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GASB Requires Public Entities to Make Room in the Debt Column for Availability Payment-Based P3 Projects: Ballard Spahr

For those interested in availability payment (AP) or service payment structures for public-private partnerships (P3s), June 15, 2020, was an important day despite lack of fanfare. In a policy debate within the P3 space between those who view APs as contractual obligations versus those who view APs as “debt,” the Governmental Accounting Standards Board (GASB) picked a side: APs constitute a debt obligation of the public sector participant in the P3.

In GASB’s Statement No. 94, “[Public Private and Public-Public Partnerships and Availability Payment Arrangements](#),” the Board purports to “improve financial reporting” as it relates to AP arrangements, effective in June 2022. GASB refers to AP arrangements as “APAs,” as distinguished from revenue- or user fee-type P3s, which GASB classifies as “service concession arrangements” or SCA-type P3s. GASB-94 requires that APs are to be “accounted for by a government as a financed purchase of the underlying nonfinancial asset.”

More broadly, GASB-94 sets out to provide “accounting and financial reporting requirements for all other” P3s, specifically, those that aren’t “leases” or SCAs. P3s that are structured similarly enough to leases are guided by a prior statement, [GASB-87](#), from 2017, which essentially requires that a lessor similarly “recognize a lease receivable.” An even earlier statement, [GASB-60](#), from 2010, addresses SCAs and accounting and reporting requirements that are more complicated, given the transfer or sharing of revenue risk associated with the P3 asset, a topic we are not addressing today.

Taking the position that APs constitute debt is vitally important, as GASB promulgates the “generally accepted accounting principles” (GAAP), the accounting and financial reporting standards state and municipal governments observe, and require that many contractors do, as well, in many transactions.

Aligning APs more closely to leases than to SCAs also strikes an important policy position. Many public entities with a long history of procuring AP P3s have reasonably taken the opposite view – that APAs are more like SCAs. With SCAs, rather than taking a revenue or user fee risk (that is, payment for use of a facility, such as bridge toll), a private sector partner/concessionaire takes the underlying performance risk (that is, whether or not there is a toll, the private sector partner is paid if the facility is available for use and thus capable of assessing the toll/user fee). This opposing view holds that APAs and SCAs are more alike than different, and the nature of the transaction was to document the agreement about which P3 party would have more or less exposure to the users.

Accordingly, procuring public entities negotiated detailed, project-specific performance criteria – valuing those aspects of performance that were important to the public entity and its constituency. For example, if a transit line failed to keep its headways, then the public agency would pay the private sector/concessionaire less. The risk of variability of payments incentivized performance. In an effort to mediate what was left of the user-fee risk – for instance, despite a water works functioning properly, consumer use was down – procuring agencies were able to attract more

competition and better prices for the P3 contracts.

With GASB's position, the variability of the payments is not relevant to whether those payments are a structured purchase (i.e., debt obligation). It takes a position that there will always be payments, which presumes that the private sector/concessionaire will consistently and fully perform. This is an optimistic view.

Now, public entity treasurers and CFOs are charged with recognizing "[g]overnmental fund revenue ... in a systematic and rational manner over the P3 term," which is not a clear guide. And the public sector has to figure this out in the context of the payments as debt payments, albeit variable debt payments under circumstances in someone else's control. This will likely require, under other accounting practices and conventions, restatements and revisions as the performance (or lack of performance) of the facility or private sector partner/concessionaire plays out over the term of the P3.

For certain sectors and P3 projects, the ability to treat an AP P3 as an SCA and not as debt from an accounting standpoint is often a motivating factor in deciding whether to pursue the project from the outset. If the APs are not debt, then the obligation to pay the APs would not count towards the public entity's overall debt restrictions, including debt caps (whether statutory or via covenants) and debt-related covenants (including debt service coverage ratios). One result of GASB-94 is to remove an impetus for projects and programs. The APs will count as debt for these various calculations, which may result in potential AP P3s being less attractive to the public entity.

But the ultimate impact of GASB-94 is yet to be determined. It takes effect for those fiscal years beginning after June 15, 2022. P3s currently in procurement and predevelopment will likely undergo near-term reconsideration of their affordability.

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