General Obligation Bonds

Missouri
DEPARTMENT OF ELEMENTARY & SECONDARY
EDUCATION

Bond Transactions

A school district may issue bonds for a variety of purposes as outlined in Section 164.121, RSMo. A school may issue original (new) bonds or refund (refinance) existing bonds. While school district officials are not expected to know all of the intricacies of issuing bonds, they should attempt to educate themselves and their local boards on the basics concepts and procedures involved in issuing bonds, the professional services that will be necessary, the various costs to be incurred, and the structuring of the initial repayment schedule. Districts are encouraged to evaluate the costs of professional services when issuing bonds and to bid out such services when practical. Segregating the services of the underwriter, financial advisor, and purchaser of the bonds helps to ensure the district is obtaining the best possible deal.

Districts must also remember the correct placement of bond proceeds and the correct fund from which issuance costs may be paid, as outlined in this section.

Repayment Schedule Considerations

Increasing or escalating principal payments on a bond issue are common. As growth occurs in the district's assessed valuation, the district can service more bond payments with the same tax levy. Minimizing the fluctuations in the district's tax levy is a wise move in many regards. However, when the repayment schedule for a new bond issue is being established, school officials should evaluate the repayment structure. If a district is trying to blend the new bond payments in with the payments on prior bond issues, it may be appropriate not to have principal payments on the new issue for several years. However, if the district does not have other bond issues outstanding, reasonable bond principal payments should be made throughout the life of the bonds to minimize the overall costs to the taxpayers. A bond repayment schedule that provides for minimal principal payments in the early years and larger payments near the end, is costlier to the taxpayers and almost guarantees that a refunding will be recommended a few years after the initial issuance (for which the district will incur additional costs). In many cases, the refunding results in the repayment schedule being shortened by a year or two and the principal payments being moved up on the repayment schedule. This can give the appearance that the district is saving a lot of money by completing the refunding. However, if the bonds had been structured in a different manner initially, the refunding may not have been necessary. As discussed later in this accounting manual section, school districts are encouraged to review the net present value of a bond refunding prior to completing such a transaction.

New Bond Issues

Proceeds are <u>always placed in the Capital Projects Fund</u> since this is the fund from which all planned capital expenditures will be made. **Issuance costs are typically paid from the <u>Capital Projects Fund</u> where the bond proceeds have been placed but may, at the discretion of the district, be paid from the <u>General (Incidental) Fund</u>.** It is not appropriate, however, to place a portion of the bond proceeds in the General (Incidental) Fund to pay the costs of issuance. All bond proceeds are to be placed in the Capital Projects Fund per Section 165.011.1, RSMo. Typical issuance costs include bond attorney costs, financial advisor fees, underwriter fees, bond rating fees, SAO registration fees, bond printing costs, and other costs associated with issuing the bonds. (NOTE: Paying agent fees are paid from the Debt Service Fund. Paying agent fees are fees charged by the financial institution responsible for making the payments of principal and interest on the district's outstanding bonds.)

Arbitrage

A factor in many bond issues is the concept of arbitrage (positive or negative depending on current bond market conditions). <u>Positive arbitrage</u> (generally just referred to as arbitrage) results when bond proceeds are invested in investments yielding higher returns than the yield on the tax-exempt bonds. Excess earnings are subject to being rebated to the federal government at certain intervals over the life of the bond issue. Several rebate exceptions exist. These include the small issuer exception, the eighteen-month spending exception, and the twenty-four month construction spending exception. Negative arbitrage is the reverse of arbitrage in that the bond proceeds investments are not producing a higher yield than the tax-exempt bonds. In some instances, the district must add monies to the escrow account to fully fund the requirements on the refunded bonds. If arbitrage (positive or negative) is noted in the rebate computations, the district should work with their bond advisors and independent auditor to make sure the arbitrage has been appropriately reported and accounted for.

Bonds Sold at a Premium

Questions arise periodically on the proper way for school districts to account for a premium generated on the sale of general obligation bonds. There is not a consensus of opinion on the proper recording of these monies as they relate to new money issues. The following discussion is intended to outline the opposing views and to show that bond premiums and bond discounts must be handled similarly.

