement.

Accounting treatment of service concession modifications could be developed for financial liability, GORTO and hybrid arrangements for a number of scenarios such as:

- Asset additions included in the original contract – already included in estimated cash flows of original service concession liability
- Contract modifications that result in an additional asset or service (the asset must be identifiable as a separate component; the change is not contemplated in the original agreement; the cash flows can be allocated to the additional asset/service)
- Contract modifications of service concessions with no additional asset or service being recognised, or where it is unclear how cash flows should be allocated.

The lease modification requirements in AASB 16 *Leases* and contract modification requirements in AASB 15 *Revenue from Contracts with Customers* could be a useful basis to formulate the accounting requirements for service concession modifications.

12. Are there any other comments regarding the AASB 1059 recognition and measurement requirements for service concession assets that you think the AASB should consider?

Timing of reclassifying grantor contributed Assets Under Construction (AUC)

HoTARAC would welcome additional guidance on when grantor contributed and/or constructed assets should be reclassified from PPE AUC to SCA-AUC? For example, should it be the date when the operator starts providing services with the asset or any other date? Arguably, this date should correlate with the date when the control criterion in AASB 1059 is satisfied or with the date on which the operator has access to the underlying existing asset to be able to provide the agreed public service.

How to account for increases in construction costs which are not passed on to the grantor

In some instances, some SCA construction costs not envisaged in the contract price are absorbed by the operator (e.g. the operator under-priced the contract or the cost of materials has increased since the arrangement was entered into), therefore the costs are not passed on to the grantor. However, where these costs form part of the asset's CRC, should these costs be considered as an asset valuation adjustment to the asset revaluation reserve or should they impact the underlying GORTO liability in a GORTO or hybrid arrangement?

Service concession liabilities

ITC49:
"Some stakeholders have commented that there are challenges in measuring financial liabilities in service concession arrangements involving variable or contingent consideration or minimum guarantee payments, where the grantor pays any shortfall between the amounts received by the operator from users of the asset and the contracted minimum consideration for the operator. In such a situation, it is unclear whether the grantor is required to recognise:
(a) a financial liability for the present value of the minimum guaranteed amounts over the term of the arrangement; or
(b) a provision under AASB 137 Provisions, Contingent Liabilities and Contingent Assets for the expected shortfalls in the revenue received by the operator from the users.

The GORTO liability is required to be amortised according to the 'economic substance of the arrangement'.
Some stakeholders commented that it is unclear whether the economic substance of the arrangement refers to:
(a) how access to the service concession asset is provided to the operator over the arrangement term, as in AASB 1059 paragraph B71. In this case, the GORTO liability would be amortised on a straight-line basis when the access to the asset is provided uniformly over the arrangement term; or
(b) the basis on which the operator can charge users of the service concession asset, which might not be uniform over the arrangement term, thereby making the use of a straight line amortisation of the GORTO liability inappropriate.

Some stakeholders also commented that they have experienced anomalous outcomes when applying the requirements in paragraphs 11 and 12 of AASB 1059 in initially measuring a partly completed service concession asset. Stakeholders provided the following examples: (a) for an arrangement involving a financial liability, there could be situations where the grantor's contractual obligations measured under AASB 9 are greater than the CRC of the partly completed asset, resulting in a negative impact on the statement of financial position in the periods when the asset is under construction; and
(b) AASB 1059 does not specify whether (and if so, how) the liability is required to be adjusted when the asset construction is completed to reflect the same amount as the CRC of the completed asset. For an arrangement involving a GORTO liability, if the GORTO liability is not adjusted, the subsequent revenue recognition (and reduction of the GORTO liability) is

likely to be significantly lower than the depreciation of the asset, resulting in an ongoing negative impact on the statement of profit or loss."

13. Do you have comments regarding the application of the requirements in paragraphs 11 and 12 of AASB 1059 to initially measure the liability at the same amount as the service concession asset, subject to certain adjustments? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Please refer to response to questions 9.

14. In addition, do you have comments regarding the application of AASB 1059 requirements to initially recognise a partly completed service concession asset (or asset under construction) and associated liabilities? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Please refer to response to questions 9.

15. Do you have comments regarding the subsequent measurement requirements for financial liabilities? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

HoTARAC seeks clarification on variable compensation in a service concession arrangement when, for example, the grantor is only required to pay the residual amounts (a shortfall) after operator collects monies from customers. Should the liability be accounted under AASB 137 *Provisions, Contingent Liabilities and Contingent Assets* or AASB 9 *Financial Instruments*?

Refer also to our comments in response to question 9.

16. Do you have comments regarding the initial and subsequent measurement, including amortisation, of GORTO liabilities? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Understanding the "economic substance" of the arrangement

Regarding:

"The GORTO liability is required to be amortised according to the 'economic substance of the arrangement'.

