July 26, 2015

Ms. Susan M. Cosper
Technical Director
FASB
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

File Reference No. 2015-230

Re: Comments on proposed ASU: Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954) Presentation of Financial Statements of Not-for-Profit Entities

Ms. Cosper:

Dallas Theological Seminary is a private graduate level institution. Founded in 1924, the Seminary has over 2,100 students. Consolidated within our financial statements is our affiliated foundation. My response reflects two perspectives; first, as a preparer, but primarily as a user. Regarding the later, I've participated in the peer review process of our regional accreditor, SACS COC. This includes participation in site-visits teams, special committee visits, and as a finance reader for the Compliance and Review Committee. My focus in this participation has been to assess a school's financial viability and stability.

Overall I'm very pleased with the numerous improvements made throughout the exposure draft. My responses will focus more on concerns rather than my complements.

Sincerely,

Dale Larson
Vice President for Business and Finance/CFO
Dallas Theological Seminary
Response to Questions

**Question 1:** Do you agree that the disclosures about the nature of donor-imposed restrictions and their effects on liquidity in notes to financial statements would help ensure that necessary information is not lost by combining the temporarily and permanently restricted classes of net assets into one donor restricted category for purposes of presentation in the statement of financial position (balance sheet)? If not, please identify the information lost and why it is necessary.

I would agree that information would not be lost if an entity used the illustrated disclosure examples found in paragraph 958-205-55-21. The Note B example was very informative.

It would be helpful to encourage preparers to disclose greater disaggregation on net assets without donor restrictions. Misinterpretation by some that the term unrestricted net assets meant “what's available” is why the name change to net assets without donor restrictions makes sense. This eliminated that confusion but it did little to help give users a better understanding of what unrestricted net assets were available. The exposure draft provides an example disclosure for this net asset class but it is basically unchanged, and a better illustration seems warranted.

For example, distinguish net assets that are readily expendable from those that are not:

1) Available for use,
2) Net investment in plant less related debt and related debt\(^1\),
3) Net assets with limitations set by 3rd parties (not donors), e.g., aggregate state reserve requirements on gift annuities, net bond proceeds limited to property plant and equipment (PP&E), etc.

Disaggregation along these lines should be encouraged and would give users a better picture of what is expendable. Users, e.g., banks, rating agencies, and accreditors, are always searching for the answer to “What are the NFP’s expendable resources?” And the underlying question is whether the NFP can weather an economic storm. And, yes, I understand that current GAAP does not preclude a preparer from presenting this type of information in their notes now. However, from a user’s perspective this isn’t always presented well. It would help if FASB could encourage greater disclosure by improving its illustrated example for disaggregation of net assets without donor restrictions.

**Question 2:** Do you agree that the aggregated amount by which endowment funds are underwater should be classified within net assets with donor restrictions rather than net assets without donor restrictions? If not, why?

I agree, this is a better approach.

**Question 3:** Do you agree that disclosures describing the NFP’s policy on spending from underwater endowment funds, together with the aggregated original gift amount or the amount that is required to be maintained by donor or by law, would provide creditors, donors, and other users with information useful in assessing an NFP’s liquidity and potential constraints on its ability to provide services without imposing undue costs? Why or why not?

I agree. Its usefulness would likely show itself after a severe market downturn.

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\(^1\) Excluding related plant debt is based on the observation that most entities rely on future operating revenues for repayment, not current or existing resources. [Net Investment in Plant (NIP) = PP&E less accum. depreciation, less related debt]
Question 4: Do you agree that providing information in notes to financial statements about financial assets and liabilities and limits on the use of those assets is an effective way to clearly communicate information useful in assessing an NFP’s liquidity and how it manages liquidity without imposing undue costs? If not, why, and what alternative(s) would you suggest?

It does not appear that obtaining information about these assets and liabilities would impose undue costs. For internal purposes we already prepare a balance sheet related to unrestricted net assets only. So the donor-restricted financial assets and liabilities are known, and identifying other limitations should not be too difficult.

