

From: [Doug Kinney](#)
To: [Director - FASB](#)
Subject: Comment Letter - File Reference No. 1820-100
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Financial Accounting Standards Board
401 Merritt 7
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Norwalk, CT 06856-5116

Attn: Technical Director – File Reference No. 1820-100
(Via U.S. Mail and Electronic Mail)

Re: Comments on the FASB and IASB’s Exposure Draft on Revenue Recognition from Contracts with Customers

Ladies and Gentlemen:

I am a part owner and CFO of a general construction company in Kansas, specializing in the construction of water and wastewater treatment plants. Our company completes approximately \$30 million per year in contract revenue. Before making a career change to the construction industry in 1998, I also spent 23 years as a Surety Bond Underwriter, making daily credit decisions on the basis of audits presented by dozens of contractor clients. Because of my career history, I am in a good position to understand the impact of accounting standards on both the reporting company and the users of audited financial statements.

Our company has very strong concerns regarding the proposed “performance obligation method” of revenue recognition for contracts with customers. We see no significant benefit to this revised method of revenue recognition, either to the reporting companies or to the users of the audited financial statements. In fact, we feel that attempting to recognize revenue on a “performance obligation” basis will lead to higher costs for everyone concerned, financial statements that are much more complicated and difficult to interpret, and more opportunities for contractors to manipulate financial reporting. The performance obligation method is simply bad accounting practice for the construction industry.

At our company we have had some preliminary discussions of the possible impact of the proposed new revenue recognition rule, and the overriding fact that becomes immediately apparent is that no two individuals can come to the same conclusion regarding what constitutes a separate and distinct “performance obligation”. We cannot agree even within our own company on these obligations. The proposed new rules will generate increased probability of conflict between contractors and their auditors regarding how projects should be subdivided into performance obligations.

Contractors do not estimate, bid, build, or keep the books on projects on a segregated “performance obligation” basis. The proposed regulation would require a complete overhaul of contractors’ accounting systems, forcing us to set up a separate “job” in our accounting system for each performance obligation. Instead of 10 active jobs to track, we will now be required to track 40, 50 or even more jobs, depending upon how “performance obligation” is interpreted. In like manner, our WIP statements will increase from one page listing 10 jobs, to multiple pages listing dozens of jobs. We fail to see how that improves financial reporting

for the end users of our financial statements.

Tracking and allocating revenue by performance obligation rather than at the job level would greatly increase overhead costs for small to mid-size contractors. My company's accounting department consists of a CFO, a Controller, and two Accounts Payable / Payroll managers. We do not have the staff to subdivide each of our projects into multiple performance obligations and track each obligation as if it were a separate job. It makes no sense for us be required to add additional accounting staff and additional overhead just to track our projects differently for no significant benefit. In addition, we anticipate inevitable increases in fees paid to our outside auditors, as their work is further complicated and more field work is required to complete our audit. Time is money for both contractors and accountants. Tracking and auditing projects that are reported on a performance obligation basis is going to cost us more money.

From an accounting theory standpoint, we believe that attempting to subdivide construction projects into separate performance obligations does not make sense, because the risks to the contractor are inseparable within the contract. In our case in particular, we enter into contracts to provide a fully usable and functioning water or wastewater treatment plant, and all elements of the plant must function together in order for us to fulfill our obligations under the contract. We cannot "sell" a separate and distinct clarifier or UV filter system. We must sell a total, integrated package of systems which all function smoothly together to process water or wastewater.

It is also important to remember who is using our audited financial statements. For small to mid-sized contractors, the primary users of our financial information are sureties and banks. Based upon my 23 years of experience in the surety industry and my conversations with current surety executives, I can say without any doubt that the surety professionals in this country are definitely not in favor of further complicating contractors' audited statements by reporting on the basis of performance obligations rather than recognizing revenue at the job level. The current "job level" revenue recognition system has been working admirably for the surety industry for many years, and to my knowledge there is not a great deal of sentiment in the surety industry to change a method that currently works well. Just as contractors do not wish to track and report 40 or 50 different performance obligations on our WIP schedules, I can assure you that the surety companies don't want to try and analyze WIP schedules that are presented in that manner.

Bank lending officers, in my opinion, generally have a less detailed understanding of WIP analysis than surety professionals. They are barely able to follow our job level reporting now. Breaking each job down into multiple performance obligations will only confuse them.

The ultimate outcome in the case of both sureties and banks is predictable: More uncertainty on their part equals tighter credit. Is anyone in the surety or banking industry experiencing problems or issues with the current method of job level percentage of completion revenue recognition? I am not aware of any outcry from either of those industries requesting changes in the current accounting method.

In conclusion, we at Walters-Morgan Construction, Inc. feel that the proposed "performance obligation" basis of revenue recognition does not make sense for construction contractors, and will only further complicate our financial reporting systems, restrict available credit, drive up our overhead costs, and create more opportunities for contractors to manipulate

financial reporting to their advantage. It is a bad response to a perceived problem that really doesn't even exist. We strongly encourage the FASB to reconsider this accounting approach for construction contractors.

Yours truly,

Doug Kinney

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