



The Chair  
Australian Accounting Standards Board  
PO Box 204  
Collins Street West  
Victoria, 8007

Our ref ED 261 - Submission letter

4 August 2015

Dear Kris

**Submission - Exposure Draft 261 - Service Concession Arrangements: Grantor**

We appreciate the opportunity to comment on Exposure Draft 261 *Service Concession Arrangements: Grantor* (ED).

We support the issue of an accounting standard on grantor accounting in Service Concession Arrangements (SCAs) by the Australian Accounting Standards Board (Board) as there is divergence in practice between grantors and operators of SCAs and also between the various grantors.

Overall we support the accounting approach proposed in the ED which is based on a control or regulation approach which is consistent with IPSAS 32 *Service Concession Arrangements: Grantors* and Interpretation 12 *Service Concession Arrangements* as this will create consistency between grantors and operators.

However we note the following which we consider should be clarified in the Standard:

*Grant of right model – interaction with AASB 15*

The nature of the liability when it is a Grant of Right obligation is unclear. For example, BC 24 notes that the Board is of the view that SCA which involves a transfer of an intangible asset is not a contract with a customer within the scope of AASB15 *Revenue from contracts with customers*. However AG 52 requires grantors to recognise revenue in accordance with the economic substance of the arrangement. If Grant of Right SCAs are considered to be outside the scope of AASB 15, then it is possibly other income (as opposed to revenue) that should be recognised consistent with the economic substance of the SCAs. Where there is continuing substantive involvement by the grantor during the SCA term, the amount is deferred and progressively recognised as other income over the term of the involvement.

If the Board considers that Grant of Right SCAs are within the scope of AASB 15, revenue recognition should be based on the principles of AASB 15. An explanation should be provided for the basis of revenue recognition as noted in paragraph 25, for example, it is considered that the grantor in such SCAs has an obligation to provide a service over the life of the arrangement.



We note a number of issues in Appendix B which we consider the Board should continue to develop after the issue of the Standard. We also recommend that the Board undertakes a post implementation review project. However the Board should not delay the issue of the Standard to resolve these questions.

Appendix A to this letter comments on the specific questions raised in the ED.

Please contact either myself on (03) 9288 6261 or Elleni Daniels on (02) 9455 9324 if you wish to discuss any of the issues raised in this letter.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Pat Stebbens', with a long horizontal flourish extending to the right.

Patricia Stebbens  
Partner

## Appendix A

### KPMG's Response to Specific Questions posed by the AASB

Our comments on the specific matters raised for comment by the AASB are set out below:

- 1) The proposed application to all public sector entities is wider than IPSAS 32 Service Concession Arrangements: Grantor, upon which the [draft] Standard is based. IPSAS 32 applies to all public sector entities other than Government Business Enterprises (GBE). A GBE is akin to a for-profit public sector entity. The proposed approach is consistent with the AASB's policy of making accounting Standards that require like transactions and events to be accounted for in a like manner for all types of entities, which is referred to as transaction neutrality. Do you agree with the proposed application to all public sector entities? Why or why not?*

We agree with the concept of transaction neutrality and therefore agree with the application of this Standard to all public sector entities including Government Business Enterprises.

However there may be a concern that the application of the Standard to GBEs may result in those entities being unable to claim compliance with International Financial Reporting Standards (IFRS). The AASB should include a statement in the Standard on whether entities applying this Standard could still claim IFRS compliance or if compliance cannot be claimed, the Standard should set out the potential areas of differences.

- 2) The proposed scope in paragraph 5 applies to arrangements involving a 'service concession asset', which would include intangible assets and land. This is consistent with the scope of IPSAS 32 but broader than the scope of AASB Interpretation 12 Service Concession Arrangements. AASB Interpretation 12 applies to 'infrastructure' of a service concession arrangement, which would exclude intangible assets and land. AASB Interpretation 12 is applicable to infrastructure assets that the private sector operator constructed or acquired from a third-party, or to which it was given access by the grantor, for the purpose of the arrangement. Consequently, the intangible assets or land that has been granted by the grantor is outside the scope of AASB Interpretation 12. Do you agree with the proposed scope of the [draft] Standard? Why or why not?*

We agree with the proposal to include land and intangible assets. Increasingly intangible assets, such as software, are becoming the subject of SCAs. These arrangements have the same characteristics as SCAs involving infrastructure assets except that the underlying asset is intangible or land and therefore should be treated consistently.

