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***Australian Bureau of Statistics (ABS) comments on ED 261 Service Concession Arrangements: Grantor***

Dear Ms Peach,

1. The ABS appreciates the opportunity to comment on *Exposure Draft 261 Service Concession Arrangements: Grantor* (ED 261). We appreciate the need to maximise harmonisation between Government Finance Statistics (GFS) and Generally Accepted Accounting Principles (GAAP). These comments are based on our knowledge of GFS concepts and issues, and viewing the exposure draft through this lens.
2. Within GFS, and more broadly in ABS macroeconomic statistics, Service Concession Arrangements are considered with other types of Public Private Partnership (PPP) arrangements. The general advice provided when determining the nature of PPP agreements can be summarised as follows:
  - i. PPP agreements are complex and variable. As such, each arrangement should be examined on a case by case basis to ensure consistency with the statistical standards.
  - ii. Macroeconomic statistics requires consistent treatment between both parties of a transaction. Both sides of the transaction must record the transaction in a consistent and coherent manner.
  - iii. Economic ownership of assets constructed under PPP arrangements are determined based on assessing which unit bears the majority of the risks and which unit is expected to receive a majority of the rewards of the asset. There are risks which are associated with constructing or acquiring the asset, and risks associated with operating the asset. In some cases, the mix of risks is such that there is a different economic owner during the construction phase and during the operation phase. Some of the specific risks considered when determining the economic ownership of PPP assets are outlined in Appendix 1.
  - iv. If the grantor (government) is considered the owner of the asset then it will be recorded on its balance sheet. In most cases the grantor will not make full payment for the asset initially - in this case it will also likely record a liability for future considerations to the operator, such as future payments. Depending on the nature of the agreement these are likely to be a mix of financing and operating transactions. At the end of the agreement the government often owns the asset outright with no liability payable to the operator. The scope of ED 261 is limited to this situation.
  - v. If the operator is considered the economic owner of the asset then it will be recorded on its balance sheet. Any associated liabilities will also be recorded by the operator. Often ownership will transfer to the government once the agreement expires with limited

considerations. In this case it is best practice for the grantor to gradually record a financial claim over time, with the operator recording a corresponding liability, such that the value of the claim is equal to the residual value of the assets to be transferred.

3. ED 261 proposes a control-based approach when determining asset ownership. This states that the grantor controls the asset if and if (a) the grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them, and at what price; and (b) the grantor controls – through ownership, beneficial entitlement or otherwise – any significant residual interest in the asset at the end of the term of the arrangement.

4. ED 261 notes that the control approach is considered more appropriate than the risk and rewards approach in an Australian context as it focuses on service potential of the asset rather than the distribution of economic benefits between the two parties. The control approach is also preferred because similar treatment would be adopted by the operator and the grantor. The ABS appreciates the need for consistency between parties, and recognises that the control approach has an advantage in this aspect. However, the relevant accounting standard for leases (AASB 117) uses a risk and rewards approach for determining control. In some cases, there may be situations where the two approaches may provide different outcomes. For example, in example 2 provided in ED 261 (p48 - 52) the operator receives revenue from road users. Under the control approach the grantor is deemed the owner. Under the risk and rewards approach the demand risk for using the asset is assumed by the operator, which would be an indicator that the operator is the economic owner. While other factors would need to be considered, and in practice there should be similar outcomes between the two approaches, this example shows that care needs to be taken when determining control. The ABS uses a risks and rewards approach consistent with international statistical standards.

5. ED 261 also seeks comments on some specific matters. Some of these are addressed below.

- ABS supports the use of the standard across all public sector entities, not public sector entities other than Government Business Enterprises (question 1).
- ABS supports the scope of the standard to include intangible assets and land (question 2).
- ABS proposes the use of the risk and rewards approach to allocating control of any service concession asset so that the standard can be consistently applied across PPP-type arrangements (question 3).
- ABS supports the use of fair value measurement for service concession assets. This is consistent with the market valuation approach preferred in macroeconomic statistics (question 4).
- The ABS supports the use of the 'financial liability model' and the 'grant of a right to the operator model' to measure the service concession liability in principle (question 5). However, there would be potential deviations between GAAP and GFS in the 'grant of a right to the operator model' in the case where the licence that provides the right to the operator can be traded. In this situation GFS would treat the licence as an intangible asset classified as a contract, leases and licences.

- In the 'grant of a right to the operator model', the reduction in liability over the life of the agreement is recognised as other revenue on the statement of profit and loss and other comprehensive income (paragraph 7). ABS's view is that this would not be considered revenue for GFS purposes as the government is not undertaking any operating activity to increase its net worth. It is likely that the reduction in liability would be reflected in GFS as a revaluation of the grant to a right to the operator liability.

6. ABS is currently reviewing the Australian standards used to compile Government Finance Statistics as was noted in the exposure draft. Our views outlined in this submission are not expected to change under these changes. A prepublication version of the Australian GFS manual will be published on the ABS on the 31st July 2015. We welcome feedback from interested parties, including the AASB. The ABS has also recently started a web-portal called the 'GFS community'. The purpose of this portal is to encourage comment and discussion between parties interested in GFS related matters. In this spirit we will publish this note on the portal to promote discussion on GAAP/GFS harmonisation. We encourage AASB participation in this forum. Please contact Jonathon Khoo (email: j.khoo@abs.gov.au, ph: 07 3222 6142) if you would like to discuss this response further.

Kind regards,

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## Appendix: Determining the economic ownership of PPP-related assets

The economic owner of the assets related to a PPP is determined by assessing which unit bears the majority of the risks and which unit is expected to receive a majority of the rewards of the asset. The factors that need to be considered in assessing economic ownership of PPP-related assets include those associated with acquiring the asset and those associated with using the asset.

### Some of the risks associated with acquiring the asset are:

- The degree to which the government controls the design, quality, size, and maintenance of the assets; and
- Construction risk, which includes the possibility of additional costs resulting from late delivery, not meeting specifications, or building codes, and environmental and other risks requiring payments to third parties.

### Some of the risks associated with operating the asset are:

- Supply risk - covers the degree to which the government is able to control the services produced, the units to which the services are provided, and the prices of the services produced;
- Demand risk - includes the possibility that the demand for the services, either from government or from the public at large in the case of a paying service, is higher or lower than expected;
- Residual value and obsolescence risk - includes the risk that the value of the asset will differ from any price agreed for the transfer of the asset to government at the end of the contract period; and
- Availability risk - includes the possibility of additional costs or the incurrence of penalties because the volume and/or quality of the services do not meet the standards specified in the contract.