Information Paper

Public Private Partnerships and Service Concession Arrangements

Objective of this paper

1 This paper provides background on Public Private Partnerships (PPP) and is for information purposes only.

Structure of this paper

2 This paper is structured as follows:

(a) An overview of Public Private Partnerships (PPPs) (paragraphs 3- 4);

(b) Types of PPPs (paragraphs 5-6);

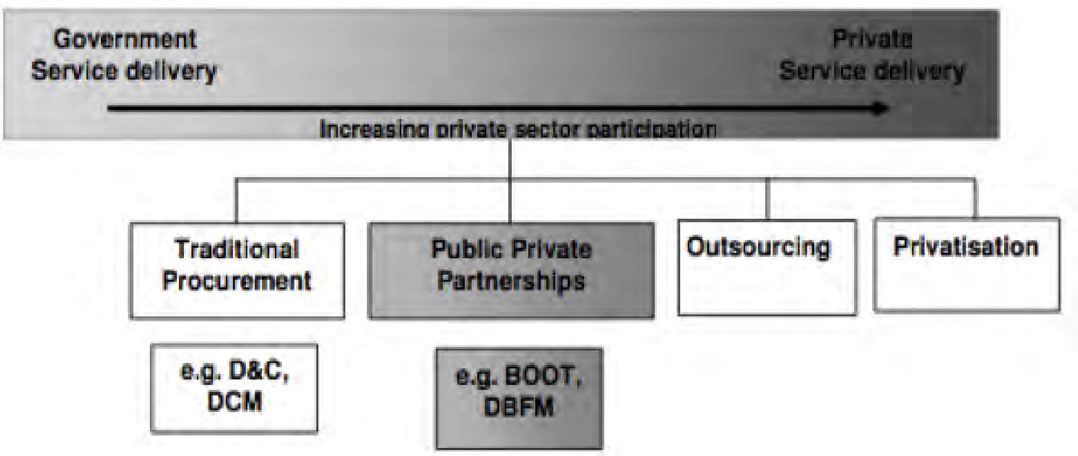
(c) PPP arrangements in Australia (paragraphs 7-11); and

(d) Service concession arrangements as a form of PPP in Australia, including the key rights and obligations of a grantor in a service concession arrangement that involves a licence for the 'right to charge users' (paragraphs 12-16).

Overview of Public Private Partnerships

3 A PPP is a structure that engages the private sector to assist in the delivery of public infrastructure so that social obligations are met and successful sector reforms and public investments are achieved.[1] A PPP may be used to bridge the gap between public finances and infrastructure development needs, and to benefit from the project management expertise and efficiencies that the private sector can bring to the delivery of the public infrastructure and/or related services.

4 A PPP is one of many ways to provide public infrastructure and related services. Diagram 1[2] below illustrates the spectrum of public infrastructure delivery methods.



1 Asian Development Bank, *Public-Private Partnerships Handbook*, 2008.
2 Infrastructure Australia, *National Public Private Partnership Guidelines: Overview*, December 2008, pg 4.

Legend

D&C – private sector entity is compensated to design and construct, as opposed to finance, the infrastructure

DCM – private sector entity is compensated to design, construct and maintain, as opposed to finance, the infrastructure

BOOT – private sector entity is compensated to build, own (including finance), operate and transfer (at the end of an agreed term) the infrastructure

DBFM – private sector entity is compensated to design, build, finance and maintain the infrastructure

Types of Public Private Partnerships

5 Build-Own-Operate-Transfer (BOOT) or Build-Operate-Transfer (BOT) arrangements are a type of PPP that involves the public sector entity providing the private sector entity with a payment or a 'right to charge users' in return for the private sector entity constructing the public infrastructure and delivering the related services on behalf, or in support, of the public sector entity's objectives or broader service responsibilities. These arrangements may be long-term, for example, 20-30 years. In many cases, legal title of the public facility is initially with the private sector entity, at which time the private sector entity is typically responsible, fully or partially, for the condition and performance of the public infrastructure and/or related services throughout the term of the arrangement. At the end of the term, the title is transferred on to the public sector entity. This type of arrangement is also known as a service concession arrangement and is in the scope of the AASB project.

6 Other forms of contracts between public and private sector entities are namely lease contracts and management contracts, which are closely related to service concession arrangements but differ in the remuneration and other rights of the private sector entity.

