

March 20, 2012

International Accounting Standards Board  
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United Kingdom  
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**Subject: Comment letter on the November 2011 exposure draft on Revenue from Contracts with Customers**

Dear Sirs,

Bombardier welcomes the opportunity to provide comments to the International Accounting Standards Board on the November 2011 Exposure Draft on Revenue from Contracts with Customers (ED).

We are a Canadian, world-leading manufacturer of innovative transportation solutions. We operate under two broad manufacturing segments: aerospace and rail transportation. We generate 93% of our revenues outside Canada, with a global workforce of 70,000 employees and 76 production and engineering sites in 25 countries and a worldwide network of services centers.

Our rail transportation segment designs and manufactures highly complex rail equipment and systems and provides related services. Most of its business is conducted under fixed-price contracts that extend over many years. These contracts are currently accounted for under a continuous transfer model using the 'cost to cost' method to measure progress towards completion. Accounting for these contracts involves considerable use of estimates in determining contract costs, revenues and progress toward completion. These contracts bring many different complexities such as accounting for change orders, claims, penalties, options, combining and segmenting that are driven by the nature and complexity of the work to be performed.

Our aerospace segment designs and manufactures aircraft for the business, commercial and specialized aircraft markets and provides related services. Revenue is currently recognized at the time of delivery of each aircraft using a unit of production costing method. The aerospace industry is capital intensive, requiring significant investments in product development and the incurrence of significant learning curve costs in the early stage of the production process. Due to the long lead times and the significant costs incurred to produce aircraft, our customary business practice, and that of our industry, is to receive progress payments from our customers when certain milestones are reached. Our aircraft must meet high standards of product performance and stringent certification and approval requirements.

As the specific nature of our businesses involves complex transactions with various types of payment terms, revenue recognition is of particular interest for a large multinational publicly-owned company like Bombardier.

We support convergence of International Financial Reporting Standards and U.S. GAAP towards a single harmonized accounting standards framework. We also strongly support the Boards' efforts to create a revenue recognition standard that improves consistency across various industries and geographies and reduces the number of standards to which entities have to refer. We also appreciate the Boards' consideration of many of the concerns expressed in our previous comment letter on the revenue recognition project. However, we remain concerned by certain elements of the revised proposal. Certain principles set forth in the ED will not accurately reflect the underlying economics of our businesses or provide decision-useful information to users of our financial statements. We are also concerned by the costs that will be incurred to comply with certain disclosure requirements, which in our view, will largely outweigh the benefits for financial statement users.

### ***Identifying separate performance obligations – Clarification requested***

#### Criteria for determining when to bundle

Paragraph 28 of the ED specifies the criteria for determining if a good or service is distinct and paragraph 29 states that a good or a service in a bundle of promised goods or services is not distinct, and should be accounted for as a single performance obligation, if the following criteria are met:

- a) the goods or services in the bundle are highly interrelated and transferring them to the customer requires that the entity also provide a significant service of integrating the goods or services into the combined item(s) for which the customer has contracted; and
- b) the bundle of goods or services is significantly modified or customized to fulfil the contract.

Absent additional guidance on this topic, we are concerned that the application of these criteria may sometimes lead to the accounting for each individual unit of a multiple unit contract as a distinct performance obligation when this would be inappropriate, e.g. the construction of 50 trains based on the customer's own specifications. In our view, this may arise because the criterion "highly interrelated" for this type of contract would likely not be met, despite the fact that:

- both the entity and the customer negotiated the contract as a package (i.e. one performance obligation);
- the goods are manufactured in a continuous sequence;
- the delivery of the goods to the customers (i.e. the units) could take place at a single point of time or at different points in time;
- a modification to a unit will usually require a modification to all other units, even to those already delivered to the customer; and
- significant contract execution risks and product performance risks are not separable to individual units.

In light of the above, we believe the meaning and application of the criterion "highly interrelated" should be clarified and extended by adding other indicators that would indicate when accounting as a bundle is appropriate. We suggest adding the following indicators of qualification as a bundle:

- The bundle of goods or services constitutes in essence an agreement to do a single project, which was negotiated as a package in the same economic environment. A project for this purpose consists of construction, or related

service activity with different elements, phases, or units of output that are closely interrelated or interdependent in terms of their design, technology, and function or their ultimate purpose or use.

- Goods or services in the bundle are produced or performed concurrently or in a continuous sequence under the same project management.

