



August 15, 2013

Memorandum

To: Members of the Board
From: Domenic N. Savini, Assistant Director

Wendy M. Payne

Through: Wendy M. Payne, Executive Director

Subject: **Project Update: Public-Private-Partnerships (P3)¹ – Tab D**

OBJECTIVE

The objective of this session is to seek **Board input** concerning progress made on the project since our June meeting. Specifically, the following **three matters will be discussed**:

- a suggested draft P3 definition/description,
- P3-Centric Reporting Characteristics, and
- Fiscal Exposure (risk) disclosures.

BRIEFING MATERIAL

You may electronically access all of the briefing material at <http://www.fasab.gov/board-activities/meeting/briefing-materials/>.

BACKGROUND

At the June 2013 meeting Board members broadly focused on several issues affecting both approach and scope to the project. Members primarily focused on the following matters: (1) the relationship of the P3 project to the Risk Assumed project, (2) the finance/financial component of P3s, and (3) the potential P3-Centric reporting characteristics.

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.

Although members generally supported the direction of the project in identifying and disclosing P3 fiscal exposure (risks), they agreed to await further development of the potential P3-Centric reporting characteristics and asked staff to simplify their presentation so that the potential for increased fiscal exposure/risk can be more readily apparent.

Members stated that P3s are in essence alternative financing arrangements and that a major concern deals with an agency's off-budget and off-balance sheet borrowing or incurrence of debt, respectively. Members also agreed that fiscal exposure (risk) is a concern that we need to address; specifically noting their interest in the quantitative reporting of fiscal exposure (risk).

In addition, members suggested that staff specifically link each potential P3-Centric reporting characteristic to its associated risk and note whether the characteristic's existence should result in disclosure of qualitative and/or quantitative information.

Staff noted that the next steps of the project included finalizing the P3-Centric reporting characteristics and further evaluation of the 17 major P3 accounting practice issues. Staff reassured members that recognition matters were intended to be worked concurrently with other aspects of the project.

As a result, the Board deferred specific decisions on other aspects of the project, including pursuing guidance to address the identified 17 major accounting practice issues, pursuing technical bulletins to address P3s that are in essence long-term leases, and determining whether the P3-Centric reporting characteristics to identify reportable P3s are appropriate.

During the meeting the Chairman stated that a significant value he sees arising from this project is in assisting and guiding preparers to the applicable accounting literature when reporting on P3 arrangements/transactions.

MEMBER FEEDBACK

If you require additional information or wish to suggest another alternative not considered by staff, please contact staff as soon as possible. In most cases, staff would be able to respond to your request for information and prepare to discuss your suggestions with the Board, as needed, in advance of the meeting. If you have any questions or comments prior to the meeting, please contact me by telephone at 202-512-6841 or by e-mail at savinid@fasab.gov with a cc to paynew@fasab.gov.

Thank you.

Attachment 1: User Information Needs: An Interview with a Mayor

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Suggested Draft P3 Definition/Description

Suggested Draft P3 Definition/Description

Although Board members did not object to staff's overall project approach, members were concerned with how any forthcoming disclosure requirements would be practically applied without having a P3 definition or description in place.

As a result, in consultation with the P3 Task Force, staff has developed the following suggested draft P3 definition/description:

Federal public-private partnerships (P3s) are contractual² arrangements or transactions between public and private sector entities to deliver a service or an asset for either government or general public use which allows for more private sector participation than is traditional.³ As a result, federal P3s can (1) fall outside typical federal contracting policies and guidelines, (2) be highly complex and sophisticated risk-transfer systems where in theory risks are allocated⁴ to the party which is best able to manage them, and (3) include the formation of consortiums often called special purpose vehicles or SPV's. Through these arrangements or transactions, the partners typically share resource⁵ such as real and personal property, multi-sector skills and expertise, and financial⁶ as well as risks and rewards⁴ to deliver desired policy outcomes.

The above definition captures the most widely identified features of federal P3s and many arrangements will likely meet this definition. P3s should be assessed against the conclusive and suggestive characteristics presented below to identify those subject to these disclosure requirements.

The above draft language attempts to cover the key elements and points embodied in various other P3 definitions which immediately follow on the next page. The intent is to craft and develop a working, but yet malleable, P3 definition/description early-on in the project that the Board can later refine as additional points arise during our work. Once final, the definition will become part of the standards.

² GAO Office Glossary, April 1999.

³ U.S. Dept. Transportation Report to Congress on P3s. December 2004.

⁴ PWC - Delivering the P3 Promise. November 2005.

⁵ The National Council for P3's.

