Supplier finance arrangements: financial reporting considerations

Reporting update
5 April 2024, 24RU-05

In recent years, there has been calls for more transparency on how supplier finance arrangements affect an entity's liquidity risk, cash flows and financial liabilities.

In response, the AASB amended AASB 107 *Statement of Cash Flows* and AASB 7 *Financial Instruments: Disclosures* for entities to provide additional disclosures regarding supplier finance arrangements. These new disclosures are applicable for reporting periods beginning on or after 1 January 2024, with transition relief available.

While not in scope of the amendments, other financial reporting matters that entities with payables subject to supplier finance arrangements should take into consideration include:

- Presentation of liabilities on the balance sheet
- Classification and presentation of cash flows
- Disclosure of judgements and accounting policy information
- Impact on covenant compliance and other regulatory requirements

Supplier finance arrangements

Financial reporting considerations

April 2024

Supplier finance arrangements: financial reporting considerations

What's the issue?

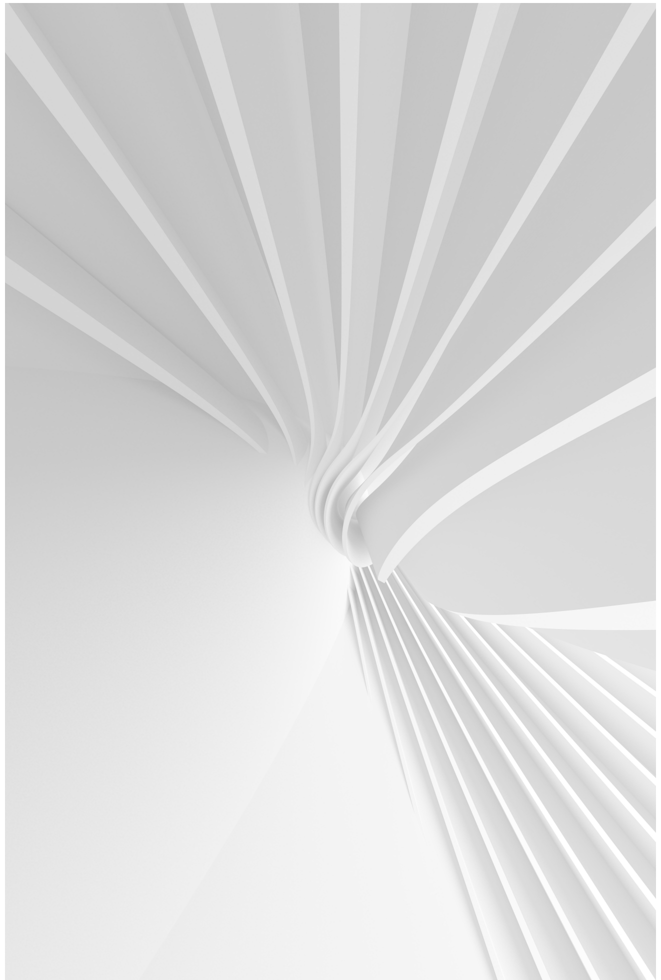
- Supplier finance arrangements are a common tool for managing working capital.
- In recent years, there were calls for more transparency on how supplier finance arrangements affect an entity's liquidity risk, cash flows and financial liabilities.
- In response, AASB 7 *Financial Instruments: Disclosures* and AASB 107 *Statement of Cash Flows* were amended to require disclosure of information that enables users: (a) to assess how supplier finance arrangements affect an entity's liabilities and cash flows; and (b) to understand the effect of supplier finance arrangements on an entity's exposure to liquidity risk and how the entity might be affected if the arrangements were no longer available to it.
- These new disclosures are applicable for reporting periods beginning on or after 1 January 2024, with transition relief available.

What's the impact?

- New disclosures include the terms and conditions of supplier finance arrangements, including carrying amounts of financial liabilities subject to these arrangements and the extent of which payments from finance providers have been made to suppliers.
- Information about these arrangements form part of management of liquidity risk disclosures.

What's next?

- Start collating data for new disclosures.
- Connect with finance providers to obtain information that may not be readily available. For example, the carrying amount of financial liabilities for which suppliers have already received payment from finance providers as at reporting date.
- To obtain this information, changes may be required to contractual arrangements to grant access.
- Plan for new processes and controls to ensure completeness and accuracy of collation of information.



