August 28, 2018

Director of Research and Technical Activities, Project No. 26-6
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116
director@gasb.org

Re: Exposure Draft - Conduit Debt Obligations (Project No. 26-6)

Dear Sir:

The Michigan Government Finance Officers Association (MGFOA) has reviewed the Exposure Draft of the Governmental Accounting Standards Board on the Proposed Statement of the Governmental Accounting Standards Board (Project No. 26-6), dated July 30, 2018. We offer the following responses to your specific questions:

General Comments

In general, the MGFOA supports the concept that conduit debt obligations should be disclosed, rather than recognized in the issuer’s financial statements. We similarly support following the basic approach introduced in GASB 70 to recognize a liability and expense when the issuer government determines that it is more likely than not that it will support debt service payments for a conduit debt obligation.

However, we believe the Exposure Draft could be improved by more clearly defining certain terms, and by explicitly stating certain facts that we believe are implicit in the ED, but potentially subject to misunderstanding. We found a number of real-world situations to which we could see this standard being applied that we do not believe were necessarily within the Board’s intent for the ED, as described below.

Specific Recommendations

1. The term third-party obligor should be defined. What level of involvement in a debt issue is sufficient to qualify as a third-party obligor? For example, does the third-party obligor have to legally be a party to the debt agreement? For example, what if a county government were to issue debt for the benefit of several of its townships? If the debt is issued in the name of the county, but the expectation is that the townships will make debt service payments to the county to enable it to make the master debt service payment, are the townships third-party obligors? Does it matter if the arrangement between the county and townships is included in the documents authorizing the initial debt issue vs. in one or more separate agreements?

2. The meaning of ultimately receives the proceeds should be clarified. We believe it is the Board’s intent to focus on proceeds in the sense of cash, rather than any capital assets constructed or acquired with such cash. However, the ED isn’t explicit on this point. For example, if an issuer uses the proceeds of a borrowing to construct an asset that is subsequently leased to a third-party obligor (as opposed to providing the proceeds to the third-party), is that third-party obligor ultimately receiving the proceeds?
Or is that fact that the issuer directed the use of the proceeds in constructing an asset enough to say that the third-party did not ultimately receive the proceeds?

3. The term primarily obligated should be defined. This term appears especially subjective. What criteria determine this? Is it the entity responsible for making the debt service payments directly to the bond holders and/or paying agent? Or would the fact that one or more third-parties are responsible for paying the issuer an amount equal to the debt service (for the issuer to then use for making payment to the bond holders and/or paying agent) also qualify? Going back to the example above, if the county issued debt on behalf of several of its townships, is the county primarily obligated because it is the issuer and makes all the debt service payments, or are the townships primarily obligated, because the county only issued the debt on their behalf and they are legally bound to fund the County's obligation (by remitting their share of the debt service to the County)?

4. The meaning of extending a guarantee should be clarified. Is there a distinction between issuing debt that pledges a government's full faith and credit and extending a guarantee for payments to be made by a third-party? Intuitively, a guarantee seems like something one entity makes in support of the debt of another, not something an issuer makes on its own debt. Additional guidance would be helpful here.

5. The aggregate outstanding principal amount of all conduit debt obligations may be difficult information for many governments to obtain. Some governments do not currently track the outstanding principal amount of conduit debt with no related commitment, and may be unaware of any missed payments. In those cases, we recommend that the Board explicitly permit governments to estimate the amount still outstanding (based, for instance, on initial debt amortization schedules), or to disclose the original amount of conduit debt and the date it was expected to be retired. In our view, asking governments to annually track and monitor the status of this debt (especially where no commitment was made) would be an unreasonable burden to impose with no practical value.

6. The term third-party obligor's agent should be further explained. Specifically, is it possible for the issuer to also serve as the third-party obligor's agent? Or, does the fact that the issuer receives the proceeds (even if they are used in a manner that benefits the third-party) prevent such a transaction from qualifying as conduit debt? The resolution to better explain third-party obligor's agent will need to be closely aligned to the resolution and treatment in #2 above, given they are so intertwined.

We believe that clarifying these matters will greatly assist preparers in implementing this statement.

These comments represent the consensus opinion of the Accounting Standards Committee and have been approved by our Board of Directors. Thank you for your consideration and the opportunity to express our points of view.

Very truly yours,

[Signature]

Tamar A. Lewis, Board President
Michigan Government Finance Officers Association