



OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1 100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100

COMPTROLLER

JAN 27 2015

Ms. Wendy M. Payne  
Executive Director  
Federal Accounting Standards Advisory Board  
Mailstop 6H19  
441 G Street, NW, Suite 6814  
Washington, DC 20548

Dear Ms. Payne:

The Department of Defense appreciates the opportunity to comment on the Federal Accounting Standards Advisory Board Public-Private Partnerships Disclosure Requirements Exposure Draft. The proposed definition of Public-Private Partnerships is too broad and can be misconstrued to include instruments that are not Public-Private Partnerships. The requirement to disclose certain remote risks may result in voluminous disclosures easily misinterpreted by readers of the financial statements. The Department concurs with the alternative view proposed by Mr. Dacey as outlined in Paragraphs A31 through A41 in the Exposure Draft.

Responses to specific questions are enclosed. My contact is Ms. Maryla E. Engelking. She can be reached at [maryla.e.engelking.civ@mail.mil](mailto:maryla.e.engelking.civ@mail.mil) or 703-571-1657.

Sincerely,

  
Mark E. Easton  
Deputy Chief Financial Officer

Enclosure:  
As stated

**Department of Defense (DoD) Responses to  
FASAB Questions for Respondents**

Q1. The Board proposes defining the term “public-private partnerships” as shown below:

Federal public-private partnerships (P3s) are contractual arrangements or transactions between public and private sector entities to provide a service or an asset for either government or general public use where in addition to the sharing of resources, each party shares in the risks and rewards of said arrangements or transactions. Sharing of risks and rewards is evidenced by conditions such as (1) agreements covering a significant portion of the economic life of a project or asset, and/or lasting more than five years, (2) financing provided in whole or shared in part by the private partner, (3) conveyance or transfer of real property, personal property, or multi-sector skills and expertise, or (4) formation of special purpose vehicles (SPVs).

**Do you agree or disagree that the P3 definition proposed at paragraph 17 captures the most widely identified features of federal P3s (refer to paragraphs A7 – A9 for a detailed discussion and related explanations)? Please provide the rationale for your answer.**

The DoD disagrees. The proposed definition of P3s is too broad.

- a) The characteristics listed may be representative of some P3s, but could also characterize contracts that are not P3s. For example, the definition could also be used for capital leases.
- b) The inclusion of SPVs also confuses the issue. SPVs are commonly used in a variety of business transactions that have nothing to do with a P3. For example, in a DoD enhanced use lease authorized under Title 10 USC 2667, DoD may out-lease a parcel of underutilized land to a private entity in exchange for the fair market value of the lease. The private entity would likely use a SPV as the legal entity and lessee. No other P3 conditions would exist and there is no risk sharing. The definition should be expanded to state that the federal entity sponsors or is party to the SPV.
- c) The definition can be improved by focusing on the conclusive characteristics for consistency and understanding.
- d) The definition should also state that transactions that are routine or standard in nature should be excluded from this standard.
- e) The definition will be enhanced with the inclusion of examples of arrangements that meet the definition.

Q2. The Board’s proposed definition at paragraph 17 is intended to help identify risk-sharing arrangements or transactions that possess significant risk (that is, fiscal exposure) to the entity. Such arrangements or transactions are commonly referred to as *Public-Private Partnerships* (P3s) but may also be referred to as *Alternative Financing Arrangements* or *Privatization Initiatives*. For example, informal arrangements or transactions that do not share risks or rewards and are solely designed to foster goodwill, encourage economic development, promote research and innovation, coordinate and integrate strategic initiatives, etc., would generally be exempt from applying this Statement. One member has an alternative view that expresses concern that the definition of P3s is not confined solely to P3 arrangements or transactions and is not

sufficiently clear to facilitate consistent application of the standard (refer to paragraphs A31-A41 for the Alternative View).

**a. Do you agree or disagree that the P3 definition helps identify risk-sharing arrangements or transactions that could possess significant risk (that is, fiscal exposure) to the federal reporting entity (refer to paragraphs 17, 18, A7- A9, and A10 - A12 for related comments)? Please provide the rationale for your answer.**

The DoD disagrees.

