



November 2, 2018

Mr. David Bean, Director of Research and Technical Activities  
Governmental Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, Connecticut 06856-5116

RE: Project No. 26-6 *Conduit Debt Obligations*

Dear Mr. Bean:

On behalf of the Association of Government Accountants (AGA), the Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments to the Governmental Accounting Standards Board (GASB) on its Exposure Draft of *Conduit Debt Obligations*, (CDOs).

The FMSB is comprised of 19 members (list attached) with accounting and auditing backgrounds in federal, state and local government, as well as academia and public accounting. The FMSB reviews and responds to proposed standards and regulations of interest to AGA members. Local AGA chapters and individual members are also encouraged to comment separately.

We appreciate the GASB's continued effort in setting and providing clarification of the standards relating to the State and Local Governments. We have reviewed the Exposure Draft and we believe it is a positive step for state and local government financial reporting transparency to clarify the provisions of GASB Interpretation No. 2, *Disclosure of Conduit Debt Obligations*, along with related questions in the *Implementation Guide* and various paragraphs related to CDOs in other GASB Statements.

The FMSB has some concerns however. Discretely presented component units of states routinely issue CDOs that would fit the definition proposed by the GASB. This is often done through state revolving funds utilizing a leveraged model. Often, the third-party obligor pays a trustee, who pays the bondholders. However, in some cases, the third-party obligor pays the issuer, which then pays bondholders. The issuer may retain the bond proceeds for construction purposes as well.

In either case, the provisions of the exposure draft does not indicate which entity (or entities) would record some form of debt, if the recently updated definition of "debt" contained in GASB Statement No. 88, par. 4, [GASB Codification Section 1500.129, as amended] applies to CDOs. We ask the GASB to address the state revolving fund process further and provide examples of recognition and reporting for these scenarios.

We are also concerned about whether the financial support of the primary government to a third-party obligor for debt issued by a discretely presented component unit constitutes conduit debt. If a government can issue debt through its component unit and then issue appropriations to a third-party obligor in the form of some form of municipal assistance (or aid) to support that debt, it appears we believe the government may be able to essentially hide the CDO debt outside of their CAFR. In some cases, CDOs may go unreported by any party to the transaction. Such support provided by a

government should be explicit. This specificity should be included in paragraph 5(f) to the Exposure Draft. In many situations, the support is a general obligation of the issuer and may be pledged.

We also believe the provisions of paragraph 5(b) need to be strengthened. We agree the issuer and the third-party obligor should not be in the same reporting entity to recognize a CDO. However, no mention is made in the Exposure Draft for reporting of CDOs in standalone financial statements of a discretely presented component unit as an issuer or as a third-party obligor.

The FMSB understands the Board deliberated the issues of State Revolving Funds as discussed in paragraph B5 of the Basis for Conclusions. However, we do not believe these issues were adequately addressed. Indeed, many issues of State Revolving Funds are parity bonds or have cross-collateralization features. But others do not have these features. If such entities issue CDOs as defined in a final standard, we believe the issuer should recognize the debt through maturity and recognize any receivable from general obligation support from another government and / or the third-party obligor(s). Third-party obligors should recognize borrowings related to financing of capital assets of the obligor in a similar manner to other forms of debt.

We are concerned that paragraphs 8 through 12 of the Exposure Draft are almost word for word elements of the qualitative aspects for recognition contained in GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees*. If a government has extended a nonexchange financial guarantee related to a CDO, it is reasonable that the government apply the provisions of GASB Statement No. 70, pars. 7-10, [GASB Codification Sections N30.103-106]? We recommend making a reference to GASB 70 instead of including the wording. If the current exposure draft is finalized as is, a preparer would need to refer to two separate standards to address financial guarantees.

The provisions of paragraphs 13 through 18 seem reasonable. However, in situations we have encountered, we do not believe an issuer has title to a capital asset (as discussed in paragraphs 15 through 18). In general, the issuer provides financing for capital assets retained and exclusively used by the third-party obligor. In such cases, as previously stated, a debt exists at the obligor and should be disclosed in accordance with the provisions of GASB Statement No. 88, par. 4 [GASB Codification Section 1500.129, as amended]. The issuer would recognize a receivable as discussed previously.

In terms of the proposed notes to financial statements, we believe the provisions of paragraphs 19 and 20 are reasonable. However, we also believe that if an issuer of a CDO has the characteristics of a debt issuer in accordance with GASB Statement No. 88, par. 4 [GASB Codification Section 1500.129, as amended], the issuer should align to the provisions of GASB-88. If the issuer has recognized a liability related to a nonexchange financial guarantee, the issuer should provide disclosure in accordance with the provisions of GASB Statement No. 70, paragraphs 14 and 15 [GASB Codification Sections N30.110-111].

Missing from the provisions of the Exposure Draft are note disclosure elements of third-party obligors. Currently, many third-party obligors disclose some form of financing, especially in the case of a constructed asset financed through a CDO. The Exposure Draft is unclear as to what third-party obligors should disclose. We again, suggest some linkage to GASB Statement No. 38, par. 10, as amended by GASB 88, pars. 4 and 6 [GASB Codification Section 1500.129, as amended] and not to GASB Statement No. 87.

We also ask the GASB to consider glossary entries in a final statement for:

- Conduit Debt Obligation
- Issuer
- Third-party Obligor

- Party bond
- Cross-collateralized
- Debt Trustee (perhaps also referencing corporate trustee)

Due to these issues, we believe that the proposed Effective Date and Transition provisions in the Exposure Draft are reasonable. If deliberations are extended, we presume the GASB will extend those provisions accordingly.

We appreciate the opportunity to comment on this document and will be pleased to discuss this letter with you at your convenience. If there are any questions regarding the comments in this letter, please contact Lealan Miller, Chair at [lmiller@eidebailly.com](mailto:lmiller@eidebailly.com) or at 208-383-4756.

Sincerely,



Lealan Miller, CGFM, CPA  
Chair- AGA Financial Management Standards Board

cc: John H. Lynskey, CGFM, CPA, AGA National President

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