Federal Accounting Standards Advisory Board

August 10, 2012

Memorandum

To: Members of the Board

From: Domenic N. Savini, Assistant Director

Through: Wendy M. Payne, Executive Director

Subj: **Status Report: Public-Private Partnerships – Tab G**[1]

MEETING OBJECTIVES

To decide whether to defer this effort until more progress has been made on the *Federal Entity* and *Leases* standards. To that end and at the Board's request, staff is providing additional information in the form of Congressional Budget Office (CBO) examples of Public-Private Partnerships and two additional case studies to illustrate the different types of public-private arrangements that exist. This additional material is being provided for informational purposes only and does not include staff analysis or recommendations concerning any of the specific examples or cases shown.

BRIEFING MATERIAL

The transmittal memorandum includes the following briefing material:

1. **Attachment 1 - CBO Examples of Public-Private Partnership Ventures**
2. **Attachment 2 - Case Study: Washington Metropolitan Area Transit Authority**
3. **Attachment 3 – Case Study: In-Q-tel**
4. **Attachment 4 – April 2012 Public-Private Partnerships Status Report (TAB H-4)**

If you require additional information please contact me as soon as possible. If you have any questions or comments, please contact me by telephone at 202.512.6841 or by e-mail at savinid@fasab.gov

[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.

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Examples of Public/Private Ventures

Each public/private venture has unique features, so observers may disagree about what is typical. Nonetheless, a review of some recent public/private ventures provides insight into what the ventures are and how they are being used.

Ventures Initiated Under DoD's Housing Privatization Authorities

Under its housing privatization authorities, DoD can enter into public/private ventures that need not be authorized by the Congress on an individual basis.[3] Those authorities, first granted DoD-wide in 1996, allow the department to enter into a wide range of financial agreements—including direct loans, loan guarantees, outleases of land, rental guarantees, bartering arrangements, direct investments by the government, and transfers of property—with private-sector participants to provide housing for military families.

In those ventures, the private partner typically obtains private, third-party financing to build or renovate family housing units for DoD. The department generally provides to the venture a lease for government land and control over the housing units located there. It may guarantee the venture's debt against base closures, deployments, or downsizing. DoD may also provide direct loans or contribute equity to the venture, in some cases becoming a legal partner with an explicit ownership interest in the venture.

The principal and interest on the funds the venture borrows to construct or renovate units, as well as the costs to maintain and manage completed units, are typically covered by rental payments equal to the service members' housing allowances. Because service members who live in the privatized units receive housing allowances whereas those living in conventional DoD-owned units do not, one effect of such ventures is to raise the amount that DoD spends on housing allowances.

In two of the earliest housing ventures—those conducted by the Navy under experimental authorities granted to it in 1994—the housing units were on private

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3. 10 U.S.C. 2871-2885.

land and were to be sold to individual private owners at the end of the project, rather than reverting to the federal government. In addition, under the original terms of those projects, the rents paid by military members for the units could exceed their housing allowances. Although military tenants had preferential access, renting to civilian tenants was a practical option. At one point in 1998, civilian tenants accounted for 20 percent of the occupied units at a Navy site in Texas. In the most recent projects, however, the extent of the government's involvement and control over the ventures has been much greater, often making the projects indistinguishable from standard military housing.

For example, in 2001 the Army entered into a limited partnership (Fort Hood Family Housing, LP) with a private partner, Lend Lease Actus. The partnership will own, operate, and maintain all 5,912 units located at Fort Hood, Texas, for 50 years. (The Army often tries to convey all housing units at a particular installation to a public/private venture.) At the end of the 50-year ground lease, the Army has the option to renew the partnership for another 25 years. If it does not renew, the units and land revert to the Army. According to the Army, military members will see no difference in their housing costs or assignments because of the use of the public/private venture rather than standard DoD housing.

The construction of new units and the rehabilitation of existing units at Fort Hood will have an up-front cost of about $260 million. To cover that cost, the partnership will take out a $186 million loan, the Army will invest $52 million in equity, and Bank One will provide $20 million in equity. Actus will provide an additional $6 million in equity for additional development at the end of the fifth year. Actus will earn a preferred return on its equity consistent with industry standards (in the range of 10 percent to 12 percent) as well as a share in any partnership earnings beyond that, up to a predetermined ceiling on its earnings. Actus will also provide management services to the partnership for a fee equal to a fixed percentage of the project's gross revenue.

The military services do not always participate as a legal partner in the ventures. At Elmendorf Air Force Base in Alaska, Aurora Housing—a privately owned limited liability corporation specifically created for the purpose—has entered into contracts with the Air Force to build or rehabilitate 828 housing units by 2003 and then manage the units for 50 years.[4] The up-front cost of the project will be approximately $100 million. Of that, $6.3 million is to be equity provided by Aurora's private backers, $47.99 million is to be a direct loan to Aurora from the Air Force at below-market rates, and $48 million is to be a first mortgage provided by the Alaska Housing Commission and guaranteed by the Air Force in the event of

4. The firm responsible for managing the units on Aurora's behalf will receive a management fee consistent with the industry standard (in the range of 4 percent to 6 percent of the project's gross revenues).

base closure, deployments, or downsizing. The Air Force also will provide land and existing housing units.

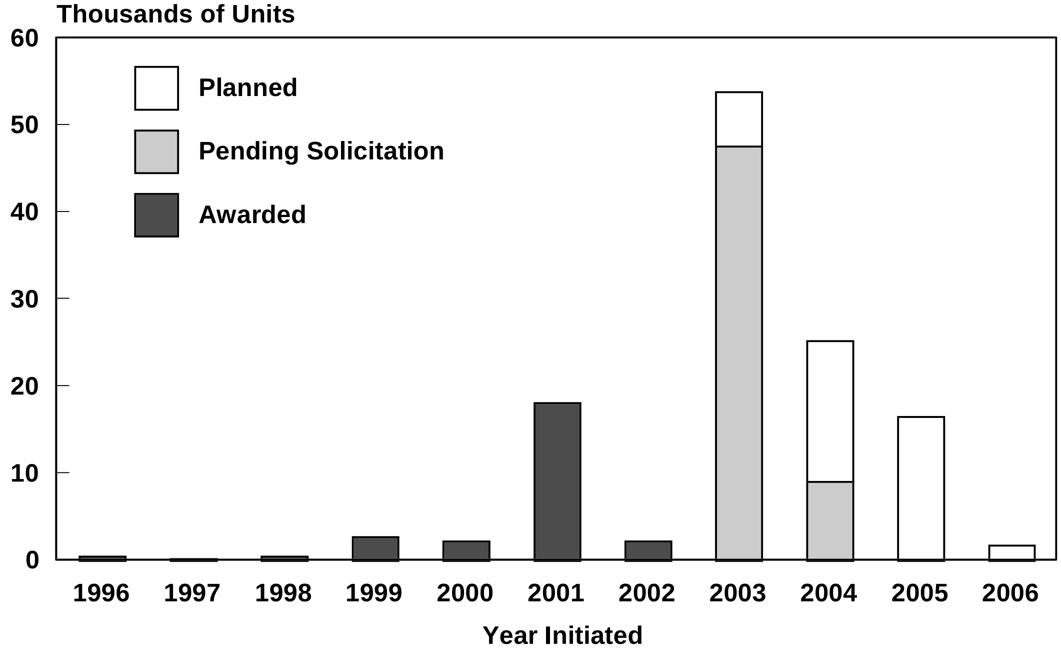
The contracts between Aurora Housing and the Air Force that establish the Elmendorf housing venture specify that they are not a partnership agreement. Nonetheless, Aurora has obtained a private legal opinion indicating that for tax purposes, the Air Force might be viewed as having entered into a partnership. According to that opinion, the Air Force has contributed equity to the partnership in the form of existing land and units. In addition, the Air Force benefits from the venture's earnings, just as a partner would, because of provisions requiring Aurora to deposit residual earnings into a fund devoted to the Air Force's programs for housing and improved quality of life. Ownership risk to Aurora's private backers is restricted because the $6.3 million in equity, plus an ensured "bid profit" of $9.0 million, earns a preferred rate of return consistent with industry standards (in the range of 10 percent to 12 percent a year) until the project is able to pay off the preferred return balance.

Looking at the Fort Hood and the Elmendorf projects as a whole, one might argue that the military services have a controlling interest in both. Much of that control is exercised through contracts that establish the ventures, ensure that they meet the services' needs, provide for the services to receive a share of any earnings above some threshold, and ensure that the units are in good condition when they revert to the services at the end of the lease. In both projects, the units must be offered first to military personnel, and become available to civilian tenants only if the vacancy rate exceeds some agreed-upon limit. In addition, the ventures cannot charge rents that, together with expected utility charges, exceed the service members' housing allowances.

Since 1996, DoD's use of military housing ventures has increased substantially (see Figures 1 and 2). As of September 2002, DoD had entered into 16 partnerships that will renovate or build 26,166 family housing units at bases throughout the United States. The department was soliciting or preparing to solicit private participants for additional projects covering 56,757 units. Another 40,512 units were covered by projects in the planning stage, bringing the total number of units that DoD plans to have privatized by 2006 to 123,435. By that time, DoD expects that privatized units will constitute more than half of its total stock of leased, owned, or privatized units in the United States.

If DoD carries out its plans, use of the public/private ventures will speed the replacement or renovation of its aging housing units as well as permit the construction of units that the department says it needs to overcome existing shortfalls. DoD estimates that accomplishing that task with appropriations for military construction would take from 30 years to 40 years and cost nearly $30 billion. DoD's goal is to leverage its appropriation for family housing so that it can obtain $3 in construction

Figure 1.
Number of Housing Units in the Department of Defense's Military Housing Ventures, as of April 2002



Source: Congressional Budget Office based on data from the Department of Defense.

