



Dr Keith Kendall
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Australian Accounting Standards Board
PO Box 204
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AUSTRALIA

23 February 2023

Dear Dr Kendall

AASB Invitation to Comment ITC 49 *Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors*

The Australasian Council of Auditors-General (ACAG) welcomes the opportunity to comment on AASB Invitation to Comment ITC 49 *Post-implementation Review of AASB 1059 Service Concession Arrangements: Grantors*. The views expressed in this submission represent those of all Australian members of ACAG, unless otherwise specified.

ACAG supports the Board's efforts to seek stakeholders' feedback about their implementation experience of AASB 1059.

In this letter, ACAG has raised numerous accounting and application issues, and auditing or assurance issues. The disparity of views and judgements on some areas were not only across the ACAG network but also arose from our audit experience where divergent interpretations were reached by consultants used by our clients. While ACAG has tried to provide a summary of the implementation experience of various jurisdictions, supported by examples where relevant, ACAG offices will be happy to engage directly with the AASB staff, should they need more information on any of the aspects covered in the letter.

ACAG has also included other suggestions and recommendations that we believe will help promote greater consistency and comparability of application across the public sector.

The attachment to this letter addresses the AASB's specific matters for comment outlined in the ITC.

ACAG appreciates the opportunity to comment and trusts you find the attached comments useful.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Margaret Crawford'.

Margaret Crawford
Chair
ACAG Financial Reporting and Accounting Committee

Attachment

AASB Specific Matters for Comment

Topic 1: Public service

Question 1

Do you have comments regarding the application of the following requirements of AASB 1059:

- (a) the use of the term 'public service';
- (b) the operator's involvement in providing public services on behalf of the grantor;
- (c) the operator managing at least some of the public services under its own discretion; and
- (d) the approach to secondary assets?

If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

(a) The use of the term 'public service'As included in AASB 1059

ACAG found determining whether an arrangement provided 'public services' to be a key judgement area, that resulted in significant costs in some cases relative to applying the remainder of the standard. There is currently diversity in whether similar arrangements are classified as service concession arrangements. However, ACAG did not identify any situations where the public service test was not met, yet the other control criteria of AASB 1059 were met for arrangements where the assets were not already on balance sheet. For one jurisdiction, any arrangement (that was not already on-balance sheet) that failed the public services test (or agreed to disagree with client because of the diversity of views), but met the other control criteria, were recognised on-balance sheet under other accounting policies - accounting for PPPs that are not service concession arrangements.

When assessing whether an arrangement provides 'public services' it is not always clear whether the services provided by an asset:

- are necessary or essential to the general public as this is a judgement area and can vary depending on different perspectives and different subsets of the general public
- are generally expected to be provided by a public sector entity in accordance with government policy or regulation as what is generally expected to be provided by the public sector changes over time. For example: ports, ferries, electricity, prisons and detention centres were all government services and we note some of these may now be provided wholly or partially by private sector operators.

The following provides examples of a jurisdiction's reasoning for why particular services are a public service:

Student accommodation

When determining whether student accommodation provides public services as a secondary asset, it was important to first assess whether universities provide public services with their primary assets. Given most universities earn a significant portion of revenue from international students and international students pay significantly higher fees, it was a matter of significant judgement to assess whether universities provide public services. Overall, it was concluded that universities provide public services, because:

- (a) With international education being a key contributor to Australia's exports and Gross Domestic Product, the level of international students' intake and fee-setting are largely matters of government policy for Australian public universities.
- (b) Education (primary, secondary and tertiary) is essential to the public and there would be a general community expectation government provides tertiary education and makes it

accessible to the public even if a sub-set of the community uses those services (AASB 1059.B6).

Therefore, the jurisdiction considered it reasonable to conclude that Australian public universities provide public services (irrespective of the proportion of overseas exports vs local consumption).

Ports

There was significant debate whether only imports should be considered to be providing public services (such as motor vehicles and container cargo) rather than both exports and imports as providing public services.

There was a further discussion on dividing the port activities between imports and exports to determine to what extent ports provide public services. Within the jurisdiction, some had views that exports should not be considered as public services as exports primarily impact private corporations and more broadly the Australian economy.

Overall, the jurisdiction concluded that ports provide public services as:

- (a) these are services that are necessary or essential to the general public and are generally expected to be provided by a public sector entity in accordance with government policy or regulation
- (b) the services would be considered as accessible to the public, 'even if it is a subset of the community that uses the services'
- (c) consumer industries rely heavily on the ports
- (d) goods shipped are ultimately used by the public, and
- (e) these services are also considered as essential services under the *Essential Services Commission Act 2001* (VIC).

ACAG considered whether the requirement for a service concession arrangement to provide a public service should be retained. Refer below to alternatives considered by ACAG. If the public service test is retained, ACAG believes that the AASB should provide more guidance and clarification on what factors should be considered when determining whether an asset or arrangement provides a public service.

Alternatives considered by ACAG

ACAG considered whether the public service test should be retained. The jurisdictions' views varied between:

- Removing the test – based on the view that the test of providing public services is not in the conceptual framework or any other asset recognition standard. Similarly, a comment was made that aren't all services provided by the public sector 'public services'. Another view to support removal is that the other 5 criteria in AASB 1059 in relation to control of the asset are sufficient to determine whether the grantor controls the asset or not.
- Retaining the test – as providing public services is the key feature of public private partnership (PPP) agreements that are meant to be scoped in AASB 1059. Furthermore, the test mirrors the requirements in AASB Interpretation 12 *Service Concession Arrangements*. However, jurisdictions that expressed this view requested additional guidance on what 'public services' means and clarification on what factors should be considered when determining whether an asset or arrangement provides a public service.

ACAG also considered whether the test could be changed to 'providing services to the public'. Similar diverse views to those mentioned above were expressed as to whether this would be effective. Additional views supporting the use of the term 'providing services to the public' considered that the change would assist in assessing outsourcing type arrangements (refer to examples in item (b) below). However, opposing views considered that the term 'providing services to the public' would not differentiate outsourcing arrangements as the ultimate service was provided to the public.

(b) The operator's involvement in providing public services on behalf of the grantorAgency vs Consolidated

It is not clear in AASB 1059 whether a service concession arrangement can be recognised only in an agency's consolidated financial statements, at the sector level (general government sector or public non-financial corporations' sector) or whole of government financial statements. This has led to diverse opinions within ACAG as to whether a service concession arrangement needs to be recognised at an agency level (before it can be recognised at the consolidated level), or whether an arrangement can be recognised only at the consolidated level.

At least one jurisdiction believes that a service concession arrangement must first be recognised at an agency level before being recognised at the consolidated level. On the other hand, at least one other jurisdiction believes that a service concession arrangement can just be recognised at the consolidated level, for example, if the pricing (one of the recognition criteria) was set by Cabinet, and not by the individual agency – consistent with the proceeds being received at whole-of-government, and not by the agency. Further complications have arisen for arrangements that appear in an agency's administered activities, and different arrangements for implementing the Cabinet decision (for example is the agency part of the service concession arrangement with the state, and whether the agency does have ultimate decision making over price changes that need Cabinet approval).