⁶ S&P - P3 Credit Survey. 2005

Various Definitions for Public-Private-Partnerships

Various Definitions for Public-Private-Partnerships

<u>Organization</u>	<u>Definition or Description</u>
1. The National Council for Public-Private Partnerships http://www.ncppp.org/howpart/index.shtml#define	A Public-Private Partnership (PPP) is a contractual agreement between a public agency (federal, state or local) and a private sector entity. Through this agreement, the skills and assets of each sector (public and private) are shared in delivering a service or facility for the use of the general public. In addition to the sharing of resources, each party shares in the risks and rewards potential in the delivery of the service and/or facility.
2. General Accountability Office Glossary GAO/GGD-99-71, April 1999	Under a public-private partnership, sometimes referred to as a public-private venture, a contractual arrangement is formed between public and private-sector partners. These arrangements typically involve a government agency contracting with a private partner to renovate, construct, operate, maintain, and/or manage a facility or system, in whole or in part, that provides a public service. Under these arrangements, the agency may retain ownership of the public facility or system, but the private party generally invests its own capital to design and develop the properties. Typically, each partner shares in income resulting from the partnership. Such a venture, although a contractual arrangement, differs from typical service contracting in that the private-sector partner usually makes a substantial cash, at-risk, equity investment in the project, and the public sector gains access to new revenue or service delivery capacity without having to pay the private-sector partner.
3. U.S. Department of Transportation Report to Congress on Public-Private Partnerships www.fhwa.dot.gov/reports/pppdec2004/pppdec2004.pdf Similar December 2004	A contractual agreement formed between public and private sector partners, which allows more private sector participation than is traditional. The agreements usually involve a government agency contracting with a private company to renovate, construct, operate, maintain, and/or manage a facility or system. While the public sector usually retains ownership in the facility or system, the private party will be given additional decision rights in determining how the project or task will be completed. The term public-private partnership defines an expansive set of relationships from relatively simple contracts (e.g., A+B contracting), to development agreements that can be very complicated and technical (e.g., design-build-finance-operate-maintain). In the context of this report, the term public-private-partnership is used for any scenario under which the private sector would be more of a partner than they are under the traditional method of procurement. Further, the broad definition used for public-private partnerships includes many elements that are applied fairly regularly on appropriate projects.

Various Definitions for Public-Private-Partnerships

<u>Organization</u>	<u>Definition or Description</u>
4. General Service Administration January 2012	An agreement between a public and private sector entity in which a private entity would provide the investment and expertise to develop or renovate property for government use. The private entity assumes development risk; in almost all cases, the public sector ends up owning developed real estate, significantly reducing leasing costs over the long term.
5. Congressional Budget Office, H.R. 2573 Cost Estimate, Public Private Partnership Act of 2003 http://www.cbo.gov/doc.cfm?index=4632&type=0 October 15,2003	Most of the projects undertaken by these agencies have involved forms of project financing. Project financing is backed by the cash flows or asset value of a particular economic unit or asset rather than the financial resources of the owner, operator, or sponsor. Project financing typically involves a series of contracts and agreements that serve two functions: creating an entity that will act on behalf of the sponsors to implement the project (including obtaining financing) and protecting lenders from the credit risk associated with the project's development or operations. Many of the government projects financed by the private sector have made a federal agency the sole or primary beneficiary of a special-purpose entity (SPV) that is created to implement the project. Agencies usually have retained significant control over the decisions made by the SPV, including the project development and management agreements. The SPVs associated with previous federal projects have taken different legal forms, including trusts and limited-liability companies, some of which involve direct government ownership. Most projects have been rated as investment grade by credit rating firms, largely because of their strong federal support. The types of commitments backing the cash flow of federal projects have varied, ranging from explicit obligations (e.g., lease or purchase agreements) to indirect measures that mitigate the credit risk (e.g., covenants or economic incentives for an agency to voluntarily extend its use of an asset). CBO has concluded that many of the projects characterized as public-private ventures involve significant government control and use, and therefore, should be treated in the budget as governmental entities.

Various Definitions for Public-Private-Partnerships

<u>Organization</u>	<u>Definition or Description</u>
6. Standard & Poor's PPP Credit Survey 2005	Any medium-to-long term relationship between the public and private sectors, involving the sharing of risks and rewards of multi-sector skills, expertise and finance to deliver desired policy outcomes.
7. PriceWaterHouseCoopers, Delivering the PPP promise: A review of PPP issues and activity. November 2005	The term “public-private partnership” (“PPP”) has been in general use since the 1990s. However, there is no widely agreed, single definition or model of a PPP. Different types of PPPs tend to share some common characteristics. These include contracting between the public and private sectors for the delivery of services, often involving infrastructure development and management, where risks are shared between the parties. Risks are allocated to the party which is best able to manage them, i.e. reduce their impact and/or absorb their consequences. Appropriate risk allocation should therefore minimize the cost of risks. The need to utilize private sector management and experience, and not only the capability of raising finance, is also key.

P3-Centric Reporting Characteristics

P3-Centric Reporting Characteristics

As noted in our suggested draft P3 definition/description, P3s share certain features but are diverse. We believe some common characteristics can be used to identify P3s that create fiscal exposure such that more information should be disclosed.

The following P3-Centric Reporting Characteristics have been developed and categorized by the P3 Task Force from its initial comprehensive list of characteristics that distinguish P3s from traditional procurements. Such characteristics are intended to apply to all types of P3s: construction, housing, utilities, military depots, etc. Also, these characteristics are intended to assist a federal entity in ascertaining which P3 arrangements or transactions should be considered for disclosure. Once a P3 is identified for disclosure consideration, such arrangements or transactions would then be evaluated in light of the entity's materiality considerations, e.g., threshold(s).

Specifically, the following characteristics should be applied to assist a federal entity in determining which P3 arrangements or transactions may be eliminated from disclosure requirements, i.e., no disclosure is required if the P3: (1) does not result in an asset or liability recognition or de-recognition by any P3 party; or (2) poses little or no fiscal exposure (risk) that could lead to a loss or a liability for any P3 party.

As a result, staff suggests that we categorize the characteristics as:

- **Conclusive characteristics** where answering "Yes" to any 1 characteristic means the P3 arrangement or transaction must be considered for P3-Centric disclosures; and
- **Suggestive characteristics** where answering "Yes" to any 1 characteristic suggests that the P3 arrangement or transaction should be disclosed but that this 1 characteristic must be considered in the aggregate with all other Suggestive characteristics before a decision to consider the P3 for P3-Centric disclosures is reached.

