



The  
Treasury

Contact: Sean Osborn  
Telephone: (02) 9228 5932  
Our Reference: FA551815

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

Dear Chair

**AASB ED 261 Service Concession Arrangements: Grantor**

NSW Treasury is grateful for the opportunity to provide comments on this exposure draft and supports the AASB's efforts to develop requirements and guidance on grantor accounting for service concession arrangements.

In our submission we recommend the AASB more clearly explain the principles behind the proposed standard and guidance. We also recommend the AASB initiate and prioritise a project to develop a more principles-based, transaction neutral approach to accounting for service concession arrangements that would allow preparers to state compliance with IFRS.

This submission also provides examples of challenges NSW Treasury, preparers and their advisors are experiencing in attempting to apply the proposed requirements. Due the relatively short comment period for this ED NSW Treasury has not had the opportunity to review all arrangements to which the proposed standard may apply, but would be more than willing to work with the AASB to further identify and analyse existing and proposed arrangements to further inform the AASB's decisions.

Yours sincerely

Karen Sanderson  
for Secretary

## General Comments

NSW Treasury supports the AASB's efforts to provide authoritative guidance on grantor accounting for service concession arrangements. However, we recommend the AASB pursue an approach that would result in requirements and/or guidance that are less rules based and more principles based. The new standard should also be transaction neutral and enable for-profit entities to state compliance with international accounting standards (IFRS).

Although the proposed standard will provide guidance for many service concession arrangements, there is risk current and future transactions will fall into a gap where they do not currently meet the control criteria. This provides an opportunity to structure arrangements to achieve different accounting outcomes and may not sufficiently accommodate the trend to innovative arrangements in delivering public services.

NSW has at least 50 public private partnerships (PPPs). These include many innovations to the traditional PPP which have stretched the limit of existing guidance. There is an increasing trend toward privatisation (for example, the sale of the electricity generation and retail businesses), partnerships with the private sector (for example new rail and road infrastructure, new schools and hospitals) and business models in which the government competes with the private sector (for example, NSW TAFE now competes with private sector vocational education providers). In this environment the need for robust, principles-based and transaction neutral standards is increasingly important.

### NSW Treasury's Preferred Approach

NSW Treasury's preferred approach would be for the AASB to initiate and prioritise a project to develop guidance and/or requirements that are principles-based and transaction neutral. This would more comprehensively address the perceived gap in guidance on grantor accounting for service concession arrangements and ensure the guidance continues to support consistent, relevant, transparent and easily understood financial reporting into the future.

NSW Treasury would also support an approach in which the AASB more fully articulated the principles and concepts that support the rules embodied in the proposed standard. This would allow preparers to more consistently and appropriately extrapolate these to new, innovative arrangements.

In either approach we recommend the AASB explain in more detail:

- What the standard considers the nature of a service concession arrangement to be. For example, are they financing arrangements to pay for the building or upgrading of infrastructure? Is it a way for the grantor to procure both assets and services? This would assist preparers to determine whether new types of arrangements are in substance similar to or different from service concession arrangements accounted for under the proposed standard.  
  
Interpretation 12 states that the operator acts as a service provider, providing construction or upgrade services and operation services (paragraph 12). ED 261 alludes to the fact such arrangements include an asset component and a service component (paragraph 22, AG35-AG38). However the Basis for Conclusions explains that the grant of a right model is "in the nature of financing the construction of the service concession asset (BC24)". If the AASB were to more clearly articulate their conceptual views of these arrangements, it would assist application of the concepts to new and different arrangements, even if they do not fit neatly in the rules of the proposed standard. This may also assist preparers differentiate between service concession arrangements and outsourcing, service contracts or privatisations.
- Which standards may apply when arrangements do not meet the control criteria. From discussions with NSW government agencies, we understand that where an arrangement does

not meet scope of the control criteria most preparers are expecting to default back to the risks and rewards assessment, applying *FRS 5 Reporting the Substance of Transactions Appendix F Private Finance Initiatives and Similar Contracts* or Interpretation 4 *Determining whether an arrangement contains a lease*. To provide clarity and encourage consistent accounting treatment, NSW Treasury recommends the AASB more clearly articulate why the arrangements are not in substance leases and what approach is considered appropriate if the risks and rewards, control and rights and obligation approaches are not considered appropriate (BC8-BC17). NSW Treasury notes the proposed definition of a service concession arrangement is an arrangement in which the grantor gives the operator a "right of access" (Appendix A) and that this differentiates it from a lease, which transfers a right of use. NSW Treasury recommends the AASB more fully explain what a "right of access" is in the context of service concession arrangements.

- The proposed standard requires preparers to assess assets according to the recognition criteria in AASB 116 and AASB 138 before applying the control criteria in paragraphs 8 and 9. NSW Treasury recommends the AASB provide additional guidance on how these recognition criteria apply to service concession arrangements. Arguable once the recognition requirements of AASB 116 or AASB 138 are met, the control criteria in ED 261 is redundant.