ACAG requests that AASB provide guidance on this topic to reduce any future diversity in applying AASB 1059.

Applying 'on behalf of grantor' concept when multiple agencies are involved in the arrangement

- Identification of grantor:
Some jurisdictions found it difficult to identify the grantor where multiple agencies were involved in the arrangement. The standard refers to 'grantor' however there is very little guidance on what a grantor means when there is more than one public sector entity entering into a contract, that is, more than one public sector entity with different roles and responsibilities. ACAG believes it would be beneficial for the AASB to provide guidance on how to identify a grantor when multiple parties with respective roles and responsibilities are involved.
- Interpreting 'on behalf of the grantor':
Paragraph 2(a) of AASB 1059 refers to an operator 'providing public services related to a service concession asset on behalf of a grantor'. The concept 'on behalf of the grantor' is not currently defined in AASB 1059. ACAG believes additional guidance is required to apply this concept, particularly where multiple parties are involved in a public service or enter into a contract.

This may help reduce interpretation issues between preparers and auditors in applying the requirements.

Two jurisdictions encountered problems when applying the concept of 'on behalf of the grantor'. These primarily relate to situations where the potential grantor did not have the legislative ability to deliver the public service in its own right (that is, it can only contract the service out) or the potential grantor agency may not have the primary responsibility for providing the public service. An example of these has been included below.

Examples encountered by one jurisdiction

In this jurisdiction there are different agencies within the transport sector that have different roles in providing transport services to the public. Some of these transport agencies do not have the legislative ability to deliver the public service in their own right (that is, they can only contract the service out) or the agency may not have the primary responsibility for providing the public service. One or more of these agencies have entered into a service concession arrangement or are involved in a service concession arrangement.

Example 1

A transport asset manager entered into an agreement with a private sector operator to operate and maintain a certain number of stations on the rail network. While the transport asset manager had the legislative ability to deliver the public service in its own right, it was unable to exercise this function due to a restriction placed by the portfolio minister on operating and maintaining train stations. Instead, the operation and maintenance of these train stations was contracted to a private sector operator. Passenger railway services were also provided by a different government agency. The other requirements in AASB 1059 including retaining the residual interest were met by the transport asset manager.

The transport asset manager recognised this arrangement as a service concession arrangement on the basis that operating and maintaining train stations was consistent with its legislative functions and considered a public service (this is notwithstanding the fact it did not have the current ability to exercise that function in its own right, but only contract for the provision of the service due to the restriction placed by the portfolio minister).

Example 2

A coordinating transport entity has the ability to enter into contracts for the provision of a public passenger service, but does not have the legislative ability to provide that transport service directly. Legislation provides that another transport agency (agency A) may conduct these transport services.

The coordinating agency entered into a contract in its own accord with a private sector entity for them to provide public services for specific routes using the operator's own transport assets. The other requirements in AASB 1059 including retaining the residual interest were met by the coordinating agency as the assets reverted to the coordinating agency at the end of the arrangement.

Example 2 contrasts with another arrangement where the coordinating agency contracted with a private sector operator on behalf of agency A above (i.e. as their agent). Agency A held the residual interest and met all of the other conditions for recognising a service concession arrangement. It was agreed that the arrangement should be recognised in the financial statements of agency A.

Application of criteria

While the combined factors (subject to the public services test discussed above) are useful for determining whether to include a service concession asset on-balance sheet – particularly where the private sector has paid for the construction of the asset and the operator is responsible for capital expenditure renewals, the tests are not conclusive in excluding other government arrangements.

One jurisdiction encountered the following government arrangements that have been argued to meet the definition of a service concession arrangement:

- Prisons – constructed by agency and maintained by agency
- Water treatment plant – constructed by agency and maintained by agency
- Social housing – housing constructed by agency and maintained by agency
- Grant for health services using grantor owned buildings
- Land required to be used for public space as part of property development arrangement.

In each of the above, the tests (i) the operator providing public services, (ii) the operator managing at least some of those services under its own discretion, and (iii) the grantor controls or regulates what services the operator must provide, to whom and at what price, were considered to be met (refer Appendix A), even though there was no private sector (or other) involvement in the construction or capital expenditure renewals of the asset. Essentially, no substantive operating provisions of the standard applied (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator) – apart from the mandated use of the cost approach to fair value, and additional disclosures.

However, some other jurisdictions with similar arrangements arrived at the conclusion that such arrangements were not service concession arrangements.

There is diversity in whether already on-balance sheet arrangements, where noted above, no substantive operating provisions of the standard apply are (or should be) accounted for under AASB 1059. Some, but not all, of the above arrangements were classified as service concession arrangements. This may be due to different facts and circumstances and/or different interpretations of the criteria.

Another jurisdiction encountered issues with local government (LG) entities contracting with private sector operators to manage existing LG facilities (such as an aquatic centre, recreational centre or landfill site) for a short period (for example, for 2 years), where the LG entity sets the prices to be charged to users. There was diversity in practice as to whether this was treated as a service concession arrangement or as an outsourcing arrangement.

Treated as a separate line-item class on face of balance sheet

Consistent with the guidance in AASB 1059 paragraph 29, at least one jurisdiction's Treasury department has mandated that service concession arrangement assets be classified as one class and as a separate line item on the face of the balance sheet.

This may lead to the loss of information as assets that would otherwise have been disclosed as land, buildings and infrastructure are classified as a separate class. In particular, service concession assets are not included in the building and infrastructure classes of PPE, even though they are of a similar nature as other PPE infrastructure assets. An example of the consequence of issues raised above is for arrangements that would otherwise have been considered outsourcing arrangements and included in PPE are reclassified as service concession arrangements in a different asset grouping and note to the financial statements.

(c) The operator managing at least some of the public services under its own discretion

Some jurisdictions believe it would be helpful if the AASB provides additional guidance on an operator managing at least some of the public services under its own discretion. The term 'at least some' is open to a significant amount of judgement. The current examples are very black and white on whether maintenance or other services are a significant component of the public service provided by the asset and the operator is responsible for at least some of the management of the public services. For example, while it is clear maintenance is not significant to a school but is significant for a road, it becomes less clear whether maintenance is significant for other public transport assets, such as buses and ferries especially when the grantor manages and sets the timetables.

A jurisdiction considered an operator's role to maintain the buses, trains etc as significant as proper maintenance is necessary for ensuring smooth running of such trains and buses and making sure these are hazard free for the health and safety of commuters.

Some jurisdictions also suggest adding guidance or an example on circumstances where the grantor has a right to / needs to review plans for providing services using the assets and considerations when these rights may be protective or substantive in nature. One jurisdiction has had circumstances where these rights were deemed only protective in nature and others where these rights were substantive, and the arrangement did not fall within the scope of AASB 1059. Example 5(a) of AASB 1059 implementation guidance only refers to protective rights in the context of determining whether services were provided on behalf of the grantor.

Application of criteria

As noted above, there is diversity in whether already on-balance sheet arrangements, where no substantive operating provisions of the standard apply (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator) are (or should be) accounted for under AASB 1059.

(d) The approach to secondary assets

There was considerable confusion, time, effort expended, and diversity in relation to considering secondary assets. These mainly related to student accommodation and hospital car parks.