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 characteristics in the suggestive category.

If a P3 arrangement or transaction is identified for potential disclosure they should be further evaluated in light of materiality considerations that include both qualitative and quantitative assessments in determining the information that should be presented regarding P3 arrangements or transactions.

The following page presents this approach in the form used for Standards to clarify the intent. Following the example language, a table explains how each characteristic relates to fiscal exposure (risk).

P3-Centric Reporting Characteristics

Example of what a draft Exposure Draft could contain follows:

Definition of Public-Private Partnerships

8. Federal public-private partnerships (P3s) are contractual arrangements or transactions between public and private sector entities to deliver a service or an asset for either government or general public use which allows for more private sector participation than is traditional. As a result, federal P3s can (1) fall outside typical federal contracting policies and guidelines, (2) be highly complex and sophisticated risk-transfer systems where in theory risks are allocated to the party which is best able to manage them, and (3) include the formation of consortiums often called special purpose vehicles or SPV's. Through these arrangements or transactions, the partners typically share resource such as real and personal property, multi-sector skills and expertise, and financial as well as risks and rewards to deliver desired policy outcomes.
9. The above definition captures the most widely identified features of federal P3s and many arrangements will likely meet this definition. P3s should be assessed against the conclusive and suggestive characteristics presented below to identify those subject to these disclosure requirements.

Identification of P3's Requiring Disclosure

10. If any one of the following Conclusive Characteristics is met, the P3 arrangement or transaction must be considered for P3-Centric disclosure.

Conclusive Characteristics
1. Has the arrangement resulted in the conveyance or creation of an asset or liability?
2. Is the federal entity a party to an arrangement wherein the private sector partner or special purpose vehicle (SPV) has either borrowed or invested capital contingent upon the entity's promise, whether implied or explicit, to make future payments?
3. Does the federal entity participate in or help sponsor an SPV, partnership, trust, etc.?
4. Is the principal arrangement exempt from the Federal Acquisition Regulation (FAR) or other comparable laws, regulations or provisions preserving and protecting the government's rights?
5. Is the term of the procurement or contract arrangement longer than 5 years?

P3-Centric Reporting Characteristics

11. While meeting one of the Suggestive Characteristics implies there is some persuasive evidence that a P3 should be disclosed, each characteristic must be considered in the aggregate with the other Suggestive characteristics before a final decision to consider for P3-Centric disclosure is reached. Each Conclusive characteristic is definitive whereas each Suggestive characteristic will require entity judgment as each one is analyzed in connection with the other characteristics in the Suggestive category. If P3 arrangements or transactions are identified for potential disclosure, they should be further evaluated in light of the entity's materiality considerations; e.g., threshold.

Suggestive Characteristics

1. Is a value for money or other similar cost-benefit analysis performed?
2. Is the principal arrangement NOT managed by an Administrative Contracting Officer (ACO) and/or Procurement Contracting Officer (PCO)?
3. Is the consideration or items given up in an arrangement not readily apparent?
4. Are significant work force duties, activities, or knowledge cross-shared between public and private sector P3 parties?
5. Is the focus more on collaboration and informal, real-time, resolution processes as opposed to formal, contractual, administrative processes?
6. Do operational performance metrics exist absent strategic milestone metrics?
7. Are separate payments, as opposed to a unitary payment, made to the private sector partner?
8. Does the government rely on either the private sector partner's or a third party's determination of a P3's performance or return on investment/equity, without performing its own verification of performance/return on investment/equity?

P3-Centric Reporting Characteristics

#	Conclusive Characteristics	Fiscal Exposure (Risk) Rationale Implication
1.	Has the arrangement resulted in the conveyance or creation of an asset or liability?	<p>Not all P3s result in the conveyance or construction of an asset. However, in those that do, the government's risk may be significantly increased because of costs that often accompany asset ownership or control. Further, some private partners may incur substantial liabilities in preparation for delivering services even if an asset is not created.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> those P3's where an asset is either conveyed or constructed in order to execute mission because of the inherent costs of ownership/control that (1) the government may absorb and (2) the risk-sharing nature of P3s as exhibited by numerous and complex agreements that "allocate" asset ownership/control risks to the party best able to manage them. Some believe that the government is the party best able to manage all P3 risk and that this alone requires increased disclosure; i.e., potential for moral hazard. Those P3s where the private partner incurs a liability may impose a moral hazard – that is, the government must remain in the partnership to ensure the liabilities are met.
2.	Is the federal entity a party to an arrangement wherein the private sector partner or special purpose vehicle (SPV) has either borrowed or invested capital contingent upon the entity's promise, whether implied or explicit, to make future payments?	<p>MR. GRANOF: In agreement with Mr. Showalter, Mr. Granof noted that experience with State and local government confirms that P3s are borrowing arrangements. In his opinion, there's no question that P3s are in fact alternative financing mechanisms.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> the fact that the SPV is nothing more than an indirect funding mechanism, not recognizing the amount of an agency's explicit or implicit long-term debt or promise to pay the SPV because of the form of the arrangement.
3.	Does the federal entity participate in or help sponsor an SPV, partnership, trust, etc.?	Entities such as SPVs, partnerships, trusts, etc., can be established for a variety of strategic and/or tactical reasons. Generally speaking, they are commonly considered risk-containment vehicles and are more often than

