

Testimony of
Richard Forrestel, Jr.
on behalf of
The Associated General Contractors of America
Presented to the
U.S. Senate
Committee on Banking, Housing and Urban Affairs
Subcommittee on Securities and Investment
on the topic of
The Financial Accounting Standards Board
and
Small Business Growth
November 12, 2003



The Associated General Contractors of America (AGC) is the largest and oldest national construction trade association in the United States. AGC represents more than 35,000 firms, including 7,500 of America's leading general contractors, and over 12,000 specialty-contracting firms. Over 14,000 service providers and suppliers are associated with AGC through a nationwide network of chapters. These contractors are engaged in the construction of the nation's commercial buildings, shopping centers, factories, warehouses, highways, bridges, tunnels, airports, waterworks facilities, waste treatment facilities, dams, water conservation projects, defense facilities, multi-family housing projects and site preparation/utilities installation for housing development.

THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA
333 John Carlyle Street, Suite 200 • Alexandria, VA 22314 • Phone: (703) 837-5310 • FAX: (703) 837-5407

Building Your Quality of Life

November 12, 2003
U.S. Senate
Committee on Banking, Housing and Urban Affairs
Subcommittee on Securities and Investment

I am Richard Forrestel, Jr., a CPA and Treasurer of Cold Spring Construction Company, based in Akron, NY. I am testifying on behalf of the Associated General Contractors of America (AGC), a national trade association representing more than 33,000 firms, including 7,200 of America's leading general contractors, and 12,000 specialty-contracting firms. AGC is the voice of the construction industry.

While AGC's membership is diverse, the majority of AGC firms are closely-held businesses like ours. AGC member firms are 94% closely held, 81% are owned by fewer than four people.

I serve as the Chair of AGC's Tax and Fiscal Affairs Committee. It is this subgroup of small business CFOs and construction accounting professionals who have spent the last few months trying to understand why the Financial Accounting Standards Board (FASB) would inflict Financial Accounting Standard 150 (FAS 150) on the industry. This FASB standard has hit our industry and my committee like an earthquake. Its has the potential to undermine the fiscal stature of tens of thousands of construction companies, like mine.

I would like to thank Chairman Enzi and the other members of this distinguished committee for the opportunity to discuss both the potentially devastating impact of FAS 150 on family-owned businesses as well as the general process of communication between American small businesses and FASB.

Cold Spring Construction Company was founded by my Grandpa in 1911. We are a closely-held, family-owned construction firm that specializes in highway and bridge construction. Our projects range in size from \$1 million to \$40 million. Dad and his brother, Uncle Tom, both entered the business after serving our country in WW II and worked together until Uncle Tom died in 1977. As Dad, our Chairman, approaches his 79th birthday, he still remains very active in the business. In addition, my brothers, Steve, President and CEO, and Andrew, Vice President, are actively involved in managing our business today. We have eight siblings who have chosen other career paths; however, each worked for the company every summer to pay for college, as did 12 of my first cousins.

You get the picture, we, like thousands of other businesses in this industry, are privately held and intend to remain so. It was with this backdrop that we faced the potential onslaught of FAS 150. Through our involvement with AGC, I was able to visit FASB in Norwalk, CT, along with two other representatives of AGC on October 30, 2003.

The risks of FAS 150 to privately held firms like ours, and the majority of AGC members, cannot be overstated. As written, FAS 150 would have dramatically affected all privately held companies with mandatory redemption clauses in their buy-sell agreements. That is, if your “buy-sell¹” agreement is written so that the company must buy your stock back at some point in the future (for example at death or retirement), then the contingent future liability must be booked or accounted for today. For my family’s company, this is all our shares. The result will

¹ Buy-sell agreements are an agreement between shareholders, and possibly the corporation, for the transition of ownership.

be to take our company's more than \$10 million net worth and make it zero through the imposition of this standard.

I will briefly touch upon the ramifications of such an accounting bombshell. Cold Spring builds only public works projects, all of which require surety bonds². First, wiping out our equity would make us unable to obtain bonds. Second, we would be in violation of loan covenants³. Third, many states like Pennsylvania have pre-qualification requirements⁴ in order to bid on public works projects. FAS 150 would have rendered us unqualified to bid on most projects in Pennsylvania, because the state requires the contractor to show net worth in order to bid. Finally -- and this is strictly a psychological reason -- this change would have dramatically altered the way our balance sheet looked. Dad first worked for Cold Spring the summer after the Japanese attacked Pearl Harbor. He has worked his tail off for more than six decades. No way, not on my watch, will he be told that the company just lost all its net worth, even if it is only on paper.

FAS 150 first came to my attention at an AGC Tax and Fiscal Affairs committee meeting in June of this year. During our two-day meeting, we discussed the implications of the standard -- which at that point was effective in December 2003 -- and decided our best course of action was to put together a task force to contact FASB with our concerns. At the end of August, AGC sent our four-page letter. This letter was timed to arrive at FASB the day before their board meeting addressing FAS 150. Because of our letter, and the letters of other associations of nonpublic companies, FASB delayed extension of FAS 150 for an additional year.

