



DATE: 12 JUNE 2006
MEMO TO: MEMBERS OF THE IPSASB
FROM: RICK NEVILLE
SUBJECT: **IPSASB SERVICE CONCESSIONS SUBCOMMITTEE
MEETING WITH NATIONAL STANDARDS SETTERS**

ACTION REQUIRED

The IPSASB is asked to:

- **note** this update on IFRIC's project on Service Concession Arrangements; and
- **consider** materials prepared for discussion with national standards setters and other authoritative bodies on actioning a collaborative project
- **discuss** collaborative project with participants at meeting in Paris

AGENDA MATERIAL:

	Pages
12.2 Background on IFRIC's Service Concession Arrangements	12.4 – 12.10
12.3 Agenda for Discussion with national standards setters and similar bodies	12.11 – 12.13
12.4 Issues for Discussion with NSS	12.14 – 12.23

BACKGROUND

The IPSASB Subcommittee

The International Accounting Standards Board (IASB) International Financial Reporting Interpretations Committee (IFRIC) is developing Interpretations dealing with service concession arrangements.

On 3 March 2005, IFRIC issued draft Interpretations: D12, "Service Concessions Arrangements – Determining the Accounting Model", D13, "Service Concessions Arrangements – The Financial Asset Model" and D14, "Service Concessions Arrangements – The Intangible Asset Model" (collectively known as the Draft Interpretations). The IPSASB submitted a response to the draft interpretations on 1 June 05. That response raised a number of concerns about the narrow scope of the project, its implications for notions of control in the public sector, and the proposed models for recognition of revenue over the life of the arrangement.

Following its July 2005 meeting, the IPSASB established a subcommittee to monitor the work of the IFRIC. The role of the IPSASB subcommittee is to keep the IPSASB informed of developments and make proposals to the IPSASB re any actions the subcommittee considers appropriate.

The IPSASB subcommittee comprises the following members: Canada (Chair), Australia, Israel, France, New Zealand, South Africa, United Kingdom, USA and OECD

Agenda item 12.2 identifies IFRIC progress/decisions on service concessions as reflected in the IFRIC Update, published after each IFRIC meeting. It is anticipated that IASB members and/or

staff attending this session will provide an update on the current status of the IFRIC deliberations and confirm or otherwise that our interpretations of the decisions reported in the IFRIC Update are appropriate. A brief history sheet of the IPSASB's project and an extract from the IASB's website which provides an overview of the Draft Interpretations are included as Appendices 1 and 2 to Agenda item 12.2.

Major decisions/discussions/conclusions reported in IFRIC Updates (in March and May 2006) issued since my last report to the IPSASB are to:

- Better align explanations in D.12 with the definition of a financial asset in IAS 32 – to reflect that a financial asset exists when the operator has a contractual right to receive cash;
- Extend the scope of arrangements dealt with by the Interpretations to encompass arrangements which involve the use of the asset for the whole of its useful life;
- Clarify that any significant residual interest in an asset at the completion of the arrangement is to be controlled by the grantor;
- Consider whether pre-existing assets of the operator should also be included within the scope of the Interpretations (currently only pre-existing assets of the grantor are included.);
- Clarify and better explain the amortization methods that could be adopted for intangible assets under the Interpretations;
- Include guidance to the IASs/IFRSs that might apply to arrangements falling outside the scope of the Interpretation;
- Combine in a single Interpretation matters previously dealt with in draft Interpretations D12-D14;
- Deal in a separate project with IFRICs previous conclusion that a “sale and leaseback” arrangement which incorporates a repurchase provision should not, in fact, be accounted for as a sale and leaseback (because the seller retains effective control and therefore the criteria for recognizing a sale would not be met). This decision reflects that this conclusion has wider implications than for just service concession arrangements.

COLLABORATIVE PROJECT WITH NATIONAL STANDARDS SETTERS AND OTHER AUTHORITATIVE BODIES

As agreed at the last meeting, the IPSASB has invited a number of national standards setters and other authoritative bodies who have responsibilities for public sector entities to meet with the IPSASB to discuss the manner in which a collaborative project might be progressed and matters it might deal with.

Standards setters and other authoritative bodies from the following countries have been invited to participate in the discussion and are expected to participate: Canada, China, Australia, France, Italy, Netherlands, New Zealand, South Africa, Spain, Switzerland, UK, USA and the FEE Public Sector Committee. The IASB and the International Task Force on Harmonization of Public Sector Accounting (TFHPSA) will also be represented.

An agenda for the meeting is included at Agenda item 12.3 and a staff paper on matters/issues for discussion at the meeting are identified at Agenda item 12.4. Those matters include consideration of whether a collaborative project should be actioned and the nature and objectives of any such project. It also considers the mechanisms that may be adopted for project development and resourcing and timing of key milestones in project initiation.

I have asked staff to include in the issues paper their preliminary views on key matters raised as a mechanism to focus our discussion at the forthcoming meeting. The key element of the staff paper is that the project should not be directed at putting in place authoritative guidance which mirrors the

IFRIC Interpretation when issued. Rather, there is a case for a more fundamental approach starting with the preparation of a consultation paper which analyses the issues, considers current practice and requirements in a number of jurisdictions, and draws out the implications of existing definitions and concepts of for example, assets and liabilities for dealing with those issues. Such an approach need not be constrained by interpreting, and applying to service concession arrangements, requirements that are reflected in current standards at the international level or in any particular national jurisdiction. It could also consider the implications of its proposals for accounting by both the grantor and the operator.

These are staff views and not necessarily the views of the IPSASB subcommittee monitoring IFRIC or of other IPSASB members - but they do provide an useful basis for our discussion. I anticipate that IPSASB members and other participants will wish to explore these matters further at the meeting and will raise additional matters for discussion.

As is indicated at agenda item 12.3, we hope to reach tentative agreement on a number of key matters related to progressing this project during our relatively short meeting in Paris. Those decisions will influence our ongoing work on this project.

