North Carolina
Office of the State Controller

Financial Reporting Update

GASB 91 Effective for Fiscal Year 2023

May 9, 2022

In May 2019, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 91, *Conduit Debt Obligations* (GASB 91). This statement provides a single method for reporting conduit debt. GASB 91 also addresses arrangements that are often characterized as leases that are associated with conduit debt.

Conduit debt is defined as a debt instrument issued in the name of a government (the issuer) that is for the benefit of a third-party primarily liable for the repayment of the debt instrument (the third-party obligor). Conduit debt obligations are generally tax-exempt. These types of financings allow non-profit organizations and for-profit entities to secure financing at tax-exempt rates.

A conduit debt obligation should have all five of the following characteristics:

- There are at least three parties involved: 1) an issuer, 2) a third-party obligor, and 3) a debt holder or a debt trustee.
- The issuer and the third-party obligor are not within the same financial reporting entity. (If a debt issuer and third-party obligor are within the same financial reporting entity, the debt should be recognized by the issuer).
- The debt obligation is not a parity bond of the issuer. It is also not cross-collateralized with other debt of the issuer.
- The third-party obligor or its agent ultimately receives the proceeds from the debt issuance. The issuer may initially receive the debt proceeds and then pass the proceeds to the third-party obligor through a debt trustee in a relatively short time period.
- The third-party obligor is primarily obligated for the payment of all amounts associated with the debt obligation.

Limited Commitments Associated with Conduit Debt Obligations

All conduit debt obligations involve the issuer making a limited commitment to, at a minimum, maintain the issue's tax-exempt status. Limited commitments may also include facilitating payments from the third-party obligor to the debt holder directly or through an agent. Some issuers extend additional or voluntary commitments of its own resources to support debt service payments in the event the third-party obligor is unable to do so.

In most cases, an issuer's commitment is limited under conduit debt obligations. In a limited commitment the issuer assumes no responsibility for the debt service payments beyond the resources provided by the third-party obligor. Under a limited commitment agreement, the issuer should not recognize a conduit debt obligation as a liability and is not required to perform an annual evaluation to determine whether recognition criteria have been met.

Additional Commitments Associated with Conduit Debt Obligations

An issuer can extend an additional commitment of its resources. Under the additional commitment the issuer agrees to support the debt service payments in the event the third-party obligor is or will be unable to do so. Examples of additional commitments include, but are not limited to:

- extending a moral obligation pledge,
- extending an appropriation pledge,
- extending a financial guarantee, or
- pledging its own property, revenue or other assets as security.

As long as the conduit debt obligation is outstanding, the issuer of additional commitments should evaluate at least annually the likelihood that it will pay on that commitment. If certain recognition criteria are met, a liability will be recognized. See the Recognition and Measurement sections below for liability recognition criteria and measurement guidance.

Voluntary Commitments Associated with Conduit Debt Obligations

An issuer can make a voluntary commitment. This is the case when an issuer does not make an additional commitment but on a voluntary basis decides to make a debt service payment or request an appropriation for debt service payment in the event the third-party is, or will be, unable to do so.

When an event or circumstance occurs that causes the issuer in a limited commitment agreement to consider supporting debt service payments for the conduit debt obligations, the issuer should evaluate the likelihood that it will make a debt service payment due to a voluntary commitment. If certain recognition criteria are met, a liability will be recognized. See the Recognition and Measurement sections below for liability recognition criteria and measurement guidance. If a liability is recognized, the issuer should reevaluate at least annually in subsequent years whether the recognition criteria continue to be met for that debt issue only.

Recognition and Measurement in Financial Statements Prepared Using Economic Resources Measurement Focus (Government Wide, Proprietary Funds (Enterprise Funds, Internal Service Funds, Component Units such as Universities and Community Colleges), and Fiduciary Funds)

An issuer of conduit debt agreements with additional commitments to support debt service payments should recognize a liability and an expense in the financial statements if qualitative factors indicate that it is more likely than not (likelihood of more than 50 percent) that the issuer will support one or more debt service payments. The qualitative factors include, but are not limited to, the following:

- A third-party obligor initiating the process of entering into bankruptcy or financial reorganization.
- A third-party obligor breaching a debt contract in relation to conduit debt obligation.
- A third-party obligor experiencing significant financial difficulty.
- Termination of the project that was the source of funding for the debt service payments.
- Litigation that would negatively affect the project.

- The issuer's concern that its access to capital markets could be affected by a third-party obligor's default on outstanding conduit debt obligation.
- The issuer's history of fulfilling its additional commitments to support debt service payments for other conduit debt obligations, including voluntarily supporting debt service payments.
- The issuer's ability or willingness to support debt service payments.