- a) The definition identifies risks that are related to P3s and non-P3s. Once again, the proposed definition of P3s is too broad and could result in reporting of remote contingent liabilities for non-P3 contracts.
- b) The definition of significant risk is unclear and can lead to inconsistent application.
- c) The definition should directly tie to the conclusive characteristics. For instance, clearly stating that the principal arrangement or transaction is exempt from the Federal Acquisition Regulation (FAR) would enhance the definition.
- d) Current accounting guidance already provides for disclosures of risks and long standing agreements and transactions entered into by the federal government.

**b. Do you agree or disagree that the P3 definition, while capturing P3s based on their most widely identified features, excludes contracts or other arrangements or transactions that are routine in nature and not generally identified as P3s for other purposes (refer to paragraphs 17, 18, A7- A9, and A10 – A12 for related comments)? Please provide the rationale for your answer.**

The DoD disagrees.

- a) The definition as written should include a caveat stating arrangements or transactions that are routine in nature are generally not identified as P3s.
- b) The definition should also include specific exclusions such as those in Paragraph A12.

**c. Are there any features other than those identified in the proposed P3 definition that would assist entities in identifying risk-sharing arrangements or transactions that could possess significant risk (that is, fiscal exposure) to the federal reporting entity (refer to paragraphs 17, 18, A7- A9, and A10 - A12 for related comments)? Please provide the rationale for your answer.**

P3s are contractual relationships with specific terms and conditions of the contract that defines the nature of the services, obligations, and risks for each party. The definition should be more specific in identifying P3s as discussed in responses to previous questions.

**d. The scope of the ED excludes those informal arrangements or transactions that do not share risks or rewards and for example, are solely designed to foster goodwill, encourage economic development, promote research and innovation, coordinate and integrate strategic initiatives, etc. Do you agree with the exclusion? Is it clear what would be excluded by this provision? If not, what features, if any, differentiate them from those arrangements or transactions that do possess significant risk (that is, fiscal exposure) to the**

**federal reporting entity (refer to paragraphs 17, 18, A7- A9, A10 – A12, and A13 – A14 for related comments)? Please provide the rationale for your answer.**

The DoD agrees with the exclusion of informal arrangements or transactions that do not share risks or rewards and are solely designed to foster goodwill, encourage economic development, promote research and innovation, coordinate and integrate strategic initiatives, etc. However, such exclusions should be specifically included in the proposed Standard.

**e. Do you agree or disagree with the one member’s concern that the definition of P3s is not confined solely to P3 arrangements or transactions and is not sufficiently clear to facilitate consistent application of the standard (refer to paragraphs A31-A41 for the Alternative View)? Please provide the rationale for your answer.**

The DoD agrees. The broad definition of P3s could include many activities that are not related to P3s.

Q3. The Board has developed P3 risk-based characteristics (that is, conclusive and suggestive characteristics) to ascertain what P3s, if any, should be considered for disclosure (refer to paragraphs A1 – A6 for related comments). The characteristics apply to all types of P3’s; construction, housing, utilities, military depots, etc. These characteristics may eliminate the need to disclose P3 arrangements/transactions that do not possess significant fiscal exposure(s).

**a. Do you agree or disagree that only those P3s (identified pursuant to the above definition) possessing risk-based characteristics (that is, conclusive or suggestive characteristics) should be subject to the disclosure requirements proposed at paragraphs 21 – 24 (refer to paragraphs A13 – A14 for a detailed discussion and related explanations)? Please provide the rationale for your answer.**

The DoD agrees. Once it is determined that the arrangement is a P3, the disclosures are warranted. However, the risk should be probable and measurable as defined in Statement of Federal Financial Accounting Standards 5, Accounting for Liabilities in the Federal Government. Including remote risks could easily be misinterpreted by the reader of the financial statements.

**b. Do you believe that there are other arrangements or transactions besides P3s for which the risk-based characteristics are present and therefore disclosure should be required? Please provide the rationale for your answer.**

Any other arrangements and transactions are addressed by other FASAB Standards. Additionally, the reporting entity has the ability to include other disclosures in their financial statements if they deem it necessary.

**c. Do you believe that when the final Statement becomes effective, the entities with which you are associated have P3s that are subject to disclosure pursuant to the proposed requirements (refer to paragraphs A1, A4, A6(a), A10 – A12 for a detailed discussion and related explanations)? Please provide the rationale for your answer.**

There will be some activities within the DoD that will require disclosure. One such program is the Military Family Housing Privatization Initiative.