In reviewing the issues paper subcommittee members noted that there are some aspects that will need to be explored further in discussions at Paris, these include such matters as:

- whether a subcommittee approach is appropriate;
- whether the composition and size of the subcommittee is appropriate;
- who should be appointed as chair of the subcommittee; and
- is timing for initiation and completion of this stage of the project appropriate.

Participants at the meeting are of course most welcome to raise additional issues for discussion as we consider whether and how to move forward on a collaborative project.

SUBSEQUENT ACTIONS

The subcommittee will continue to monitor IFRIC's progress and report back to the IPSASB. IFRIC has not yet agreed the final Interpretation(s), determined whether amendments to the draft Interpretations are such that it needs to be re-exposed, or put the final Interpretation to the IASB for formal approval to issue. (The IASB votes on the text of the Interpretation. Affirmative votes of at least 9 IASB members are required for approval to issue an Interpretation).

Subsequent actions with respect to an IPSASB project will of course be dependent on the outcome of discussions with the standards setters and other bodies at the forthcoming meeting. Subject to those discussions, I believe this subcommittee could usefully be tasked with an ongoing role in the development of the project brief for consideration by the IPSASB and the NSS and other organizations that will participate in the collaborative project.

I also believe that if the staff proposal for the development of a consultation paper are accepted (or some variation on it) members of this subcommittee could usefully be involved in the ongoing development. However, I do accept that any IPSASB subcommittee involved in the project development will need to have an appropriate representation of membership, should include representation of the national standards setters or other organizations not already represented on the IPSASB, and should not impose too heavy a burden on members already involved in other IPSASB subcommittees.

Background - IFRIC's Service Concession Arrangements Project

IFRIC Decisions to end 2005

Major decisions on service concessions made by IFRIC post the end of comment period on D12, D13, D14 to the end of December 2005 include:

- To progress this project itself as an Interpretation(s) rather than refer it to the IASB for the development of an IFRS. The IFRIC members believed that, with its limited scope project, the IFRIC was better placed than the IASB to deal with the pressing issues in a timely way and decided to continue its work on the project.
- The Interpretations will not specify accounting by grantors. However, the basis for conclusions will note that, in many cases, the government/grantor will control the physical assets, but the resulting accounting had not been considered explicitly by IFRIC.
- The scope of the Interpretations will not include private-to-private service concession arrangements. However, IFRIC noted that application by analogy could be appropriate under the hierarchy in accordance with IAS 8, "Accounting Policies, Changes in Accounting Estimates and Errors". IFRIC will consider examples to test this proposal at its next meetings (3-4 November and/or 1-2 December, 2005).
- For service concession arrangements within the scope of the draft Interpretations, the infrastructure should not be recognized as property, plant and equipment of the operator because the indicators of control lead to the conclusion that the grantor controls the asset. The control indicators are the grantor's ability to control the use of the infrastructure throughout the concession and its control of the residual infrastructure at the end of the concession.
- To change the proposals in the draft Interpretations to narrow the circumstances in which financial assets would be recognized. This is to ensure that the Interpretations were consistent with IAS 32 "Financial Instruments: Disclosure and Presentation" and IAS 39 "Financial Instruments: Recognition and Measurement". The basis for conclusion will note agreement that might be supportive of a wider interpretation of IAS 32. Text is being developed.

Other issues that IFRIC has indicated it will re-consider in light of responses from constituents (some of these issues were also highlighted by the IPSASB in its submission to IFRIC):

- The meaning of 'control', 'public service obligation' and 'infrastructure';
- Distinction/boundary between the financial asset model and the intangible asset model based on "who paid for the arrangements";
- Whether users and grantors should be considered separate parties in all instances;
- Relationship of the scope of the Draft Interpretations to SIC 29, "Disclosure–Service Concession Arrangements";
- Exclusion of "whole of life" arrangements (arrangements where no significant residual interest exists); and
- Lack of guidance on the application of the requirements proposed in the draft Interpretations to partly regulated assets.

IFRIC meeting in January, 2006

A project plan submitted by staff proposed delivery of final Interpretations by the third quarter of 2006, assuming that re-exposure is not necessary. While continuing to move forward, the IFRIC noted that issuing final Interpretations in the third quarter of 2006 may be optimistic.

Major issues discussed by the IFRIC at its January meeting included:

- The scope of D12. Many respondents, including the IPSASB, had expressed concern that D12 did not deal with a range of potential arrangements. The IFRIC noted that guidance was needed most urgently for those arrangements that were dealt with in D12. IFRIC decided not to extend the scope of the project, but to explain in the basis for conclusions that a spectrum of arrangements is possible and users should refer to relevant standards for arrangements not dealt with in the Interpretations. Any further guidance needed, may be undertaken as a separate IFRIC project.
- The pattern of recognition of revenue and profit under the “ Intangible Asset Model“. IFRIC determined to continue with the view as proposed in D14.
- Additional issues to consider. As the project develops, the IFRIC will also consider “whole-of-life” arrangements (arrangements where all the service potential of the infrastructure is consumed under the terms of the arrangement) and approaches that apply the requirements in IAS 16 “Property, Plant and Equipment” to improvements in infrastructure subject to service concession arrangements.

Background - Appendix 1: - IPSASB's work on Service Concession Arrangements

The IPSASB has on its work program a project to deal with service concession arrangements. Part of the work in this project includes monitoring the IASB's IFRIC's project on service concession arrangements.

On 3 March 2005, IFRIC published for comment three draft Interpretations on service concession arrangements. At the IPSASB's 14 – 17 March 2005 meeting it was agreed that IPSASB would submit comments to IFRIC. A subcommittee was appointed to review the draft Interpretations and provide comments to staff who would then prepare a draft comment letter to IFRIC. The draft comment letter would then be circulated to all IPSASB members for their review and approval to submit.

