May 12, 2021

Mr Ross Smith

Technical Director

International Public Sector Accounting Standards Board

International Federation of Accountants

277 Wellington Street, 4th floor

Toronto

Ontario M5V 3H2

CANADA

RE: Responses to RFI, *Concessionary Leases and Other Arrangements Similar to Leases*

Dear Mr. Smith,

We welcome the opportunity to comment on RFI, *Concessionary Leases and Other Arrangements Similar to Leases*. Our responses to the specific questions raised in the RFI as well as other comments are set out in Appendix 1.

Should you have any queries concerning the matters in this submission, or wish to discuss them in further detail, please contact Mr. Abdullah Alhomaida via email at:

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Yours sincerely,

Abdullah Al Mehthil

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Appendix 1 – Comments on RFI, *Concessionary Leases and Other Arrangements Similar to Leases*

Question 1: In your jurisdiction, do you have concessionary leases (or similar arrangements) as described in this RFI? If yes, please: (a) Describe the nature of these leases (or similar arrangements) and their concessionary characteristics; and (b) Describe the accounting treatment applied by both parties to the arrangement to these types of leases (or similar arrangements), including whether the value of the concession is reflected in the financial statements.

Comment: Yes, we have. The Ministry of Environment, Water and Agriculture leases out land plots to private investors at below market or nominal rates under long-term leases to cultivate as farms or to use in non-agricultural ventures. Similarly, the Ministry of Municipal Rural Affairs & Housing leases out land plots to businesses at below market or nominal rates under long-term leases to use as workshops or warehouses. These leases are typically renewable at the option of the lessee and provide that all facilities erected on site becomes the property of the lessor on termination of the lease. As public sector entities have been reporting under a cash basis of accounting and are now transitioning to accrual accounting, a specific accounting treatment has yet to be determined for such arrangements. See the answer to Question 2 regarding the literature that is being considered for accounting policies on nominal/below-market consideration leases.

Also, some public sector entities provide housing to their employees for a nominal consideration or at below-market rates during their employment. As public sector entities have been reporting under a cash basis of accounting and are now transitioning to accrual accounting, a specific accounting treatment has yet to be determined for such arrangements. However, we understand that under accrual-basis IPSASs, the housing facilities, if owned, would be treated as owner-occupied properties, the nominal consideration would be treated as revenue from non-exchange transactions, and the depreciation of property and equipment would be expensed as employee costs unless an IPSAS requires its inclusion in the cost of another asset.

Question 2: In your jurisdiction, do you have leases for zero or nominal consideration as described in this RFI? If yes, please: (a) Describe the nature and characteristics of this type of lease (or similar arrangement); and (b) Describe if and how the value of the concession is reflected in the financial statements of both parties to the arrangement.

Comment: Yes, we have. The State Properties General Authority (SPGA) was created to centrally hold title to and manage state-owned properties. SPGA may assign state-owned properties free of charge and indefinitely to public sector entities for use solely in achieving their service delivery objectives. SPGA may cancel the assignment and reassign the property to another entity where, among other situations, the property is no longer needed/used by the entity.

In other instances, SPGA may have an arrangement with a public sector entity whereby the properties assigned to the entity or parts thereof are made available to let by the public (for example, shacks, vendor spaces, workshops, warehouses) and any rents generated are shared in pre-agreed ratios between SPGA and the public sector entity.

Similarly, a number of cities/governorates have royal commissions that have legal title to a wide range of public properties within those cities/governorates and that allow certain specialized properties to be used free of charge by other public sector entities to deliver services. For example, school buildings are used by the Ministry of Education to provide education.

As public sector entities have been reporting under a cash basis of accounting and are now transitioning to accrual accounting, accounting policies are being developed for these transactions. There is currently no IPSAS that is specifically applicable, and, therefore, research into other literature and international practices is being undertaken to arrive at appropriate accounting policies in light of Paragraphs 12-15 of IPSAS 3. Following is a summary description of some of the relevant literature that has been identified as part of the research:

- The UN: The UN and affiliated organizations have adopted accrual-basis IPSASs as their financial reporting framework. The *UN Corporate Guidance on Leases and Donated Right-to-Use Arrangements* shows that, as lessees, the UN entities treat donated right-to-use arrangements similar to leases, applying IPSAS 13 *Leases* and IPSAS 23 *Revenue from Non-Exchange Transactions (Taxes and Transfers)*. The arrangement is classified as either a finance lease or operating lease, depending on whether it transfers substantially all the risks and rewards incidental to ownership of the underlying asset. "Finance leases" give rise to an asset, measured at fair value, and a corresponding liability being deferred revenue. The asset and associated deferred revenue are depreciated/amortized over the useful life of the asset resulting in a depreciation expense and a matching non-exchange revenue. "Operating leases", on the other hand, give rise to a rent expense, measured at fair value of the rent that would be paid, and a matching non-exchange revenue.