Q4. The Board proposes that the P3 risk-based characteristics be categorized as either: conclusive characteristics - where answering – “Yes” to any one characteristic means the P3 arrangement or transaction should be considered for disclosure; or suggestive characteristics - where answering "Yes" to any one suggestive characteristic suggests that the P3 arrangement or transaction may be subject to disclosure but that preparers consider suggestive characteristics in the aggregate before reaching a final decision. Each conclusive characteristic is meant to be definitive whereas each suggestive characteristic will require entity judgment as each one is analyzed in connection with the other suggestive characteristics. The conclusive and suggestive characteristics are presented at paragraphs 19 to 20 and more fully discussed at paragraphs A15 – A16.

**Do you agree or disagree with the risk-based characteristics, their related classification as either conclusive or suggestive, and their proposed application at paragraphs 19 and 20 (refer to paragraphs A15 – A16 for a detailed discussion and related explanations)? Please provide the rationale for your answer.**

The DoD agrees. The conclusive characteristics in and of themselves identify P3s. Although utilizing the conclusive characteristics may result in disclosing arrangements that are not P3s given the way P3s are defined.

Q5. The Board proposes the following component reporting entity disclosures:

- a. The purpose, objective, and rationale for the P3 arrangement or transaction and the relative benefits/revenues being received in exchange for the government's consideration, monetary and non-monetary, and the entity's statutory authority for entering into the P3.
- b. The mix and amount of funding, federal and non-federal, used to meet mission requirements and service delivery needs to support the P3.
- c. The operational and financial structure of the P3 including the entity's rights and responsibilities, including:
  - i. A description of the contractual terms governing payments to and from the government over the life of the P3 arrangement or transaction to include:
    1. in-kind contributions/services and donations,
    2. the time periods payments are expected to occur, and
    3. whether payments are made directly to each partner or indirectly through a third-party, such as, military housing allowances.
  - ii. The amounts received and paid by the government during the reporting period(s) and the amounts estimated to be received and paid during each of the succeeding five years and in aggregate over the life of the P3.

- d. Identification of the significant contractual risks the P3 partners are undertaking that could materially change the estimated cash flows, including a description of (1) the risk and (2) the potential effect on cash flows if the risks were realized (for example, early termination requirements including related exit amounts and other responsibilities such as asset condition (hand-back) requirements, minimum payment guarantees, escalation clauses, contingent payments, renewal options, etc.).
- e. As applicable:
- i. Associated amounts recognized in the financial statements such as gains or losses and capitalized items.
  - ii. Significant instances of non-compliances with legal and contractual provisions governing the P3 arrangement or transaction.
  - iii. Whether the private partner(s), including any Special Purpose Vehicle (SPV), have borrowed or invested capital contingent upon the entity's promise to pay whether implied or explicit.
  - iv. Description of events of termination or default.

**Do you agree or disagree with the component entity report disclosures proposed at paragraph 23 (refer to paragraphs A25 – A27 for a detailed discussion and related explanations)? Please provide the rationale for your answer.**

The DoD agrees in concept. However, in practice, the disclosures may be difficult to apply consistently in all situations.

- a) The disclosures are very detailed and will be burdensome for preparers and overwhelming for readers.
- b) Disclosures relating to private, related-party transactions may need to be added to the required disclosures. These disclosures may be deemed as proprietary to the private partner. The private partner may not agree to reveal proprietary information.

Q6. The Board believes that significant P3 risks, including those that may be deemed remote should be disclosed. One member has an alternative view that expresses concern that (1) disclosure of remote contingencies is not limited to the terms of contractual arrangements, (2) the concept of “significant exposure” is not sufficiently clear to result in consistent disclosures, and (3) risks related to entity operations or performance (referred to in the Alternative View as business risks) would be included in the risk disclosures (refer to paragraphs A31-A41 for the Alternative View). The Board’s position is as follows:

*Consideration should be given to those risks that management does not expect to be likely, but represent a significant exposure to the government if they were to occur. With this being said, the Board also notes that such remote risks may have a reasonably high materiality threshold. As such, remote risks should not be dismissed from disclosure without further consideration of user needs and the qualitative and quantitative characteristics when applying materiality.*

**a. Do you agree or disagree with the Board’s position as stated above and included at paragraph A24 (refer to paragraphs A22 – A24 for a detailed discussion and related explanations)? Please provide the rationale for your answer.**

The DoD disagrees. Reporting remote risks expands the requirements currently espoused in Statement of Federal Financial Accounting Standards 5, Accounting for Liabilities in the Federal Government. These disclosures, although remote, could be misinterpreted by readers of financial statements as being possible or probable to occur. If these disclosures are to be required, they must be labeled as remote to avoid being misleading. Finally, this requirement may result in voluminous disclosures that may be easily misconstrued by the reader.