The subcommittee comprised members from Canada, France, United Kingdom, Argentina, Australia, Israel, New Zealand, South Africa and USA. A draft letter was circulated out-of-session for approval by IPSASB members. The submission was approved subject to minor revisions. Those revisions were processed and cleared with the relevant member and the IPSASB Chair.

The IPSASB's submission was submitted to IFRIC on 1 June 05. The IPSASB's submission expressed concern about a number of aspects of the draft Interpretations. These concerns include:

- the narrow scope of the draft Interpretations;
- the focus on providing guidance to the operator without guidance on treatment by the grantor;
- the notion of the 'control' approach used in the draft Interpretations (members were concerned with IFRIC's interpretation of control, particular in respect of its implications for the public sector);
- whether the rationale that the 'control' approach was superior to the 'risks and rewards' approach was convincing;
- the use of different accounting models based solely on the " identity of the payer/funder of the concession arrangements"; and
- that the matter was being dealt with by IFRIC rather than the IASB. Members were of the view that a Standard rather than an Interpretation (or series of Interpretations) was necessary to deal with the issues that arise in respect of service concession arrangements for both the grantor and operator.

At its November/December 2005 meeting in Cape Town, the IPSASB noted an update on IFRIC's deliberations from the IPSASB subcommittee. The IPSASB agreed to write to national standards setters to explore the potential for a collaborative project to provide authoritative guidance to public sector entities that are party to service concession arrangements.

At its March 2006 meeting in Tokyo, the IPSASB noted a further update on IFRIC's deliberations from the IPSASB subcommittee. The IPSASB also noted that responses from a number of national standards setters indicated an interest in exploring the potential for a collaborative project. The IPSASB agreed to invite those standards setters and other relevant

organizations to meet with the IPSASB at its next meeting to discuss further a collaborative project. Members agreed to provide staff with the names of organizations in their jurisdictions that should be invited.

At the IPSASB's March meeting, the OECD observer noted that:

- the OECD was holding a major symposium on public private partnerships (PPPs) in Madrid during the week of the IPSASB meeting; and
- the IPSASB, its members and national standards setters would be invited to attend a session of the OECD symposium to discuss financial reporting issues. As requested, details of those attending the IPSASB meeting were provided to the OECD.

During April and May 2006, invitations were issued to a number of organizations to meet with the IPSASB in Paris in July. An attendance list is included in these materials. (It is anticipated that the OECD will also invite these organizations to participate in the OECD symposium in Madrid.)

May and June 2006. An issues paper was prepared by IPSASB staff in conjunction with the subcommittee as a basis for discussions at the IPSASB meeting.

Background - Appendix 2: Overview of the Draft Interpretations

The overview of the draft Interpretations below is extracted from the IASB's website when IFRIC initially issued the draft Interpretations for comment.

Introduction

- 1 On 3 March 2005, the IFRIC published for comment three draft Interpretations on service concessions. Comments have been requested by 31 May 2005.
- 2 The draft interpretations address arrangements whereby public services—such as the construction and operation of roads, hospitals, prisons, waste disposal plants or energy distribution facilities—are contracted to private 'operators'. The draft interpretations address only the accounting by the operators. They do not specify the accounting by the 'grantors' of the contracts, typically governments or their agencies.
- 3 These arrangements typically involve significant capital expenditure on infrastructure. The infrastructure may already exist and need only be maintained (and perhaps enhanced) by the operator. Or the concession may require the operator to construct the infrastructure before operating it.
- 4 The draft interpretations apply only to concessions in which the grantor retains control over the use to which the infrastructure is put: it decides what services the operator must provide, to whom it must provide them and at what price; and it retains control of the residual interest in the infrastructure at the end of the concession.
- 5 The way in which operators at present account for such infrastructure under their local GAAPs varies. In some countries, the accounting has been characterised by smoothing adjustments designed to report smooth profit trends over the concession. There has been uncertainty about the requirements of IFRSs. One question is about the nature of the operator's expenditure on construction of infrastructure—should the operator recognize property, plant and equipment or some other type of asset? Another question is about the treatment of borrowing costs incurred by the operator to finance the infrastructure. These borrowing costs tend to be higher in early years—can they be capitalized and allocated evenly over the contract?
- 6 The IFRIC has sought to address these questions and provide guidance on other aspects of service concession accounting. Because of the range of matters to be covered, the IFRIC has split the interpretations into three separate documents.

D12 Determining the Accounting Model

- 7 D12, the first draft Interpretation, specifies how an operator should classify its expenditure on construction of infrastructure. D12 proposes that, because the operator does not control the use of the infrastructure, it should not recognize it as its own property plant and equipment. Instead, it should account for the rights it receives in return for providing construction services to the grantor.
- 8 D12 proposes that the classification of the operator's rights should depend on who is required to pay for the concession services:
 - a) if the grantor will pay for the concession services itself, the operator has a contractual right to receive cash in exchange for its construction services. D12 proposes that such a right to receive cash meets the definition of a financial asset and should be accounted for as such.

- b) if instead, the contract gives the operator a right to charge users for the concession services—for example, to charge tolls for operating a road—D12 proposes that the operator does not have a contractual right to receive cash. Instead, the operator has a right to charge users if and when they use the concession services—a right that meets the definition of an intangible asset. The operator should therefore recognize the right it receives in exchange for providing construction services as an intangible asset.
- 9 The two different models have different accounting consequences and are dealt with separately in the second and third of the interpretations.

D13 The Financial Asset Model

- 10 D13 sets out the accounting proposed when the financial asset model applies. The operator would apply standard construction contract accounting, recognizing revenue on a percentage of completion basis as construction progressed. The resulting asset (the amount due from the grantor) would meet the definition of a financial asset and be accounted for in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*. The amounts subsequently received from the grantor for the concession services would be allocated between three components:
- repayment of the financial asset
 - finance income — the effective interest on the outstanding receivable
 - operating revenue — for provision of ongoing services such as maintenance and staffing.
- 11 Often an operator's borrowings will be similar to the amount due from the grantor, both tending to reduce over the duration of the contract. Applying the financial asset model, the impact on profit of higher borrowing costs in earlier years and lower borrowing costs in later years would tend to be offset by a similar pattern of finance income.

