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Guidance for Conduit Debt Obligations

In May 2019, the GASB issued GASBS No. 91, *Conduit Debt Obligations*, to eliminate diversity in practice related to conduit debt obligations. The statement clarifies the definition of conduit debt obligations, establishes guidance for their accounting and reporting, and expands their required disclosures.

Practical Consideration:

GASBS No. 91 is available on Checkpoint at **checkpoint.riag.com** if you subscribe to GASB content. You can also access the statement on the GASB website at **www.gasb.org**.

Definition

Conduit debt obligations are debt instruments issued in the name of a state or local government for the benefit of a third-party obligor that is primarily responsible for repaying the debt and has all of the following elements:

- At least three parties are involved: an issuer, a third-party obligor, and a debt holder or trustee.
- The issuer and the third-party obligor are not part of the same financial reporting entity.
- The obligation is not a parity bond (i.e., two or more bond issues with equal rights to collateral) or cross-collateralized with other debt of the issuer.
- The third-party obligor (or its agent) ultimately receives the debt proceeds.
- The third-party obligor is primarily responsible for repayment of the debt. (However, the issuer may facilitate payment from the third-party obligor to the debt holder.)

All issuers make limited commitments related to conduit debt obligations to maintain their tax-exempt status. Some issuers may make additional commitments associated with conduit debt obligations, including moral obligation pledges, appropriation pledges, financial guarantees, and asset or revenue pledges as security. In addition, an issuer may

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voluntarily make a debt service payment if the third-party obligor is unable to do so.

Recognition and Measurement

Issuers do not record a liability for the conduit debt obligation unless it is more likely than not that the issuer will make one or more debt service payments associated with its additional or voluntary commitments. An issuer with only limited commitments is required to perform a more likely than not assessment when an event or circumstance causes it to consider making a voluntary debt service payment. An issuer with additional commitments is required to perform an annual assessment of qualitative factors to determine if it is more likely than not that it will make a debt service payment. For financial statements using the economic resources measurement focus, the liability is measured as the present value of the best estimate of the debt service payments expected to be made. For financial statements using the current financial resources measurement focus, the liability is generally recorded as the amount of the debt service payment when the debt service payment is due and payable.

Capital Asset Arrangements

Issuers of conduit debt obligations may enter into arrangements associated with capital assets, sometimes referred to as leases, that should *not* be accounted for in accordance with lease guidance. These arrangements involve construction or acquisition of a capital asset with the proceeds of the debt in which title of the capital asset is retained by the issuer and the third-party obligor makes payments to the issuer that coincide with and cover the debt service repayment schedule. If the arrangement qualifies as a service concession arrangement, it should be accounted for in accordance with GASBS No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*. Otherwise, the arrangements should be accounted for as follows:

- If title of the asset transfers to the third-party obligor at the end of the arrangement, the issuer should not recognize a conduit debt obligation, the capital asset, or a receivable for the payments received from the third-party obligor.
- If title of the asset does not transfer to the third-party obligor but the third-party obligor has exclusive use of the asset during the arrangement, the issuer should recognize the capital asset at acquisition value with an associated inflow of resource *at the end of the arrangement*.
- If title of the asset does not transfer to the third-party obligor but the third-party obligor has exclusive use of portions of the asset during the arrangement, the issuer should recognize the entire capital asset with an associated deferred inflow of resources *at the inception of the arrangement*. In addition, over the term of the arrangement, the issuer should recognize an inflow of resources and reduce the deferred inflow of resources in a systematic and rational manner.

Disclosure Requirements

GASBS No. 91 requires issuers to disclose the amount and description of conduit debt obligations, including limited, additional, or voluntary commitments. If a liability is recognized, the issuer is also required to disclose a rollforward of the liability (e.g., beginning balance, increases, decreases, ending balance), the cumulative amount of any payments made to date, and any amounts expected to be recovered.

Effective Date and Transition

GASBS No. 91 is retroactively effective for reporting periods beginning after December 15, 2020, with earlier application encouraged.

GASB Issues Updated Implementation Guide

In April 2019, the Governmental Accounting Standards Board issued Implementation Guide No. 2019-1, *Implementation Guidance Update—2019*. The Guide addresses new questions and answers (Q&A) and amends Q&A from previously reported implementation guides. The updated guidance includes new Q&A related to postemployment benefits, derivative instruments, nonexchange transactions, insurance recoveries, intra-entity asset transfers, fund balance reporting, tax abatement, and irrevocable split interest agreements. Additionally, amendments to previously issued Q&A are also included in the updated Guide.

What's New?

The Guide includes new Q&A for these topics:

- *Postemployment Benefits Other Than Pensions—Plan and Employer Accounting and Reporting.* The Guide added five new Q&A related to this topic. The first two new Q&A clarify that the average of index rates at different dates cannot be used when determining the discount rate for purposes of measuring a total pension liability, a total OPEB liability, or a (collective) OPEB liability. To remain in accordance with the GASBS, the rate must be measured as of the pension/OPEB plan's fiscal year-end or the pension/(collective) OPEB's liability date. The last three new Q&A discuss the inclusion of the implicit rate subsidy when OPEB benefit payments are implicit in amounts paid by the employer or government for active employees.

