

## STAFF PAPER

July 2016

## IFRS® Interpretations Committee Meeting

<b>Project</b>	<b>IFRIC 12 <i>Service Concession Arrangements</i></b>		
<b>Paper topic</b>	Service concession arrangements with leased infrastructure		
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This paper has been prepared for discussion at a public meeting of the IFRS Interpretations Committee (the Interpretations Committee). Comments on the application of IFRS Standards do not purport to set out acceptable or unacceptable application of IFRS Standards—only the Interpretations Committee or the International Accounting Standards Board (the Board) can make such a determination. Decisions made by the Interpretations Committee are reported in IFRIC® *Update*. The approval of a final Interpretation by the Board is reported in IASB® *Update*.

## Introduction

1. The IFRS Interpretations Committee (the Interpretations Committee) received a request to clarify how an operator accounts for a service concession arrangement (SCA) for which the infrastructure is leased. In this SCA, the operator is not required to provide any construction or upgrade services with respect to the infrastructure.
2. The submitter described an arrangement that involves three parties: a grantor, an operator and a lessor. The operator enters into an arrangement with the grantor to operate a public service. The infrastructure in the arrangement is leased from the lessor. The lessor and the grantor may be controlled by the same governmental body. The operator is contractually required to pay the lessor for the lease of the infrastructure. The operator has an unconditional contractual right to receive cash from the grantor to reimburse those payments. In arrangements in which the lessor and the grantor are not controlled by the same governmental body, the grantor provides the lessor with a guarantee of the lease payments to be made during the lease term and of any residual value at the end of the lease term. The grantor also has an option to renew the lease at the end of the initial non-cancellable period of the contract.
3. The submitter asked the Interpretations Committee to clarify whether the arrangement is within the scope of IFRIC 12 *Service Concession Arrangements* (scope issue). If the arrangement is within the scope of IFRIC 12, the submitter notes that the lease of

the infrastructure is not within the scope of IFRS 16 *Leases* (IAS 17 *Leases*) for the operator. Consequently, the submitter also asked the Interpretations Committee to clarify how the operator accounts for any assets and liabilities arising from the arrangement with the lessor (recognition and presentation issues).

4. With respect to the scope issue, the Interpretations Committee observed that:
  - (a) assessing whether a particular arrangement is within the scope of IFRIC 12 requires consideration of the specific facts and circumstances. In particular, the operator assesses whether the control conditions in paragraph 5 of IFRIC 12 and the condition relating to the infrastructure in paragraph 7 of IFRIC 12 apply; and
  - (b) the operator is not required to provide construction or upgrade services with respect to the infrastructure for the arrangement to be within the scope of IFRIC 12.
  
5. With respect to the recognition and presentation issues, if the arrangement described in the submission is within the scope of IFRIC 12, the Interpretations Committee observed that the grantor, rather than the operator, controls the right to use the infrastructure. Accordingly, the Interpretations Committee observed that:
  - (a) the operator assesses whether it is obliged to make payments to the lessor for the lease or whether the grantor has this obligation. This assessment requires consideration of the specific facts and circumstances. If the grantor is obliged to make payments to the lessor, then in that case the operator is collecting cash from the grantor that it remits to the lessor on the grantor's behalf.
  - (b) if the operator is obliged to make payments to the lessor as part of the SCA, then the operator recognises a liability for this obligation when it is committed to the SCA and the infrastructure is made available by the lessor. At the time the operator recognises the liability, it also recognises a financial asset because the operator has a contractual right to receive cash from the grantor to reimburse those payments.
  - (c) the operator's liability to the lessor described in (b) above is a financial liability. Accordingly, the operator offsets the liability to make payments to

the lessor against the corresponding receivable from the grantor only when the criteria for offsetting a financial asset and a financial liability in IAS 32 *Financial Instruments: Presentation* are met.

6. The Interpretations Committee concluded that the requirements in IFRS Standards provide an adequate basis to enable an entity to determine how to account for the arrangement.
7. In the light of the existing requirements in IFRS Standards, the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee tentatively decided not to add this issue to its agenda.
8. The purpose of this paper is to provide the Interpretations Committee with an analysis of the comments received on the tentative agenda decision and to ask the Interpretations Committee if it agrees with the staff recommendation to finalise the agenda decision.