In some situations, arrangements relating to secondary assets that are similar to toll roads (private sector entity constructs the asset and is responsible for capital expenditure renewals) were classified as service concession arrangements, and some were not.

The following are the problem areas encountered:

- built at a different time
- does the primary asset need to be a service concession asset?
- primary asset owned by a different agency
- largely of a commercial nature.

Built at a different time

AASB 1059 paragraph B7 introduces guidance that if the secondary asset is constructed at a different time to the primary asset, then the secondary asset may not be a service concession asset. The guidance does not explain how a different construction time affects the characteristics of a service concession asset, and the underlying control criteria of AASB 1059.

ACAG requests that the AASB explain how the time period from original construction affects the control criteria of AASB 1059 and explains how long a period it had in mind for the secondary asset to be a service concession asset.

ACAG jurisdictions have encountered various time periods involving toll road type arrangements for car parks being constructed after the initial buildings, varying from a few months to decades.

Does the primary asset need to be a service concession asset?

It is not clear whether the primary asset needs to be a service concession asset.

It is also not clear, in the circumstances that the primary asset is a service concession asset, whether the primary asset needs to be part of the same arrangement as the secondary asset.

ACAG jurisdictions have encountered student accommodation and hospital car parks where the primary asset (university PPE and hospital PPE) was not subject to a service concession arrangement (under AASB 1059) or a public-private partnership.

Primary asset owned by a different agency

It is not clear whether the primary asset needs to be owned or controlled by the same entity that is the grantor of the secondary asset.

Largely of a commercial nature

There is ambiguity in determining the term 'largely' to assess whether an arrangement is of a commercial nature. Jurisdictions considered various factors to determine whether the arrangement is of a largely commercial nature such as:

- (a) the university's / grantor's control in setting prices of student accommodation
- (b) the ability of the operator to let out apartments to the general public when the demand of student accommodation is low from students
- (c) the length of time the operator could let out the apartments (for example, where the apartments were required to be vacated prior to the start of the academic year).

Question 2

Do you have comments regarding the characteristics of an arrangement that would distinguish it as a service concession arrangement from other arrangements such as a privatisation or outsourcing arrangement, or a lease? If so, please provide your views on those characteristics.

Because of the various areas of uncertainty, and diversity in application described above, there were no clear characteristics to distinguish service concession arrangements from other arrangements such as a privatisation or outsourcing arrangement, or a lease in addition to those specified in paragraph IG 12 and IG 13. For example, in some jurisdictions, already on-balance sheet assets were considered to meet the criteria of a service concession arrangement (refer Question 1(b) *The operator's involvement in providing public services on behalf of the grantor* above, and Appendix A).

In another jurisdiction, similar arrangements were determined to be out of scope, because while the operator had the ability to make some decisions, the level of discretion was not sufficient (for example because the services were subject to strict requirements and/or changes had to be approved by the grantor – this was considered more than a protective right).

Possible characteristics that would be relevant to the provisions of the standard (GORTO liability and financial liability) are when the grantor pays the operator to construct the asset (or the operator constructs the asset for future user charges) and/or the operator is responsible for capital expenditure replacement.

Topic 2: Grantor's control of the asset**Question 3**

Do you have comments regarding the application of the following requirements in AASB 1059 paragraph 5:

- (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 any significant residual interest in the asset at the end of the term of the arrangement?

If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

(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

Similar to Question 1(b), while the factors (apart from partly regulated assets) are useful for including a service concession asset on-balance sheet – particularly where the private sector has paid for the construction of the asset and/or the operator is responsible for capital expenditure renewals, the tests could be clearer in clarifying whether already on-balance sheet arrangements should be classified as service concession arrangements or outsourcing type arrangements.

Also similar to the response to Question 1(b) *The operator's involvement in providing public services on behalf of the grantor* above, and the analysis in Appendix A, there was diversity in the classification of already on-balance sheet arrangements as service concession arrangements.

Partly Regulated Asset

There were different views as to what 'enough of the service is regulated' (AASB 1059 paragraph B26) means, and consequently what level of regulation is sufficient for classification as a service concession arrangement. There is a lack of reference in the standard to what quantum 'enough' represents. One suggestion was to refer to the term 'significant', although that was acknowledged as having interpretation difficulties as well.

There were also different views as to how to assess whether 'enough of the service is regulated'. In particular, could enough of services be judged from the quantum of revenue generated from regulated and unregulated services, or whether it would be considered as one of the indicators that needed to be assessed with other factors of the arrangement. In this regard, there were also different views as to how to assess the amount of revenue. For example, revenue can vary from one year to another – so which year's revenue should be considered for assessing whether enough of services are regulated?

Controls the price

One jurisdiction suggested that the AASB clarify that an available Government subsidy (for example, aged care subsidy) does not result in the grantor (or a regulator) controlling the price, because the operator is still able to determine the price charged to customers.

(b) Residual Interest

Jurisdictions encountered practical issues in applying the residual interest test, with different approaches taken. Issues included:

- what rough quantitative % does 'significant' represent?
- assessing how remaining economic life was considered compared to relative fair values
- how to assess residual interest when replacements and lifecycle assets are included
- the criticality of the asset to the entity in delivering its objectives.

Often, the residual interest test is met, as the asset is on the grantor's land, and at the end of the arrangement, the grantor gains legal ownership and/or beneficial entitlement and so on, to whatever service concession asset remains on that land. Also, often it is an operating asset (for example, a toll road that has to meet a specific performance standard) and consequently will have a significant residual value. However, sometimes the residual interest is on the operator's land. In such circumstances, it is more important to determine how the residual interest is calculated in order to assess whether there is "significant residual interest in the asset at the end of the term of the arrangement".

AASB 1059 paragraph B35 appears contradictory. In the first part, it treats replacements and lifecycle costs as part of the asset. However, in the second part, it treats replacements and lifecycle costs as separate assets. Therefore, when assessing the estimated value of the asset (on arrangement expiry), is it the fair value of the original asset (of which major components will no longer exist), or will the fair value include the expiry value of the replaced components?

When assessing what level 'significant' represents, should reference be made to the 20% threshold under equity accounting, or the 20-30% some applied under the former IAS 39 / AASB 139 available for sale impairment testing, or did the AASB have another view of what quantitative level 'significant' should be? A dictionary definition of 'significant' is 'sufficiently great or important to be worthy of attention; noteworthy'.

ACAG suggests that the AASB provide additional guidance on the effect of common contractual alternatives at the end of the concession period including:

- the grantor acquires the assets – at a set operating performance standard (for example, a working toll road) for nil consideration
- the grantor acquires the assets – at a set operating performance standard for fair value consideration
- the operator is granted a second concession term
- a new operator is allowed to acquire the assets.

ACAG suggests the AASB include additional guidance when the grantor has the option to acquire the assets at fair value. For example, it can be argued that the grantor still controls the residual interest, as the operator cannot control the infrastructure until the grantor has decided what to do with the option.