(a) A lease contract typically gives a private sector entity (the lessee) the right to operate and maintain a public sector entity's asset exclusively for its own purpose. An example is roads built from a mine to a port specifically for a mining entity, but the land upon which the roads are built remains the control of the public sector entity (lessor). This type of arrangement is not in the scope of the AASB project. AASB 117 *Leases* applies to this type of PPP.

(b) Under a typical management contract, a private sector entity (the service provider) is paid an agreed fee for performing stipulated public services and/or collect fees or revenues on behalf of the public sector entity. This type of arrangement is not in the scope of the AASB project. AASB 118 *Revenue* applies to this type of PPP.

PPP arrangements in Australia

7 Many Australian public sector entities enter into PPP arrangements. Some of the completed and ongoing PPP arrangements in Australia are:

(a) the Hawkesbury Hospital, the Sydney Harbour Tunnel, the M5 and Eastern Distributor motorways, and the Sydney SuperDome in New South Wales;

(b) the City Link, Peninsula Link and East Link motorways, the Hopkins Correctional Centre, the Southern Cross Station Redevelopment, and the Wonthaggi desalination plant in Victoria;

(c) the Brisbane AirportLink and New Generation Rollingstock in Queensland;

(d) the Royal Adelaide Hospital, and regional police stations and courts in South Australia; and

(e) public hospital services in Western Australia and Tasmania.

8 The *National Public Private Partnership Guidelines: Overview* ('Guidelines') prepared and endorsed by Infrastructure Australia[3] and the State, Territory and Commonwealth Governments sets out an agreed framework for the delivery of PPP projects[4], including the process for determining the need for a PPP and the method of delivery, selecting the preferred proposal or private sector entity to execute the PPP, and contract management. The Guidelines apply to PPP arrangements that involve a private sector entity providing public infrastructure and related services on behalf of the public sector entity. Examples of types of projects in the scope of the Guidelines are schools, hospitals and roads.

9 The risks underlying a PPP are allocated to the entity that is best able to manage them, which could be the private sector entity or the public sector entity. The private sector entity is typically expected to bear the risks associated with designing, building and operating the infrastructure. The public sector entity takes on those risks that it can manage for less than it would have to pay the private party to bear.[5] The key principle in PPP projects is 'value for money'.[6]

10 The risks may not be shared equally between the public and private sector entities. For example, the public and private sector entities may agree to limit one entity's risk exposures and/or to establish a mechanism whereby the parties can act together to mitigate and share the consequences of the specified risk.[7]

11 Ultimately, the risk and responsibility for the delivery of public services remains with the public sector entity.[8]

Service concession arrangements as a form of PPP in Australia

12 As mentioned in Agenda paper 8.1, the focus of the AASB project is on service concession arrangements as these are the arrangements that existing Australian accounting standards do not address adequately. A narrow-scope project, at least at this stage, would enable us to develop appropriate solutions to resolve the major accounting issues that have been identified. The accounting for service concession arrangements could then provide useful guidance for dealing with similar components of other types of PPP arrangements if necessary.

13 The features, terms and conditions, and risk allocation of service concession arrangements are determined on a project-by-project basis. In addition, the legal and economic structure of these arrangements can be complex involving a network of individual contractual agreements and multiple parties.

14 Service concession arrangements typically include the following key characteristics.

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3 Infrastructure Australia is a statutory body established under the *Infrastructure Australia Act 2008*, which came into effect on 9 April 2008, to advise governments, investors and infrastructure owners on a wide range of issues. More details are available on http://www.infrastructureaustralia.gov.au/about/.
4 Section 1.1 of the *National Public Private Partnership Guidelines: Overview*.
5 Section 5.1 of the *National Public Private Partnership Guidelines: Overview*.
6 Section 6 of the *National Public Private Partnership Guidelines: Overview*.
7 Section 5.1 of the *National Public Private Partnership Guidelines: Overview*.
8 Section 5.1 of the *National Public Private Partnership Guidelines: Overview*.

(a) the grantor (public sector entity) determines the operating features of the public infrastructure (the service concession asset) and related services–in particular, it sets the use, users and the usage price of the service concession asset;

(b) the operator (private sector entity) finances the construction or upgrade of a service concession asset;

(c) the operator provides public services involving the service concession asset to the public (third party users) for a defined period of time;

(d) the grantor makes regular payments[9] (also known as 'availability payments') or provides a licence for the 'right to charge users'[10] (or a combination of both) to the operator in exchange for the delivery of the service concession asset and related services over the term of the arrangement;

(e) the grantor may also guarantee a minimum return to the operator and share in the operator's revenue; and

(f) the operator agrees to transfer the related services to the grantor at the end of the agreed term.