P3-Centric Reporting Characteristics

#	Conclusive Characteristics	Fiscal Exposure (Risk) Rationale Implication
		<p>not, purposefully kept off of budgets and balance sheets.</p> <p>Several federal agencies have entered into P3 arrangements that use SPVs, etc, to execute mission.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> 1. an agency's participation representing either an explicit or implicit guarantee of the P3s performance and/or profitability, and 2. external pressures (e.g., economic, societal, political, etc.) that could create fiscal exposure beyond the agency's legal obligation or duty.
4.	Is the principal arrangement exempt from the Federal Acquisition Regulation (FAR) or other comparable laws, regulations or provisions preserving and protecting the government's rights?	<p>The FAR is the primary regulation for use by all Federal Executive agencies in their acquisition of supplies and services with appropriated funds. The FAR is part of an administrative framework that includes procurement and legal requirements to help safeguard and protect taxpayer dollars. Many if not most of the terms and conditions contained at FAR Part 52 have been tried and tested in various agency tribunals over the past 50 years. For example, the Armed Services Board of Contract Appeals (ASBCA) established in 1962 is an administrative tribunal that hears claims arising from contracts between civilian providers of goods and services and agents of the United States military. A civilian agency version of the ASBCA also exists for disputes between contractors and executive agencies such as the Departments of State, Treasury, Commerce, and Education.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> 1. because P3s are often operating without a uniform administrative framework in place, any agency P3 that is exempt from FAR is at an increased-risk because well-established safeguards and contract resolution mechanisms are abandoned in favor of substitute contract terms and conditions and/or alternate contract dispute resolution venues.
5.	Is the term of the procurement or contract	In order for a P3 to be financially lucrative to the private partner while also securing performance efficiencies and lower cost of financing for the

P3-Centric Reporting Characteristics

#	Conclusive Characteristics	Fiscal Exposure (Risk) Rationale Implication
	arrangement longer than 5 years?	<p>government sponsor, arrangements are longer than usual; ranging anywhere from 25 to 99 years. From a procurement point of view, any procurement or P3 arrangement greater than 5 years is considered to be longer than usual.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none">1. those P3 procurement or contract arrangements greater than 5 years because there is often no re-procurement or re-negotiation opportunity for the agency. As a result, changed conditions that could warrant a fair and reasonable re-negotiation or re-competition cannot be exercised and increased costs that would otherwise be avoided are incurred for the duration of the arrangement.

P3-Centric Reporting Characteristics

#	Suggestive Characteristics	Fiscal Exposure (Risk) Rationale Implication
1.	Is a value for money or other similar cost-benefit analysis performed?	<p>Because the term VfM is almost always used in connection with P3 arrangements, if an entity conducts a VfM it is likely that the project in question is a P3. VfM's are typically more subjective than traditional cost-benefit analyses and are sometimes done ex-post facto. In order not to exclude VfM analyses by another name or cost-benefit analyses that incorporate qualitative "value" analysis, staff advises that we refer to "other similar cost-benefit analysis performed."</p> <p>Additionally, due to the potential complexity of these analyses, entities would probably only perform them on their more important or sensitive programs.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> 1. the inherent details of the underlying P3 business model and, 2. the VfM analysis itself because VfM analyses are broader in scope emphasizing qualitative factors as opposed to the more traditional quantitatively based cost-benefit analyses most often performed.
2.	Is the principal arrangement NOT managed by an Administrative Contracting Officer (ACO) and/or Procurement Contracting Officer (PCO)?	<p>Typically, when a contract is awarded under the FAR, the procuring organization has an independent administrative contracting officer administer and manage aspects of the contract to ensure contract compliance. This activity can be either assigned to an Administrative Contracting Officer (ACO) who is usually external to the procuring organization or delegated internally to a Procurement Contracting Officer (PCO). In some cases dual-administration will occur. However, if an entity does not delegate administration responsibility to any contracting officer and retains administration internally, there may be less objectivity and independence in ensuring that contract requirements are adhered to.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> 1. those cases where contract non-compliances may result in increased costs or fiscal exposure to the government as a result of less objective and/or independent contract monitoring.

P3-Centric Reporting Characteristics

#	Suggestive Characteristics	Fiscal Exposure (Risk) Rationale Implication
3.	Is the consideration ⁷ or items given up in an arrangement not readily apparent?	<p>Generally under common law consideration from both parties is required in order to have what constitutes as a binding contract. Because P3s are often extremely complex risk-transfer or risk-sharing arrangements, consideration may not always be apparent or easily identified. Some courts have ruled that in those cases where the exchange appears excessively one sided, no quid-pro-quo exists and the contract may be void by law.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> those cases where consideration from either party is not readily apparent that could lead to recourse or remedies that have adverse financial ramifications to the agency.
4.	Are significant work force duties, activities, or knowledge cross-shared between public and private sector P3 parties?	<p>As military depots face under-utilization and skill retention issues, with Congressional approval, many depots have begun entering into P3 arrangements to put both infrastructure and government personnel to heightened work. However, there is a concern that the analyses (e.g., Value for Money) used to justify these arrangements may be skewed resulting in a transfer of activities and/or knowledge to the private partner that would otherwise be done as efficiently and at less cost if the activities were retained by government personnel.</p> <p>Therefore, the risk rests in:</p>

⁷ **Consideration defined** - “Something of value **given by both parties** to a contract that induces them to enter into the agreement to exchange mutual performances. Consideration is an essential element for the formation of a contract. It **may consist of a promise to perform a desired act or a promise to refrain** from doing an act that one is legally entitled to do. **In a bilateral contract**—an agreement by which **both parties exchange mutual promises**—each promise is regarded as sufficient consideration for the other. **In a unilateral contract**, an agreement by which **one party makes a promise in exchange for the other's performance**, the performance is consideration for the promise, while the promise is consideration for the performance. **Consideration must have a value that can be objectively determined**. A promise, for example, to make a gift or a promise of love or affection is not enforceable (*You better ask my better-half what she thinks about this “bright” idea*) because of the subjective nature of the promise.” (**Bolding** added for emphasis and *italics* added for some light-hearted humor and to see who is paying attention!) Source: <http://legal-dictionary.thefreedictionary.com/consideration>