How effective this disclosure will be is not clear; it almost seems more like a disclosure experiment. Okay, that might be too harsh of an expression. It is just not apparent that this would provide additional or significantly useful information. The use of entity determined time horizons for managing liquidity seems necessary but that also eliminates the possibility of a useful measure for comparative purposes. Allowing management intent is also necessary, e.g., exclusion of quasi-endowments, but it also opens up the possibility to some degree of manipulation. For example, management or the governing board’s intent for a quasi-endowment could have a dual purpose (i.e., long-term investing and in a pinch an immediate source for meeting liquidity needs). Consequently, some NFPs might include these while others might not. My view is that if we had sufficient information on the composition of the net assets without donor restrictions we probably would not need additional disclosures regarding liquidity.

I want to add that I can’t think of a better alternative, and I am very thankful that a classified balance sheet is not being required.

Question 5: Most business-oriented health care NFPs are required to present a classified balance sheet. Continuing care retirement communities and other NFPs may choose to sequence their assets and liabilities according to their nearness to cash as an alternative to using a classified balance sheet. As a result of the proposed requirement to provide enhanced disclosures of information useful in assessing liquidity, would there no longer be a need to hold business-oriented health care NFPs to the more stringent standard for their balance sheets? If not, why?

No comment.

Question 6: Do you agree that requiring intermediate measures of operations would provide users of NFP financial statements with more relevant and comparable information for purposes of (a) assessing whether the activities of a period have drawn upon, or have contributed to, past or future periods and (b) understanding the relationship of resources used in operations of a period to resource inflows available to fund those operations? Do you also agree that classifying and aggregating information in that way would not require major system changes? If not, why?

I agree that a required measure of operations will help users evaluate NFPs, particularly if the disclosures on transfers are sufficiently robust. See response to question 7.

I do not see any significant system changes being required.

Question 7: Do you agree that intermediate measures of operations should include only those (a) resource inflows and outflows that are from or directed at carrying out an NFP’s purpose for existence and (b) resources that are available for current-period operating activities before and after the effects of internal governing board appropriations, designations, and similar actions? If not, why?
I agree, although I disagree with the view that considers net assets released related to the acquisition of long-lived assets is an inflow that is being made available for operating activities. See response to question 10.

From a user perspective I am concerned about the qualitative nature of the disclosures regarding transfers. The example in 958-225-45-10B includes descriptions of transfers described as “resulting from standing board policies and one-time decisions.” These two categories are not meaningful. They might tell what caused the transfer but a user is more interested in the purpose or objective of the transfer. Descriptions that describe the reason or intent of the transfer are more helpful. Descriptions along these lines would be useful:

- for investing and/or appropriation of certain nonoperating returns,
- for reserves/contingencies,
- for future period operating expense, and
- for future renovation and capital additions.

Using clearer descriptions helps me and other users modify the total operating excess or (deficit) after transfers into a measure that will meet our unique needs. For example, I might add or subtract all transfers from a reserve since doing so will give me a better picture of whether the NFP has a problem with fundamental financial equilibrium.

The purpose and objective for the first operating subtotal is clear, but the second subtotal is less clear. This subtotal does not point out the direction of where the NFP is headed fiscally, although it does show how management funded current period expenses or plans for future expenses. Robust disclosures on transfers will help users determine the NFP’s fiscal direction and develop answers to the following questions:

- Are operating expenses balanced with available resource inflows?
- To what degree have “available” revenues exceeded operating expenses?
- Or as stated in a FASB staff handout should the measure “show how current period expenses relate to the current period revenues/resources that were available when received or became available to support those current period expenses or activities?”

**Question 8:** Do you agree that all internal transfers (governing board appropriations, designations, and similar actions that make resources unavailable or available for operations of the current period) should be reflected on the statement of activities immediately after an intermediate measure of operations before transfers and immediately before an intermediate measure of operations after transfers? If not all internal transfers, on what basis would you distinguish between those transfers that should and not be reflected and how would you make that distinction operable? Do you also agree that reflecting those internal decisions (or lack of them) on the face of the statement rather than in notes will help an NFP communicate how its operations are managed without adding undue complexities? Why or why not?