- The UK: The financial reporting framework used is the EU-adopted IFRSs as adapted or interpreted for the public sector context by HM Treasury. HM Treasury's *Government Financial Reporting Manual: 2020-21* and *IFRS 16 Application Guidance* show that peppercorn leases (leases for which the consideration paid is nil or nominal; that is, significantly below market value) are accounted for from a lessee perspective under IFRS 16 *Leases* and IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*. A right-of-use asset is recognized and initially measured at current value in existing use or fair value, depending on whether the right-of-use asset will be held for its service potential. A lease liability is recognized and measured in accordance with IFRS 16. Any difference between the carrying amount of the right-of-use asset and the lease liability is recognized as income as required by IAS 20. The right-of-use asset is measured subsequently using the revaluation model.
- Australia: The financial reporting framework used is the Australian Accounting Standards which are largely IFRS-equivalents. Leases that have significantly below-market terms and conditions principally to enable the entity to further its objectives are accounted for from a lessee perspective under AASB 16 *Leases* and AASB 1058 *Income of Not-for-Profit Entities*. A right-of-use asset and a lease liability are recognized and measured following the principles in AASB 16 (which are the same as in IFRS 16). However, a not-for-profit entity may elect to measure the right-of-use asset at initial recognition at fair value. If this election is made, the not-for-profit entity will still measure the lease liability in accordance with AASB 16 and will recognize any related items (including revenue) in accordance with AASB 1058. The right-of-use asset is measured subsequently using the cost model unless (i) the lessee applies the fair value model in AASB 140 *Investment Property* to its investment property and the right-of-use assets meets the definition of investment property in

AASB 140, in which case the lessee will apply the fair value model to the right-of-use asset; or (ii) the right-of-use assets relate to a class of property, plant and equipment to which the lessee applies the revaluation model in AASB 116 *Property, Plant and Equipment*, in which case the lessee may elect to apply the revaluation model to all of the right-of-use assets that relate to that class of property, plant and equipment.

Mirroring the treatments from the lessee's perspective described above, such arrangements would give rise, in the financial statements of lessors, to such items as deferred transfer expense, derecognition of leased assets, lease receivables, transfer expense, interest revenue, rent revenue and depreciation expense, depending on how the arrangement is classified and whether it involves a consideration.

An added accounting complexity is that many of the assigned properties had been owned by the assignees but whose title was later transferred for no consideration, by act of government, to SPGA following its establishment. Due to the analogy, IFRIC 12 *Service Concession Arrangements* and the accounting under the Grant of a Right to the Operator Model in IPSAS 32 *Service Concession Arrangements: Grantor* are also being considered for situations where an asset is provided and used by one entity while control of the asset rests with another entity.

Question 3: Does your jurisdiction have arrangements that provide access rights for a period of time in exchange for consideration? If yes, please describe the nature of these arrangements and how they are reflected in the financial statements of both parties to the arrangement.

Comment: Yes, we have. Examples include concession contracts entered into between government and private sector operators, port storage, public paid parking, frequency usage.

As mentioned before, public sector entities have been reporting under a cash basis of accounting and are now transitioning to accrual accounting. However, we understand that:

- Public sector grantors would apply IPSAS 32 *Service Concession Arrangements: Grantor* to service concession agreements, and that private sector operators are already applying IFRIC 12 *Service Concession Arrangements*.

- Under IPSASs, port storage and public paid parking would be treated as operating leases while frequency usage charges would be treated in accordance with IPSAS 9 *Revenue from Exchange Transactions* (or the final IPSAS on *Revenue with Performance Obligations*).

As regards the question of whether government acquires rights of access to privately-owned property and/or land (easements/servitudes) as described in paragraphs 16-18 of the RFI, rather than buying right of access to a privately-owned property or land, the general approach followed by government involves expropriating the property or land or part thereof, as needed, for the benefit of the overall public subject to the payment in advance of fair compensation.

Question 4: There are cases where public sector entities deliver services (for example, education services) using properties provided by third parties (for example, trusts and non-government entities). In some cases, these entities can substitute the properties, and in other cases they cannot. Often, there is no written arrangement, but the public sector entity can only use the properties for their specific service. In your jurisdiction, do you have arrangements with the same or similar characteristics to the one identified above? If yes, please describe the nature of these arrangements and how they are reflected in the financial statements of both parties to the arrangement.

Comment: Yes, we have. However, the properties are typically provided by other government entities rather than by trusts and non-government entities. See the answer to Question 2.

Question 5: In your jurisdiction, do you have arrangements involving social housing with lease-type clauses or other types of lease-like arrangements with no end terms? If yes, please describe the nature of these arrangements and how they are reflected in the financial statements of the social housing provider.

Comment: Yes, we have. The Ministry of Municipal Rural Affairs & Housing provides social housing to eligible citizens at nominal rates under irrevocable rental contracts with very extended terms (100 years). As public sector entities have been reporting under a cash basis of accounting and are now transitioning to accrual accounting, a specific accounting treatment has yet to be determined for such arrangements. However, we understand that under accrual-basis IPSASs, if control of the buildings and equipment is deemed to have passed at the inception of the lease, their cost would be expensed as distributed inventory, land would still be recognized, and the nominal rent would be treated as revenue from non-exchange transactions.

Question 6: In your jurisdiction, do you have arrangements involving the sharing of properties without a formal lease contract? If yes, please describe the nature of these arrangements and how they are reflected in the financial statements of both parties to the arrangement.

Comment: Yes, we have many public sector entities that share properties without formal lease contracts. Such sharing is normally based on a decision or directive by the appropriate level of government.

As public sector entities have been reporting under a cash basis of accounting and are now transitioning to accrual accounting, a specific accounting treatment has yet to be determined for such arrangements. See the answer to Question 2 regarding the literature that is being considered for accounting policies on zero consideration leases.

Question 7: In your jurisdiction, do you have other types of arrangements similar to leases not mentioned in this RFI? If so, please describe the characteristics of these arrangements and how they are presently being reflected in the financial statements of both parties to the arrangement.

Comment: We are not aware of any other types of arrangements similar to leases not mentioned in the RFI.

Other Comments:

We believe that any Standard on the arrangements described in the RFI should address the accounting from the perspective of each party to the arrangement where both parties are commonly public sector entities.