



April 13, 2016

Memorandum

To: Members of the Board

From: Monica R. Valentine, Assistant Director
Domenic N. Savini, Assistant Director

Through: Wendy M. Payne, Executive Director

Subj: Leases Project – **Tab C**¹

MEETING OBJECTIVES

The objective of this session is to address the issue of service concession agreements in the proposed lease standards.

BRIEFING MATERIAL

- **Staff Memo**
- **Attachment 1: Excerpts: GASB No. 60, *Accounting and Financial Reporting for Service Concession Arrangements***
- **Attachment 2: Excerpts: IPSAS 32, *Service Concession Arrangements: Grantor***

UPDATE

Since the February meeting staff has been following the progress of the GASB lease project and continuing to draft the non-intragovernmental and intragovernmental lease proposal.

¹ The staff prepares Board meeting materials to facilitate discussion of issues at the Board meeting. This material is presented for discussion purposes only; it is not intended to reflect authoritative views of the FASAB or its staff. Official positions of the FASAB are determined only after extensive due process and deliberations.

STAFF ANALYSIS

GASB's Leases exposure draft specifically excludes, "Contracts that meet the definition of a service concession arrangement in paragraph 4 of Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements (SCAs)*." Currently FASAB standards are silent on SCAs.

Through discussions with our task force we know that several federal entities have SCAs. Staff is concerned that the proposed lease definition [*a contract or agreement that conveys the right to use a nonfinancial asset (the underlying asset) for a period of time in an exchange transaction*] could inadvertently scope in SCAs.

Staff believes that there are two notable differences between SCAs and leases:

(1) In an SCA the **transferor** controls the use of the asset, whereas in a lease the **lessee** controls the use of the asset and in an SCA the transferor accrues financial benefits related to the use of the asset, whereas in a lease the lessor **does not** typically accrue financial benefits (beyond any lease payments) related to the use of the asset, and

(2) SCAs are typically based on or significantly incorporate a risk/reward model as opposed to leases which are primarily based on an ownership/control or rights/obligations model(s).

Therefore, consistent with other standards-setters,² staff recommends that the lease standard specifically **exclude** SCAs. To accomplish the exclusion, we should adopt the GASBS 60³ definition of SCA because we do not yet have a federal definition of SCA. Until SCAs are specifically addressed by FASAB in the P3 project's second phase dealing with measurement and recognition staff believes the GAAP hierarchy would aid preparers and auditors in addressing SCA accounting issues. For example, federal entities would look to:

1. upon issuance, SFFAS 49 (Public-Private Partnerships) for guidance concerning disclosures regarding SCAs that also meet the P3 definition,
2. existing FASAB standards on asset and liability measurement and recognition, and

² In addition to GASB excluding SCAs in its Leases guidance, the IASB has also taken the same position in its Leases standard; International Financial Reporting Standard (IFRS) 16 Leases. In its Exposure Draft on Leases, the IASB noted that service concessions were not within the scope of their Exposure Draft primarily because (1) service concession arrangements do not meet their definition of a lease and (2) leases may be but one element in a broader set of agreements with private partners to construct, own, operate and/or transfer assets.

³ The IPSASB definition is presented in Attachment 2. Staff recommends use of the GASB definition because doing so would limit the differences in our lease projects.

3. where appropriate, the concepts statements and/or GASBS 60, *Accounting and Financial Reporting for Service Concession Arrangements*, for additional guidance concerning measurement and recognition.

NEXT STEPS

Staff will revise the non-intragovernmental lease proposal as needed based on the Board discussion and continue to work with the task force to address any issues raised. Staff will also continue to work with (1) the task force on the proposed intragovernmental lease standards and (2) agencies concerning any SCA measurement and recognition issue arising prior to the issuance of specific SCA guidance.

MEMBER FEEDBACK

Please contact staff as soon as possible to convey your questions or suggestions. Communication before the meeting will help make the meeting more productive. You can contact Monica by telephone at 202-512-7362 or by e-mail at ValentineM@fasab.gov and Domenic by telephone at 202-512-6841 or by e-mail at SaviniD@fasab.gov with a cc to PayneW@fasab.gov

The following excerpts are from GASB No. 60, *Accounting and Financial Reporting for Service Concession Arrangements (SCAs)*.

