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Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, CT 06856-5116
Attn: Technical Director

File Reference No. 1820-100 Revenue Recognition Topic (605)

Dear Technical Director:

Thank you for the opportunity to respond on the IASB/FASB revenue recognition project. Employers Mutual Casualty Company (EMC) is a regional insurance company with a surety operation that provides surety bonds for small to medium sized contractors performing under $50 million in annual volume. EMC is writing this letter from the perspective of the user of CPA prepared financial statements.

Please understand that surety companies, like EMC, are one of the most prominent users of contractors' financial statements prepared by independent CPAs. In many cases, the surety will extend bond credit in the millions of dollars on the basis of the financial statement. It is both important and necessary that we give our input on any significant changes that will impact the content of a CPA prepared financial statement. We appreciate the IASB/FASB for taking our comments in consideration.

Construction accounting is very industry specific and has unique characteristics, including the proper way to recognize revenue. The Audit and Accounting Guide for Construction Contractors, SOP 81-1, has been a valuable tool for preparers and users alike for many years. Revenue recognition, as presented in SOP 81-1, has been widely accepted by the surety industry.

Following are our reasons we feel SOP 81-1 (percentage of completion, cost-to cost) is the most accurate, objective and useful method for revenue recognition for construction contractors:

- It provides a uniform and consistent method of recognizing revenue for all contracts. This is important for small to medium size construction firms that have to account for many projects with a limited staff.

- The WIP schedule computations are easily identifiable to the users of the financial statements.
- This method clearly identifies any underbillings and overbillings, allowing the user to question any issues regarding a project.
- This method allows surety companies to perform their own profit trending analysis based upon the various period WIP schedules.
- Surety companies have based their underwriting on this method of reporting.

It is our understanding that the proposed IASB/FASB revenue recognition project would completely repeal SOP 81-1 and put in place a new method that would require revenue recognition based upon certain performance obligations and/or require certain contracts to be arbitrarily segmented. Furthermore, under the new method, contract costs are redefined and decoupled from revenue.

Following are our objections to this new method:

- Performance obligations might allow for an intentional (or perhaps unintentional) acceleration of gross profit, only to be adjusted back in the following period.
- There may be difficulty in defining and communicating the performance obligations between the contractor, CPA, surety and banker. A single performance obligation at the overall contract level leads to consistency for everyone involved with the financial statements.
- EMC primarily works with small to medium sized contractors under $50 million in revenue. In our opinion, the vast majority of these contractors do not have the ability to properly account for performance obligations below the overall contract level.
- The computation of revenue recognition under this method will be more convoluted and more judgment based making the computation less reliable for the user.
- Decoupling costs from the revenue recognition process goes against the matching principal.
- As a surety, we are bonding the entire contract, not a segment of the contract. It is important that we know where the costs and gross profit are on the entire project during each reporting period.
- When a project is heavily underbilled based on the percentage of completion, cost-to-cost basis, a surety can easily identify a potential issue with a project. What useful meaning will underbillings and overbillings have under the new method?

- We are concerned that the internal accounting staff of the construction firm will not have the time to spend for each project to allow for this new method of reporting. This could lead to big swings on the internally prepared WIP schedule, income statement and balance sheet when the CPA completes their year end audit.
- An additional concern would be the increase overhead expense for the construction firm in retraining their staff, investing in new software and higher audit fees. Surety companies are reminding their contractors to keep overhead expenses as low as possible, especially in this current economic climate.
- We do not see this change as beneficial to the construction industry.

The new proposed method will not be the best fit for the construction industry and their users of the financial statements. We encourage IASB/FASB to continue the usage and guidance of SOP 81-1 for revenue recognition for contractors or exempt the construction industry from the new proposed standard. At the very least, we would like to see an exemption for smaller, private firms from this new method.

Please let us know if you have any questions or comments on this letter.

Sincerely,

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