

IFRS Alert

Bringing transparency on
supplier finance

11 January 2024

Key points

Supplier finance arrangements provide companies with solutions for managing working capital. As the use of these solutions expands, it has become increasingly important that investors have transparency over the effect on a company's liabilities, cash flows and exposure to liquidity risk.

Starting in 2024, IFRS reporters will be required to provide additional disclosures about these arrangements to fulfil those investor needs.

This alert tells you what you need to know to account for supplier finance arrangements.

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1. Introduction



To efficiently manage working capital, some companies look for solutions to extend the term of their trade payables. Supplier finance arrangements are an example of an agreement between a company (as the buyer), its supplier and a bank (or other finance provider) that can serve several purposes:

1. to extend the buyer's payment terms, by having a payment date to the bank later than the original due date of the invoice;
2. for the bank to act as the buyer's paying agent, and to pay the buyer's suppliers on its behalf on the date the payables are due;
3. to provide liquidity to the buyer's suppliers seeking payment before the due date.

These arrangements can be substantial in size, and so it is important to understand the impacts that they can have on the financial statements—particularly for the buyer. There can be significant impacts on presentation in the statement of financial position and the cash flow statement, as well as disclosures.

Judgement and careful analysis of terms and conditions will often be needed when accounting for supplier financing arrangements. The fundamental underlying principle is to provide investors with clear and transparent information about material arrangements.

IAS 1 explains that: *“Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.”*

Materiality depends on the nature or magnitude of information, or both. An entity assesses whether information, either individually or in combination with other information, is material in the context of its financial statements taken as a whole.” [\[IAS 1 para 7\]](#).



2. Scope

What is a supplier finance arrangement?

Supplier finance arrangements often go by a number of names, including 'reverse factoring', 'supply chain finance' or 'payables finance'. A supplier finance arrangement is identified through its characteristics, rather than how it is labelled. A key characteristic is that three parties (that is, a buyer, a supplier and a finance provider) are interacting to achieve a financing objective for at least one of the parties [\[IAS 7 para 44G\]](#).

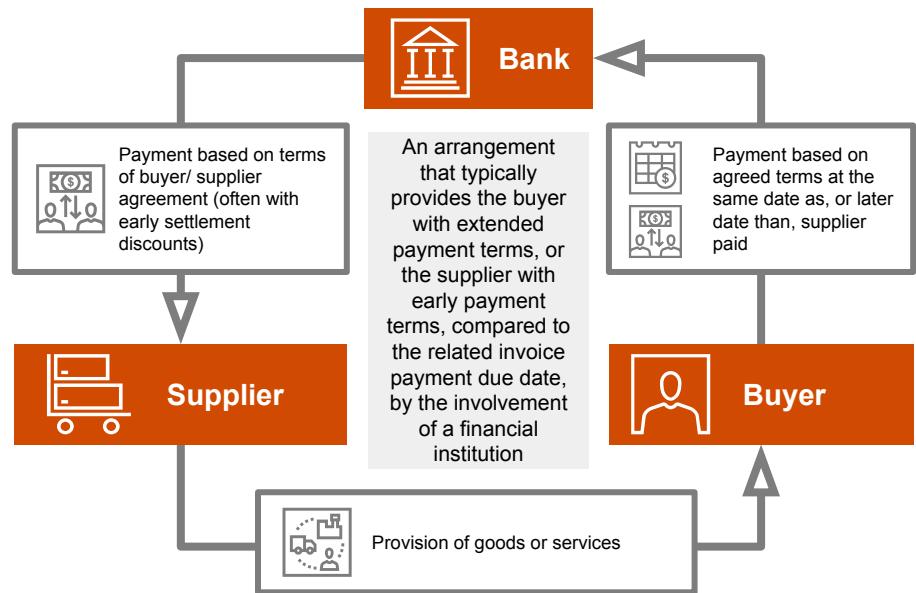
In many cases, it will be clear with little analysis whether an arrangement is supplier finance. However, it will be difficult to draw the line in other cases.

For the purpose of the specific supplier finance disclosure requirements (see Section 5), IFRS Accounting Standards explain that:

"Supplier finance arrangements are characterised by one or more finance providers offering to pay amounts an entity owes its suppliers and the entity agreeing to pay according to the terms and conditions of the arrangements at the same date as, or a date later than, suppliers are paid. These arrangements provide the entity with extended payment terms, or the entity's suppliers with early payment terms, compared to the related invoice payment due date." [\[IAS 7 para 44G\]](#).