D14 The Intangible Asset Model

- 12 D14 sets out the accounting proposed when the intangible asset model applies. The operator would again apply construction contract accounting, recognizing construction revenue on a percentage of completion basis as construction progressed. But it would not be receiving cash for its services. So instead of giving rise to a receivable, the revenue-earning activity would give rise to an intangible asset. This intangible asset would be accounted for in accordance with IAS 38.
- 13 The amounts reported in the income statement would be different from those reported under the financial asset model. Overall, the net profit or loss reported over the duration of the contract would be the same. But both revenues and operating expenses would be higher: all receipts from users—not just those attributable to operating the facilities after construction—would be recognized as revenues, matched by additional operating expenses from the amortization of the intangible asset. And the pattern of profit recognition could be different: higher borrowing costs in earlier than later years would contribute to lower profits (or losses) being recognized in earlier years and higher profits in later years (because there would be no corresponding finance income). The IFRIC concluded that it would be inconsistent

with IFRSs, and the IASB's conceptual framework, to defer borrowing costs in order to smooth profits over the duration of the contract.

Effective date

- 14 The IFRIC aims to issue the Interpretations in final form before the end of 2005. It is likely that, on that timetable, they would be effective for financial years commencing in January 2006 onwards.

Proposed Program for Discussion
IPSASB and National Standards Setters and Other Bodies (NSS)

**SERVICE CONCESSION ARRANGEMENTS
(PUBLIC PRIVATE PARTNERSHIPS (PPPs))**

3.45pm – 5. 45pm Tuesday July 5, 2006

at

**Ministère de l'Économie, des Finances et de l'Industrie,
139 rue de Bercy, Paris, France**

The schedule for the discussion is outlined below. It is intended to be a general discussion of the need for and nature of a collaborative project. A paper identifying matters for consideration at this meeting is attached.

Participants should also raise any additional issues for discussion.

A list of IPSASB members and other participants is attached

At the end of the day it is intended that the meeting agree:

- ***Whether a collaborative project should be actioned;***
- ***The objectives/nature of the project;***
- ***The parties that will actively participate in the project development; and***
- ***The next steps in project activation, and responsibilities and timelines.***

Proposed Agenda

Time	Activity
3.45 – 3.50	1. Session Objectives <i>Mr. Philippe Adhémar, IPSASB Chair</i>
3.50 – 4.15	2. Update on current status of IFRIC deliberations and likely outcomes. (IASB representative). <i>Mr Wayne Upton, Director of Research, IASB</i>
4.15 – 5.15	3. Discussion of whether a collaborative project should be actioned and, if agreed, its nature, objectives and resourcing. <i>All participants</i>
5.15 – 5.45	4. Proposed future actions and responsibilities. <i>Mr Philippe Adhémar.</i>
5.45	Meeting close

**REPRESENTATIVES OF NATIONAL STANDARDS SETTERS and OTHER
ORGANIZATIONS**
(Subject to final confirmation of all attendees)

NAME	REPRESENTING
Mr Wayne Upton	International Accounting Standards Board
Ms Caroline Mawhood	FEE-Public Sector Committee
Ms Lucie Laliberté	International Task Force on Harmonization of Public Sector Accounting (TFHPSA)
Professor Giuseppe Farneti	Commissine Enti Pubblici CNDC & CNR, Italy
Marcello Bessone	Ministerio delle Economia e delle Finanze, Italy
Mr W.G.J. Wijntjes	Commissie Besluit Begroting en Verantwoording, The Netherlands
Ms Li Hongxia	Chinese Accounting Standards Committee
Mr Jim Paul	Australian Accounting Standards Board
Mr Ron Salole	Public Sector Accounting Board (PSAB), Canada
Mr Frank Mordacq	Ministère de l'Économie, des Finances et de l'Industrie, France
Mr David Bean	Governmental Accounting Standards Board
Ms Joanna Perry	Financial Reporting Standards Board, New Zealand
Ms Erna Swart	Accounting Standards Board, South Africa
Mr Ian Mackintosh	Accounting Standards Board, England
Ms Marianne Andreassen	Norwegian Government Agency for Financial Management
Mr Beat Blaser	Federal Department of Finance, Switzerland
Mr José Manuel Adan Carmona	Ministry of Economy and Finance, Spain

IPSASB MEMBERS AND OBSERVERS IN ATTENDANCE

NAME	REPRESENTING
Philippe Adhémar, Chair	France
Mike Hathorn, Deputy Chair	United Kingdom
Carmen Palladino	Argentina
Wayne Cameron,	Australia
Richard J. Neville,	Canada
Pankaj Jain	India
Ron Alroy	Israel
Tadashi Sekikawa	Japan
Mohd. Salleh Mahmud	Malaysia
Alejandro Luna Rodríguez	Mexico
Frans Van Schaik	Netherlands
Greg Schollum	New Zealand
Tom Olsen	Norway
Erna Swart*	South Africa
Ron Points	United States of America
Prof. Andreas Bergmann	Public Member, Switzerland
John Peace	Public Member, USA
Prof. Stefano Pozzoli	Public Member, Italy
Ping-Yung Chiu,	IPSASB Observer, ADB
Gilbert Gelard	IPSASB Observer, IASB
Robert Dacey	IPSASB Observer, INTOSAI
Jon Blondal	IPSASB Observer, OECD
Jayantilal M Karia	IPSASB Observer, UN
Gwenda Jensen	IPSASB Observer, UN and UNDP
Marius Koen	IPSASB Observer, World Bank

