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AGC of America
THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA
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September 20, 2010

via email: director@fasb.org

Mr. Russell Golden
Technical Director
Financial Accounting Standards Board
301 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

File Reference: No. 1840-100, Proposed Accounting Standards Update, Contingencies (Topic 450), *Disclosure of Certain Loss Contingencies*

Dear Mr. Golden:

On behalf of the Associated General Contractors of America (AGC), I respectfully submit the following comments in response to the Exposure Draft, *Disclosure of Certain Loss Contingencies*. AGC appreciates the efforts of the Board and its staff in preparing the Exposure Draft and for the opportunity to comment on the proposed principles.

AGC is the largest and oldest national construction trade association in the United States. AGC represents more than 33,000 firms, including 7,500 of America's leading general contractors, and over 12,500 specialty-contracting firms. Over 13,000 service providers and suppliers are associated with AGC through a nationwide network of chapters. AGC contractors are engaged in the construction of the nation's commercial buildings and industrial facilities, highway and public transportation infrastructure, water and wastewater systems, flood control and navigation structures, defense installations, multi-family housing, and more.

The construction industry has played a powerful role in sustaining economic growth, in addition to producing structures that add to productivity and quality of life. Unfortunately, the construction industry has suffered as a result of the economic downturn. Whereas the construction industry provided jobs for 7.7 million workers in August 2006, there are currently 5.6 million workers in the industry (down 28 percent). The industry's unemployment rate in August 2010 was 17.0 percent, not seasonally adjusted, nearly double the all-industry rate. Nonetheless, the construction industry is a significant source of good-paying jobs, is a major customer of U.S. manufactured goods, and makes a large contribution to U.S. Gross Domestic Product (6.4 percent in 2009).

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Going Concern Basis and Multiemployer Plan Issues

The Exposure Draft seems to be written with a prejudice towards the measurement of a liability based upon the termination value of an entity—in other words, not a going concern basis—as opposed to a viewpoint of the entity measured as one that is expected to continue in business. Specifically, the proposed changes to employer participants in multiemployer plans fit this description:

> **715-80-50-2** An employer shall apply the provisions of Topic 450, if either of the following would occur:
>
> a. An employer would withdraw from the plan under circumstances that would give rise to an obligation

The Board applies and uses the terms "probable" and "reasonably possible" throughout its Exposure Draft but uniquely removes these measurements from its proposed changes only for multiemployer plans. Why are multiemployer plans and not all other obligations of an employer or business proposed to be measured in this same manner? For example, if one applies the proposed principles of the multiemployer proposed potential liability change, it would require all employers and businesses to disclose their potential obligations if:

a. An operating and profitable business division is terminated
b. All or a large number of employees would be terminated
c. Contractual obligations would not be fulfilled (whether performance obligations such as a construction contract or right to use contracts such as an operating lease on business facilities)

Currently, the disclosures of Topic 450 are only applicable if withdrawal from a multiemployer plan under circumstances would give rise to an obligation is either probable or reasonably possible. The current Topic 450 disclosures remain appropriate to multiemployer plans, not the proposed changes.

In addition, assuming that the Board reconsiders and applies the "probable" and "reasonably possible" disclosure measurements to the proposed changes for multiemployer plans, the provisions relating to disclosures of asserted but remote loss contingencies that could have a "severe impact" should be modified as it relates to withdrawal liabilities from multiemployer plans. These liabilities, by their nature, will frequently rise to the "severe impact" level; however, since significant voluntary actions need to be taken to incur this liability, requiring disclosure without evidence that the required actions are "probable" or "reasonably probable" make these disclosures misleading to the readers.

Furthermore, there appears to be an inherent conflict between the thresholds of application between this Exposure Draft and the recently released Exposure Draft on Compensation—Retirement Benefits—Multiemployer Plans (Subtopic 715-80). The Exposure Draft on Multiemployer Plans would require withdrawal liability to be disclosed *if obtainable* (ASC 715-

80-50-1B m.2). However, from the Exposure Draft on Loss Contingencies, financial reporting entities would disclose withdrawal liabilities if they pose a potentially "severe impact" (ASC 715-80-35-1/715-80-50-1&2; 450-20-50-1D). The only way to know if a withdrawal liability poses a severe impact is to know what that withdrawal liability amount is at that date in time, which is impossible. Therefore, while one standard would require the latest obtainable information, the other standards would require reporting entities to know what that information is at that date in time and form a judgment regarding severity. This appears to be a conflict in the drafting of the two proposed standards which needs to be addressed.

