IFRS

STAFF PAPER

December 2020

IFRS® Interpretations Committee meeting

Project	**Supply Chain Financing Arrangements—Reverse Factoring**
Paper topic	Comment letters on tentative agenda decision

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Introduction

1. In June 2020, the IFRS Interpretations Committee (Committee) published a tentative agenda decision in response to a submission about reverse factoring arrangements. Specifically, the request asked:

   (a) how an entity presents liabilities to which reverse factoring arrangements relate (ie how it presents liabilities to pay for goods or services received when the related invoices are part of a reverse factoring arrangement); and

   (b) what information about reverse factoring arrangements an entity is required to disclose in its financial statements.

2. In a reverse factoring arrangement, a financial institution agrees to pay amounts an entity owes to the entity's suppliers and the entity agrees to pay the financial institution at a date later than suppliers are paid.

3. The Committee observed that IAS 1 *Presentation of Financial Statements* specifies requirements for the presentation of liabilities in an entity's statement of financial position. Paragraph 54 requires an entity to present 'trade and other payables' separately from other financial liabilities. 'Trade and other payables' are sufficiently different in nature or function from other financial liabilities to warrant separate presentation (paragraph 57 of IAS 1). The Committee concluded that an entity presents a financial liability 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.

4. In the statement of cash flows, an entity that has entered into a reverse factoring arrangement determines whether to classify cash flows under the arrangement as cash flows from operating activities or financing activities applying IAS 7 *Statement of Cash Flows*. The Committee observed that an entity's assessment of the nature of the liabilities that are part of the arrangement may help in determining the nature of the related cash flows as arising from operating or financing activities.

5. IAS 7 requires an entity to provide 'disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes'. The Committee observed that reverse factoring arrangements often give rise to liquidity risk and that IFRS 7 *Financial Instruments: Disclosures* requires disclosure of information about an entity's liquidity risk.

6. The Committee also highlighted the requirements in IAS 1 to (a) provide information about the judgements management has made that have the most significant effect on the amounts recognised in the financial statements, and (b) disclose information that is relevant to an understanding of the entity's financial statements, which for entities that enter into reverse factoring arrangements could include information about those arrangements.

7. Finally, at the June meeting the Committee discussed a possible narrow-scope standard-setting project to develop disclosure requirements for arrangements entered into to fund payables to suppliers.

8. The objective of this paper is to:

(a) analyse the comments on the tentative agenda decision; and

(b) ask the Committee whether it agrees with our recommendation to finalise the agenda decision.

9. There are two appendices to this paper:

   (a) Appendix A—Proposed wording of the agenda decision; and

   (b) Appendix B—Comment letters.

Comment letter summary

10. We received 22 comment letters by the comment letter deadline. All comments received, including any late comment letters, are available on our website[1]. This agenda paper includes analysis of only the comment letters received by the comment letter deadline, which are reproduced in Appendix B to this paper.

11. 18 respondents (Autorité des normes comptables (ANC), the Accounting Standards Committee of Germany (ASCG), the Bankers Association for Finance and Trade (BAFT), Comissão de Valores Mobiliários (CVM), David Hardidge, Deloitte, Eumedion, the European Securities and Markets Authority (ESMA), the Financial Reporting Council of Nigeria (FRC Nigeria), the Accounting Standards Board of the Institute of Chartered Accountants of India (ICAI), the Institut der Wirtschaftsprüfer in Deutschland (IDW), EY, the Financial Reporting Council (UK FRC), the Malaysian Accounting Standards Board (MASB), Mazars, Petrobras, PwC and Syngenta) agree with the Committee's decision to publish an agenda decision. Most agree with the Committee's analysis of the requirements in IFRS Standards, but some have comments on that analysis. The ANC says publishing an agenda decision would enhance consistent application and improve the reporting of information about reverse factoring arrangements.

12. Eight of those respondents (PwC, ANC, ESMA, Deloitte, IDW, UK FRC, Eumedion and Mazars) suggest continuing to work on a standard-setting project to develop requirements for disclosures about reverse factoring arrangements.

13. Fermat Capital Management (FCM)) suggest that the Committee not publish an agenda decision and, instead, that narrow-scope standard-setting be undertaken to

[1] At the date of posting this agenda paper, there were no late comment letters.

address presentation and disclosure of reverse factoring arrangements in financial statements. The European Leveraged Finance Association (ELFA) also suggests undertaking standard-setting to address presentation and disclosure of reverse factoring arrangements.

14. Some respondents suggest clarifying particular aspects of the tentative agenda decision.

15. Further details about the matters raised by respondents, together with our analysis, are presented below.

Should the Committee publish an agenda decision?

16. In June 2020 the Committee discussed a possible narrow-scope standard-setting project to develop disclosure requirements for arrangements entered into to fund payables to suppliers. Committee members provided their views on such a project.

17. At that meeting, the Committee decided to publish a tentative agenda decision highlighting the requirements in IFRS Standards that apply to reverse factoring arrangements. It was noted that feedback on the tentative agenda decision could provide further input regarding possible narrow-scope standard-setting—the Board could then consider this feedback in deciding whether standard-setting is needed to meet the information needs of users of financial statements (investors).

18. Respondents to the tentative agenda decision provide comments on the need for standard-setting (see paragraphs 61–69). In particular:

    (a) ten respondents suggest undertaking standard-setting—eight of those support doing so in addition to publishing an agenda decision; and

    (b) two respondents say standard-setting is not required.

