ST Marine
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Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M6XH

Dear Sirs,

Exposure Draft ED/2010/6 *Revenue from Contracts with Customers*

1. Thank you for providing us the opportunity to comment on the Exposure Draft *Revenue from Contracts with Customers* (the "ED").

2. While we understand that the proposed decision to develop a single revenue recognition model that would apply to a wide range of industries would improve comparability of financial statements across entities, we are writing to you to express our concerns relating to the following issues:

   - the identification of separate performance obligations;
   - the use of the concept of transfer of control to recognise revenue; and
   - the accounting for warranty for defects.

3. In this regard, we would like to provide our comments specifically to questions 2, 3 and 15 of the ED. The requirements to identify and account for the performance obligations in a single contract separately, the use of the concept of transfer of control to recognise revenue and the need to defer a portion of the revenue for the vessel's component expected to be replaced or repaired, are likely to have an impact on the way Singapore Technologies Marine Ltd (ST Marine) recognise revenue for our shipbuilding contracts[1]. Currently, ST Marine recognises revenue from long-term contracts using the percentage of completion method.

[1] The services provided by ST Marine in a shipbuilding construction project typically include the following: planning, design, engineering, procurement, fabrication, construction, testing and commissioning of vessels.

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4. In respect of the identification of separate performance obligations, we do not believe that multiple performance obligations exist in our shipbuilding contracts and we respectfully request that the ED be modified to more clearly and affirmatively state that a single performance obligation may exist for certain long-term contracts. We believe that the standard should allow for the determination of a single performance obligation as a possible outcome when contract activities are performed in an overlapping, concurrent and/or highly interrelated manner and the pricing of the related activities is not distinct or readily determinable in the market. As drafted, the ED would result in the identification of multiple performance obligations in our long-term contracts. However, we do not believe that users of our financial statements or our customers view our contracts in this manner.

5. By their nature, shipbuilding contracts are individually unique in both their design and execution, such that the terms, conditions and deliverables are not comparable to terms, conditions and deliverables of contracts used in other industries. We believe that for shipbuilding contracts in which we perform various tasks over multiple phases that are overlapping, concurrent and/or highly interrelated, such goods or services, or tasks performed, are generally not distinct. Such tasks are merely interdependent steps in the overall process of delivering the vessel to the customer.

6. In shipbuilding contracts, tasks are regularly performed as a bundled set of services or activities with a single objective: the delivery of the vessel to the customer in accordance with their specifications. Accordingly, in situations where we do not price the tasks individually, we and our customers do not separately negotiate the individual tasks when we establish the total value of the contract, and when the tasks are managed in an overlapping, concurrent and/or highly interrelated manner, the rebuttable presumption is that the contract represents a single performance obligation.

7. Consequently, we do not believe that the separate tasks within the bundled set of services or activities should always, or by a default treatment, be determined to be "distinct" and accounted for separately just because, on occasion, we might be asked and agree to perform only one task that could be viewed by some as "similar." Accordingly, the pricing of the individual tasks, depending on the facts and circumstances including the intentions of the parties and our respective business models and the type of negotiation we enter into with our customers, will vary widely from one project to the next. Consequently, there is not a standard margin realised from one project to the next.

8. In their simplest form, we believe that shipbuilding contracts in our industry regularly contain just one performance obligation: a single project that is a representation of what the entity promises to provide in the shipbuilding process and what the customer specifies and expects to receive.

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9. In respect of the use of the concept of transfer of control to recognise revenue, we are of the opinion that the indicators of control stated in the ED are unclear, narrow and difficult to apply to most long-term contracts. Based on the proposed definition in the ED, control is transferred to customer when:

(a) the customer has the ability to direct the use of the asset, i.e. the present right to use the asset for its remaining economic life; or to consume the asset in the customer's activities; and

(b) the customer has the ability to receive the benefit from the asset, i.e. the present right to obtain substantially all of the potential cash flows from that asset (either cash inflow or reduction in cash outflow) through use, sale, exchange etc.

10. In ST Marine's case, it is not clear whether there is continuous transfer of control (though we believe there are) under the proposed definition. Having said that, we do not believe that completed contract method is the basis that we should apply to recognise revenue. We believe that the accounting reality of performing long-term contracts is that revenue and profit/loss are earned continuously as the work progresses. The continuous earnings process is a more realistic accounting concept to represent the contractual agreement between contractors and customers than is the transfer of control at interim points during the performance of a contract or at the completion of the contract.