Some stakeholders commented that it is unclear whether the economic substance of the arrangement refers to:

(a) how access to the service concession asset is provided to the operator over the arrangement term, as in AASB 1059 paragraph B71. In this case, the GORTO liability would be amortised on a straight-line basis when the access to the asset is provided uniformly over the arrangement term; or
(b) the basis on which the operator can charge users of the service concession asset, which might not be uniform over the arrangement term, thereby making the use of a straight line amortisation of the GORTO liability inappropriate.:

It is HoTARAC's view that recognising revenue according to the economic substance would usually be in accordance with how access to the asset is provided to the operator. As such the straight-line method would be appropriate in most cases. IN addition, the approach suggested in point (b) above is practically harder to implement.

Amortisation of GORTO liabilities related to replacement of major components
One HoTARAC member raised that amortisation of GORTO liabilities relating to replaced components does not seem to take into account the expected life or replacement frequency of the component (refer to Illustrative Example 7 in AASB 1059) and recommends the AASB provide guidance on how to account for such a situation.

For example, there is a 30-year service concession and a particular component of the SCA is replaced every 5 years. Our understanding is the amortisation of the GORTO liability relating to this component will be as follows –

- The initial component installed during construction is amortised over 30 years,
- The 1st replacement at start of year 6 is amortised over 25 years,
- The 2nd replacement at start of year 11 is amortised over 20 years,
- The 3rd replacement at start of year 15 is amortised over 15 years, etc…

This results in more and more revenue recognised in the later years. The financial statement impact can potentially be material, where the grantor has major components requiring replacement multiple times over the course of the service concession.

One of the options to resolve this issue would be amortisation of the GORTO liability relating to this component over 5 years each time it is replaced, aligning with asset depreciation principles. However, this would require componentising the GORTO liability, and brings about an additional cost burden.

Refer also to Appendix A which sets out one HoTARAC members dissenting view.

17. Are there any other comments regarding the AASB 1059 recognition and measurement requirements for liabilities of a service concession arrangement that you think the AASB should consider?

HoTARAC believes that more guidance would be advisable for distinguishing financial liability and GORTO. For example, there may be an arrangement structured in a way that the grantor acts as an agent collecting revenue from third party users for the operator and this raises the question whether the grantor should recognise financial liability or GORTO liability.

In our view, the following question should be considered to make an assessment whether the grantor's liability is financial liability or GORTO:

- Is it the grantor or the operator who bears the economic risks when there is toll evasion, fee disputes, unplanned service disruption, etc?

If the grantor bears these risks, the grantor may need to recognise a financial liability based on expected third party usage. It would be up to the grantor to ensure it collects all the revenue from third parties to cover its payments to the operator.

If the grantor does not bear the risks and simply remits what it collected to the operator, it could be a GORTO liability instead.

Topic 5: Other matters

18. Do you have any comments regarding the disclosure requirements in AASB 1059 (paragraphs 28 and 29), which cover both qualitative and quantitative information about a grantor's service concession arrangements? If so, please provide your views on those requirements and their significance.

19. Do you have any comments regarding the Implementation Guidance and Illustrative Examples that accompany AASB 1059? If so, please provide your views and any suggested amendments.

Provided above.

20. Are there any other matters that the AASB should consider as part of this PIR? If so, please explain those matters and why they should be considered, and provide examples to illustrate your response. For example, in your view are there new or emerging arrangements for which it is difficult to determine whether they are within the scope of AASB 1059 or for which service concession accounting might not be suitable?

AASB General Matters for Comment In addition to the specific matters for comment on each topic, the AASB would also particularly value comments on the following:

21. Does the application of AASB 1059 adversely affect any regulatory requirements for grantors?

No regulatory issues identified.

22. Does the application of AASB 1059 result in major auditing or assurance challenges?

This submission indicates that there were significant challenges of judgment in accounting and auditing of service concession arrangements.

The other observation is that AASB 1059 increases the number of judgements made by preparers and auditors, therefore increasing audit challenges.

23. Overall, does AASB 1059 result in financial statements that are more useful to users of public sector grantors' financial statements?

Generally, agree.

Refer to the comments to question 12. One of the HoTARAC members does not think that recognition of GORTO arrangements on balance sheet makes the financial statements more useful to users. They are of the view that it artificially inflates the State's assets and liabilities and detracts from economic substance – in their view it is hard to substantiate a 'present obligation' for the GORTO liability and it has limitations being construed as genuine "revenue" – consequently, experienced users are having difficulties making sense of this liability and what it actually means. Refer to Appendix A for more explanation.

24. In your view, do the benefits of applying the requirements of AASB 1059 exceed the implementation and ongoing application costs?

Generally, agree. AASB 1059 helped achieve consistency in the accounting for service concession arrangements, pending areas where further guidance is requested as part of this submission. However, one of the HoTARAC members considers the benefits of the standard as it stands do not exceed the implementation and application costs (including additional costs of asset valuation, GFS differences and user confusion around what SCAs/liabilities mean/represent). For financial liability SCAs, the additional guidance is welcome but it did not result in significantly different accounting treatments from what had been adopted pre-AASB 1059.

Appendix A – Dissenting View

In addition to the comments in the main part of this submission, one of the HoTARAC members raised the following three issues.

