Australian Accounting Standards Board

Interpretation Advisory Panel

Service Concession Arrangements – Public Sector Grantors

Report of the Panel to the AASB (December 2007)

1 ISSUES FOR CONSIDERATION

1.1 The general interpretation issue for consideration by the Interpretation Advisory Panel concerns the accounting by public sector grantors for service concession arrangements. The AASB agreed at its December 2006 meeting to appoint an advisory panel to develop recommendations on this issue, in accordance with the *Interpretations Model* (June 2006). The Panel's report will be considered by the AASB to assist it in determining whether additional work is required on this issue.

1.2 This issue has arisen in conjunction with the issuance by the AASB of Interpretation 12 *Service Concession Arrangements* in February 2007. This Interpretation is the Australian equivalent of IFRIC Interpretation 12 (same title), which was developed by the IASB's International Financial Reporting Interpretations Committee (IFRIC). Interpretation 12 addresses the accounting by operators for certain public-to-private service concession arrangements, but explicitly does not address the accounting by grantors.

1.3 At its meeting in August 2007, the AASB decided that its Interpretations Agenda Committee should consider and recommend the specific issues that the Panel should address. The Committee's recommendations were then discussed at the AASB's September meeting. The AASB decided that the Panel should consider the following questions:

Q1 For service concession arrangements within the scope of AASB Interpretation 12, does the Interpretation determine the general accounting by public sector grantors through application of the hierarchy for selecting accounting policies set out in AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*?

Q2 If so, what accounting is required of public sector grantors and is that appropriate and sufficient?

Q3 If Interpretation 12 does not determine the general accounting by public sector grantors, what accounting may they adopt for such arrangements under existing Australian Accounting Standards, and why?

1.4 Selected extracts from authoritative accounting literature and other guidance are included in the Appendix. Reference should be made to the full requirements. The text of AASB Australian equivalents to International Financial Reporting Standards (IFRSs) is consistent with the IFRSs, which are not separately identified in this paper.

2 OVERVIEW OF PANEL'S REPORT

2.1 This part of the report summarises the views of the Panel members on the questions put to the Panel by the AASB.

Relevance of Interpretation 12 to Public Sector Grantor Accounting

2.2 In response to Question 1, a majority of seven out of nine Panel members take the view that, under the hierarchy for selecting accounting policies set out in AASB 108, AASB Interpretation 12 does not determine the general accounting by public sector grantors for service concession arrangements within the scope of the Interpretation. The other two Panel members consider that the Interpretation does determine the basic grantor accounting in the absence of any other AASB pronouncement on the issue. Section 3 of the Report details the bases for these views.

2.3 However, the majority of Panel members considers that grantors can choose to follow Interpretation 12, even though it does not apply mandatorily. Therefore, the Panel has considered the appropriateness of such accounting in its response to Question 3.

Application of Interpretation 12 to Public Sector Grantor Accounting

2.4 Question 2 is not required to be addressed by the Panel as a result of the majority view concerning Question 1.

Possible Accounting by Public Sector Grantors

2.5 In response to Question 3, the range of possible accounting by public sector grantors for service concession arrangements within the scope of Interpretation 12 is set out in section 4 of this Report, addressing both recognition and measurement policies. The Panel's evaluation of various approaches and methods is set out in section 5.

2.6 A majority of the Panel members concluded that grantors currently can choose from four different approaches to determining how to account for the property underlying a service concession arrangement, in addition to a range of other recognition and measurement accounting policies. The majority has not concluded whether one of these four approaches should be preferred, but has concluded that the "control or regulation" approach of Interpretation 12 is the only approach that should not be permitted to be applied by grantors, due to potential problems with the way it addresses control and regulation issues in the public sector.

2.7 A majority of the Panel members also concluded that the scope exclusion for service concession arrangements that was added to Interpretation 4 *Determining whether an Arrangement contains a Lease* when Interpretation 12 was issued needs to be clarified because its application is presently unclear due to ambiguous wording.

2.8 The Panel's principal majority conclusions, which are noted in the paragraphs above, are collected in section 6 of the Report.

3 RELEVANCE OF INTERPRETATION 12 TO PUBLIC SECTOR GRANTOR ACCOUNTING (Question 1)

3.1 Paragraph 4 of Interpretation 12 states that it gives guidance on the accounting by operators for public-to-private service concession arrangements. Paragraph 9 states that the Interpretation does not specify the accounting by grantors. On the face of these paragraphs, the Interpretation itself does not directly determine the general accounting by grantors for arrangements within the scope of the Interpretation.

3.2 However, there is an issue concerning whether the Interpretation applies by analogy to grantors because of the operation of the hierarchy for the selection of accounting policies that is set out in Accounting Standard AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors*. The effective scope exclusion in Interpretation 12 for grantors indicates that the Interpretation does not specifically apply to service concession arrangements from the perspective of grantors. Paragraphs 10-12 of AASB 108 therefore apply. These paragraphs concern the selection of accounting policies in the absence of an Australian Accounting Standard (which reference includes Interpretations) that specifically applies to a transaction, other event or condition.

3.3 AASB 108 paragraph 10 requires the management of an entity to use its judgement in developing and applying an accounting policy so that the resulting information is both relevant and reliable. Paragraph 11 states that the management shall refer to and consider the applicability of the following sources, in descending order: (a) the requirements and guidance in Australian Accounting Standards dealing with similar and related issues; and (b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the *Framework for the Preparation and Presentation of Financial Statements*. Under paragraph 12, the management may also consider the most recent pronouncements of other standard setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature and accepted industry practices, to the extent that these do not conflict with the sources stated in paragraph 11.

3.4 Clearly, Interpretation 12 deals with "similar and related issues"; indeed it deals with transactions to which the public sector grantors are themselves parties, as paragraph AG6 states clearly. However, there are two views on the implications of this. One view is that grantors are therefore obliged to adopt accounting that mirrors to the extent feasible that required of operators under the Interpretation. The opposing view is that grantors are not required to adopt symmetrical accounting due to the specific exclusion for grantors. The majority of Panel members support this latter view.

The Effect of a Specific Exclusion when Applying the Hierarchy

3.5 The question here is whether paragraphs 10-12 of AASB 108 override the specific exclusion re grantor accounting that is in Interpretation 12. The IASB itself has provided precedent that a specific exclusion is not overridden when applying the hierarchy. As set out in the Appendix, the *IASB Update* of September 2004 reported the views of the IASB on the retention of a scope exclusion in IFRS 3 *Business Combinations* for combinations involving mutual entities and by contract alone without the obtaining of an ownership interest. The IASB stated that the hierarchy for selecting accounting policies set out in IAS 8 (to which AASB 108 corresponds) would need to be applied. The IASB concluded that in accounting for combinations

involving mutual entities or by contract alone without the obtaining of an ownership interest, entities would be "permitted" to look to IFRS 3 for guidance.

3.6 What this means is that entities were not required to follow the accounting specified in the directly relevant Standard (had there been no scope exclusion), but that they could choose to apply its requirements to the excluded transactions: i.e. "permitted", but not "required". Applying this approach to grantor accounting for service concession arrangements, a grantor would be permitted, but not required, to follow the requirements specified in Interpretation 12. This is the view of the majority of Panel members.

3.7 Panel members also note that IASB and IFRIC pronouncements are designed to apply to general purpose financial reports and other financial reporting of all for-profit entities. Paragraph 9 of the IASB's *Preface to International Financial Reporting Standards* goes on to state that "Although IFRSs are not designed to apply to not-for-profit activities in the private sector, public sector or government, entities with such activities may find them appropriate." The IASB therefore has said that public sector not-for-profit entities are not required to follow IFRSs: once again, "permitted" but not "required". This position is noted in paragraph BC15 of the IFRIC's Basis for Conclusions on Interpretation 12. By contrast, paragraph BC14 notes that application of the Interpretation by analogy under the hierarchy in IAS 8 would be appropriate for private-to-private service concession arrangements. No such explicit statement is made in respect of grantor accounting.

3.8 The minority of Panel members takes the view that as Interpretation 12 is the pronouncement most relevant to the question of public sector grantor accounting, grantors would be required to follow it to the extent possible in setting their accounting policies. In their view, the AASB would need to issue a pronouncement to allow grantors to adopt accounting different from Interpretation 12, if some other accounting was considered to be more appropriate.

4 POSSIBLE ACCOUNTING BY PUBLIC SECTOR GRANTORS (Question 3)

4.1 This section of the Report first addresses grantor accounting for service concession arrangements on a basis consistent with Interpretation 12: in particular, does this mean "symmetrical" accounting between grantor and operator? The possible accounting methods that could potentially be adopted by grantors are then addressed based on four alternative, general approaches to the recognition of the property underlying an arrangement. In order to illustrate the possible accounting methods, two broad categories of service concession arrangements are considered: those where the grantor pays the operator, and those where the grantor provides the operator with a licence to charge users of the underlying property. Finally, the possible accounting outcomes are summarised in a number of tables. Tables 1 and 2 present an overview of the recognition accounting policies, whereas Tables 3 and 4 provide more detail concerning those policies and also add measurement policies. The Tables are supported by numerous explanatory notes.

Symmetrical Accounting?

4.2 The "application" of Interpretation 12 by a public sector grantor would appear to require the grantor to follow it to the extent possible in setting their accounting policies. Under this approach, grantors would be required to adopt accounting symmetrical with that required of operators under the Interpretation, as far as possible. For example, since paragraph 11 of the Interpretation states that the operator cannot recognise the infrastructure subject to an arrangement as an asset, and paragraph AG6 concludes that the infrastructure is controlled by the grantor, symmetrical accounting would have the grantor recognising the whole of the infrastructure as its asset.

