EUROPEAN COMMISSION
EUROSTAT

Directorate C: Macro-economic statistics
Unit C1: National accounts methodology; Standards and indicators

**EPSAS WG 20/11**

**Luxembourg, 15 October 2020**

# EPSAS Working Group meeting

To be held in Luxembourg by videoconference

on 09-10 November 2020, starting at 10:00

**Item 4 of the Agenda**

# Draft EPSAS Screening Report
# IPSAS 32 – Service Concession Arrangements: Grantor

*Paper by PwC in cooperation with Eurostat*

*- for discussion -*

*This document was commissioned by Eurostat. It analyses the consistency of the named IPSAS standard with the draft EPSAS framework, with a view to informing future EPSAS standard setting. This version was prepared taking into account comments received from the participants of the Cell on Principles related to EPSAS Standards.*

# EPSAS screening report

IPSAS 32 - Service concession arrangements: grantor

October 2020

# Table of contents

Background 3

Screening of IPSAS 32 ‘Service concession arrangements: grantor’ against criteria set in the draft EPSAS framework 6

Conformity with Qualitative Characteristics 6

Alignment with other frameworks 16

European Public Good 18

Conclusion 20

# Background

### Objectives

Reference should be made to the general introduction to the EPSAS screening reports that covers the following elements:

- Key objectives of EPSAS.
- Standard setting process in the public sector.
- Purpose and scope of the screening reports.
- Approach of the screening reports.
- European public good.
- Common elements considered when preparing the reports.

### General introduction to IPSAS 32

IPSAS 32 'Service concession arrangements: grantor' is adapted from Interpretation 12 (IFRIC 12) 'Service concession arrangements', developed by the International Financial Reporting Interpretations Committee and published by the International Accounting Standards Board (IASB). This IPSAS also contains extracts from Interpretation 29 (SIC-29) 'Service concession arrangements: disclosures'. In developing IPSAS 32, the International Public Sector Accounting Standards Board (IPSASB) applied its 'Process for Reviewing and Modifying IASB Documents' that identifies public sector modifications where appropriate. This approach enables the IPSASB to build on best practices in private sector financial reporting, while ensuring that the unique features of the public sector are addressed.

A service concession arrangement is defined in IPSAS 32 as a binding arrangement between a grantor (usually a government or other public sector body) and an operator, in which the operator:

(a) Uses the service concession asset to provide a public service on behalf of the grantor for a specified period of time; and

(b) Is compensated for its services over the period of the service concession arrangement' (IPSAS 32.8).

A service concession asset can both be tangible (IPSAS 17 'Property, plant and equipment') or intangible (IPSAS 31 'Intangible assets') as long as it fulfils the definition of an asset and is used to provide public services in a service concession arrangement. A service concession arrangement can also be either a new asset as it is being constructed or upgraded, or a reclassification from other tangible or intangible assets in the balance sheet (IPSAS 32.9).

There is a wide variation in the accounting treatment of service concession arrangements in the Member States, and accounting for such structures poses challenges to the financial accountants in the countries. The main accounting issue in service concession arrangements is whether the grantor should recognise such arrangements on or off its balance sheet.

**Scope of the report**

The present screening report analyses the recognition, measurement, presentation and disclosure requirements of service concession arrangements from the point of view of the grantor.

**Reference to EFRAG assessment**

EFRAG published its final endorsement advice on IFRIC 12 (as revised in 2006) in March 2007. EFRAG's overall assessment is that it is not contrary to the 'true and fair principle'; and it meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

All EFRAG members agree that IFRIC 12 ensures much greater consistency in accounting for service concession arrangements. The majority of EFRAG members believe that the appropriate principles have been identified for service concession arrangements (some question whether certain aspects of the model are based on a correct interpretation of existing IFRS). Furthermore, all but two EFRAG members considered the resulting accounting treatment for service concession arrangements as acceptable.

**Reference to EPSAS issue papers[1]**

The PwC study of 2014[2] analysed the suitability of the IPSAS standards as a basis for developing EPSAS. This included the analysis of IPSAS 32. Following this analysis, IPSAS 32 was classified among the category 'Standards that could be implemented with minor or no adaptations'.

