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Technical Director  
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***File Reference No. EITF12H: Service Concession Arrangements***

I appreciate the opportunity to comment on the Financial Accounting Standards Board (the “Board”) Proposed Accounting Standards Update: *Service Concession Arrangements* (the “Exposure Draft”). I generally support the Board’s efforts to clarify and synchronize accounting guidance in this area. I feel the Exposure Draft would improve financial reporting through increased consistency within the United States as well as better alignment with International Financial Reporting Standards (IFRS).

**Question 1: Do you agree that the scope of the Exposure Draft should include only service concession arrangements for which the grantor is a public sector entity? If not, what other types of arrangements should be included within the scope of the Exposure Draft?**

While the Exposure Draft does not explicitly outline a conceptual basis for requiring different accounting treatment when the grantor is a “public sector entity” and when the grantor is not a “public sector entity”, I do not feel this is a major issue because I agree that most service concession arrangements will inherently involve “public sector” grantors. Considering this, there is not a glaring need to expand the scope at this time and I agree that explicitly limiting the Exposure Draft scope will expedite the issuance process. However, I would not be surprised if a more detailed conceptual definition of what constitutes and differentiates a public sector entity may be needed in the future.

I would like to submit one consideration for clarifying the scope of the Exposure Draft:

- IFRIC 12 applies to arrangements where the concession arrangement covers essentially the entire useful life (whole of life assets) of the infrastructure irrespective of which entity would own any residual interest. It is not clear if the Exposure Draft is also meant to include these types of arrangements. I feel that the Exposure Draft should include these arrangements and I feel that this should be explicitly addressed in the Exposure Draft. This is important because I would expect that few arrangements in the U.S. would contain provisions where infrastructure (hospital, power plants, etc.) explicitly reverts to a governmental body after a specified period.

**Question 2: Do you agree that a service concession arrangement within the scope of this proposed Exposure Draft should not be accounted for as a lease under Topic 840?**

I agree with this conclusion. While I understand that these arrangements may fit into the conceptual definition of a lease, lease guidance was not drafted to address the intricacies of these types of arrangements. The current lease analysis required in assessing these arrangements is indeed confusing and can be driven by micro-level interpretations of fixed-price-per-unit concepts in the leasing literature. The end result is that two arrangements which are very similar in economic substance can be accounted for differently based on this lease analysis and this is always a concern within financial reporting. The Exposure Draft represents a significant improvement in this regard.

**Question 3: Do you agree that the infrastructure that is the subject of a service concession arrangement within the scope of this Exposure Draft should not be recognized as property, plant and equipment of the operating entity?**

I generally support this treatment; however, I do have some questions about the ramifications of this conceptual change in asset nature for the impacted entities. In the basis for conclusions, the Board notes that the operating entity should not classify the infrastructure as PPE because the grantor dictates who it can sell to and for what prices. This could be construed as creating a new definition of “control”. Other definitions of control rely more on a risk/benefits analysis and the power to control the most significant economic activities of an entity. Could these concepts conflict?

For example, consider a Sponsor Company which creates a Project Company (VIE) to construct and operate a single power plant subject to a service concession arrangement for the life of the plant. In a VIE analysis, the project company would show the PPE and the concession agreement would absorb the market risk from the plant (assuming it is a fixed price agreement). Here the grantor would be a variable interest and an analysis would be done to figure out who controls the plant entity’s most significant economic decisions (e.g. operations and dispatch). Under the Exposure Draft, the grantor could conceptually be considered to control the plant but the Sponsor Company could control the ongoing economic decisions of the plant. Does a conclusion that the grantor controls the plant imply that the most significant economic activities are the pricing and deployment decisions made at the inception of the service concession agreement? Does this create an immediate presumption that the grantor should consolidate the Project Company or that power is shared? This could cause confusion and uncertainty for ongoing VIE analyses within impacted entities.

I also note that currently a single power plant entity with a service concession arrangement would be considered in-substance real estate under ASC 360. If that entity no longer reports PPE and replaces it with an intangible asset, is it the Board’s intention that the single plant entity would no longer be considered in-substance real estate? Would any historical real estate accounting treatments (i.e. a sale of in-substance real estate with continuing involvement) that resulted from the entity’s status as real estate be modified as part of the transition?

Additionally, I feel that more detailed guidance in this area would be helpful. If the operating entity does not record PPE, the Exposure Draft only directs users to follow other guidance. I feel it would be helpful for the Board to outline their intentions regarding the alternative accounting treatments. Does the Board intend that a model similar to the IFRIC 12 model be used (intangible or financial asset based on whether there are unconditional payments or the right to charge users)? One of the conceptual challenges in IFRIC 12 was the idea of revenue recognition during the construction of the infrastructure under the intangible asset model. IFRIC 12 prescribes that a user record an intangible asset and revenue during construction based on costs of the infrastructure plus a profit margin. Does the Board intend for these provisions to be adopted under the Exposure Draft? I feel that including more guidance here would help the Board achieve its objective of greater financial reporting consistency.

**Question 4: Do you agree that the amendments in this Exposure Draft should be applied using a modified retrospective approach to all arrangements existing at the beginning of the reporting entity's fiscal year of adoption?**

I agree with this conclusion.

**Question 5: Would the transition requirements in the Exposure Draft be difficult to apply?**

As mentioned above, the Exposure Draft is not specific on alternative accounting and without fully understanding the Board's intentions it is difficult to assess the analysis that would be needed in transition. Given the size and nature of infrastructure, I would expect the change from a PPE classification to an intangible asset classification to also have ramifications on other material items in the financial statements. Specifically, I feel that the following are points which should be explicitly addressed in transition guidance:

- An asset retirement obligation is defined as an obligation related to the removal of a tangible long-lived asset. If the operating entity no longer has the PPE on its books, does the Board intend that these obligations now be included in the scope of ASC 420 for the operating entity? Should ARO amounts previously capitalized to the infrastructure asset be immediately written off upon adoption?
- Once the infrastructure is placed in service, do additional maintenance obligations give rise to an additional intangible asset and revenue (if following an IFRIC 12 model)?
- If the asset is considered an intangible right to bill, does that imply that test energy produced when starting a power plant should be revenue and not taken against the PPE?
- If an entity removes PPE and recognizes an intangible asset, are capitalized interest costs permitted to be included in the intangible asset base as they are under IFRIC 12?
- If the Company previously concluded that a service concession agreement qualified as a lease and capitalized certain initial direct costs of that lease, would those costs need to be written off upon adoption?

**Question 6: The proposed amendments would apply to both public and nonpublic entities. Should the proposed amendments be different for nonpublic entities? If so, please describe how and why you think they should be different.**

I agree that the amendments should apply to both public and nonpublic entities.

**Question 7: For preparers, how much time would be needed to implement the proposed amendments?**

I believe the amendments would not present a substantial implementation challenge. As I have mentioned above, more detailed transition guidance would be helpful in implementing the amendments quickly and accurately. I would also advocate allowing early adoption of the amendments as applicable.

I appreciate the Board's consideration of my comments.

Sincerely,

Greg Capps, CPA