I agree that internal transfers should be located as proposed (i.e., after an intermediate measure of operations before transfers). The first operating subtotal would then provide useful information. I would prefer an exception to this rule which is to have all endowment related appropriations on true and quasi-endowments included within the first operating subtotal. These inflows persist year in and year out and one could argue these will always be available.

I disagree with some who say we should just not include transfers anywhere in the statement activities. Initially excluding all investing and financing activities as nonoperating will capture much of what users and many preparers currently classify within their nonoperating section. The transfers are absolutely necessary as they add back into the operating section the
resource inflows that fund the business. The primary example is endowment spending appropriations.

Initially, I was concerned that these transfers could be used to create a false picture of profit or loss. I now think that you have included sufficient limitations on these transfers to make that potential problem diminish. Again, the importance of adequate disclosures related to these transfers will help users assess whether something is amiss. See response to question 7.

**Question 9:** Do you agree that to promote comparability, the Board should eliminate one of the two optional methods for reporting expirations of donor restrictions on gifts of cash or other assets to be used to acquire or construct long-lived assets? Do you also agree that requiring the expiration of those donor restrictions on the basis of the placed-in-service approach rather than the current option to present a release from restriction over the useful life of the acquired long-lived asset is most consistent with the underlying notions of the intermediate measures of operations? If not, why?

I agree.

**Question 10:** Do you agree that gifts of, or for, property, plant, and equipment (long-lived assets) should be considered operating revenue and support when received (or when placed in service in the case of a gift to acquire a long-lived asset)? Do you also agree that because the long-lived asset is not immediately fully available to be utilized in the current period, an NFP should be required to present a transfer from operating activities to other activities for the amount of the gifted asset or portion of the asset funded by restricted gifts? If not, why?

I agree that gifts of property without additional donor restrictions should be considered operating resource inflows. It seems that every year the Seminary receives a gift of property (a residence or land) which is typically sold and used for operations or special initiatives.

However, the release of contributions restricted for long-lived assets should **not** go into the operating section first and then be transferred out to nonoperating. The net asset release related to the acquisition of long-lived assets should go directly into the nonoperating section for the following reasons:

- A release into operating does not accurately reflect the reality of the transaction. A donor’s understanding is that the NFP needed a long-lived asset to fulfill its mission. Consequently, they donate funds for its acquisition. If a donor thought that management was going to pause and wonder about whether it would sell or monetize the newly constructed asset they would have never given the gift.
- This capital release into the operating section reduces the usefulness of the first operating subtotal. The first subtotal should reflect all resource inflows that could be available to meet current period operating activities (i.e., expenses). Release inflows related to PP&E were never truly available both from a practical perspective and from the perspective of the donor. Only if you were going out of business would it be appropriate to include in operating.
- An ethical limitation continues even after the accounting and legal restriction disappears. A number of years ago the need for additional parking space resulted in the Seminary asking a donor for a gift to buy property adjacent to campus. The gift was received and the land bought. Years passed and circumstances changed. We received

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2 My initial question was, “How are transfers back into operations being constrained? What criteria exist regarding transfers back into operating?” The answer appears clear in 958-225-45-10A. It was helpful to see these transfers back into operations are described as “certain nonoperating returns or previously transferred amounts…” If there are other types it would be helpful to know.
offers from developers to buy that land. Options opened up where our parking needs could be met without the need of that land. The first thing our president did was to contact that donor to see if they would be okay with our selling the property. My point is that we felt ethically obligated to always fulfill donor intention and never depart from being accountable. The idea that we are conceptually considering monetization of this newly acquired long-lived asset is at odds with this principle.