During the course of developing the technical proposal on EPSAS, Eurostat commissioned a series of twenty technical issues papers (IPs), which analyse in particular key public sector specific accounting issues. The papers were discussed at the EPSAS Working Group meetings during the period 2016-2018. The papers are all publicly available on Eurostat's website.

The EPSAS issue paper on service concession arrangements was discussed by the EPSAS WG on 19-20 November 2018.

[1] EPSAS Issues papers are available on https://ec.europa.eu/eurostat/web/epsas/key-documents/technical-developments

[2] Collection of information related to the potential impact, including costs, of implementing accrual accounting in the public sector and technical analysis of the suitability of individual IPSAS standards (Ref. 2013/S 107-182395)

Eurostat tentatively concluded the following:

- In addition to the standard on this highly complex accounting area, efforts should be placed on devising processes, and on monitoring and audit, in order to secure comprehensive, sound and comparable recognition and measurement of service concession arrangements at the reporting entity level. The discussion confirmed the earlier position that the future EPSAS standard needed to be complemented by clear guidance.
- It was not possible to “unify” the approaches of financial accounting and statistics, as in the case of the former the key objective was to provide information for decision-making and accountability, whereas in the case of the latter the aim was mainly to serve macroeconomic analyses and fiscal surveillance. From a financial accounting point of view, the comprehensive recognition and measurement of service concession arrangements also served entity level financial management purposes. In addition, the main purpose of EDP reporting was to provide information for net lending/borrowing and gross debt, which did not in themselves serve the same decision making and accountability purposes as financial reporting.
- Even if, under financial accounting terms, IPSAS/EPSAS would be recognising more concession arrangements in general purpose financial statements than would be recognised in national accounts/ GFS, this was helpful for statisticians as it facilitated the selection of those concession arrangements that were falling within the scope of national accounts/ GFS rules.
- Transparency on what was recognised or not recognised, and for which purpose, in both of the two reporting frameworks was a key piece of information for users of financial statements and statistics. Moreover, public audit had a significant role to play in this respect.

# Screening of IPSAS 32 ‘Service concession arrangements: grantor’ against criteria set in the draft EPSAS framework

### Introduction

The EPSAS criteria listed in the draft EPSAS framework have been used to perform an assessment of IPSAS 32 ‘Service concession arrangements: grantor’, published in 2011 by the IPSASB, with minor amendments made from that date.

In order to develop recommendations, one should first consider whether IPSAS 32 would meet the qualitative characteristics of the draft EPSAS CF, i.e. whether it would provide relevant, reliable, complete, prudent, neutral, verifiable, economically substantive, understandable, timely and comparable information and would not be contrary to the true and fair view principle.

This report considers recognition, classification and measurement as well as presentation and disclosure requirements applicable to service concession arrangements for each of the qualitative characteristics of the draft EPSAS CF.

Further, this paper includes a high-level comparison between the requirements of IPSAS 32 and other international accounting and financial reporting frameworks applied by the public sector entities in various jurisdictions, such as IFRS, ESA 2010 and EU Accounting Rules, bearing in mind the objective of alignment, reduction of cost of implementation and compliance cost.

The findings are presented below and the conclusion is included in the next section of this report.

## Conformity with Qualitative Characteristics

### Relevance

Financial and non-financial information is relevant if it is capable of making a difference in achieving the objectives of GPFSs. Financial and non-financial information is capable of making a difference when it has confirmatory value, predictive value, or both.

The objective of the IPSAS 32 standard is to prescribe the accounting treatment for service concession arrangements by the grantor, a public sector entity. The standard addresses the general accounting requirements for service concession arrangements; assets and liabilities recognised as a consequence of service concession arrangements should be treated in accordance with the relevant standards. This includes IPSAS 17 ‘Property, plant and equipment’ and IPSAS 31 ‘Intangible assets’ for assets, as well as IPSAS 28 ‘Financial Instruments: Presentation’ and IPSAS 41 ‘Financial Instruments’ for financial liabilities.