### ***Constraint applicable to variable consideration - Question 3 – We disagree***

#### Criteria to satisfy the “reasonably assured” threshold

Paragraph 81 implies that it may be possible to satisfy the “reasonably assured” threshold with evidence other than the entity’s own experience, or access to the experience of other entities. We agree with the ability to rely on other evidence to reach the reasonably assured threshold in the absence of entity specific experience for similar performance obligations, or access to the experience of others. We suggest it would be beneficial to better explain this concept in the standard.

However, we question the need to have a different threshold (or recognition criteria) only applicable to variable consideration. We understand that the intent behind this rule is clearly to impose a higher threshold for recognition of variable consideration but we fail to see a consistent principle behind it. Nevertheless, if this notion is retained, we find the nuance between “expects to be entitled” and “is reasonably assured” far from being clear. At a minimum, the standard should clarify the difference between the two thresholds. We are concerned that the application of this rule, as currently proposed, could lead to large profits being recognized later than when normally expected, as the practice could well evolve in waiting for uncertain event(s) to materialize before recognizing profits.

### ***Time value of money – We partially disagree***

We agree with the concept of introducing time value of money to account for revenues from certain contracts with customers when there is an obvious financing component. However, we question whether the suggested basis for determining the significance of the financing component should be a comparison of the timing of transfer of goods and services with the timing of payments in cash.

Paragraph 59 lists certain factors to consider in assessing whether a financing component is significant to a contract and paragraph BC 147 of the basis for conclusions further explains this concept. As a result, for a separate performance obligation that is satisfied at a point in time, absent the one year exemption, we understand that an adjustment to reflect the financing component of a contract with a customer will often be required when payments are received in advance of deliveries.

While the approach proposed by the ED has some merit, we believe that this approach does not properly consider situations where significant costs are incurred for a specific contract with a customer, over a long period of time prior to delivery. In our aerospace business segment, it is customary business practice to request progress payments from customers when certain milestones are reached in order to help fund a significant portion of the costs related to the production of aircraft. We strongly suggest that when payments are proportionate to costs incurred in the case of specific production for customers, and this practice is normal for an industry, such payments should not be considered as giving rise to a financing component. Therefore, the proposed model

should be revised for transfer of goods at a point in time (we believe the model works for continuous transfer situations), to reflect the above suggestions, or that other indicators be added to take into consideration the situation described for our aerospace segment.

In addition, business models like ours, where implicit financing is inherent in contracts with customers, generally have similar arrangements with suppliers and collaborative partners. An accounting model that discounts only revenues could significantly distort the financial results of such businesses. It is therefore imperative that the Boards address time value of money in a holistic manner.

### ***Onerous performance obligation – We disagree***

We understand from the basis for conclusions why an onerous liability should be recognized at the individual performance obligation when revenue is recognized over time. However, we still believe that recording an onerous performance obligation at inception of an overall profitable contract does not provide decision-useful information. In our view, the onerous liability test should be performed at the contract level at inception of the contract, subject to certain criteria being met. In the ordinary course of business, entities enter into loss-making individual performance obligations for various strategic reasons while the overall contract is profitable. Recording the impact of entering into a contract with a customer based on the overall profitability of the contract will better reflect the economics of the transaction. In other words, we do not believe that testing at the level of each separate performance obligations and requiring up-front recognition of a loss on some performance obligations, while recognizing profits later on other performance obligations, accurately depicts an entity's expected economic outcome for the contract.

We understand from the basis for conclusions that some of the reasons advocating against the use of the contract level as the unit of account for assessing an onerous performance obligation include, among others: (i) the complexity in determining what the contract level should be and (ii) the inconsistency with the level at which revenue is recognized. We believe that for the purpose of this test, the contract level should be a single contract unless the criteria for combining contracts is met as stipulated in the ED under paragraph 16 and 17.

After inception of the contract, subsequent onerous liability tests should be done at the performance obligation level as this would provide more useful information to financial statement users (subsequent to initial recognition, deterioration in the profitability of a performance obligation should not be carried to other performance obligations). This would also be consistent with how the revenue is recognized, as proposed in the ED.

We agree to limit the scope of the onerous liability to situations when revenues are recognized over time. However, we believe that clarification should be added regarding what principles should be applied for a performance obligation that an entity satisfies at a point in time. The basis for conclusions mentions that existing standards (e.g. IAS 2 *Inventories*) already provide requirements on how an entity should test for impairment of inventory that is subject to a sales contract. The basis for conclusions also points out paragraph 31 of IAS 2 *Inventories*; this paragraph refers to IAS 37 *Provision, contingent liabilities and contingent assets* where the accounting for onerous contracts is addressed. Therefore, we understand that the guidance of IAS 37 related to onerous

contracts would apply in that case. However, we believe that clearly mentioning this requirement in the ED would avoid confusion and misapplication.