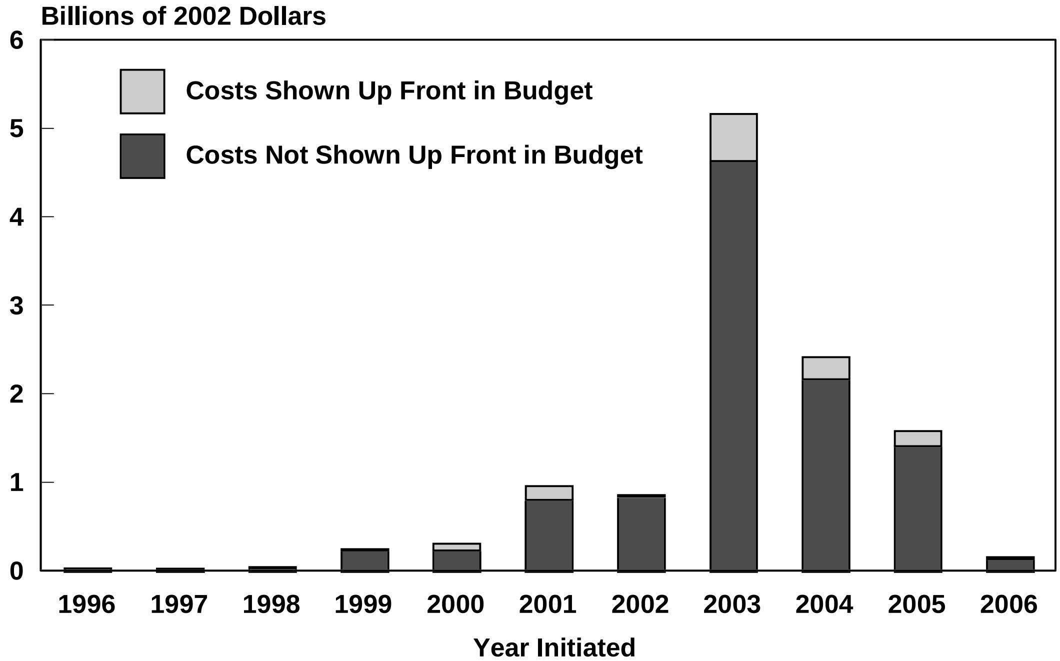
for each dollar in up-front funding. CBO estimates that as of September 2002, DoD had used the ventures to obtain about $2.3 billion in housing while recording $255 million in obligations.

Over the long run, however, it is unclear that housing privatization will reduce DoD's requirements for appropriated funds. The number of service members collecting housing allowances will rise as existing units are privatized and new units are built. The projects may also lead to the construction of on-base units in locations where adequate private housing already exists for military families. DoD's principal justification for the privatization of housing is that the approach will enable the department to meet its goals for the quantity and quality of on-base housing more quickly than it could using military construction.

Ventures Initiated Under the Department of Veterans Affairs' Enhanced-Use Leasing Authorities

The VA first received broad authorities to enter into so-called enhanced-use leases in the fall of 1991. The VA's current authorities allow the agency to lease land to

Figure 2.
The Costs of the Department of Defense's Military Housing Ventures, as of April 2002



Source: Congressional Budget Office based on data from the Department of Defense.

private partners for up to 75 years.[5] The land can then be developed by the private partners for the VA's uses or others'. The VA may use compensation that it receives from the enhanced-use leasing agreement—whether cash, facilities, or services—as it sees fit in pursuing its mission, without any further appropriation. The VA may also lease back for its own use some or all of the facilities developed by the private partners. Although the VA is authorized to enter into contracts under those authorities, it must notify the Congress of its intent 60 days before entering into an enhanced-use leasing agreement.

By 2002, the VA had undertaken enhanced-use leasing to obtain a number of facilities, including office buildings for regional headquarters and parking facilities. In addition, the VA used the approach to obtain services that depend on large capital investments, including the services of electric and steam cogeneration facilities, nursing homes, single-room occupancy facilities, and child care centers for VA employees.

5. 38 U.S.C. 8161-8169.

Mountain Home Cogeneration Facility. The power plant at the VA Medical Center at Mountain Home, Tennessee, provides an example of an enhanced-use leasing venture in which the government is paying for an asset over time through the price it pays for energy. Construction of the plant—a facility that would generate electric power and steam—depended on a series of interdependent agreements signed concurrently on November 1, 1999.[6] Those agreements do the following:

- Create an owner trust, the Mountain Home Energy Trust, specifically to own and provide financial management for the cogeneration project. The trust's sole asset is the cogeneration plant, and its sole beneficiary is the VA.

- Provide the owner trust with a 34-year enhanced-use lease from the VA for land on which to build the plant adjacent to a large regional VA medical center.

- Establish a development and management contract between the VA, the owner trust, and a private limited liability corporation (Mountain Home Energy Center, LLC) in which the LLC agrees to build the plant for a fixed price and then operate and maintain it for predetermined fees.

- Establish an energy services agreement between the owner trust, the VA, and the LLC setting the terms under which the VA medical center at Mountain Home will purchase utilities from the cogeneration plant.

- Provide for the Johnson City Industrial Development Board to issue $32 million in taxable municipal revenue bonds.

- Provide for the loan of the bond proceeds to the owner trust to pay for the construction of the cogeneration plant.

The ability of the owner trust to obtain financing to build and operate the plant depended largely on the energy services agreement between the owner trust, the VA, and the LLC. In that agreement, the VA enters into a two-year contract for energy services that would renew automatically over a 24-year period (provided that the VA continues to operate its regional medical center at Mountain Home).[7] The

6. A description of those transactions is provided in the official statement of the Industrial Development Board of Johnson City, Tennessee, regarding taxable revenue bonds for the project. That statement, identified by the bond issue's CUSIP number (478274CT8), was submitted to the Municipal Securities Rulemaking Board and can be obtained from it.

7. Reported to the Congressional Budget Office in a briefing by the VA, July 26, 2002, and a Memorandum of Understanding, "Enhanced-Use Energy Development at the James H. Quillen VAMC at Mountain Home, TN," entered into between the VA and Energy Systems Group, November 20, 1998.

agreement also sets the prices that the VA will pay for energy. If the VA reduced the quantity of energy that it purchased during the subsequent two-year contracts, its payments for fuel and "standby" electricity would decline, but the portion of its payments that covered capital and maintenance for the plant would remain fixed.[8] Because of the VA's purchase commitment, the bonds to finance the cogeneration plant were insured by the MBIA Insurance Corporation and subsequently received a triple-A rating from Standard & Poor's and Moody's.

At the end of the 34-year lease, the VA will become the owner of the cogeneration plant, which is to be maintained in good condition by the LLC operating on behalf of the owner trust. During the term of the lease, the owner trust, and ultimately the VA as its beneficiary, will receive a share of the revenues if the facility sells electricity to non-VA customers.[9]

Chicago West Side Regional Headquarters. The VA's Chicago West Side project provides an example of an arrangement in which the VA uses an enhanced-use lease to obtain a new $60 million regional headquarters building and parking facility. The financial structure for the West Side project, similar to that used for Mountain Home, also involved a series of interdependent, concurrent agreements.[10] The agreements, dated October 1, 2002, accomplish the following:

- Create an owner trust, the West Side Enhanced-Use Lease Trust, with the VA as the sole named beneficiary.

- Provide the owner trust with a 35-year enhanced-use lease from the VA for a four-acre site adjacent to the VA Medical Center in downtown Chicago.

- Establish the terms under which a commercial development and building management firm (MedPark Development and its affiliate, MedPark Management) will design, build, furnish, and manage the office building and parking facility on behalf of the owner trust and the VA.

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8. The contract states that all of the VA's payments are subject to the availability of appropriations. However, the Johnson City Industrial Development Board, in its official description of the bond issue, interprets the availability of appropriations to mean the availability of appropriations to the VA as a whole.

9. The VA shares revenues (from sales of chilled water and steam) with the state of Tennessee, which has also agreed to purchase services from the cogeneration plant.

10. A description of those agreements is found in the official statement of the Illinois Development Finance Authority regarding taxable revenue bonds for the project. That statement, identified by the bond issue's CUSIP number (45188RZ77) was submitted to the Municipal Securities Rulemaking Board and can be obtained from it.

- Provide for the Illinois Development Finance Authority to issue $59 million in taxable revenue bonds.

- Provide for the loan of the bond proceeds to the owner trust to pay for the design and construction of the office building and parking facility.

As was the case for Mountain Home, the VA's commitments play a crucial role in allowing the owner trust to borrow through the development authority. Because the VA is committed to a two-year lease of 95 percent of the space in the building and 95 percent of the parking facility, almost all of the owner trust's revenues will initially come from the VA. The initial two-year lease is automatically renewed unless the VA takes specific steps at the end of the lease period to halt it.[11] In addition, as long as the VA chooses to occupy any portion of the facility it must make payments that are sufficient to cover amortization and interest on the owner trust's debt as well as the trustee's expenses. Moreover, the VA agreed that if it vacated the facility, it would not use its enhanced-use leasing authority to secure a replacement. The VA has the right to purchase the building from the owner trust at any time for a price that would cover payments on the trust's debt. In view of the VA's commitments, the bonds to finance the project were insured by Ambac Assurance Corporation and subsequently rated triple-A.

Because the building is in a valuable location at the center of Chicago's medical district, supporters of the project argue that finding another tenant would not be difficult. If the VA vacated all or part of the building and the owner trust leased space to another tenant, the VA would benefit from the lease revenue as the sole beneficiary of the owner trust.