What’s in this publication?

01 What is a supplier finance arrangement?

In scope

Supplier finance arrangements that are in the scope of the new disclosure requirements are arrangements where:

- a finance provider offers to pay the supplier of goods or services of an entity (the **buyer**), and
- the buyer agreeing to pay the financier at the same date or a later date.

For it to be in scope, the buyer has a liability to the supplier, and the finance provider is offering to pay that supplier.

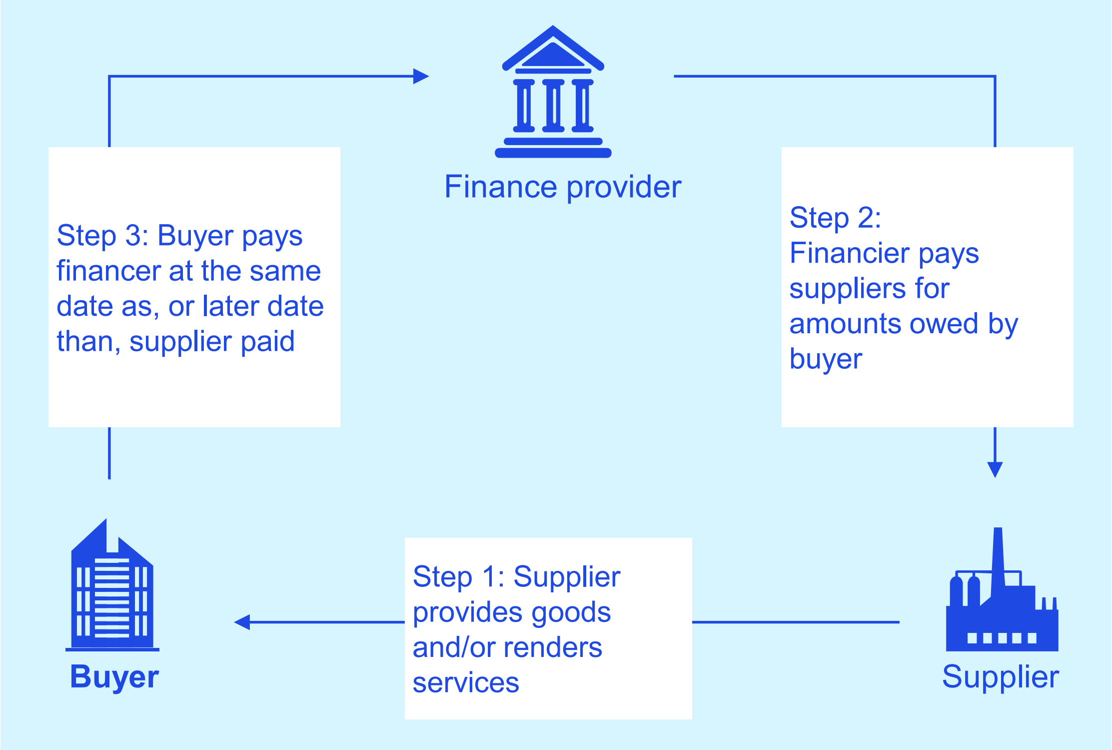
Supplier finance arrangements are a common working capital tool that allows buyers to:

- better manage cash flows and liquidity. This may be achieved by extending the payment terms including deferral of payment beyond the original payment date of the supplier's invoice, and
- streamline the accounts payable process as the buyer typically only has to make a single monthly payment to the finance provider rather than managing the payment of each individual supplier's invoices.

Supplier finance arrangements are also referred to as "supply chain finance", "payables finance" or "reverse factoring".

The new disclosures apply to the buyer's financial report.

A typical supplier finance arrangement is illustrated below:



This Reporting Update focuses on the financial reporting considerations for the "**buyer**" in the supplier finance arrangement and is the term used throughout this document.

01 What is a supplier finance arrangement?

Out of scope

Other working capital arrangements that do not involve the financier paying **'amounts owed by an entity to its suppliers**' are not in scope.

Examples of working capital arrangements that are not in scope for the additional disclosure requirements include:

- receivable financing,
- inventory financing,
- solely credit enhancements (e.g., financial guarantees, letters of credits used as credit guarantees) for the buyer, or
- where an instrument such as a credit card is supplied to the buyer for it to use to settle directly with a supplier for the amounts owed

What is receivable financing?