Question 4

An arrangement is within the scope of AASB 1059 for recognition as a service concession arrangement if all of the following conditions are satisfied:

- (a) the operator provides public services related to a service concession asset on behalf of the grantor;
- (b) the operator manages at least some of the public services under its own discretion;
- (c) 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
- (d) the grantor controls any significant residual interest in the asset at the end of the term of the arrangement. This includes the grantor having substantive rights to prevent the operator from selling or pledging the asset during the service concession arrangement.

Do you consider it appropriate for an arrangement to be accounted for under AASB 1059 only when all of the above conditions are satisfied? Please provide reasons to support your view.

As discussed above, there is diversity in how service concession arrangements are assessed. In some situations, arrangements similar to toll roads (private sector entity constructs the asset and is responsible for capital expenditure renewals) were classified as service concession arrangements, and some were not, for example the arrangements with secondary assets discussed above.

Also, as noted in question 1(b) some arrangements where all the above tests were considered met were classified as service concession arrangements, even though there was no private sector (or other) involvement in the construction and/or capital expenditure renewals of the asset and essentially, no substantive operating provisions of the standard applied (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator). ACAG requests additional implementation guidance and illustrative examples to clarify this issue.

Consequently, some ACAG jurisdictions do not consider it appropriate for an arrangement to be accounted for under AASB 1059 only when all of the above conditions are satisfied as the above criteria (based on current guidance) are not sufficiently discriminatory to result in consistent conclusions on whether certain arrangements should be classified as service concession arrangements. As noted above, there was a diversity of views within ACAG jurisdictions on the retention of the 'public services' test or a revision of that test. Some ACAG Jurisdictions support the use of the above conditions if guidance can be strengthened to ensure a more consistent classification of like arrangements.

ACAG believes the guidance needs to be strengthened to ensure a more consistent classification of like arrangements, that is, service concession arrangements or outsourcing arrangements. We discussed above suggestions to improve the requirements, including different views on whether the 'public services' test should be retained.

Question 5

In addition to the conditions in AASB 1059 paragraphs 2 and 5 (as set out in Question 4), are there other factors that you consider would assist in determining whether an arrangement is within the scope of AASB 1059? If so, please provide details of those factors and explain why you think they would be useful.

AASB 1059 is broadly the mirror accounting for AASB Interpretation 12 *Service Concession Arrangements*. Interpretation 12 was very helpful in determining whether infrastructure assets (plant and equipment) paid for and maintained by the private sector operator should be recognised as an asset of the operator, when under the arrangements the PPE was controlled by the grantor. Using a control-based approach, rather than a risks and rewards-based approach, also caused changes to the existing treatment.

Applying those concepts from the grantor perspective has meant that toll roads have been recognised on-balance sheet. However, as noted above, there has been diversity in treatment of similar arrangements for student accommodation and hospital car parking.

Some jurisdictions believe there appears little purpose in classifying an already on-balance sheet arrangement as a service concession arrangement. For these arrangements, none of the substantive operating provisions of AASB 1059 apply (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator), and yet requirements such as mandated cost approach fair valuation and disclosures apply.

Topic 3: Public sector operator

Question 6

Do you have comments regarding a public sector entity applying AASB 1059 as the grantor when the operator is another public sector entity? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting. If you propose excluding public-to-public arrangements from the scope of AASB 1059, what is the rationale for your view?

Most of the issues in relation to public sector grantor and public sector operator arrangements was determining whether the arrangement was a service concession arrangement or an outsourcing arrangement (refer to difficulties and application issues discussed above in Topic 1 and Topic 2).

The discussion in question 1(b) (regarding whether the service concession arrangement should be recognised in an agency's financial statements or only at the consolidated level) becomes more relevant when the arrangement is between two public sector entities. In this regard, some jurisdictions believe that the cost of undertaking service concession assessment and accounting may exceed the benefit if the arrangement is between two public sector entities as the arrangement gets eliminated at the consolidated level. Furthermore, there are not many instances of public-to-public service concession arrangements. Therefore, the AASB could consider scoping out public-to-public service concession arrangements by clarifying the definition of operator and amending AASB1059.BC129.

However, before AASB grants such an exemption:

- it will be important to understand the AASB's rationale for scoping in such arrangements in the standard in the first place and taking a different approach to AASB Interpretation 12 that only deals with public to private service concession arrangements
- a proper impact assessment will need to be conducted as some arrangements are between two public sector entities but in different sectors (that is, one public sector entity is in GGS and the other in the PNFC sector). Therefore, scoping out arrangements could mean an impact on the balance sheets of such sectors.

Another important point which we recommend the AASB to clarify is the interaction of AASB 1059 with AASB 10 (which is most relevant in case of public-to-public service concession arrangements). Generally, if the operator is controlled by the grantor under AASB 10, it will be difficult to meet the criteria 'whether the operator has discretion in managing some of the public services' because if any action of the operator is subject to the approval of the operator's Board and the operator's Board is controlled by the grantor, then AASB 10 will overrule AASB 1059.

One jurisdiction previously had a toll road operated by a public sector subsidiary, with the PPE of the roads accounted for on-balance sheet of the operator. This arrangement has now ceased.

Topic 4: Recognition and measurement of service concession assets and related liabilities

Topic 4A: Recognition and measurement of service concession assets

Question 7

Do you have any comments regarding:

- (a) initially measuring a service concession asset at its current replacement cost using the cost approach in AASB 13; and
- (b) subsequently measuring the service concession asset at current replacement cost under the revaluation model in AASB 116 or AASB 138 (if the revaluation model is adopted by the entity)?

Where you do have comments on (a) and/or (b), please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Mandating the (replacement) cost model

ACAG believes that the mandated measurement at current replacement cost (CRC) should be reconsidered, and preferably removed, as it is an unnecessary modification to IFRS.

The majority of ACAG jurisdictions also disagree with the resultant accounting especially in case of an internally generated intangible asset recognised at nil, then revalued to millions of dollars (even though it is still controlled by the grantor), and then at the end of the service concession arrangement, it retains this revalued amount.

There should be less need for this requirement (based on the perception that some people previously interpreted AASB 13 as requiring a discounted cash flow approach for an asset held for its service potential) given the changes to AASB 13 by AASB 2022-10 *Amendments to Australian Accounting Standards – Fair Value Measurement of Non-Financial Assets of Not-for-Profit Public Sector Entities*.

The valuation of land registries using CRC has proved particularly challenging, specifically related to:

- what is the unit of account (the database or a record)?
- how new records should be treated (as a revaluation adjustment or asset addition)?
- to the extent the new record is an addition, how should they be accounted for? Also, how does the addition of new records to the database that increases the service concession asset value interact with the argument that the overall cash generating ability of the database has not changed and arguments that the land registry has an indefinite useful life?
- the anomalous situation (caused by being heavily reliant on the entity's own information about the costs of processing) that an inefficient approach, reliant on manual records and processing, results in a higher valuation than that of a more efficient approach assuming that the valuation is based on replacing the records in their current form in the current system.

The majority of ACAG jurisdictions believe that because of the high degree of estimation uncertainty, the valuation borders on not being relevant or reliable. Those who have revalued have disclosed the basis for that valuation given the degree of assumptions involved. For example, [Attorney-General's Department.pdf \(audit.sa.gov.au\) Note 5.2](#). Another jurisdiction did not recognise this intangible service concession asset on the basis that the valuation could not be measured reliably.