² Surety bonds are guarantees that the contract will be completed and that workers, suppliers and subcontractors will be paid. Virtually all public contracts require surety bonds.

³ Loan covenants often require a target net worth.

While we appreciated the delay, FAS 150 still needed to be permanently amended for nonpublic companies. During the AGC Midyear Convention in Washington DC in September, contractors began to educate Members of Congress about this issue. The Tax and Fiscal Affairs Committee met at the same time, and decided to request a personal meeting with FASB in Norwalk. FASB responded and began the process of putting a meeting together. Schedules being what they are, the meeting was set for October 30, 2003.

Walking into this meeting, I was unwilling to accept any other outcome other than a complete change by FASB regarding 150. There is absolutely no way I would have followed through with this standard – and I told FASB this. I was frustrated that this standard was in place, which seemed like such an obvious mistake to me, and I believed this was my best, and possibly only, chance to make myself heard. I could not let this standard be enacted. At the same time, as a contingency effort, AGC continued educating Congress about the devastating impact of this standard.

After much thoughtful preparation, on October 30, two AGC representatives and I met for three hours with two Board members and five staff members of FASB. These people are, in my opinion, the best and the brightest people in the country in the accounting profession. I found them engaging and concerned with the way FAS 150 would affect my company, Cold Spring, and the rest of the industry. The seven FASB representatives asked direct and penetrating questions- honestly, it made the CPA exam seem easy in comparison. They gave us a chance to

⁴ Pre-qualification: In order to bid on public projects, contractors are required to submit information to the agency. The agency evaluates the contractor's financial ability to complete the contract.

tell our stories and listened well. They did not promise an outcome but did thank us for our input. We could have asked for nothing more. My mindset walking out of that meeting was completely unexpected to me. Rather than a brick wall, I found an intelligent, thoughtful room interested in hearing about my nonpublic company and how FASB standards affected me and my industry.

I believe FASB heard us. Last week FASB issued a change and indefinitely suspended the portion of the standard that would have forced companies like ours, who have mandatory redemption clauses with an uncertain date and value of redemption, to book it. In summary, there is no change to my financial statement. But, the other shoe has yet to drop because it is FASB's apparent intention to address this issue again in the future. The uncertainty of not knowing what will happen, if anything, will undoubtedly continue to cause heartburn for lots of folks currently contemplating buy-sell agreements.

I intend to remain available to FASB if I can be of further assistance. Having been through this process now, I know I will find the doors of FASB wide open to the concerns of my company and to small businesses in general as they move forward. It appears to me that FASB board members and staff are incredibly interested in how their standard will affect all the users of the financial statement, and willing to hear from everyone.

So, FASB's process worked, but it is unfortunate that it came down to the eleventh hour. The small business community is certainly partly to blame for our late involvement in this issue. However, I believe that this experience can be instructive for others. A better, more public,

mechanism could be put in place to ensure useful communication between FASB and the American small business community at large.

Large, public companies are accustomed to lobbying for or against changes with FASB. We small companies are not. We often get caught up in changes that probably should be, at least in my opinion, intended for public companies. I think this is exactly the case with FAS 150. Great idea for the public companies, disastrous for us. Our small construction company perspective is necessary to ensure they have evaluated all of the potential wrinkles in their standard.

One possible effort to consider is a biannual or annual meeting with FASB staff and representatives of small businesses. Just as the IRS, the Small Business Administration, and other entities have meetings just with small businesses, this would be an opportunity for all sides to meet and talk. FASB would benefit from having small business representatives provide their point of view, and at the same time, share drafts of upcoming new standards. In this way, both small business and FASB are 'on the hook' and working together.

I know that AGC is moving forward with FASB on a new working relationship. The AGC Tax and Fiscal Affairs committee will meet in January, and we are inviting a representative from FASB to join us. We are going to work proactively and ensure we are staying abreast of new draft standards. We also will continue to provide information on FAS 150 until this standard is finalized. Our intention is to keep the lines of communication open and make sure our voice is heard.

In conclusion, I would like to thank you for the chance to testify today, and your willingness to listen to and potentially address our concerns. As a fellow CPA, I agree with what I believe is Chairman Enzi's viewpoint – Congress shouldn't be legislating accounting standards. I appreciate and agree with the many reasons FASB is an independent organization. Nevertheless, this committee's oversight is critical to ensuring all standard-setting agencies are responsive to the industry.

I would also like to thank the members of the FASB and their staff. Having now had the opportunity to work with them directly, I have found them to be smart, dedicated and responsive. I would also like to suggest that a better communication mechanism between the FASB and American small business would benefit the entire economy and its 285 million participants. Thank you and I will gladly answer any questions you might have.