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Technical Director
International Public Sector Accounting Standards Board
International Federation of Accountants
227 Wellington Street West
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Dear Sir

CONSULTATION PAPER: ACCOUNTING AND FINANCIAL REPORTING FOR SERVICE CONCESSION ARRANGEMENTS

1. The National Audit Office (NAO) is pleased to comment on this consultation paper.

2. The NAO, on behalf of the Comptroller and Auditor General, carries out the external audit of all UK central government departments and a wide range of other UK and international public bodies. We will in due course carry out the external audit of the Whole of Government Accounts, which the government intends to produce as a consolidation of the financial statements of all parts of the UK public sector.

3. We welcome the Board's consideration of the various issues surrounding the accounting and financial reporting of service concession arrangements. This has for a number of years been an important area for the United Kingdom public sector where it has been apparent that the guidance employed has allowed inconsistent accounting both between public and private sectors and within different parts of the public sector. The United Kingdom's Treasury has recently developed and published guidance based on the IASB's IFRIC 12 statement to address these matters in relation to the UK's Private Finance Initiative, but we welcome the consultation paper's wider and more comprehensive scope in the public-private partnership arrangements addressed.

4. We are also pleased that whilst the Board has considered these matters afresh, the consultation paper has largely followed the broad principles of IFRIC 12. It is important for some jurisdictions that there should be some symmetry between the accounting principles employed for the private sector operators and those for the public sector grantors and this would appear to be right in concept, notwithstanding any conceptual weaknesses in the IFRIC 12 statement.

5. We would, therefore, question the paper's use of 'residual interest' as a criterion for control, as opposed to the IFRIC 12 criterion of 'significant residual interest'. Control over the residual interest, whether or not that interest is deemed to be significant, is viewed by the paper as important in preserving the continuous public sector use of the property. But we believe that where there is only an insignificant residual interest but that the first control criterion of grantor control and regulation of the services and to whom and at what price they should be provided, is met, then continuous public sector use of the property has in substance been achieved. If this were not to be the case then arguably the residual interest retained by the operator should be classified as 'significant'. Our concern here is lest a property may not be reported by a grantor simply because of a very insignificant residual interest retained by the operator.

6. On the subject of the calculation of the interest rate used to impute the finance charge inherent in a service concession arrangement (paragraph 122 of the paper) we note that there has been some divergence of opinions and that, for example, the UK Government Financial Reporting Manual requires use of the UK long-term real interest rate, as a market risk-free rate representing the grantor's cost of capital. We consider the rationale for using the operator's cost of capital specific to the arrangement set out in paragraph 122 to be more persuasive, but would support further refinement of this towards a rate that would be more property specific. This would reflect the guidance in the UK FRS 5 PFI Application Note and the relevant leasing accounting standards.

7. There is one other matter to which we think that the Board should give some further thought. We are not convinced that a grantor will have a liability to the operator in those concessions where the operator collects usage fees directly from third parties rather than the grantor. Having made an initial grant of a license to the operator it is difficult to see that there is then a further obligation to transfer economic resources that would constitute a liability under IPSAS 19.

8. In the light of our comments above our responses to the specific matters for comment raised in the Consultation Paper are:

   Question 1 – the criteria for determining control – we agree with the suggested approach, but would question the departure from the IFRIC 12 principle regarding residual interest, as discussed at paragraph 5 above.

   Question 2 – reporting of asset and liability – we generally agree with the proposal, subject to some reservation regarding the nature and extent of the liability arising in service concession arrangements where the operator's income is received direct from third party users, as discussed at paragraph 7 above.

   Question 3 – revenue recognition – we agree with the suggested approach.

I hope these observations are useful to you.

Yours sincerely

ANDREW BAIGENT

Director, Financial Audit Policy