May 29, 2015
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116
Attn: Technical Director – File Reference No. 2015-240
(via Electronic Mail)

Re: Comments on Proposed Changes to Topic 606 of the FASB Accounting Standards Codification

Dear FASB Technical Director,

We, four representatives of the Contract Manufacturing industry, are responding to the Financial Accounting Standards Board’s (“Board”) invitation to comment on the above-referenced exposure draft. We welcome the opportunity to comment on the exposure draft and appreciate the Board’s decision to consider a deferral of the effective date of ASC Topic 606.

**Question 1:** Should the effective date of the guidance in Update 2014-09 be deferred for one year for public business entities, certain not-for-profit entities, and certain employee benefit plans? Please explain why.

**Question 3:** In addition to providing a one-year deferral of the effective date of the guidance in Update 2014-09, should the Board also provide an optional two-year deferral for all entities that apply that guidance retrospectively to each reporting period presented? Please explain why.

**Question 4:** Should earlier application of the guidance in Update 2014-09 be permitted as of the effective date originally included in Update 2014-09? Please explain why.

We strongly believe that 1) the effective date of the guidance in Update 2014-09 should be deferred for one year for all public business entities, 2) entities that apply the guidance retrospectively should be given an optional two-year deferral, and 3) early adoption should be allowed.

Comparability of financial statements aids users in analyzing the performance and position of a company relative to industry standards, and investing and lending decisions essentially involve evaluations of alternative opportunities, which cannot be made rationally if comparative information is not available. Because of the robust disclosure requirements of the new standard, together with current disclosure requirements for accounting standards pending adoption, we believe comparability can be maintained if companies elect to adopt the new standard at different times. Additionally, we believe comparability will ultimately be enhanced if entities are allowed sufficient time to
collaborate with industry peers and external audit firms to consistently apply the standard’s principles.

We believe deferral of the effective date is necessary for the following reasons:

- Significance of the new standard
- Timing of issuance of the new standard and related clarifications
- Scope and complexity of the new standard
- Implementation requirements associated with the new standard

**Significance of the New Standard**

Revenue is one of the most important financial statement elements. We greatly appreciate the Board’s time, effort, thoroughness and use of due process in developing a comprehensive, principles-based revenue recognition standard to replace today’s plethora of rules-based authoritative literature.

Just as it was important for the Board to take sufficient time to develop a comprehensive and improved standard, we believe it is equally important to allow sufficient time for companies to properly interpret and implement this important new standard. As discussed below, the complexities of the new standard, combined with the implementation requirements, will require a careful, thorough and planned interpretation and implementation to ensure credibility and reliability of this important financial statement element. Due to uncertainty regarding the ultimate decisions on key elements of the new standard, we do not believe entities could have sufficiently interpreted and planned their implementation in advance of the final standard and related interpretations and clarifications being issued.

A deferral of the effective date will allow all companies, regardless of the magnitude and extent of impact, to properly interpret and implement the new standard. Continued use of existing standards for an additional one-to-two year period will not negatively impact capital markets. Revenue under today’s accounting standards is generally well-understood by, and meets the needs of, the U.S. capital markets, which are generally regarded as the most stable, transparent and efficient capital markets in the world. On the other hand, restatements caused by improper interpretation and/or implementation will have a significant negative effect on the capital markets and could have ramifications (e.g., clawbacks) under the Dodd-Frank and Sarbanes-Oxley Acts.

**Timing of Issuance of the New Standard**

On May 28, 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, with an effective date for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period.

Absent a deferral, the new standard would be effective for 12/31 year-end companies at the beginning of calendar year 2017, a little over two years from the date the final
standard was issued. Although this may initially appear to provide a sufficient amount of
time to implement the standard, companies electing to apply the guidance retrospectively
would need to measure revenue under the guidelines of the new standard as early as the
beginning of calendar year 2015, a mere seven months from the date the final standard
was issued.

Further, in June 2014, the FASB and IASB announced the formation of the Joint
Transition Resource Group for Revenue Recognition (“TRG”). The objective of the TRG
is to inform the FASB and IASB about potential implementation issues that could arise
when companies implement the new standard.

As of the date of this letter, the TRG’s current projects include:

1. Identifying Performance Obligations and Licenses
2. Narrow Scope Improvements and Practical Expedients
3. Effective Date
4. Research Project: Principal versus Agent (reporting revenue gross versus net)

Based on the TRG’s efforts in these areas, the FASB has decided to 1) clarify how the
FASB and IASB intend certain guidance to be applied, 2) incorporate further
amendments in Topic 606 to address certain implementation issues and 3) make some
technical corrections to Topic 606. These important clarifications, amendments and
technical corrections have not yet been published.