The Department's view is that both premiums and discounts on bonds sold are interest adjustments and are to be accounted for in the Debt Service Fund. A premium results when bonds are issued at an interest rate higher than the current market rate. Thus, the taxpayers will pay more over the life of the bonds to retire them and it seems appropriate to place the premium in the Debt Service Fund to offset the future interest expenses on the bonds. Likewise, when bonds are sold at a discount, the Debt Service Fund accounts for the discount and the full par amount of the bonds are accounted for in the Capital Projects Fund.

Another view is that premiums represent additional "bond proceeds" which are statutorily required to be placed in the Capital Projects Fund. Section 165.011, RSMo, states in part "…All money received from … the sale of bonds other than refunding bonds shall be placed to the credit of the capital projects fund…." If bond premiums are considered additional bond proceeds, then bond discounts would have to be accounted for as a reduction to bond proceeds and handled in a similar manner. If bonds were sold at a discount, then the Capital Projects Fund would only receive the lower bond proceeds and the project for which the bonds were issued would have to be completed based on the lower proceeds.

The entries in this accounting manual are based on the Department's view that the most appropriate and fair (to the taxpayers) method of accounting for bond premiums and discounts is to treat them as future interest adjustments and account for them in the Debt Service Fund. Districts desiring to handle premiums and discounts in a different manner may wish discuss the issue with the district's auditor.

Refunding Bond Issues

Proceeds are actually placed in an escrow account but are accounted for in the Debt Service Fund from which expenditures to pay off existing debt will be made. Issuance costs may be paid from the General (Incidental) Fund or from refunding bond proceeds from the Debt Service Fund per Section 108.140, RSMo. Typical issuance costs include bond attorney costs, financial advisor fees, underwriter fees, bond rating fees, SAO registration fees, bond printing costs, and other costs associated with issuing the bonds. (NOTE: Paying agent fees are paid from the Debt Service Fund. Paying agent fees are fees charged by the financial institution responsible for making the payments of principal and interest on the district's outstanding bonds.)

Journal Entries

The journal entries associated with either type of bond issue are complex. Further complicating the issue of bonds is a combined issuance where a district issues new bonds along with a refunding of existing bonds. In this case, care must be taken to ensure the proper entries are made for each transaction individually. Section "A" below provides a series of entries typically used to record a new issue of bonds. Section "B" provides a series of entries typically used to record various types of bond refundings.

Section A - Issuance of New Bonds

The following transactions address a typical new issue scenario, but may not address every situation encountered. If questions arise, the district auditor may be a valuable resource in resolving a journal entry question.

Assumptions:

New Bonds Issued	$18,000,000.00
Discount on Bonds Sold*	$133,768.90
Premium on Bonds Sold*	$159,591.65
Accrued Interest	$2,744.30
Costs of Issuance	$259.257.02

* There will not always be a discount and a premium. Most issues have neither. Some have either a discount or premium. This example has both a premium and a discount.

ASBR Transactions for a New Bond Issue

Part II - Revenue Summary in the **Capital Projects Fund:**

5611	Sale of Bonds	$18,000,000.00

Part II - Revenue Summary in the **Debt Service Fund:**

5141	Earnings on Investments ($2,744.30 + $159,591.65)	$162,335.95

Part III - Expenditures (for Bond Issuance Costs)

If these costs are not capitalized, they may be paid from either the **Capital Projects Fund** or the **General (Incidental) Fund** and are recorded as:

5311-6631	Other (Fin. Fees, Etc.)	$259,257.02

If these costs are capitalized as part of the building project, they are paid from the **Capital Projects Fund** and recorded as:

4051-6521	Facilities Acquisition and Construction	$259,257.02

Part III - Expenditures in the **Debt Service Fund:**

5221-6621	Interest	$133,768.90

Part IV, Long and Short Term Debt

8001	Balance, Beginning of Year	$0.00
8002	Amount Borrowed During Year	$18,000,000.00
8003	Amount Repaid During Year	* $0.00
8004	Balance, End of Year	* $18,000,000.00
8005	Interest Paid During Year	* $0.00

*These may be different if the new bonds require a payment during the fiscal year in which the bonds are issued.

Detail of Part I, 3412, Restricted Fund Balance By Fund:

1004	Bond Proceeds (Capital Projects Fund)	$18,000,000.00

This represents the unspent bond proceeds at the end of the fiscal year (the example assumes total proceeds are unspent at the end of the fiscal year). These funds are restricted for the purposes for which the bonds were issued.

