

PUBLIC BENEFIT ENTITY FINANCIAL REPORTING STANDARD 45 SERVICE CONCESSION ARRANGEMENTS: OPERATOR (PBE FRS 45)

Issued September 2014 and incorporates amendments to 31 January 2017 other than consequential amendments resulting from early adoption of PBE IFRS 9 *Financial Instruments*

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Reporting entities that are subject to this Standard are required to apply it in accordance with the effective date, which is set out in paragraph 30.

In finalising this Standard, the New Zealand Accounting Standards Board has carried out appropriate consultation in accordance with section 22(1) of the Financial Reporting Act 2013.

This Tier 1 and Tier 2 PBE Standard has been issued as part of a revised full set of PBE Standards that incorporate enhancements for not-for-profit public benefit entities.

This Standard, when applied, supersedes PBE FRS 45 *Service Concession Arrangements: Operator* issued in May 2013.

PBE FRS 45 SERVICE CONCESSION ARRANGEMENTS: OPERATOR

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**PBE FRS 45 SERVICE CONCESSION
ARRANGEMENTS: OPERATOR**

CONTENTS

	Paragraph
Objective.....	1
Scope	2–8
Definitions.....	8.1–8.3
Treatment of the Operator’s Rights over the Infrastructure.....	9
Recognition and Measurement of Arrangement Consideration.....	10–11
Construction or Upgrade Services	12–17
Consideration Given by the Grantor to the Operator	13–17
Operation Services.....	18–19
Contractual Obligations to Restore the Infrastructure to a Specified Level of Serviceability.....	19
Borrowing Costs Incurred by the Operator	20
Subsequent Accounting Treatment of a Financial Asset.....	21–23
Subsequent Accounting Treatment of an Intangible Asset.....	24
Items Provided to the Operator by the Grantor.....	25
Disclosure	26–29
Effective Date.....	30–30.1
Withdrawal and Replacement of PBE FRS 45 (May 2013)	31
Application Guidance	
Basis for Conclusions	
Comparison with NZ IFRIC 12 and NZ SIC-29	
History of Amendments	

Public Benefit Entity Financial Reporting Standard 45 *Service Concession Arrangements: Operator* is set out in paragraphs 1–31 and the Application Guidance. All the paragraphs have equal authority. PBE FRS 45 should be read in the context of its objective, the NZASB’s Basis for Conclusions on PBE FRS 45, the *Public Benefit Entities’ Conceptual Framework* and Standard XRB A1 *Application of the Accounting Standards Framework*. PBE IPSAS 3 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

Objective

1. The objective of this Standard is to prescribe the accounting for service concession arrangements by the operator, including to specify disclosures of service concession arrangements not addressed by other PBE Standards.

Scope

2. **This Standard applies to Tier 1 and Tier 2 public benefit entities.**
- 2.1 **A Tier 2 entity is not required to comply with the requirements in this Standard denoted with an asterisk (*). Where a Tier 2 entity elects to apply a disclosure concession it shall comply with any RDR paragraphs associated with that concession.**
3. **An entity¹ shall apply this Standard in accounting for service concession arrangements when it is the operator to the arrangement.**
4. This Standard applies to service concession arrangements if:
 - (a) The grantor controls or regulates what services the operator must provide with the infrastructure, to whom it must provide them, and at what price; and
 - (b) The grantor controls—through ownership, beneficial entitlement or otherwise—any significant residual interest in the infrastructure at the end of the term of the arrangement.
5. Infrastructure used in a service concession arrangement for its entire useful life (whole of life assets) is within the scope of this Standard if the conditions in paragraph 4(a) are met. Paragraphs AG1–AG8 provide guidance on determining whether, and to what extent, service concession arrangements are within the scope of this Standard.
6. This Standard applies to both:
 - (a) Infrastructure that the operator constructs or acquires from a third party for the purpose of the service arrangement; and
 - (b) Existing infrastructure to which the grantor gives the operator access for the purpose of the service arrangement.
7. This Standard does not specify the accounting for infrastructure that was held and recognised as property, plant and equipment by the operator before entering the service arrangement. The derecognition requirements of PBE Standards (set out in PBE IPSAS 17 *Property, Plant and Equipment*) apply to such infrastructure.
8. PBE IPSAS 32 *Service Concession Arrangements: Grantor* addresses the accounting by grantors.