A one-year deferral of the effective date of the new standard would mean that calendar-
year companies electing to apply the guidance retrospectively would need to measure
revenue under the guidelines of the new standard as of the beginning of calendar year
2016, which will be less than seven months from the date these critical clarifications,
amendments and technical corrections are published.

We believe a deferral of the effective date is necessary. This will allow all companies a
sufficient period of time to implement this significant and complex new accounting
standard.

Scope and Complexity

Unlike certain other new accounting standards, the new revenue recognition standard will
affect virtually all public business entities. The impact of the new standard will range
from minimal to significant, depending on the industry and specific nature of each entity.

We believe the effective date of the new standard needs to appropriately consider those
companies, such as contract manufacturers, for which the impact will be significant.
Minimally-to-moderately impacted companies can delay implementation without
consequence, but significantly impacted companies cannot unreasonably accelerate
implementation without consequence.
The creation of the TRG, in and of itself, is an indication of the complexity of the standard. The fact that the TRG, almost one year after formation, is still working on critical issues such as “identifying performance obligations” is a further indication of the complexity of the new standard.

This level of complexity will require companies to spend a considerable amount of time interpreting the new standard, which will involve numerous discussions with other companies in the same industry and external audit firms. We have had these discussions over the past two years, but progress has been slow due to the complexity of the standard and the significant amount of judgment allowed in critical areas of the standard.

**Implementation Requirements**

We represent the Electronics Manufacturing Services (“EMS”) industry. Companies in our industry are generally global providers of customized, integrated electronics manufacturing services. Industry-leading EMS companies offer end-to-end services, including product design and engineering, manufacturing, final system assembly and test, direct order fulfillment and logistics services, after-market product service and support, and global supply chain management. These end-to-end supply chain solutions encompass the entire lifecycle of a customer’s product, from product design and engineering, through manufacturing, to direct order fulfillment and after-market services and support. Customers may choose to use all or some of these services.

We typically conduct manufacturing operations in numerous facilities located in numerous countries and manufacture thousands of different products, consisting of complete systems or subsystems, including:

- Communications infrastructure equipment such as wireless and wireline access, filters, optical networking and transmission, radio access base stations, enterprise networking systems, and switching, routing and transmission systems.
- Computing and storage systems for both enterprise and cloud-based deployments, and security appliance products.
- Multimedia products such as digital set-top boxes, point-of-sale equipment, digital home gateways, professional audio-video equipment and internet protocol entertainment devices.
- Consumer products such as mobile devices (including smart phones), wearable electronics, game consoles, connectivity devices, notebook personal computing, tablets and printers.
- Industrial and semiconductor capital equipment, front-end environmental chambers, optical inspection and x-ray equipment, explosive detection equipment and large format printing plate machines.
- Defense and Aerospace products such as avionics systems and processors, weapons guidance systems, tactical and secure network communications systems and detection systems for homeland defense.
• Medical systems such as blood glucose meters, respiration systems, blood analyzers, ultrasound imaging systems and a variety of patient monitoring equipment.

• Automotive products such as engine control units, body controllers, radios, automotive lighting and power electronics, and HVAC control heads and blower modules.

Manufacturing services of large EMS companies are vertically integrated, allowing us in certain instances to build a finished product for our customer using both components manufactured by us and components purchased by us from other vendors. Components manufactured by EMS companies may include:

• Printed circuit boards (“PCBs”)
• Backplanes (very large PCBs that serve as the backbones of sophisticated electronics products) and backplane assemblies
• Enclosure systems, which are used to house and protect complex and fragile electronic components, modules and sub-systems
• Cable assemblies, which are used to connect modules, assemblies and sub-assemblies in electronic devices
• Precision machining
• Plastics
• Optical and Radiofrequency components and modules
• Memory modules, which are integrated subsystems that use industry standard integrated circuits

Once a customer’s product is ready for volume manufacturing, high volumes of identical units are manufactured to a customer’s unique specifications. The manufacturing cycle for the majority of products is less than two weeks. Contracts generally require the customer to provide us with a periodic forecast of their near-term production needs. Based on this forecast, we procure materials through the supply chain to ensure that sufficient materials will be available to meet our customer’s specific delivery requirements. Some of the materials used in the manufacturing process are unique to a customer’s product, and some are common to products of many customers. Our customers are generally contractually liable for materials we purchase to support their forecast requirements. We generally do not begin manufacturing activities until we receive a firm purchase order from a customer and are generally entitled to payment for work performed-to-date in the event an order is cancelled.

Today, in accordance with ASC Topic 605, Revenue Recognition, we generally recognize revenue upon delivery to the customer, provided all other revenue recognition criteria have been met by that time. Our systems, processes and controls are currently designed to support a revenue recognition model based on delivery (a point-in-time measurement),
which is objective and measurable and coincides with our billing activities and the timing of liability recognition by our customers.

