

LETTER OF COMMENT NO. 3

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

## Reference No.

File Reference: No. 1600-100

Proposed FASB Statement
Disclosure of certain loss contingencies, an amendment to FASB Statement 5 & 141 (R)

Dear Sir or Madam:

Thank you for the opportunity to address this proposed Statement. I am the Executive Vice President/CFO of a 53 year old mid-size (\$32-\$40 million), privately owned Construction Company. The construction industry by its very nature reeks of both loss and gain contingencies. Therefore, I read with very much interest FASB's attempt to enhance our financial statements through this proposed amendment to Statements 5 and 141 (R).

My responses to your "Request for Comments" follow.

1. Will the proposed Statement meet the project's objective of providing enhanced disclosures about loss contingencies so that the benefits of those disclosures justify the incremental cost? No. I do not think that additional disclosures concerning loss contingencies that have been deemed "remote" (defined as "The chance of the future event or events occurring is slight" FAS5-3c.) will provide any additional benefit to the financial statement users. Why should entities waste time and money (legal fees and costs of outside advisors) disclosing things that are only remotely possible? Why yell fire in a crowd when someone lights up a cigarette? The potential benefits of additional disclosures of loss contingencies when the "likelihood is remote" for the financial statement user would be negligible at best and certainly not be reliable as a projection of future cash flows.

Most of our companies past loss contingency disclosures falling in the remote category consisted of the "The company is involved in various claims and lawsuits arising in the normal course of business. In management's opinion, the outcome of these matters will not have a material adverse effect on the Company's consolidated financial position". I think this type of disclosure would still be appropriate.

2. Do you agree with the Board's decision to include within the scope of this proposed Statement obligations that may result from withdrawal from a multiemployer plan for a portion of its unfunded benefit obligations, which are currently subject to the provisions

of Statement 5?No. When entities decide to withdraw from multiemployer plans, they go through a formal withdrawal process usually facing hostility from the plans wishing to resist their withdrawal. The plans administrators attempt to stonewall the withdrawal proceedings by any means at their disposal. Meanwhile, withdrawing companies have no access to data indicating the probabilities that the plans will remain fully funded during the remaining liability period, if any, nor is there any way for a withdrawing company to obtain information upon withdrawal. The trustees of the multi-employer plans are charged with the fiduciary responsibility to invest the plans assets and the employers have no voice in their chosen investments. A plan can be heavily invested in the stock markets and be fully funded one day and the next day be significantly under funded due to a market fluctuation downward. Therefore, due to lack of information available to withdrawing employers to be able to calculate their portion, if any, of a potential under funded position in a multi-employer plan makes its improbable to come up with a reasonable estimate at any time, much less at year end or interim end of the employer.

- 3. Should an entity be required to provide disclosures about loss contingencies, regardless of the likelihood of loss, if the resolution of the contingencies is expected to occur within one year of the date of the financial statements and the loss contingencies could have a severe impact upon the operations of the entity? No. If management is convinced through its due diligence that the likelihood of loss is remote, then regardless of severity of a negative outcome, it has not risen above remote and therefore should not be disclosed.
- 4.a. Do you believe that this change ("The Board decided to require entities to disclose the amount of claim or assessment against the entity, or, if there is no claim or assessment amount, the entities best estimate of maximum possible exposure to loss") would result in an improvement in the reporting of quantitative information about loss contingencies? No. Usually the ranges of possible outcomes that both sides of a lawsuit or claim seek are so far apart that it makes it impractical to venture a guess as to amounts of actual exposure. As an example, in the case of construction warranties (typically 1 year but subject to 10 years statutes of repose) there is no reasonable methodology to quantify amounts of possible loss contingencies. The vast majority of past construction projects will incur no warranty expense. However, when a warranty claim does occur, it can be quite large and, without additional investigation, an estimate of how much it will cost to repair or whether the claim damage losses can be subrogated is unknown. To hazard a guess as to the maximum possible amount of exposure for these type of loss contingencies would be irresponsible and without basis. Our company's current disclosures that warranty costs are expensed as incurred (disclosing actual cost incurred in all years in the report) and that future expenses cannot be reasonably estimated is the most accurate information available.
- 4.b. Do you believe that disclosing possible loss or range of loss should be required, rather than optional, if an entity believes the amount of the claim or assessment or its best estimate of the maximum possible exposure to loss in not representative of the entity's actual exposure? No. If disclosure is required it should be an entity's best

estimate of actual exposure, if known, or in its absence an option to disclose the range of possible exposure, if calculable, provided the likelihood of loss is more than just remote.

