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Regarding: Service Concession Arrangements-Grantor- Exposure 43
Comments: **Dr. Joseph S. Maresca CPA, CISA**

Colleagues,
I thank you for the opportunity to critique Exposure Draft 43. Details follow :

Background:

The service concession arrangement is an operator developed asset compensated by a binding arrangement. (usually) The grantor grants the service concession to the operator. Essentially, public sector entities operate in this fashion. This submission deals with **public services**.

The grantor controls or operates services which the operator provides. The grantor may have significant residual interest. The grantor may compensate the operator by payment to operate, rights to collect fees or granting the operator access to another revenue generating asset. The grantor initially measures the originating service concession asset at fair value. The grantor may compensate the operator for a service concession asset via payment or the creation of a financial liability. pp. 11

The grantor accounts for revenues as earned for exchange transactions. pp. 12
Generally, the grantor discloses service concession arrangements.
i.e. the description, significant terms, rights to use assets etc.   The grantor recognizes financial liabilities when obligated to make payments to the operator for providing the service concession asset. pp. 14   The grantor needn't control the price. pp. 15 The grantor may make payments to the operator, create financial liabilities or create guarantees. pp. 19

The operator may compensate the grantor up front or share revenues or make rental payments for providing the operator access to a revenue generating asset. pp. 21 Contingent liabilities may apply and the treatment is set forth in IPSAS 19.

Generally, I concur.

Analysis:
Increasingly, offshore drilling operations for valuable mineral rights may be subject to State ownership, investment or control, as in China. Although, a public ownership of the mineral resource may apply in some cases, the **operator (if outsourced by the government) is the party with the extraction and safety experience** involved in developing valuable oil resources.

The operator may compensate the grantor up front or share revenues or make rental payments for providing the operator access to a revenue generating asset. pp. 21   Contingent liabilities may apply and the treatment is set forth in IPSAS 19. The best policy is for the grantor and operator to create an agreement where it is absolutely clear what rights, duties, liabilities and recourse which apply in the continuing application of the Agreement.

Some of these risks can be very real. Environmental risks of hurricanes, earthquakes, Tsunamis can halt projects into the foreseeable future. Major cost over-runs can be incurred due to material spikes in the cost of energy.

In Availability risk , the operator bears the risk of insufficient management, strikes, work slowdowns, outsourcing risks due to language barriers and unanticipated Acts of G-d, inefficiencies and downtime in training or even employee turnover.

Demand risk may be due to the business cycle, new market trends,changes in user preferences, changes in the political climate or technical obsolescence. The fixed price contract transfers the construction risk to the builder.

The current economic environment has demand risk due to investor uncertainty with regard to the predictability of energy prices. Auto owners determine new market trends with regard to manufacturing energy efficient cars.

For instance, the operator of an offshore oil platform may have a considerable team of experts to accomplish the safe extraction of valuable mineral resources. The extraction may be compensated by giving the grantor monies up front, a revenue-sharing or similar arrangement.

IPSAS 19 provides for the outsourcing of a major government department on pp. 35. The present obligation flows from a reasonable expectation that the government division will be outsourced. A proviso is made for the best estimate of the cost of the outsource. **Once outsourced, the operator must make provisions for the ongoing operations, contingency plan, testing of the contingency plan, disaster recovery planning and testing of the disaster recovery plan unless otherwise agreed.**

The outsourcer in an area of Tsunami storms may face the major destruction of facilities due to the vagaries of nature. Oil drilling companies off the Gulf Coast routinely encounter significant repairs of damaged equipment due to hurricane activity.

The obligating event is giving the guarantee which gives rise to a legal obligation. An outflow of resources may embody economic benefits or service potential . When it is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation, a provision should be made for the best estimate of the obligation.

A typical oil production platform is self-sufficient in energy and water needs, housing electrical generation, water desalinators and all of the equipment necessary to process oil and gas such that it can be either delivered directly onshore by pipeline or to a floating platform and/or tanker loading facility. Elements in the oil/gas production process include wellhead, production manifold, production separator, glycol process to dry gas, gas compressors, water injection pumps, oil/gas export metering and main oil line pumps.

An offshore operations platform generally consists of a considerable team of experts in the art of oil well engineering operations and continuing maintenance. i.e.

The OIM (offshore installation manager) is the ultimate authority during his/her shift and makes the essential decisions regarding the operation of the platform. There may be a hierarchy of team leaders to facilitate continuous operations. The offshore operations engineer (OOE) is the senior technical authority on the platform. Operations coordinators manage crew changes.

Dynamic positioning operators assist with navigation, ship or vessel maneuvering (MODU), station keeping, fire and gas systems escalation in the event of incidents. A hierarchy of "mates" meet staffing requirements of flag state, operate fast rescue craft, cargo operations and fire coordination. Crane operators run cranes for lifting cargo around the platform. Scaffolders manage scaffold building when workers are required to work at heights. Coxwains maintain the lifeboats. The catering crew handle cooking and laundry. Production techs run the production plant. Helicopter pilots navigate between the platform and the shore during crew relief or changes. Maintenance technicians manage instrumentation, electrical and mechanical systems and processes.

The operator who builds and operates a major offshore oil platform must meet the conditions for recognition of a service concession asset in Par. 10 pp. 33. Certain basic legal doctrines may apply to transactions transnationally based. i.e.

The “Principle of Comity” may make the grantor’s laws dispositive as long as the laws are consistent with accommodating nations, trading partners or business partners. The contract must delineate whose laws are in operation with regard to the implementation of the ongoing contract.

The “Act of State Doctrine” is a judicially created doctrine that states the judicial branch of one country should not examinethe validity of public acts committed by a recognized foreign government with regard to business activity or any activity within its own borders. The contract should provide for foreseeable conflicts in the conduct of the arrangement; such that, the discretion of the host country is not invoked adversely to the operator.

The Doctrine of Foreign Immunity immunizes foreign nations from the jurisdiction of American Courts. A contractor or operator must be satisfied as to the proper venue to seek redress for major contractual non-compliance, non-cooperation or outright expropriation.

The contract between the Public Service Organization and the operator must be clear as to the choice of language and the choice of forum to designate dispute resolution, local court jurisdiction or forced arbitration venues. The governing law with respect to the contract performance should be set forth clearly. In cases where the performance arises out of intellectual property, the governing law may be the United States Patent Law or European Patent Office.