Under **receivable financing**, the entity "sells" its receivables portfolio typically at a discount to a financer for a lump sum upfront, and the financier is entitled to the cash flows collected from the portfolio. If the receivables are not derecognised, funds received are generally presented as short-term borrowings.

What is inventory financing?

Under **inventory financing**, the entity has a short-term loan or revolving line of credit from a financier which enables the entity to pay its suppliers, and the inventory serves as collateral for the borrowing. These arrangements are not in scope as the financier is not offering to pay the buyer's suppliers. The amount is generally presented as short-term borrowings.

02 What are the new disclosure requirements?

New specific disclosure requirements

The buyer in a supplier finance arrangement discloses the following in aggregate:

a)	the terms and conditions of the arrangements (e.g., extended payment terms and security or guarantees provided) If terms and conditions are dissimilar, they should be disclosed separately.
b)	as at the beginning and end of the reporting period:
i.	the carrying amounts, and associated line items presented in the balance sheet, of the financial liabilities that are part of a supplier finance arrangement.
ii.	the carrying amounts, and associated line items, of the financial liabilities disclosed under (i) for which suppliers have already received payment from finance providers.
iii.	the range of payment due dates (e.g., 30–40 days after the invoice date) for both the financial liabilities disclosed under (i) and comparable trade payables that are not part of a supplier finance arrangement. Comparable trade payables are, for example, trade payables of the entity within the same line of business or jurisdiction as the financial liabilities disclosed under (i). If ranges of payment due dates are wide, an explanatory information about those ranges or additional ranges (e.g., stratified ranges) are disclosed.

Illustrative disclosures

Qualitative information

The Group participates in a supply chain financing arrangement (SCF). Under the arrangement, a bank agrees to pay amounts to a participating supplier in respect of invoices owed by the Group and receives settlement from the Group at a later date. The principal purpose of this arrangement is to facilitate efficient payment processing and enable the willing suppliers to receive payments from the bank before the invoice due date.

Quantitative information

	End of reporting period 31.12.2024	Beginning of reporting period 1.1.2024
Carrying amount of liabilities that are part of supplier financing arrangements		
Presented within trade and other payables.	$xxx	$xxx
- of which suppliers have received payment from finance provider	$xxx	$xxx
Range of payment due dates		
Liabilities that are part of the arrangement	XX-XY days after invoice date	XZ-ZX days after invoice date
Trade payables that are not part of an arrangement	YY-YX days after invoice date	YZ-ZZ days after invoice date

02 What are the new disclosure requirements?

Impact of non-cash changes

Under the amendments, buyers disclose the impact (include quantitative information) of non-cash changes on the carrying amounts of financial liabilities relating to supplier finance arrangements as at the beginning and end of the reporting period.

Examples of transactions that may have a non-cash impact on the carrying amount of liabilities relating to supplier finance arrangements include:

- effect of business combinations (e.g., the acquiree has supplier finance arrangements),
- exchange differences (e.g., the financial liabilities subject to supplier finance arrangements are denominated in foreign currencies), or
- other transactions that do not require the use of cash or cash equivalents.

Illustrative disclosure

There were no material business combinations or foreign exchange differences or other non-cash transfers relating to the carrying amount of liabilities subject to supplier finance arrangements.

Impact on management of liquidity risk

As part of the information on how a buyer manages its liquidity risk, an entity considers and discloses whether it has access to supplier finance arrangements. This includes whether it has accessed, or has access to, supplier finance arrangements that provide the buyer with extended payment terms or the entity's suppliers with early payment terms.

Additional guidance on how to identify whether there is concentration of liquidity risk is also included. Some of the factors to consider are as follows:

- Repayment terms of financial liabilities,
- sources of borrowing facilities,
- reliance on a particular market to realise liquid asset; or
- **concentration of finance providers for supplier chain arrangements.**

Illustrative disclosure

The Group also participates in a supply chain financing arrangement (SCF) with the principal purpose of facilitating efficient payment processing of supplier invoices. The SCF allows the Group to centralise payments of trade payables to the bank rather than paying each supplier individually. While the SCF does not significantly extend payment terms beyond the normal terms agreed with other suppliers that are not participating, the programme assists in making cash outflows more predictable.

02 What are the new disclosure requirements?

Application

The amendments are effective for annual reporting periods beginning on or after 1 January 2024.