4.3 However, it is not necessarily clear what "following the Interpretation to the extent possible", or "symmetrical" accounting, would really mean for the accounting by grantors. For example, if the operator recognises an intangible asset for its consideration for construction services, does this mean that the grantor has to recognise an "intangible liability"? Some argue that the grantor has no liability at all in such a case, let alone an "intangible" one, since the grantor does not recognise rights to charge for the use of public infrastructure as assets.

4.4 Financial reporting does not automatically require symmetrical accounting by the parties to a transaction. For example, AASB 117 *Leases* requires lessors and lessees to apply the same criteria in classifying leases as either finance leases or operating leases. However, it does not require the same outcome: different lease classifications by the lessor and the lessee may be warranted if the lessor benefits from a residual value guarantee provided by a party unrelated to the lessee (see paragraph 9).

Recognition of the Property underlying a Service Concession Arrangement

4.5 The fundamental accounting issue for service concession arrangements in general is how the property that underlies the arrangement is accounted for. This is a difficult issue, because in substance both grantor and operator are associated with the property, regardless of which party has legal title. There are a number of general approaches for addressing the recognition of the subject property:

(i) substantially all/majority of risks and rewards;

(ii) control;

(iii) control or regulation; and

(iv) rights and obligations.

These are considered in the following analysis in turn.

Substantially All/Majority of Risks and Rewards Approach

4.6 The "substantially all/majority of risks and rewards" approach determines whether the operator or the grantor should recognise the property underlying the service concession arrangement based on assessing the risks and rewards arising from the property for each party. However, either the operator or the grantor recognises the property in full – it is not "split" between them according to the extent to which each entity bears the risks and rewards. This approach is utilised in AASB 117 *Leases*, for example. Under that Standard, a lease that transfers substantially all the risks and rewards incidental to ownership of the leased item to the lessee is classified as a finance lease: the lessee recognises the leased item as an asset, and the lessor recognises a receivable instead of the leased item.

4.7 The application of a "risks and rewards" approach to service concession arrangements is exemplified by the UK Accounting Standards Board's Application Note F "Private Finance Initiative and Similar Contracts", which was added in 1998 to its Financial Reporting Standard FRS 5 *Reporting the Substance of Transactions* (refer to the Appendix for extracts). The basic principle is that a party will have an asset of the property where that party has access to the benefits of the property and exposure to the risks inherent in those benefits. This has been interpreted in practice as requiring assessment of whether the majority of the risks and rewards relating to the property lie with the grantor or the operator. Based on that assessment, either the grantor or the operator would report the whole of the property as an asset.

4.8 Application Note F states that whether a party has an asset of the property should be determined by looking at the extent to which each party would bear any variations in property profits or losses. The Note identifies the principal factors that might be relevant to an arrangement as demand risk, third-party revenues, who determines the nature of the property, penalties for underperformance or non-availability, potential changes in relevant costs, obsolescence and residual value risk. The Note states that it is necessary to look at the overall effect of these factors taken together.

4.9 The principles of FRS 5 Application Note F have been incorporated into detailed guidance developed by the Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) and endorsed by the Heads of Treasuries. This guidance was issued in January 2004 and revised in June 2005 to address additional issues. The guidance is currently being applied in some, but not all, Australian jurisdictions.

Control Approach

4.10 Under the "pure" control approach, the entity that controls the property would recognise it as an asset. This is based on the *Framework's* definition of an asset, which refers to a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity (paragraph 49). This approach is utilised in AASB 116 *Property, Plant and Equipment*, for example. Under that Standard, an item of property, plant and equipment is recognised by an

entity as an asset if it is probable that future economic benefits associated with the item will flow to the entity and the cost of the item can be measured reliably.

4.11 Indicators of whether the property underlying a service concession arrangement is controlled by the operator or by the grantor could include the following:

(i) whether the arrangement enables the grantor to specify significant operating policies and procedures with respect to the property;

(ii) whether the arrangement precludes or significantly restricts the operator from using the property for other purposes;

(iii) whether the arrangement precludes the operator from using other assets to fulfil its public service obligations;

(iv) whether the arrangement precludes or significantly restricts the operator from providing services to other parties;

(v) whether the arrangement specifies the maintenance program with respect to the property;

(vi) whether the arrangement precludes the operator from modifying or replacing the property without the consent of the grantor; and

(vii) whether the arrangement precludes the operator from selling or transferring the property (and the service obligation) without the consent of the grantor.

The overall effect of the range of factors would need to be considered in determining whether the grantor or the operator controls the property underlying the arrangement, and therefore would recognise the property in full.

Control or Regulation Approach

4.12 Interpretation 12 uses an extended control approach, described in this Report as the "control or regulation" approach. This is because the Interpretation addresses public-to-private service concession arrangements under which the grantor "controls or regulates" the services the operator must provide, to whom it must provide them and the price (paragraph 5(a)). However, Interpretation 12 identifies control based on only this limited set of control indicators.

4.13 Under the control indicators identified in Interpretation 12, a grantor would be considered to control the property underlying a service concession arrangement when the grantor controls the services the operator must provide, to whom it must provide them and the price. Under this view, the operator has a right of access to operate the property but not a right of use, which is explained in Interpretation 4 *Determining whether an Arrangement contains a Lease* as the right to control the use of the property. Therefore, the operator neither controls nor leases the property, and could not recognise the property as either a direct property asset or a leased asset.

4.14 The reference in paragraph 5(a) to regulation is explained in the application guidance that is part of the Interpretation. Paragraph AG2 states that the control or regulation could be by contract or otherwise (such as through a regulator), and goes on that the grantor and any related parties (i.e. "the public sector as a whole"), including any

regulators acting in the public interest, shall be considered together in applying this condition.

4.15 This means that a grantor would be regarded as controlling the property underlying a service concession arrangement, and required to recognise the property in full, even when a regulator established in the same public sector jurisdiction (and not the grantor itself) determines the services the operator must provide, to whom it must provide them and the price. In substance, this approach therefore extends from control by the grantor itself to control by the grantor and related public sector entities considered together.

4.16 It is assumed that the application of this approach in Australia would not extend beyond each public sector jurisdiction. Thus, a grantor in one State presumably would not be regarded as controlling the property underlying an arrangement if the operator's use of the property was subject to the requisite degree of regulation by a regulator established by another State or by the Australian government.

Rights and Obligations Approach

4.17 Unlike the previous approaches, the rights and obligations approach does not assume that either party to an arrangement should recognise the subject property in its entirety. Instead, it views the property as a bundle of future economic benefits, some of which may be controlled by one party and some by the other party. Under this approach, both parties could recognise assets that arise from their association with the property. Assessment of the rights and obligations under an arrangement would identify the assets controlled (and the liabilities incurred) by each entity and address the likelihood of the entity obtaining (sacrificing) the relevant future economic benefits.

4.18 There is no single view on the extent to which rights and obligations arising under a transaction should (or can) be identified by the parties and recognised separately when the recognition criteria are met. In substance, this is a unit of account issue: how narrow or how broad should the "individual" recognised assets, liabilities and other elements be? For example, Interpretation 12 states "This Interpretation sets out general principles on recognising and measuring the obligations and related rights in service concession arrangements" (paragraph 10). However, it adopts the control or regulation approach for determining whether the operator should recognise the property as a single asset, rather than seeking to identify and recognise assets and liabilities at a lower level of aggregation.

4.19 A rights and obligations approach is adopted in AASB 139 *Financial Instruments: Recognition and Measurement*. For example, that Standard specifies that an entity has to determine whether the derecognition requirements should be applied to all of or a part of a financial asset or a group of similar financial assets (paragraph 16). It may also be argued that AASB 138 *Intangible Assets* adopts the rights and obligations approach, since intangible assets are defined as identifiable non-monetary assets without physical substance, and thus represent rights controlled by an entity.

4.20 The IASB is in the early stages of developing a rights and obligations approach for accounting for leases, where one outcome could be the disappearance of the classification of leases as either operating leases or finance leases. For example, a lessee under what is presently classified as an operating lease could be required to recognise an asset and a liability in relation to the rights and obligations it has under

the lease agreement, instead of merely recognising lease payments as they are made. Such an approach would appear to be at odds with Interpretation 4 and its distinction between a right to use (control the use of) property and a right of access to property.

Application of the Approaches

4.21 The Panel has not concluded whether one of these four approaches should be preferred for the accounting by public sector grantors. However, a majority of the Panel members does not support the "control or regulation" (Interpretation 12) approach. The Panel's evaluation of these approaches is provided in section 5 of the Report, after the descriptions of the possible accounting by grantors.

4.22 Accordingly, the following descriptions of the possible accounting by grantors are based on the extent to which the grantor recognises the property underlying a service concession arrangement, without justifying that conclusion based on one or other of these general approaches. A grantor must be able to justify the accounting policies that it adopts, in terms of consistency with Australian Accounting Standards.

The Possible Grantor Accounting Policies

Categories of Service Concession Arrangements

4.23 The Panel considered the possible accounting approaches that public sector grantors could apply to service concession arrangements within the scope of Interpretation 12 by reference to two typical broad categories of arrangements. The two categories are distinguished according to whether:

(i) the grantor agrees to pay the operator for the construction or upgrade services (i.e. the operator has a financial asset) and for the operation services; or

(ii) the grantor provides the operator with the right or licence to charge users of the public service (i.e. the operator has an intangible asset).