11. We had recently participated in the IASB Outreach Meeting held in Singapore on 5 October 2010. In the Board's presentation slides for "Exposure Draft, Revenue from Contracts with Customers", slide #12 states that "for development or construction contracts, revenue recognized continuously only if customer controls WIP." The presenter, Wayne Upton (IASB Director of International Activities), also shared with us some indicators of customers having control over the work-in-progress (WIP). Thus, even though the ED has limited guidance on the indicators of continuous transfer of control, based on our discussion with Wayne in the IASB Outreach Meeting, we believe we have met the continuous transfer of control criteria (and thus percentage of completion method can still be applied for our shipbuilding contracts) due to the following reasons and indicators:

- The designs of our vessels are customer-specific. ST Marine does not have the right to replace the design after it is accepted by the customer. This is consistent with the indicator specified under paragraph 30(d) of the ED.

- ST Marine requires the customer to pay for the work when the major milestones are met. This is an obligation of the customer. This is consistent with the indicator specified under paragraph 30(a) of the ED.

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12. In addition to the above, there is a provision in the contract that requires the customer (or an independent party engaged by the customer) to sign an acceptance certification at each major milestone in the contract where the customer actively participates in the periodic evaluation of the work completed to date. We believe this should be included as one of the indicators that the customer obtains continuous control over the WIP as work progresses.

13. As the ED does not provide clear guidance on the continuous transfer of control, this may have the unintended consequence of moving revenue recognition for long-term shipbuilding contracts to a completed contract method. This would pose the following two distinct issues to ST Marine in its recognition of shipbuilding revenue:

(i) Year on Year lumpiness in revenue and profit/loss figures; and
(ii) Distortion between value creation and financial numbers.

The lumpiness in the financials caused by recognising revenue in its entirety at the completion of construction may not portray the accurate financial performance of ST Marine for each financial period to its shareholders and the users of its financial statements. In addition, if revenue is not recognised as work progresses, there will be a distortion created between economic value generated by ST Marine based on the economic activities undertaken during the period vis-à-vis the financial numbers represented in the financial statements.

14. If the ED is adopted as a standard and we are not able to meet the control definition, we may not have revenue for up to 4 years even though we have continuously rendered our services in accordance with the contract. Moreover, the IASB should consider the implications the ED would have from the perspective of entities engaged in construction contracts and whether there is a scope for revenue recognition requirements to be further tailored according to different business models.

15. In respect of the accounting for warranty for defects, we provide a 12 months warranty to cover for defects or deficiencies concerning the vessel or parts which are caused by faulty design, defective material and/or poor workmanship on the part of the ship builder or its sub-contractors. Though a warranty is provided under the contract, we do not believe that our vessel has any defects at the time of delivery. This is due to the requirement to perform extensive testing and inspection by both the customer and the ship builder throughout the construction period.

16. In addition, after the vessel is completed, we would carry out sea trial in the presence of representatives from the Classification Society and/or Regulatory Bodies in a manner consistent with the specifications described in the contract and sufficient in scope and duration to enable all parties to verify and establish that all elements of the vessel are functioning in accordance with the specifications of the contract. Based on the results of the trial, the customer would sign an acceptance certificate accepting that the vessel conforms to the specifications of the contract. Since the vessel is not defective at the time of delivery, we believe we should recognise the entire revenue upon delivery.

17. We view the warranty that we provide to our customers as coverage for faults that arise after the vessels are transferred to the customers. According to the ED, we are required to assess if this warranty meets the criteria to be accounted for as a separate performance obligation. In our case, we do not believe that our warranty is a distinct service as neither ST Marine nor our competitors sell such a warranty to the customers separately. In addition, there is no distinct profit margin since the price for the warranty service is not negotiated separately.

18. We view our obligation to repair the vessel for defects caused by the above-mentioned reasons as business expenses which should be provided as a liability. This is consistent with the definition of provisions under IAS 37 – a provision is recognised for a legal or constructive obligation arising from a past event, if there is a probable outflow of resources and the amount can be estimated reliably. Since the ED does not provide guidance on how such warranty should be accounted for, we believe our type of warranty should continue to be accounted for under IAS 37.

19. We sincerely hope that you would agree with our opinion. In addition, we request that there be a re-examination of the issues raised by us relating to the identification of separate performance obligations, the use of the concept of transfer of control to recognise revenue and the accounting for warranty for defects, such that they are useful to portray the commercial substance of long term shipbuilding contracts and the performance of the Company.

Yours faithfully,

Ong Tek Liam
Senior Vice President/Group Financial Controller