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Supplier Finance Arrangements
Cover note

Objective

1 The objective of this session is to discuss and agree to recommend to the EFRAG FRB, a draft endorsement advice and invitation to comment on *Supplier Finance Arrangements (*Amendments to IAS 7 and IFRS 7) ('The Amendments') which were issued by the IASB on 25 May 2023.

Background

2 In November 2021, the IASB published its Exposure Draft on Supplier Finance Arrangements ('the ED'), which proposed amendments to IAS 7 Statement of Cash Flows and IFRS 7 Financial Instruments: Disclosures that would require entities to disclose additional information in the notes about Supplier Finance Arrangements ('SFAs').

3 EFRAG published its comment letter on the ED on 28 March 2022. In its comment letter, EFRAG broadly supported the IASB's project which enhanced the transparency of reporting for SFAs and increased conformity with existing disclosure requirements in IFRS Accounting Standards.

4 However, EFRAG considered that the IASB's proposals did not completely address the wider issue of presentation and classification of such arrangements in the primary financial statements, the necessary transparency on liquidity risk and working capital leverage. EFRAG also considered that, at a later stage, further efforts were needed in terms of reporting for such arrangements and encouraged the IASB to consider possible improvements related to SFAs in other cross-related projects.

5 In November 2022, the IASB considered the feedback received from respondents together with the IASB staff analysis and recommendations on how to proceed on the project and took a number of tentative decisions related to the proposed disclosure requirements in the ED.

6 On 18 January 2023, EFRAG FR TEG discussed the IASB's tentative decisions. In the agenda paper issued for that session (here), the EFRAG Secretariat summarised and analysed the IASB's ED proposals, the feedback obtained by the IASB, EFRAG's recommendations as included in its comment letter and the IASB's tentative decisions. In addition, we provide in Appendix 1 a summarised table that compare the provisions included in the Amendment with the proposals made by EFRAG in its comment letter.

7 In the meeting EFRAG FR TEG members acknowledged a broad spectrum of SFAs in practice and the following information about these arrangements was important:

(a) the amount drawn under the SFAs;

(b) the undrawn amount under the SFAs which had been secured by the entity; and

(c) the quantitative impact of the SFAs on the entity's statement of cash flows.

8 Members further made the following comments on:

(a) disclosure of the carrying amount and presentation of financial liabilities in an entity's statement of financial position that are part of SFAs - members were supportive of the proposed requirement. It was noted that there were already requirements in IAS 1 to cater for such disclosure.

(b) disclosure of the carrying amount of financial liabilities that are part of SFAs for which suppliers have already received payment from the finance providers - members generally supported the IASB's proposed disclosure requirement and observed that for SFAs initiated by the buyer the data generally would be easily available. Members further noted that it was an important piece of information without which the information provided for SFAs would be incomplete. Two members expressed concerns about the availability of this information for other types of SFAs and the costs associated with obtaining and auditing the data.

(c) disclosure of the range of payment due dates - two members were not sure how this disclosure requirement would be useful to users of financial statements. It was explained by the IASB representative that knowing the range of payment due dates would allow users to estimate the effects of SFAs on the entity's cash flows. The IASB representative also elaborated that having a weighted average of due dates would be more useful, however, setting up such a disclosure requirement would trigger questions about the actual calculation or the need to prescribe such a process. and potentially result in higher costs for preparers.

(d) relevance of the SFAs project for the statement of cash flows - members expressed regrets that the IASB did not require entities to provide information about the effects of these arrangements on the statement of cash flows. In particular, there were no specific IFRS requirements to provide the necessary information about non-cash movements in the statement of cash flows and access the liquidity risks associated with the reporting entity.

(e) materiality concept - members also discussed how the disclosures would apply under the materiality concept which is pervasive in IFRS Accounting Standards. Members observed that for SFAs auditors would take a smaller materiality threshold if the use or increased use of SFAs is considered material also from a qualitative angle, i.e., the information provided under SFAs could be considered immaterial only if a small amount of the financial liabilities is covered under the arrangement.

Amendments issued

9 On 25 May 2023, the IASB issued the Amendments which were approved for issue by 12 of 14 members of the IASB. Two members abstained from voting because of their recent appointment to the IASB.

10 An entity shall apply the Amendments for annual reporting periods beginning on or after 1 January 2024. Earlier application is permitted. An entity is not required to disclose:

(a) comparative information for any reporting periods presented before the beginning of the annual reporting period in which the entity first applies those amendments;

(b) most of the information explicitly required as at the beginning of the annual reporting period in which the entity first applies the Amendments (the entity has to disclose the beginning carrying amounts, and associated line items presented in the entity's statement of financial position, of the financial liabilities that are part of a supplier finance arrangement); and

(c) the information otherwise required for any interim period presented within the annual reporting period in which the entity first applies the Amendments.