The principal issues in accounting for service concession arrangements are the following:

- Conceptual approach to asset recognition.
- Treatment of service concession arrangements by the public sector operator.
- Technical complexity.
- Treatment of non-financial liabilities.
- Consistency of presentation and disclosures.

Under IPSAS, recognition of the service concession asset by the grantor (i.e. the public sector entity) is based on whether it controls that asset and not on whether it bears the risks and rewards related to it. All facts and circumstances of the arrangement should be considered in making this assessment.

*Service concession assets*

The recognition principles in the standard are consistent with the definition of an asset in the draft EPSAS CF. As a reminder, an asset is a resource presently controlled by the entity as a result of past events or transactions. A resource is an item with service potential or the ability to generate economic benefits. Service potential is the capacity to provide services that contribute to achieving the entity's objectives. Economic benefits are cash inflows or a reduction in cash outflows.

The grantor recognises an asset provided by the operator and an upgrade to an existing asset of the grantor as a service concession asset if it:

- Controls or regulates what services the operator must provide with the asset, to whom it must provide them, and at what price; and

- Controls - through ownership, beneficial entitlement or otherwise - any significant residual interest in the asset at the end of the term of the arrangement (IPSAS 32.9).

For ‘whole–of-life assets’, only the first requirement above must be fulfilled.

Service concession assets and corresponding liabilities are recognised as progress is made towards completion of the asset, (...) where the grantor has little ability to avoid accepting an asset constructed or developed to meet the specifications of the contract, or a similar binding arrangement (...) (IPSAS 32.AG23). During the construction phase, this approach should be applied carefully, bearing in mind the definition of an asset in the EPSAS CF, to make sure that the assets under construction are not recognised before control actually transfers to the grantor.

The grantor initially measures the service concession asset at its fair value (e.g. during the construction or development of the asset, the costs may be measurable based on the progress reports given by the operator-constructor), except when it already owns the asset. Where an existing asset of the grantor meets the conditions to be recognised as a service concession asset, the grantor reclassifies the existing asset as a service concession asset. The reclassified service concession asset is accounted for in accordance with IPSAS 17 ‘Property, plant and equipment’ or IPSAS 31 ‘Intangible assets’, as appropriate.

After initial recognition or reclassification, service concession assets follow the accounting policies applicable to the class of assets to which they belong, in accordance with IPSAS 17 or IPSAS 31, as appropriate.

*Related liabilities*

When a service concession asset is recognised, a corresponding liability is also recognised, unless the concession asset is an existing asset that the grantor simply needs to reclassify from property, plant and equipment or intangible assets, as appropriate.

The treatment, by the grantor, of the liability side in a service concession arrangement depends on the type of arrangement. The grantor should analyse the substance of the arrangement and follow either the financial liability model or the grant of a right to the operator model (in which revenue is not recognised upfront but deferred as a non-financial liability recognised in surplus/deficit over the term of the concession).

*Predictive and confirmatory value*

Information about assets and liabilities has both predictive and confirmatory value, since the initial measurement of a service concession asset is its fair value. This fair value would represent the level of investment made by the operator in the infrastructure, helping the user to estimate its service potential.

Subsequent measurement made by grantors is based on the requirements of IPSAS 17 and/or IPSAS 31. Items of property, plant and equipment and intangible assets are measured subsequent to initial recognition at either cost less accumulated depreciation and any accumulated impairment losses, or at a revaluation amount (except for intangibles for which no active market exists).

Apart from recognition and measurement, disclosures also provide relevant information, enabling the users to interpret the amounts with a description of the arrangement, and the significant terms that may affect the amount, timing, and certainty of future cash flows. Further details are provided in the ‘Completeness’ QC section.

**Faithful representation / Reliability**

The notion of faithful representation and reliability in the draft EPSAS CF is linked to the qualitative characteristics of completeness, prudence, neutrality, verifiability and substance over form. These are separately discussed below.

Overall, IPSAS 32 provides a faithful representation of the economic phenomena that it purports to represent. However, it does not include specific guidance on the accounting by public sector entities acting as operators.

