1820-100
Comment Letter No. 534

Grassi & Co., CPAs, P.C.

An Independent Firm Associated with Moore Stephens International LTD

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

Re: FASB Exposure Draft "*Revenue Recognition from Contracts with Customers*"
FASB File No. 1820-100 (the "Exposure Draft")

Dear Technical Director:

Thank you for the opportunity to respond to the above-referenced Exposure Draft.

Grassi & Co., CPAs, P.C. has had a major concentration of clients in the construction and related industries for the past 30 years. As such, we work closely with the management teams of companies within the industry to ensure their financial statements are presented accurately and are in accordance with U.S. Generally Accepted Accounting Principles. These financial statements are the lifeline of a contractor as it relates to obtaining bank and surety credit. We also consult with financial institutions and sureties to assist in their underwriting of contractors' financial statements. The following comments relate to the adverse impact that the Exposure Draft will have on the industry.

We have the following concerns about the proposed guidance:

1- We question the feasibility of providing a "one-size-fits-all" revenue recognition standard for all businesses in all industries.
2- Segregating a contract into separate performance obligations introduces additional levels of subjectivity into the revenue recognition process and increases the cost of compliance.
3- For companies in the construction industry, we believe that the costs of complying with the proposed guidance will significantly outweigh any potential benefits derived.

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One Revenue Recognition Standard

We believe that a common revenue standard is not realistic and that specific guidance for selected industries continues in practice.

With respect to a construction contractor, we believe that the guidance proposed by the Exposure Draft would result in revenue recognition which does not reflect economic reality. All construction companies bid and manage their projects on a contract-by-contract basis. Individual components / line items of a given contract might be bid at lower or higher margins, depending on circumstances unique to each project (e.g., unit price contracts often have unbalanced bidding by line item, cost plus contracts may involve meeting or exceeding certain performance targets or metrics, etc); however, the overall margin on the entire contract is the basis for determining economic performance. A contractor would accept the disparity between profit margins on individual components due to the overall profit margin expected on the project. A contractor would not accept a lower profit margin on certain components without consideration of the entire project. As such, the requirement to report each component as a separate economic unit is contrary to how contracts are structured and how a contractor operates. Furthermore, the users of the financial statements of our clients, specifically banks and surety companies, require regular work-in-progress reports by contract, acknowledging the contract as the economic unit of measure. Accounting for revenue by segregating contracts into separate performance obligations, as proposed by the Exposure Draft, is contrary to management's intent and to the needs of the users of the financial statements, given that it would distort the entity's financial results.

Long-term contracts are inherently complex in that they often involve information from numerous subcontractors, may require change orders, span over more than one fiscal year, and generally require constant revisions to estimated costs as a job progresses. We believe that such complex accounting transactions should not be forced into a one-size-fits-all standard for revenue recognition and warrants its own specific treatment.

We believe that current accounting guidance for revenue from construction contracts contained in FASB ASC Sub-Topic 605-35 ("FASB ASC 605-35") (formerly SOP 81-1) has served the industry well over the past 30 years and should be retained. A large number of construction contractors are nonpublic entities. The primary users of the financial statements are not third-party investors but include owners/managers of companies, bankers, sureties and government agencies. The reporting requirements of FASB ASC 605-35 are well understood by these users and have given them the confidence that financial statements of construction contractors are understandable, informative and comparable. Our involvement with these users over the past 30 years has given us no indication that a change in the method of revenue recognition is either necessary or desirable. We believe that the proposed guidance in the Exposure Draft will not improve financial reporting for construction contractors. It will add an additional level of complexity to the revenue recognition process and fail to reflect the true economic performance / financial results of the entity.

Segregation of Contracts into Separate and Distinct Performance Obligations

The Exposure Draft introduces additional levels of subjectivity into the revenue recognition process by requiring the segregation of each contract into separate performance obligations. Paragraphs 50-52 require the contract (transaction) price be allocated to each performance obligation based on the stand alone selling price of each good or service underlying each performance obligation. In some cases, the stand alone selling price will be objectively determinable, especially if the good or service is sold separately by the contractor; however, in many, if not most cases, this price must be estimated.

Revenue recognition for long-term construction contracts is currently largely dependent on estimates provided by project managers. Under the proposed standard, contracts would have to be segmented and profit margins allocated across these segments, which adds additional layers of estimation. We believe that these additional layers of estimation will add significantly to the costs of complying with the proposed guidance. Contractors will need to develop and support the estimates. Auditors will need to gain comfort with additional amounts estimated, resulting in added complexity to the audit process. Users will need to be educated on the nature of the estimates and how they affect the financial statements.

The Exposure Draft will result in a considerable amount of subjectivity. If two contractors were engaged to construct identical structures, each contractor may arrive at different conclusions regarding the performance obligations. This would result in revenue being recorded in different periods for each contractor. More specifically, increasing subjectivity could potentially provide the opportunity for management teams to manipulate financial results. This added level of subjectivity will, in all likelihood, result in widely divergent practices among contractors resulting in a lack of comparability in results of operations. Because revenue and profit is recognized based on performance obligations, a contractor could record large profits on components that are completed at the start of a project and losses on components completed at the end of the project. Conversely, large losses could be recognized at the start of a project where performance obligations are completed while profits would not be considered until certain components are completed at the end of the project. This scenario could have a dampening effect on the credit industry, as banks and sureties will be more suspect of individual company reporting.

Cost / Benefit Analysis of Compliance

In the midst of an extremely difficult time for the construction industry, the additional time and costs of complying with the proposed guidance for both contractors and their auditors would be considerable, without any potential benefits to the primary users of the financial statements. In addition to those already mentioned, compliance costs we foresee include, but are not limited to, the following:

1- Modifications of accounting systems and related controls to account for the segregation of contracts into multiple performance obligations, including the allocation of material and labor costs, accordingly. Development of additional estimates by management as contracts would have to be segmented and profit margins allocated across these segments.
2- Reconciliations of amounts reported in the financial statements to amounts required by financial statement users, specifically lenders and sureties.
3- Far more detailed disclosures of required financial information.
4- Full retrospective application of the proposed standard.
5- Different recordkeeping and reconciliations required for income tax purposes to comply with tax regulations.
6- Additional accounting staff.

We believe that the proposed guidance would persuade many of our construction clients to prepare OCBOA financial statements or reports with qualified opinions due to a GAAP departure for not presenting long-term construction contracts under the new standard. This will only serve to erode the significance of the audit opinion.

Recommendation for Changes to Exposure Draft

Based on the above, we recommend that the Board provide an exemption for construction contractors from the provisions of the Exposure Draft, or alternatively, permit revenue recognition using the contract as the economic unit of measure instead of the performance obligation.

We respectfully ask that the Board strongly consider these issues as they apply to the construction industry, and not as they apply to "global" standard setting.

Sincerely,

GRASSI & CO., CPAs, P.C.

Louis C. Grassi, CPA, CFE
Managing Partner