*Also representing the Accounting Standards Board, South Africa

INTERNATIONAL FEDERATION OF ACCOUNTANTS
INTERNATIONAL PUBLIC SECTOR ACCOUNTING STANDARDS BOARD

ISSUES FOR DISCUSSION WITH NATIONAL STANDARDS SETTERS AND OTHER
BODIES - PARIS JULY 2006

Service Concession Arrangements - Public Private Sector Partnerships (PPPs)

BACKGROUND

On 3 March 2005, the International Financial Reporting Interpretations Committee (IFRIC) of the International Accounting Standards Board (IASB) issued the following draft Interpretations dealing with financial reporting of service concession arrangements for comment by 3 May 2005:

- IFRIC: D12, “Service Concessions Arrangements – Determining the Accounting Model”;
- D13, “Service Concessions Arrangements – The Financial Asset Model”; and
- D14, “Service Concessions Arrangements – The Intangible Asset Model” (collectively known as the Draft Interpretations).

The IPSASB submitted a response to the draft interpretations. That response raised a number of concerns about the proposed guidance, including the narrow scope of the project, its implications for notions of control in the public sector, and the basis for differentiation between the proposed models for recognition of revenue over the life of the arrangement. These and other concerns were also raised by other respondents to the draft Interpretations.

The IFRIC received some 77 responses in total. Making an assessment of where responses lie on a spectrum of approval to disapproval is always subject. However, it is fair to say that a review of responses indicates a substantial majority having significant concerns with the approach being proposed in the draft Interpretations.

Over the past (approximately)12 months IFRIC has been working through all comment letters and progressively dealing with issues raised.

This paper attempts to identify key issues that the IPSASB and the national standards setters and other authoritative bodies (referred to collectively as NSS in this paper) will need to consider in determining whether to action a collaborative project and, if so agreed, in establishing objectives and operating procedures for the project development.

This paper does not attempt to deal with specific technical issues that will determine the accounting for PPPs. These will be developed as project progresses. Nor does the paper attempt to identify potential concerns with the proposals in the IFRIC draft Interpretations. Those concerns have been identified in submissions to IFRIC, and are being considered and dealt with as appropriate by IFRIC.

The issues dealt with in this paper can be grouped into those that relate to project initiation, project objectives and scope, and the development process. These issues of course are interrelated, with decisions on some impacting others.

Issues related to Project Initiation include:

1. Is a collaborative project needed?
2. If yes, should the project be actioned at this time?
3. Should the project be directed at putting in place guidance for public sector “grantors” which mirrors that in the final IFRIC Interpretation(s) - that is, a short term “authoritative” project?
4. Should the project take a broad view and commence with a research project directed at identifying issues, current practices and their implications for service concession arrangements, and the principles and concepts that should be considered in dealing with the issues identified. If yes, should the project deal with both financial reporting by the grantor and operator?
5. Subject to decisions on 3 and 4 above, what should be the objective of the project and what type of document(s) to be produced – discussion paper(s), consultation paper(s), exposure draft(s), other?
6. Who will participate in project development and the nature of that participation - will a subcommittee/development group be used and, if yes, how will the work of that subcommittee be shared with and influenced by the views of the IPSASB and others?
7. How will the project be resourced?
8. What timelines should be established for achievement of key stages of the project.

As a mechanism to focus discussions at the meeting, this paper includes preliminary staff views on these issues and identifies recommended follow up actions. These are not necessarily the views of the IPSASB or the IPSASB subcommittee currently monitoring the IFRIC developments (IPSASB - IFRIC subcommittee). No doubt these views will be further develop further with the benefit of discussions in Paris.

Summary of staff recommendations

A summary of staff views on these matters is outlined below.

1. A collaborative project is needed. The project should be developed by the IPSASB on a collaborative basis with the active participation of members of the NSS group.
2. This meeting should agree to action the project and identify its broad operating parameters. A detailed project brief should be developed following this meeting to reflect decisions made about the scope, nature and likely timing of the project. That project brief will be widely circulated to all participants for input, and formally agreed by the IPSASB at its November 2006 meeting.
3. The project should not be directed at putting in place in the short term guidance for grantors which reflects that in IFRIC’s final Interpretation. As appropriate, each jurisdiction will develop and put in place any such guidance.
4. The project should be research based and commence with the preparation of a paper directed at identifying issues and relevant principles for their resolution. It should include an overview of current practices and could usefully draw out the authors’ view of the implications for grantors of adoption of the IFRIC Interpretation(s). It should also make recommendations for action by the IPSASB. It should deal with accounting by the grantor, but not exclude consideration of the implications of that approach for the operator.
5. The paper should be prepared by a group of IPSASB and NSS members (hereafter referred to as the PPP subcommittee) and issued as a consultation paper by the IPSASB. The paper would not necessarily reflect the views of the IPSASB or any individual NSS,

but would provide input to the IPSASB (and the NSS) as a precursor to the development of authoritative guidance. The paper could also be issued by participating NSS in their jurisdiction with appropriate introductory contextual material to “place” the paper in the national environment.

6. A PPP subcommittee comprising 3 IPSASB members and 4 members of the NSS would be established to develop the paper. An IPSASB member would chair the PPP subcommittee, which would have broad representation. A designated member of each NSS not actively participating on the PPP subcommittee would form a Project Advisory Panel (PAP) and be provided with all PPP subcommittee materials for comment. PPP subcommittee and PAP members would keep their Boards/Organizations informed of issues and progress. During development of the paper, drafts will be provided to all IPSASB and NSS members on request.
7. Staff of one NSS member would take the lead in development of the paper. Staff of the IPSASB and relevant NSSs would act as TAs to the participants on the PPP subcommittee and would provide input and support to the lead NSS staff as appropriate.
8. Realistically, a time frame for completion of major milestones in the project can only be undertaken when views on the preceding matters are known. Staff have included recommendations for immediate follow up actions and their timing - in particular, that the detailed project brief will be agreed by the IPSASB after consultation with NSS members at its November 2006 meeting.