P3-Centric Reporting Characteristics

#	Suggestive Characteristics	Fiscal Exposure (Risk) Rationale Implication
		<p>1. in those cases where significant work force duties, activities or knowledge is cross-shared under a skewed VfM that did not include all the personnel or legacy costs. Because such costs were not identified or considered, the government is left absorbing them with no related activity base, and</p> <p>2. potential liabilities arising from union and/or employee litigation.</p>
5.	Is the focus more on collaboration and informal, real-time, resolution processes as opposed to formal, contractual, administrative processes?	<p>Due to their very nature P3 arrangements involve risk-sharing and in some cases, issues such as contract disputes are resolved informally. However, such informal resolution processes could lead to potential liability when contracting, procurement, or legal personnel are not involved.</p> <p>Therefore, the risk rests in:</p> <p>1. the potential liability arising from informal resolution of what otherwise would require more formal contractual administrative processes.</p>
6.	Do operational performance metrics exist absent strategic milestone metrics?	<p>The presumption is that strategic milestones are best used to monitor project and/or partner performance when the private partner has in fact assumed responsibility and related risk over a given area. However, an indicator that greater agency risk still exists in a given area (either at the inception of the P3 agreement or assumed by the agency at a later date) is when an agency employs operational performance metrics <u>absent</u> strategic milestone metrics. For example, this could imply that the agency has retained a certain type of volatile risk or a significant amount of risk that warrants fairly close agency monitoring at an operational or granular level.</p> <p>Therefore, the risk rests in:</p> <p>1. those cases where an agency uses operational performance metrics absent strategic milestone metrics. Such a condition could point to increased risk volatility or a significant amount of risk retained or assumed by the agency.</p>
7.	Are separate payments, as opposed to a unitary payment, made to the private sector partner?	<p>The presumption is that unitary (i.e., single or lump-sum) payments are best used to monitor project and/or partner performance when the private partner has in fact assumed responsibility and related risk over a given area. However, an indicator that greater agency risk exists (either at the inception of the P3 agreement or assumed by the agency at a later date) is when an agency</p>

P3-Centric Reporting Characteristics

#	Suggestive Characteristics	Fiscal Exposure (Risk) Rationale Implication
		<p>employs separate payments. Using separate payments could imply that the agency has retained a certain type of volatile risk or a significant amount of risk that warrants fairly close agency monitoring at a granular billing level.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> 1. those cases where an agency uses separate payments to monitor project and/or partner performance. Such a condition could point to increased risk volatility or a significant amount of risk retained or assumed by the agency.
8.	Does the government rely on either the private sector partner's or a third party's determination of a P3's performance or return on investment/equity, without performing its own verification of performance/return on investment/equity?	<p>Agencies often rely on 3rd party experts to assist in performing VfM and/or cost-benefit analyses, return-on-equity calculations, asset appraisals, risk-transfer analyses, etc. However, it has been noted both at the federal and state level that conflicts of interest often exist because there are only a few firms who practice in this highly sophisticated area. As a result, some firms have benefitted on both ends of the P3 arrangement by providing advisory services to both the private partner and government. In addition, fees are often based on the dollar volume of the arrangement creating what some believe are self-serving incentives.</p> <p>Therefore, the risk rests in:</p> <ol style="list-style-type: none"> 1. those P3 arrangements where an agency does not or cannot perform its own independent analysis thus <u>relying solely</u> on either the private partner or a third party determination of a P3's performance or return on investment/equity without performing its own verification. Such analyses may belie the actual risk or fiscal exposure the government has or will incur.

Disclosures - Fiscal Exposure (Risk)

Disclosures - Fiscal Exposure (Risk)

General Approach to Disclosures⁸ - Narrative & Quantitative

In addressing disclosures staff recommends following a similar approach used in the *Federal Entity Exposure Draft*.⁹ However, due to the relative complexity and potential voluminous nature of P3s that an entity might be party to, the disclosures would permit entities to provide broad and summarized information instead of unique or discrete 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.

Specifically, the disclosures would reveal (1) the nature of the P3 arrangements or transactions; (2) relevant P3 activity during the reporting period, (3) the SPV's created, if any, to execute mission and their relationship to the reporting entity, and (4) the reporting entity's future fiscal exposures to risks and rewards resulting from the P3 relationships.

Factors in Determining Disclosures – Materiality and Some Others

Materiality - As is the custom, P3 disclosures will be subject to materiality as an overarching consideration in financial reporting and preparers would be reminded to consider both qualitative and quantitative materiality in determining the information that should be presented regarding P3 arrangements or transactions.

Some Others - In addition to materiality, the following factors could be considered in making judgments about the extent of appropriate P3 disclosures:

- a. Relevance to reporting objectives (For related staff analysis, please refer to pages 20-23)
- b. Nature and magnitude of the potential risks/exposures or benefits associated with the relationship
- c. Complexity of the relationship

⁸ **Disclosure** is the reporting of information in the notes or a narrative regarded as an integral part of the basic financial statement. SFFAC 5, *Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements*, states that unrecognized elements are candidates for disclosure in the notes to financial statements or as supplementary information and that items, because of their uncertainty that do not meet the basic recognition criteria may be candidates for disclosure. Source: FASAB 2012 Handbook.