### **Comment letter summary and staff analysis**

9. We received three comment letters, which have been reproduced in Appendix B to this paper. Two respondents (Deloitte and the Accounting Standards Committee of Germany (the ASCG)) agree with the Interpretations Committee's technical analysis and conclusions. One respondent (ACTEO) disagrees with the Interpretations Committee's conclusion on the recognition issue. The concerns noted by respondents, together with our analysis of them, are summarised below.

### **Clarifications to agenda decision and/or IFRIC 12**

#### *Concerns raised by respondents*

10. Deloitte agrees with the Interpretations Committee's decision not to add this issue to its agenda for the reasons set out in the tentative agenda decision. However, Deloitte says that it would be useful for the agenda decision to include further explanation of the facts and circumstances that an operator considers in determining which party (ie the operator or the grantor) is obliged to make payments to the lessor.

11. The ASCG agrees with the conclusions reached by the Interpretations Committee. Nonetheless the ASCG says that they would prefer the Interpretations Committee to provide a clarification to IFRIC 12 that enhances ‘the practical application of the assessment on the recognition and presentation issue’.

*Staff analysis*

12. We agree with the Interpretations Committee’s tentative conclusion that the requirements in IFRS Standards provide an adequate basis to enable an entity to determine how to account for the SCA.
13. Therefore, we recommend not adding further clarifications to the agenda decision and/or proposing amendments to IFRIC 12. In analysing the recognition and presentation issues (if the SCA is within the scope of IFRIC 12), the Interpretations Committee observed that the operator first assesses the substance of the arrangement (ie to determine which party is obliged to make the lease related payments)—see paragraph 5 of this paper. This assessment depends on the specific facts and circumstances of the SCA. We think that providing further explanation of these facts and circumstances would not be practical or useful because of the unique nature of each SCA. If the Interpretations Committee were to include any further indicators or guidance, these would be quite generic, and accordingly, are unlikely to be particularly helpful. More importantly, there is a risk that such generic indicators or guidance could detract from a full consideration of the particular facts and circumstances in question.
14. The Interpretations Committee observed that if the operator determines that it is obliged to make the lease-related payments, the operator applies the requirements of relevant IFRS Standards (ie to determine when to recognise a liability to make the lease-related payments, and whether to offset the liability and the corresponding receivable from the grantor). We continue to think that these requirements are clear and that a clarification to IFRIC 12 is not required in this respect.

## **Recognition issue**

### *Concern raised by a respondent*

15. ACTEO disagrees that, in the fact pattern submitted, the operator recognises a liability to make payments to the lessor when the infrastructure is made available by the lessor. This is because it says that making an asset available is not sufficient to justify the recognition of an asset and a liability applying existing IFRS Standards. ACTEO say that, even if an asset is made available, an entity does not recognise a liability:
- (a) in the case of an operating lease applying IAS 17; and
  - (b) in the case of a service contract applying IFRS 16.

### *Staff analysis*

16. We agree with the Interpretations Committee’s tentative conclusion that an operator recognises a liability for its obligation to make payments to the lessor when it is committed to the SCA and the infrastructure is made available by the lessor. At this time, the lessor has performed under the contract and hence the operator has a liability, assuming that it has been concluded that the operator, and not the grantor, is obliged to make payments to the lessor for the lease. Our analysis of why the operator recognises a liability to make payments to the lessor at this time is outlined in paragraphs 15-24 of [Agenda Paper 4](#) from the Interpretations Committee’s May 2016 meeting. We emphasise that if the arrangement is in the scope of IFRIC 12, the operator does not control the right to use the infrastructure. Accordingly, the arrangement is not a lease for the operator applying IFRS 16 (IAS 17). In our analysis in [Agenda Paper 4](#) from the Interpretations Committee’s May 2016 meeting, we have looked to paragraph BC25 of IFRS 16 only for the purpose of assessing when the counterparty (ie the lessor) has performed under the contract.
17. We also emphasise that the tentative agenda decision does not conclude that the operator is obliged to make payments to the lessor for the lease—rather, it says that an entity assesses whether the grantor, or the operator, has that obligation on the basis of specific facts and circumstances.