Definitions

- 8.1 **The following terms are used in this Standard with the meanings specified:**

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

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

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

- (a) **Is provided by the operator which:**
 - (i) **The operator constructs, develops, or acquires from a third party; or**

¹ An entity for the purposes of this Standard is referred to as the operator.

- (ii) **Is an existing asset of the operator; or**
- (b) **Is provided by the grantor which:**
 - (i) **Is an existing asset of the grantor; or**
 - (ii) **Is an upgrade to an existing asset of the grantor.**

Terms defined in other PBE Standards are used in this Standard with the same meaning as in those Standards, and are reproduced in the *Glossary of Defined Terms* published separately.

- 8.2 Common features of a service concession arrangement are:
- (a) The grantor is a public benefit entity;
 - (b) The operator is responsible for at least some of the management of the service concession asset and related services and does not merely act as an agent on behalf of the grantor;
 - (c) The arrangement sets the initial prices to be levied by the operator and regulates price revisions over the period of the service concession arrangement;
 - (d) The operator is obliged to hand over the service concession asset to the grantor in a specified condition at the end of the period of the arrangement, for little or no incremental consideration, irrespective of which party initially financed it; and
 - (e) The arrangement is governed by a binding arrangement that sets out performance standards, mechanisms for adjusting prices, and arrangements for arbitrating disputes.
- 8.3 Examples of service concession assets are: roads, bridges, tunnels, prisons, hospitals, airports, water distribution facilities, energy supply and telecommunication networks, permanent installations for military and other operations, and other non-current tangible or intangible assets used for administrative purposes in delivering public services.

Treatment of the Operator's Rights over the Infrastructure

9. **Infrastructure within the scope of this Standard shall not be recognised as property, plant and equipment of the operator because the contractual service arrangement does not convey the right to control the use of the infrastructure to the operator. The operator has access to operate the infrastructure to provide the public service on behalf of the grantor in accordance with the terms specified in the contract.**

Recognition and Measurement of Arrangement Consideration

10. Under the terms of contractual arrangements within the scope of this Standard, the operator acts as a service provider. The operator constructs or upgrades infrastructure (construction or upgrade services) used to provide a service and operates and maintains that infrastructure (operation services) for a specified period of time.
11. **The operator shall recognise and measure revenue in accordance with PBE IPSAS 11 *Construction Contracts* and PBE IPSAS 9 *Revenue from Exchange Transactions* for the services it performs. If the operator performs more than one service (i.e., construction or upgrade services and operation services) under a single contract or arrangement, consideration received or receivable shall be allocated by reference to the relative fair values of the services delivered, when the amounts are separately identifiable. The nature of the consideration determines its subsequent accounting treatment. The subsequent accounting for consideration received as a financial asset and as an intangible asset is detailed in paragraphs 21–24 below.**

Construction or Upgrade Services

12. **The operator shall account for revenue and costs relating to construction or upgrade services in accordance with PBE IPSAS 11.**