Future Projects. The VA currently plans additional projects and has established an Office of Enterprise Development within its Facilities Management Office to promote the use of partnerships and provide guidelines for their development. It has completed or awarded 24 projects at a total cost of $283 million (see Figure 3) and is examining the potential of enhanced-use leasing for more than 50 projects in development. Some, although not all, proposed projects involve the acquisition of assets through annual lease payments or purchases of services. The possible number of such projects is substantial as the VA controls more than 23,000 acres of land and 5,000 buildings at approximately 270 locations. Many of those sites include underutilized buildings or land.

Enhanced-use leasing has both its supporters and its opponents. Many supporters would like to see the authorities extended to other agencies, including

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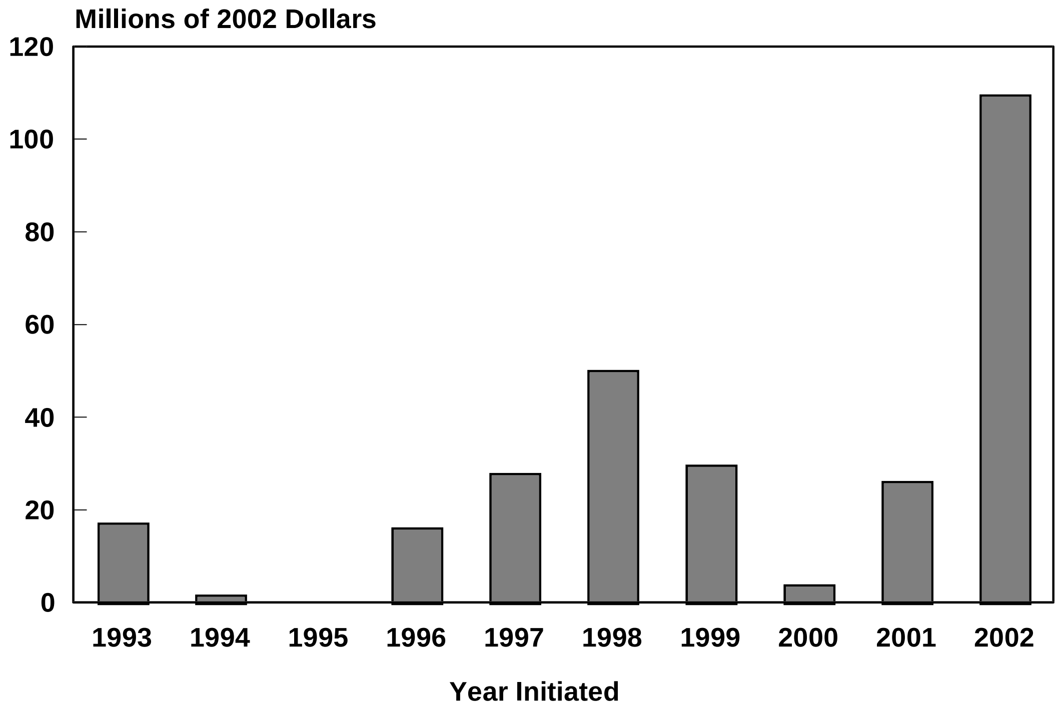
11. The trust is required to offer the VA the opportunity to continue to occupy the building if the agency takes no action at the end of the initial two-year lease, and VA's failure to respond to that offer would constitute acceptance.

Figure 3.
The Costs of the Department of Veterans Affairs' Enhanced-Use Leasing Ventures



Source: Congressional Budget Office based on data from the Department of Veterans Affairs.

Note: These costs do not appear up front in the federal budget.

GSA and NASA. Supporters note that without the authorities, agencies have little incentive to part with land that may be providing only marginal services. A central feature of enhanced-use leasing is that it provides an opportunity for agencies to exchange underutilized assets for assets or services that they can use fully.

Many opponents are concerned about the effects on Congressional control. They point out that much of the apparent savings from enhanced-use leases arise because projects are not subject to the same restrictions as other government activities. For example, in the case of the VA's Chicago West Side project, much of the savings that the VA expects to receive from relying on enhanced-use leasing (rather than construction using appropriated funds) stems from the assumption that federal procurement regulations and the budget process would slow construction and increase of the cost of the building. Estimated revenues for the enhanced-use leasing project are also greater than they would have been because the owner trust, unlike the VA, can charge non-VA employees for parking.

Another concern is that heavily leveraged public/private ventures—while potentially offering taxpayers a higher expected return—may also subject them to greater market risks. If legislation is needed to allow agencies to benefit from underutilized assets, some analysts argue that a better approach would be to authorize agencies only to conduct outright sales or provide arm's-length ground leases, rather than allowing them—in effect—to use the assets as down payments to secure private financing for projects they might not otherwise pursue.

The debate over the merits of enhanced-use leasing—like the debate over the value of public/private ventures or lease-purchases—is not central to the analysis in this paper. The appropriate budgetary treatment of enhanced-use leases depends on the extent of the federal government's financial commitment and control, not on whether the total benefits of specific ventures justify the financial commitment.

Recent Ventures Initiated by the Tennessee Valley Authority and the Oak Ridge National Laboratory

DoD's and the VA's public/private ventures have been initiated under relatively new legal authorities. Other government activities authorized to operate in a businesslike manner have undertaken similar ventures.

TVA's Lease-Leaseback Ventures. The Tennessee Valley Authority is a federal agency that produces and sells electricity. Unlike most government agencies, it was established with broad authorities to enter into business agreements and to spend revenues without further appropriations. It pays its capital and operating costs from revenues obtained by selling electricity to communities and industries throughout the Southeast and finances much of its investment in land and equipment through sales of bonds to the public. Its borrowing, however, is limited by a statutory debt ceiling of $30 billion.

TVA has used its authorities in new ways for 16 power plants that it built between 1999 and 2001. In an arrangement called lease-leaseback, the TVA leased the power plants for 50 years to special-purpose entities created for that purpose and then leased the plants back for a period of 20 years (or about half of their useful life). The special-purpose entities paid for their 50-year leases with a one-time, up-front payment, while TVA spread its leaseback payments over a 20-year period.

Those transactions generated roughly $620 million in up-front cash for TVA, allowing it to avoid issuing additional bonds to finance its investments. In effect, the special-purpose entities borrowed on behalf of TVA. They obtained $527 million through the sale of pass-through certificates. TVA did not explicitly guarantee those certificates, but the certificates were fully backed by TVA's commitment to make lease payments to the entities for 20 years. Private equity accounted for the remaining $93 million of the entities' financing.

TVA expected that its approach would allow it to avoid issuing additional bonds that might count against its debt ceiling. Furthermore, the indirect borrowing allowed TVA to benefit from some of the tax advantages that private firms enjoy when they invest in capital assets. The bank that contributed equity to the projects became eligible to deduct the depreciation of the plants from the profits it pays taxes on. Thus, over time, the Treasury receives less tax revenues than it would have otherwise. The contributor of the equity passes some of those tax benefits on to TVA in the form of lower lease payments.[12]

The Oak Ridge National Laboratory. The Oak Ridge National Laboratory, under the control of the Department of Energy, is a government-owned, contractor-operated laboratory complex in Tennessee that conducts scientific research in a wide range of fields, including energy technologies. UT-Batelle, a private limited liability corporation, is the contractor currently operating Oak Ridge under a management and operations contract with the department.

DOE is using its existing authorities to obtain $70 million in private financing for new office and research facilities at Oak Ridge without recording large up-front obligations and outlays. UT-Batelle, in its role as the operator, has the authority—with DOE's approval—to enter into leases for real property that it needs to carry out its functions at Oak Ridge. DOE, in turn, has the authority to reimburse its operator for those lease expenses as the operator pays them. Those authorities open the door for a new type of lease-purchase or public/private venture.

DOE has provided UT-Batelle Development Corporation, a nonprofit corporation created for this project, with the title to the property on which the new facilities are to be built. The development corporation agreed in turn to lease the site to Keenen Development Associates, the private developer selected to build the new facilities and issue the private bonds that will pay for them. The interest and principal on the bonds, which have been rated A+ by Standard & Poor's, are covered by the commitment of UT-Batelle (the operator) to sublease the facilities from UT-Batelle Development Corporation for an initial term of 10 years followed by three five-year renewals (for a total of 25 years). The sublease payments are designed to cover the costs of building and financing the project. DOE, however, provides the ultimate backing for the bonds, because it has approved the sublease and committed

12. Ultimately, TVA's savings are passed on to TVA customers in the form of lower electricity costs.

to reimbursing UT-Batelle for the sublease payments as a legitimate operating cost of the facility.

DOE is not required to renew UT-Batelle's contract with Oak Ridge when it expires in 2005. The department has agreed, however, to require that any future operator at Oak Ridge assume the sublease of the facilities. At the end of 25 years, DOE has the right to repurchase the land and facilities at a nominal price. It also has the right to ask the operator to cancel the lease agreements earlier, but the department would then lose its right to repurchase the land and facilities. Construction of the new facilities is to be completed by August 2003.