### **Future-proofing Accounting for Service Concession Arrangements**

There is a risk the proposed control criteria will quickly become out of date because:

- The criteria are rules based rather than principles based.  
There is a risk future arrangements could be structured to achieve a desired accounting outcome. The proposed rules may not be sufficiently flexible to be applied consistently and effectively to innovative arrangements not currently contemplated by ED 261.
- The criteria are too narrow.  
It is not clear how to account for service concession arrangements where the asset does not meet the control criteria in paragraphs 8 and 9. For example, where the grantor does control or regulate prices.
- Only control by the grantor is considered  
The criteria are set up to answer the question "does the grantor control the asset?" rather than "who controls the asset?" The criteria can never conclude that the operator controls the asset, only that the grantor does or does not control it. Because of this neither Interpretation 12 nor ED 261 provide guidance on how to account for service concession arrangements where the operator controls the asset.

### **Examples of Application Difficulties**

Although NSW Treasury has not had sufficient time to review all arrangements to which the standard may apply, below are some examples of arrangements that the proposed standard does not appear to contemplate:

- An operator builds and operates a public hospital in exchange for a right to charge the grantor for service rendered to the public. The amount charged is calculated as the volume of services multiplied by an agreed price and is capped at a maximum annual amount. In this arrangement the grantor does not have a contractual obligation to pay cash or another financial asset, nor does it involve granting the operator the right to charge third party users (paragraph 23). Although this arrangement is not contemplated by ED 261, the arrangement is, in substance, similar to a grant of a right to charge users.

- An operator builds and operates a shared facility which is used to treat patients from both adjoining private and public hospitals. The grantor and operator contribute to the cost of construction based on the relative bed count of their respective hospitals. At the end of the arrangement the operation and management of the shared facility returns to the grantor. The operator charges the grantor for services provided to public hospital patients (based on volume and an agreed price, capped at an annual maximum). The grantor does not control any aspects of the services provided to private hospital patients. The shared facility cannot be further componentised as there are no separate and determinable cash flows associated with either the construction or operations of discrete parts of the shared facility.  
If the bed count of the private hospital is greater than the bed count of the public hospital it might be considered that the grantor does not control what services are provided, to whom or at what price for the purposes of 8(a) of ED 261. In this case it is not clear how the grantor should account for its contribution to the construction costs and right to receive the shared facility back at the end of the period.
- A grantor agrees to extend the concession period on one toll road to help the operator fund the building of a second, new and unconnected toll road

NSW Treasury would be willing to work with the AASB to identify and describe more arrangements to help inform further decision making.

As well as difficulties applying the proposed standard to new types of arrangements NSW Treasury, external advisors and agencies have had difficulty applying the proposed standard to existing arrangements. For example:

- A grantor engages an operator to build and maintain a school for a period of time. The grantor compensates the operator through a series of payments made up of a fixed component to cover the cost of construction and variable component to cover maintenance services, subject to performance. The grantor uses the school to provide public education to the community while the operator maintains the asset (e.g. facilities management, cleaning etc).  
It is unclear whether this arrangement is in the scope of ED 261. The maintenance services could be considered to be a public service as part of the usual government function, financed by the government and supporting the provision of the public service of free education. However, the service is not provided to the community and the operator does not use the school to provide the services (rather the services are applied to the asset). We note that such an arrangement is considered within the scope of Interpretation 12 from the operator's point of view.
- A community housing provider (CHP) leases (three year rolling lease) public housing property from the State and sub-leases it to a community housing tenant. The arrangement between the State and CHP stipulates what services are provided and to whom and regulates the price at which services are provided. It is not clear whether the arrangement meets the definition of a service concession arrangement by virtue of the three year lease being a "specified period of time" or whether the rolling nature of the arrangement means the definition is not met.
- An operator of an existing service concession arrangement enhances the service concession asset in exchange for an extension to the arrangement by 4 years.

### **Statement of Compliance with IFRS**

NSW Treasury understands that the AASB has not determined whether ED 261 is consistent with IFRS, in particular the requirement to recognise revenue over the period of the concession (paragraph 23-24, AG51-AG53). We also understand this is the reason the AASB has not included non-public sector entities in the scope of the proposed standard.

The ability to state compliance with IFRS and apply transaction neutral accounting is important to the NSW public sector. The trend in NSW is towards, innovative arrangements between the public and

private sectors. The ability of NSW public sector entities to state compliance with the same accounting framework as private sector buyers, partners and competitors will promote comparability, competitiveness and transparency.

NSW Treasury recommends the AASB more fully consider whether preparers could apply a proposed standard and still state compliance with IFRS. NSW Treasury's preferred approach is for the AASB initiate and prioritise a project to develop a standard and/or guidance on accounting for service concession arrangements which allows preparers to prepare financial statements that are consistent with IFRS.

Alternatively it would be useful for preparers of financial statements to understand the inconsistencies between the ED 261 and IFRS. This would allow financial statements to explain the how and why accounting policies do not comply with IFRS.