ISSUES

Background on each of these issues and staff views thereon is provided below. A number of these issues are closely linked and are therefore considered together.

- 1. Is a Collaborative Project needed?**
- 2. If yes, should the project be actioned at this time?**

The IPSASB has had a project on PPPs on its work program for many years, but has devoted only limited resources to it.

The initial stage of the PSC (subsequently reconstituted as the IPSASB in November 2004) standards setting program was established with the specific limited objectives of developing a credible core set of IPSASs within a short period of time. PSC papers prepared to support promotion of the program in late 2000/early 2001 explained that while the first stage of the standards program focused on IFRS convergence objectives, the PSC had identified a number of specific public sector issues not addressed, or not adequately addressed, by the IASs. That paper also explained that these issues together with completion of outstanding projects from the first stage of the Standards Program were to form the basis of the second phase of the PSC’s work program for the period 2002-2005. One of those issues was the development of guidance on Public Private Partnerships (PPPs), then a widely used term for service concessions:

“Accounting for asset construction and financing arrangements between the private and public sectors has raised a number of controversial accounting issues in countries such as Australia, Canada, France and the United Kingdom. The PSC could usefully draw on the experiences in these jurisdictions and develop requirements for the accounting treatment of these arrangements. Whilst this project would draw heavily on a number of existing

Standards such as IPSAS 13, Leases and IPSAS 8, Financial Reporting of Interests in Joint Ventures, it is likely to be of sufficient importance to warrant its own Standard.”

Limited resources, other high priority projects and the actioning of the project by IFRIC meant that an IPSASB project on PPPs was not actioned during 2002 – 2005, or later. Subsequent IPSASB papers noted developments at IFRIC and potential concerns with certain aspects of the draft Interpretations as they were being developed.

At its meetings in late 2004 and early 2005, the PSC noted preliminary results emerging from a broad survey of (then) PSC members intended to indicate whether PPPs were an issue in their jurisdictions, whether guidance was in place in their jurisdictions and, if yes, how that guidance lined up with what was anticipated to be reflected in the IFRIC draft Interpretations. (With the release of the draft Interpretations imminent, completion of the survey was not pursued.) While now out of date, that survey indicated the importance of the issue in a number of jurisdictions, that guidance was in place or being developed in those jurisdictions and that guidance was not necessarily the same.

In March 2005, the IFRIC draft Interpretations were issued. As noted above, the IPSASB submitted comments noting its concerns with certain aspects of the draft Interpretations, particularly that they did not deal with accounting for the grantor, typically (but not exclusively) the public sector party to a service concession agreement, the notion of control adopted and the basis for differentiation between the financial asset and intangible asset models for recognition of revenue over the life of the arrangement.. Whether or not one agrees with the conclusions being reached by IFRIC, about the models for recognition of revenue or the notion of control being adopted, IFRIC has made it clear that authoritative guidance for grantors will not be provided by the draft Interpretations.

Staff Views

A collaborative project should be actioned.

IFRIC has been making significant progress in responding to a number of concerns raised in comment letters to draft Interpretations D12-D14 - for example, concerns regarding exclusion from the scope of the Interpretation of assets which are fully consumed in the concession, clarification of the criteria for selection of the intangible asset or financial asset model for accounting for the arrangement, guidance on Standards that may apply to arrangements that are outside the scope of the Interpretations.

However, it is clear that the final Interpretation will not deal with accounting by the grantor in such arrangements, nor resolve concerns that a number of respondents expressed about the control model reflected in the draft Interpretations. As such, the need for the development of guidance for grantors, typically public sector entities, remains. In addition, it is not clear that the interpretation of what constitutes control being adopted by IFRIC will fit comfortably with definitions in IPSASs and interpretations in the public sector. As such, it is overly optimistic to expect that practice in the public sector will evolve to adopt an approach which is symmetrical to that reflected in the IFRIC.

This is an issue that will need to be dealt with by the many jurisdictions which adopt or are moving to adopt the accrual basis of accounting. It makes sense to develop an approach that is broadly the same across those jurisdictions if possible.

As has been noted in respect of the conceptual framework project, actioning a collaborative project with a number of NSS has the potential to be a resource efficient mechanism for development of guidance that is common across a number of jurisdictions. It enables participants to draw on the work and knowledge from other jurisdictions and has favorable resource implications for those who might otherwise be faced with the prospect of developing guidance in their own jurisdictions. A collaborative project can avoid duplication of effort and unnecessary and unintended differences in the national requirements.

From the IPSASB perspective, establishing a collaborative project on this issue would further strengthen relationships between IPSASB and the national bodies responsible for developing authoritative requirements for financial reporting by public sector entities in their jurisdictions.

It is anticipated that IFRIC will conclude its deliberations and final Interpretations issued by the end of 2006. That is likely to prompt action by public sector standards setters to develop their own requirements in response. Whether the intention will be to “mirror” the requirements of the IFRIC Interpretations for public sector entities, continue with existing requirements where such are in place, or undertake additional research and development work will be determined on a jurisdictional basis. There is then the potential for different approaches to be developed or further entrenched in different jurisdictions in the short term. In this environment it is timely that an international collaborative approach be actioned. Such an approach can pool resources and make use of expertise from many jurisdictions.

The treatment of PPPs is also being considered as part of ongoing developments in financial reporting models adopted by national accountants in the statistical community (SNA, ESA 95 and GFSM 2001). The IPSASB has developed good working relationships with the statistical community through its participation in the international Task Force for Harmonization of Public Sector Accounting (TFHPSA). Actioning a collaborative project at the international level provides the opportunity to link with work going on in the statistical community and further enhance convergence of accounting and statistical bases of financial reporting to the extent appropriate.