Consideration Given by the Grantor to the Operator

13. **If the operator provides construction or upgrade services the consideration received or receivable by the operator shall be recognised at its fair value. The consideration may be rights to:**
 - (a) **A financial asset, or**
 - (b) **An intangible asset.**
14. **The operator shall recognise a financial asset to the extent that it has an unconditional contractual right to receive cash or another financial asset from or at the direction of the grantor for the construction services; the grantor has little, if any, discretion to avoid payment, usually because the agreement is enforceable by law. The operator has an unconditional right to receive cash if the grantor contractually guarantees to pay the operator (a) specified or determinable amounts or (b) the shortfall, if any, between amounts received from users of the service and specified or determinable amounts, even if payment is contingent on the operator ensuring that the infrastructure meets specified quality or efficiency requirements.**
15. **The operator shall recognise an intangible asset to the extent that it receives a right (a licence) to charge users of the service. A right to charge users of the service is not an unconditional right to receive cash because the amounts are contingent on the extent that the service is used.**
16. **If the operator is paid for the construction services partly by a financial asset and partly by an intangible asset it is necessary to account separately for each component of the operator's consideration. The consideration received or receivable for both components shall be recognised initially at the fair value of the consideration received or receivable.**
17. **The nature of the consideration given by the grantor to the operator shall be determined by reference to the contract terms and, when it exists, relevant contract law.**

Operation Services

18. The operator shall account for revenue and costs relating to operation services in accordance with PBE IPSAS 9.

Contractual Obligations to Restore the Infrastructure to a Specified Level of Serviceability

19. The operator may have contractual obligations it must fulfil as a condition of its licence (a) to maintain the infrastructure to a specified level of serviceability or (b) to restore the infrastructure to a specified condition before it is handed over to the grantor at the end of the service arrangement. These contractual obligations to maintain or restore infrastructure, except for any upgrade element (see paragraph 14), shall be recognised and measured in accordance with PBE IPSAS 19 *Provisions, Contingent Liabilities and Contingent Assets*, i.e., at the best estimate of the expenditure that would be required to settle the present obligation at the end of the reporting period.

Borrowing Costs Incurred by the Operator

20. In accordance with PBE IPSAS 5 *Borrowing Costs*, borrowing costs attributable to the arrangement shall be recognised as an expense in the period in which they are incurred (the benchmark treatment), except to the extent that they are capitalised in accordance with paragraph 18 of PBE IPSAS 5 (the allowed alternative treatment). Where the operator uses the allowed alternative treatment and has a contractual right to receive an intangible asset (a right to charge users of the service), borrowing costs attributable to the arrangement shall be capitalised during the construction phase of the arrangement in accordance with PBE IPSAS 5.

Subsequent Accounting Treatment of a Financial Asset

21. PBE IPSAS 28 *Financial Instruments: Presentation*, PBE IPSAS 29 *Financial Instruments: Recognition and Measurement* and PBE IPSAS 30 *Financial Instruments: Disclosures* apply to the financial asset recognised under paragraphs 14 and 16.
22. The amount due from or at the direction of the grantor is accounted for in accordance with PBE IPSAS 29 as:
 - (a) A loan or receivable;

- (b) An available-for-sale financial asset; or
 - (c) If so designated upon initial recognition, a financial asset at fair value through surplus or deficit, if the conditions for that classification are met.
23. If the amount due from the grantor is accounted for either as a loan or receivable or as an available-for-sale financial asset, PBE IPSAS 29 requires interest calculated using the effective interest method to be recognised in surplus or deficit.

Subsequent Accounting Treatment of an Intangible Asset

24. PBE IPSAS 31 *Intangible Assets* applies to the intangible asset recognised in accordance with paragraphs 15 and 16. Paragraphs 44–45 of PBE IPSAS 31 provide guidance on measuring intangible assets acquired in exchange for a non-monetary asset or assets or a combination of monetary and non-monetary assets.

Items Provided to the Operator by the Grantor

25. **In accordance with paragraph 9, infrastructure items to which the operator is given access by the grantor for the purposes of the service arrangement are not recognised as property, plant and equipment of the operator. The grantor may also provide other items to the operator that the operator can keep or deal with as it wishes. If such assets form part of the consideration payable by the grantor for the services, they are recognised as assets of the operator, measured at fair value on initial recognition. The operator shall recognise a liability in respect of unfulfilled obligations it has assumed in exchange for the assets.**