***Contract costs – Clarification requested***

We agree with the Boards' proposition, however, we believe that clarification can be added on how accumulated costs shall be recognized to profit and loss for certain performance obligations satisfied over time. For such performance obligations, which could comprise a bundle of goods or services, entities could use different methods for measuring their progress towards completion (output or input methods). As various methods could be used for recognizing accumulated costs as expense, accounting outcomes could vary greatly as the ED does not specify how to account for accumulated costs.

For certain methods, such as the cost-to-cost method, we believe it is clear that costs would be recognized as incurred. However, if any other measurement methods are selected for recognizing revenue (e.g. output methods based on units of delivery or milestones), we believe there is not enough guidance provided to determine the amount of cost to be recognized at each revenue recognition event.

We recommend that additional guidance be provided with regard to this topic to help entities to establish how costs associated with the progression of their performance obligations should be recognized. We also believe companies should disclose their accounting policy for recognizing costs to profit and loss for performance obligations satisfied over time.

***Disclosure – We disagree***

Given the numerous contracts with customers in our industries, certain additional quantitative disclosures and tabular reconciliations of balance sheet amounts described in the ED, such as a reconciliation of contract balances, would impose a significant burden on entities while not providing decision-useful information to financial statement users. Our concern remains particularly acute in connection with the reconciliation of contract balances suggested in paragraph 117. Significant costs may be incurred as this information would have to be tracked at the performance obligation level, which would likely require modification of existing systems. In our view, such costs would largely outweigh any benefits that might be provided to the users of financial statements.

In addition, there is currently a wide diversity in practice in what is included in 'contract balances' and this diversity exists both across industries and within specific industries. The lack of standardization in accounting for contract costs will make such disclosure very confusing for users. Therefore, absent a comprehensive review of accounting for contract costs, the proposed disclosure should not be pursued.

***Interim reporting requirements - Question 5 – We disagree***

The ED proposes that certain annual disclosures be required on an interim basis, which comprises the disaggregation of revenues, reconciliation of contract balances, certain information related to performance obligations and onerous performance obligations.

While we recognize that these disclosures may be useful to financial statement users on an annual basis, we believe that providing such information on an interim basis will result in costs significantly outweighing the benefits.

Therefore, we suggest that interim disclosures be limited to the following:

- a disaggregation of revenue in a manner similar to the annual financial statements; and
- new material onerous performance obligations occurring during the period.

#### ***Disclosure of forecasted information – We disagree***

We believe the requirement to disclose forecasted information such as the aggregate amount of the transaction price allocated to remaining performance obligations significantly increases the scope of the financial statements and is inappropriate as the financial statements are prepared using historical financial results and information. This disclosure will be built using information based on an entity's projections and will result in having forward-looking data in audited financial statements. Furthermore, this level of information goes beyond what is currently provided to shareholders and analysts in the typical earnings guidance and would disclose sensitive information to our industry competitors.

Additionally, auditors would be required to audit long-range planning information that is subject to many changes and variability and that are often based on management's critical accounting estimates.

If the Boards still view this information as necessary, we would suggest requiring it be disclosed in the form of a qualitative discussion.

#### ***Transition – We disagree***

We are strongly concerned with the retrospective implementation approach proposed in the ED. We believe that in most instances in the industries in which we operate, retrospective application will be very difficult and costly to apply.

We recognize the importance of providing comparative information in order for financial statement users to understand entities' results. Therefore, we recommend that the Boards allow preparers to choose between a retrospective and a modified retrospective transition method according to their circumstances. The modified retrospective method would consist of entities converting all active revenue-generating contracts to the new standard on a single date and apply the new standard going forward. If such selected date is the date of initial application of the new standard, additional disclosure would be required consisting of management's best estimate of the comparative period impact. We believe this approach would provide investors with sufficient decision-useful quantitative and qualitative information about the effect of adopting the new standard on an entity's results, without the financial and process burdens to preparers associated with providing full retrospective presentation.

If the Boards believe that the retrospective implementation approach proposed in the ED is necessary, preparers will need more time than currently scheduled to implement the proposed requirements.

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Please do not hesitate to contact the undersigned if you wish to discuss our comments with us.

Best regards,

Signed in Montréal: Jean Paré

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