2. Scope (continued)

Key steps in a supplier finance arrangement



A typical supplier finance arrangement will often include most or all of the following steps:

1. The supplier delivers goods to the buyer, creating a trade payable for the buyer and a trade receivable for the supplier.
2. The buyer confirms the trade payable - that is, confirms the amount, the due date, and the fact that the goods have been delivered and/or that it will pay the trade payable by the date agreed with the finance provider (depending on the arrangement in place, this might be by the due date or later).
3. The supplier's trade receivable is assigned or novated to the bank, in exchange for the buyer committing to pay the bank.
4. The supplier receives payment from the bank, either at the original due date or earlier.
5. The buyer pays the bank, typically on or after the due date of the invoice.



3. Recognition and derecognition

Recognition of a trade payable

The buyer recognises a trade payable liability when goods or services are purchased from the supplier. This is generally pretty straightforward.

Derecognition of the trade payable

IFRS 9 derecognition requirements apply to trade payables. When applying those requirements to trade payables included in supplier finance arrangements, careful consideration of all of the terms and conditions is required. Typically, one of the key questions is whether the buyer:

- continues to recognise that trade payable liability up until the point in time when the buyer pays the bank; or instead
- derecognises the trade payable liability, and replaces it with a new liability, when that trade payable becomes part of a supplier finance arrangement.

Applying IFRS 9, a financial liability (trading or other) is derecognised when it is extinguished (that is, when the obligation is discharged, is cancelled or expires) [\[IFRS 9 para 3.3.1\]](#). In addition, a substantial modification of the terms of an existing financial liability (or part of it) is an extinguishment of the original financial liability and recognition of a new financial liability [\[IFRS 9 para 3.3.2\]](#).

As such, the buyer in a supplier finance arrangement needs to assess whether the arrangement has substantially modified the trade payable, such that it should be considered as a new arrangement.

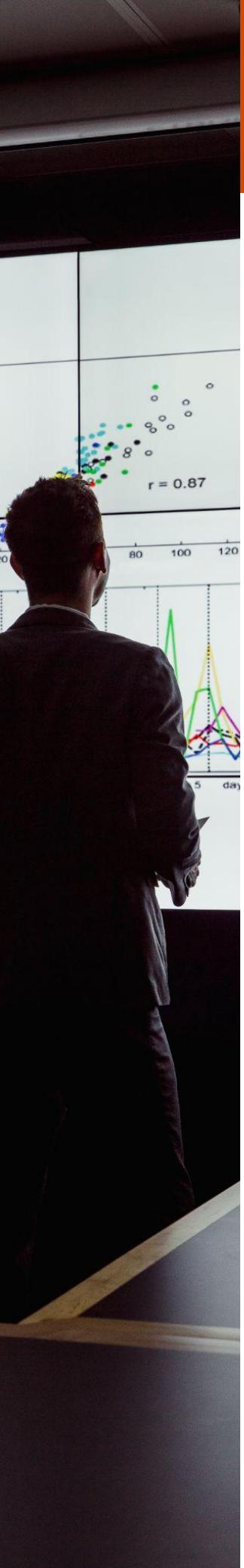
If the buyer derecognises a trade payable and recognises a new financial liability, the possible effects on the cash flow statement need to be carefully considered.

4. Measurement

If the buyer derecognises its original liability (the trade payable) and recognises a new liability with the bank (see Section 3), it will recognise:

- the new financial liability at fair value; and
- a gain or loss, based on the difference between the carrying amount of the original liability and the fair value of the new liability.

5. Presentation and disclosure



As mentioned above, the presentation of SFA arrangements in the statement of financial position and statement of cash flows sometimes require the application of judgement and careful analyses. In 2022, the IFRS Interpretation Committee (IFRC) issued an agenda decision on the presentation of financial liabilities that are part of SFAs.

Furthermore, in May 2023, the IASB issued amendments to IAS 7 and IFRS 7 to introduce new disclosure requirements for SFAs in financial statements. These amendments aim to enhance the transparency of SFAs and their effects on an entity's liabilities, cash flows and exposure to liquidity risk. The new disclosures include:

- i. the terms and conditions of SFAs;
- ii. the carrying amount of financial liabilities that are part of SFAs and the line items in which those liabilities are presented;
- iii. the carrying amount of the financial liabilities in (ii) for which suppliers have already received payment from the finance providers;
- iv. the range of payment due dates for both the financial liabilities that are part of SFAs, and comparable trade payables that are not part of such arrangements;
- v. the type and effect of non-cash changes in the carrying amounts of the financial liabilities that are part of SFAs; and
- vi. liquidity risk information (e.g. concentration of risks; access to SFA facilities for liquidity requirement).

New processes and controls may be required to ensure the complete and accurate gathering of relevant information for the disclosures above. These disclosure requirements are effective for annual reporting periods beginning on or after 1 January 2024 (earlier application is permitted).

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