~~The Budgetary Treatment of Public/Private Ventures~~

~~The budgetary treatment of public/private ventures is evolving as Congressional scorekeepers and OMB gain an increased understanding of the types of ventures that agencies are undertaking. For example, CBO recently scored legislation authorizing new public/private ventures for GSA, a DoD laboratory, and the National Aeronautics and Space Administration with direct spending on the grounds that the ventures, which would be effectively under the government's control, would be used to finance government investments. At the same time, however, agencies that already have authority to enter into public/private ventures continue to use them, in essence, to borrow and invest without recording the resulting obligations and outlays up front in the federal budget.~~

~~The Roles of the Executive Branch and the Congress~~

~~The executive branch is responsible for recording the obligations and outlays for individual public/private ventures during the execution of the budget. Because the actual terms and conditions of a specific public/private venture are not known until a contract is signed, the executive branch bears the frontline responsibility for ensuring that the ventures receive appropriate treatment.~~

~~To date, OMB's general approach has been to treat public/private ventures in a piecemeal manner, adding up the explicit financial commitments entailed by each venture without looking at the commitments implied by the venture as a whole. In practice, that approach has meant that investment spending undertaken by public/private ventures on the government's behalf is seldom recorded up front in the budget as a federal commitment.~~

Washington Metropolitan Area Transit Authority

Background [2]

In recent years the Washington Metropolitan Area Transit Authority (WMATA) has faced serious financial and budgetary problems as well as continuing challenges related to the safety and reliability of its transit services. At the same time, ridership is at an all-time high, and WMATA continues to provide critical services and considerable benefits to the Washington, D.C., region's economic well-being and to the federal government. Over the years, the federal government has provided WMATA with about 60 percent of the funds used to construct the Metrorail subway system, and Congress has a continued interest in the viability of WMATA due to the system's importance to the functioning of the federal government and the orderly movement of people during major events and times of regional or national emergencies.

Governance Structure [3]

Pursuant to Public Law 89-774 WMATA was created effective February 20, 1967, by the Interstate Compact (Compact) by and between Maryland, Virginia and the District of Columbia. WMATA was created to plan, construct, finance, and operate a public transit system serving the Washington Metropolitan Area including the following participating jurisdictions: the District of Columbia; the cities of Alexandria, Falls Church, Fairfax, Manassas and Manassas Park; and the counties of Arlington, Fairfax, Loudoun and Prince William in Virginia, and Montgomery, Anne Arundel, Charles and Prince George's in Maryland.

The Authority is governed by a Board of eight voting Directors and eight alternate Directors from each signatory to the compact and from the Federal government. The Directors and Alternates for Virginia are appointed by the Northern Virginia Transportation Commission; for the District of Columbia, by the City Council; and, for Maryland, by the Washington Suburban Transit Commission and for the Federal Government, by the Administrator of the General Services Administration.

The Board governs and sets policy for the Authority. Subject to policy direction and delegations from the Board, the General Manager (GM) is responsible for all activities of the Authority. The staff carries out these activities through the approved organizational structure of the Authority. Based upon the provisions of US-GAAP applicable to government entities, management has determined that it is a joint venture of the participating jurisdictions.

Budget and Finance Considerations [4]

Following Board adoption of the annual capital and current expense budgets, the GM forwards certified copies of the budgets to the principal budget officer at each participating jurisdiction at such time and manner as may be required under their respective budgetary procedures. Pursuant to Article VII, Section 18 of the Compact, each budget indicates the amounts, if any, required from each participating jurisdiction to balance the budgets.

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[2] GAO-06-516, *Issues Related to Providing Dedicated Funding for the Washington Metropolitan Area Transit Authority*, a report to the Chairman, Committee on Government Reform, House of Representatives, May 2006.
[3] Fiscal Year Ending 30 June 2011, *Comprehensive Annual Financial Report*, page 27.
[4] Washington Metropolitan Area Transit Regulation Compact ("Transit Regulation Compact"), Article VIII - Budget, paragraphs 25 and 26.

Since inception, the Authority has operated at a loss, which has been fully subsidized each year by the participating jurisdictions. For purposes of determining the current year's operating loss to be funded by the local participating jurisdictions, the Authority calculates the results of transit operations on an agreed upon basis different from that reflected in the Statements of Revenues, Expenses and Changes in Net Assets[5].

Subject to review and approval as may be required by their budgetary or other applicable processes, the participating jurisdictions are required to (1) include in their yet-to-be adopted budgets their share of the amounts needed to balance the annual capital and current expense budgets and (2) appropriate or otherwise provide said amounts certified to each of them.

[5] Fiscal Year Ending 30 June 2011, *Comprehensive Annual Financial Report*, page 35.

IN–Q-TEL

Background [6]

By the late 1990s Central Intelligence Agency (CIA) recognized that it could not effectively compete for Information Technology (IT) innovation and talent. Because private industry confronted similar issues in areas such as biotechnology, communications, and energy, agency officials determined that private industry should not be ignored.

The CIA understood that to extend its reach and access it had to not only act as a consumer of IT, but also as a provider or seller. To that end, the agency developed a venture capital business model to offer private industry. In February 1999 the CIA chartered In-Q-Tel, a venture capital fund, as a non-profit organization with the support of Congress and with the help of a small group of private citizens. The non-profit corporation was initially established to do only unclassified work for the CIA and because the agency wanted to encourage companies to work with In-Q-Tel, it designed a non-FAR (Federal Acquisition Regulation) agreement with the corporation to allow for greater flexibility in areas such as procurement, contracting and technology transfers.

In-Q-Tel's former CEO, Mr. Gilman Louie said the following in an interview:

> The best thing about In-Q-Tel, to me, is that it's risky. The CIA and the rest of the government need to catch the entrepreneurial, risk-taking spirit that's driving the Silicon Valley technology revolution. The CIA's new venture may fall flat, but so what. Washington has been a zero-defect culture for too long. If we want a CIA that performs better, we'll need to take more risks—and give our government freedom to fail.[7]

In-Q-Tel now supports multiple agencies as the National Geospatial-Intelligence Agency, Defense Intelligence Agency, and Department of Homeland Security Science and Technology Directorate. The Corporation has offices in Washington, DC and Menlo Park, CA.

Governance Structure [8]

In-Q-Tel was established as a 501(c) (3) independent nonprofit (public charity) corporation with a 10 member Board of Trustees with three-year terms. Trustees are required to meet twice a year but have met quarterly and formed committees to carry out responsibilities. Trustee functions have included initially guiding and overseeing the entity's startup activities and setting strategic direction and policies. The Chief Executive Officer reports to the Board of Trustees.

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[6] http://www.iqt.org/about-iqt/history.html and http://www.iqt.org/about-iqt/ic-partners.html and In-Q-Tel: *A New Partnership Between the CIA and the Private Sector*, by Rick E. Yanuzzi. Posted May 4, 2007. The Joint Military Intelligence College, Inc.

[7] David Ignatius, "*The CIA as Venture Capitalist*," Washington Post, September 29, 1999, p. A1

[8] Business Executives for National Security. *Report of the Independent Panel on the CIA In-Q-Tel Venture*, June 2001 and Acquisition Review Quarterly , *THE CIA'S IN-Q-TEL MODEL ITS APPLICABILITY*, by Wendy Molzahn, Winter 2003 and www.irs.gov, Exempt Organizations Select Check EIN 52-2149962.

Although In-Q-Tel does not require Agency approval for its business deals there is a significant amount of coordination between the CIA and In-Q-Tel on all business-related issues. The CIA does not have a typical "program management" oversight relationship with In- Q-Tel as the corporation makes decisions and provides the CIA with results. However, the corporations' investment policy states that, *"In-Q-Tel is obligated to consult with the Agency (CIA) prior to entering into any new equity investment agreement using funds that have been provided by the Agency…"* [9]

Budget and Finance Considerations

Although In-Q-Tel's budget is not released to the public, the CIA presents IN-Q-Tel's budget information to Congress as a "Strategic Technical Investment Project." The charter agreement does not require that the CIA review or approve In-Q-Tel's budget. Congress appropriates funds for the purpose of funding IN-Q-Tel investments and the corporation's salaries and expenses. According to the CIA-OIG, *"Without Federal funds, IN-Q-Tel would not be a viable going concern."* [9]

The most readily available financial information follows*:* [10]

Income Statement

Revenues	**2008**	**2007**	**2006**	**2005**	**2004**
Contributions					
Government Grants	55,577,088	54,024,972	54,366,103	44,330,106	50,907,009
Program Services					
Investments	5,272,021	(486,348)	10,222,197	5,191,351	(4,461,939)
Special Events					
Sales					
Other Revenue					
Total Revenue	60,849,109	53,538,624	64,588,300	49,521,457	46,445,070
Expenses	**2008**	**2007**	**2006**	**2005**	**2004**
Program Services	34,864,909	33,081,958	35,222,544	28,630,384	38,412,897
Administration	11,998,339	13,051,656	12,967,722	10,614,327	9,522,843
Other Expenses					
Total Expenses	46,863,248	46,133,614	48,190,266	39,244,711	47,935,740
Net Income	**13,985,861**	**7,405,010**	**16,398,034**	**10,276,746**	**(1,490,670)**

[9] ODNI-CFO Memorandum dated 23 December 2009, May 29 Final InQTel Position and FS Disclosure Paper
[10] https://openendowment.appspot.com/organization/view?id=52-2149962

Balance Sheet

Assets	2008	2007	2006	2005	2004
Cash & Cash Equivalents	80,908,958	72,400,608	46,009,230	32,701,879	31,522,058
Accounts Receivable					
Pledges and Grants Receivable	3,377,548	7,434,363	32,588,852	21,824,223	10,046,293
Other Receivable	1,214				
Inventories					
Investments: Securities	41,157,945	31,017,466	16,805,427	15,185,269	7,193,331
Investments: Other	4,535,395	3,989,773	2,141,049	569,124	59,458
Fixed Assets	1,398,119	666,616	1,046,842	1,702,467	1,412,813
Other Assets	1,298,212	419,204	1,469,833	222,093	469,685
Total Assets	132,677,391	115,928,030	100,061,233	72,205,055	50,703,638
Accounts Payable	8,486,508	7,801,409	7,209,768	7,002,964	9,753,092
Grants Payable					
Deferred Revenue	53,482,782	54,049,767	53,789,422	41,090,237	31,160,432
Loans					
Bonds					
Other Liabilities					
Total Liabilities	61,969,290	61,851,176	60,999,190	48,093,201	40,913,524
Equity Balance	**70,708,101**	**54,076,854**	**39,062,043**	**24,111,854**	**9,790,114**

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April 13, 2012

Memorandum

To: Members of the Board

From: Domenic N. Savini, Assistant Director

Through: Wendy M. Payne, Executive Director

Subj: **Status Report: Public-Private Partnerships – Tab H-4**[1]

MEETING OBJECTIVES

To provide an update on activities undertaken by staff on the Public-Private Partnerships project. This material is being provided for informational purposes only and will not be discussed at the April meeting unless specifically requested by one or more board members.