- *Accounting and Financial Reporting for Derivative Instruments.* The new Q&A clarifies that when the government terminates an interest rate swap, it is released from the rights and obligations of the swap and must report both the deferred outflow or inflow of resources and the settlement receivable or payable as of the termination date.
- *Statement No. 33, Accounting and Financial Reporting for Nonexchange Transactions.* The new Q&A clarifies that a city government cannot recognize voluntary nonexchange revenue for the reimbursement of costs previously incurred related to a natural disaster until the federal disaster-related grant agreement is executed.
- *Statement No. 42, Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries.* The new Q&A clarifies that the reporting of insurance recoveries is dependent on whether the insurance recoveries are realized or are measurable and available in the same year (net against the related storm damage cleanup expenditures) or subsequent years (report in other financing sources or extraordinary items).
- *Statement No. 48, Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues.* The Guide added two new Q&A related to this topic. The new Q&A clarifies that capital assets transferred to component units should be reported at the transferor's carrying value on financial statements of the component unit and maintain their classification as capital assets, even if the component unit's intent is to sell the capital asset at the appraised value after the transfer.
- *Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions.* The new Q&A clarifies that the long-term portion of notes receivable for revenue not yet recognized should be reported as a deferred inflow of resources and not be included in the fund balance, because the funds are not yet available.
- *Statement No. 77, Tax Abatement Disclosures.* The new Q&A clarifies the calculation of the gross dollar amount when local governments utilize fees in lieu of taxes (FILOT) agreements with local businesses in addition to other incentives.
- *Statement No. 81, Irrevocable Split-Interest Agreements.* The Guide added two new Q&A related to this topic. The Q&A clarifies how the remainder interest should be recorded when it is required to be used to establish a permanent endowment and when a state government is the lead interest beneficiary.

What Changed?

The Guide amended Q&A affecting the following topics:

- *The Financial Reporting Entity.* The Guide amends Question 4.17.1 in Implementation Guide 2015-1 for a technical correction related to the application of the financial accountability provisions of Statement 14, as amended, relative to special-purpose governments.
- *Pensions—Plan and Employer Accounting and Reporting.* The Guide amends Question 5.74.1 in Implementation Guide 2015-1 to clarify that the guidance is specific to stand-alone plan financial reporting.
- *Postemployment Benefits Other Than Pensions: Plan and Employer Accounting and Reporting.* The Guide amends Question 4.53 in Implementation Guide 2017-2 to clarify that the guidance is specific to stand-alone plan financial reporting.
- *Accounting and Financial Reporting for Derivative Instruments.* The Guide amends Question 10.46.10 in Implementation Guide 2015-1 for a technical correction related to paragraph 10 of Statement 38 and to clarify that the guidance is specific to disclosure requirements of Statement 53.

Effective Date

Implementation Guide 2019-1 is effective for reporting periods beginning after June 15, 2019, with earlier application encouraged if the pronouncements addressed by the Q&A have been implemented. Changes to conform to the provisions of this Guide should be applied retroactively using restated financial statements for all prior periods, if practicable. If not practicable, report the cumulative effect, if any, of applying this Guide as a restatement of beginning net position for the earliest restated period. The first financial statement applying this Guide should include notes disclosing the nature and effect of the restatement and the reason for not restating prior periods.

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Upcoming GASB Activity

The GASB will be busy this summer with plans to propose new or revised standards in multiple projects. In this article, we discuss the GASB's projects and what you can expect in the upcoming months.

PPPs and APAs

This project addresses accounting and financial reporting for public-private partnerships (PPPs) and availability payment arrangements (APAs). The project will also consider possible amendments to Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, including accounting and financial reporting guidance related to Service Concession Arrangements (SCAs), and provide guidance for other types of PPPs that are not within the scope of Statements No. 60 and No. 87, *Leases*, such as APAs. The ED is expected to be issued in June with a comment period deadline in September.

Deferred Compensation Plans

As a result of GASB's reexamination of Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*, which found that some Section 457 deferred compensation plans have evolved to closely resemble defined contribution pension plans, the Board has decided to propose that if a Section 457 plan meets the definition of a pension plan as defined in Statement No. 68, *Accounting and Financial Reporting for Pensions*, as well as Statements No. 67, *Financial Reporting for Pension Plans*, and No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68*, then pension standards should be applied by a government. The ED is expected to be issued in June with a comment period deadline in September.

Omnibus Proposal

This project addresses numerous technical corrections and practice issues that have been identified. The project will propose revisions to: change the effective date of Statement No. 87, *Leases*, to *fiscal years* beginning after the implementation date rather than *reporting periods*; address intra-entity transfers of assets; change the definition of collections in Statement No. 84, *Fiduciary Activities*; address inconsistencies in reinsurance recoveries; add an explicit exclusion for asset retirement obligations to Statement No. 69, *Government Combinations and Disposals of Government Operations*; and provide a technical correction for Statement No. 72, *Fair Value Measurement and Application*. The ED is expected to be issued in June with a comment period deadline that extends into October.

Practical Consideration:

Once issued, EDs are available on Checkpoint at **checkpoint.riag.com** if you subscribe to GASB content, as well as the GASB website at **www.gasb.org**.

Future articles will keep you informed of future GASB activity related to these projects.