When an event or circumstance has occurred as described in the voluntary commitments section above, the issuer should recognize the liability associated with a voluntary commitment to support debt service payments and an expense in the financial statements if the qualitative factors listed above and in paragraph 13 of GASB 91 indicate that it is more likely than not (likelihood of more than 50 percent) the issuer will support one or more debt service payments for conduit debt obligations.

Issuers should measure the liability and the expenses as the discounted present value of the best estimate of future outflows expected to be incurred. If there is no best estimate for future outflows expected to be incurred, but only a range can be estimated and no amount within that range is a better estimate than any other, the discounted present value of the minimum amount of that range should be recognized.

Recognition and Measurement in Financial Statements Prepared Using the Current Financial Resources Measurement Focus (Governmental Funds – General Fund, Special Revenue Funds, Capital Projects Funds, and Permanent Funds)

If the qualitative factors listed above and in paragraph 13 of GASB 91 indicate that it is more likely than not (likelihood of more than 50 percent) that the issuer will support debt service payments associated with additional commitments or after an event or circumstance has occurred, the issuer will support one or more debt service payments through a voluntary commitment, the issuer should recognize a fund liability and an expenditure to the extent that the liability is normally expected to be liquidated with expendable available financial resources. A fund liability is normally expected to be liquidated with expendable available financial resources when a payment to support conduit debt obligations is due and payable.

Arrangements Associated with Conduit Debt Obligations

The statement addresses arrangements associated with conduit debt obligations where capital assets are constructed or acquired and used by third-party obligors. The arrangements have all of the following attributes:

- The construction or acquisition of the capital asset is financed with proceeds from the conduit debt obligation.
- The issuer retains title to the capital asset from the beginning of the arrangement.
- The payments from the third-party obligor are to cover the debt service payments.
- The payment schedule of the arrangement coincides with the debt service repayment schedule.

Issuers should not report these arrangements as leases. If an arrangement associated with a conduit debt obligation meets the definition of a service concession arrangement, the issuer should account for the service concession arrangement by applying paragraphs 8-12 of Statement 60.

Generally, arrangements associated with conduit debt obligations, other than service concession arrangements, can be classified in one of the following three categories:

1) The issuer relinquishes title to the capital asset at the end of the arrangement at which time the conduit debt has generally been paid off.
2) The issuer does not relinquish the title to the capital asset. The third-party obligor has exclusive use of the entire capital asset until the end of the arrangement.
3) The issuer does not relinquish title to the capital asset. The third-party obligor has exclusive use of only portions of the capital asset until the end of the arrangement.

When the issuer relinquishes title to the capital asset at the end of the arrangement, the issuer should not recognize a liability for the conduit debt obligation, the capital asset, or receivable for the payments related to the arrangement.

When the issuer retains title and the third-party obligor has exclusive use of the entire capital asset, the issuer should not recognize a liability for the conduit debt obligation, the capital asset, or a receivable for the payments related to the arrangement. When the arrangement ends, the issuer should recognize the capital asset at acquisition value in accordance with Statement 72, paragraph 79, and an inflow of resources.

When the issuer retains title and the third-party obligor has exclusive use of portions of the capital asset, the issuer should recognize the entire capital asset, rather than portions, at acquisition value and a deferred inflow of resources for the same amount at the inception of the arrangement. The issuer should not recognize either a liability or a receivable for the payments related to the arrangement. The deferred inflows of resources should be reduced, and an inflow of resources should be recognized in a systematic and rational manner over the term of the arrangement.

Disclosures

This statement requires issuers to disclose general information about their conduit debt obligations:

- General description of the issuer’s conduit debt obligations.
- General description of the issuer’s limited commitments.
- General description of the issuer’s voluntary commitments.
- General description of the issuer’s additional commitments which include:
    - The legal authority and limits for extending commitments.
    - The length of time of the commitments.
    - Arrangements, if any, for recovering payments from the third-party obligor.
- The aggregate outstanding principal amount of all conduit debt obligations that share the same type of commitments.

If an issuer has recognized a liability, it should disclose the following:

- Brief description of the timing of recognition and measurement of the liability and information about the changes in the recognized liability, including the following:

  - Beginning-of-period balances
  - Increases
  - Decreases
  - End-of-period balances
- Cumulative amounts of payments made on the recognized liability at the reporting date, if any
- Amounts expected to be recovered from those payments, if any.

To gain additional understanding of GASB 91, please refer to GASB Pronouncements from which you can access a PDF file of GASB 91 as well as other GASB pronouncements.

Thank you for your time and attention to this important change. OSC will continue to provide updates as the standard is implemented. Questions regarding this specific update should be directed to Joy Darden at Joy.Darden@osc.nc.gov.