BRIEFING MATERIAL

The transmittal memorandum includes the following briefing material:

1. **Attachment 1 - Various Definitions for Public-Private Partnerships**
2. **Attachment 2 - Types of Public-Private Partnership Arrangements**
3. **Attachment 3 - Sample Public-Private Partnership Arrangement**

If you require additional information please contact me as soon as possible. If you have any questions or comments, please contact me by telephone at 202.512.6841 or by e-mail at savinid@fasab.gov

[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.

BACKGROUND

This project was added to the agenda because federal agencies have increasingly turned to public-private partnerships (e.g., PPPs, P3s) to accomplish goals. Budget pressures are likely to further increase the use of P3s. Making the full costs of such partnerships transparent would be the overall objective of the project. As stated in our report to stakeholders[2], a detailed project plan along with active work on this project would not begin until FY2013 with final standards following a two to three year effort.

Specific objectives could include:

1. Defining terms (e.g., service concession arrangements, P3s)
2. Providing guidance for the recognition and measurement of:
    - assets and liabilities
    - revenues and expenses
3. Considering implications for other arrangements related to P3s (sale-leaseback or other long-term arrangements).

The Board expects to benefit greatly from the work of Governmental Accounting Standards Board (GASB) and the International Public Sector Accounting Standards Board (IPSASB).

The use of P3's in this country dates back to the colonial period. In 1742 Benjamin Franklin helped sponsor the first medical school in America that was supported by the Pennsylvania House of Representatives. Although the founders at the Constitutional Convention in 1787 believed (educational and scientific) activities should be independent of direct national governmental control, they felt that the national government should remain an influential force exerting its influence through indirect rather than direct means. Thomas Jefferson is credited with ushering in a more direct role for the government in the area of science by sponsoring the Lewis and Clark research expedition in 1803. The 1800's saw rapid P3 growth in response to medical emergencies (1822 cholera epidemic), establishment of universities and institutions (1824 Rensselaer Polytechnic Institute and 1829 Smithsonian Institution), and direct funding of applied science (1838 Samuel Morse telegraph). During the 20th century both world wars brought about increased pressure to advance scientific and technical advancements. For example, President Woodrow Wilson was advised by the *National Academy of Sciences* to create a *National Research Council* to coordinate efforts between government, industry and the academic communities to reach common national goals. In 1940 President Franklin D. Roosevelt established the *National Defense Research Committee* whose purpose was to organize scientific and technological resources toward enhancing national defense. After World War II there was an imbedded belief that scientific and technological advancements are fundamental for economic growth, and that the government has an important supporting role—both direct and indirect—to ensure such growth. As recent as President William J. Clinton who led efforts to transfer publicly funded technology to the private sector and President George W. Bush who advocated making tax policy (use of credits) P3 friendly, the use of these arrangements can be clearly seen throughout most of government.[3]

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[2] Federal Accounting Standards Advisory Board, *Report to Stakeholders: FASAB Three-Year Plan* dated January 11, 2012, page 22.
[3] Albert N. Link, "The History of Public-Private Partnerships from: *Public/Private Partnerships, Innovation Strategies and Policy Alternatives*", ISBN 978-0-387-29774-3 (2006), Chapter 2,

STAFF ANALYSIS AND RECOMMENDATIONS

Staff has conducted the following initial research:

1. Reviewing relevant GASB and IPSASB accounting standards,
2. Conducting a preliminary literature review,
3. Assessing domestic and European perspectives,
4. Reviewing selected agency financial reports,
5. Consulting with Financial Accounting Standards Board research staff, Federal program managers, and a public policy expert, and
6. Analyzing P3 arrangements in light of existing FASAB guidance (gap analysis).

At this time, staff believes many issues may be addressed through the standards under consideration in the reporting entity and leases projects. At a minimum, staff believes standards for P3s should be consistent with standards developed in these areas. Therefore, staff recommends deferring this effort until more progress has been made on these standards. Doing so would provide for consistency while allowing for consideration of implementation guidance in lieu of a standard. Staff recommends the following project objectives should the Board decide to proceed:

1. **Issuance of a Technical Bulletin.**

   Because fairly robust FASAB guidance exists regarding the recognition and measurement of assets/liabilities and revenues/expenses, staff advises the Board to consider issuing a Technical Bulletin. Such bulletins provide guidance for applying FASAB Statements and Interpretations and resolving accounting issues not directly addressed by either the Statements or Interpretations. The following kinds of guidance may be provided in the Technical Bulletin:

   a. Guidance to clarify, explain, or elaborate on an underlying Statement or Interpretation, and

   b. Guidance to address areas not directly covered by existing Statements or Interpretations.

   Technical Bulletin procedures provide for both due process (more limited in scope and within a tighter minimum time frame than provided for Statements and Interpretations) and review by FASAB members.

   Generally, a Technical Bulletin can provide guidance if the problem can be resolved within the following guidelines:

   a. The guidance is not expected to cause a major change in accounting practice.

   b. The administrative cost involved in implementing the guidance is not expected to be significant to most affected entities.

   c. The guidance does not conflict with a broad fundamental principle or create a novel accounting practice.

2. **In lieu of defining terms, characteristics of P3 arrangements should be identified.**

   As recently experienced in the development of SFFAS 40[4], defining terms which are intended for uniform and general application across the federal government is an extremely laborious and time consuming process. However, identifying the more common characteristics of P3's which are generally accepted throughout government would significantly reduce staff time and agency burden and provide a sound basis for any subsequent accounting standard. Some of the more commonly agreed to P3 characteristics include: contractual agreements, shared risks, shared rewards, shared skills and expertise, and shared financing.

3. **P3 structural arrangements and implications should be evaluated against federal entity requirements.**

   Fairly robust FASAB guidance exists regarding the recognition and measurement of assets/liabilities and revenues/expenses. However, attention should be given to the accounting implications raised by the formal or informal formation of P3 arrangements (i.e., legal or economic) that could include: special purpose vehicles (SPV) or special purpose entities (SPE) such as trusts, partnerships, and joint ventures to include variable interest entities (VIE)[5].

   For example, P3 arrangements should be evaluated against core, non-core, and related party definitions and criteria so that appropriate reporting objectives can be satisfied. Specifically, an analysis of ownership and control criteria should be conducted to evaluate if P3's that are material to an entity would be treated as "off balance sheet" or sufficiently included within the federal reporting entity or model.

   P3 arrangements not meeting either the ownership or control criteria could be reported as a related party.

4. **P3 contractual arrangements and implications should be evaluated against federal capital lease requirements.**

   P3 arrangements that do not involve the formation of a separate legal or economic entity should be evaluated against federal capital lease requirements. Please note that we currently have a Leases project underway. Current FASAB standards addressing leasing transactions include Statement of Federal Financial Accounting Standard (SFFAS) 5, *Accounting for Liabilities of the Federal Government* [pars. 43 – 46] and SFFAS 6, *Accounting for Property, Plant, and Equipment* [pars. 20 & 29]. These lease standards were originally developed from FASB lease standards effective at that time. The joint FASB/IASB project is expected to issue a revised Exposure Draft during the second half of 2012.

[4] SFFAS 40; *Definitional Changes Related to Deferred Maintenance and Repairs: Amending Statement of Federal Financial Accounting Standards 6, Accounting for Property, Plant, and Equipment.*
[5] VIE control (controlling interest) is not based on majority ownership.

5. **Federal accounting guidance should not be limited to service concession arrangements.**

   Both GASB and IPSASB limit public-private partnership guidance to service concession arrangements directly benefitting the general public. As a result, P3 arrangements that provide services to the government entity or grantor are excluded. GASB refers to these as "service and management arrangements" or SMA's.

   As previously mentioned, because sufficient guidance exists regarding the recognition and measurement of assets/liabilities and revenues/expenses, it can be effectively used for the accounting of service concession arrangements.

   Additionally, P3 arrangements whether benefitting the general public directly or providing services to the government entity or grantor fall within the remit of the federal financial reporting objectives.[6] Specifically, budgetary integrity and operating performance are directly impacted as are, stewardship and systems and control. Refer to Figure 1.0 on the next page for an analysis.

6. **Other Matters**

   Intellectual Property – Staff has identified this area for potential research. SFFAS 1, *Accounting for Selected Assets and Liabilities and* SFFAS 6 *Accounting for Property, Plant and Equipment* do not discuss intangible assets. Staff has come across P3 arrangements where patents are jointly created and owned. Additional research would be required to assess the accounting implications for the accounting for intangibles.

   Privatization – The basic question is at what point could a P3 arrangement result in a de facto privatization? Also, P3 arrangements could be an entity's initial step into a privatization program. In both cases the appropriate accounting treatment and classification for assets/liabilities and revenues/expenses would need to be considered. For example, should assets being held for privatization be separately classified on the balance sheet? Another accounting issue could be the treatment of employee legacy costs and/or service contract termination costs.

