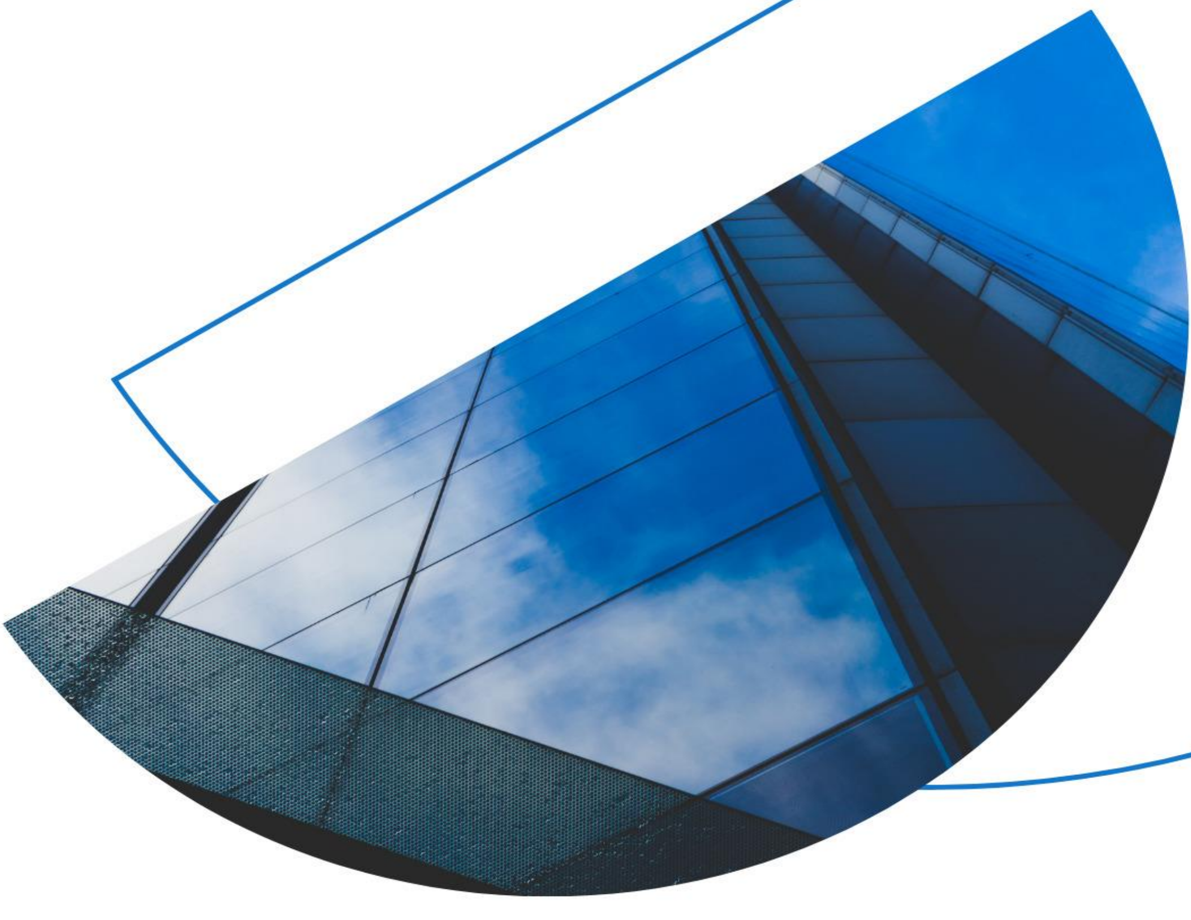
SUPPLIER FINANCE ARRANGEMENTS

Amendments to Ind AS 7 and Ind AS 107



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Supplier Finance Arrangements

INTRODUCTION

A supplier finance arrangement facilitates payments between a customer and its supplier for delivering goods and/or providing services. These are characterised by one or more finance providers offering to pay amounts a customer owes its suppliers and the customer agreeing to pay according to the terms and conditions of the arrangements at the same date, or a date later than, suppliers are paid. These arrangements provide the customer with extended payment terms, or the suppliers with early payment terms, compared to the related invoice payment due date, facilitating efficient payment processing of supplier invoices. Supplier finance arrangements are often referred to as –

1	2	3
Supply chain finance	**Payables finance**	**Reverse factoring arrangement**