A service concession arrangement is an arrangement between a transferor (entity government) and an operator (governmental or nongovernmental) in which: (1) the transferor conveys to an operator the right and related obligation to provide services through the use of infrastructure or another a public asset (a facility) in exchange for significant consideration and (2) the operator collects and is compensated by fees from third parties. [*GASB 60 – Summary Section*]

A service concession arrangement is a type of public-to-private or public-to-public partnership (P3) and refers to a variety of service arrangements including those possessing management functions that may be associated with the operation of the service arrangement. The terms of an SCA may include payments from the operator to the government sponsor for the right to build, operate, and collect user fees on infrastructure or other public assets and may provide for revenue sharing between the government and the operator during the term of the arrangement. [*GASB 60, Paragraph 1*]

An SCA is an arrangement between a government (the transferor) and an operator¹ in which all of the following criteria are met:

- a. The transferor conveys to the operator the right and related obligation to provide public services² through the use and operation of a capital asset³ (referred to in this Statement as a —facility) in exchange for significant consideration, such as an up-front payment, installment payments, a new facility, or improvements to an existing facility.
- b. The operator collects and is compensated by fees from third parties.⁴
- c. The transferor determines or has the ability to modify or approve what services the operator is required to provide, to whom the operator is required to provide the services, and the prices or rates that can be charged for the services.
- d. The transferor is entitled to significant residual interest in the service utility of the facility at the end of the arrangement.

Footnote 1 - An operator may be a governmental entity (governmental operator) or a nongovernmental entity. References to operators include both governmental and nongovernmental entities. References to governmental operators include only governmental entities.

Footnote 2 - These services relate to the primary function of the facility (for example, operating a city zoo) rather than ancillary services operated in

conjunction with the facility (for example, operating the souvenir stand at a city zoo).

Footnote 3 - A capital asset, as defined in paragraph 19 of Statement No. 34, Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments, includes infrastructure, equipment, and other tangible and intangible assets.

Footnote 4 - The scope of this Statement excludes agency relationships (that is, an arrangement in which an operator accepts payments from third parties and remits those payments to the transferor for an established fee).

[GASB 60 – Paragraph 4]

SCAs include, but are not limited to:

- a. Arrangements in which the operator will design and build a facility and will obtain the right to collect fees from third parties (for example, construction of a municipal complex for the right to lease a portion of the facility to third parties)
- b. Arrangements in which the operator will provide significant consideration in exchange for the right to access an existing facility (for example, a parking garage) and collect fees from third parties for its usage
- c. Arrangements in which the operator will design and build a facility for the transferor (for example, a new tollway), finance the construction costs, provide the associated services, collect the associated fees, and convey the facility to the government at the end of the arrangement. [GASB 60 – Paragraph 5]

Basis for conclusions - The June 2009 Exposure Draft included Alternative Views by some Board members on the accounting for arrangements in which only some control criteria were met. The guidance in the June 2009 Exposure Draft would have required the transferor to derecognize the facility and report a gain or loss upon commencement of the arrangement to reflect a transfer of the facility to the operator if the control criteria were not met. Some Board members disagreed with the resulting total immediate gain or loss recognition. After considering respondent comments, the Board concluded that because the substance of arrangements in which control of the facility is retained by the transferor is sufficiently different from the substance of arrangements in which control shifted to the operator, the scope of the standard should be modified to exclude those arrangements in which control of the facility is not retained by the transferor. The Board believes that those excluded arrangements generally would be reported subject to existing lease accounting requirements.” [GASB 60 BFC – Paragraph 39]

The following excerpts are from *IPSAS 32: Service Concession Arrangements: Grantor*.

A service concession arrangement is a binding arrangement between a grantor and an operator in which:

- (a) The operator uses the service concession asset to provide a public service on behalf of the grantor for a specified period of time; and
- (b) The operator is compensated for its services over the period of the service concession arrangement.

[*IPSAS 32 – Paragraph 8*]

A service concession asset is an asset used to provide public services in a service concession arrangement that:

- (a) Is provided by the operator which:
 - (i) The operator constructs, develops, or acquires from a third party; or
 - (ii) Is an existing asset of the operator; or
- (b) Is provided by the grantor which:
 - (i) Is an existing asset of the grantor; or
 - (ii) Is an upgrade to an existing asset of the grantor.

[*IPSAS 32 – Paragraph 8*]

Application Guidance – Paragraph 8 defines a service concession arrangement.

Common features of a service concession arrangement are:

- (a) The grantor is a public sector entity;
- (b) The operator is responsible for at least some of the management of the service concession asset and related services and does not merely act as an agent on behalf of the grantor;
- (c) The arrangement sets the initial prices to be levied by the operator and regulates price revisions over the period of the service concession arrangement;
- (d) The operator is obliged to hand over the service concession asset to the grantor in a specified condition at the end of the period of the arrangement, for little or no incremental consideration, irrespective of which party initially financed it; and
- (e) The arrangement is governed by a binding arrangement that sets out performance standards, mechanisms for adjusting prices, and arrangements for arbitrating disputes.

[*IPSAS 32 – Paragraph AG3*]