AGC believes that issues relating to multiemployer plan disclosure would be more appropriately considered in the context of the Exposure Draft on Multiemployer Plans and hence any references to multiemployer plan disclosures should be deleted from the Exposure Draft on Contingencies.

Insurance Offset Issues

The Exposure Draft states "When assessing the materiality of loss contingencies to determine whether disclosure is required, the entity shall not consider the possibility of recoveries from insurance or other indemnification arrangements."

This provision is not appropriate for situations where the loss contingencies are fully covered by funded insurance. In those situations, the loss contingencies have been removed from the entity and transferred to the insurance carrier. An example of this would be when the entity is a member of an insurance captive. Under many insurance captive arrangements, the entity is required to fund by cash or letters of credit the actuarially calculated exposure for a certain time, usually for period of a year, for insurances such as general liability, workers compensation, and automobile coverage. There is no risk of default of non-coverage to the entity by the captive insurance carrier as the losses are fully funded, in advance, and any additional potentially catastrophic losses have been passed to reinsurance carriers by the captive.

In addition to captive arrangements, for typical insurance, the insuring agreement of the standard Commercial General Liability Coverage Form (ISO Form CG 00 01 10 01) reads:

> We will pay those sums that the insured becomes legally obligated to pay as damages because of "bodily injury" or "property damage" to which this insurance applies. We will have the right and duty to defend the insured against any "suit" seeking those damages. However, we will have no duty to defend the insured against any "suit" seeking damages for "bodily injury" or "property damage" to which this insurance does not apply. We may, at our discretion, investigate any "occurrence" and settle any claim or "suit" that may result.

Under these situations not permitting the entity to offset its potential loss contingencies with the funded insurance would distort its financial position. Reporting the claim liability and the

carrier's obligation to satisfy the liability "gross" distorts the assets and liabilities of the reporting entity. The reporting entity contractually has passed that liability off to the carrier that accepted the claim. At that point the reporting entity has also lost control over the ultimate resolution of the claim with the claimant. Accounting for the claim liability independent of the carrier's obligation to satisfy that liability would not be fair representation of the transaction.

An entity should consider insurance recoveries in determining if a loss should be disclosed and should be permitted to net expected insurance recoveries against contingent liabilities. The insurer's duties to defend the entity and pay the entity's legal obligation should not be ignored when the entity assesses the materiality of a loss contingency.

For non-captive insurance situations, the following is an example of a typical construction related insurance claim. Assume that:

- An employee falls from a scaffold at the entity's job site
- The employee is seriously injured, engages an attorney, and initiates a proceeding against the entity seeking compensation in a material amount
- The entity determines that its workers' compensation insurance fully covers the claim

Because insurance is expected to cover the claim fully, the entity should not be required to accrue an estimated possible loss, record an equivalent insurance recovery, or disclose the claim (based on a determination that the probability of a material loss to the entity is remote and not severe.)

Under the proposed guidance, assuming that the claim is material, the example entity likely must accrue an estimated loss contingency and associated insurance recovery, and disclose all of the following:

1. The name of the court or agency in which the proceedings are pending
2. The date instituted
3. The principal parties to the proceedings
4. A description of the factual basis alleged to underlie the proceedings
5. The current status of the litigation contingency

This example demonstrates that application of the proposed guidance to insured claims would result in unwarranted detail in financial statements and disclosures, and dilute important loss contingency information, and potentially materially distort some of its financial ratios.

Only in cases where there is an actual dispute as to whether insurance coverage applies to the loss contingency in question, potential insurance recoveries should not offset the potential loss.

Regarding the provision in the Exposure Draft that would require the disclosure of information about possible recoveries from insurance and other sources if "it is discoverable by either the plaintiff or a regulatory agency" does not seem to match the reality of real world issues addressed in litigation. Often, just because an item "is discoverable" does not mean that the plaintiff has in fact requested the particular item. Additionally, the determination of whether an item "is discoverable" can be an item of legal debate for a court to decide.

Potential Loss Contracts

SOP 81-1, ASC Topic 605, fully covers the issues related to potential loss contracts for performance contracts. The stated goal of the Exposure Draft is "more timely disclosure of remote loss contingencies with a potentially severe impact." This Exposure Draft will confuse or overlap the accounting and disclosures for performance contracts already addressed by Topic 605 or the new proposed Exposure Draft, *Revenue from Contracts with Customers*.

Performance contracts should be exempted from this Exposure Draft.

Questions for Respondents

Question 1: Are the proposed disclosures operational. If not, please explain why?

No. The proposed multiemployer plan liability disclosures are not operational as further explained in our response herein.