Example 1 - New Bonds Sold at Par, Premium, or Discount when there are Sufficient Funds in the Debt Service Fund

Entries to record the issuance of the bonds:

Date	General Long-Term Debt Account Group Entry	A/C No.	Debit	Credit
7/1/xx	Amount to be Provided for Payment of Bonds	1611	$18,000,000.00	
	Amount Available for Payment of Accrued Interest	1631	$2,744.30	
	Bonds Payable	2711		$18,000,000.00
	Accrued Bond Interest Payable	2142		$2,744.30

The Amount to be Provided for Payment of Bonds (GL 1611) and Bonds Payable (GL 2711) accounts will be reduced by the amount of principal paid on the payment date, through a reversing entry. The amount available for Payment of Accrued Interest (GL 1630) and Accrued Bond Interest Payable (GL 2142) will be reversed at the time of the first interest payment subsequent to the bond issuance.

General Journal entries to record the issuance of the bonds (if there are not sufficient funds in the Debt Service Fund to cover the discount, see Example 2):

Date	Capital Projects Fund Entry	A/C No.	Debit	Credit
7/1/xx	Cash in Banks	1111	$18,000,000.00	
	Sale of Bonds	5611		$18,000,000.00

General Journal entries to record the payment of bond issuance costs vary depending on whether these costs are capitalized as part of the building project or not.

If these costs are not capitalized, the entry is:

Date	Capital Projects Fund or General (Incidental) Fund Entry	A/C No.	Debit	Credit
7/1/xx	Fees - Bonded Indebtedness	5311-6631	$259,257.02	
	Cash in Banks	1111		$259,257.02

If these costs are capitalized, the entry is:

Date	Capital Projects Fund	A/C No.	Debit	Credit
7/1/xx	Architecture, Engineering, and Legal Services/Buildings	4031-6521	$259,257.02	
	Cash in Banks	1111		$259,257.02

General Journal entries to record the amount of monies received for accrued interest upon issuance of the bonds:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
7/1/xx	Cash in Banks	1111	$2,744.30	
	Accrued Interest on Bonds Sold	5142		$2,744.30

General Journal entries to record the bond premium:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
7/1/xx	Cash in Banks	1111	$159,591.65	
	Premium on Bonds Sold	5143		$159,591.65

General Journal entries to record the bond discount. (If there are not sufficient funds in the Debt Service Fund, see Example 2.):

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
7/1/xx	Discount on Bonds Sold - Interest Adjustment	5241-6624	$133,768.90	
	Cash in Banks	1111		$133,768.90

Example 2 - New Bonds Sold at a Discount when there are not Sufficient Funds in the Debt Service Fund to Cover the Discount

(All entries are the same as Example 1, except the following two)

General Journal entries to record the issuance of the bonds:

Date	Capital Projects Fund Entry	A/C No.	Debit	Credit
7/1/xx	Cash in Banks	1111	$17,866,231.10	
	Due from Debt Service Fund	1296	$133,768.90	
	Sale of Bonds	5611		$18,000,000.00

General Journal entries to record the bond discount:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
7/1/xx	Discount on Bonds Sold - Interest Adjustment	5241-6624	$133,768.90	
	Due to Capital Projects Fund	2187		$133,768.90

When the district receives tax revenue and can reimburse the Capital Projects Fund for the amount of the discount, the following transactions need to be made:

General Journal entries to reduce the amount that is due from the Debt Service Fund:

Date	Capital Projects Fund Entry	A/C No.	Debit	Credit
7/1/xx	Cash in Banks	1111	$133,768.90	
	Due from Debt Service Fund	1296		$133,768.90

General Journal entries reduce the amount that is due to the Capital Projects Fund:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
7/1/xx	Due to Capital Projects Fund	2187	$133,768.90	
	Cash in Banks	1111		$133,768.90

Recording Annual Principal and Semi-Annual Interest Payments

General Journal entries to record the payment of principal and interest:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
3/1/xx	Principal - Bonded Indebtedness	5111-6611	$500,000	
	Interest - Bonded Indebtedness	5211-6621	$412,200	
	Cash in Banks	1111		$912,200

Date	General Long-Term Debt Account Group Entry	A/C No.	Debit	Credit
3/1/xx	Bonds Payable	2711	$500,000	
	Amount to be Provided for Payment of Bonds	1611		$500,000

Recording a Call Premium

When bonds are issued, the bond transcript will specify whether or not the bonds may be called in for early redemption, and whether a premium must be paid to exercise the call option. Such premium will be expressed as a percentage of par.