Although operators in service concession arrangements are generally private companies, public sector entities can also sometimes act as operators. The scope of IPSAS 32 is limited only to the accounting of service concession arrangements from the perspective of the grantor. The standard does not specify the accounting by operators, and IPSAS 32.7 refers to the relevant international or national accounting standard dealing with service concession arrangements.

The fact that the operator can use national or international accounting standards could lead to diversity, depending on whether these national standards have substantially the same principles as IFRS (in this case, IFRIC 12). Consequently, this reference to the national accounting standards may (potentially) result in a significantly different accounting for transactions in which the public entity acts as an operator. Application of EPSAS CF (and notably IFRIC 12 requirements developed under a similar IFRS CF) would reduce these potential differences.

**Completeness**

The information which fulfils the recognition criteria should be complete within the bounds of materiality and cost-benefit considerations.

Application of the control-based approach under IPSAS 32 leads to recognition of all service concession assets which comply with the **definition of assets** in the IPSAS Conceptual framework. The comprehensive reporting of such assets on the balance sheet better serves the accountability and decision-making objectives of financial statements: it provides a more comprehensive picture of the **assets under the control of the government entity and therefore of the resources entrusted to that government entity**, which is key information for a public sector entity.

In addition to the recognition and measurement criteria for assets and liabilities mentioned in the 'Relevance' QC, information should be also disclosed in the notes to the financial statements. The key disclosures to be provided include, individually for each material service concession arrangement or in aggregate for service concession arrangements involving services of a similar nature:

- A description of the arrangement, and the significant terms that may affect the amount, timing, and certainty of future cash flows, such as the period of the concession, re-pricing dates, and the basis upon which re-pricing or re-negotiation is determined.
- The nature and extent of rights to use specified assets and to expect the operator to provide specified services, service concession assets recognised during the period, rights to receive specified assets at the end of the service concession arrangement, renewal and termination options, other rights and obligations, and obligations to provide the operator with access to service concession assets or other revenue generating assets.
- Changes in the arrangement occurring during the period.

## Prudence

The ‘Prudence’ QC is achieved with the inclusion of a degree of caution in the exercise of the judgments needed in making the estimates required under conditions of uncertainty, such assets or revenue are not overstated while liabilities or expenses are not understated.

When recognising a service concession asset, a liability is usually also recognised. Where the grantor has an unconditional obligation to make payments or give another financial asset to the operator, IPSAS 32 requires the recognition of a financial liability at fair value. When it does not have such an obligation (i.e. under the grant of a right to the operator model), the grantor accounts for a non-financial liability as the portion of the revenue arising from the exchange of assets between the grantor and the operator should not be recognised upfront.

The IPSASB debated on whether the credit to the asset under the grant of a right to the operator model should be a liability, net assets/equity, or revenue. The IPSASB decided to treat the credit to the service concession asset as revenue (IPSAS 32 BC35), since the credit does not represent a direct increase in the grantor’s net assets/equity:

- the operator has not made a contribution to the grantor that results in a financial resource that could be considered as contribution from owners;
- the credit related to the recognition of a service concession asset represents an individual transaction and not an accumulation of an entity’s surpluses and deficits;
- reserves generally arise from items recognised directly in net assets/equity under specific IPSAS requirements. The credit related to the recognition or reclassification of a service concession asset does not represent such a gain or loss;
- the credit related to the recognition of a service concession asset does not meet the definition of a non-controlling interest because the operator does not have such an interest in the grantor.

In line with that reasoning, the IPSASB agreed that the credit represents revenue arising from an exchange transaction. However, until the criteria for recognition of revenue have been satisfied, the credit is recognised as a (non-financial) liability.

## Neutrality

Information is neutral if it is free from bias. GPFSs are not neutral if the information they contain has been selected or presented in a manner designed to influence a decision or judgment in order to achieve a predetermined result or outcome.

Under IPSAS 32, the grantor recognises the underlying asset, both in the financial liability model and the grant of a right to the operator model. The reason for recognition is that the service concession asset is controlled by the grantor.