**Other comment***Concern raised by a respondent*

18. ACTEO agrees with the Interpretations Committee's conclusions on the scope issue. However, they say that [Agenda Paper 13](#) from the Interpretations Committee's November 2015 meeting seems to conclude that the grantor controls the residual interest (ie the control criterion in paragraph 5(b) of IFRIC 12 is met) because of the existence of the renewal option. Although ACTEO acknowledges that agenda papers are not part of IFRS authoritative literature, it says that the wording in the agenda paper could be used to force every arrangement for which the grantor has a renewal option to be within the scope of IFRIC 12.

*Staff analysis*

19. The wording of the tentative agenda decision specifies that an entity considers all facts and circumstances when assessing whether a particular arrangement is within the scope of IFRIC 12. It does not say that the existence of a renewal option in itself results in a particular conclusion. A similar point is made in [Agenda Paper 13](#) from the November 2015 Interpretations Committee's meeting (see analysis in paragraphs 33-42 of that paper).
20. In addition, as noted at the top of every agenda paper, comments made in relation to the application of an IFRS Standard in an agenda paper do not purport to be acceptable or unacceptable application of that IFRS Standard. As outlined in paragraph 3.7 of the IFRS Foundation's [Due Process Handbook](#), the objective of an agenda paper is to:

...provide sufficient information so that the IASB or Interpretations Committee members can make informed decisions on technical matters.

**Staff recommendation**

21. On the basis of our analysis, we recommend confirming the tentative agenda decision as published in the [IFRIC Update](#) in May 2016 with no substantial changes. Appendix A to this paper outlines the draft wording of the final agenda decision.

**Question for the Interpretations Committee**

Does the Interpretations Committee agree with the staff recommendation to finalise the agenda decision outlined in Appendix A to this paper?

## Appendix A—Finalisation of agenda decision

- A1. We propose the following wording of the final agenda decision (new text is underlined and deleted text is struck through)

**IFRIC 12 *Service Concession Arrangements*—~~Accounting for s~~ Service concession arrangements with leased infrastructure**

The Interpretations Committee received a request to clarify how an operator accounts for a service concession arrangement for which the infrastructure is leased. In this arrangement, the operator is not required to provide any construction or upgrade services with respect to the infrastructure.

The submitter described an arrangement that involves three parties: a grantor, an operator and a lessor. The operator enters into an arrangement with the grantor to operate a public service. The infrastructure in the arrangement is leased from the lessor. The lessor and the grantor may be controlled by the same governmental body. The operator is contractually required to pay the lessor for the lease of the infrastructure. The operator has an unconditional contractual right to receive cash from the grantor to reimburse those payments. In arrangements in which the lessor and the grantor are not controlled by the same governmental body, the grantor provides the lessor with a guarantee of the lease payments to be made during the lease term, and of any residual value at the end of the lease term. The grantor also has an option to renew the lease at the end of the initial non-cancellable period of the contract.

The submitter asked the Interpretations Committee to clarify whether the arrangement is within the scope of IFRIC 12 *Service Concession Arrangements* (scope issue). If the arrangement is within the scope of IFRIC 12, the submitter notes that the lease of the infrastructure is not within the scope of IFRS 16 *Leases* (IAS 17 *Leases*) for the operator. Consequently, the submitter also asked the Interpretations Committee to clarify how the operator accounts for any assets and liabilities arising from the arrangement with the lessor (recognition and presentation issues).

With respect to the scope issue, the Interpretations Committee observed that:



- a. assessing whether a particular arrangement is within the scope of IFRIC 12 requires consideration of ~~all~~ the specific facts and circumstances. In particular, the operator assesses whether the control conditions in paragraph 5 of IFRIC 12 and the condition relating to the infrastructure in paragraph 7 of IFRIC 12 apply; and
- b. the operator is not required to provide construction or upgrade services with respect to the infrastructure for the arrangement to be within the scope of IFRIC 12.