- 3) ***The [draft] Standard proposes the specific control concept in paragraph 8(a) that a grantor controls the asset if the “grantor controls or regulates what services the operator must provide with the asset, to whom it must provide them and at what price”. This mirrors the control concept in AASB Interpretation 12. The AASB notes that a broader concept of control currently applies in other Australian Accounting Standards. An asset that does not meet the control and regulation definition of this [draft] Standard may still need to be recognised under other accounting Standards. Do you agree with the proposed specific control concept in paragraph 8(a) of the [draft] Standard? That is, applying a narrower concept of control in the [draft] Standard than other accounting Standards. Why or why not?***

We agree that a grantor should recognise the service concession asset underlying the SCA in its financial statements if the grantor controls the asset.

Whilst acknowledging that the proposed control concept is a narrower concept of control, (it can be viewed as a subset of the broader concept of control), we agree with the proposals as this would at least provide some guidance on how control should be assessed in SCAs. As noted in Appendix B, the AASB should monitor the implementation of the Standard and if necessary, update the Standard at a later date.

#### *Control of services requirements*

It would be useful to provide more guidance on how to assess whether services are considered to be controlled or regulated by the grantor. The degree of specificity of the services that have to be provided in SCAs varies in practice. For example, specification may be with reference to the type of services or tasks that need to be provided or in terms of the amount of output that should be delivered. We consider that the grantor controls the service if the arrangement sets out either the nature or type of service or task to be provided, or the amount of output that needs to be provided. Given the subjectivity of the assessment, additional guidance would mitigate any potential divergence in practice.

- 4) ***The [draft] Standard proposes that the grantor initially measures the service concession asset at its fair value unless the service concession asset is an existing asset of the grantor. Do you agree that the proposed requirements and guidance appropriately explain the application of fair value to a service concession asset? Why or why not?***

We agree with the concept of recognising the service concession asset at fair value, using the principles of AASB 13 *Fair Value Measurement* as it is appropriate that this Standard does not introduce its own fair value principles over the guidance in AASB 13. Where guidance on the fair value measurement is required, this should be sourced from AASB 13.

We however acknowledge that there is a lack of guidance on the application of the fair value concept for not-for-profit entities including the public sector. We consider that this should not be resolved in this Standard but should be the subject of a separate project .

5) *The [draft] Standard proposes that:*

*(a) where the grantor recognises a service concession asset, the grantor also recognises a liability measured at the same amount as the service concession asset adjusted for other consideration between the grantor and operator. Do you agree that the proposed requirements and guidance appropriately measure the consideration between the grantor and the operator of the service concession arrangement? Why or why not?*

*(b) the measurement of a service concession liability using the 'financial liability model' and/or the 'grant of a right to the operator model'. Do you agree with the proposed models? Why or why not? If you do not agree with the proposed models, what alternative model(s) would you recommend?*

a) *Measurement of consideration between grantor and operator:*

Subject to the comment about the nature of the Grant of Right obligation as noted in our covering letter, we agree with the proposed requirements and guidance.

b) *Service concession liability models:*

*Financial liability model*

We agree with the recognition of a financial liability under this model. However we consider that the finance charge should not be based on the operator's cost of capital. Under financial instruments principles, the effective interest rate should reflect the risk free rate and the grantor's credit rating and any other credit enhancements, for example, collateral.

In addition where there is only a financial liability component, the rate can be determined as the internal rate of return given the fair value is derived from the asset and the cash flows are known. However there may be circumstances where it may be easier to determine the fair value of the asset by discounting the predetermined cash flows with an appropriate discount rate.

*Grant of right model*

Our comments about the nature of the liability under this model are discussed in the covering letter.

6) *The [draft] Standard proposes that the grantor account separately for each part of the total liability recognised for the service concession arrangement where the arrangement involves the grantor both incurring a financial liability and granting a right to the operator. Do you agree that the [draft] Standard provides appropriate guidance for the separate recognition of the liability? Why or why not?*

We consider that further guidance on how the fair value of the asset should be apportioned between financial liability and Grant of Right liability should be provided. For example, should the grantor apply a relative fair value approach or should the grant of right obligation be the residual which would be consistent with the approach prescribed on transition?

- 7) ***IPSAS 32 includes guidance in relation to other revenues in paragraphs AG55 – AG64. Other revenues relate to compensation by the operator to the grantor for access to the service concession asset by providing the grantor with a series of pre-determined inflows of resources. The [draft] Standard does not include this guidance, for the reasons outlined in paragraphs BC27 and BC28. Do you agree that guidance on the accounting treatment of other revenues from a service concession arrangement is not required? Why or why not?***

The guidance in AG55 to AG64 of IPSAS 32 is useful and inclusion of the guidance will ensure less divergence in practice. However we question whether it is consistent with the revenue recognition concepts in AASB 15. If the AASB considers that the guidance in IPSAS 32 may not be consistent with AASB 15, we agree that the guidance should be excluded from the Standard.

