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GASB Proposes Guidance for Debt that is Extinguished Early Using Only Existing Resources.

Norwalk, CT, August 29, 2016 — The Governmental Accounting Standards Board (GASB) today proposed guidance that state and local governments would apply when extinguishing debt prior to its maturity. Specifically, the Exposure Draft, *Certain Debt Extinguishment Issues,* proposes guidance for transactions in which only existing resources are placed in a trust for the purpose of extinguishing debt.

Current GASB standards provide guidance on how to account for and report when the proceeds of refunding bonds are placed in a trust for the future repayment of outstanding debt. However, the standards do not apply when only existing resources (in other words, other than bond proceeds) are placed in a trust for the future repayment of outstanding debt. Consequently, governments could account for what is essentially the same transaction in two different ways.

The Exposure Draft proposes uniform accounting and financial reporting guidance for debt that is "defeased in substance," regardless of the source of the resources that are placed in a trust.

"Whether you borrow the money to extinguish the debt or use cash you already have, the treatment ought to be the same because the economic substance of the transaction is the same," said GASB Chair David A. Vaudt. "From a government's perspective, the source of the money that is being used to refund debt should not matter as long as the requirements for in-substance defeasance are met."

In this context, in-substance defeasance refers to a situation in which the debt remains outstanding but sufficient resources—in the form of essentially risk-free monetary assets—have been placed into an irrevocable trust to make payments on the debt when they come due. When debt is defeased in substance, the debt and the resources placed in trust are no longer reported in the financial statements. Governments are required, however, to disclose information in the notes to the financial statements about debt that has been defeased in substance.

The Exposure Draft also proposes guidance relating to prepaid insurance on debt that is extinguished and notes to the financial statements for certain defeased debt. One proposal would require disclosure if a government is not prohibited from subsequently exchanging the essentially risk-free monetary assets in the trust with monetary assets that are not essentially risk-free.

The Exposure Draft is available on the GASB website, www.gasb.org. Stakeholders are encouraged to review and provide comments by October 28, 2016.

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