With respect to the recognition and presentation issues, if the arrangement described in the submission is within the scope of IFRIC 12, the Interpretations Committee observed that ~~it is the grantor, and not rather than~~ the operator, ~~that~~ controls the right to use the infrastructure. Accordingly, the Interpretations Committee observed that:

- a. the operator assesses whether it is obliged to make payments to the lessor for the lease or whether the grantor has this obligation. This assessment requires consideration of ~~all~~ the specific facts and circumstances. If the grantor is obliged to make payments to the lessor, then in that case the operator is collecting cash from the grantor that it remits to the lessor on the grantor's behalf.
- b. if the operator is obliged to make payments to the lessor as part of the service concession arrangement, then the operator recognises a liability for this obligation when it is committed to the service concession arrangement and the infrastructure is made available by the lessor. At the time the operator recognises the liability, it also recognises a financial asset because the operator has a contractual right to receive cash from the grantor to reimburse those payments.
- c. the operator's liability to the lessor described in (b) above is a financial liability. Accordingly, the operator offsets the liability to make payments to the lessor against the corresponding receivable from the grantor only when the criteria for offsetting a financial asset and a financial liability in IAS 32 *Financial Instruments: Presentation* are met.

The Interpretations Committee ~~noted~~ concluded that the requirements in IFRS Standards provide an adequate basis to enable an entity to determine how to account for the arrangement.

In the light of the existing requirements in IFRS Standards, the Interpretations Committee determined that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee {decided} not to add this issue to its agenda.

## **Appendix B—Copies of comment letters**

Wayne Upton  
Chairman  
IFRS Interpretations Committee  
30 Cannon Street  
London  
United Kingdom  
EC4M 6XH

22 July 2016

Dear Mr Upton

**Tentative agenda decision – IFRIC 12 *Service Concession Arrangements: Accounting for service concession arrangements for which the infrastructure is leased***

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the May IFRIC Update of the tentative decision not to take onto the Committee's agenda a request for clarification of how an operator accounts for a service concession arrangement not including any construction or upgrade services for which the infrastructure is leased.

We agree with the IFRS Interpretations Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision, although we believe that further explanation of the facts and circumstances that would be considered in determining whether the operator or the grantor has the obligation to make payments to the lessor could usefully be added to the final agenda decision.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely



Veronica Poole  
Global IFRS Leader



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Wayne Upton  
Chairman of the  
IFRS Interpretations Committee  
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**IFRS Technical Committee**

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Berlin, 15 July 2016

Dear Wayne,

**IFRS IC's (tentative) agenda decisions in its May 2016 meeting**

On behalf of the Accounting Standards Committee of Germany (ASCG), I am writing to comment on the tentative agenda decisions and on one (final) agenda decision, taken by the IFRS Interpretations Committee (IFRS IC) and as published in the May 2016 *IFRIC Update*. Please find our detailed comments in the appendix to this letter.

If you would like to discuss our views further, please do not hesitate to contact Jan-Velten Große ([grosse@drsc.de](mailto:grosse@drsc.de)) or me.

Yours sincerely,

*Andreas Barckow*

President

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Prof. Dr. Andreas Barckow (President)  
Peter Missler (Vice-President)

## **Appendix A – Comments on tentative agenda decisions**

### ***IFRIC 12 – Combined service concession & lease arrangements***

The IFRS IC received our request to clarify how an operator accounts for a service concession arrangement for which the infrastructure is leased. We asked the IFRS IC to clarify whether the arrangement is within the scope of IFRIC 12 (scope issue). With respect to this issue, we welcome the IFRS IC's observation that the operator is not required to provide construction or upgrade services with respect to the infrastructure for the arrangement to be within the scope of IFRIC 12 and, in this case, the lease of the infrastructure is not within the scope of IFRS 16 Leases (IAS 17 Leases) for the operator.