We note that paragraph 29 requires grantors to apply AASB 10XX Income of Not-for-Profit Entities for other revenues from SCAs. We recommend that this paragraph be deleted. A not-for-profit public sector entity would apply AASB 10XX in accordance with the scope of AASB 10XX. If the principles in AASB 10XX are consistent with those in AASB 15, there is no need to make this explicit statement for GBEs grantors. Conversely if the principles are different, then GBEs should be applying AASB 15, and not AASB 10XX. We also note that the cross referencing to AASB 10XX may hold up the issue of the Standard if the Not-for-Profit Entities project is delayed.

- 8) ***The [draft] Standard includes defined terms in Appendix A. Do you agree that the proposed defined terms in Appendix A appropriately explain the significant terms in the [draft] Standard? Why or why not?***

***In particular, do you agree with the proposed definition of a ‘public service’ as a “service that is provided by government or one of its controlled entities, as part of the usual government function, to the community, either directly (through the public sector) or by financing the provision of services”? Why or why not?***

***Are there additional terms that should be defined in Appendix A to assist application of the [draft] Standard?***

Subject to below, we agree that the proposed defined terms appropriately explain the significant terms and the proposed definition of a public service.

- Public service

Whilst we acknowledge the difficulty in defining this term and appreciate the inclusion of a definition (which is absent in Interpretation 12), we consider that further clarification as noted below will assist with the application of the Standard. The following highlights some examples that based on the proposed definition, it is unclear whether they would be in or out of scope:

- Are assets used in the pursuit of public policy within the scope of the standard? Such assets include judicial buildings and Centrelink offices.
- Does the ultimate user of the asset have to be the public at large or whether the government can be the user but in pursuit of public policy? For example, an internal communication network is used by a government agency as part of providing emergency services to be public, but the network is not accessible by the public directly. Other examples include a government authority purchasing services from a water treatment plant as an intermediary step to providing clean water to the public.
- What are the types of services that are considered to be part of the usual government function? For example, are the services provided by ports or airports considered to be those that would be provided as part of usual government function?

A further clarification which could assist users in determining the scope of a public service would be to provide context for those arrangements that are considered to be outside the scope of public service. For example paragraph 6 identifies outsourcing, service contracts and privatisation as outside scope. Providing examples of such arrangements and the factors that make these types of arrangements out of scope will assist with the application of the Standard.

- Service concession arrangements

To capture SCAs during the construction/development phase we would recommend updating the wording of this definition from “access to the service concession asset to provide a public service” to “access to the service concession asset to provide *or will provide* a public service”. While minor this will remove any unintended consequences of not meeting the definition of a SCA during the construction/development phase.

- Service concession asset

Similar to the comment above, we recommend updating the wording of this definition to include “An asset used to provide *or will provide* public services”. This will ensure that the service concession asset is captured by this definition during the construction/development phase.

**9) *The [draft] Standard includes examples on the accounting treatment of lifecycle costs of a service concession asset that might be a benefit to the grantor. Lifecycle costs are costs incurred by the operator to maintain the asset during the service concession period. An example of a lifecycle cost is the cost to periodically resurface a road during the operating and maintenance phase of the service concession arrangement. Do you agree that the examples in the [draft] Standard provide sufficient guidance on the accounting treatment of lifecycle costs of a service concession asset that might be a benefit to the grantor? Why or why not?***

We agree that the examples provide guidance on how to account for lifecycle costs.

However, it will be useful to explain lifecycle costs in the Standard as currently there is no mention of “lifecycle costs” in the Standard.

The example includes a number of assumptions which may not always be present in a SCA. For example, the example assumes there is sufficient certainty regarding the timing and amount of resurfacing work for it to be recognised as a separate component and that the expected cost of the resurfacing can be used to estimate the initial cost of the separate asset. It may be beneficial for the Standard to include guidance on how to estimate or how these costs should be accounted for if the amounts cannot be estimated reliably.

**10) Do you agree with the proposed disclosures for a service concession arrangement set out in paragraphs 30 to 32? Why or why not?**

***In particular, do you agree with the proposed disclosure of paragraph 31 applying individually for each material service concession arrangement or in aggregate for each class of service concession arrangements?***

We agree that a grantor should include the proposed disclosures in its financial statements. However, given this information is already required by Interpretation 129 *Service Concession Arrangement: Disclosures* which applies to both grantors and operators, we do not consider that it is necessary to duplicate the requirements again in the Standard.