[6] Statement of Federal Financial Accounting Concepts 1: *Objectives of Federal Financial Reporting.*

Figure 1.0

Public-Private Arrangements and their Relationship To Federal Reporting Objectives

By subjecting all P3 activities to FASAB reporting requirements we meet the following reporting objectives:	
Budgetary Integrity 1. How budgetary resources have been obtained and used and whether their acquisition and use were in accordance with the legal authorization.	**Example:** 1. Identifying the full costs of P3s to enable comparison of these costs with budgetary resources.
Operating Performance 1. The costs of providing specific programs and activities and the composition of, and changes in, these costs.	**Example:** 1. In some cases costs and related liabilities are understated. For example, some P3 arrangements may not involve any lease payments and to the contrary, involve a revenue stream flowing to the government in exchange for offering low cost leases of government property, committing to future purchases, or transferring assets to the P3.
Stewardship 1. The government's financial position improved or deteriorated over the period. 2. Future budgetary resources will likely be sufficient to sustain public services and to meet obligations as they come due. 3. Government operations have contributed to the nation's current and future well-being.	**Discussion:** 1. Not reflecting all asset/liabilities on the balance sheet makes this more difficult and could skew results. 2. Revealing the full costs may facilitate consideration of future budgetary resource needs. 3. Assessing the full cost of P3s is important in considering the benefits.
Systems and Control 1. 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. 2. Assets are properly safeguarded to deter fraud, waste, and abuse.	**Discussion:** 1. Excluding organizations from coverage may make it difficult to assess compliance. Not reflecting all asset/liabilities on the balance sheet makes this difficult if not impossible to accomplish and could mislead readers or users of the financial statements. 2. Not reflecting all asset/liabilities on the balance sheet makes this difficult if not impossible to accomplish and could mislead readers or users of the financial statements.

Attachment 1 - Various Definitions for Public-Private Partnerships

Organization	Definition or Description
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.pdfSimilar 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.
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.

Attachment 1 - Various Definitions for Public-Private Partnerships

Organization	Definition or Description
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 (SPE) that is created to implement the project. Agencies usually have retained significant control over the decisions made by the SPE, including the project development and management agreements. The SPEs 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.
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.

ATTACHMENT 2 – Types of Public-Private Partnership Arrangements

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
1. Build-Own-Operate (BOO)	Under a BOO transaction, the contractor constructs and operates a facility without transferring ownership to the public agency. Legal title to the facility remains in the private sector, and there is no obligation for the public agency to purchase the facility or take title. A BOO transaction may qualify for tax-exempt status as a service contract if all Internal Revenue Code requirements are satisfied.	If the public agency decides to: **Lease** – Capital lease requirements are covered in SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i] and SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. **Purchase** – Asset recognition is covered in SFFAS 6, *Accounting for Property, Plant, and Equipment,* paragraph 26[iii].
2. Build/Operate/Transfer (BOT) or 3. Build/Transfer/Operate (BTO)	Under the BOT option, the private partner builds a facility to the specifications agreed to by the public agency, operates the facility for a specified time period under a contract or franchise agreement with the agency, and then transfers the facility to the public agency at the end of the specified period of time. In most cases, the private partner will also provide some, or all, of the financing for the facility, so the length of the contract or franchise must be	**Asset transfer** – can be accomplished either via a lease or a purchase. Capital lease requirements are covered in SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i] and SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. Asset recognition is covered in SFFAS 6, *Accounting for Property, Plant, and*

[7] Source: Government Accountability Office (GAO) Glossary, GAO/GGD-99-71, *Public-Private Partnerships, Terms Related to Building and Facility Partnerships,* dated April 1999 and Congressional Budget Office (CBO) Report , *The Budgetary Treatment of Leases and Public/Private Ventures*, dated February 2003.

[8] Any of the 19 listed Public-Private Partnership types could be part of an arrangement that establishes a Special Purpose Entity (SPE), Special Purpose Vehicle (SPV, Trust or some type of Variable Interest Entity (VIE); where the public agency holds a controlling interest that is not based on the majority of voting rights. Such arrangements would come under the Federal Entity principles which as of the date of this analysis include the following inclusion principles: (a) in the budget, (b) majority ownership interest, (c) control with expected benefits of risk or loss, (d) misleading to exclude. Also, non-core disclosure objectives include relationship, relevant activity and future exposures.

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	sufficient to enable the private partner to realize a reasonable return on its investment through user charges. At the end of the franchise period, the public agency can assume operating responsibility for the facility, contract the operations to the original franchise holder, or award a new contract or franchise to a new private partner. The BTO model is similar to the BOT model except that the transfer to the public owner takes place at the time that construction is completed, rather than at the end of the franchise period.	*Equipment,* paragraph 26[iii]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv].
4. Buy-Build Operate (BBO)	A BBO transaction is a form of asset sale that includes a rehabilitation or expansion of an existing facility. The public agency sells the asset to the private sector entity, which then makes the improvements necessary to operate the facility in a profitable manner.	**At Sale** - SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 38[v] and SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraph 36e – 47[vi]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv].
5. Operations and Maintenance	A public agency (federal, state, or local government agency or authority) contracts with a private partner to operate and/or maintain a specific service. Under the	**At Contract** - SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraph 19[vii].

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	private operation and maintenance option, the public agency retains ownership and overall management of the public facility or system.	
6. Operations, Maintenance, and Management	A public agency (federal, state, or local government agency or authority) contracts with a private partner to operate, maintain, and manage a facility or system providing a service. Under this contract option, the public agency retains ownership of the public facility or system, but the private party may invest its own capital in the facility or system. Any private investment is carefully calculated in relation to its contributions to operational efficiencies and savings over the term of the contract. Generally, the longer the contract term, the greater the opportunity for increased private investment because there is more time available in which to recoup any investment and earn a reasonable return. Many local public governments use this contractual partnership to provide wastewater treatment services.	**At Contract** - SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraph 19[vii]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv].
7. Design-Build-Operate (DBO)	In a DBO project, a single contract is awarded for the design, construction, and operation of a capital improvement. Title to the facility remains with the public agency unless the project is a	**At Contract** - SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraph 19[vii]. **At Build** – SFFAS 6, *Accounting for*

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	design/build/operate/transfer or design/build/own/operate project. The DBO method of contracting is contrary to the separated and sequential approach which involves one contract for design with an architect or engineer, followed by a different contract with a builder for project construction, then followed by the owner's taking over the project and operating it. A simple design-build approach creates a single point of responsibility for design and construction and can speed project completion by facilitating the overlap of the design and construction phases of the project. On a public project, the operations phase is normally handled by the public agency or awarded to the private sector under a separate operations and maintenance agreement. Combining all three phases into a DBO approach maintains the continuity of private sector involvement and can facilitate private-sector financing of public projects supported by user fees generated during the operations phase.	*Property, Plant, and Equipment,* paragraph 34[viii]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv]. **Fees** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraphs 34 – 47[ix].
8. Developer Financing	Under developer financing, the private party (usually a real estate developer)	**Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,*

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	finances the construction or expansion of a public facility in exchange for the right to build residential housing, commercial stores, and/or industrial facilities at the site. The private developer contributes capital and may operate the facility under the oversight of the public agency. The developer gains the right to use the facility and may receive future income from user fees. While developers may in rare cases build a facility, more typically they are charged a fee or required to purchase capacity in an existing facility. This payment is used to expand or upgrade the facility. Developer financing arrangements are often called capacity credits, impact fees, or exactions. Developer financing may be voluntary or involuntary depending on the specific local circumstances.	paragraph 23[iv]. **Fees** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraphs 34 – 47[ix].
9. Enhanced Use Leasing (EUL)	An EUL is an asset management program in the Department of Veterans Affairs (VA) that can include a variety of different leasing arrangements (e.g., lease/develop/operate, build/develop/operate). EULs enable the VA to long-term lease VA-controlled property to the private sector or other public entities for non-VA uses in return for receiving fair consideration (monetary or in-kind) that enhances VA's mission or	**Lease** – SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. **Fees** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraphs 34 – 47[ix].

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	programs. (See 38 U.S.C. § 8161, et seq.)	
10. Lease/Develop/Operate (LDO) or 11. Build/Develop/Operate (BDO)	Under these partnership arrangements, the private party leases or buys an existing facility from a public agency; invests its own capital to renovate, modernize, and/or expand the facility; and then operates it under a contract with the public agency. A number of different types of municipal transit facilities have been leased and developed under LDO and BDO arrangements.	**Lease** – SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. **Sale** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraph 36e – 47[vi]. **Fees** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraphs 34 – 47[ix]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv].
12. Lease/Purchase	A lease/purchase is an installment-purchase contract. Under this model, the private sector finances and builds a new facility, which it then leases to a public agency. The public agency makes scheduled lease payments to the private party. The public agency accrues equity in the facility with each payment. At the end of the lease term, the public agency owns the facility or purchases it at the cost of any remaining unpaid balance in the	**Lease** – SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i] and SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv].