Under the new standard, we believe that in the majority of instances we will be required to recognize revenue throughout the manufacturing process, which is a drastic departure from how / when we recognize revenue today.

In order to determine whether revenue should be recognized over a period of time or at a point-in-time, each contract must be reviewed to determine whether we have an enforceable right to payment for work-in-process upon termination of the contract. If we do, revenue must be recognized over a period of time; if we do not, revenue must be recognized at a point-in-time.

We have thousands of customers, many of which operate under numerous legal documents – for example, our contractual rights and obligations with respect to a customer relationship may be set forth in a combination of a master supply agreement, a local product agreement, our sales terms and conditions and the customer’s purchasing terms and conditions. Additionally, we may have a different contract with the same customer for each country in which we do business with the customer and for each product / service we provide for the customer.

Our contract-by-contract review will need to consider past business practices, the order of precedence of each legal document, the governing law of each such contract, the laws of the jurisdiction in which the customer resides, the jurisdiction in which we reside, and the jurisdiction in which we manufacture product / provide services. This will be a lengthy process and will require a significant amount of judgment to determine whether we have an enforceable right to payment for work-in-process upon termination of the contract.

We believe recognition of revenue over a period of time, as opposed to at a point-in-time, is “unnatural” for companies that manufacture high volumes of products with short manufacturing cycles. Therefore, implementation of systems, processes, internal controls, etc. to measure and recognize revenue throughout the manufacturing process will be extensive and time-consuming.

It is likely that a single manufacturing location could have some customers for which revenue is required to be recognized over a period of time and some customers for which revenue is required to be recognized at a point-in-time. To further complicate matters, a single customer may have some products for which revenue is required to be recognized over a period of time and some products for which revenue is required to be recognized at a point-of-time.

Needless to say, it will be a daunting, complex and time-consuming challenge from a systems, processes and internal controls perspective to accurately differentiate to this level of granularity.

Once we are systematically able to identify customers / products for which revenue should be recognized over a period of time, further differentiation will be required in order to identify specific situations for which recognition of revenue may not be
appropriate for work in-process. These situations may include those in which 1) manufacturing has begun before a contract has been concluded, 2) we are building “safety stock” units for which we do not have an enforceable right-to-payment, 3) manufacturing has begun before we have a right-to-payment for work-in-process under the contract – for example, we began manufacturing outside of the agreed-upon manufacturing lead time, etc.

Finally, we will have to determine how to measure revenue for work-in-process. This will inherently require a significant amount of judgment and significant use of estimates, thereby being highly susceptible to error and manipulation. For example, if an input method is used to measure revenue, the “mark-up” to apply to arrive at the appropriate amount of revenue will differ for each product and may change frequently since we typically negotiate new prices on a quarterly basis. Further, if a product being manufactured is a component of a higher-level assembly, the estimate of revenue would likely be different than it would be if that product was the final deliverable to the customer (i.e., was not being used in a higher-level assembly).

We are not aware of any company in our industry that currently has systems in place to systematically and accurately measure revenue on each product throughout the manufacturing process. Further, it is our understanding that software vendors are suspending development and issuance of new solutions until implementation guidance is finalized, which is not expected to occur until the end of 2015. Therefore, entities electing to apply the standard retrospectively will face severe limitations on their ability to run parallel systems for a period of two years prior to the effective date of the standard.

We understand that a principles-based standard will require more judgment than a rules-based standard. However, we are extremely concerned that, in our particular situation, the numerous layers of judgment (identifying the contract involves judgment, interpreting the contract with respect to an enforceable right to payment involves judgment, identifying performance obligations involves judgment, etc.) and estimates used to measure revenue will be highly susceptible to error and manipulation. Given the significant level of judgment and use of estimates introduced by the standard, as acknowledged by both the PCAOB and the public accounting firms, designing and implementing appropriate internal controls (including education and training) will require a sustained and intensive effort. Considering the importance of revenue to financial statements users, we believe it is important to allow sufficient time during the implementation process to design and implement systems, processes and internal controls that will significantly mitigate the risk of error and manipulation.

Summary

In summary, we appreciate the Board’s consideration of a deferral of the effective date of the new standard and are strongly of the view that it is in the best interests of reporting entities, users of financial statements and fair and efficient capital markets for the Board to permit a one-year deferral for all companies. Further, we hope the Board can further appreciate the complexities involved in analyzing, interpreting and implementing the
standard for entities for which the end result could be a wholesale change from how revenue is recognized today. As a result of the changes in processes, systems and internal controls that are required, we respectfully request that the Board also permit an optional two-year deferral for companies electing to retrospectively apply the principles of the new standard.

Sincerely,

Donald F. Adam
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Anila Grover
VP Finance and Corporate Controller
Celestica Inc. (foreign private issuer for U.S. reporting purposes; prepares consolidated financial statements in Canada and the U.S. in accordance with IFRS)

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