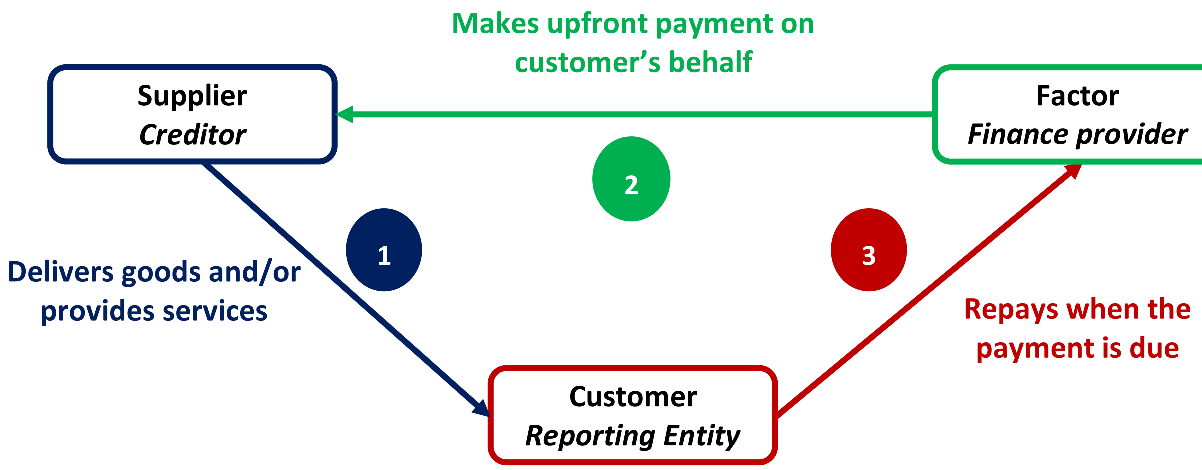
1. It optimises working capital for the customers and the suppliers.
2. A financial intermediary facilitates faster payment of supplier invoices.
3. A bank provides early payment to suppliers.

In most cases, the legal form of the supplier finance arrangement involves three parties, ie, the customer, the supplier, and the finance provider. One of the key characteristics of the supplier finance arrangement is that although it is generally initiated by the customer and the finance provider, these three parties interact together in achieving a financing objective. Arrangements that are solely credit enhancements for the entity, (eg, financial guarantees including letters of credit used as guarantees) or instruments used by the entity to settle directly with a supplier (eg, credit cards) are not supplier finance arrangements.

An entity shall disclose information about its **supplier finance arrangements** that enables users of financial statements to assess the effect of those arrangements on the entity's liabilities and cash flows and on the entity's exposure to ***liquidity risk*** (ie, the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset). Some factors to consider are sources of finance, repayment terms, extension period, etc

EXAMPLE 1

A finance provider (eg, a bank) agreed to make upfront payment for amounts owed by the customer (the reporting entity) to its supplier at a discounted amount and the customer will make payment to the finance provider when payment to the supplier is due or at the end of extended credit period. Therefore, under this arrangement, the finance provider may allow the customer to extend payment terms that optimises the working capital and improves the supplier's liquidity. Although, the amount payable to the bank is not technically a direct trade payable, it appears in the same line item as "Trade and other payables" in the Balance Sheet of the customer, when the liabilities are similar in nature and function to trade payables.



Ind AS 7

NEW DISCLOSURE REQUIREMENTS

Though a supplier finance arrangements is a debt-like liability (ie, off-balancing funding), these amendments do not require any accounting recognition for such an arrangement, but need significantly additional disclosures that apply only to the customer's financial reporting periods beginning on or after 1 April, 2025. An entity shall **disclose in aggregate for its supplier finance arrangements** –

(a) the terms and conditions of the arrangements (eg, extended payment terms and security or guarantees provided). However, an entity shall disclose separately the terms and conditions of arrangements that have dissimilar terms and conditions.

(b) as at the beginning and end of the reporting period:
   - (i) the carrying amounts, and associated line items presented in the entity's 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 the finance providers.
   - (iii) the range of payment due dates (eg, 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, eg, 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 entity shall disclose explanatory information about those ranges or disclose additional ranges (eg, stratified ranges).

(c) the type and effect of non-cash changes in the carrying amounts of the financial liabilities disclosed under (b) (i). Examples of non-cash changes include the effect of business combinations (ie, the acquiree has supplier finance arrangements), exchange differences (ie, the financial liabilities that are subject to supplier finance arrangements denominated in foreign currencies) or other transactions that do not require the use of cash and cash equivalents (ie, effect of non-cash changes in the carrying amount of the financial liabilities).