11 The European Commission issued a letter on 26 May 2021 requesting EFRAG to provide advice on the endorsement of the Amendments (uploaded as paper 03-04). The letter does not identify specific additional issues to investigate.

12 A link to the IASB publication, on EFRAG's website, is provided under permission of the IASB and is only valid until the publication of the Amendments in the official journal. (here).

Draft endorsement advice

13 The EFRAG Secretariat has prepared a Draft Endorsement Advice (letter to the European Commission). The EFRAG Secretariat's initial assessment is that the Amendments meet the technical requirements for EU endorsement as set out in the IAS Regulation and that endorsing the Amendments is conducive to the European public good.

14 However, the EFRAG Secretariat has heard some concerns from constituents about the feasibility for an entity to disclose the information required under paragraph 44H(b)(ii) of the Amendments (the disclosure of the carrying amount of financial liabilities that are part of SFAs for which suppliers have already received payment). The aforementioned concerns are related to the availability of the information, as SFA agreements might prohibit an entity from obtaining it, and to the costs of obtaining and auditing the information. The IASB has introduced transition provisions (see paragraph 10 above) to mitigate this and enable preparers to modify their SFA agreements and adopt internal processes to gather the information.

15 To ensure that the information is available and that the costs of implementing the Amendments do not outweigh their benefits from an EU perspective, the EFRAG Secretariat intends to conduct the following outreach activities:

(a) Survey addressed to the EFRAG FR CFSS to inquire on the costs and benefits of the Amendments as well as on constraints in their jurisdictions for preparers to obtain from the finance providers and disclose the carrying amount of financial liabilities that are part of SFAs for which suppliers have already received payment;

(b) Consultation to the EFRAG User Panel to receive confirmation that the information required by the Amendments is useful; and

(c) Consultation to the EFRAG FIWG members (or other relevant persons within their companies/organisations) on the possibility for their organisations to provide entities with the data requested in paragraph 44H(b)(ii) when acting as a provider of finance in SFA covered by the scope of the Amendments.

16 When considering the Amendments, the EFRAG Secretariat notes that the scope of the Amendments now states that payments with credit cards are excluded from the scope of the Amendments.

17 The Amendments thus state in paragraph 44G 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. Supplier finance arrangements are often referred to as supply chain finance, payables finance or reverse factoring arrangements. Arrangements that are solely credit enhancements for the entity (for example, financial guarantees including letters of credit used as guarantees) or instruments used by the entity to settle directly with a supplier the amounts owed (for example, credit cards) are not supplier finance arrangements.

18 The EFRAG Secretariat is unsure whether the example with the credit card is a distraction when determining whether an arrangement is covered by the scope of the Amendments – or it is helpful.

19 The EFRAG Secretariat has not expressed concerns about the clarity of the scope of the Amendments in its outlined Draft Endorsement Advice. Different interpretations of the scope of the Amendments could result in one entity providing the disclosures required by the Amendments and another entity not – although the supplier finance arrangements are the same.

Questions for EFRAG FR TEG

20 Does EFRAG FR TEG have any concerns related to the clarity of the scope of the Amendments (following the inclusion of the example of credit cards)? If so, how should this be addressed in the draft endorsement advice?

Agenda Papers

21 In addition to this cover note, agenda papers for this session are:

(a) Agenda paper 03-02 – Draft letter to the EC regarding endorsement of Supplier Finance Arrangements (Amendments to IAS 7 and IFRS 7);

(b) Agenda paper 03-03 – Invitation to comment; and

(c) Agenda paper 03-04 – EC letter requesting advice on the endorsement of the Amendments.

Appendix A: Follow-up on EFRAG's comment letter recommendations

EFRAG views and recommendations	Amendments
SFA project approach	
EFRAG observed that the project did not completely address the wider issue of providing necessary transparency on liquidity risk and how entities leverage their working capital to effectively obtain finance. This includes presentation and classification in the statement of financial position, liquidity risk disclosures and relevance of the statement of cash flows in general. EFRAG suggested that further efforts are needed in terms of reporting of such arrangements in the primary financial statements and encouraged the IASB to consider possible improvements related to SFAs in the future.	The IASB decided to keep its initial approach to the SFA project as laid out in the ED. The IASB decided to keep the narrow scope of the project (disclosure-only project) and not to expand it by including presentation and classification of these arrangements in the statement of financial position, liquidity risk disclosures and relevance of the statement of cash flows in general. Notwithstanding the above, EFRAG notes that in July 2022, the IASB added to its research pipeline a project on the statement of cash flows and related matters.
Scope of SFA	
In its comment letter, EFRAG constructively supported the IASB's project on SFA to timely enhance the transparency of reporting of SFA. EFRAG also supported a narrow-scope project to develop specific disclosure requirements. EFRAG recommended that the IASB elevate paragraph BC8 of the ED to become part of the proposed amendments. This would strengthen the description of SFA by clarifying that both SFA providing early payment terms to suppliers and SFA providing extending credit terms to buyers are within the scope of the project.	The EFRAG Secretariat observes that the IASB decided not to amend the description of SFA by elevating paragraph BC8 of the ED as suggested by EFRAG. The EFRAG Secretariat acknowledges that the proposed description of an SFA already includes the key elements of paragraph BC8 of the ED. In addition, the IASB decided to add examples to illustrate payment arrangements or instruments excluded from the scope.
Disclosure objective and requirements	
EFRAG was generally supportive of the direction of the project to enhance transparency about SFA. However, EFRAG observed that future efforts are needed to address also classification and presentation of those arrangements in the statement of financial position and in the statement of cash flows.	*Disclosure objective* The IASB decided to add a reference to liquidity risk in order to improve the disclosure objective by referring to an entity's exposure to liquidity risk and risk management.