4.24 Within each category of arrangement, two types of arrangement are identified, depending on whether there is a significant residual interest in the infrastructure at the end of the arrangement. An arrangement with no significant residual interest (or a significant interest controlled by the operator) is called a Build-Own-Operate (BOO) arrangement, and one with a significant residual interest controlled by the grantor is called a Build-Own-Operate-Transfer (BOOT) arrangement. An arrangement falls within the scope of Interpretation 12 only if the grantor controls the residual interest (a BOOT arrangement) or there is no significant residual interest (a whole-of-life BOO arrangement).

Accounting Policy Tables

4.25 The possible accounting by grantors for service concession arrangements that are within the scope of Interpretation 12 is set out in this Report as follows:

Accounting Policies	"Grantor Pays" Arrangement	"Licence to Charge Users" Arrangement
Recognition (overview)	Table 1	Table 2
Recognition and measurement (detailed)	Table 3	Table 4

Tables 3 and 4 give more detail on the recognition policies summarised in Tables 1 and 2. Tables 3 and 4 also include measurement policies, which increases the combinations of accounting policy choices available to the grantor.

4.26 The Tables summarise only accounting policies that a grantor could justify under Australian Accounting Standards. Policies that might be justified by reference to the *Framework* but are inconsistent with any of the Standards are not permitted, in accordance with the hierarchy of accounting pronouncements to which management may refer in determining appropriate policies, as set out in AASB 108 paragraph 11.

Grantor Recognition Policies – Overview

TABLE 1 – GRANTOR PAYS THE OPERATOR

Assets	Liabilities	Comments
BOO or BOOT Arrangements		
A. Recognise Property in Full Apply AASB 116; e.g. depreciate the property over its useful life	Financial liability Apply AASB 139	
OR		
B. Recognise Finance Lease Asset Apply AASB 117	Finance lease liability Apply AASB 117	Operating lease classification unlikely
OR		
BOOT Arrangements Only		
C. Recognise Residual Interest Only Apply AASB 116 as PP&E; OR Apply AASB 138 as intangible asset		Property relating to operation period not recognised by grantor
Alternative timing of RI recognition: .. at inception; OR .. accumulate over period of arr't; OR .. at end of the period	Various liability/unearned revenue approaches	Refer to Table 3 for details
Depreciate RI over remaining useful life once grantor operates property		Treat as PP&E when grantor starts to operate the property
OR		
BOO Arrangements Only		
D. No Recognition No asset recognised	No liability recognised	All payments expensed when incurred

4.27 Table 1 summarises the alternative accounting policies for asset and liability recognition that a grantor under a "grantor-pays" arrangement could adopt, classified by type of arrangement. For example, the grantor under such a BOO arrangement

could select policy A or B or D. The grantor under such a BOOT arrangement could select policy A or B or C, and under policy C it would need to select an approach to the timing of recognition of its residual interest in the property underlying the service concession arrangement.

4.28 The Table provides a summary of only the principal accounting policies, to allow a ready comparison of the alternative approaches. The Table does not indicate the basis upon which a grantor may choose a particular accounting policy. For example, the grantor may decide to recognise the property underlying a service concession arrangement in full based on the "substantially all/majority of risks and rewards" approach, the control approach, or the control or regulation approach.

Policy A – Recognise Property in Full

4.29 This accounting policy is applied by a grantor that concludes that it should recognise the whole of the property, whether that conclusion is based on application of the risks and rewards approach, the control approach, or the control or regulation approach of Interpretation 12. This policy may be applied to whole-of-life BOO arrangements (i.e. no significant residual interest) and to BOOT arrangements. Typically, the property would be recognised under AASB 116 *Property, Plant and Equipment*.

4.30 As the grantor will pay the operator for the construction services performed, the grantor recognises a financial liability alongside its recognition of the property. The financial liability would be accounted for under AASB 139 *Financial Instruments: Recognition and Measurement*.

Policy B – Recognise Finance Lease Asset

4.31 A grantor may choose to adopt lease accounting under AASB 117 *Leases* for the leases entered into under a service concession arrangement. It may be assisted by Interpretation 4 *Determining whether an Arrangement contains a Lease* in identifying leases under the arrangement. As this Report addresses only arrangements within the scope of Interpretation 12, it does not deal with BOO arrangements in which a significant residual interest is not controlled by the grantor. Therefore, it is unlikely that treating an arrangement within the scope of Interpretation 12 as a lease would result in operating lease classification, unless the grantor's "control" was due to the effects of regulation, and the grantor applied the "pure" control model.

4.32 In recognising finance lease assets under AASB 117, the grantor would also recognise finance lease liabilities.

Policy C – Recognise Residual Interest Only

4.33 A grantor may conclude that it should not recognise any asset or liability in relation to the operation period of an arrangement, based on its view of its rights and obligations under the arrangements. Alternatively, the grantor may have decided to apply one of the other general property recognition approaches to the operating period separately from the post-arrangement period, concluding either that it does not control the property during the arrangement period or that it does not have substantially all (or a majority of) the risks and rewards of the property in that period.

4.34 However, the grantor may recognise its residual interest in the property under a BOOT arrangement as an asset, based on its accounting policy as per the previous

paragraph. The grantor may consider the asset to be in the nature of property, plant and equipment, even though its use as such is deferred until the end of the arrangement, or it may regard it as an intangible asset, being the right to obtain the property at the end of the arrangement.

4.35 The grantor would have to select one of the three policy alternatives for the timing of the initial recognition of the residual-interest asset: at inception, accumulate over the operation period of the arrangement, or at the end of the operation period. Furthermore, "inception" could be interpreted by the grantor in various ways, e.g. (1) when the agreement is signed, (2) when construction is complete, or (3) when the contracted services start being performed under the arrangement. These alternatives are not shown in the Table.

4.36 The "accumulate over the period" method reflects the requirements in FRS 5 Application Note F (refer to the Appendix) concerning a difference between the contracted amounts (including zero) payable for the transfer of the residual interest to the grantor and its estimated fair value as at the transfer date (i.e. the end of the arrangement). Thus, expenses or revenues arise for the grantor over the period of the arrangement to the extent that the payments exceed or are less than the estimated fair value. Different methods could be adopted by grantors to accumulate the residual-interest asset over the arrangement period.

4.37 The nature of the asset under the accumulation method is unclear: some grantors may treat the accumulating asset as PP&E, some as intangible. Treating it as an intangible asset, such as the right to receive the property at the end of the service concession arrangement, would appear to prevent the asset being revalued during the period of the arrangement, because AASB 138 *Intangible Assets* allows application of the revaluation model to an intangible asset only when there is an active market, which is not likely for properties under service concession arrangements. However, an alternative view is that the right is being acquired over the period of the arrangement, requiring an accumulation process to properly recognise it.

4.38 Recognition of the residual-interest asset at the end of the arrangement period might be adopted by a grantor that considers the acquisition of the residual interest to be an equally proportionately unperformed contract, which typically would not be recognised in financial statements.

4.39 On the credit side of the entry to recognise the residual-interest asset, there are a number of alternative liability and unearned revenue approaches. These approaches vary depending on the payment arrangements for the residual interest and the timing of its recognition. Table 3 includes more detail on these alternatives.

4.40 Under AASB 116, the depreciable amount of an asset is allocated over its useful life, which is defined basically as the period over which an asset is expected to be available for use by the entity. Therefore, the residual-interest asset would normally start to be depreciated once the grantor began to operate the asset, whichever approach was adopted in recognising the asset initially. This would seem to apply even if the residual interest had been recognised initially as an intangible asset.

Rights and Obligations Approach

4.41 Policy C, recognition of only the residual-interest asset and related credits, is one example of a rights and obligations approach, under which the grantor recognises

assets and liabilities according to its assessment of how the economic benefits embodied in the property have been unbundled and shared between the grantor and the operator. Given the subjectivity of this general approach, no further possibilities under this approach are shown in the Table.

Policy D – No Recognition

4.42 The grantor under a BOO arrangement might conclude that it has no assets or liabilities to recognise in advance of payments that it incurs to the operator, whether applying a control approach or a risks and rewards approach. Payments incurred would be recognised by the grantor as expenses for the services obtained through the arrangement.

4.43 Such a "no recognition" approach is not likely to apply to a BOOT arrangement, since the grantor obtains the subject property at the end of the arrangement.

TABLE 2 – GRANTOR PROVIDES OPERATOR WITH LICENCE TO CHARGE USERS

Assets	Liabilities	Comments
BOO or BOOT Arrangements		
A. Recognise Property in Full Apply AASB 116; e.g. depreciate the property over its useful life	Various revenue/unearned revenue approaches	Refer to Table 4 for details
OR		
BOOT Arrangements		
B. Recognise Residual Interest Only Apply AASB 116 as PP&E; OR Apply AASB 138 as intangible asset		Property relating to operation period not recognised by grantor
Alternative timing of RI recognition: .. at inception; OR .. accumulate over period of arr't; OR .. at end of the period	Various revenue/liability/unearned revenue approaches	Refer to Table 4 for details
Depreciate RI over remaining useful life once grantor operates property		Treat as PP&E when grantor starts to operate the property
OR		
BOO Arrangements		
C. No Recognition No asset recognised	No liability recognised	No accounting recognition when there are no payments

4.44 Table 2 summarises the alternative accounting policies for asset and liability recognition that a grantor could adopt under a "licence-to-charge-users" arrangement, classified by type of arrangement. For example, the grantor under such a BOO arrangement could select policy A or C. The grantor under such a BOOT arrangement could select policy A or B, including a recognition timing policy under policy B.