ATTACHMENT 2 – Types of Public-Private Partnership Arrangements

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	lease. Under this arrangement, the facility may be operated by either the public agency or the private developer during the term of the lease. Lease/purchase arrangements have been used by the General Services Administration for building federal office buildings and by a number of states to build prisons and other correctional facilities.	
13. Sale/Leaseback	A sale/leaseback is an arrangement in which the owner of a facility sells it to another entity, and subsequently leases it back from the new owner. An innovative application of the sale/leaseback technique is the sale of a public facility to a public or private holding company for the purposes of limiting public agency liability under certain statutes. Under this arrangement, the public agency that sold the facility leases it back and continues to operate it.	**Sale** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraph 36e – 47[vi]. **Purchase** – SFFAS 6, *Accounting for Property, Plant, and Equipment,* paragraphs 26[iii]. **Lease** – SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i] and SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[iii].
14. Tax-Exempt Lease	Under a tax-exempt lease arrangement, a public agency finances capital assets or facilities by borrowing funds from a private investor or financial institution. The private partner generally acquires title to the asset, but then transfers it to the public agency either at the beginning or end of	**Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv]. **Asset transfer** – can be accomplished either via a lease or a purchase. Capital lease requirements are covered in

TYPE[7]	**DESCRIPTION**	**RELEVANT ACCOUNTING STANDARDS**[8]
	the lease term. The portion of the lease payment used to pay interest on the capital investment is tax exempt under state and federal laws. Tax-exempt leases have been used to finance a wide variety of capital assets, ranging from computers to telecommunication systems and municipal vehicle fleets.	SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i] and SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. Asset recognition is covered in SFFAS 6, *Accounting for Property, Plant, and Equipment,* paragraph 26[iii].
15. Turnkey	Under a turnkey arrangement, a public agency contracts with a private investor/vendor to design and build a complete facility in accordance with specified performance standards and criteria agreed to between the agency and the vendor. The private developer commits to build the facility for a fixed price and absorbs the construction risk of meeting that price commitment. Generally, in a turnkey transaction, the private partners use fast-track construction techniques (such as design-build) and are not bound by traditional public agency procurement regulations. This combination often enables the private partner to complete the facility in significantly less time and for less cost than could be accomplished under traditional construction techniques. In a turnkey transaction, financing and ownership of the facility can rest with	**Purchase** – SFFAS 6, *Accounting for Property, Plant, and Equipment,* paragraphs 26 [iii]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23 [iv]. **Risk assumption** - SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i].

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	either the public or private partner. For example, the public agency might provide the financing, with the attendant costs and risks. Alternatively, the private party might provide the financing capital, generally in exchange for a long-term contract to operate the facility.	
16. Concession Benefits	Concession benefits are rights to receive revenues or other benefits for a fixed period of time. (Also see franchising.)	**Fees** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraphs 34 – 47[ix].
17. Cooperative Agreements	A cooperative agreement as set forth in 31 USC 6305 is the legal instrument an executive agency uses to reflect a relationship between the U.S. public agency and a state, a local public agency, or other recipient when (1) the principal purpose of the relationship is to transfer a thing of value to the state, local public agency, or other recipient to carry out a public purpose of support or stimulation authorized by U.S. law, and (2) substantial involvement is expected between the executive agency and the state, local public agency, or other recipient in carrying out the activity contemplated in the agreement.	**Asset transfer** – can be accomplished either via a lease or a purchase. Capital lease requirements are covered in SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i] and SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. Asset recognition is covered in SFFAS 6, *Accounting for Property, Plant, and Equipment,* paragraph 26[iii]. **Risk Assumption** - SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraph 19[vii]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,*

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
		paragraph 23[iv].
18. Franchising	Under the franchising of external services, the public agency grants a concession or privilege to a private-sector entity to conduct business in a particular market or geographical area—for example, operating concession stands, hotels, and other services provided in certain national parks. The public agency may regulate the service level or price, but users of the service pay the provider directly.	**Lease** – SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. **Fees** - SFFAS 7, *Accounting for Revenue and Other Financing Sources and Concepts for Reconciling Budgetary and Financial Accounting,* paragraphs 34 – 47[ix].
19. Lease – Leaseback	In an arrangement called lease-leaseback, the public agency leases an asset long-term (i.e. for 50 years) to a private-sector entity or a special-purpose entity created for that purpose and then leases the asset back for a shorter period (i.e.,20 years or about half of the asset's useful life). The private-sector entity or special-purpose entity pays for their long-term lease with a one-time, upfront payment, while the public agency spreads its leaseback payments over the (shorter) lease period. Such transactions generate up-front cash for the public agency allowing it to avoid seeking either budgetary appropriations or	**Lease** – SFFAS 5, *Accounting for Liabilities of the Federal Public agency,* paragraphs 43 – 46[i] and SFFAS 6, *Accounting for Property, Plant, and Equipment*, paragraph 20[ii]. **Financing** – SFFAS 2, *Accounting for Direct Loans and Loan Guarantees,* paragraph 23[iv].

TYPE[7]	DESCRIPTION	RELEVANT ACCOUNTING STANDARDS[8]
	issuing additional bonds to finance its investments. In effect, the private-sector entity or special-purpose entity borrows on behalf of public agency. The private sector partner obtains financing through the sale of pass-through certificates which the public agency may or may not explicitly guarantee. However, these certificates are usually fully backed by the public agency's contractual commitment to make lease payments. The public agency entity benefits from some of the tax advantages that the private sector partner enjoys in the form of lower lease payments.	

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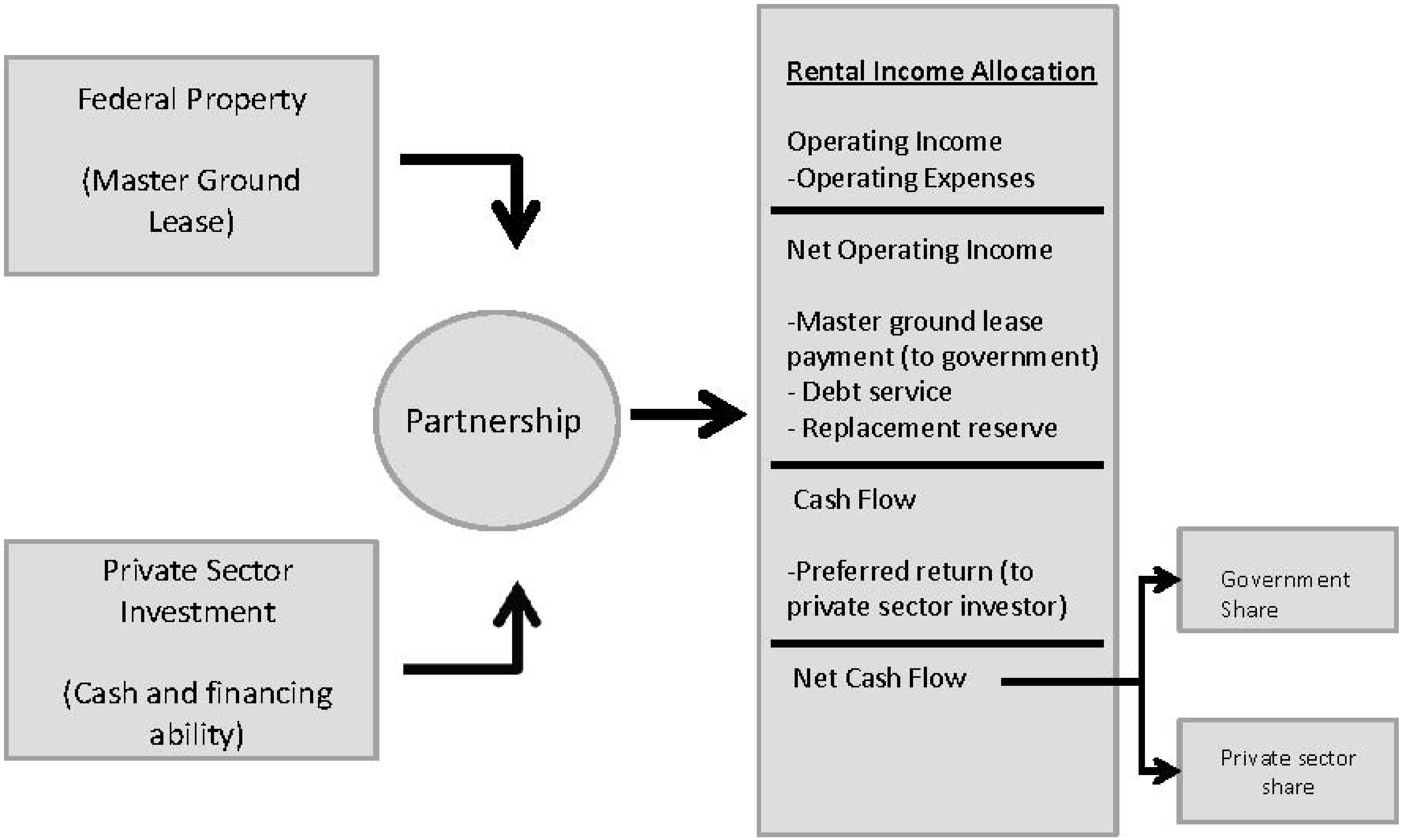
ATTACHMENT 3 –Sample Public-Private Partnership Arrangement



ATTACHMENT 2 - END NOTES

[i] 43. Capital leases are leases that transfer substantially all the benefits and risks of ownership to the lessee. If, at its inception, a lease meets one or more of the following four criteria, the lease should be classified as a capital lease by the lessee:

- The lease transfers ownership of the property to the lessee by the end of the lease term.
- The lease contains an option to purchase the leased property at a bargain price.
- The lease term is equal to or greater than 75 percent of the estimated economic life of the leased property.
- The present value of rental and other minimum lease payments, excluding that portion of the payments representing executory cost, equals or exceeds 90 percent of the fair value of the leased property.

The last two criteria are not applicable when the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property. If a lease does not meet at least one of the above criteria it should be classified as an operating lease.

44. The amount to be recorded by the lessee as a liability under a capital lease is the present value of the rental and other minimum lease payments during the lease term, excluding that portion of the payments representing executory cost to be paid by the lessor.20
However, if the amount so determined exceeds the fair value of the leased property at the inception of the lease, the amount recorded as the liability should be the fair value. If the portion of the minimum lease payments representing executory cost is not determinable from the lease provisions, the amount should be estimated.