Application of a control-based approach brings greater neutrality in the EPSAS reporting, compared to a risk and rewards approach, as it makes it more difficult to structure certain transactions in a way that allows assets used by the entity (and the related liabilities) to be presented off balance sheet. Moreover, this principle is consistent with the new lease model for the public sector (currently under development by the IPSASB).

However, inconsistent interpretation of the control principle could lead to diversity in accounting for service concessions, especially for complex arrangements, as noted under the 'Substance over form' QC.

**Verifiability**

The 'Verifiability' QC is achieved when the quality of information assures users that GPFSs are based on supporting evidence in a way that it faithfully represents the substance of economic and other phenomena that it purports to represent.

The grantor initially measures the service concession asset at its fair value, except when it already owns the asset. Where an existing asset of the grantor meets the conditions to be recognised as a service concession asset, the grantor reclassifies the existing asset as a service concession asset. The reclassified service concession asset is accounted for in accordance with IPSAS 17 'Property, plant and equipment' or IPSAS 31 'Intangible assets', as appropriate.

The grantor must have reliable information about the cost or fair value of the asset during its construction or development for it to be recognised. This may be obtained from the progress reports which the operator may deliver periodically to the grantor. This evidence would normally result in information to be verifiable. However, it should also be further stressed that the reliability and verifiability aspects largely depend on the availability and the reliability of data on the performance of the service concession provided by an external party (i.e. operator).

IPSAS 32.AG25 states that the type of compensation exchanged between the grantor and the operator affects how the fair value of the service concession asset is determined on initial recognition. Fair value on initial recognition is determined by:

(a) the fair value of the (stream of) payments for the asset, where payments are made by the grantor to the operator,

(b) the same way as an exchange of non-monetary assets in IPSAS 17 and IPSAS 31, where the grantor does not make payments to the operator for the asset.

This information provided would result in its being verifiable, by its supporting documentation, and to a certain extent, by the cash flow information provided in the different notes of the financial statements.

### Substance over form

The ‘Substance over form’ QC requires that the underlying transactions, other events, activities or circumstances are accounted for and presented in accordance with their substance and economic reality, and not merely their legal form.

The party who has control over the service concession asset recognises the asset and a corresponding liability in the balance sheet. The grantor has control over the service concession asset when it regulates both the service and the price to the end user and has a significant residual interest in the asset.

*Partly regulated use of the service concession asset*

Sometimes, in practice, the use of a service concession asset is only partly regulated with regards to what services the operator must provide with the asset, to whom it must provide them, and at what price.

In these situations, the overall assessment of whether or not the service concession asset should be recognised will depend on the extent to which they are regulated. IPSAS 32 provides with the following guidance in para AG12:

- When a portion of an asset is physically separable and meets the definition of a cash-generating unit (e.g. a hospital wing), control should be assessed separately.

- The provision of “purely ancillary activities” (e.g. a hospital shop) do not affect the control tests; these are being applied as if those services did not exist.

However, in practice, there is a wide variety of combinations of partially regulated assets, which are not delivered in physically separable portions of the asset. Examples of more complex, yet common arrangements, include:

- where prices for the same activities are regulated for some public, and not for others; or
- where prices are regulated at certain times, but not at others (hour restrictions).

Thus, further guidance could be provided in order to identify the point until which a partially regulated activity can be considered as ‘purely ancillary’, or the assessment that needs to be made when the portion of the asset is not physically separable.

*Significant residual interest*

The assessment of whether the grantor controls the service concession asset includes the assessment of whether it has any significant residual interest in the asset at the end of the term of the arrangement. Further guidance could be provided on how ‘significant residual interest’ should be interpreted.

IPSAS 32.AG9 clarifies that:

- it should restrict both the operator's practical ability to sell or pledge the asset and give the grantor a continuing right of use throughout the period of the service concession arrangement; and that
- the residual interest in the asset is the estimated current value of the asset as if it were already of the age and in the condition expected at the end of the period of the service concession arrangement.

However, the term 'significant' is not defined, so some diversity in practice can be expected. In some cases, a grantor has the option to reacquire the asset at the end of the concession period. Applying guidance in IPSAS 32, it may be unclear how this price (fair value or not) may affect the conclusions regarding control.