4.45 The Table provides a summary of only the principal accounting policies, to allow a ready comparison of the alternative approaches. The Table does not indicate the basis upon which a grantor may choose a particular accounting policy. For example, the

grantor may decide to recognise the property underlying a service concession arrangement in full based on the "substantially all/majority of risks and rewards" approach, the control approach, or the control or regulation approach.

Policy A – Recognise Property in Full

4.46 This accounting policy is applied by a grantor that concludes that it should recognise the whole of the property, whether that conclusion is based on application of the risks and rewards approach, the control approach, or the control or regulation approach of Interpretation 12. This policy may be applied to whole-of-life BOO arrangements (i.e. no significant residual interest) and to BOOT arrangements.

4.47 The grantor immediately recognises either revenue or unearned revenue equal to the amount of the property recognised. The up-front recognition of revenue may be justified on the grounds that the grantor does not give up a recognised asset of its own in exchange for the property, since rights to charge users of property typically are not recognised as assets by grantors. An alternative justification is that the grantor could first recognise the licence to charge users as an asset, with the credit to revenue, and the licence asset is then used to settle the acquisition of the property. A grantor may choose to adopt an unearned revenue policy instead, based on the view that the grantor is required to perform in certain ways under the arrangement, with revenue recognised over the arrangement period as those actions are performed. Further detail is provided in Table 4.

Lease Accounting

4.48 Table 2 does not include an approach based on Interpretation 4 or the leasing Standard AASB 117, in contrast with Table 1. It seems difficult to conclude that the grantor leases the property from the operator, since the grantor does not make a series of payments (or any payment) to the operator in return for the right to use (control the use of) the property. The definition of a lease in AASB 117 refers to a payment or series of payments, rather than to the provision to the lessor of something of value to the lessor, such as the right to charge users.

Policy B – Recognise Residual Interest Only

4.49 A grantor may conclude that it should recognise its residual interest in the property under a BOOT arrangement as an asset, but that it should not recognise any asset or liability in relation to the operation period of an arrangement. This approach is the same as Policy C in Table 1, in respect of when and how the residual-interest asset should be recognised. Paragraphs 4.33 to 4.40 under Table 1 also apply generally here to Policy B.

4.50 However, there are more choices for the grantor's recognition of a liability or revenue in relation to the residual-interest asset, depending upon whether the grantor is required to make any payment or payments for the residual interest, even if it is not required to make payments during the period of the arrangement in relation to the services being provided by the operator. Thus, recognising the residual-interest asset at the inception of the arrangement could result in the recognition of a liability for the payments required, immediate revenue for the grantor if no payment is required, or revenue amortised over the arrangement period.

Policy C – No Recognition

4.51 The grantor under a BOO arrangement might conclude that it has no assets or liabilities to recognise, whether applying a control approach or a risks and rewards approach. As the grantor typically does not pay for the services provided by the operator using the property underlying the arrangement, there may be no accounting recognition of the arrangement for the grantor. However, disclosure in notes to the financial statements may be warranted, since the ability to issue additional licences or the limitations placed on the grantor's future actions may be material information.

4.52 As with Table 1, such a "no recognition" approach is not likely to apply to a BOOT arrangement, since the grantor obtains the subject property at the end of the arrangement.

Grantor Recognition and Measurement Policies – Detailed

TABLE 3 – GRANTOR PAYS THE OPERATOR

Assets	**Liabilities**	**Comments**
BOO or BOOT Arrangements		
A. Recognise Property in Full Measure at cost = fair value [116.15] Depreciate over useful life, not period of arrangement [116.50]	Financial liability .. measure at fair value [139.43] .. subseq at amortised cost [139.47] .. interest expense (fixed payment) .. service expense (variable payt)	Service expense recognised for variable payt > fixed payt
OR		
B. Recognise Finance Lease Asset Finance lease asset, as lessee [117.20]	Finance lease liability [117.20]	Operating lease classification unlikely
OR		
BOOT Arrangements Only		
C. Recognise Residual Interest Only Property relating to operation period not recognised by grantor	No liability relating to operation period	
Residual interest (RI) recognised: C1 At inception: .. at cost – PP&E [116.15]; OR .. at cost – intangible [138.24]; OR	Liability at inception; OR Unearned revenue at inception .. amortise to revenue [118.20]	Allocate payts to reduce liab OR All payments expensed, with revenue recognised separately
C2 Accumulate over period of arr't: .. straight-line method; OR .. annuity method; OR	Liability/expense accumulates if total payment for RI > FV; asset/revenue accumulates if total RI payment < FV	Results in RI recorded at FV at end of the arrangement period
C3 At end of the arrangement period, as PP&E [AASB 116]	No unearned revenue	
Depreciate RI over remaining useful life once grantor operates property [116.50]		Treat as PP&E when grantor starts to operate the property
OR		
BOO Arrangements Only		
D. No Recognition No asset recognised	No liability recognised	All payments expensed when incurred

4.53 Table 3 portrays the alternative accounting policies for asset and liability recognition and measurement that a grantor under a "grantor-pays" arrangement could adopt, classified by type of arrangement. The Table 1 notes concerning recognition all apply equally to this Table, however more detail is provided in this Table, and in the following paragraphs, for the credit side of the recognition entries, as well as adding measurement policy alternatives. As with the previous tables, Table 3 does not indicate the basis upon which a grantor may choose a particular accounting policy.

Policy A – Recognise Property in Full

4.54 An asset recognised under AASB 116 *Property, Plant and Equipment* may be measured after initial recognition using either the cost model or the revaluation model (if fair value can be measured reliably).

4.55 The subsequent measurement of financial liabilities at amortised cost using the effective interest method under AASB 139 *Financial Instruments: Recognition and Measurement* results in the recognition of interest expense. Fixed payments made by the grantor would be divided between repayment of the liability and interest. If the payments to be made by the grantor under the service concession arrangement include variable payments reflecting operating conditions, then operation or service expenses would also be recognised.

Policy B – Recognise Finance Lease Asset

4.56 Refer to paragraph 4.31 re recognition of finance leases. Measurement of the lease asset and liability is as per AASB 117.

Policy C – Recognise Residual Interest Only

4.57 In addition to various recognition timing policies (labelled C1, C2 and C3 in Table 3), there are various measurement policies as well under policy C. The cost of the residual-interest asset recognised at "inception" (policy C1) could be measured based on the amount required to be paid by the grantor for the asset. For example, this could be the undiscounted aggregate of the payments required or the present value of those payments. The latter approach would incorporate the unwinding of the discount in each period. If a not-for-profit grantor (most, if not all, public sector grantors) recognised the asset under AASB 116, paragraph Aus15.1 would require it to be measured at fair value if it was acquired at no cost or for a nominal cost.

4.58 Whereas a residual-interest asset recognised under AASB 116 could be measured subsequently under the revaluation model (if fair value can be measured reliably), the same asset recognised under AASB 138 *Intangible Assets* could be measured subsequently under the revaluation model only if there is an active market for the asset, which is most unlikely.

4.59 Table 3 shows two alternatives for the recognition of the residual-interest asset over the period of the service concession arrangement (policy C2): straight-line accumulation, and an annuity method. Both are intended to have recorded the residual-interest asset by the end of the arrangement at its fair value at that time. The straight-line method simply recognises this amount in equal annual amounts over the period of the arrangement. The annuity method recognises an annual amount that will compound with interest over the period of the arrangement to the fair value amount. This approach is intended to compensate for the time value of money, which in a

long-term service concession arrangement would mean that the fixed annual amount under the straight-line method would diminish in significance over time. The annuity method is used in New South Wales, for example.

4.60 The credit side of the residual-interest asset recognition entry varies according to the grantor's policy. Under policy C1 (recognition of the asset at inception), the grantor may recognise either a liability, to be reduced by the future related payments, or unearned revenue, to be recognised as revenue over the period of the arrangement with the related payments being expensed.

4.61 Under policy C2 (recognition of the residual-interest asset over the period of the arrangement), a liability or asset is recognised on a cumulative basis, along with annual expenses or revenue respectively, depending on whether the related payments exceed or are less than the estimated future fair value of the residual-interest asset. There is no "unearned" amount under this approach.

4.62 Policy C3 (recognition of the residual-interest asset at the end of the arrangement) does not result in unearned revenue. When the grantor recognises the asset, it recognises either revenue (if no payment is required), a liability (if required payments not yet made) or a reduction in assets for the consideration paid at the end of the arrangement. Any consideration paid for the residual-interest asset during the period of the arrangement presumably would be treated as a prepayment asset, if policy C3 was to be applied strictly.