Disclosure

26. Certain aspects and disclosures relating to some service concession arrangements are already addressed by other PBE Standards (e.g., PBE IPSAS 32 *Service Concession Arrangements: Grantor* prescribes the accounting by the grantor, PBE IPSAS 17 applies to acquisitions of items of property, plant and equipment, PBE IPSAS 13 *Leases* applies to leases of assets, and PBE IPSAS 31 applies to acquisitions of intangible assets). However, a service concession arrangement may involve executory contracts that are not addressed in PBE Standards, unless the contracts are onerous, in which case PBE IPSAS 19 applies. Therefore, this Standard addresses additional disclosures of service concession arrangements by operators.
- *27. **All aspects of a service concession arrangement shall be considered in determining the appropriate disclosures in the notes. An operator shall disclose the following in each period:**
- (a) **A description of the arrangement;**
 - (b) **Significant terms of the arrangement that may affect the amount, timing and certainty of future cash flows (e.g., the period of the concession, re-pricing dates and the basis upon which re-pricing or re-negotiation is determined);**
 - (c) **The nature and extent (e.g., quantity, time period or amount as appropriate) of:**
 - (i) **Rights to use specified assets;**
 - (ii) **Obligations to provide or rights to expect provision of services;**
 - (iii) **Obligations to acquire or build items of property, plant and equipment;**
 - (iv) **Obligations to deliver or rights to receive specified assets at the end of the concession period;**
 - (v) **Renewal and termination options; and**
 - (vi) **Other rights and obligations (e.g., major overhauls);**
 - (d) **Changes in the arrangement occurring during the period; and**
 - (e) **How the service arrangement has been classified.**
- *28. **An operator shall disclose the amount of revenue and surpluses or deficits recognised in the period on exchanging construction services for a financial asset or an intangible asset.**

- *29. The disclosures required in accordance with paragraph 27 of this Standard should be provided individually for each service concession arrangement or in aggregate for each class of service concession arrangements. A class is a grouping of service concession arrangements involving services of a similar nature (e.g., toll collections, telecommunications and water treatment services).

Effective Date

30. **A public benefit entity shall apply this Standard for annual financial statements covering periods beginning on or after 1 April 2015. Earlier application is permitted for not-for-profit public benefit entities as long as the full suite of PBE Standards is applied at the same time.**

Withdrawal and Replacement of PBE FRS 45 (May 2013)

31. This Standard, when applied, supersedes PBE FRS 45 *Service Concession Arrangements: Operator* issued in May 2013.

Application Guidance

This Appendix is an integral part of PBE FRS 45.

Scope (paragraph 4)