⁹ Exposure Draft dated April 3, 2013 - *Federal Reporting Entity*.

Disclosures - Fiscal Exposure (Risk)

Sources for Recommended Fiscal Exposure (Risk) Disclosures

Staff has conducted research and uncovered examples of some of the more important disclosures surrounding P3s that the Board may wish to consider. These examples have been developed from a variety of authoritative sources which address information needs for different types of users and audiences. The sources for these recommended disclosures follow:

- *Surface Transportation Authorization Act of 2009* dated June 22, 2009. House of Representatives. Committee Print, 111th Congress.
- GAO-08-44 dated February 8, 2008. *Highway Public-Private Partnerships: More Rigorous Up-Front Analysis Could Better Secure Potential Benefits and Protect the Public Interest*.
- Office of the State Comptroller, Thomas P. DiNapoli, State Comptroller. *Controlling Risk Without Gimmicks: New York's Infrastructure Crisis and Public- Private Partnerships*. January 2011.
- Ellen Dannin, *Crumbling Infrastructure, Crumbling Democracy: Infrastructure Privatization Contracts and Their Effects on State and Local Governance*, 6 Nw. J. L. & Soc. Pol'y. 47 (2011).
- United Nations Economic Commission for Europe. *Guidebook on Promoting Good Governance in Public-Private Partnerships*. United Nations, New York and Geneva, 2008.
- *Disclosure of Project and Contract Information in Public-Private Partnerships*. World Bank Institute. January 2013.

User Information Needs of Fiscal Exposure (Risk) Disclosures

In SFFAC 1, *Objectives of Federal Financial Reporting*, the Board centered on two fundamental values of governmental accounting and financial reporting; “accountability” and its corollary, “decision usefulness”, stating that they comprise the foundation for the federal financial reporting objectives. To that end, the Board identified four major user groups of federal financial information:

- **Citizens** - As individuals, citizens typically have limited time and ability to analyze reports about their government; they want and rely on assurances that the government is functioning economically, efficiently, and effectively. As they are organized and represented by analysts working for interest groups and the news media, citizens want more information about the government’s activities.
- **Congress** - Congress is concerned with broad policies, priorities, and the programs that implement those priorities. It decides what taxes to impose, what funds should be spent, and for what purpose. Thus, Congress is concerned both with how to finance programs and with how they are executed.
- **Executives** - Executives focus on the strategic plans and programs that are intended to achieve presidential and congressional goals and to implement their policies. Executives are directly concerned about the management of programs, that

Disclosures - Fiscal Exposure (Risk)

is, with the actual delivery of services and with the efficiency and effectiveness of the delivery process. and

- **Program managers** - Program managers assist in the design of programs and organize the method selected for delivering services. Their concerns include operating plans, program operations, and budget execution as they need to provide information to enable executives and Congress to monitor the programs.

Suggested P3 Disclosures That Help Meet User Information Needs

The P3 disclosure examples that follow on the next page are primarily project specific. As such, they will need to be tailored and made to apply to an entity's overall grouping of P3 arrangements or transactions so that users are presented with information that is comprehensive and material to an entity's financial statements and without placing an undue burden on preparers to provide P3 specific or granular level information.

However, an entity would be permitted to disclose information related to individually significant P3 arrangements/transaction separately if entity management believed that such disclosure would better meet user needs.

Generally, a reader should have an understanding of:

1. The nature and rationale or purpose for the P3 arrangement or transaction, or categories of P3s.
2. The process used to qualify and select a private partner.
3. The structure of the P3 including its term and events that could lead to termination or default.
4. The entity's rights and obligations under the P3 arrangement/transaction.
5. The purported benefits of the P3 in contrast to the more traditional procurement approaches.
6. The relative benefits/revenues being received in exchange for all of the government's consideration, monetary and non-monetary.
7. Significant risks the P3 partners are undertaking in this arrangement.
8. Amounts the government can be reasonably expected to incur/pay over the life of the P3 arrangement or transaction.
9. Financial results of the P3 and how well the P3 arrangement/transaction is meeting its expected outcome(s).

Disclosures would be required for the initial period and all annual periods thereafter where an entity is party to a material P3 arrangement/transaction.

Disclosures - Fiscal Exposure (Risk)

Fiscal Exposure (Risk) Disclosures¹⁰ and their Relationship To Federal Reporting Objectives

Federal Reporting Objectives	Examples of Fiscal Exposure (Risk) Disclosures that Meet the Objectives:	
Federal financial reporting should provide information that helps the reader to determine:	Narrative/Qualitative	Quantitative
<p>Budgetary Integrity</p> <ol style="list-style-type: none">How budgetary resources have been obtained and used and whether their acquisition and use were in accordance with the legal authorization. <p>Operating Performance</p> <ol style="list-style-type: none">The costs of providing specific programs and activities and the composition of, and changes in these costs.The efficiency and effectiveness of the government's management of its assets and liabilities.	<ol style="list-style-type: none">Identification of all costs & contingenciesTax arrangements affecting financing/costs	<ol style="list-style-type: none">Total payment amounts (e.g., cash flows) to and from the federal entityIdentification of the full fair value of any public property used and/or assets conveyed or constructed

¹⁰ The examples are primarily project specific and as such, they will need to be tailored and made to apply to an entity's overall grouping of P3 arrangements or transactions so that users are presented with information that is comprehensive and material to an entity's financial statements and without placing an undue burden on preparers to provide P3 specific or granular level information.