Policy D – No Recognition

4.63 Refer to paragraphs 4.42 and 4.43.

TABLE 4 – GRANTOR PROVIDES OPERATOR WITH LICENCE TO CHARGE USERS

Assets	**Liabilities**	**Comments**
BOO or BOOT Arrangements		
A. Recognise Property in Full Measure at cost = fair value [116.15] Depreciate over useful life, not period of arrangement [116.50]	A1 Revenue recognised in full; OR A2 Unearned revenue .. amortise to revenue over period of arrangement [118.20]	No recognised asset given up; or Grantor to provide services or limit its actions over period
OR		
BOOT Arrangements Only		
B. Recognise Residual Interest Only Property relating to operation period not recognised by grantor	No liability relating to operation period	
Residual interest (RI) recognised: B1 At inception: .. at cost – PP&E [116.15]; OR .. at cost – intangible [138.24]; OR	Liability at inception; OR Revenue recognised in full; OR Amortise unearned revenue	Payments reduce liability; OR No payments required; OR No payts but amortise revenue
B2 Accumulate over period of arr't: .. straight-line method; OR .. annuity method; OR	Liability/expense accumulates if total payment for RI > FV; asset/revenue accumulates if total RI payment < FV	Results in RI recorded at FV at end of the arrangement period
B3 At end of arrangement period, as PP&E [AASB 116]	No unearned revenue	

Assets	Liabilities	Comments
Depreciate RI over remaining useful life once grantor operates property [116.50]		Treat as PP&E when grantor starts to operate the property
OR		
<u>BOO Arrangements Only</u>		
C. No Recognition		
No asset recognised	No liability recognised	No accounting recognition when there are no payments

4.64 Table 4 portrays the alternative accounting policies for asset and liability recognition and measurement that could be adopted by a public sector grantor when it provides the operator with a right or licence to charge users of the property underlying the service concession arrangement, classified by type of arrangement. The Table 2 notes concerning recognition all apply equally to this Table, however more detail is provided in this Table, and in the following paragraphs, for the credit side of the recognition entries, as well as adding measurement policy alternatives. As with the previous tables, Table 4 does not indicate the basis upon which a grantor may choose a particular accounting policy.

Policy A – Recognise Property in Full

4.65 An asset recognised under AASB 116 *Property, Plant and Equipment* may be measured after initial recognition using either the cost model or the revaluation model (if fair value can be measured reliably).

4.66 Under policy A1 (refer to the liabilities column), the grantor immediately recognises revenue equal to the amount of the property recognised. This approach may be justified on the grounds that the grantor does not give up a recognised asset of its own, since rights to charge users of property typically are not recognised as assets by grantors. This is so even if there are limits on the rights that could be provided by a grantor. For example, a city might be able economically to support three toll roads, but not four or more. The third licence might exhaust the unrecognised "right to charge for road use" asset, but again no outflow of recognised economic benefits would be required. An alternative justification for the up-front revenue recognition is that the grantor recognises the licence to charge users as an asset, with the credit to revenue, and the licence asset is then used to settle the acquisition of the property.

4.67 Approach A2, on the other hand, takes the view that the grantor is required to perform in certain ways under the arrangement, which requires the grantor to recognise revenue over the arrangement period as those actions are performed, in accordance with AASB 118 *Revenue*. The actions in a toll road case might be (1) continuing to make the grantor's land available to the operator for the toll road; (2) not withdraw the right to toll users; (3) continue to enforce penalty collection; (4) continue to connect the grantor's roads to the toll road; and (5) not add competing transport methods, such as new or wider roads or public transport.

Lease Accounting

4.68 As for Table 2, there is no lease accounting approach since the grantor does not make a series of payments (or any payment) to the operator in return for the right to use (control the use of) the property.

Policy B – Recognise Residual Interest Only

4.69 In addition to various recognition timing policies (labelled B1, B2 and B3 in Table 4), there are various measurement policies as well under policy B. For example, recognising the residual-interest asset at the inception of the arrangement (approach B1) could result in the recognition of a liability for any payments required in respect of the residual interest, immediate revenue for the grantor if no payment is required, or unearned revenue amortised as revenue over the arrangement period.

4.70 The accounting under policies B2 and B3 would be the same as that for policies C2 and C3 for "grantor pays" arrangements – refer to paragraphs 4.59, 4.61 and 4.62.

Policy C – No Recognition

4.71 Refer to paragraphs 4.51 and 4.52.

5 EVALUATION OF THE POSSIBLE ACCOUNTING APPROACHES AND POLICIES

5.1 The Questions set for the Panel's consideration do not require an evaluation of the possible accounting approaches and policies, except in respect of Interpretation 12 if the Panel found that grantors were required to follow the Interpretation (Question 2). As a majority of the Panel holds the view that grantors are not required to follow the Interpretation, the Panel is not required by its terms of reference to evaluate the approaches and policies set out in this Report.

5.2 However, the Panel decided to add its views on various approaches and policies, to assist the AASB in considering whether it should limit in any way the accounting policy choices available to public sector grantors. This part of the Report addresses the following:

(i) the four general approaches to recognising the property underlying a service concession arrangement, which are described in paragraphs 4.5 to 4.20 above;

(ii) the accounting by public sector grantors "applying" Interpretation 12, noting in particular issues concerning the reference to regulation; and

(iii) the scope exclusion inserted into Interpretation 4 at the same time as the issue of Interpretation 12, given uncertainty over its meaning.

The General Approaches to Property Recognition

5.3 Under the AASB 108 requirements, the consideration of Standards (which reference includes Interpretations) dealing with similar and related issues (paragraph 11) is intended to assist the management of an entity in making the judgement described in paragraph 10: the development and application of accounting policies that result in relevant and reliable information for the users of the entity's financial report. With this in mind, the Panel discussed whether it could recommend to the AASB that one or more of the four general approaches should not be able to be adopted by grantors in determining how to account for the property underlying a service concession arrangement.

Risks and Rewards Approach and Control Approach

5.4 The Panel concluded that the substantially all/majority of risks and rewards approach and the control approach both had significant support in Accounting Standards and that neither approach could be rejected, despite Panel members holding different views on the extent to which these approaches were discrete or interrelated.

Rights and Obligations Approach

5.5 The rights and obligations approach received less support from the Panel members, but not to the degree that the Panel could conclude that it should not be applied by grantors. Some Panel members consider that this approach is the most appropriate, especially for arrangements under which the grantor provides the operator with a licence to charge users. Other Panel members hold the view that the principal application of the rights and obligations approach presently is in respect of financial instruments, and that to extend it to non-financial elements would be going too far at this stage. They note that the IASB's project on applying a rights and obligations

approach to lease accounting will take a long time to develop. Some Panel members consider that a rights and obligations approach to service concession arrangements has the potential to be inconsistent with the leasing Standard as it is now, and perhaps with other Standards such as AASB 116 *Property, Plant and Equipment*.

5.6 However, other Panel members take the view that the rights and obligations approach cannot be rejected because in effect it represents a unit of account issue. For example, accounting for property, plant and equipment as tangible items depends on the level at which separate items are identified. For complex items, this could mean the recognition of either the composite items or the components of the items, all of which are rights held in some form by the entity.

Control or Regulation Approach

5.7 The control or regulation approach, which is adopted in Interpretation 12, is the only one of the four general approaches that a majority of the Panel members considered should not be available for grantors to apply. Panel members note that this approach has not been adopted in other Standards. They suggest that the incorporation of control by independent regulators in determining whether a public sector grantor should recognise the property underlying an arrangement goes too far. This is elaborated upon in the following section of the Report. The indicators of control applied in Interpretation 12 also were viewed by some Panel members as too limited.

5.8 The majority view is that following Interpretation 12 would be likely to result in relevant and reliable financial information in the financial statements of grantors, except when the paragraph 5(a) criteria are satisfied due only to the operator's access to the infrastructure (or property) being so restricted by an independent regulator. In this case, the view is that the grantor does not control the property and should not recognise it in full as an asset – even though the operator does not recognise it either by virtue of its application of the Interpretation.

Accounting by Grantors following Interpretation 12

Relevant and Reliable Information

5.9 The Panel members hold the general view that following the Interpretation to the extent possible in terms of accounting reflecting that of operators is likely to may result in relevant and reliable financial information in the financial statements of grantors – when the grantor itself controls the property underlying the service concession arrangement with no need to refer to "regulatory" arrangements in reaching that conclusion. In such cases, they consider that paragraph 10 of AASB 108 would be satisfied in following the requirements of Interpretation 12 under paragraph 11, whether this was done voluntarily or mandatorily.

5.10 However, a majority of Panel members argue that it is inappropriate to simply follow Interpretation 12 for public sector grantors without separate consideration of the accounting issues from the grantors' perspective. They note that the IFRIC, in developing Interpretation 12, did not consider the accounting issues from the perspective of grantors. If this had been done, they suggest that it is conceivable that requirements for grantors would differ from a mere symmetrical or consistent outcome.

5.11 Consequently, a majority of Panel members consider that following the Interpretation to the extent possible in terms of accounting reflecting that of operators may not necessarily achieve the primary objective of providing relevant and reliable financial information in the financial statements of grantors. For example, they take the view that the Interpretation has dealt inappropriately with control and regulation in relation to public sector entities, and that the statement in paragraph AG6 of the Interpretation that the grantor controls infrastructure within the scope of the Interpretation was not necessary for the IFRIC to conclude upon the accounting by operators. In their view, the IFRIC need only have concluded that operators do not control the infrastructure, as is stated in paragraph BC24 of the IFRIC's Basis for Conclusions, without stating whether or not grantors control the infrastructure instead.

Control and Regulation in the Public Sector

5.12 Paragraph 5(a) of Interpretation 12 states that it applies to public-to-private service concession arrangements if the grantor "controls or regulates" the services that the operator must provide with the infrastructure, to whom, and at what price. Furthermore, paragraph AG2 states that this control or regulation could be by contract or otherwise (such as through a regulator), and goes on that the grantor and any related parties (i.e. "the public sector as a whole"), including any regulators acting in the public interest, shall be considered together in applying this condition.

5.13 The AASB objected strongly to these statements when commenting to the IASB upon the near-final draft of the Interpretation in November 2006. The AASB was particularly concerned with the reference to regulation as a factor in determining control, and requested the IASB to delete the reference to "regulates" in paragraph 5(a) and the attendant application guidance in paragraph AG2. The AASB considered that the interpretation of control should depend on the substance of the arrangement without referring to the form of regulation under which the service concession operates. The inclusion of rights or responsibilities of related parties of a grantor in assessing control or regulation inappropriately blurs the line between entities. The elements of financial statements are defined in the *Framework* in relation to individual entities, not entities in conjunction with their related parties.