The majority of ACAG jurisdictions do not consider the resulting information useful to users. Although acknowledging the valuation challenges, one jurisdiction considers the resulting information useful to users have considered the value it provides to the private sector who are willing to pay money for it.

Mandating the (replacement) cost model – construction work in progress

The examples are confusing in relation to revaluation of service concession assets under construction. The examples seem to indicate that the service concession asset is revalued to (replacement) cost even when not yet in use. Some jurisdictions ordinarily require the (historical) cost model to be used for PPE under construction.

Mandating a revaluation on change in use

ACAG believes that the mandated revaluation of service concession assets on change of use from non-service concession assets to service concession assets should be reconsidered, and preferably removed, as it is an unnecessary modification to IFRSs.

The main practical issue for this is the land registries – if an agency controlled the registry before the service concession arrangement, and controls it after the service concession arrangement commences, why does the AASB force a revaluation (especially of intangibles) not otherwise permitted by the standards?

No other standards require a forced revaluation for a change in use (unless after the change in use fair value is the new measurement model – for example, PPE to investment property at fair value).

Question 8

Do you have any comments regarding the recognition and measurement of a service concession asset under construction? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

ACAG believes that the AASB should provide clear guidance on how the progressive recognition of an asset during construction should be recorded, that is, at cost or fair value as the current guidance provided in AASB 1059, particularly examples 6, 7 and 8 is causing confusion. Two jurisdictions have adopted an interest accretion approach to determine a fair value uplift in order to continue to recognise assets under construction at fair value. The interest accrual on the financial liability from the State to the operator is used as a proxy for the increase in the value of work-in-progress (WIP) during the construction period.

A majority of ACAG jurisdictions believe that service concession assets under construction should not be mandated to be valued at fair value. This view relates both to the issues in the above response to Question 7 and to the objection of including borrowing / funding costs (refer to response below to Question 9).

One jurisdiction supports the fair value model during construction. This is because if the asset is not carried at fair value under-construction, entities will have an adjustment when the asset is reclassified from WIP and gets recognised as service concession assets.

Question 9

Do you have any comments regarding the calculation and treatment of borrowing costs or implied funding costs in measuring the current replacement cost of a service concession asset? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Illustrative examples 6, 7 and 8 include implied funding costs in the current replacement cost of the road (paragraphs IE18, IE 24 and IE34(a) and (c)), however there is no guidance or mention in the standard itself on implied funding costs. As these implementation examples only accompany, but do not form part of the standard it is not clear whether these implied funding costs need to be included in the current replacement cost of an asset when construction occurs over more than one year. It is also not clear what the purpose is of including the implied funding costs in the CRC. For example, is the purpose of implied funding costs to include borrowing costs while the asset is being constructed or an uplift on WIP assets in order to continue to recognise these at CRC? If the purpose is for WIP assets

to be valued at CRC then borrowing costs alone in a high inflationary environment will not necessarily result in the asset being recorded at its fair value and other indexation may be required.

If the AASB requires implied funding costs to be included in the CRC of a service concession asset under construction, then ACAG believes it is important for the AASB to add guidance on the purpose of implied funding costs and the circumstances when these costs should be included in the CRC of a service concession asset to ensure the requirements are consistently applied. ACAG notes that providing guidance would be inconsistent with the AASB's decision not to provide guidance on borrowing costs in the recent AASB 2022-10 amendments to AASB 13.

As noted above, the examples appear to revalue the service concession assets under construction and not yet in use. Some jurisdictions ordinarily require the (historical) cost model to be used for PPE under construction.

ACAG also has specific concerns with the examples that we have detailed below. ACAG therefore believes illustrative examples 6, 7 and 8 of AASB 1059 need to be revisited and revised.

Example 6

The example is confusing. For example, paragraph IE17 states “the asset is recognised as it is constructed (CU525 in year 1 and CU557 in year 2).” However, this does not appear to be aligned with the underlying accounting we expect in the example (and which is illustrated in Table 6.2) which is:

Dr	Asset	525	
Cr	Financial liability		525

Year 1 construction of the asset

Dr	Asset	525	
Cr	Financial liability		525

Year 2 construction of the asset

Dr	Finance expense	32	
Cr	Financial liability		32

Finance expense of 6.18% on financial liability of 525

Dr	Asset	32	
Cr	Asset revaluation reserve		32

Increase in fair value (current replacement cost) of the asset

This example is also confusing as the increase in the fair value (current replacement cost) uses the borrowing costs of the operator, and not the borrowing costs of the grantor or an assessment of the borrowing costs of a (usually non-existent) hypothetical market participant.

Example 7

This example is confusing and appears incorrect in its underlying reasoning. The example (paragraph IE24) includes an implied funding cost as part of the cost of the asset acquisition – being the second year of construction of the asset. No funding cost is included in the acquisition / construction of the asset in Year 1, or for the replacement surface layer in Year 8.

There is no indication that there is some sort of deferred payment or implied financing of the construction of the road in Year 2. The GORTO liability is broadly unearned revenue and not a financial liability, so including a financing expense for unearned revenue appears incorrect. Therefore, inclusion of an implied funding cost in Year 2 appears incorrect and should be removed.

Also, the treatment of the carrying value under fair value current replacement cost is not clear. Paragraph IE23 includes a cost of Year 2 of 557. In reality, it is a cost of 525. There is an additional 32 for the implied funding cost that is not part of the cost of the asset. Instead, it appears that there is an increase in current replacement cost of 32 – but no increase in the asset revaluation reserve. This accounting treatment is different from example 6, where the increase in fair value has been recognised in the asset revaluation reserve rather than in the financial liability.

Similar to our comments on Example 6 above, ACAG questions the use of the operator's funding costs in a current replacement cost valuation.

Example 8

This example should be updated for the above comments. The accounting treatment of the uplift in example 8 for a hybrid arrangement only applies the principles for the financial liability in example 6. It is not clear why different methods have been used for the financial liability and GORTO methods or why in the case of a hybrid arrangement the implied funding has not been calculated using the principles in both examples 6 and 7.

Question 10

Do you have any comments regarding the recognition and measurement of upgrades or replacement of major components of a service concession asset? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Upgrades

AASB 1059.B38 and B48 requires the grantor to recognise an upgrade (for example, an increase in capacity) or the replacement of a major component of an asset as a service concession asset and a corresponding liability, when the upgrade or replacement occurs, whereas paragraph B59 states that after initial recognition, a grantor applies AASB 116 or AASB 138 to subsequent costs incurred. It is currently unclear how minor capital additions to a service concession asset that are not an upgrade or major replacement should be accounted for e.g. should these be treated as lifecycle costs. The section below contains more details on lifecycle payments.

Paragraph IE7 is causing confusion, as it does not adequately explain how to account for upgrades. The paragraph's wording "then it would be appropriate to instead recognise revenue relevant to that improvement only once it has occurred" can be interpreted as meaning that revenue can be recognised immediately once the improvement upgrade has been completed. However, would this not be an upgrade captured by B48 and therefore require recognition of a corresponding liability? The inclusion of a new lane is not actually included in the implementation examples, and it is therefore difficult to understand the AASB's intent.