Assumptions:

Principal Remaining at Call Date	$12,000,000.00
Premium on Bonds Called*	$240,000.00
Accrued Interest at Call Date**	$330,000.00

* Bonds were called at 102% of principal balance remaining.
** Bond interest accrued at 5.5% paid semiannually. Bonds were called on payment date.

General Journal entries to record the payment of a called bond with a premium:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
3/1/xx	Principal - Bonded Indebtedness	5111-6611	$12,000,000.00	
	Interest - Bonded Indebtedness	5211-6621	$330,000.00	
	Fees - Bonded Indebtedness (Call Premium on Bond)	5311-6631	$240,000.00	
	Cash in Banks	1111		$12,570,000.00

Section B - Issuance of Refunding Bonds

There are two types of debt refundings: current refundings and advanced refundings.

Current Refundings

The old bond issue is callable within 90 days of the issuance of the new issue and the proceeds of the new issue are used immediately to repay the old issue.

Advance Refundings

The old bond issue is not callable within 90 days of the issuance of the new issue. Advance refundings are further identified as either **defeased** or **crossover**.

Defeased

The proceeds of the new issue are placed in an escrow account and used to pay the entire portion of the old issue being refunded (principal and interest) up to and including the call date. This results in a defeasance of the portion of the debt being refunded as the old issue becomes the responsibility of the escrow account trustee and the district begins paying on the new issue immediately. Therefore, the portion of the old issue that is defeased is removed from the district-wide financial statements, if reported, and the money in the escrow account is not reflected in the district's financial statements. In some cases, the district may have to add additional monies to the escrow account from the Debt Service Fund in order for the escrow account to be able to satisfy all of the payments on the old issue. Often, the purpose of this type of refunding is to restructure the district's debt payments.

Crossover

The proceeds of the new issue are placed in an escrow account. However, unlike defeased bonds, the escrow account pays only the interest payments on the new issue and the district continues to make all of the payments on the old issue until the optional call date of the old bonds. This date is often referred to as the crossover date. Under this type of refunding, the payments to be made by the district will not change until the crossover date. From the date of the refunding to the crossover date, the district will continue making the payments on the old bonds. The old bonds will remain on the district's books because these bonds have not been defeased. Consequently, both the new issue and the old issue will be reported in the district's financial records until the crossover date. At the crossover date, the old bonds become callable, which means the old issue is defeased and removed from the district's financial statements. The district then begins making payments on the new issue. The district will record the refunding bonds (new issue) as a liability or increase in bonds outstanding. The securities purchased or assets acquired from the bond proceeds (escrow account) will be recorded as an increase in the district's Debt Service Fund with the escrow amount shown as "restricted". Therefore, there is no net increase in total debt outstanding as the escrow account assets offset the increased liability of the refunding bonds. The ultimate effect of a crossover refunding is to reduce the bond payments (cash flow requirements) from the crossover date to the final maturity of the old issue.

Differences in Advanced Refundings:

	Defeasance	Crossover
The district:	Immediately begins making all payments that are required for the new issue.	Continues to pay all required payments of the old bonds until the crossover date. At the crossover date the district begins making payments on the new issue.
The escrow account:	Is fully funded so that it can make all required payments of the old issue.	Pays the interest payments on the new issue until the crossover date. At the crossover date the balance in the escrow account pays off the old bonds.
The debt of the district includes:	Only the new bonds. The old bonds are completely written off the district's books.	Both the new and the old bonds until the old bonds are paid off on the crossover date.
Accrued interest is sent to:	The district.	The escrow account.

The following examples may not exactly correspond with the documents the district receives during the bond issuance. Some bond underwriters net the costs of issuance against the bond proceeds and send a check (wire transfer) for the net difference. The following information shows what the district needs to report on the ASBR.

Paying agent fees, fees charged by the financial institution responsible for making the payments of principal and interest on the district's outstanding bonds, are paid from the Debt Service Fund. Other fees such as the bond attorney costs, costs of bond sales, registration fees, bond printing, and other costs associated with issuing bonds may be paid from the General (Incidental) Fund or from refunding bond proceeds from the Debt Service Fund per Section 108.140, RSMo.