Additionally, the Exposure Draft has proposed the following new disclosure: "During early stages of asserted litigation contingencies, at a minimum, the contentions of the parties (for example, the basis for the claim and the amount of damages claimed by the plaintiff and the basis for the claim and the amount of damages claimed by the plaintiff and the basis for the entity's defense or statement that the entity has not yet formulated its defense)." We believe that this requirement would be meaningless as many claimed or asserted damage amounts by plaintiffs are typically greatly overstated and seldom indicative of the final outcome.

Question 2: Are the proposed disclosures auditable? If not, please explain why?

No. The majority of the disclosures are not auditable. In an audit, confirmations or information, such as the legal letter written by an entity's outside legal counsel, and other outside sources have much more value in an audit than management's representations. In disclosures regarding loss contingencies related to lawsuits, an entity's outside counsel letter is paramount to proper disclosures. If the information required by the Exposure Draft is not supplied by an entity's outside counsel, the information will not be auditable. Unless the Board coordinates the Exposure Draft's new required disclosures with the American Bar Association and is able to obtain agreed upon changes to the document issued in 1975, *American Bar Association Statement of Policy Regarding Lawyers' Responses to Auditors' Request for Information*,

auditors will not be successful in being able to determine if management's representations are fairly presented on this issue.

Additionally, the proposed disclosures regarding multiemployer plans may: (1) be costly to obtain as either the employer or the pension plan will be required to calculate withdrawal liabilities for each and every participant in the plan on an annual basis under certain actuarial assumptions (Currently, such calculations are not performed on a regular basis.); (2) not be able to be obtained unless the plans themselves perform the calculations and supply it to the employers as typically only the plan(s) have the available data and plan statistics that a participating employer may not have; or (3) not be able to be obtained in a timely manner (Specifically, the data may become available well after the employer's year end.).

Question 4: Is the proposed effective date operational? If not, please explain why.

Yes. The proposed effective date is operational only if agreement can be reached with the ABA on litigation disclosures so that requested attorney's letters provide the data that the Exposure Draft is required to be disclosed.

Question 5: Do you belief that the proposed disclosures will enhance and improve the information provided to financial statement users about the nature, potential magnitude, and potential timing (if known) of loss contingencies?

Yes, for public entities. No, for nonpublic entities. For nonpublic entities, any additional information can be requested directly by the users of the entity's financial statements.

Question 6: Do you agree that nonpublic entities *should be exempt from the tabular reconciliation disclosures required in the amendments in this proposed Update? If not please explain why. Are there any other aspects of the amendments that should be applied differently to nonpublic entities? If so, please identify and explain why.*

Yes. Nonpublic entities should be exempt from the tabular reconciliation disclosures.

Additionally, nonpublic entities should be exempt from these proposed amendments altogether, as these amendments are neither relevant nor cost effective for nonpublic entities. In its initial Exposure Draft and in its efforts of input at roundtable discussions, it seems that the Board has not asked for, nor received input on the different needs and concerns of the users of nonpublic entities. The users of public entities' financial statements frequently cannot obtain information directly, nor have their requests for additional information, or certain questions, answered by a public entity. Users of nonpublic entities' financial statements can, however. Owners of nonpublic entities want information to manage their businesses and can obtain information about contingencies directly from management and/or their legal counsel. Owners of public entities, however, are not able to obtain information about contingencies directly. Additionally, owners of public entities want as much information as they can obtain in order to determine any potential affects to the values of an entity on an ongoing basis. Nonpublic

owners, on the other hand, are not concerned about the value of their entities on an ongoing basis.

Furthermore, a disclosure exemption for information that could prejudice an entity's position in a legal proceeding should be provided for nonpublic entities. Many nonpublic entities are involved in only one legal dispute at any one time, and for such entities, aggregate disclosure is not applicable. The Illustrative Disclosures of the Update are extremely detailed and the disclosure of certain information (e.g., discoverable information not provided to the plaintiff and the entity's rationale for its litigation contingency) could be detrimental to the settlement or outcome of the litigation.

Question 7: The amendments in this proposed Update would defer the effective date for nonpublic entities for one year. Do you agree with the proposed deferral? If not, please explain why.

Yes. The proposed deferral is acceptable, as a start, until the *Blue Ribbon Panel* on Private Entity GAAP reaches its decision on the future of accounting for private entities. If the Panel does not reach its decisions by then, the deferral for nonpublic entities should be made indefinite until it does.

Again, thank you for the opportunity to comment and for your consideration of our views.

Sincerely,

Stephen E. Sandherr
Chief Executive Officer