Lifecycle payments

Many service concession arrangements relating to the operator constructing the underlying asset also have provisions for the operator to maintain the underlying asset to a particular performance standard (for example toll roads). Arrangements involving the operator constructing an asset, that may not be considered as a service concession arrangement and were accounted for as a purchase, have similar arrangements for the operator to maintain the asset at a particular performance standard (e.g. school buildings). These payments relate to capital expenditure replacements, and are considered separate to ongoing facility maintenance payments.

Lifecycle payments might include categories such as building substructures, columns, roof, windows, doors, floor finishes, fitments, plumbing, mechanical services, fire protection, electric light and power, communications and hydraulics.

There is diversity in how lifecycle payments are accounted for, with the accounting treatment often being dependent upon the availability of information provided by the operator to the grantor. If the information is not available, the payments are generally expensed. In other instances, the replacements are accounted for similarly to capital expenditure replacements under AASB 116 as they can be tracked because monitoring of the asset management plan is sufficiently detailed, and/or there is cost sharing / gain sharing over set thresholds (that is, someone is monitoring the payments and what is being purchased).

A further complicating factor is that sometimes the lifecycle payments are paid based on expected timing and amounts (with the consequence that payments are lumpy), and sometimes they are 'straight-lined'. If the payments are 'straight-lined' (that is, having a consistent lifecycle payment in the quarterly service cash payment), then there is an element of a prepayment.

The operator effectively takes on the risk (including potential benefits) associated with the timing and quantum of lifecycle costs. There may be no contractual requirement for the operator to spend predetermined lifecycle payments on specific assets at a specific point in time. Further, there may not be any contractual obligation to substantiate actual expenditure incurred by the operator to the grantor. However, the lifecycle payments are based on an expected level of service from the assets – that is, if the underlying assets deteriorate earlier than expected, the operator is required to replace the assets without additional payment from the grantor.

Because of the diversity in accounting for lifecycle payments, ACAG requests the AASB to provide further guidance on the issue. As noted above, this issue also applies to arrangements that are not classified as service concessions.

Intangible assets – Land registries

There is a diversity of views in how to account for record 'additions' to the land registry databases. As noted above, there are related issues for the valuation of these databases. The divergence is in part due to differences in interpretation about what is actually providing the service potential of the asset, and what is the unit of account.

One argument is that new records should be accounted for as part of the overall revaluation of the asset. This is premised on the argument that the additional records would not seem to be 'upgrades or replacements' of major components of service concession assets and therefore those paragraphs of AASB 1059 which would require these to be treated as new service concession assets do not apply.

Under this argument, the requirements of AASB 138 should be applied. Broadly, if the database was accounted for as an owned asset, subsequent expenditure would not meet the capitalisation criteria (similar to other internally generated intangible assets like customer lists).

Further, this argument is based on a view that the service potential of the data assets is embodied in the state's statutory obligation to provide land titling and administrative services to the public and therefore is it those services as a whole that represent the service potential, not the number of records in the database. Rather, the entry of new records maintains the service potential of the asset.

The alternate view is that as components of the database, new records have service potential that increase the value of the land registry database (noting that for not-for-profit entities, future economic benefits are synonymous with the notion of service potential). Without these new records, the land registry database would not be current and complete. Therefore, new records increase the value of the service concession asset and the GORTO liability (paragraph 11).

Question 11

Do you have any comments regarding how contract modifications should be accounted for under AASB 1059? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Service concession arrangements are often subject to numerous changes from the Base Case Financial Model, for example differences between actual and expected CPI. However, these modifications are dealt with within the agreement.

The following were examples of some of the modifications encountered by jurisdictions that involved amendments to agreements (some details slightly changed for explanatory purposes):

Hospital Car Park lease:

- Commenced 1999, original term 20 years.
- Amended 2005 to include expansion for additional floors. Original term extended 6 years (so remaining term is 20 years from amendment date).

Toll road

- Initial agreement for Toll Road A, original term 40 years (from 1996 – completion 2000) (terminating 2034).
- Expansion of Toll Road A (additional lanes) – Concession was increased by one year, minimum toll increase of 4.5% retained for an additional year (that affects all future tolls) and truck tolls increases.
- Additional agreement for Toll Road B – Construction commenced in 2018 (still under construction). Consideration by operator was for tolls on this Toll Road B until 2045 and for an extension of the Toll Road A concession (as expanded) for another 10 years (terminating in 2045) and a higher annual minimum toll increase.

Difficulty was encountered with the toll road example particularly in relation to the amortisation of the GORTO liability and revenue recognition (refer Question 16).

In NSW, there have been various contract modifications to toll road arrangements prior to implementation of AASB 1059. For information on these, the AASB can refer to note 14 of Transport for NSW's publicly available financial statements.

Modifications to existing service concession arrangements are likely in the future. The AASB should consider the above examples in providing guidance on contract modifications.

Question 12

Are there any other comments regarding the AASB 1059 recognition and measurement requirements for service concession assets that you think the AASB should consider?

The Queensland Audit Office, in March 2017, advised the AASB of issues relating to variable consideration for service concession arrangements in its response to *AASB 10XY Service Concession Arrangements: Grantors – Fatal-Flaw Review*.

https://www.aasb.gov.au/admin/file/content106/c2/QAO%20Response%20-%20Fatal%20Flaw%20Review%20-%20AASB10XY%20SCA%20for%20Grantors_24-03-2017_153439.pdf

While there are no further variable consideration payments for the identified arrangement, the accounting for such payments has not been resolved for future service concession arrangements.

Topic 4B: Recognition and measurement of liabilities in service concession arrangements

Question 13

Do you have comments regarding the application of the requirements in paragraphs 11 and 12 of AASB 1059 to initially measure the liability at the same amount as the service concession asset, subject to certain adjustments? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

The statement 'initially measure the liability at the same amount as the service concession asset' is causing confusion, as there are potential differences in the accounting for the service concession asset and related liability (financial liability and/or GORTO liability) at the different times of asset construction, during construction of the asset and at construction completion.

ACAG has highlighted above under Question 9 issues related to:

- Example 6 (financial liability) where the service concession asset and liability appear to be the same during the construction period as we have concerns as to why and how that was achieved.
- Example 7 (GORTO liability) where we have highlighted that the example appears incorrect by capitalising a financing cost on unearned revenue – that results in the service concession asset and liability appearing to be the same on completion.

In these examples, it is not clear whether the asset is the same as the service concession liability during construction because it is required, or it is the impact of recognising interest accretion using different methods i.e. through revaluation surplus (under the financial liability model and hybrid models example 6 and 8) and as an addition to the unearned revenue liability (under the GORTO model in example 7) or just a coincidence.

To ensure that the standard is being applied consistently, ACAG suggests the AASB clarify whether a liability needs to be measured at the same amount as the service concession asset as the asset is being constructed, on completion or both.

Question 14

In addition, do you have comments regarding the application of AASB 1059 requirements to initially recognise a partly completed service concession asset (or asset under construction) and associated liabilities? If so, please provide your views on those requirements, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Jurisdictions have also had difficulties in certain instances when validating costs related to service concession assets under construction as:

- details provided by the operator are not detailed enough
- there is difficulty validating the costs provided by the operator when the grantor is not necessarily approving the invoices for costs incurred during construction by the operator
- there is difficulty in segregating values of plant and equipment and land and buildings at the WIP stage.