- 4.c. If you disagree with the proposed requirements, what quantitative disclosures do you believe would best fulfill user's needs for quantitative information and at the same time not reveal significant information that may be prejudicial to an entity's position in a dispute. I do disagree with the proposed requirements and do not believe that users need additional disclosures concerning "likelihood is remote" type disclosures. I think FAS 5 disclosures are adequate as they now exist for accrued loss contingencies and that details concerning litigation should be kept confidential and non-prejudicial.
- 5. If a loss contingency does not have a specific claim amount, will an entity be able to provide a reliable estimate of the maximum exposure to loss...that is meaningful to users? No. How can an entity provide a "reliable estimate" if the claim amount hasn't been identified by the claimant? What constitutes a reliable estimate? What if an entity's estimate does not turn out to be reliable? How would the user of the financial statements that had relied on those estimates react? The blame game begins with the entity's management for providing the "reliable estimates" when none were available and the entity's auditors for signing off on them.
- 6. Should disclosure of the amount of settlement offers made by either party be required? No. Settlement offers should be kept confidential and are points of trying to negotiate a solution to the claim but are not indications of possible exposure. Most settlement offers are meant to mitigate further legal proceedings and the expense and time wasted by both parties. If a settlement offer is accepted then there is no longer a doubt as to the amount of loss accrual but until one is accepted, there usually are many attempted offers to settle in compromise. To disclose these attempts would serve no fruitful purpose for users other than to second guess management for not settling in the event an offer is not accepted and the ultimate conclusion ends up worse than one of the settlement offers.
- 7. Will the tabular reconciliation of recognized loss contingencies, provided on an aggregate basis, provide useful information about loss contingencies for assessing future cash flows and understanding changes in the amounts recognized in the financial statements? No. Future cash flows of uncertain events cannot be accurately assessed by a user of the financial statements from this reconciliation. Current cash flow disclosures will reflect impacts of resolved contingencies and claims and on the amounts accrued for future contingencies.
- 8. This proposed Statement includes a limited exemption from disclosing prejudicial information. Do you agree that such an exemption should be provided? Yes. If the FASB decides to go forward with these new requirements, any kind of disclosure which would compromise the entity's position in the litigation should not be disclosed.
- 9. If you agree with providing a prejudicial exemption, do you agree with the two-step approach in paragraph 11? No. Legal and contractual basis should not be disclosed, the current status should be assumed that it is not settled and is an open claim or lawsuit

thereby not needing additional disclosure. Timing of resolution and a description of factors that are likely to affect the ultimate outcome of the contingency along with potential impact on the outcome are speculative at best and should be avoided in footnotes. These new disclosures are proposed to cover "likelihood as remote" as well as for loss contingencies that cannot be reasonably estimated. Remote contingencies should not take up much space in an entity's footnotes.

- 11. Do you agree with the description of prejudicial information as information whose "disclosure...could affect, to the entity's detriment, the outcome of the contingency itself? Yes. I believed this to be the case for disclosure in FIN 48 also. This disclosure provides the IRS with a road map to challenge uncertain tax positions an entity has taken, most certainly to the entity's detriment.
- 12. Do you believe it is operational for entities to disclose all of the proposed requirements for interim and annual reporting periods? Should the tabular reconciliation be required only annually? No. The additional information detracts from the usefulness of the financial statements and further clutters the minds of its users with speculation instead of facts. The tabular reconciliation is a waste of time and expense and adds no useful information to the reader.
- 13. Do you believe other information about loss contingencies should be disclosed that would not be required by this proposed Statement? No.
- 14. Do you believe it is operational for entities to implement the proposed Statement in fiscal years ending after December 15, 2008? No. The proposed Statement will significantly expand the disclosures required for contingencies and will include certain contingencies in the scope of those disclosures that were previously not included under Statement No. 5. I would recommend that this proposed Statement be suspended indefinitely or until convergence with the IFRS in the next few years. If you don't like indefinite suspension or waiting for IFRS, then a one-year deferral is necessary so as to raise the level of awareness of the scope and magnitude of the required disclosures by all parties affected.

I think FAS 5 as it now exists provides adequate disclosures for loss contingencies to investors and the other users of financial information. Additional disclosures as proposed by the Statement will not provide any additional benefit to them and will cost considerable time and money to implement and then maintain.

Thank you for allowing me to comment on the above issues.

Michael D. Humphrey Executive Vice President Dee Brown, Inc.