This of course is the initial meeting to consider this issue, and staff appreciate that participants will need to further consider the nature, objectives and operation of the project and their participation in it. However, staff recommend that at this meeting participants make an “in-principle” agreement to action a collaborative project – that will send a clear signal to constituents that the organizations responsible for establishing authoritative guidance for public sector entities acknowledge the need for an international converged response to financial reporting by grantors in service concession arrangements. A detailed project brief dealing with objectives, operating processes and intended outcomes will then need to be developed to reflect decisions made in respect of other matters identified below and agreed by participants before development work commences.

- 3. Should the project be directed at putting in place in the short term, authoritative guidance for public sector “grantors” which mirrors that in the final IFRIC Interpretation(s) ?**
- 4. Should the project commence with a more fundamental research project, and should it deal with both financial reporting by the grantor and operator?**
- 5. What document(s) should be produced?**

Developing authoritative guidance for public sector grantors which mirrors the requirements of the IFRIC interpretation will deal with certain concerns raised by the IPSASB and others - for example, that the draft Interpretations do not provide authoritative guidance on accounting by grantors and, therefore, it is not clear that consistent accounting policies will be applied in accounting for service concession infrastructure by both the operator and grantor. This approach would ensure that there is symmetry in financial reporting requirements for those service concession arrangements caught within the scope of the IFRIC Interpretation(s).

The IFRIC has indicated its intention to provide in the final Interpretations guidance on which IASs/IFRSs may apply to service concession arrangements falling outside the scope of the Interpretation. Given that IPSASs are based on IFRSs unless there is a public sector reason for a departure, it is likely that that guidance will also be applicable to entities applying IPSASs (with of course the caveat that the applicability of all IASs/IFRSs to the public sector have not yet been considered by the IPSASB and that not all “recent” improvements and revisions to IASs/IFRS are reflected in the IPSASs). Therefore, building public sector guidance on the basis of the Interpretation provides the potential to “cover the field”.

Developing authoritative guidance that mirrors the IFRIC will be particularly relevant for those jurisdictions which adopt IFRSs for private sector entities (or ensure their national private sector standards are harmonized with IFRSs) and adopt the same requirements for the public sector unless there is a public sector reason to differ.

However, such an approach will not deal with concerns identified by respondents about such matters as the notion of control reflected in the draft Interpretations and its interpretation in determining whether the grantor or the operator controls service concession assets, and whether a risks and rewards model (or other model) also has a place in determining which party controls service concession assets. It also does not respond to the view of the IPSASB that service concession arrangements is likely to raise a number of issues that do not fit easily within the current suite of standards and therefore needs to be dealt with in a separate Standard rather than as an interpretation of existing standards.

There is then a case for a more fundamental approach – starting with a basic research project/document which analyses the issues, considers current practice and requirements in a number of jurisdictions, and draws out the implications of existing definitions and concepts of for example, assets and liabilities for dealing with those issues.

Such an approach need not be constrained by interpreting, and applying to service concession arrangements, requirements that are reflected in current standards at the international level or in any particular national jurisdiction. It could also consider the implications of its proposals for accounting by both the grantor and the operator.

The nature of the document to be developed will be dependent on decisions made in respect of issues 3 and 4 above. If authoritative guidance mirroring the IFRIC is to be developed in the short term, then a draft exposure draft or IPSASB guideline or good practice guidance will need to be developed.

If a research type project is to be actioned, a consultation paper could be developed and issued by the IPSASB. That paper could make recommendations and provide input to the

IPSASB (and NSS) as a precursor to the development of authoritative guidance. That paper would not necessarily reflect the views of the IPSASB or the NSS who were involved in the development process – rather it would reflect the views of the authors themselves.

The IPSASB has previously issued consultation papers which encompass: Invitations to Comment (ITCs) developed by steering committees; Studies developed by individual authors; and Research Reports prepared by individuals or subcommittees. In the case of the recently issued consultation paper on heritage assets, the IPSASB issued a paper developed by a NSS after input and comment by an IPSASB subcommittee and with an introduction which explained the nature and role of the paper. None of these papers necessarily reflected the views of the IPSASB, but provided valuable input to the IPSASB process.

Staff View

A broad research project should be actioned and a consultation paper developed by a subcommittee/development group (the PPP subcommittee) comprising IPSASB and NSS members (see issues 6 and 7 below for proposals regarding the PPP subcommittee composition). That paper would not necessarily reflect the views of the IPSASB or the NSS, but would make recommendations to the IPSASB for the development of authoritative guidance. This would provide the best opportunity for developing a harmonized approach in the long term. That project should also consider the implications of the IFRIC approach if symmetrical accounting was to be adopted by the grantor.

While the project would focus on the identification of issues and their resolution in financial reporting by the grantor, it should also draw out the implications of any recommended approaches for financial reporting by the operator. Indeed, there is a case that this project should be responsive to comments made to IFRIC that there is a need to consider both the grantor and the operator in service concession arrangements, and establish its scope accordingly.

Subject to the outcome of that research report, participants could then consider whether they wished to participate with the IPSASB in the development of authoritative international guidance and the process for such development.

IFRIC is responding to the need to put in place in the short term authoritative guidance applicable to private sector operators which are party to service concession arrangements by interpreting existing IASs/IFRSs. It is a practical response to a current need of the IASB's constituents. The establishment of a research project as proposed is a viable mechanism to add value to the process without undermining or endorsing what IFRIC needs to achieve in the short term.

As noted above, the IPSASB consultation paper would not be authoritative and would present the views of the PPP subcommittee rather the boards/organizations of which they are a member. As such, it also provides the opportunity for IASB participation or input in the development process. Such participation would auger well for the future development of authoritative guidance appropriate for both sectors.

- 6 Who will participate and the nature of that participation?**
- 7. How will the project be resourced?**
- 8. How will the project be developed and its timing?**

Again, decisions made in respect of previous issues will influence participant's views on how the project is to be developed and resourced.