**b. Do you agree or disagree with the one member’s concern that (1) disclosure of remote contingencies is not limited to the terms of contractual arrangements, (2) the concept of “significant exposure” is not sufficiently clear to result in consistent disclosures, and (3) risks related to entity operations or performance (referred to in the Alternative View as business risks) would be included in the risk?**

The DoD agrees. The disclosure of remote contingencies is not limited to the terms of contractual arrangements and would include business risks. The term “significant exposure” needs to be defined in order for it to be applied consistently across the Federal Government.

Q7. The Board proposes that due to the relative complexity and potentially large number of P3s that an entity might be party to, the proposed disclosures would permit entities to provide broad summarized information instead of individual arrangement or transaction detail. For example, disclosures of P3 arrangements or transactions could be grouped by an entity’s strategic objectives, departmental or bureau categorizations, program budget classifications, etc. In this way, users are presented with information that is comprehensive and material to an entity’s financial statements without placing an undue burden on preparers to provide P3 specific or granular level information.

**Do you agree or disagree that entities should be permitted to aggregate or group disclosures as proposed at paragraph 21 (refer to paragraphs A28 – A29 for a detailed discussion and related explanations)? Please provide the rationale for your answer.**

The DoD agrees. The reporting entities are given the option of aggregating P3s or reporting them separately. In most cases, P3s are material individual contractual arrangements and will be reporting separately. Aggregation may make it even more difficult for financial statement users to determine the nature and extent of these arrangements, but it should be made available for P3s below materiality thresholds.

Q8. The Board encourages respondents to not only provide input concerning any and all aspects of the proposed changes, including whether concepts are sufficiently clear and the proposed effective date, but also other matters which may not have been specifically addressed in this exposure draft. In addition, the basis for conclusions explains the Board’s goals for this project (see comments beginning at paragraph A1) and also discusses other issues raised by task force members as well as experts and practitioners both within and external to government (as an

example, see paragraphs A4 through A6). Respondents are asked to particularly note the Alternative View beginning at Paragraph A31.

**Please provide any comments or suggestions you have regarding the goals for this project, other issues identified in the basis for conclusions, or areas which have not been addressed.**

After much research, P3s pose issues and questions for both the private and public sectors. By hiding liabilities in partnerships or other similar arrangements, there were cases when countries were able to meet requirements (i.e., debt as a percentage of GNP) that allowed them to meet financing agreements with international agencies. However, a concern is if a contractor fails to perform, the government will have to step in to provide these services. Although there may be remedies that could be pursued, it is likely it will not cover the full cost of the failed project and the government and taxpayers will carry the burden of paying the bill. The disclosures in financial statements will not change this fact. Although we agree in concept with this approach, this disclosure will be challenging to apply uniformly.

Another concern is the potential difference of opinion between the reporting entity and their auditor as to whether a disclosure is sufficient or whether a contingent liability should be recorded for the financial risks of a P3 arrangement. Also, the P3 definition is too broad and can lead to disagreements between management and auditors on the scope of the entity's disclosure requirements. The Exposure Draft did not provide sufficient detail to allow federal financial management and the audit communities to agree on the necessary disclosures required to achieve the reporting objectives of the standard. Further explanation may be required of paragraph 23(b), "The mix and amount of funding, federal and non-federal used to meet mission requirements and service delivery needs to support the P3." Is this cumulative, prospective, or just the mix/amount of funding associated with the reporting years? FASAB may need to provide examples or additional requirements related to paragraph 23(b).

More detail will be required to explain risk sharing and DoD may need additional guidance for disclosures or financial transactions when a default or decrease in public interest in the asset occurs. Finally, how does the P3 definition compare and contrast with contract financing payments for major efforts with private entities?

The following terms within the Exposure Draft warrant clarification and/or definitions:

- a) Long-lived asset
- b) Remote risk
- c) Significant exposure

An appendix should be added to the standard providing disclosure examples to aid preparers in developing the necessary and consistent disclosures. More examples are needed indicating what is included and what is excluded from the definition of P3s so that the non-accountant (functional community) tasked with providing financial information on business operations can fully comprehend and understand the requirement and how it relates to current operations.