15 Based on the findings from targeted outreach[11], examples of types of service concession arrangements in Australia for which the grantor provides availability payments to the operator include arrangements for the delivery of hospitals, schools, prisons and water treatment plants. Typically, a grantor provides a licence for the 'right to charge users' to the operator for service concession arrangements that are more capital-intensive, for example, arrangements for the delivery of toll roads, tunnels and bridges.

16 The following are key themes in the rights and obligations of a grantor to toll arrangements[12]. This list is not exhaustive.

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9 AASB 139 *Financial Instruments: Recognition and Measurement* or AASB 9 *Financial Instruments* apply in this circumstance. This type of arrangement is not within the scope of Agenda paper 8.3 or Issue 2 of Agenda paper 8.1.

10 This is the subject of Agenda paper 8.3 or Issue 2 of Agenda paper 8.1.

11 A summary of feedback on the targeted outreach conducted will be tabled at the July AASB meeting (Agenda paper 8.4).

12 Issue 2 (as mentioned in Agenda paper 8.1) relates to the issue of the accounting for the licence for the 'right to charge users' that the grantor provides to the operator in exchange for the construction of the service concession asset and related services. Issue 2 is the subject of Agenda paper 8.3. Staff have reviewed the following toll arrangements as background to considering the revenue recognition of licences for the 'right to charge users' in Agenda paper 8.3:
http://www.treasury.nsw.gov.au/__data/assets/pdf_file/0010/3115/m7_contr.pdf
http://www.treasury.nsw.gov.au/__data/assets/pdf_file/0003/123249/01_Attachment_for_Eastern_Distributor_Roads_Contract_Summary.pdf
http://www.treasury.nsw.gov.au/__data/assets/pdf_file/0017/123524/M2_contracts_summary_28May2013.pdf
http://www.treasury.nsw.gov.au/__data/assets/pdf_file/0004/3100/Cross_City_Tunnel_contracts_summary_2008_update_lowres.pdf
http://www.treasury.nsw.gov.au/__data/assets/pdf_file/0017/24533/M5_Contracts_Summary_25_June_2012_small.pdf
http://www.contracts.vic.gov.au/major/44/City_Link_Melbourne_City_Link_Concession_Deed.pdf
http://www.macquarie.com.au/au/corporations/acrobat/connecteast_prospectus.pdf
http://www.brisconnections.com.au/media/7760/final_pds_noapplication_20june_2008.pdf

(a) The public sector entity may be obliged to consult with the private sector entity about the public infrastructure that is within the scope of the service concession arrangement if and when the public sector entity plans to undertake further improvements or expansions to the Government's roads network master plan. Even though the public sector entity may have an obligation to consult, the public sector entity may not be not restricted from developing another public road network and other public transport system.

(b) The public sector entity may be obliged to, for example, renegotiate the term of the arrangement, the toll price and/or its financial or operational contribution to the arrangement, if the public sector entity undertakes activities that would cause material adverse effects on the private sector entity's collection of toll revenue, or the repayment of/on capital and debt issues. Examples of activities that would cause material adverse effects include implementing 'competing road projects'[13] and interrupting traffic connections to the private sector entity's motorway.

(c) The public sector entity may be obliged to assist the private sector entity in managing or facilitating traffic between connecting public arterial roads, freeways or other road networks and parts of the private sector entity's motorway, for example, in the event of accidents, approved lane closures on the motorway for repairs, and peak hour traffic.

(d) The public sector entity (through the Government's road and transport authority) may be obliged to assist the private sector entity in identifying non-paying vehicles and in the collections of non-payment toll fares.

(e) The public sector entity may be obliged to assist the private sector entity in liaising, managing relationships and resolving disputes involving other public sector entities, the private sector entity, stakeholders and the public during the course of the service concession arrangement, for example, dealing with a local council on the impact of construction or traffic on its precinct or suburbs.

(f) The public sector entity may be entitled to a share of the tolled revenue if actual toll revenue is higher than the forecasted revenue.

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13 Any new road or upgrading or widening of existing roads that both parties have agreed not to compete with the toll road, tunnel or bridge that is the subject of the service concession arrangements.