Disclosures - Fiscal Exposure (Risk)

Federal Reporting Objectives	Examples of Fiscal Exposure (Risk) Disclosures that Meet the Objectives:	
Federal financial reporting should provide information that helps the reader to determine:	Narrative/Qualitative	Quantitative
<p>Operating Performance</p> <ol style="list-style-type: none"> 1. The costs of providing specific programs and activities and the composition of, and changes in, these costs. <p>Stewardship</p> <ol style="list-style-type: none"> 2. Future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due, and 3. government operations have contributed to the nation's current and future well-being. 	<ol style="list-style-type: none"> 3. Expected and actual levels of performance 4. Major milestones 5. Identification of stabilization clauses/compensating events 6. Identification of non-compete clauses or agreements 7. Identification of termination for convenience provisions 	<ol style="list-style-type: none"> 3. Annual payment amounts between government and private partner 4. Tariffs, User fees and pricing 5. Guarantees and other arrangements that affect financing/costs

Disclosures - Fiscal Exposure (Risk)

Federal Reporting Objectives	Examples of Fiscal Exposure (Risk) Disclosures that Meet the Objectives:	
Federal financial reporting should provide information that helps the reader to determine:	Narrative/Qualitative	Quantitative
<p>Budgetary Integrity</p> <ol style="list-style-type: none"> 1. How budgetary resources have been obtained and used and whether their acquisition and use were in accordance with the legal authorization. <p>Systems and Control</p> <ol style="list-style-type: none"> 2. Transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purposes authorized, and are recorded in accordance with federal accounting standards. <p>Stewardship</p> <ol style="list-style-type: none"> 3. The government's financial position improved or deteriorated over the period. 4. Future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due. 5. Government operations have contributed to the nation's current and future well-being. 	<ol style="list-style-type: none"> 8. Rationale for project and for PPP option 9. Description of tender process or other selection process 10. Project structure and parties to the contract 11. Events of default and termination payments 12. Independent assurance that all costs & contingencies are considered 	

Disclosures - Fiscal Exposure (Risk)

Federal Reporting Objectives	Examples of Fiscal Exposure (Risk) Disclosures that Meet the Objectives:	
Federal financial reporting should provide information that helps the reader to determine:	Narrative/Qualitative	Quantitative
<p>Stewardship</p> <ul style="list-style-type: none">1. Government operations have contributed to the nation's current and future well-being. <p>Systems and Control</p> <ul style="list-style-type: none">2. Transactions are executed in accordance with budgetary and financial laws and other requirements, consistent with the purposes authorized, and are recorded in accordance with federal accounting standards.3. Assets are properly safeguarded to deter fraud, waste, and abuse.	<ul style="list-style-type: none">13. Ensuring value for money and/or that costs exceed benefits.14. Analysis of a P3 procurement approach vs. traditional procurement	<ul style="list-style-type: none">6. Total payment amounts (e.g., cash flows) to and from the federal entity7. Identification of the full fair value of any public property or assets used8. Other asset transfers

Questions for the Board

Questions for the Board

- 1. Does the Board agree with the suggested draft P3 definition/description? If not, what changes would the Board advise be made?**

In answer to the question of what is a Federal Public-Private-Partnership, in consultation with the task force, staff recommends the following:

Federal public-private partnerships (P3s) are contractual arrangements or transactions between public and private sector entities to deliver a service or an asset for either government or general public use which allows for more private sector participation than is traditional. As a result, federal P3s can (1) fall outside typical federal contracting policies and guidelines, (2) be highly complex and sophisticated risk-transfer systems where in theory risks are allocated to the party which is best able to manage them, and (3) include the formation of consortiums often called special purpose vehicles or SPV's. Through these arrangements or transactions, the partners typically share resource such as real and personal property, multi-sector skills and expertise, and financial as well as risks and rewards to deliver desired policy outcomes.

The above definition captures the most widely identified features of federal P3s and many arrangements will likely meet this definition. P3s should be assessed against the conclusive and suggestive characteristics presented below to identify those subject to these disclosure requirements.

NOTE: This defines the universe of arrangements that should be considered for risk-based disclosures.

Does the Board agree with the suggested draft P3 definition/description? If not, what changes would the Board advise be made?

Questions for the Board

- 2. Staff proposes the development of 2 categories of P3-Centric Reporting Characteristics; Conclusive and Suggestive. Does the Board generally agree with the notion of these 2 categories? If not, what changes would the Board advise be made?**

The aforementioned P3-Centric Reporting Characteristics have been designed to assist a federal entity in ascertaining what P3 arrangements or transactions within its portfolio should be considered for disclosure. Once identified, the P3 arrangements or transactions should be evaluated in light of the entity's materiality considerations; e.g., threshold.

The characteristics are intended to apply to all types of P3's; construction, housing, utilities, military depots, etc. These characteristics are intended to be used as an agency filter that in connection with materiality tolerances would eliminate reporting P3 arrangements that pose no (1) financial recognition or de-recognition concerns, or (2) other fiscal exposure (risk) that could lead to a liability.

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 characteristics in the Suggestive category. If identified for potential reporting, the P3 arrangements or transactions should be further evaluated in light of materiality considerations.

Staff proposes the development of 2 categories of P3-Centric Reporting Characteristics; Conclusive and Suggestive. Does the Board generally agree with the notion of these 2 categories? If not, what changes would the Board advise be made?