- The release first into operating creates unnecessary and confusing entries. Readers will ask, “How can one transaction (i.e., a net asset release for PP&E) create four entries on the face of the financial statements?” As I recall John Kroll said, “That journal entry is going to be very tired by the time it’s all done.” These added transfers appear as clutter which reduces readability.
- Confusion and the need to explain this transaction to our audit committee and board will be never ending. For example, if my board heard that I put the release first into operating, then conceptually paused to see if I’d monetize it, they would say that is crazy. It definitely doesn’t sound like I was fulfilling the donor’s intention. They would say I never should have considered this a resource that might be available for current period activities.

Even if the FASB board concludes that, theoretically, the donor funded long-lived asset could have been made available for operating activities (assuming the donor doesn’t file suit), then I’d ask that you make an exception and flow all net asset releases related to acquisition of PP&E directly into the nonoperating section and avoid this confusing sidetrip.

**Question 11:** Do you agree that the addition of required intermediate measures of operations for all NFPs would make unnecessary the need for NFP business-oriented health care entities to also present their currently required performance indicator? Why or why not?

No comment.

**Question 12:** Do you think the flexibility currently allowed by GAAP to present a statement of activities as either a single statement or two articulating statements and to use either a single-column or a multicolumn format should be retained or narrowed? If narrowed, why and in what ways?

I agree that these options and flexibility should be retained.

**Question 13:** Do you agree that reporting operating expenses by both their function and nature together with an analysis of all expenses (other than netted investment expenses) provides relevant and useful information in assessing how an NFP uses its resources and, thus, should be required? Why or why not?

I agree. I think this is an improvement.

**Question 14:** Do you agree that requiring investment income to be reported net of external and direct internal investment expenses will increase comparability and avoid imposing undue costs to obtain information about all investment fees (for example, embedded fees of hedge funds, mutual funds, and funds of funds)? If not, why?

I agree.

**Question 15:** Do you agree that the disclosure of the amount of all investment expenses is unnecessary but that disclosure of internal salaries and benefits that are netted against investment
return is of sufficient relevance, not too costly to obtain, and thus should be required? Why or why not?

I agree that the disclosure of all investment expense is unnecessary.

Net investment return is the most important number. Its components are not. By that I mean knowledge of the specific amounts for 1) dividends and interests, 2) unrealized and realized gains/losses, and 3) investment expense do not, by themselves, give me useful information when assessing an entities prospect for future returns.

Investment assets at the Seminary are not large enough to warrant internal investment staffing so the disclosure of internal salaries and benefits causes me little concern. However, as a user of financial statements I question whether that information is relevant and useful. All it will likely create is a debate at board meetings and the added pressure to outsource certain functions, sometimes a more costly approach. Staffing size can be driven by the complexity of the portfolio. For example, high asset allocations to alternative investments require more staffing for the added monitoring/due diligence. It is expected that excess returns will more than cover this additional cost. The unintended consequences lead me to think this disclosure is not worth the debate it will create.

Question 16: Do you agree that interest expense, whether incurred on short-term or long-term borrowing, and fees and related expenses incurred for access to lines of credit and similar cash management and treasury activities are not directed at carrying out an NFP’s purposes and, thus, should not be classified as operating activities? If not, why?

Most everyone I’ve talked to considers interest expense an operating cost. But for the sake of establishing a principle that keeps other financing activity out of the operating section I’m willing to concede, grudgingly of course. In other words, excluding financing activity from operations becomes the reason items like changes in fair value of debt related swaps are nonoperating, and also the exclusion of gains/losses on restructuring of debt.

Question 17: Do you agree with the following implementation guidance:

a. Equity transfers between NFPs that are under common control and are eliminated in a parent entity’s consolidated financial statements and equity transactions between financially interrelated entities should be presented within operating activities unless they are not available for current-period use in carrying out the purpose for the reporting entity’s existence? If not, why?

No comment.

b. Immediate write-offs of goodwill generally should be presented within operating activities? If not, why?
   Immediate write-offs of acquisitions of noncapitalized items for a permanent collection should be presented within the operating activity section if acquired with net assets without donor restrictions? If not, why?