An entity is **not** required to disclose –

- comparative information for any reporting periods presented before the beginning of the annual reporting period in which the entity first applies those amendments.
- information stated at (b)(ii) and (iii) as at the beginning of the annual reporting period in which the entity first applies those amendments.
- information stated at (b) (ii) and (iii) for any interim period presented within the annual reporting period in which the entity first applies those amendments.

EXAMPLE 2

On 1 April 20x5, Entity A (the reporting entity) purchases goods from a supplier for CU 1,000. The period of credit is 3 months from the invoice date. This means that the amount is payable by Entity A on or before 30 June 20x5. Since the supplier enters into an arrangement with a bank (the finance provider) and Entity A is aware of this arrangement, Entity A is required to settle the liability directly with the bank on or before 30 June 20x5. The effect is that where the supplier is paid earlier by the bank, while the entity settles its obligation with the bank at a later date. The point to note is that Entity A is not required to consider financing actions taken independently by the supplier, ie, factoring its accounts receivable.

Entity A shall disclose information about its supplier finance arrangements that enables users of financial statements to assess the effects of those arrangements on the entity's liabilities and cash flows and on the entity's exposure to liquidity risk.

To meet the above objectives, Entity A shall disclose in aggregate for its supplier finance arrangements –

- ➢ the terms and conditions of the arrangement (eg, in this case, extended payment terms).
- ➢ as at the beginning and end of the period:
- the carrying amounts, and associated line items presented in the entity's balance sheet, of the financial liabilities that are part of a supplier finance arrangement.
- the carrying amounts, and associated line items, of the financial liabilities (disclosed above) for which the supplier has already received payment from the bank.

EXAMPLE 3

Same as Example No. 2. The exception is that at the inception of the contract (ie, 1 April 20x5), the supplier informs Entity A about the possibility of receiving an extension of the credit period (ie, from normal 3 months to 6 months), by virtue of the supplier's finance arrangement with the bank. The point to note is that the extended credit period offered to Entity A is directly tied to the supplier's finance arrangement with the bank. The effect is that the supplier issues an invoice of CU 1,025 and 6 months credit period. In substance, this is similar to (but not identical with) a borrowing arrangement (not a supplier finance arrangement). The additional amount payable is presented under borrowings, separately from payables. The corresponding interest expense is recognised in profit and loss.

When the range of payment due date is wider than the comparable trade payables that are not part of a supplier finance arrangement, an entity shall disclose, in addition, explanatory information about that additional range.

SAMPLE DISCLOSURE

Particulars	End of reporting period 31 March 20x6	Beginning of reporting period 1 April 20x5
Carrying amount of liabilities under supplier finance arrangement	***	***
Suppliers have received payment from the bank for the above	***	***
Interest rate charged by the bank	%	%
Normal credit period of liability that are not part of supplier finance arrangement	2 months	4 months
Extended credit period under supplier finance arrangement	4 months	4 months

Ind AS 107

DISCLOSURES

An entity shall apply this amendment when it applies the amendments to Ind AS 7.

An entity might consider in providing liquidity risk disclosures, whether it has –

- instruments that allow the entity to choose whether it settles its financial liabilities by delivering cash (or another financial asset) or by delivering its own shares;
- instruments that are subject to master netting agreements [1]; or
- accessed, or has access to, facilities under supplier finance arrangements (as described in Ind AS 7) that provide the entity with extended payment terms or the entity's suppliers with early payment terms. [2]

[1] *Master netting agreements are legal contracts allowing two parties to combine multiple financial transactions (eg, derivatives) into one net payment, reducing risk by consolidating obligations and enabling single – net settlement.*

[2] *This point has been newly inserted. Earlier two points already existed in Ind AS 107.*

SIGNIFICANCE OF THE AMENDMENTS

The main significance of the amendments is that there is a clear distinction between trade payables that are not part of a supplier finance arrangement and those that are part of a supplier finance arrangement. The users of accounting information can better understand deferred payment structures and potential concentration risks, that helps to assess actual cash outflow timing versus supplier obligations. The other significance is that it enables an entity to maintain *third-dimensional consistency*, ie, benchmarking across entities in the same trade with and without such financing arrangement.