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*(b) the basis on which the operator can charge users of the service concession asset, which might not be uniform over the arrangement term, thereby making the use of a straight line amortisation of the GORTO liability inappropriate.:*

It is HoTARAC's view that recognising revenue according to the economic substance would usually be in accordance with how access to the asset is provided to the operator. As such the straight-line method would be appropriate in most cases. IN addition, the approach suggested in point (b) above is practically harder to implement.

#### ***Amortisation of GORTO liabilities related to replacement of major components***

One HoTARAC member raised that amortisation of GORTO liabilities relating to replaced components does not seem to take into account the expected life or replacement frequency of the component (refer to Illustrative Example 7 in AASB 1059) and recommends the AASB provide guidance on how to account for such a situation.

For example, there is a 30-year service concession and a particular component of the SCA is replaced every 5 years. Our understanding is the amortisation of the GORTO liability relating to this component will be as follows –

- The initial component installed during construction is amortised over 30 years,
- The 1<sup>st</sup> replacement at start of year 6 is amortised over 25 years,
- The 2<sup>nd</sup> replacement at start of year 11 is amortised over 20 years,
- The 3<sup>rd</sup> replacement at start of year 15 is amortised over 15 years, etc...

This results in more and more revenue recognised in the later years. The financial statement impact can potentially be material, where the grantor has major components requiring replacement multiple times over the course of the service concession.

One of the options to resolve this issue would be amortisation of the GORTO liability relating to this component over 5 years each time it is replaced, aligning with asset depreciation principles. However, this would require componentising the GORTO liability, and brings about an additional cost burden.

Refer also to Appendix A which sets out one HoTARAC members dissenting view.

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?

HoTARAC believes that more guidance would be advisable for distinguishing financial liability and GORTO. For example, there may be an arrangement structured in a way that the grantor acts as an agent collecting revenue from third party users for the operator and this raises the question whether the grantor should recognise financial liability or GORTO liability.

In our view, the following question should be considered to make an assessment whether the grantor's liability is financial liability or GORTO:

- Is it the grantor or the operator who bears the economic risks when there is toll evasion, fee disputes, unplanned service disruption, etc?

If the grantor bears these risks, the grantor may need to recognise a financial liability based on expected third party usage. It would be up to the grantor to ensure it collects all the revenue from third parties to cover its payments to the operator.

If the grantor does not bear the risks and simply remits what it collected to the operator, it could be a GORTO liability instead.

### Topic 5: Other matters

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.

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.

Provided above.

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?

**AASB General Matters for Comment In addition to the specific matters for comment on each topic, the AASB would also particularly value comments on the following:**

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

No regulatory issues identified.

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

This submission indicates that there were significant challenges of judgment in accounting and auditing of service concession arrangements.

The other observation is that AASB 1059 increases the number of judgements made by preparers and auditors, therefore increasing audit challenges.

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

Generally, agree.

Refer to the comments to question 12. One of the HoTARAC members does not think that recognition of GORTO arrangements on balance sheet makes the financial statements more useful to users. They are of the view that it artificially inflates the State's assets and liabilities and detracts from economic substance – in their view it is hard to substantiate a 'present obligation' for the GORTO liability and it has limitations being construed as genuine "revenue" – consequently, experienced users are having difficulties making sense of this liability and what it actually means. Refer to Appendix A for more explanation.

**24. In your view, do the benefits of applying the requirements of AASB 1059 exceed the implementation and ongoing application costs?**

Generally, agree. AASB 1059 helped achieve consistency in the accounting for service concession arrangements, pending areas where further guidance is requested as part of this submission. However, one of the HoTARAC members considers the benefits of the standard as it stands do not exceed the implementation and application costs (including additional costs of asset valuation, GFS differences and user confusion around what SCAs/liabilities mean/represent). For financial liability SCAs, the additional guidance is welcome but it did not result in significantly different accounting treatments from what had been adopted pre-AASB 1059.

## Appendix A – Dissenting View

In addition to the comments in the main part of this submission, one of the HoTARAC members raised the following three issues.

### *Grantor's control of the asset*

- (i) Fundamentally, the concept of control in AASB 1059 differs from the concept of control in AASB 10 *Consolidated Financial Statements*. This is where many AASB 1059 issues for GORTO arrangements have their root. The outcome of AASB 1059 is that both parties (the grantor and the operator) effectively control the same asset, both entities recognise the asset in their financial statements, but there is only one set of economic benefits being derived and accruing to one entity.
- (ii) The wording of AASB 1059.5(a).
  - a. It takes a black and white (or “in/out”) approach to control rather than looking at the extent (or whether “enough” substantive control resides with the grantor).
  - b. Use of the terminology “controls or regulates” in AASB 1059.5(a) is a contributory factor to this – because one can regulate an activity or entity without controlling it. This is particularly the case in a long term GORTO arrangement (such as a toll road) where the grantor does not benefit economically from the asset during the service concession period.

This HoTARAC member suggests that the AASB re-examines the distinction between “control” and “regulate” in their post implementation review process. There are some arrangements that can be regulated but the level of regulation does not give economic control to the grantor during a service concession period, even if the asset returns to the government at the end of the service concession term.

### **Recognition of GORTO arrangements**

The HoTARAC member suggests that the AASB reconsider whether long-lived GORTO arrangements should be recognised on the balance sheet.

They remain concerned with the economic substance of the argument that the State exercises genuine substantive “control” over most, if not all, of their material GORTO arrangements (especially with regards to toll roads). They continue to question the rationale for the underlying physical asset (e.g. road) and rights associated with that asset (e.g. tolling rights) to be separated and recognised by two different entities – when, in substance, it is the same asset that is being accounted for twice by two different entities.

Related to this is the fact that the ABS ignores or makes adjustments for GORTO assets and liabilities in their analysis.



They are of the view that for a GORTO arrangement, alternative options that would achieve the objective of meeting users' information needs at a much lower cost include:

- (i) recognise the residual interest in the asset through gradual accretion over the term of the arrangement, or
- (ii) Recognise the asset at its fair value when the asset returns to "control" of the State (applying control concepts similar to AASB 10 and for other assets), or
- (iii) Disclosure only for GORTO arrangements using a combination of qualitative and quantitative disclosures instead of recognition in financial statements.