Current or Defeased Refunding of Bonds

Assumptions:

New Issue	$3,090,000.00
Old Issue Balance	$3,100,000.00
Amount of District Contribution	$400,700.63
Accrued Interest (Paid to the District on Defeased Issues)	$10,493.12
Cost of Issuance	$61,800.00

Two wire transfers occur on the settlement date:

- Accrued interest is sent to the district in the amount of $10,493.12.
- Net proceeds from the new issue are sent to the escrow account (new issue minus costs of issuance) in the amount of $3,028,200.00.

The district then sends a check to the escrow account to fully defease the old issue:

$ 61,800.00	Costs of Issuance (from General Fund or Debt Service Fund)[1]
+ 10,000.00	Principal Difference in the Old and New Issues (From Debt Service Fund)
+ 328,900.63	Future Interest Payments (From Debt Service Fund)[2]
$ 400,700.63	Total District Contribution

ASBR Transactions for Current or Defeased Refunding Bonds

Part II - Revenue Summary in the **Debt Service Fund:**

5691	Refunding Bonds	3,090,000.00
5141	Earnings on Investments	10,493.12

Part III - B - Expenditures

5111-6611	Principal	$3,100,000.00
5211-6621	Interest	[1] $328,900.63
5311-6631	Other (Fin. Fees, Etc.)	[2] $61,800.00

Part IV, Long and Short Term Debt - General Obligation Bonds

8001	Balance, Beginning of Year	$3,100,000.00
8002	Amount Borrowed During Year	$3,090,000.00
8003	Amount Repaid During Year	$3,100,000.00
8004	Balance, End of Year	$3,090,000.00
8005	Interest Paid During Year	$328,900.63

The defeased bonds are no longer on the district's books. Line 8003 shows that the refunded bonds (old bonds) have been paid. The money in the escrow account is not listed in fund balances.

[2] Calculation of 5210 - 6621 Interest

New Issue	$3,090,000.00
Cost of Issuance	$61,800.00
Net Amount Received from New Issue	$3,028,200.00
Plus Amount of District Contribution	$400,700.63
Minus Old Issue	($3,100,000.00)
Interest Expense	$328,900.63

[1] Expenditures for paying agent fees are paid for from the Debt Service Fund. Other fees such as bond attorney costs, financial advisor fees, underwriter fees, bond rating fees, SAO registration fees, bond printing, and other costs associated with issuing bonds may be paid from the **General (Incidental) Fund** or from refunding bond proceeds from the **Debt Service Fund** per Section 108.140, RSMo if the bond transaction is a refunding of existing bonds.

Current or Defeased Refunding of Bonds - Journal Entries

Entries to record the issuance of the new bonds:

Date	General Long Term Debt Account Group Entry	A/C No.	Debit	Credit
8/1/xx	Amount to be Provided for Payment of Bond Principal	1611	$3,090,000.00	
	Amount Available for Payment of Accrued Interest	1631	$10,493.12	
	Bonds Payable	2711		$3,090,000.00
	Accrued Bond Interest Payable	2142		$10,493.12

The Amount to be Provided for Payment of Bonds (GL 1611) and Bonds Payable (GL 2711) accounts will be reduced by the amount of principal paid on the payment date, through a reversing entry. The amount available for Payment of Accrued Interest (GL 1630) and Accrued Bond Interest Payable (GL 2142) will be reversed at the time of the first interest payment subsequent to the bond issuance.

When recording entries to an Escrow Cash Account please make sure to use an extension so all entries and crossover balance may remain in its own account and not interfere with an existing Escrow Cash account.