5.14 The AASB added that regulators acting in the public interest by definition do not act in the interest of a government that might have established the regulator or provide on-going funding etc. Under this view, it is inappropriate to assess the issue of control over infrastructure assets by a public sector grantor by reference to whether a regulator established in the same jurisdiction has any regulatory role in relation to the service concession arrangement.

5.15 Some Panel members hold the view that many service concession arrangements in Australia do not result in the grantor controlling the underlying property directly, on the basis that the arrangements typically do not specify to whom the services are to be provided. In their view, for example, a general expectation that "the public" is the target recipient group is too broad to contend that the grantor controls to whom the services are to be provided. External regulation such as anti-discrimination legislation can affect the boundaries of the recipient group. Under this view, many arrangements would be brought within the scope of Interpretation 12 only because of its reference to "regulates" and the inclusion of regulation by regulators.

5.16 Some Panel members also suggest that the inclusion of the reference to regulation in the paragraph 5(a) criteria is inconsistent with the discussion of the factors affecting

whether a government controls another entity in AAS 31 *Financial Reporting by Governments*. The conclusion drawn in paragraph 9.1.7(d) of AAS 31 is that a government does not control another entity where it merely has the power to regulate the behaviour of the entity by use of its legislative powers: the power to establish the regulatory environment within which entities operate and to impose conditions or sanctions on their operations does not constitute control of the assets of those entities.[1]

5.17 Under this view, a public sector grantor should not be considered to control the property underlying an arrangement if paragraph 5(a) is met only because of the reference to regulation, and it would be inappropriate for the grantor to follow the accounting set out in the Interpretation. This problem in following Interpretation 12 would not arise, however, if the grantor does indeed control the services the operator must provide, to whom and the price through the contract between the grantor and operator.

5.18 A majority of Panel members endorses this approach. Accordingly, they do not support the adoption of Interpretation 12 by a public sector grantor when the paragraph 5(a) requirements are satisfied due only to the operator's access to the property being so restricted by an independent regulator. In such a case, the grantor may be able to conclude that it does not control the property for the period of the arrangement, but that it does control the property after the end of the arrangement if there is a residual interest. In this case, requiring the grantor to recognise the property as an asset for the whole of the arrangement period would not appear to result in relevant and reliable information. Therefore, neither the grantor nor the operator would recognise the whole of the property as an asset – and perhaps neither party would recognise the property asset relating to the period of the arrangement.

The Scope Exclusion in Interpretation 4

5.19 The scope of Interpretation 4 *Determining whether an Arrangement contains a Lease* was amended when Interpretation 12 was issued. Paragraph 4(b) was added to Interpretation 4 to state that it does not apply to arrangements that are public-to-private service concession arrangements within the scope of Interpretation 12. However, Panel members note that there is some uncertainty as to the operation of this scope exclusion, as follows:

(i) the exclusion applies only for annual reporting periods beginning on or after 1 January 2008, and so Interpretation 4 is directly relevant to grantor accounting prior to then; and

(ii) does the exclusion apply to any arrangement that satisfies the scope criteria set out in Interpretation 12; or

(iii) does the exclusion apply only to any arrangement that both satisfies those scope criteria and is accounted for under Interpretation 12?

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1 The AASB agreed at its November 2007 meeting to include these statements in AASB 127 *Consolidated and Separate Financial Statements*, following its short-term review of the requirements in AAS 27 *Financial Reporting by Local Governments*, AAS 29 *Financial Reporting by Government Departments* and AAS 31.

5.20 For financial years ending 30 June 2008 and other periods prior to the effective date of the exclusion added to Interpretation 4, a public sector grantor may identify leases inherent in service concession arrangements based on the requirements of Interpretation 4 – and account for the arrangements on that basis. Those requirements are whether (a) fulfilment of the arrangement depends on the use of a specific asset or assets; and (b) the arrangement conveys to the grantor a right to use the asset (refer to extracts in the Appendix).

5.21 Once the scope exclusion becomes effective, for example for financial years ending 30 June 2009, a grantor may reach a different conclusion concerning leases inherent in an existing arrangement, if it takes the view that it can no longer refer to Interpretation 4 because of the scope exclusion and must apply only the general requirements and guidance in AASB 117 *Leases*. The grantor would in this case be interpreting the exclusion as applying to any arrangement that satisfies the scope criteria in Interpretation 12, regardless of whether the arrangement is accounted for under that Interpretation. The grantor might therefore change its accounting for the arrangement because of the scope exclusion.

5.22 Alternatively, the grantor might not change its accounting for the arrangement because it concludes that although the scope exclusion strictly applies, it can still take into account the requirements of Interpretation 4 through an application of the hierarchy for determining accounting policies as set out in the Panel's response on Question 1 (see paragraph 3.6 of this Report). In other words, the grantor might look for further guidance in applying AASB 117, and find it in Interpretation 4: the grantor is permitted, but not required, to apply Interpretation 4.

5.23 As another possibility, the grantor may conclude that the scope exclusion applies only if it accounts for the arrangement under Interpretation 12, and therefore that the scope exclusion cannot apply to grantors. Under this view, Interpretation 4 would continue to apply directly to the grantor, and the previous lease identification and accounting for the arrangement would be retained.

5.24 A majority of the Panel members therefore encourages the AASB to clarify whether the Interpretation 4 scope exclusion applies to grantors in respect of any service concession arrangement meeting the Interpretation 12 scope criteria, or whether it applies only in respect of any arrangement accounted for under Interpretation 12 by the entity (and thus applies only to operators).

6 CONCLUSIONS

6.1 The Panel's principal majority conclusions are as follows:

(i) AASB Interpretation 12 does not determine the general accounting by public sector grantors for service concession arrangements within the scope of the Interpretation due to the scope exclusion for grantors, but grantors are permitted to follow the Interpretation [paragraph 3.6];

(ii) grantors currently can choose from four different general approaches to determining how to account for the property underlying a service concession arrangement, in addition to a range of other recognition and measurement accounting policies. The Panel majority has not concluded whether one of these four approaches should be preferred, but has concluded that the "control or regulation" approach of Interpretation 12 is the only approach that should not be permitted, due to potential problems with the way it addresses control and regulation issues in the public sector [paragraphs 4.21 and 5.18]; and

(iii) the scope exclusion for service concession arrangements in Interpretation 4 needs to be clarified [paragraph 5.24].

AUTHORITATIVE ACCOUNTING LITERATURE AND OTHER GUIDANCE

This Appendix to the Report includes only selected extracts. AASB pronouncements are available on the AASB website.

Australia

(a) Accounting Standard AASB 108 ***Accounting Policies, Changes in Accounting Estimates and Errors*** (July 2004, as amended)

10 In the absence of an Australian Accounting Standard that specifically applies to a transaction, other event or condition, management shall use its judgement in developing and applying an accounting policy that results in information that is:

(a) relevant to the economic decision-making needs of users; and

(b) reliable, in that the financial report:

(i) represents faithfully the financial position, financial performance and cash flows of the entity;

(ii) reflects the economic substance of transactions, other events and conditions, and not merely the legal form;

(iii) is neutral, that is, free from bias;

(iv) is prudent; and

(v) is complete in all material respects.

11 In making the judgement described in paragraph 10, management shall refer to, and consider the applicability of, the following sources in descending order:

(a) the requirements and guidance in Australian Accounting Standards dealing with similar and related issues; and

(b) the definitions, recognition criteria and measurement concepts for assets, liabilities, income and expenses in the Framework.

12 In making the judgement described in paragraph 10, management may also consider the most recent pronouncements of other standard setting bodies that use a similar conceptual framework to develop accounting standards, other accounting literature and accepted industry practices, to the extent that these do not conflict with the sources in paragraph 11.

(b) AASB Interpretation 12 ***Service Concession Arrangements*** (February 2007)

4 This Interpretation gives guidance on the accounting by operators for public-to-private service concession arrangements.

5 This Interpretation applies to public-to-private service concession arrangements if:

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

(b) the grantor controls – through ownership, beneficial entitlement or otherwise – any significant residual interest in the infrastructure at the end of the term of the arrangement.

6 Infrastructure used in a public-to-private service concession arrangement for its entire useful life (whole of life assets) is within the scope of this Interpretation if the conditions in paragraph 5(a) are met. Paragraphs AG1–AG8 provide guidance on determining whether, and to what extent, public-to-private service concession arrangements are within the scope of this Interpretation.

9 This Interpretation does not specify the accounting by grantors.

11 Infrastructure within the scope of this Interpretation shall not be recognised as property, plant and equipment of the operator because the contractual service arrangement does not convey the right to control the use of the public service infrastructure to the operator. The operator has access to operate the infrastructure to provide the public service on behalf of the grantor in accordance with the terms specified in the contract.

Application Guidance [part of Interpretation 12]

AG2 The control or regulation referred to in condition (a) [of paragraph 5] could be by contract or otherwise (such as through a regulator), and includes circumstances in which the grantor buys all of the output as well as those in which some or all of the output is bought by other users. In applying this condition, the grantor and any related parties shall be considered together. If the grantor is a public sector entity, the public sector as a whole, together with any regulators acting in the public interest, shall be regarded as related to the grantor for the purposes of this Interpretation.