EFRAG identified the same issue during the analysis of IFRIC 12 and included the following statement: "*Ideally, every scope section in every IFRS and every IFRIC Interpretation should be crystal clear. However, in a principles-based set of financial reporting requirements that will rarely be the case. Instead, those applying IFRS are expected to use their judgement and those judgements will often play a fundamental role in the accounting process (…)".*

**Understandability**

The 'Understandability' QC is the quality of presenting information in a manner that facilitates expert and non-expert users to comprehend its meaning. Understandability is enhanced when information is classified, characterised and presented clearly and concisely.

Service concession agreements may be complex, making it complicated to assess how to apply recognition and measurement rules and how to report assets, liabilities and revenue. There can also be hybrid structures with features of both an availability structure and a user pay structure[3] therefore making the accounting treatment more complex.

The analysis of such transactions under the future EPSAS rules will require specific expertise from Member States in order to properly reflect the substance of the transaction in their government financial statements.

The distinction between the financial liability model and the grant of a right to the operator model is based on the fact (and the extent) that the grantor has an unconditional obligation to pay cash or another financial asset to the operator for the construction, development, acquisition, or upgrade of a service concession asset.

[3] Typically, service concession arrangements are either grantor pay structures (where the operator designs, builds, finances, operates and/or maintains a project in exchange for a payment stream from the grantor) or user pay ("traditional concession") structures (where the operator designs, builds, finances, operates and/or maintains a project in exchange for a right to charge users). Grantor pay structures may be availability structures or demand-based structures (for the latter payments by the grantor to the operator are variable based on the demand and use of the asset, e.g. infrastructure asset such as a motorway), or a combination of the two.

The grantor has an unconditional obligation to pay cash to the operator when the grantor has guaranteed to the operator the payment of (a) specified or determinable amounts; or (b) the shortfall, if any, between amounts received by the operator from users of the public service and any specified or determinable amounts (even if the payment is contingent upon the operator ensuring that the service concession asset meets specified quality or efficiency requirements).

**Comparability**

A key objective of EPSAS is to achieve the necessary level of financial transparency and comparability of financial reporting, between and within EU Member States.

Application of the control-based approach required by IPSAS 32 brings greater consistency in the way concession arrangements would be reported using a risks and rewards approach. Application of IPSAS 32 requirements makes it more difficult to structure transactions to achieve off-balance sheet treatment. In addition, in many service concession arrangements, the risks are shared between the grantor and the operator and objectives criteria for assessing risks and rewards are difficult to determine. Assessing which party is the economic owner based on a risks and rewards analysis would therefore often be highly judgemental and would require significant efforts to ensure comparability across the Member States.

In complex arrangements, the determination of whether a grantor controls the service concession asset may be open to interpretation, due to the limited guidance provided, as noted in the ‘Substance over form’ QC. Thus, comparability would be enhanced by providing additional guidance on this respect.

IPSAS requires accounting for service concession assets as a separate class of assets. However, such assets do not necessarily need to be presented separately on the face of the statement of financial position. The same applies to (financial or non-financial) liabilities that are recorded in relation to service concession assets. Specific requirements for its presentation in the face of the financial statements may lead to a higher degree of harmonisation in this respect.

Discussion under the QC ‘Faithful representation/Reliability’ about the accounting by operators could also be relevant to the assessment of comparability. As a reminder, the scope of IPSAS 32 is limited only to the accounting of service concession arrangements from the perspective of the grantor. The standard does not specify the accounting by operators, and IPSAS 32.7 refers to the relevant international or national accounting standard dealing with service concession arrangements.

*Consistency of presentation*

As noted in the ‘Completeness’ QC, disclosures are provided individually for each material service concession arrangement or in aggregate for service concession arrangements involving services of a similar nature (e.g., toll collections, telecommunications or water treatment services). Consequently, each entity may group their different service concession arrangements following different classifications based on their own assessment, potentially impairing comparability among the different countries.