Disclosure objective EFRAG supported the IASB proposals to add an overall disclosure objective and specific disclosure requirements in IAS 7 to help users of financial statements assess the effects of SFAs on an entity's liabilities and cash flows. EFRAG further suggested that the disclosure objective be expanded to also include the effects of those arrangements on an entity's liquidity risk and financial performance. *Level of aggregation* EFRAG suggested the IASB to require entities to disclose aggregated information (when terms and conditions are similar) and require disaggregation at the level of a single arrangement when it is necessary in order to provide relevant information. *SFA for which suppliers have been paid* EFRAG observed that this information might not be available to entities in all cases or require incurring additional costs. EFRAG recommended to only require such disclosure when information is available without undue costs and efforts. *Other suggestions* EFRAG acknowledged that the IASB's proposals on disclosures would be beneficial for users. However, it recommended further improvements. ➢ to require disclosures that would enable users to understand cash flows arising from SFA in the statement of cash flows; ➢ to clarify the linkage between the definition of trade payables in IAS 37 and the proposed disclosures which relate to financing arrangements; ➢ to provide guidance to entities regarding disclosure of their accounting policies about SFA in addition to general requirement in IAS 1 to disclose material accounting policies; ➢ to clarify whether the range of payment due dates refer to payment due date to the finance provider or payment due date to the supplier;	The IASB decided to make no change to add a reference to 'materiality' or to the effects of supplier finance arrangements on an entity's financial performance. *Level of aggregation* The IASB decided to require an entity to aggregate information provided about its SFAs and to disaggregate information - if required - to avoid omitting or obscuring material information. *SFA for which suppliers have been paid* The IASB decided to proceed with requiring an entity to disclose the carrying amount of financial liabilities that are part of SFAs for which suppliers have already received payment from the finance providers. *Other decisions* The IASB decided to make no change to the proposal to require an entity to disclose the terms and conditions, and, in particular, to make no change to add the word 'key' to the proposal. The IASB decided to add no requirement for an entity to disclose the line item(s) for the statement of cash flows in which changes in financial liabilities that are part of SFAs are presented. The IASB decided to clarify that if the carrying amount of financial liabilities that are part of SFAs is presented in more than one line item, an entity would be required to disclose each line item and the associated carrying amount presented in that line item; and The IASB decided to clarify that when an entity discloses the range of payment due dates of financial liabilities that are part of a SFA and trade payables that are not part of such an arrangement, the financial liabilities and trade payables should be on a comparable basis.

➢ to require 'relevant' terms and conditions instead of all terms and conditions; ➢ to highlight that the materiality principle and the usefulness of information are the leading ones when reporting for SFA; ➢ to clarify the usage of the term 'financial liability' when applied to SFA (in particular about its presentation); and ➢ to elevate the explanation in paragraph BC19 of the ED.	
Examples added to disclosure requirements	
EFRAG agreed with the IASB proposal to add SFA as an example in paragraph 44B of IAS 7. This disclosure would emphasise that such disclosures are relevant for users to obtain better information about changes in liabilities arising from financing activities under SFAs. EFRAG agreed with the IASB proposal to add an example within the liquidity risk disclosure requirements in IFRS 7. This proposed disclosure would emphasise that such information is relevant for users to better assess the effects of SFAs on an entity's exposure to liquidity risk and its risk management. However, EFRAG observed that the concentration of liquidity risk might vary and recommended the IASB consider adding an explicit proposal that would require disclosure of concentration of risk to specific supplier finance provider(s) instead of supplier finance arrangements in general.	The IASB decided against proceeding with the proposed amendments to add SFA as example within the disclosure requirements about changes in liabilities arising from financing activities in paragraph 44B of IAS 7. The IASB decided to proceed with the proposed amendments to add SFA as an example within the disclosure requirements about liquidity risk in paragraph B11F(j) and IG18 of IFRS 7- without making those proposed amendments more prescriptive. The IASB also decided against proceeding with the proposed amendments in paragraph B11F(a) because the wording may imply that all SFA are lines of credit.