AG3 For the purpose of condition (a), the grantor does not need to have complete control of the price: it is sufficient for the price to be regulated by the grantor, contract or regulator, for example by a capping mechanism. However, the condition shall be applied to the substance of the agreement. Non-substantive features, such as a cap that will apply only in remote circumstances, shall be ignored. …

AG4 For the purpose of condition (b), the grantor's control over any significant residual interest should both restrict the operator's practical ability to sell or pledge the infrastructure and give the grantor a continuing right of use throughout the period of the arrangement. The residual interest in the infrastructure is the estimated current value of the infrastructure as if it were already of the age and in the condition expected at the end of the period of the arrangement.

AG5 Control should be distinguished from management. If the grantor retains both the degree of control described in paragraph 5(a) and any significant residual interest in the infrastructure, the operator is only managing the infrastructure on the grantor's behalf – even though, in many cases, it may have wide managerial discretion.

AG6 Conditions (a) and (b) together identify when the infrastructure, including any replacements required (see paragraph 21), is controlled by the grantor for the whole of its economic life. For example, if the operator has to replace part of an item of infrastructure during the period of the arrangement (e.g. the top layer of a road or the roof of a building), the item of infrastructure shall be considered as a whole. Thus condition (b) is met for the whole of the infrastructure, including the part that is

replaced, if the grantor controls any significant residual interest in the final replacement of that part.

Basis for Conclusions on *IFRIC Interpretation 12* [accompanies, but not part of, AASB Interpretation 12]

Private-to-private arrangements

BC14 Some respondents to the draft Interpretations suggested that the scope of the proposed Interpretation should be extended to include private-to-private service arrangements. The IFRIC noted that addressing the accounting for such arrangements was not the primary purpose of the project because the IFRIC had been asked to provide guidance for public-to-private arrangements that meet the requirements set out in paragraph 5 and have the characteristics described in paragraph 3. The IFRIC noted that application by analogy would be appropriate under the hierarchy set out in paragraphs 7–12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Grantor accounting

BC15 The Interpretation does not specify the accounting by grantors, because the IFRIC's objective and priority were to establish guidance for operators. Some commentators asked the IFRIC to establish guidance for the accounting by grantors. The IFRIC discussed these comments but reaffirmed its view. It noted that in many cases the grantor is a government body, and that IFRSs are not designed to apply to not-for-profit activities in the private sector, public sector or government, though entities with such activities may find them appropriate (see *Preface to IFRSs* paragraph 9).

Treatment of the operator's rights over the infrastructure

BC24 The IFRIC considered whether arrangements within the scope of IFRIC 12 convey 'the right to control the use of the underlying asset' (the public service infrastructure) to the operator. The IFRIC decided that, if an arrangement met the conditions in paragraph 5, the operator would not have the right to control the use of the underlying asset and should therefore not recognise the infrastructure as a leased asset.

BC25 In arrangements within the scope of the Interpretation the operator acts as a service provider. The operator constructs or upgrades infrastructure used to provide a public service. Under the terms of the contract the operator has access to operate the infrastructure to provide the public service on the grantor's behalf. The asset recognised by the operator is the consideration it receives in exchange for its services, not the public service infrastructure that it constructs or upgrades.

BC27 … The IFRIC concluded that this treatment is also consistent with IAS 18 *Revenue* because, for arrangements within the scope of the Interpretation, the second condition of paragraph 14 of IAS 18 is not satisfied. The grantor retains continuing managerial involvement to the degree usually associated with ownership and control over the infrastructure as described in paragraph 5.

BC28 In service concession arrangements rights are usually conveyed for a limited period, which is similar to a lease. However, for arrangements within the scope of the Interpretation, the operator's right is different from that of a lessee: the grantor retains control over the use to which the infrastructure is put, by controlling or regulating what services the operator must provide, to whom it must provide them, and at what

price, as described in paragraph 5(a). The grantor also retains control over any significant residual interest in the infrastructure throughout the period of the arrangement. Unlike a lessee, the operator does not have a right of use of the underlying asset: rather it has access to operate the infrastructure to provide the public service on behalf of the grantor in accordance with the terms specified in the contract.

(c) AASB Interpretation 4 *Determining whether an Arrangement contains a Lease* (February 2007)

4 This Interpretation does not apply to arrangements that:

(a) are, or contain, leases excluded from the scope of AASB 117; or

(b) are public-to-private service concession arrangements within the scope of AASB Interpretation 12 *Service Concession Arrangements*.

6 Determining whether an arrangement is, or contains, a lease shall be based on the substance of the arrangement and requires an assessment of whether:

(a) fulfilment of the arrangement is dependent on the use of a specific asset or assets (the asset); and

(b) the arrangement conveys a right to use the asset.

Fulfilment of the arrangement is dependent on the use of a specific asset

7 Although a specific asset may be explicitly identified in an arrangement, it is not the subject of a lease if fulfilment of the arrangement is not dependent on the use of the specified asset. For example, if the supplier is obliged to deliver a specified quantity of goods or services and has the right and ability to provide those goods or services using other assets not specified in the arrangement, then fulfilment of the arrangement is not dependent on the specified asset and the arrangement does not contain a lease. …

8 An asset has been implicitly specified if, for example, the supplier owns or leases only one asset with which to fulfil the obligation and it is not economically feasible or practicable for the supplier to perform its obligation through the use of alternative assets.

Arrangement conveys a right to use the asset

9 An arrangement conveys the right to use the asset if the arrangement conveys to the purchaser (lessee) the right to control the use of the underlying asset. The right to control the use of the underlying asset is conveyed if any one of the following conditions is met.

(a) The purchaser has the ability or right to operate the asset or direct others to operate the asset in a manner it determines while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.

(b) The purchaser has the ability or right to control physical access to the underlying asset while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.

(c) Facts and circumstances indicate that it is remote that one or more parties other than the purchaser will take more than an insignificant amount of the output or other utility that will be produced or generated by the asset during the term of the arrangement, and the price that the purchaser will pay for the output is neither contractually fixed per unit of output nor equal to the current market price per unit of output as of the time of delivery of the output.

(d) Heads of Treasuries of Australian Governments, *Additional Guidance on the Application of FRS 5 – Methods to Determine Control of Infrastructure Assets Used in the Australian Public Sector and Recognition of Emerging Assets, Up-Front Contributions and Leased Land* (June 2005)

1.1 Application

It is expected that this guidance material will be used to apply FRS 5 methods to contracts between a public sector entity (*concession provider*) and a private sector operator (*concession operator*) for the private provision of public infrastructure and services projects (PPPs).

1.2 Scope

This guidance material covers:

1. determining which party controls an asset, including:

   - practical application of the guidance using a decision tree which has been adapted from guidance material in TN 1 [UK Treasury Taskforce Technical Note No. 1 *How to Account for PFI Transactions*] and AN F [UK Accounting Standards Board, FRS 5, Application Note F];
   - explanation of key concepts applied in FRS 5, AN F and TN 1, using examples to illustrate these concepts;
   - discussion of common practical difficulties encountered with accounting assessments of PPP projects; and
   - case studies developed from actual PPP transactions in Australia and the UK, illustrating the key concepts.

2. when and how to recognise the emerging asset.

International Accounting Standards Board

(a) *IASB Update* (September 2004)

Business Combinations (phase I)

In the light of respondents' comments, the Board decided not to proceed with the proposals in the Exposure Draft [Exposure Draft of Proposed Amendments to IFRS 3 *Business Combinations – Combinations by Contract Alone or Involving Mutual Entities* (April 2004)]. Instead, IFRS 3 would retain the scope exclusions for combinations involving mutual entities and by contract alone without the obtaining of an ownership interest, pending completion of the joint project on purchase method procedures.

The Board noted the following implications of this decision:

- entities would need to account for combinations involving mutual entities or by contract alone without the obtaining of an ownership interest by applying the requirements in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* on developing accounting policies in the absence of a Standard or an Interpretation that specifically applies to a transaction or event.

- in accordance with the requirements in IAS 8, management must use its judgement in developing and applying an accounting policy that results in information that is:

  - relevant to the economic decision-making needs of users; and

  - reliable, including that the financial statements reflect the economic substance of the transaction or event.

  In making this judgement, management must refer to, and consider the applicability of, the requirements and guidance in Standards and Interpretations dealing with similar and related issues, and the definitions, recognition criteria and measurement concepts in the *Framework*. Management may also consider the most recent pronouncements of other standard-setting bodies that use a similar conceptual framework, other accounting literature and accepted industry practice, but only to the extent that these do not conflict either with the guidance in Standards and Interpretations dealing with similar and related issues or with the *Framework*.

- in accordance with IAS 8, an entity is precluded from applying a superseded Standard, such as the guidance in IAS 22 *Business Combinations* that was withdrawn in March 2004, when accounting for combinations involving mutual entities or by contract alone without the obtaining of an ownership interest. However, entities would be permitted to look to IFRS 3 for guidance. [pages 1-2]

United Kingdom

(a) Accounting Standards Board, Financial Reporting Standard FRS 5 *Reporting the Substance of Transactions* – Application Note F "Private Finance Initiative and Similar Contracts" (September 1998)

[This accounting standard is not necessarily IFRS compliant]

NB In this Application Note the following terminology is used:

(a) the entity (usually a public sector body) that acquires services under the Private Finance Initiative (PFI) contract is referred to as the 'purchaser'.

(b) the entity (usually a private sector body) that provides services under the PFI contract is referred to as the 'operator'.

(c) the road, hospital, prison etc that is the subject of the PFI contract is referred to as the 'property'. The word 'asset' is reserved for items that are recognised in the balance sheet.

