

**Issues Paper – IPSAS 32 *Service Concession Arrangements: Grantor*  
as the Basis for an Australian Exposure Draft**

At the September meeting, the AASB decided that if the IPSASB were to approve its draft Standard for issue as a Standard, rather than re-exposing it for comment, the AASB would consider at a future meeting whether to issue an exposure draft based on that Standard that includes proposed requirements that are modified from the IPSASB's requirements. For example, the proposals might include modified revenue recognition requirements consistent with the outcome of the IASB project on revenue from contracts with customers.

The IPSASB approved the draft Standard at its September meeting for issue as IPSAS 32, for application to reporting periods beginning on or after 1 January 2014. The final Standard has not yet been published, and it is uncertain when it will be published. Publication processes for IPSASs include editorial review by IFAC staff.

**Issues previously identified by the AASB**

The minutes of the September meeting record that the AASB identified the following issues with the draft Standard to be considered by the IPSASB:

- (a) the treatment of regulation that is the responsibility of third-party regulators in relation to whether the grantor controls or regulates the services that the operator must provide under a service concession arrangement, the recipients and the pricing of the services. Members noted that a third-party regulator could be from a different jurisdiction to the grantor, which may affect the assessment of whether the grantor should recognise service concession assets provided by the operator; and
- (b) the initial measurement of the grantor's liability under a service concession arrangement at the fair value of the service concession assets, rather than the fair value of what the grantor has given up – when the grantor grants a licence to the operator to charge users of the service concession assets, the licence covers both the availability of the assets to the operator over the term of the arrangement and the services to be provided by the operator, so that the grantor's assets may include both the underlying service concession assets and a prepaid service component. The Board considered that the draft Standard should address the creation of licences by the grantor in connection with service concession arrangements.

These issues remain as the Standard retains the same approaches in respect of these aspects as in the draft Standard.

**Regulation by third-party regulators**

The treatment of regulation by third-party regulators in relation to whether the grantor “controls or regulates” the services that the operator must provide under a service concession arrangement, the recipients and the pricing of the services is problematic. This is the criterion in the pivotal paragraph 9(a) of IPSAS 32.

Paragraphs AG6-AG8 make clear that a grantor could be taken to control or regulate the service concession assets – and hence required to recognise them – even if a third-party regulator regulates the assets in the manner and to the degree required. This approach is intended to mirror the approach in IFRIC Interpretation 12, wherein the operator does not recognise the assets as its own if the grantor and/or related regulators control or regulate the

assets to the degree required. Paragraph AG8 concludes that the grantor's control may derive from the specific regulation itself and not from the grantor being related to the regulator.

There are alternative views on whether the approach in IPSAS 32 is appropriate.

#### The IPSAS 32 Approach is Inappropriate

The basis for this view is that the mirror approach does not hold true for the grantor. The mirror approach appears to be that if the operator does not recognise the service concession assets under its equivalent of paragraph 9(a), then the grantor ought to do so.

Under this view, it is not appropriate for the grantor to recognise the service concession assets if the requisite control or regulation is obtained only through the third-party regulator. In such a case, the grantor itself does not control or regulate the assets and hence should not recognise them.

What this means is that at some level in the public sector jurisdiction, the rights of the grantor and of the third-party regulator will combine to amount to the control or regulation of the service concession assets contemplated in paragraph 9(a). It is only at that level that the public sector entity should recognise the assets. In some jurisdictions, this may be at the whole of government level or else at the parent "crown entity" or "central government entity" level. In such cases, the grantor itself would not be entitled to recognise the service concession assets as its own assets.

A further problem arises where the third-party regulator is from a different public sector jurisdiction to the grantor. For example, the regulator could be a federal government entity, and the grantor a state government entity. In such a case, if the grantor itself or in combination with other entities within its state government did not satisfy the paragraph 9(a) criterion, then it would appear that no public sector entity would recognise the service concession assets where the federal and state governments were not consolidated into some overarching public sector entity. No such consolidation is prepared in Australia.

#### The IPSAS 32 Approach is Appropriate

This view takes a different perspective on how the operator and the grantor would review the effect of regulations on the question of which entity controls service concession assets under an arrangement. The perspective is to treat the effects of third-party regulation essentially as the predetermination of certain activities or parameters within which the service concession arrangement must be operated. Given those parameters, the question is then whether the operator or the grantor controls the assets.

This is perhaps a "control of assets" equivalent to the issue of the control of entities when certain activities of an entity are predetermined. AASB 10 *Consolidated Financial Statements* addresses those circumstances.

#### **Recognition of revenue under the grant of rights model**

The initial measurement of the grantor's liability under a service concession arrangement at the fair value of the service concession assets, rather than the fair value of what the grantor has given up, does not appear to be the appropriate focus for the grantor's accounting. The AASB considered that the Standard should address the creation of licences by the grantor in connection with service concession arrangements.

If the grantor recognised the licence initially at fair value, then the credit would appear to be either revenue or a liability or a combination, in accordance with the existing Standards on the recognition of revenue. The exchange of the licence for the service concession assets under the service concession arrangement then results in the grantor recognising those assets in lieu of the licence.

As the licence covers both the availability of the assets to the operator over the term of the arrangement and the services to be provided by the operator, the fair value of the licence may exceed the fair value of the service concession assets. The difference may represent a prepaid service component.

Paragraph 26 in IPSAS 32 is expected to state:

“Where the grantor compensates the operator for the service concession asset and service provision by granting the operator the right to earn revenue from third-party users of the service concession asset or another revenue-generating asset, the exchange is regarded as a transaction that generates revenue. As the operator has the right to earn revenue over the period of the service concession arrangement, the revenue is not recognized immediately. Instead, a liability is recognized for any portion of the revenue that is not yet earned. The revenue is recognized in accordance with the economic substance of the service concession arrangement and the liability is reduced as revenue is recognized.”

#### **Process for developing an AASB Exposure Draft**

Given the present lack of the final version of IPSAS 32, staff suggest that the AASB’s service concessions committee should develop the proposals for the AASB’s Exposure Draft, for consideration at the AASB’s December meeting.

IPSAS 32 will be provided to Board members once it has been published by the IPSASB.

Do Board members have comments on the issues raised and the proposed process for developing an exposure draft?
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