**11) In relation to the proposed application date and transitional requirements:**

***(a) Do you agree the proposed application date is appropriate, and if not, what further considerations should be taken into account to determine the application date of the [draft] Standard?***

***(b) Do you agree with the proposed transitional provisions set out in paragraph 33? Why or why not? The transitional provisions permit the grantor to apply the [draft] Standard retrospectively or elect to recognise and measure the service concession asset and liabilities at the beginning of earliest period for which comparative information is presented using deemed cost.***

**a) Application date**

We support a later application date of at least 1 January 2018 as:

- the application date should be consistent with the application of the new revenue standards (AASB 15 and AASB 10XX); and
- it is expected that grantors will have to undertake an extensive process to obtain the required information to comply with the Standard.



b) *Transitional provisions*

We agree with the proposed transitional provisions.

**12) *Whether:***

***(a) There are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, including any GAAP/GFS implications?***

***(b) Overall, the proposals would result in financial statements that would be useful to users?***

***(c) The proposals are in the best interests of the Australian economy?***

a) *Regulatory or other issues affecting the implementation*

The International Monetary Fund (IMF) is in the process of revising the GFS manual. We note that the 2014 Pre-publication Draft Manual issued by the IMF applies a risks and rewards approach to the assessment of SCAs, which is in contrast to the control approach proposed by the ED. Therefore, there should be a formal assessment of the impact of the Standard on GFS when the manual is finalised and incorporated into the Australian Bureau of Statistics (ABS) GFS Manual. This should be one of the areas to be monitored in the post implementation project.

We are not aware of other regulatory issues arising in the Australian environment that may affect the implementation of the proposals.

b) *Result in financial statements useful to the users*

We believe that the Standard would result in useful financial statements as it will provide consistency in the accounting treatment of service concession agreements by operators and grantors which will enhance comparability. In addition, the Standard will ensure that government controlled assets are recognised on the balance sheet.

c) *Best interests of the Australian economy*

For all the reasons noted above, we agree that the proposals are in the best interests of the Australian economy.

**13) *Unless already provided in response to the matters for comment 1 – 12 above, the costs and benefits of the proposals relative to the current Australian Accounting Standards, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.***

Grantors would be able to provide more details about the costs of implementing the Standard.

## **Appendix B**

### **Other matters for the AASB to consider**

#### ***Post implementation project***

We recommend the AASB to undertake a post implementation review project to assess whether the Standard continues to capture the appropriate transactions and whether more guidance should be provided to reduce any divergence in practice post implementation. For example, divergence in practice could result from the subjective interpretation of “public service” as noted in Appendix A.

In addition, when the new Conceptual Framework is finalised, the Board should re-assess whether the control or regulation approach is consistent with the Framework.

#### ***Widening of scope***

We consider that there is merit in further widening the scope of the Standard. Increasingly the public sector is outsourcing the grantor role to Non-Government Organisations (NGOs). To maintain transaction neutrality, the AASB should consider whether the scope of grantors should be widened to include NGOs where they are acting as grantor on behalf of the public sector.

Similarly the same consideration should apply to public-to-public service concession arrangements, that is, whether the standard should be applicable where the operator is a public sector entity.

#### ***Further guidance***

##### ***Identifying the grantor***

In most cases the grantor for the SCA is evident. However there may be instances where the identity of the grantor is not clear. For example the price may be controlled by a Federal price regulator, services are regulated by a State licence and the residual asset may revert to a particular State entity. Guidance on who the grantor would be in these types of circumstances or the factors to consider would be beneficial for assessing which entity should recognise the SCA.

##### ***Constructed/developed assets***

The control criteria for constructed/developed assets requires the additional criteria of being “probable of future economic benefit” and “measured reliably” be met.

The ED notes that the future economic benefits for grantors is the service potential of the service concession asset. However this argument may be inconsistent when applied to a for-profit entity where the primary purpose is viewed as the ability to generate profit and not the provision of service potential. Under this argument, particularly in the grant of right model there may be circumstances where a for-profit entity could assess that there is no future economic benefit relating to the asset.

*Privatised arrangements*

Privatised arrangements are not within the scope of the Standard as it is considered that the grantor does not control the asset. In practice, the differentiation between a privatised arrangement and a SCA is unclear. Defining or providing guidance on the key differences will reduce any potential divergence in accounting.