These new disclosures are not required for interim financial statements. There are no changes to AASB 134 *Interim Financial Reporting*.

Transition relief

The requirements are not applicable to interim financial reports prepared in the first year of adoption. For example, a buyer with a 30 June year end does not need to include the disclosures in its 31 December 2024 interim report.

Comparative information is not required for the first applicable annual financial report. For example, an entity with an annual reporting date of 30 June 2025 is not be required to present 30 June 2024 comparative information.

Entities also do not have to disclose the following information **as at the beginning of the first annual reporting period:**

- the range of payment due dates for financial liabilities subject to supplier financing arrangement and comparable trade payables, and
- the extent of the carrying amount of the financial liabilities of which payments from finance providers have been made to suppliers.

For example, an entity with an annual reporting date of 30 June 2025 is not required to disclose the extent of the carrying amount of financial liabilities as at 1 July 2024 of which payments have been made to the suppliers by the finance providers.

03 Other considerations

There are other factors to consider when accounting for supplier finance arrangements. These include the presentation on the balance sheet and the cash flow statement. These are not addressed in the amendments.

This section is a summary of the considerations for both the balance sheet and cash flow statement. Refer to KPMG's *Insights into IFRS 20th Edition* for more in-depth discussion (2.3.190.45, 7.6.465, 7.10.35.75-80).

How is a liability that is part of a supplier finance arrangement presented on the balance sheet?

IFRIC discussed the presentation of liabilities that are part of such arrangements on the balance sheet. They noted that a buyer presents liabilities that are part of supplier finance arrangements:

- as trade and other payables only when those liabilities have similar nature and function as trade payables – for example when those liabilities are part of the working capital used in the buyer's normal operating cycle, and
- separately when the size, nature or function makes separate presentation relevant to an understanding of the buyer's balance sheet.

How are cash flows classified and presented?

Some users of financial statements refer to cash flow statements to determine the quality of earnings of an entity. Hence, how supplier finance arrangements are disclosed in the cash flow statement may be a focus area for these users.

There is no specific guidance on whether payments in supplier finance arrangements are operating or financing in nature. In our view, the nature of the activity to which a cash flow relates rather than the classification of the related item in the balance sheet should be the primary determining factor for the appropriate cash outflow presentation.

In addition, in our view, buyers apply judgement whether there is a single cash outflow or multiple cash flows. In practice, buyers generally present a single operating cash outflow.

03 Other considerations

Judgement and accounting policy

Buyers consider disclosing material accounting policies and significant judgements about supplier finance arrangements.

Illustrative disclosure

The Group has not derecognised the original liabilities to which supplier finance arrangements apply because neither a legal release was obtained nor was the original liability substantially modified on entering into the arrangement. From the Group's perspective, the arrangement does not significantly extend payment terms beyond the normal terms agreed with other suppliers that are not participating. The Group does not incur any additional interest to the bank on the amounts due to the suppliers. The Group therefore discloses the amounts factored by suppliers within trade payables because the nature and function of the financial liability remain the same as those of other trade payables but discloses disaggregated amounts in the notes. All payables under supplier finance arrangements are classified as current as at 31 December 2024.

The payments to the bank are included within operating cash flows because they continue to be part of the normal operating cycle of the Group and their principal nature remains operating – i.e. payments for the purchase of goods and services. The payments to a supplier by the bank are considered non-cash transactions and amounted to $XX (2023: $XX).

How may supplier finance arrangements impact covenant compliance?

The buyer may also have to consider the impact of supplier finance arrangements on its debt covenants. Such arrangements may be classified as debt instruments under the covenant conditions and hence increases the risk of a covenant breach. Further complexities arise when covenants rely on "trade payables" or "debt" as defined by the accounting standards, as accounting standards do not define these terms.

For example, the debt covenants for indebtedness or gearing ratios may exclude amounts payable to suppliers or exclude the trade payables as disclosed on the balance sheet but include any amount that is considered debt or borrowing.

In some instances, a legal opinion may be required to confirm whether an arrangement falls within the scope of the debt covenant conditions.

What about other regulatory requirements?

Under *Payment Times Reporting Act 2020*, large businesses and government enterprises are required to report to the new Payment Times Reporting Regulator their payment practices to their small business suppliers, including whether supplier finance arrangements are being offered to suppliers.

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