All NSS members have the opportunity to participate in the IPSASB due process by commenting on consultative documents and exposure drafts – the IPSASB benefits significantly from this participation. In addition, a number of NSS are represented on the IPSASB, or have strong links with IPSASB members. Involvement in a collaborative process provides the opportunity for those not represented on the IPSASB to input at the early stages of project development and establishes a direct and ongoing link with the NSS on this project. It also enables the IPSASB and other participants to draw on the development work already occurring in individual jurisdictions.

The nature and extent of participation will of course differ dependant on such factors as the nature of the document to be developed, the capacity of NSS to be actively involved in project development, and the priority of the project for individual NSSs.

Participation in a collaborative project could take the form of active participation in the drafting of documents or of commenting on drafts prepared by a development sub-group. In this context, it is anticipated that those NSS which participate in the project will effectively resource the project through the time of their members and staff.

In a number of jurisdictions a discussion paper or series of discussion papers sets the ground work for the development of authoritative guidance. Those NSS which are already actively developing/reviewing their requirements for accounting by grantors in service concession arrangements and are developing relevant material could usefully take a lead roles in the early stages of project development. This would provide some early impetus to the project and be an efficient use of the collective time of IPSASB and NSS members and staff. However, to ensure that this is an effective approach it will be necessary to develop the detailed project brief that will guide the collaborative project and will respond to the concerns of all participants. Such a brief will need to be developed following these discussions and will need to be agreed by those participating in the project.

Staff views

A PPP subcommittee group comprising 3 IPSASB members and approximately 4 members of the NSS would be established to develop the paper. To the extent possible, the PPP subcommittee would be established to ensure its composition represented a broad jurisdictional coverage. The paper would represent the views of the participants of the PPP subcommittee and not necessarily the views of the IPSASB or the NSS of which those participants are members – it is then not a binding document.

The NSS not included on the development group would operate as a project advisory panel (PAP) to the development group.

An IPSASB member would chair the PPP subcommittee and would be responsible to reporting progress to the IPSASB.

A seven member development group is proposed. There is nothing hard and fast about this number. It is proposed in the expectation that it will be too difficult to co-ordinate the active participation of a much larger group, and a good jurisdictional spread would not be achieved by a much smaller group. Three IPSASB members are proposed for membership to allow for input from IPSASB as members of the PPP subcommittee rather than as its chair and to

support continuity of IPSASB participation – it also provides the potential for different IPSASB perspectives to be brought during the development stage.

A designated member of each NSS not actively participating on the PPP subcommittee would form a Project Advisory Panel (PAP) and be provided with all PPP subcommittee materials for comment. PPP subcommittee and PAP members would keep their boards/organizations informed of issues and progress. During development of the paper, drafts will be provided to all IPSASB and NSS members on request.

Different subcommittee operating models may be implemented. For example the PPP subcommittee may meet to review materials prepared by its staff (as was the case in respect of PSC Steering Committees which developed the ITCs), or could conduct its business primarily by electronic means meeting only when and if necessary and convenient. These matters should be developed as the composition of the PPP subcommittee and its objectives becomes clear.

Staff of one NSS member would take the lead in development of the paper. To the extent possible and appropriate it would make use of, and build on, materials in place in PPP subcommittee member jurisdictions and input from there PAP. (It would be useful to draw out at this meeting which jurisdictions have papers already in place and may be useful as base documents for development.)

Staff of the IPSASB and relevant NSSs would act as TAs to the participants on the PPP subcommittee, and would provide input and support to the lead NSS staff as appropriate.

The IPSASB subcommittee monitoring the IFRIC project should be charged with the task of developing a project brief reflecting decisions at this meeting and proposing a model for project development. That project brief would be circulated to all participating NSS for review and agreed by the IPSASB at its November 2006 meeting. It would include a time frame for completion of major milestones in the project.

FOLLOW UP ACTIVITIES

Staff propose the following follow up activities subject to “in-principle” agreement at this meeting to a collaborative approach to the development of a consultation document:

1. Members of the NSS confirm their interest to participate as members of:
 - o The PPP subcommittee; or
 - o The project advisory panel (PAP) to that subcommittee.
2. Members of the NSS consider and advise whether they would be prepared to take the lead in preparing draft papers for review by the PPP subcommittee and PAP. NSS with current papers on PPPs which have been issued or are under development to provide such papers as a resource for the subcommittee, unless confidential.
3. IPSASB members to advise IPSASB chair of their interest in chairing and/or participating in the PPP subcommittee.
4. The IPSASB subcommittee currently monitoring the IFRIC developments (IPSASB - IFRIC subcommittee) prepare a detailed project brief and circulate to NSS members and IPSASB members for comment.
5. The project brief to be revised based on comments received and put to the IPSASB for formal approval in November 2006. Chair of PPP subcommittee, membership of PPP subcommittee and membership of PAP to be confirmed.
6. Following November IPSASB meeting, chair of PPP subcommittee to finalize arrangements for development of project with PPP subcommittee members.

Project Establishment Schedule	
July 2006	IPSASB and NSS agree to action a collaborative project, and establish nature and objectives of project.
August 2006	<p>NSS confirm their interest in participating in project and nature of that participation.</p> <p>IPSASB members advise IPSASB chair of their interest in participation in the development of the consultation paper.</p> <p>IPSASB subcommittee currently monitoring the IFRIC developments (IPSASB - IFRIC subcommittee) develop a draft of a detailed project brief, including proposed timelines for key milestones, and circulate to IPSASB members and NSS members for comment.</p>
October 2006	IPSASB - IFRIC subcommittee revise project brief in consultation with NSS participants.
Nov 2006	IPSASB agree project brief, membership of PPP subcommittee and PPP subcommittee chair.
November/December 2006	PPP subcommittee chair agrees operating procedures with PPP subcommittee members.
2007+	Consultation paper developed and issued. Follow up actions as appropriate.