F1 Under a PFI contract, the private sector is responsible for supplying services that traditionally have been provided by the public sector. It is integral to most PFI

contracts that the operator designs, builds, finances and operates a property in order to provide the contracted service. Examples of such properties are roads, bridges, hospitals, prisons, offices, information technology systems and educational establishments.

F3 Contracts of a similar nature to PFI contracts exist between entities in the private sector, for example some contracts for warehousing and distribution services, where a property is necessary to perform the contracted service. This Application Note is relevant to such contracts.

Overview of basic principles

F4 Present practice is not to capitalise contracts for services. However, where a property is needed to fulfil a contract for services, present practice may require the property to be recognised as the purchaser's asset. (For example, this is the case for some take-or-pay contracts where the operator builds a specialist property with little alternative use.) The purpose of the analysis below is to determine:

(a) whether the purchaser in a PFI contract has an asset of the property used to provide the contracted services together with a corresponding liability to pay the operator for it or, alternatively, has a contract only for services; and

(b) whether the operator has an asset of the property used to provide the contracted services or, alternatively, a financial asset being a debt due from the purchaser;

F5 Under the general principles of the FRS, a party will have an asset of the property where that party has access to the benefits of the property and exposure to the risks inherent in those benefits. If that party is the purchaser, it will have a corresponding liability to pay the operator for the property where the commercial effect of the PFI contract is to require the purchaser to pay amounts to the operator that cover the cost of the property.

F6 In some cases the contract may be separable, ie the commercial effect will be that elements of the PFI payments operate independently of each other. 'Operate independently' means that the elements behave differently and can therefore be separately identified. Where this is the case, and where some elements relate only to services (such as cleaning, laundry, catering etc) rather than to the property, any such service elements are not relevant to determining whether each party has an asset of the property and should be ignored. A contract may be separable in various circumstances (see paragraph F10).

F7 Once any separable service elements have been excluded, PFI contracts can be classed into:

(a) those where the only remaining elements are payments for the property. These will be akin to a lease and SSAP 21 'Accounting for leases and hire purchase contracts' (interpreted in the light of the FRS) should be applied.

(b) other contracts (where the remaining elements include some services). These contracts will fall directly within the FRS rather than SSAP 21.

F8 For those contracts that fall directly within the FRS, the question of whether a party has an asset of the property should be determined by looking at the extent to which each party would bear any variations in property profits (or losses). There are three important principles to be considered when undertaking such an analysis:

(a) A range of factors will be relevant in determining the extent to which each party would bear any variations in property profits (or losses) and it will be necessary to look at the overall effect of these factors when taken together.

(b) However, any potential variations in profits (or losses) that relate purely to a service should be excluded since it is only the property that may be included on the balance sheet of one of the parties, not the capitalised value of the whole service contract. Consequently, potential variations relating to the provision of services are not relevant to determining whether each party has an asset of the property.

(c) Paragraph 14 requires that, in determining the appropriate accounting treatment, greater weight should be given to those features that are more likely to have a commercial effect in practice. Where there is no genuine commercial possibility of a particular scenario or cash flow occurring, this scenario/cash flow should be ignored.

Factors relevant to the property

F22 As noted in paragraph F19, in applying the FRS the key test is to establish who will bear any variations in property profits (or losses). Depending on particular circumstances, a range of factors may be relevant to this assessment of profit variation. The principal factors that, depending on the particular circumstances, may be relevant are:

- demand risk (see paragraphs F24-F31)
- the presence, if any, of third-party revenues (see paragraphs F32-F34)
- who determines the nature of the property (see paragraphs F35-F37)
- penalties for underperformance or non-availability (see paragraphs F38 and F39)
- potential changes in relevant costs (see paragraphs F40 and F41)
- obsolescence, including the effects of changes in technology (see paragraphs F42 and F43)
- the arrangements at the end of the contract and residual value risk (see paragraphs F44-F48)

F23 The above list of factors to be considered should be applied only with reference to the analysis given in paragraphs F24-F50. The key features of the analysis are summarised and illustrated in the table at the end of the Application Note.

Table

Variations in profits/losses for the property, in transactions falling directly within the FRS rather than SSAP 21 Three principles govern the assessment of the indications set out below: • only variations in property profits/losses are relevant. • the overall effect of all of the factors taken together must be considered. • greater weight should be given to those factors that are more likely to have a commercial effect in practice.	
Indications that the property is an asset of the purchaser	**Indications that the property is an asset of the operator**
Demand risk is significant and borne by the purchaser, eg (a) the payments between the operator and the purchaser will not reflect usage of the property so that the purchaser will have to pay the operator for the property whether or not it is used (b) the purchaser gains where future demand is greater than expected.	Demand risk is significant and borne by the operator, eg (a) the payments between the operator and the purchaser will vary proportionately to reflect usage of the property over all reasonably likely levels of demand so that the purchaser will not have to pay the operator for the property to the extent that it is not used (b) the operator gains where future demand is greater than expected.
There is genuine scope for significant third-party use of the property but the purchaser significantly restricts such use. The purchaser in some ways guarantees the operator's property income.	The property can be used, and paid for, to a significant extent by third parties and such revenues are necessary for the operator to cover its costs. The purchaser does not guarantee the operator's property income.
The purchaser determines the key features of the property and how it will be operated.	The operator has significant ongoing discretion over what property is to be built and how it will be operated.
Potential penalties for underperformance or non-availability of the property are either not significant or are unlikely to occur.	Potential penalties for underperformance or non-availability of the property are significant and have a reasonable possibility of occurring.
Relevant costs are both significant and highly uncertain, and all potential material cost variations will be passed on to the purchaser.	Relevant costs are both significant and highly uncertain, and all potential material cost variations will be borne by the operator.
Obsolescence or changes in technology are significant, and the purchaser will bear the costs and any associated benefits.	Obsolescence or changes in technology are significant, and the operator will bear the costs and any associated benefits.
Residual value risk is significant (the term of the PFI contract is materially less than the useful economic life of the property) and borne by the purchaser.	Residual value risk is significant (the term of the PFI contract is materially less than the useful economic life of the property) and borne by the operator.
The position of the parties to the transaction is consistent with the property being an asset of the purchaser, eg (a) the operator's debt funding is such that it implies the contract is in effect a financing arrangement (b) the bank financing would be fully paid out by the purchaser if the contract is terminated under all events of default including operator default.	The position of the parties to the transaction is consistent with the property being an asset of the operator, eg (a) the operator's funding includes a significant amount of equity (b) the bank financing would be fully paid out by the purchaser only in the event of purchaser default or limited force majeure circumstances.

Purchaser does not have an asset of the property – Acquisition of the Residual

F56 Where the contract specifies the amount (including zero) at which the property will be transferred to the purchaser at the end of the contract, the specified amount will not necessarily correspond with the expected fair value of the residual estimated at the

start of the contract. Any difference must be built up over the life of the contract in order to ensure a proper allocation of payments made between the cost of services under the contract and the acquisition of the residual. At the end of the contract the accumulated balance (whether positive or negative), together with any final payment, should exactly match the originally estimated fair value of the residual. …

United States of America

(a) Governmental Accounting Standards Board, Concepts Statement No. 4 *Elements of Financial Statements* (June 2007)

6 A central feature of most of the definitions is a resource. … In a general sense, a resource is a supply or other means that can be drawn on when needed. [footnote omitted] In the governmental context, a resource is an item that can be drawn on to provide services to the citizenry.

Assets

8 *Assets* are resources with present service capacity that the government presently controls.

9 The present service capacity of a resource that is an asset is its existing capability to enable the government to provide services, which in turn enables the government to fulfill its mission. The present service capacity of an asset may be used by the government in different ways. Parks and roads are examples of assets with present service capacity that is directly deployed by the government in that the citizenry or public directly use the asset. … One of the hallmarks of government is its deployment of assets that provide service directly, such as infrastructure, that need not be associated with charges to recipients of the service nor need to be able to be sold. Cash is an asset with present service capacity that is used by the government to procure services for the citizenry. The present service capacity of investments, land held for sale, or income-producing assets can be used in a similar manner because they can be sold to produce cash or to generate cash. This form of present service capacity is sometimes referred to as economic benefit.

10 An asset may be tangible and have physical form, such as buildings and equipment, or may be intangible, such as the right to use intellectual property. It remains an asset only so long as it is still capable of providing services. For example, a piece of equipment is considered an asset if the present service capacity embodied in the equipment either (a) can be used to provide services or (b) has economic benefit.

Definition and Characteristics of Control

12 Control of an asset is the ability of the government to utilize the resource's present service capacity and to determine the nature and manner of use of the present service capacity embodied in the resource. Generally, the government controlling the asset has the ability to determine whether to (a) directly use the present service capacity to provide services to citizens; (b) exchange the present service capacity for another asset, such as cash; or (c) employ the asset in any of the other ways it may provide benefit. For an asset that is provided for use by the citizenry and general public, control is held by the government that possesses the ability to control access to the present service capacity embodied in the asset. This control may be demonstrated, for

example, by determining the level of service the asset will provide, such as setting hours of operation and fee levels for a public park. …

13 Control of the present service capacity embodied in an asset generally arises from contractual rights or legal ownership. Some resources, such as real property, may represent a bundle of rights associated with the resource—for example, the right to develop the property, the right to extract minerals from the property, and the right to install and maintain utility lines crossing the property. Different entities may control different rights associated with a single property. Provided the various rights possess the other inherent characteristics of an asset and meet the recognition and measurement criteria, these different rights associated with real property, for example, would be reported as assets by different entities. In this example, no single entity would report the entire real property resource as its asset.