Furthermore, the standard does not include detailed presentation requirements. In order to achieve consistency in the presentation and disclosure of the service concession arrangements across EU governments, the future EPSAS may provide guidance in this respect. Options for separate presentation and/or disclosure could for example include:

1. Presenting service concession assets and/or the related liabilities separately on the face of the balance sheet.
2. Presenting service concession assets and/or the related liabilities separately as a subcategory within each of the main categories of assets/liabilities that are presented separately on the face of the balance sheet.
3. Presenting information on service concession arrangements (including on service concession assets and the related liabilities) in a separate note to the financial statements and making the reference to the notes about the categories of assets that contain service concession assets.

*Disaggregation requirements*

Where the grantor has an unconditional obligation to pay cash or another financial asset to the operator for the construction, development, acquisition, or upgrade of a service concession asset, the grantor recognises a financial liability. The grantor allocates the payments to the operator and account for them according to their substance as a reduction in the liability recognised in accordance with IPSAS 32 para 14, a finance charge, and charges for services provided by the operator.

The fair value of the service concession asset includes only amounts related to the asset and excludes amounts for other components of the service concession arrangement.

Where the asset and service components are not separately identifiable, the allocation is performed based on the relative fair values of the service concession asset and other components of the service concession arrangement (e.g., maintenance and operation services). When it is not possible, the service component of payments from the grantor to the operator is determined using estimation techniques. This requires a certain degree of judgment that is however inevitable, when an entity intends to fairly reflect the substance of the transaction.

# Alignment with other frameworks

## ESA 2010

ESA 2010 rules make a distinction between service concession contracts (payments principally made by the end users) and PPP (payments principally made by the grantor).

ESA 2010 rules take a risks and rewards approach to determine whether the government entity should reflect the concession contract or PPP on its balance sheet or not. The rules for PPPs place the focus on who bears the construction risk plus either the availability risk or the demand risk. In the case of service concession contracts, the government entity grantor is generally not expected to bear the majority of the risks and rewards related to the asset. This however needs to be confirmed by a careful case-by-case analysis of all facts and circumstances surrounding the transaction. The difference in accounting between the two sets of rules (IPSAS versus ESA 2010) is clear. IPSAS follows a control approach to asset recognition, while ESA 2010 rules follow a risks and rewards approach. A significant difference therefore arises as to the types of arrangements that may need to be recognised on balance sheet, with potentially more transactions being recognised on balance sheet under IPSAS.

Under ESA 2010, investments in service concession assets which are recorded on government entity's balance sheet directly increase government deficit (or reduce government surplus) (B.9). Under IPSAS, investments in service concession assets impact the statement of financial performance through the recording of a depreciation expense over the useful life of the assets.

## IFRS[4]

IPSAS 32 mirrors IFRIC 12 'Service concession arrangements'. IFRIC 12 rules are thus not explained in detail here. The difference is that IPSAS 32 deals with the accounting for the grantor, while IFRIC 12 deals with the accounting treatment for the operator. Hence, all assessments regarding control and recognition criteria are the same for the two standards, but mirrored.

From an accounting viewpoint, when a grantor recognises a service concession asset, the operator recognises either:

- A financial asset to the extent that is has an unconditional contractual right to receive cash or another financial asset; or
- An intangible asset to the extent that it receives a right (e.g. a licence) to charge users of the public service.

Public sector entities that act as operators in service concession arrangements can apply a treatment similar to the one required under IFRIC 12.

[4] Refer to the IPSAS-IFRS Alignment Dashboard regularly updated by the IPSASB available on https://www.ifac.org/system/files/uploads/IPSASB/Agenda%20Item%201.5%20IPSAS%20IFRS%20Alignment%20Dashboard_June%202019.pdf

## EU accounting rules

European Union Accounting Rules (EAR) constitute the accounting framework of the European Union Institutions, including the European Commission (EC) and its agencies.

There is no specific accounting rule developed for service concession arrangements as the Commission is typically not involved in such transactions.

# European Public Good

**Assessing whether IPSAS 32 is conducive to the European public good**

The assessment of whether IPSAS 32 would be conducive to the European public good addresses the following items:

a) Whether the standard will improve financial reporting;
b) The costs and benefits associated with the standard; and
c) Whether the standard could have an adverse effect to the European economy, including financial stability and economic growth.