Grantor's control of the asset

(i) Fundamentally, the concept of control in AASB 1059 differs from the concept of control in AASB 10 *Consolidated Financial Statements*. This is where many AASB 1059 issues for GORTO arrangements have their root. The outcome of AASB 1059 is that both parties (the grantor and the operator) effectively control the same asset, both entities recognise the asset in their financial statements, but there is only one set of economic benefits being derived and accruing to one entity.

(ii) The wording of AASB 1059.5(a).

a. It takes a black and white (or "in/out") approach to control rather than looking at the extent (or whether "enough" substantive control resides with the grantor).

b. Use of the terminology "controls or regulates" in AASB 1059.5(a) is a contributory factor to this – because one can regulate an activity or entity without controlling it. This is particularly the case in a long term GORTO arrangement (such as a toll road) where the grantor does not benefit economically from the asset during the service concession period.

This HoTARAC member suggests that the AASB re-examines the distinction between "control" and "regulate" in their post implementation review process. There are some arrangements that can be regulated but the level of regulation does not give economic control to the grantor during a service concession period, even if the asset returns to the government at the end of the service concession term.

Recognition of GORTO arrangements

The HoTARAC member suggests that the AASB reconsider whether long-lived GORTO arrangements should be recognised on the balance sheet.

They remain concerned with the economic substance of the argument that the State exercises genuine substantive "control" over most, if not all, of their material GORTO arrangements (especially with regards to toll roads). They continue to question the rationale for the underlying physical asset (e.g. road) and rights associated with that asset (e.g. tolling rights) to be separated and recognised by two different entities – when, in substance, it is the same asset that is being accounted for twice by two different entities.

Related to this is the fact that the ABS ignores or makes adjustments for GORTO assets and liabilities in their analysis.

They are of the view that for a GORTO arrangement, alternative options that would achieve the objective of meeting users' information needs at a much lower cost include:

(i) recognise the residual interest in the asset through gradual accretion over the term of the arrangement, or

(ii) Recognise the asset at its fair value when the asset returns to "control" of the State (applying control concepts similar to AASB 10 and for other assets), or

(iii) Disclosure only for GORTO arrangements using a combination of qualitative and quantitative disclosures instead of recognition in financial statements.

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10 March 2023

The Chair
Australian Accounting Standards Board
PO Box 204
COLLINS STREET WEST VIC 8007

via email: ***standard@aasb.gov.au***

Dear Keith

AASB Invitation to Comment ITC 49 Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors

Deloitte is pleased to respond to Australian Accounting Standards Board ('AASB' or 'Board') Invitation to Comment ITC 49 Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors (ITC 49).

We appreciate the opportunity to comment on AASB 1059 *Service Concession Arrangements: Grantors* (AASB 1059) to assist the Board in determining whether AASB 1059 continues to meet its objective and the pronouncement remains appropriate.

Overall, our view is that AASB 1059 does continue to meet its objectives and remains appropriate, and applying the standards results in increased transparency to users. We do, however, have observations on certain aspects relating to the following topics identified in ITC 49 below:

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- Topic 1: Public Service and Topic 2: Grantor's control of the service concession asset

  In response to questions 1,3,4 and 5 relating to Topic 1 and Topic 2 in the ITC, in our opinion, current requirements around scoping under AASB 1059 broadly reflect the guidance in Interpretation 12 *Service Concession Arrangements* /IFRIC 12. As the interpretation of the standards does involve significant judgement, there may be an opportunity for difference in practice, however when applying the requirements under AASB 1059 and IFRIC 12 a similar outcome can be achieved. We observe that certain states have felt the need to provide additional guidance to public sector entities relating to the application of AASB 1059. For example, NSW Treasury has provided guidance to assist NSW public sector entities in identifying whether the operator is managing at least some of the public services at its own discretion. Our recommendation would be for the AASB to consider incorporating some of the additional guidance that has been considered necessary by the various state governments. We note the guidance provided includes a range of topic areas and is not limited to Topic 1 and Topic 2.

- Topic 4 A: Recognition and measurement of service concession assets

  Regarding questions 7 &9 around the recognition and measurement of service concession assets at current replacement cost and application of AASB 13 *Fair Value Measurement* (AASB 13), we refer to our submission letter on ED 320 dated 7 July 2022. In practice, advice would generally be sought by NFP entities from quantity surveyors and valuation professionals working with the professionals that manage and work with the assets to determine the approach to valuing the asset and determining the replacement cost of the assets. We do not consider that adding further guidance specific to AASB 1059 would be appropriate, and any amendments arising from ITC 49 pertaining to fair value measurement should, in our opinion, would need to be incorporated into further amendments to AASB 2022-10 *Amendments to Australian Accounting Standards – Fair Value Measurement of Non-Financial Assets of Not-for-Profit Public Sector Entities*.

Please contact me at +61 3 9671 7871 or moverton@deloitte.com.au if you wish to discuss any of our comments.

Yours sincerely

Moana Overton
Partner

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