- AG1. Paragraph 4 of this Standard specifies that infrastructure is within the scope of the Standard when the following conditions apply:
- (a) The grantor controls or regulates what services the operator must provide with the infrastructure, to whom it must provide them, and at what price; and
 - (b) The grantor controls—through ownership, beneficial entitlement or otherwise—any significant residual interest in the infrastructure at the end of the term of the arrangement.
- AG2. The control or regulation referred to in condition (a) could be by contract or otherwise (such as through a regulator), and includes circumstances in which the grantor buys all of the output as well as those in which some or all of the output is bought by other users. In applying this condition, the grantor and any related parties shall be considered together. If the grantor is a public sector entity, the public sector as a whole, together with any regulators acting in the public interest, shall be regarded as related to the grantor for the purposes of this Standard.
- AG3. For the purpose of condition (a), the grantor does not need to have complete control of the price: it is sufficient for the price to be regulated by the grantor, contract or regulator, for example by a capping mechanism. However, the condition shall be applied to the substance of the agreement. Non-substantive features, such as a cap that will apply only in remote circumstances, shall be ignored. Conversely, if for example, a contract purports to give the operator freedom to set prices, but any excess profit is returned to the grantor, the operator's return is capped and the price element of the control test is met.
- AG4. For the purpose of condition (b), the grantor's control over any significant residual interest should both restrict the operator's practical ability to sell or pledge the infrastructure and give the grantor a continuing right of use throughout the period of the arrangement. The residual interest in the infrastructure is the estimated current value of the infrastructure as if it were already of the age and in the condition expected at the end of the period of the arrangement.
- AG5. Control should be distinguished from management. If the grantor retains both the degree of control described in paragraph 4(a) and any significant residual interest in the infrastructure, the operator is only managing the infrastructure on the grantor's behalf—even though, in many cases, it may have wide managerial discretion.
- AG6. Conditions (a) and (b) together identify when the infrastructure, including any replacements required (see paragraph 19), is controlled by the grantor for the whole of its economic life. For example, if the operator has to replace part of an item of infrastructure during the period of the arrangement (e.g., the top layer of a road or the roof of a building), the item of infrastructure shall be considered as a whole. Thus condition (b) is met for the whole of the infrastructure, including the part that is replaced, if the grantor controls any significant residual interest in the final replacement of that part.
- AG7. Sometimes the use of infrastructure is partly regulated in the manner described in paragraph 4(a) and partly unregulated. However, these arrangements take a variety of forms:
- (a) Any infrastructure that is physically separable and capable of being operated independently and meets the definition of a cash-generating unit as defined in PBE IPSAS 26 *Impairment of Cash-Generating Assets* shall be analysed separately if it is used wholly for unregulated purposes. For example, this might apply to a private wing of a hospital, where the remainder of the hospital is used by the grantor to treat public patients.
 - (b) When purely ancillary activities (such as a hospital shop) are unregulated, the control tests shall be applied as if those services did not exist, because in cases in which the grantor controls the services in the manner described in paragraph 4, the existence of ancillary activities does not detract from the grantor's control of the infrastructure.
- AG8. The operator may have a right to use the separable infrastructure described in paragraph AG7(a), or the facilities used to provide ancillary unregulated services described in paragraph AG7(b). In either case, there may in substance be a lease from the grantor to the operator; if so, it shall be accounted for in accordance with PBE IPSAS 13.

Basis for Conclusions

This Basis for Conclusions accompanies, but is not part of, PBE FRS 45.

- BC1. The New Zealand Accounting Standards Board (NZASB) has developed this Standard based on NZ IFRIC 12 *Service Concession Arrangements* and NZ SIC-29 *Service Concession Arrangements: Disclosures*. The NZASB considered that the requirements of these two Interpretations are appropriate for application by public benefit entities and noted that these two Interpretations formed part of NZ IFRS PBE as applied by PBEs prior to the adoption of PBE Standards, albeit that the scope of NZ IFRIC 12 was in relation to public-to-private service arrangements. The NZASB considered the scope to be appropriate to ensure that all PBE operators account for their service concession arrangements in a similar manner in accordance with this Standard.
- BC2. The NZASB noted that the Basis for Conclusions on IFRIC 12 *Service Concession Arrangements* summarises the IFRS Interpretations Committee's (IFRIC's) considerations in reaching its consensus on IFRIC 12 in respect of public-to-private service arrangements. In developing IFRIC 12 the IFRIC considered requests to develop guidance for other types of arrangements including private to private arrangements. The IFRIC declined to do so but noted that application by analogy would be appropriate under the hierarchy set out in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.
- BC3. Disclosure concessions have been identified in PBE FRS 45. The NZASB noted that disclosure concessions in other PBE Standards are applicable as a consequence of an operator applying presentation and disclosure requirements of those standards.
- BC4. Illustrative examples on the application of IFRIC 12 are available in the additional material for NZ IFRIC 12 *Service Concession Arrangements* on the XRB website.

History of Amendments

PBE FRS 45 *Service Concession Arrangements: Operator* was issued in September 2014.

This table lists the pronouncements establishing and substantially amending PBE FRS 45.

Pronouncements	Date issued	Early operative date	Effective date (annual financial statements ... on or after ...)
PBE FRS 45 <i>Service Concession Arrangements: Operator</i>	Sept 2014	Early application is permitted for not-for-profit public benefit entities	1 April 2015