General Journal entries to record the amount of monies received for accrued interest upon issuance of the bonds:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/1/xx	Escrow Cash	1151	$10,493.12	
	Accrued Interest on Bonds Sold	5142		$10,493.12

General Journal entries to record the issuance of the bonds:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/1/xx	Escrow Cash	1151	$3,090,000.00	
	Refunding Bonds	5692		$3,090,000.00

General Journal entries to record the district contribution to the escrow account that is required to fund the future interest payments to fully defease the old bond issue:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/1/xx	Escrow Cash	1151	$328,900.63	
	Cash	1111		$328,900.63

General Journal entries to record the payment of bond issuance costs:

Date	General (Incidental) Fund Entry	A/C No.	Debit	Credit
8/1/xx	Fees - Bonded Indebtedness	5311-6631	$61,800.00	
	Cash	1111		$61,800.00

or

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/1/xx	Fees - Bonded Indebtedness	5311-6631	$61,800.00	
	Escrow Cash	1151		$61,800.00

General Journal entries to record the payment of principal on the refunded bond issue:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/1/xx	Principal - Bonded Indebtedness	5111-6611	$3,100,000.00	
	Escrow Cash	1151		$3,100,000.00

Date	General Long-Term Debt Account Group Entry	A/C No.	Debit	Credit
8/1/xx	Bonds Payable	2711	$3,100,000.00	
	Amount to be Provided for Payment of Bonds	1611		$3,100,000.00

Crossover Refunding of Bonds

When a crossover refunding occurs, the district continues to make the bond principal and interest payments on the old issue and the escrow account pays the interest on the new issue until the crossover date. Therefore, it is necessary in this example to reflect two separate types of transactions - issuance of the refunding bonds and payments made on the old issue. The majority of crossover refundings are partial refundings of old bonds rather than a refunding of the full issue.

Assumptions:

First Transaction:

New Issue	$1,690,000.00
Balance Outstanding on Old Issue (Including Callable Bonds of $1,690,000.00)	$2,500,000.00
Accrued Interest (Paid to Escrow Account on Crossover Issues)	$2,572.01
Cost of Issuance	$33,800.00

There may be some instances where the district would need to add additional monies to the escrow account from the Debt Service Fund to make sure the escrow account can fully pay interest payments as they come due. Please consult with School Finance and your bond counsel if this should happen.

Second Transaction:

Current Year Payment on Old Issue	$70,000.00
Interest Payment on Old Issue	$111,155.00

ASBR Reporting for Crossover Refunding of Bonds - First Transaction

Part I - Detail of Part I, 3412, Restricted Fund Balance of Debt Service Fund

1005	Escrow Amount for Crossover Refunding	$1,692,572.01

Part II - Revenue Summary in the **Debt Service Fund**

5692	Refunding Bonds	$1,690,000.00
5141	Earnings on Investments	$2,572.01

Part III - Expenditures

5311-6631	Other (Fin. Fees, Etc.) (see footnote below)	$33,800.00

ASBR Reporting for Crossover Refunding of Bonds - Second Transaction

Part I, Restricted Fund Balance By Fund

1005	Escrow Amount for Crossover Refunding (Debt Service Fund)	$1,692,572.01

Part III-B-Expenditures

5110-6611	Principal - Bonded Indebtedness	$70,000.00
5210-6621	Interest - Bonded Indebtedness	$111,155.00

The two transactions together should appear as follows:

Part IV, Long and Short Term Debt - General Obligation Bonds

8001	Balance, Beginning of Year	$2,500,000.00
8002	Amount Borrowed During Year	$1,690,000.00
8003	Amount Repaid During Year	$70,000.00
8004	Balance, End of Year	$4,120,000.00
8005	Interest Paid During Year	$111,155.00

Escrow Account Interest Income and Interest Expense

The money in the escrow account will earn the same interest rate being charged for the bonds. The escrow account will receive interest income equal to interest expense for the bonds. This transaction should be reported on the ASBR as follows:

Part II - Revenue Summary in the **Debt Service Fund**

5141	Earnings on Investments	$84,500.00

Part III B - Expenditures

5211-6621	Interest - Bonded Indebtedness	$84,500.00

Crossover Refunding of Bonds - Journal Entries

Entries to record the new bond issue:

Date	General Long-Term Debt Account Group Entry	A/C No.	Debit	Credit
7/1/xx	Amount to be Provided for Payment of Bonds	1611	$1,690,000.00	
	Amount Available for Payment of Accrued Interest	1631	$2,572.01	
	Bonds Payable	2711		$1,690,000.00
	Accrued Bond Interest Payable	2142		$2,572.01

The Amount to be Provided for Payment of Bonds (GL 1611) and Bonds Payable (GL 2711) accounts will be reduced by the amount of principal paid on the payment date, through a reversing entry. The amount available for Payment of Accrued Interest (GL 1630) and Accrued Bond Interest Payable (GL 2142) will be reversed at the time of the first interest payment subsequent to the bond issuance.