Consequently, this led to our subsequent question as to how the operator should account for any assets and liabilities arising from the arrangement with the lessor (recognition and presentation issues). With respect to this issue, we share the IFRS IC's view that it is the grantor, and not the operator, who controls the right to use the infrastructure. Accordingly, the operator assesses whether it is obliged to make payments to the lessor for the lease or whether the grantor has this obligation.

Finally, the IFRS IC noted that the issues and assessments require consideration of all facts and circumstances and, in the end, concluded that the requirements in IFRS Standards provide an adequate basis to enable an entity to determine how to account for the arrangement. Whilst following the IFRS IC's line of thinking and technical arguments in the light of the existing requirements in IFRS Standards, we would have preferred had the IFRS IC provided a clarification to IFRIC 12 that would have enhanced the practical application of the assessment on the recognition and presentation issue.

IFRS Interpretations Committee  
30 Cannon Street  
London EC4M 6XH  
UK

July 29, 2016

Dear Mr. Upton,

We are writing in response to the tentative agenda decision published in the May 2016 IFRIC Update relating to **“IFRIC 12 Service Concession Arrangements—accounting for service concession arrangements for which the infrastructure is leased.”**

In this Update, the Committee has commented on two issues on which we would like to express our concerns.

**Issue 1: the scope issue**

Although we agree with the conclusions described in the Update, namely that:

- a) Assessing whether a particular arrangement is within the scope of IFRIC 12 requires consideration of all facts and circumstances. In particular, the operator assesses whether the control conditions in paragraph 5 of IFRIC 12 and the condition relating to the infrastructure in paragraph 7 of IFRIC 12 apply; and
- b) The operator is not required to provide construction or upgrade services with respect to the infrastructure for the arrangement to be within the scope of IFRIC 12,

we are concerned by the rationale developed in the agenda paper dating from November 2015 which seems to conclude that, in the case submitted, the grantor controls the residual interest only through a mere option whose characteristics are not specified. Although "agenda papers" are not part of IFRS authoritative literature, we are concerned they can nevertheless be used to force an arrangement to fall into the scope of IFRIC 12 every time the grantor has a renewal option.

The agenda paper provides in paragraph 35 some factors that entities should consider in making an assessment in relation to the condition in paragraph 5(b) of IFRIC 12. These seem to be both relevant and beneficial to an understanding of the analysis that must be performed. These factors do not suggest that any renewal option systematically gives control to the grantor on the residual interest.

## Issue 2: the recognition and presentation issues

We are particularly concerned by the conclusions of the Committee in this area for the following reasons:

1. In the absence of a clear definition and standard treatment of executory and non-executory contracts in IFRS, we do not think that it is appropriate that an IFRIC agenda decision should in effect make a ruling on this matter.

Indeed, much of the reasoning in the rejection decision is based on the way IFRS 16, a standard that is not yet effective, interprets [partially] the notion of executory or non-executory contracts, while the interpretation of an executory contract as used in the currently effective standard IAS 17 appears to be ignored. The main argument is that the making available of the property is sufficient to impose the recognition of an asset and a liability under IFRIC 12. We disagree, as in both IAS 17 and IFRS 16 this condition alone is not sufficient to recognise asset and liability.

Indeed, both IFRS 16 and IAS 17 acknowledge the existence of two different natures of contract, one being accounted for as an executory contract even when the asset has been made available for use:

- Operating lease in IAS 17
- Service contract in IFRS 16, ie a contract that does not convey the right to control the use of an identified asset.

In the situation examined by the Committee, the contract would always be accounted for as an executory contract, even when the asset has been made available for use, because:

- It is qualified as an operating lease in IAS 17
- It is not qualified as a lease contract in IFRS 16, because the operator does not control the use of the asset (since it is controlled by the grantor and that is why the transaction falls within IFRIC 12).

2. There is no reason to have different accounting treatments for the same contract depending on whether it falls within the scope of IAS 17 (IFRS 16) or IFRIC 12. In fact, IFRIC 12 is only an Interpretation intended to explain when and how to explain the relevant standards. It should not supersede the standards themselves.

Yours sincerely,

Patrice MARTEAU  
Chairman

