October 4, 2016

David Bean, Director of Research and Technical Activities
Governmental Accounting Standards Board
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Via email: director@gasb.org

Re: Project No. 19-25E

On behalf of the Florida Government Finance Officers Association (FGFOA), I am writing this letter to respond to the Governmental Accounting Standard Board’s (GASB’s) invitation to comment on the exposure draft (ED) related to Project No. 19-25E, Certain Debt Extinguishment Issues.

We understand that the primary objective of this ED is to improve consistency in accounting and financial reporting for certain debt extinguishments. We further understand that this Statement (1) establishes standards of accounting and financial reporting for transactions in which only existing resources are placed in a trust for the purpose of extinguishing debt, (2) amends accounting and financial reporting requirements for prepaid insurance associated with debt that is extinguished and (3) establishes an additional disclosure requirement related to debt that is defeased in substance.

Accounting and Financial Reporting for In-Substance Defeasance of Debt Using Only Existing Resources

We concur with the Board’s conclusion that debt should be treated as defeased when either “existing resources” or new debt proceeds are deposited into the irrevocable trust to purchase essentially risk-free monetary assets, solely for satisfying scheduled payments of both interest and principal of the defeased debt. Previous guidance did not address when “existing resources” were used to defease debt and as long as all of the trust requirements noted above are met, we believe it should not matter if the source of the funding is from newly issued debt or existing resources.

Paragraph 4 of the ED defines what “essentially risk free monetary assets” are and also adds that those trust assets are required to provide cash flows that approximately coincide as to timing and amount with the scheduled interest and principal payments of the defeased debt and goes on to say that securities that are callable would not qualify because there is no assurance that the reinvested funds would provide the yields necessary to meet the required debt service payments.

We concur with this conclusion and believe that it will cause the investment professionals structuring the defeasance to use only securities that approximate the debt service of the refunded debt and therefore eliminate any potential problems of the trust not being able to make all scheduled payments.

We do question, however, if retroactive restatement is required if a previously defeased debt issue was defeased with monetary assets not deemed to be essentially risk-free or not approximately coincide as to timing and amount with the scheduled interest and principal payments of the defeased debt under paragraph 4 of the ED. Would this provision require the re-establishment of previously defeased debt and the related trust investments on the government’s statement of net position if the investments were non-qualifying?
Recognition in Financial Statements Using the Economic Resources Measurement Focus Using Only Existing Resources

We concur that the gain or loss on defeasing debt using only existing resources should be recognized immediately in the resource flows statements prepared using the economic resources measurement focus. This appears to be consistent with guidance in Statement 62 which calls for immediate recognition when cash is used to call debt in an early extinguishment. We would recommend that the final statement perhaps add language to make it clear that this is in contrast to the treatment of the gain or loss treatment when new debt is involved so as to clearly distinguish the two treatments.

Recognition in Financial Statements Using the Current Financial Resources Measurement Focus Using Only Existing Resources

We concur that payment to the escrow agents made from existing resources should be reported as debt service expenditures in the financial statements using the current financial resources measurement focus. This is in contrast to inclusion of such amounts as an Other Financing Use when the payment is made from new bond proceeds. We believe that this difference could be stressed more however in that section of the ED to make it clear to the reader of the difference.

Notes to Financial Statements

We concur with the proposed note disclosures for both defeasance from existing resources or new debt, which appear to be ordinary and do not vary significantly from existing guidance.

Prepaid Insurance Related to Extinguished Debt

We agree that prepaid insurance associated with the refunded debt should be included by definition in the carrying amount of the old debt which clarifies that it would be included in the calculation of gain or loss on refunding as opposed to being expensed at the time of defeasance.

Statement 65 inadvertently removed the authoritative guidance on how to treat prepaid insurance related to refunded debt when it removed the reference to issuance costs from the calculation of the net carrying value of the old debt and the ED now specifically addresses the issue and provides clear guidance.

Effective Date and Transition

We do not concur with or understand why the Board decided to make implementation of the new Standard retroactive and recommend that the changes be applied prospectively, as the costs of retroactive implementation will greatly outweigh any benefits. Retroactive changes could result in prior period adjustments, which will penalize government entities that expensed prepaid insurance related to the old debt after the issuance of Statement 65 or had non-qualifying trust assets which did so based upon existing guidance. We see the prepaid insurance aspect of the Statement as clarification of existing standards, not a new standard or correction of an error. In addition, since many of the affected refunded issues could be two to four years old by the time the standard is implemented, retroactive implementation will not result in reporting any timely information, which makes retroactive implementation less useful.

We would like to thank the GASB for its efforts in preparing the ED and for the opportunity to respond. Feel free to contact me at (352) 753-0421 or Sarah.Koser@DistrictGov.org

Sincerely,

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FGFOA President