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Memo

To: Management of Memphis Symphony Orchestra, Inc. ("MSO")

From: Watkins Uiberall, PLLC

Date: February 15, 2021

Re: Accounting Treatment of Endowment Funds

Background: In fiscal year 2019, endowment funds were established by multiple donors at the Community Foundation of Greater Memphis ("CFGM") and the University of Memphis Foundation ("UMF") in connection with MSO's the "Future is Now" capital campaign. In fiscal year 2020, an additional fund of $10M was established at CFGM. All such funds established at CFGM and UMF are intended to exclusively benefit MSO and its mission. However, each of the funds are governed by separate agreements which have different conditions of acceptance and therefore, the accounting treatment by MSO is not homogeneous across the funds. This memo will examine the appropriate accounting treatment for each fund.

Relevant Accounting Guidance: As described in the AICPA *Accounting and Auditing Guide for Not-for-Profit Organizations (the "Guide") paragraph 6.20, "FASB ASC 958-30-25 and FASB ASC 958-30-30-11 discuss recognition and initial measurement of irrevocable split-interest agreements for which a third party maintains control of the donor's contributed assets. In a split-interest agreement in which cash or other assets contributed by a donor are held by an independent trustee (such as a charitable trust for which a bank, trust company, foundation, or private individual is the trustee) or by another fiscal agent of the donor or the cash or other assets are otherwise not controlled by the NFP, the NFP should recognize its beneficial interest in those assets. The contribution should be recognized when the NFP is notified of the agreement's existence." "…If, however (as noted in FASB ASC 958-605-25-31), the trustee or fiscal agent has **variance power** to redirect the benefits to another entity or if the NFP's rights to the benefits are conditional, the NFP should NOT recognize its potential for future distributions from the agreement until the NFP has an unconditional right to receive benefits under the agreement."*

Even though MSO's agreements with CFGM and UMF are not considered "split-interest agreements" because MSO is the sole beneficiary of the assets (i.e., they aren't splitting it with anyone else), the accounting and measurement treatment described above still applies to these funds.

Accounting Treatment – CFGM Funds: A donor-designated fund was established at CFGM on February 4, 2019 for the sole benefit of MSO. MSO will receive annual distributions from the fund equal to 5% of the average balances of the fund for the 20 most recent calendar quarters. The fund is intended to support MSO in perpetuity. The conditions of acceptance state, *"…if MSO ceases to be a qualified charitable organization, or if the fund's purpose becomes unnecessary, incapable of fulfillment, or inconsistent with the charitable needs of the community, CFGM may exercise its **variance power** under Article XIII of its Bylaws."*

Conclusion: Since CFGM has variance power to redirect the benefits to another entity and has broad discretion in determining if the fund's purpose is meeting the needs of the community, we believe this agreement is ultimately revocable (conditional) and no contribution should be recorded until cash is actually received from CFGM. Even though no beneficial interest in these assets is recorded, disclosure of the agreement in the financial statements is required.

On July 23, 2019, MSO received notification of another fund of $10M that was established at CFGM for the benefit of MSO. Similar to the 2/4/19 fund described above; this fund also does not appear to be an irrevocable (unconditional) promise to give to MSO. The agreement states, *"the donor has requested that such annual distributions be made as long as MSO maintains its active nonprofit status, continues to perform its mission as publicly stated for the benefit of Memphis and Shelby County, and meets other applicable criteria,* ***if any****, established by CFGM for grant support."* Additionally, the agreement states that CFGM may request additional information in order to receive the annual grant such as reports on financial health, diversity of board and staff, and succession planning, and MSO's satisfaction of these requirements will be determined in the sole judgment of CFGM.

Conclusion: Due to the nature of the conditions listed and the fact that CFGM can establish any other criteria that must be met by MSO, we believe this agreement does not represent an unconditional (irrevocable) right of MSO to receive these assets.

Therefore, no beneficial interest should be recorded for the two CFGM funds described above. Contributions should be recorded only when distributions/grants are received from the funds.

Accounting Treatment – UMF Fund: On December 18, 2018, multiple donors established an endowment fund at UMF for the benefit and use of MSO. All expenditures from the fund require the approval of both the CEO of MSO and the President of the University of Memphis ("U of M"). The intention is for at least 5% of the fund balance to be distributed annually. Unlimited spending of fund earnings and/or fund principal is permitted at any time. In the event the partnership between MSO and U of M is dissolved, the chairman of the MSO board can request in writing that the remainder of the fund be fully distributed to MSO, provided MSO is a 501(c)(3) entity at the time, or fully distributed to another 501(c)(3) entity that the chairman of the MSO board selects and identifies to UMF.

Based on review of the agreement, all decisions regarding the distribution of funds are to be made jointly by a representative of MSO and UMF. None of the language indicates the possession of variance power by UMF, giving them unilateral authority to redirect the assets to another entity.

Conclusion: As such, we believe MSO has an irrevocable right to the assets of the UMF fund and therefore should record its beneficial interest in those assets. Pursuant to FASB ASC 958-605-35-3, annual distributions from the fund are reported as investment income.