Further, current replacement cost (fair value) is expected to include amounts such as share of overheads, profit margin on the construction amount etc. (per IVS 105). It is difficult for an auditor to obtain assurance over these amounts as these will not be included in invoices.

Question 15

Do you have comments regarding the subsequent measurement requirements for financial liabilities? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Issues related to variable consideration raised previously by the Queensland Audit Office are included above under Question 12.

One jurisdiction encountered a divergent interpretation in applying the standard for an otherwise GORTO arrangement (operator takes risk for volume), but there were potential minimum guarantee payments, where the grantor pays any shortfall between the amounts received by the operator from users and the contracted minimum consideration for the operator. The divergent interpretation was that the entity recognised a GORTO liability (equal to the service concession asset constructed), plus a provision for the grantor's best estimate of the expected shortfalls. However, the Audit Office in that jurisdiction enforced the view that the entity should instead recognise:

- a gross financial liability for the present value of the minimum guaranteed amounts over the term of the arrangement using the contractually specified interest rate;
- a GORTO liability for the difference between the service concession asset and the financial liability (thus resulting in a hybrid arrangement); and
- the revenue received from the users.

Question 16

Do you have comments regarding the initial and subsequent measurement, including amortisation, of GORTO liabilities? If so, please provide your views, relevant circumstances and their significance. In your response, please also explain the accounting adopted or proposed and the reasons for that accounting.

Question 11 includes an example from one jurisdiction where an operator manages multiple service concession projects for the grantor and the operator's right to charge tolls are intertwined amongst various projects. In that example, the grantor entered into a GORTO arrangement with the operator to construct Toll Road B, and as part of the consideration the operator was able to charge tolls on Toll Road B, and was also given the right to charge tolls on Toll Road A for an additional 10 years (after the original termination of the Toll Road A agreement) and the operator was given a higher annual minimum toll increase for Toll Road A.

The provisions in AASB 1059 on the amortisation of the GORTO liability caused confusion. AASB 1059 paragraph 22 states that the grantor shall reduce the GORTO liability and recognise revenue according to the economic substance of the arrangement.

On one hand AASB1059 paragraph B71 states revenue is usually recognised as access to 'the service concession asset' is provided to the operator over the term of the service concession arrangement. In most cases, access to the subject service concession asset is uniformly provided to the operator over the term of the arrangement (as the arrangement involves one asset). Similarly, from a grantor's perspective it has received the service concession asset 'free of charge' uniformly over the agreement period. Therefore, revenue should be recognised on a straight-line basis. Furthermore, Toll Road B is available for use by toll users equally over the service concession period, therefore the straight-line method is justified.

On the other hand, for GORTO arrangements, the grantor recognises a liability 'for granting the operator the right to collect tolls' (AASB 1059 paragraph IE24). Therefore, if the right to collect tolls is not uniform over the term of the arrangement as in the example above, it can be argued that the GORTO liability should not be amortised on a straight-line basis. In this example, the receipt of tolls by the operator is back-ended in the later years (the extension of the tolling arrangement on Toll Road A from 2035 to 2045). AASB 1059 paragraphs BC78 to BC80 states that the liability is analogous to a contract liability under AASB 15 that should represent remaining performance obligations under the contract at any time. Therefore, if the grantor has granted the right to the

operator to charge tolls on multiple arrangements as a consideration for the service concession arrangement (which could be considered as a performance obligation), then the GORTO liability should not be amortised on a straight-line method basis.

Therefore, based on the above, it is not clear which notion should be followed i.e. having uniform access to the service concession asset (asset side notion) or granting right to the operator to charge toll revenues (liability side notion) which may not be uniform.

Question 17

Are there any other comments regarding the AASB 1059 recognition and measurement requirements for liabilities of a service concession arrangement that you think the AASB should consider?
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No additional items identified.

Topic 5: Other matters

Question 18

Do you have any comments regarding the disclosure requirements in AASB 1059 (paragraphs 28 and 29), which cover both qualitative and quantitative information about a grantor's service concession arrangements? If so, please provide your views on those requirements and their significance.

Treated as a separate line-item class on face of balance sheet

As noted above under Question 1(b), at least one jurisdiction's Treasury department has mandated that service concession arrangement assets be disclosed as a separate line item on the face of the balance sheet, even though the assets are a similar nature as other PPE infrastructure assets. We noted that this may lead to the loss of information as assets that would otherwise have been disclosed as land, buildings and infrastructure are classified as a different asset grouping and note to the financial statements.

Question 19

Do you have any comments regarding the Implementation Guidance and Illustrative Examples that accompany AASB 1059? If so, please provide your views and any suggested amendments.

The illustrative examples appear simplistic. Based on the comments provided in the sections above and areas highlighted, we recommend the AASB to include more guidance and illustrative examples for achieving consistent application of the standard. Following are ACAG's specific comments on some examples:

Previous comments on examples

ACAG has highlighted above under Question 9 issues related to Examples 6 (financial liability), 7 (GORTO liability) and 8 (combination).

Borrowing costs

ACAG believes that given the AASB's decision not to provide guidance on the treatment of borrowing costs for fair value under the modifications to AASB 13 by AASB 2022-10, the AASB should be consistent with that decision and not provide guidance in AASB 1059. This would require amendments to examples 6, 7 and 8 on the inclusion of implied funding costs.

Already on-balance sheet assets

As noted above, (in particular Questions 1 and 4) there is diversity in whether already on-balance sheet arrangements, where no substantive operating provisions of the standard apply (that is, no recognition of an asset supplied by the operator, no liability of the grantor for an asset supplied by the operator, and no income recognised in relation to an asset supplied by the operator) are (or should be) accounted for under AASB 1059.

ACAG requests additional implementation guidance and illustrative examples to clarify, and if necessary, revise the criteria, so that the AASB 1059 criteria are suitably discriminatory.

Land under service concession assets

One jurisdiction suggested that the AASB should clarify in the Implementation Guidance and the Illustrative Examples that the existing land owned by the grantor on which a service concession asset is constructed by the operator should also be reclassified by the grantor as a service concession asset.

Question 20

Are there any other matters that the AASB should consider as part of this PIR? If so, please explain those matters and why they should be considered, and provide examples to illustrate your response. For example, in your view are there new or emerging arrangements for which it is difficult to determine whether they are within the scope of AASB 1059 or for which service concession accounting might not be suitable? .

As discussed above under Question 10, there is diversity in how lifecycle payments are accounted for.

The diversity relates to service concession arrangements, and arrangements that fail the AASB 1059 criteria (for example public-private partnerships where the construction of the asset is considered a purchase).

AASB General Matters for Comment

Question 21

Does the application of AASB 1059 adversely affect any regulatory requirements for grantors?

One jurisdiction noted that a local government's statutory reporting ratios were affected by AASB 1059 – this being the only local government with material service concession arrangements, that were not already on-balance sheet.

Question 22

Does the application of AASB 1059 result in major auditing or assurance challenges?

