



Snapshot

by Capital Markets & Accounting Advisory Services (CMAAS)

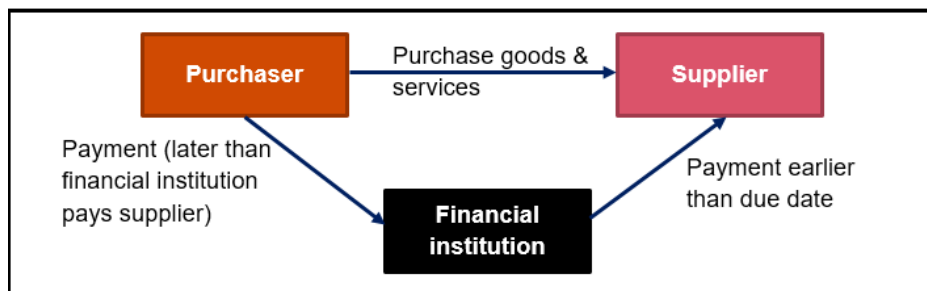
August 2020

IFRIC deliberated how to present reverse factoring in the financial statements



What is reverse factoring?

Reverse factoring is a common form of supply chain financing in which a financial institution commits to pay the supplier of goods or services purchased by the entity (purchaser), usually on a date earlier than the original due date and at a discount. The purchaser is paying the financial institution at a later date depending on the specific arrangement, such as on the original due date to the supplier.



What is the issue?

Transactions for purchasing goods or services from suppliers in credit under ordinary course of business are presented as trade payables in the statement of financial position, and its settlements are classified under operating cash flows in the statement of cash flows. Purchaser needs to relook whether this presentation of trade payables continues to be appropriate under a reverse factoring arrangement.

In April 2020, IFRS Interpretation Committee* ("IFRIC") was asked to provide guidance for presentation of liabilities when a purchaser entered a reverse factoring arrangement where payments are due to a financial institution instead of the suppliers. There is diversity in practice and lack of disclosures for reverse factoring.

* The IFRIC is the interpretative body of the International Accounting Standards Board ("IASB"). It works with the IASB in supporting consistency in application of IFRS Standards (MFRSs issued by the MASB are equivalent to IFRSs). IFRIC issues agenda decisions when it determines that IFRS Standards are clear and provide adequate principles on the accounting for the issue submitted. Agenda decisions often include explanatory materials to help entities in applying IFRS Standards.



IFRIC's analysis of accounting for reverse factoring

In its June 2020 meeting, the IFRIC identified guidance from the existing IFRS and analysed its application to the presentation of reverse factoring arrangements in the statements of financial position and cash flows, as well as the disclosures in the financial statements.

Presentation in the statement of financial position

When determining the presentation of liabilities that are part of reverse factoring, the purchaser should assess whether the size, nature or function of those liabilities are different compared with the typical terms of its trade payables which are not subject to reverse factoring arrangement. IAS 1 *Presentation of Financial Statements* (MFRS 101 is equivalent) requires financial liabilities with dissimilar nature to be presented separately from trade payables.

At June 2020 meeting, the IFRIC tentatively determined that a financial liability to be presented as a trade payable only when it:

- a. represents a liability to pay for goods or services;
- b. is invoiced or formally agreed with the supplier; and
- c. is part of the working capital used in the entity's normal operating cycle.

Derecognition of financial liability

When existing trade payables are part of the reverse factoring arrangement, the purchaser shall apply the requirements in IFRS 9 *Financial Instruments* (MFRS 9 is equivalent) to determine whether the derecognition criteria is met.

A financial liability is derecognised when:

- a. the liability is extinguished when the obligation is discharged, cancelled or expired; or
- b. there has been a substantial modification of the terms of the financial liability.

If the purchaser derecognises the trade payable and recognises a new financial liability to the financial institution, it would then assess, applying the principles in IAS 1 (MFRS 101 is equivalent), whether the nature or function of the new financial liability is sufficiently different from that of trade and other payables to be presented separately.

Presentation in the statement of cash flows

Classification of reverse factoring in the statement of cash flows would follow the presentation of the liability in the statement of financial position. Settlement of the liability is classified as operating cash flows if the liability continues to be presented as trade payable and is classified as financing cash flows when the liability is reclassified as other financial liability.



IFRIC's analysis of accounting for reverse factoring (continued)

Disclosures

The purchaser should consider disclosure requirements in relevant standards to reflect the effects of reverse factoring arrangement. For example, IAS 1 (MFRS 101 is equivalent) requires the purchaser to disclose judgements that management has made in respect of how to present liabilities and cash flows related to reverse factoring, and additional information about the arrangement that is relevant to an understanding of financial statements. IFRS 7 *Financial Instruments: Disclosures* (MFRS 7 is equivalent) also requires disclosure for exposure of liquidity risk, which reverse factoring could result in concentration risk of liabilities with one financial institution rather than a diverse group of suppliers.



IFRIC's tentative agenda decision

To sum it all up, stakeholders are seeking for consistency and transparency in the presentation and disclosures to be improved to provide them with relevant information about reverse factoring programs.

The tentative agenda decision is open for comments till 30 September 2020 on [IASB website](#). Alternatively, comments can be submitted through the [MASB](#) before 28 August 2020.

Do you need further information on this topic?

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