I agree.

Question 18: Do you agree that the direct method of presenting operating cash flows is more
understandable and useful than the indirect method? Do you also agree that the expected benefits of presenting operating cash flows in that way would justify the one-time and ongoing costs that may be incurred to implement that method of reporting? If not, please explain why and suggest an alternative that might increase the benefits or reduce any operational concerns or costs.

I agree that the direct method is more useful. I’m now considering reporting by natural classification on the statement of activities and this would correlate well with the direct method. I greatly appreciate dropping the reconciliation of cash flows from operations as this will make preparing the statement significantly easier. If I had to do both I’d probably disagree with this question 18 entirely. For small institutions preparation of the cash flow statement is at the end of the audit where time is at a premium. Reducing the time to prepare the statement becomes extremely important.

**Question 19:** Does the indirect method’s reconciliation of cash flows from operations to the total change in net assets provide any particular type of necessary information that would be lost if, as proposed, that method is no longer required? If so, please identify the potentially omitted information and explain why it is useful and whether it should be provided through disclosure rather than requiring use of the indirect method. If you suggest that requiring the indirect method is necessary, would you require that the amount for cash flows from operations be reconciled to the amount of the (a) change in net assets, (b) change in net assets without donor restrictions, or (c) proposed intermediate measure of operations before or after transfers? Why?

I agree and do not think this reconciliation is necessary.

**Question 20:** Do you agree that although operating activities is defined differently for the statement of cash flows than for the statement of activities, more closely aligning line items presented in the statement of cash flows with the proposed operating classification for the statement of activities will increase understandability even though that reporting would be somewhat different from current requirements for business entities? If you believe that operating items in the two financial statements would not be sufficiently aligned, please indicate how their alignment might be further improved.

I do **not** believe the realignment proposed will improve the usefulness of the cash flow statement. Specifically, I do not agree with the change in classification which stipulates that cash receipts from contributions for long-lived assets and cash payments for same should be operating cash flows. In one sense this change would make the cash flows from operating activities less aligned to the measure of excess or (deficit) from operations. Very seldom do contributions for PP&É and the related expenditures occur in the same period. When you redefine operating cash flows to include these it will significantly increase the year-to-year volatility of the amount reported for cash from operating activities, and reduce its usefulness for trending purposes or as an indicator of future cash flows.

One of the SACS COC accreditation standards requires an institution to “demonstrate financial stability.” Reviewers will ask whether there is sufficient cash to pay for operating expense. Does a history of positive cash flows from operations exist? Is the school spending within its means? We have found the current definition for “cash from operating activity” to be a very helpful measure. Schools under review will often point to “cash from operating activities” as a measure which evidences it can generate sufficient cash to meet operating expenses. Changing the cash flow statement definition, particularly as it relates to PP&É, will make our assessment task more difficult.
In addition, if we keep PP&E activity out of the cash flow operating section it would be in harmony with how I’d like to see net assets released for long-lived assets presented. See response to Question 10.

**Question 21:** Are there any particular proposed amendments in this Update that would require a longer period to implement than other amendments? If so, please explain.

I believe changing to the direct method cash flow statement will take the most time. Even using the “indirect” approach of adjusting revenues and expense amounts for the change during the period in related assets and liabilities will require a time consuming review of those asset/liability accounts. Most will correlate well but some accounts will need to be bifurcated, or if that is impractical, then time is needed to establish special reports that will isolate certain types of transactions. I’d feel much more comfortable if I had one full year to figure out what changes are needed, and then another year’s activity to see if my changes worked.

Given all of the changes proposed in this exposure draft I’d suggest an implementation date to periods ending on or after December 15, 2018.

**Question 22:** Are there reasons for any particular size or type of NFP to need a longer time frame to implement the proposed amendments in this Update? If so, please explain.

I see no reason for a longer time for smaller NFPs if the implementation date was after December 15, 2018.