- 3. In addressing disclosures staff recommends following a similar approach used in the Federal Reporting Entity Exposure Draft except that P3 disclosures would permit entities to provide broad and summarized narratives instead of unique or discrete arrangement or transaction detail. As such, staff recommends using factors like those currently identified in the Federal Reporting Entity Exposure Draft in making judgments about the extent of appropriate P3 disclosures. Does the Board generally agree with this approach? Are there any factors listed that the Board would advise eliminating, changing or possibly adding?**

Due to the relative complexity and potentially voluminous nature of P3s that an entity might be party to, the disclosures would permit entities to provide broad and summarized narratives instead of unique project or discrete arrangement or transaction detail.

As is the custom, P3 disclosures will be subject to materiality as an overarching consideration in financial reporting and preparers would be reminded to consider both qualitative and quantitative assessments in determining the information that should be presented regarding P3 arrangements or transactions.

Questions for the Board

In addition to materiality, the following factors currently identified in the *Federal Entity Exposure Draft* could be also considered as factors in making judgments about the extent of appropriate P3 disclosures:

- a. Relevance to reporting objectives (For related staff analysis, please refer to pages 20-23)
- b. Nature and magnitude of the potential risks/exposures or benefits associated with the relationship
- c. Complexity of the relationship

In addressing disclosures staff recommends following a similar approach used in the Federal Reporting Entity Exposure Draft except that P3 disclosures would permit entities to provide broad and summarized narratives instead of unique or discrete arrangement or transaction detail. As such, staff recommends using factors like those currently identified in the Federal Reporting Entity Exposure Draft in making judgments about the extent of appropriate P3 disclosures. Does the Board generally agree with this approach? Are there any factors listed that the Board would advise eliminating, changing or possibly adding?

4. The Task Force proposes requiring 9 broad areas of disclosure both narrative/qualitative and quantitative. Does the Board generally agree with the 9 broad areas? If not, what changes would the Board advise be made?

In SFFAC 1, *Objectives of Federal Financial Reporting*, the Board centered on two fundamental values of governmental accounting and financial reporting; “accountability” and its corollary, “decision usefulness”, stating that they comprise the foundation for the federal financial reporting objectives. To that end, the task force suggests the following disclosures for P3 arrangements/transactions:

1. The nature and rationale or purpose for the P3 arrangement or transaction, or categories of P3s.
2. The process used to qualify and select a private partner.
3. The structure of the P3 including its term and events that could lead to termination or default.
4. The entity’s rights and obligations under the P3 arrangement/transaction.
5. The purported benefits of the P3 in contrast to the more traditional procurement approaches.
6. The relative benefits/revenues being received in exchange for all of the government’s consideration, monetary and non-monetary.
7. Significant risks the P3 partners are undertaking in this arrangement.

Questions for the Board

8. Amounts the government can be reasonably expected to incur/pay over the life of the P3 arrangement or transaction.
9. Financial results of the P3 and how well the P3 arrangement/transaction is meeting its expected outcome(s).

Staff proposes requiring 9 broad areas of disclosure both narrative/qualitative and quantitative. Does the Board generally agree with the 9 broad areas? If not, what changes would the Board advise be made?

Questions for the Board

The objective of this session is to seek input from the Board concerning progress made on the project plan. Specifically, the following three matters will be discussed: a suggested draft P3 definition/description, P3-Centric Reporting Characteristics, and Fiscal Exposure (risk) disclosures.

If you require additional information or wish to suggest another alternative not considered in the staff proposal, please contact staff as soon as possible. In most cases, staff would be able to respond to your request for information and prepare to discuss your suggestions with the Board, as needed, in advance of the meeting. If you have any questions or comments prior to the meeting, please contact me by telephone at 202-512-6841 or by e-mail at savinid@fasab.gov with a cc to paynew@fasab.gov.

Questions for the Board

Questions for the Board

- 1. Does the Board agree with the suggested draft P3 definition/description? If not, what changes would the Board advise be made?**
- 2. Staff proposes the development of 2 categories of P3-Centric Reporting Characteristics; Conclusive and Suggestive. Does the Board generally agree with the notion of these 2 categories? If not, what changes would the Board advise be made?**
- 3. In addressing disclosures staff recommends following a similar approach used in the Federal Reporting Entity Exposure Draft except that P3 disclosures would permit entities to provide broad and summarized narratives instead of unique or discrete arrangement or transaction detail. As such, staff recommends using factors like those currently identified in the Federal Reporting Entity Exposure Draft in making judgments about the extent of appropriate P3 disclosures. Does the Board generally agree with this approach? Are there any factors listed that the Board would advise eliminating, changing or possibly adding?**
- 4. Staff proposes requiring 9 broad areas of disclosure both narrative/qualitative and quantitative. Does the Board generally agree with the 9 broad areas? If not, what changes would the Board advise be made?**

Attachment 1 – User Information Needs: An Interview with a Mayor

Attachment 1 – User Information Needs: An Interview with a Mayor



Source: <http://www.youtube.com/watch?v=dgQxneZn2qE>

Background: A Mayor's reaction to a Portsmouth, Virginia Circuit Court judge's decision that tolls arising from a P3 arrangement were unconstitutional. Judge James A. Cales Jr. said in his decision that the General Assembly "exceeded its power by ceding the setting of toll rates and taxes" to the Virginia Department of Transportation.

Quotes from Mayor Kenny Wright:

We were very **concerned with the contract and the terms** of the contract.

We are not as opposed to public-private partnerships but **the way it was done, how it was done and the terms that were attached** we thought was very unfair...

The whole approach to this was wrong from day one...**the government needs to have a major role in these types of large asset type projects**...there are certain elements that **we need to control**.

Questions for the Board

They tried to bundle it all together to make a huge profit center for the private entity and that's where most of the citizens couldn't stomach it.