These assessments will allow the EU authorities to draw a conclusion as to whether the standard is likely to be conducive to the European public good.

The analysis revealed no reasons why IPSAS 32 would not be conducive to the European public good:

- Recognition, classification, measurement, presentation and disclosure requirements of IPSAS 32 will provide useful information to the users of the GPFSs and will improve the overall quality of financial reporting in the public sector. Adoption of a control-based approach to asset recognition brings more benefits than a risks and rewards approach, for the reasons mentioned in this document.

- Implementation of the standard may result in a relatively significant one-off cost and in moderate additional costs on an ongoing basis for preparers.

  Even if the topic is under discussion for the next review of the statistical rules, the difference in the area of service concession arrangements between financial accounting and statistical reporting will most likely not be eliminated. It will require a significant effort for some public entities to move from a cash-based accounting and ESA 2010 statistical reporting to a control-based model in accordance with IPSAS 32, and to manage the fundamental differences between the different reporting systems (need for a 'double analysis' of both control and risks and rewards criteria).

  Another difficulty is related to the determination of the fair value of service concession assets at initial recognition, even when using the fair value as deemed cost exemption upon first-time implementation. The grantor initially measures the service concession asset at its fair value (e.g. during the construction or development of the asset, the costs may be measurable based on the progress reports given by the operator-constructor), except when it already owns the asset. The type of compensation exchanged between the grantor and the operator affects how the fair value of the service concession asset is determined on initial recognition. In practice, the complexities of determining fair value could require additional effort by public sector entities.

Considering its conceptual merits, the standard will bring improved financial reporting when compared to heterogeneous reporting requirements currently applied in the EU. As such and despite its likely implementation cost, its endorsement is conducive to the European public good in that improved financial reporting improves transparency and assists in the assessment of management stewardship. The analysis has not identified any adverse effect of the standard to the European economy, including financial stability and economic growth, or any other factors that would mean the standard is not conducive to the European public good.

# Conclusion

**Assessing IPSAS 32 against the criteria formulated in the draft EPSAS framework**

The analysis has not revealed major conceptual issues with IPSAS 32 ‘Service concession arrangements: grantor’ and has not identified any inconsistency between IPSAS 32 and the draft EPSAS framework.

Following the screening analysis summarised in the present report, the future standard setter could consider the following conclusions. The information resulting from the application of IPSAS 32:

- would provide relevant, reliable, complete, prudent, neutral, verifiable, economically substantive, understandable, timely and comparable information needed for making economic decisions and achieving the necessary level of financial transparency and comparability of financial reporting in the European Union;
- would not be contrary to the true and fair view principle; and
- would be conducive to European public good.

However, in order to achieve consistent application of the new standard within the EU context and therefore better address the comparability objective of EPSAS financial statements, additional guidance and improvements in certain areas might be desirable.

- *Scope of the standard.* IPSAS 32 mirrors the requirements included in IFRS for the accounting of service concessions arrangements by operators. However, public sector entities may act as operators, and it should be considered whether specific accounting requirements would need to be developed in this respect.

- *Control approach guidance.* Service concession arrangements are complex transactions by nature. Further guidance on determining whether arrangements with partially regulated service and conditions may result in greater consistency in accounting treatment, for analogous transactions.

- *Presentation and disclosures.* Specific guidance could be developed to achieve comparability in how service concession assets and/or the related liabilities are presented in the balance sheet or disclosed in the notes.

- *Judgment and comparability.* The use of judgment and estimates is inherent in the preparation of financial statements and may to some extent affect the comparability of financial statements.

The analysis has not identified any adverse effect of the standard to the European economy, including financial stability and economic growth, or any other factors that would mean the standard is not conducive to the European public good.

The future standard setter could consider the conclusions of this assessment and likely net benefit of using the requirements of IPSAS 32 as a starting point in implementing the equivalent EPSAS, considering the need for additional guidance in certain areas and resolution of the matters identified in the present EPSAS screening report.