Yes, the major auditing or assurance challenges include those areas where there is significant amount of judgement and those where there is a lack of guidance. Those that have been discussed above include:

- determining whether an asset provides public services (Question 1)
- applying the term 'on behalf of the grantor' (Question 1)
- applying the term 'on behalf of the grantor' when the agency may not have the primary responsibility for providing the public service (Question 1)
- whether an arrangement can be accounted for as a service concession arrangement at a consolidated whole of government level, when this has not been accounted for as a service concession arrangement at the individual agency level (Question 1)
- determining whether the operator provides at least some of the management of the public service at its own discretion (Question 1)

- whether a secondary asset provides public services, particularly when it was constructed after the initial asset (which may or may not have itself been the subject of a service concession arrangement) (Question 1)
- whether a service concession arrangement granted over a secondary asset can be within the scope of AASB 1059 where the primary asset is controlled by a different public sector entity (Question 1)
- partly-regulated assets (Question 3)
- residual interest (Question 3)
- diversity in applying the control criteria (Question 4)
- valuing land registries using current replacement cost – note this will be an on-going issue for these arrangements and involve additional costs every year (Question 7)
- applying the concept of implied funding costs (Question 9)
- lifecycle payments (Question 10)
- variable consideration (Question 12)
- accounting for assets under construction (Question 14)
- minimum guarantee payments (Question 15)
- upgrades, including linking to other service concession assets (Question 16).

Question 23

Overall, does AASB 1059 result in financial statements that are more useful to users of public sector grantors' financial statements?

ACAG generally agrees that putting on-balance sheet arrangements that the grantor controls makes public sector grantors' financial statements more useful.

As noted above, there is less agreement amongst ACAG offices about the treatment of already on-balance sheet arrangements, and as noted above, whether these are actually service concession arrangements – particularly if the operator is not involved in construction or capital expenditure renewal. It is also noted that such already on-balance sheet arrangements are often encountered in local government short-term management arrangements with the private sector.

Also as noted above, ACAG believes that there is scope to increase the consistency in accounting for service concession arrangements by providing additional guidance in the key areas we have mentioned.

As noted above under Question 7, ACAG believes that the following AASB 1059 provisions should be reconsidered, and preferably removed, as there are an unnecessary modification to IFRSs:

- the mandated revaluation of service concession assets on change of use from not being used as service concession assets to being used as service concession assets
- the mandated use of CRC.

The majority of ACAG jurisdictions believe that revaluing land registries (which would not otherwise be recognised under AASB 138) does not provide useful information.

Question 24

In your view, do the benefits of applying the requirements of AASB 1059 exceed the implementation and ongoing application costs?
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ACAG is not able to comment generally on the costs and benefits of the proposals.

However, the majority of ACAG jurisdictions believes that the valuation and audit of the valuation of previously unrecognised intangible assets (in particular, land registries) has resulted in the costs exceeding the benefits.

ACAG believes that if the AASB clarifies the issues above, and provides more guidance where relevant, this will reduce the costs of applying AASB 1059.

Appendix A – On-Balance sheet arrangements

The following are examples provided by one jurisdiction in applying the service concession criteria to already on-balance sheet arrangements, and where the substantive provisions of the standard did not apply (i.e. there was no GORTO liability, and no financial liability). Some, but not all, of the arrangements were classified as service concession arrangements.

- Prisons – Constructed by agency and maintained by agency
- Water treatment plant – Constructed by agency and maintained by agency
- Social housing – Housing constructed by agency and maintained by agency
- Grant for health services using grantor owned buildings
- Land required to be used for public space as part of property development arrangement

Prisons – Constructed by agency and maintained by agency	
AASB 1059 criteria	Analysis
Operator providing public services	Yes – Prisons are managed by the public sector
Operator managing at least some of those services under its own discretion	Yes – Operator has discretion in how prisoners and prisons are managed, and are subject to key performance indicators
Grantor controls or regulates what services the operator must provide	Yes – Operator must provide prison and prisoner services
Grantor controls to whom the operator must provide services	Yes – Operator must provide services to prisoners as determined (by the courts) and the grantor
Grantor controls what prices the operator charges	Yes – Grantor requires that no fees be charged to prisoners
Grantor controls any significant residual interest	Yes --Buildings are already owned by the grantor

Another jurisdiction, with similar arrangements, concluded that the operator did not have sufficient discretion because of the detailed requirements, including restrictions on reducing staff numbers, transferring key personnel, the number of shifts required, the number of hours per shift and expected annual hours per position.

Water treatment plant – Constructed by agency and maintained by agency	
AASB 1059 criteria	Analysis
Operator providing public services	Yes – Providing potable water is a public service
Operator managing at least some of those services under its own discretion	Yes – Operator must ‘operate the facility so that it can provide the Services to at least the Performance Standards at its own cost and risk’
Grantor controls or regulates what services the operator must provide	Yes – Water treatment plant can only be used for water treatment
Grantor controls to whom the operator must provide services	Yes – Services must be provided to the public
Grantor controls what prices the operator charges	Yes – Operator cannot charge any additional fees
Grantor controls any significant residual interest	Yes – PPE already owned by the grantor

Another jurisdiction, with BOOT arrangements for similar assets, concluded that the operator was not providing a public service, as the service was used internally by the grantor.

Social housing – Housing constructed by agency and maintained by agency	
AASB 1059 criteria	Analysis
Operator providing public services	Yes – Social housing is a public service
Operator managing at least some of those services under its own discretion	Yes – Operator has discretion in managing and selecting tenants.
Grantor controls or regulates what services the operator must provide	Yes – The social housing must be used for social housing
Grantor controls to whom the operator must provide services	Yes – The social housing must be provided (subject to capacity) to those that meet grantor determined eligibility
Grantor controls what prices the operator charges	Yes – Grantor determines rent, or discount to market
Grantor controls any significant residual interest	Yes – PPE already owned by the grantor

Grant for health services using grantor owned buildings	
AASB 1059 criteria	Analysis
Operator providing public services	Yes – Health services a public service
Operator managing at least some of those services under its own discretion	Yes – Operator has discretion in managing and selecting patients
Grantor controls or regulates what services the operator must provide	Yes – The grantor owned buildings must be used for the designated health services
Grantor controls to whom the operator must provide services	Yes – The grantor refers selected patients to the operator
Grantor controls what prices the operator charges	Yes – The operator is not permitted to charge any additional fees to the patient
Grantor controls any significant residual interest	Yes – PPE already owned by the grantor

Land required to be used for public space as part of property development arrangement. Operator / property developer permitted to use major parts of land for retail. Hotel and carpark usage, but must use some of the land for public space	
AASB 1059 criteria	Analysis
Operator providing public services	Yes – Providing land as public space is a public service
Operator managing at least some of those services under its own discretion	Yes – Operator permitted to hold events, at its discretion, on public space – as long as access to public space not unreasonably restricted
Grantor controls or regulates what services the operator must provide	Yes – public space must be provided for public space
Grantor controls to whom the operator must provide services	Yes – the public space must be open to the public
Grantor controls what prices the operator charges	Yes – the public space must be open to the public for free
Grantor controls any significant residual interest	Yes – The property / land is already owned by the grantor