45. The discount rate to be used in determining the present value of the minimum lease payments ordinarily would be the lessee's incremental borrowing rate unless (1) it is practicable for the lessee to learn the implicit rate computed by the lessor and (2) the implicit rate computed by the lessor is less than the lessee's incremental borrowing rate. If both these conditions are met, the lessee shall use the implicit rate. The lessee's incremental borrowing rate shall be the Treasury borrowing rate for securities of similar maturity to the term of the lease.

46. During the lease term, each minimum lease payment should be allocated between a reduction of the obligation and interest expense so as to produce a constant periodic rate of interest on the remaining balance of the liability.

[ii] 20. Capital leases are leases that transfer substantially all the benefits and risks of ownership to the lessee. If, at its inception, a lease meets one or more of the following four criteria, the lease should be classified as a capital lease by the lessee. Otherwise, it should be classified as an operating lease.

- The lease transfers ownership of the property to the lessee by the end of the lease term.
- The lease contains an option to purchase the leased property at a bargain price.
- The lease term is equal to or greater than 75 percent of the estimated economic life9 of the leased property.
- The present value of rental and other minimum lease payments, excluding that portion of the payments representing executor cost, equals or exceeds 90 percent of the fair value of the leased property. The last two criteria are not applicable when the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property.

[iii] 26. All general PP&E shall be recorded at cost. Cost shall include all costs incurred to bring the PP&E to a form and location suitable for its intended use. For example, the cost of acquiring property, plant, and equipment may include:

- amounts paid to vendors;
- transportation charges to the point of initial use; • handling and storage costs;
- labor and other direct or indirect production costs (for assets produced or constructed);
- engineering, architectural, and other outside services for designs, plans, specifications, and surveys;
- acquisition and preparation costs of buildings and other facilities;
- an appropriate share of the cost of the equipment and facilities used in construction work;
- fixed equipment and related installation costs required for activities in a building or facility;
- direct costs of inspection, supervision, and administration of construction contracts and construction work;
- legal and recording fees and damage claims;
- fair value of facilities and equipment donated to the government; and
- material amounts of interest costs paid.

[iv] Post-1991 Loan Guarantees. 23. For guaranteed loans outstanding, the present value of estimated net cash outflows of the loan guarantees is recognized as a liability. Disclosure is made of the face value of guaranteed loans outstanding and the amount guaranteed.

[v] 38. In the period of disposal, retirement, or removal from service, general PP&E shall be removed from the asset accounts along with associated accumulated depreciation/amortization. Any difference between the book value of the PP&E and amounts realized30 shall be recognized as a gain or a loss in the period that the general PP&E is disposed of, retired, or removed from service.

[vi] 36. Revenue from specific types of exchange transactions should be recognized as follows: (e) When an asset other than inventory is sold, any gain (or loss) should be recognized when the asset is delivered to the purchaser.

37. When advance fees or payments are received, such as for large-scale, long-term projects, revenue should not be recognized until costs are incurred from providing the goods and services (regardless of whether the fee or payment is refundable). An increase in cash and an increase in liabilities, such as “unearned revenue,” should be recorded when the cash is received. “Unearned revenue” should also be recorded if an agency requests advances or progress payments prior to the receipt of cash and records the amount.

38. The measurement basis for revenue from exchange transactions should be the actual price that is received or receivable under the established pricing arrangements.

39. When cash has not yet been received at the time revenue is recognized, a receivable should be recorded. An appropriate allowance for estimated bad debts should be established.

40. To the extent that realization of the full amount of revenue is not probable due to credit losses (caused by the failure of the debtor to pay the established or negotiated price), an expense should be recognized and the allowance for bad debts increased if the bad debts can be reasonably estimated. The amount of the bad debt expense should be separately shown.

41. To the extent that realization of the full amount of revenue is not probable due to returns, allowances, price redeterminations, or other reasons apart from credit losses, the revenue that is recognized should be reduced by separate provisions if the amounts can be reasonably estimated. The amounts of such provisions should be reflected as revenue adjustments, rather than costs of operations, and should be separately shown.

42. The recognition and measurement of revenue and credit losses due to direct loans and loan guarantees is determined by SFFAS No. 2, Accounting for Direct Loans and Loan Guarantees. Appropriate allowances should be established as determined by those standards.

43. Exchange revenue should be recognized in determining the net cost of operations of the reporting entity during the period. The exchange revenue should be recognized regardless of whether the entity retains the revenue for its own use or transfers it to other entities. Gross and net cost should be calculated as appropriate to determine the costs of outputs and the total net cost of operations of the reporting entity. The components of the net cost calculation should separately include the gross cost of providing goods or services that earned exchange revenue, less the exchange revenue earned, and the resulting difference. The components of net cost should also include separately the gross cost of providing goods, services, benefit payments, or grants that did not earn exchange revenue. The U.S. government-wide financial statements need not break out gross costs of providing goods, services, benefit payments, or grants that did not earn exchange revenue, separately from those programs that earned exchange revenue.

44. The net amount of gains (or losses) should be subtracted from (or added to) gross cost to determine net cost in the same manner as exchange revenue is subtracted. Exchange revenue that is immaterial or cannot be associated with particular outputs should be deducted separately in calculating the net cost of the program, suborganization, or reporting entity as a whole as appropriate. Nonexchange revenues and other financing sources should not be deducted from the gross cost in determining the net cost of operations for the reporting entity.

45. Under exceptional circumstances, such as rents and royalties on the Outer Continental Shelf, an entity recognizes virtually no costs (either during the current period or during past periods) in connection with earning revenue that it collects.

45.1 The collecting entity should not offset its gross costs by such exchange revenue in determining its net cost of operations. If such exchange revenue is retained by the entity, it should be recognized as a financing source in determining the entity's operating results. If, instead, such revenue is collected on behalf of other entities (including the U.S. Government as a whole), the entity that collects the revenue should account for that revenue as a custodial activity, i.e., an amount collected for others.

45.2 If the collecting entity transfers the exchange revenue to other entities, similar recognition by other entities is appropriate.

a. If the other entities to which the revenue is transferred also recognize virtually no costs in connection with the Government earning the revenue, the amounts transferred to them should not offset their gross cost in determining their net cost of operations but rather should be recognized as a financing source in determining their operating results.

b. If the other entities to which the revenue is transferred do recognize costs in connection with the Government earning the revenue, the amounts transferred to them should offset their gross cost in determining their net cost of operations.

45.3 Because the revenue is exchange revenue regardless of whether related costs are recognized, it should be recognized and measured under the exchange revenue standards.

DISCLOSURES AND OTHER ACCOMPANYING INFORMATION

46. Each reporting entity that provides goods or services to the public or another Government entity should disclose the following:
(a) differences in pricing policy from the full cost or market pricing guidance for exchange transactions with the public as set forth in OMB Circular No. A-25, User Charges (July 8, 1993), or in subsequent amendments in circulars that set forth pricing guidance; (b) exchange transactions with the public in which prices are set by what extent, the quantity demanded was assumed to change as a result of a change in price. law or executive order and are not based on full cost or on market price; (c) the nature of intragovernmental exchange transactions in which the entity provides goods or services at a price less than the full cost or does not charge a price at all, with explanations of the amount and reason for disparities between the billing (if any) and the full cost; and
(d) the full amount of the expected loss when specific goods are made to order under a contract, or specific services are produced to order under a contract, and a loss on the contract is probable (more likely than not) and measurable (reasonably estimable).
The above listed disclosure requirements are not applicable to the U.S. government-wide financial statements.

47. When making the disclosures called for by (a) and (b) in paragraph 46, cautionary language should be added to the effect that higher prices based on full cost or market price might reduce the quantity of goods or services demanded and, therefore, the difference between revenue received and such higher prices does not necessarily provide an indication of revenue foregone. If a reasonable estimate is practicable to make, the entity should provide as other accompanying information the amount of revenue foregone and should explain whether, and to what extent, the quantity demanded was assumed to change as a result of a change in price.

[vii] Definition And General Principle For Recognition Of A Liability

19. A liability for federal accounting purposes is a probable future outflow or other sacrifice of resources as a result of past transactions or events. General purpose federal financial reports should recognize probable and measurable future outflows or other sacrifices of resources arising from (1) past exchange transactions, (2) government-related events, (3) government-acknowledged events, or (4) nonexchange transactions that, according to current law and applicable policy, are unpaid amounts due as of the reporting date.

[viii] 34. PP&E shall be recognized when title passes to the acquiring entity or when the PP&E is delivered to the entity or to an agent of the entity. In the case of constructed PP&E, the PP&E shall be recorded as construction work in process until it is placed in service, at which time the balance shall be transferred to general PP&E.

[ix] RECOGNITION AND MEASUREMENT OF EXCHANGE REVENUE

34. Revenue from exchange transactions should be recognized when goods or services are provided to the public or another Government entity at a price.

35. When a transaction with the public or another Government entity at a price is unusual or nonrecurring, a gain or loss should be recognized rather than revenue or expense so as to differentiate such transactions.

36. Revenue from specific types of exchange transactions should be recognized as follows:

(a) When services are provided to the public or another Government entity (except for specific services produced to order under a contract), revenue should be recognized when the services are performed.

(b) When specific goods are made to order under a contract (either short- or long-term), or specific services are produced to order under a contract (either short- or long-term), revenue should be recognized in proportion to estimated total cost when goods and services are acquired to fulfill the contract. If a loss is probable (more likely than not), revenue should continue to be recognized in proportion to the estimated total cost and costs should continue to be recognized when goods and services are acquired to fulfill the contract. Thus, the loss should be recognized in proportion to total cost over the life of the contract.