When recording entries to an Escrow Cash Account please make sure to use an extension so all entries and crossover balance may remain in its own account and not interfere with an existing Escrow Cash account.

General Journal entries to record the amount of monies received for accrued interest upon issuance of the bonds:

		A/C No.	Debit	Credit
	Escrowed Cash	1151	$2,572.01	
	Accrued Interest on Bonds Sold	5142		$2,572.01

General Journal entries to record the initial issuance of the refunding of the bonds:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
7/1/xx	Escrowed Cash	1151	$1,690,000.00	
	Refunding Bonds	5692		$1,690,000.00

General Journal entries to record the payment of bond issuance costs:

Date	General (Incidental) Fund Entry	A/C No.	Debit	Credit
8/1/xx	Fees - Bonded Indebtedness	5311-6631	$61,800.00	
	Cash	1111		$61,800.00

or

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/1/xx	Fees - Bonded Indebtedness	5311-6631	$61,800.00	
	Escrow Cash	1151		$61,800.00

General Journal entries to record the earnings on escrow account:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/30/xx	Escrow Cash	1151	$84,500.00	
	Earnings From Temporary Deposits	5141		$84,500.00

General Journal entries to record the payment of interest on new bond issue (until crossover date):

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
8/30/xx	Interest - Bonded Indebtedness	5211-6621	$84,500.00	
	Escrow Cash	1151		$84,500.00

General Journal entries to record the payment of the refunded bond issue at the crossover date:

Date	Debt Service Fund Entry	A/C No.	Debit	Credit
3/1/xx	Principal - Bonded Indebtedness	5111-6611	$2,500,000.00	
	Escrow Cash	1151		$2,500,000.00

Date	General Long-Term Debt Account Group Entry	A/C No.	Debit	Credit
3/1/xx	Bonds Payable	2711	$2,500,000.00	
	Amount to be Provided for Payment of Bonds	1611		$2,500,000.00

Refinancing of Bonds and/or Lease Purchases

Districts may refinance existing debt for several reasons: saving money, restructuring the repayment schedule or removing restrictive bond covenants. However, a district attempting to save money by refinancing debt must look beyond the reported gross savings over the life of the debt. Particularly, the district needs to know what the reported gross savings over the term of the debt are in present day dollars, because the actual value of money decreases over time. This concept is referred to as "net present value".

The net present value of gross savings for any given refinancing of debt should be calculated after all refinancing costs and district cash contributions have been deducted from gross savings in order to evaluate the true economic benefit to the district. Net present value is directly affected by the discount rate used in the calculation. An administrator should ask how the "discount rate" was determined. Discounted net present value is very sensitive to variations in the discount rate used in the calculation. If some standard method of determining the discount rate is not used, the calculation of net present value becomes suspect. The discount rate is typically the "reinvestment bond yield" on the refinancing issue.

A district contemplating a refinancing **to save money** should request data as shown in the example below to determine if there is in fact an economic gain to the district resulting from the refinancing. While some sources would indicate any positive net present value provides an economic gain and should be considered, the Department staff would suggest that a net present value savings of at least 2% (preferably 3-4%) of refunded par value should be the district's goal.

Par Value of Refunded Bonds: $2,900,000
Average Interest Rate (Bond Yield): 4.720070%
Discount Rate Used to Calculate Net Present Value: 4.72%

Calculation of Savings	**Gross Savings**	**Net Present Value**
Gross Savings	$324,637.50	$181,437.35
Less: Costs of Issuance	$(58,000.00)	$(58,000.00)
Less: Add'l Issuer Cash Contribution	$ (9,604.34)	$ (9,604.34)
NET Savings	**$257,033.16**	**$113,833.01**
Net Present Value Savings	$113,833.01	
NPV Savings as % of Par Value Refunded	($113,833.01 ÷ $2,900,000)	3.925%

As shown in the example above, the gross savings on the bond ($324,637.50) is considerable higher than the net present value after all costs and contributions have been accounted for ($113,833.01). The gross savings figure does not reflect the true benefits of the refunding and should not be relied upon in evaluating whether or not the refunding should be undertaken. Districts should ask their bond professionals to provide a table similar to the one shown above in order to evaluate the actual savings to the district.

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