Respondents' comments—undertaking only standard-setting

19. FCM suggests that a standard-setting project be undertaken because the Committee's tentative agenda decision does not adequately address the concerns about reverse

factoring arrangements raised in the submission. FCM says, without adequate disclosures:

(a) it is difficult to compare financial statements of entities that use and do not use reverse factoring;

(b) reverse factoring can obscure 'debt-like liabilities'; and

(c) reverse factoring can complicate default risk assessments by obfuscating the important distinction between operating and financing cash flows.

20. FCM says the current disclosures that entities provide are insufficient to meet the needs of investors, and make suggestions regarding standard-setting that could be undertaken to improve the information entities provide. Paragraphs 61–67 of this paper summarise those suggestions, together with standard-setting suggestions from other respondents.

Staff analysis

21. As noted in paragraph 69, we plan to bring a paper to the Board at a future Board meeting that will include all of the input and feedback on possible narrow-scope standard-setting with respect to supply chain financing arrangements. The Board will consider whether to add such a project, taking into account the feedback received and staff research undertaken as well as other financial reporting priorities already identified as the subject of a possible standard-setting project.

22. The question therefore is whether the Committee should publish an agenda decision on reverse factoring arrangements in addition to the Board's future consideration of whether to undertake standard-setting with respect to disclosure.

23. In our view, the Committee should publish an agenda decision that would include explanatory material. The *Due Process Handbook* notes that the objective of including explanatory material in an agenda decision is to improve the consistency of application of IFRS Standards. Feedback on the tentative agenda decision suggests that the explanatory material on reverse factoring arrangements is expected to achieve that objective.

24. In addition, we note that the tentative agenda decision deals with more than just disclosure—it also discusses presentation in the statements of financial position and cash flows. The Committee's tentative conclusion is that the principles and requirements in IFRS Standards provide an adequate basis regarding presentation in the statements of financial position and cash flows, and regarding for example liquidity risk disclosures. This conclusion does not however preclude consideration of whether additional, more specific, requirements—for example, regarding disclosure—might be needed to meet investor information needs in relation to supply chain financing arrangements.

25. We therefore recommend that the Committee publish an agenda decision outlining how an entity applies the existing requirements in IFRS Standards to reverse factoring arrangements.

The Committee's tentative conclusions

Presentation of financial liabilities subject to a reverse factoring arrangement

Respondents' comments

26. Some members of the Accounting Standards Board of the ICAI say it could be argued that the nature of liabilities subject to a reverse factoring arrangement are always sufficiently different from the nature of other financial liabilities, thereby requiring separate presentation in the statement of financial position.

27. In contrast, David Hardidge says many financial liabilities subject to reverse factoring arrangements remain in the nature of trade payables—in his view, the underlying obligation continues to be linked to the original purchase (even if now owed to the financial institution) and the due date is also linked to the original purchase date (even if later). He says a financial liability can be a trade payable even if not payable within 12 months.

Staff analysis

28. Paragraphs 21–26 of Agenda Paper 2 to the Committee's June 2020 meeting set out our views on the determination of how to present a financial liability subject to a

reverse factoring arrangement. IFRS Standards do not explicitly define ‘trade and other payables’; however paragraph 70 of IAS 1 and paragraph 11(a) of IAS 37 include descriptions of characteristics of trade payables. Based on those descriptions, we continue to agree with the Committee’s conclusion that a financial liability is a trade payable 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 an entity’s normal operating cycle.

29. We also continue to agree with the Committee’s conclusions that an entity presents:

(a) other payables together with trade payables only when those other payables have a similar nature and function to trade payables; and

(b) liabilities that are part of a reverse factoring arrangement separately when the size, nature or function of those liabilities makes separate presentation relevant to an understanding of the entity’s financial position.

30. In our view, it is not possible to conclude that the nature of all liabilities subject to a reverse factoring arrangement is *always* sufficiently different from the nature of other financial liabilities to warrant separate presentation as specified in paragraph 57 of IAS 1. To do so would go beyond the existing requirements in IFRS Standards. A spectrum of reverse factoring arrangements exist that can include very different terms and conditions. An entity may therefore need to apply judgement—considering the specific terms and conditions of the reverse factoring arrangement and of its other financial liabilities—in determining whether the size, nature or function of the financial liabilities subject to that arrangement is such that separate presentation is relevant to an understanding of the entity’s financial position.

Derecognition of a financial liability

Respondents’ comments

31. IDW, PwC and some members of the Accounting Standards Board of the ICAI say when a trade payable subject to a reverse factoring arrangement is derecognised

applying IFRS 9, an entity should not present any new liability as trade and other payables.

32. Some members of the Accounting Standards Board of the ICAI note that the new liability would be payable to the financial institution—not the supplier of the goods and services—and therefore say the new payable is not a trade or other payable. IDW refers to the requirements for legal extinguishments as well as substantial modifications of financial liabilities in IFRS 9—it says a targeted qualitative assessment with respect to substantial modifications may warrant the derecognition of trade payables subject to reverse factoring arrangements. Shady Mehelba suggests that paragraph B3.3.4 of IFRS 9 may be relevant.

33. SOCPA says when an entity enters into a reverse factoring arrangement, it derecognises its trade payable and recognise a loan payable (loans payable are defined in IFRS 7 as 'financial liabilities, other than short-term trade payables on normal credit terms'). SOCPA says liabilities subject to a reverse factoring arrangement are not trade and other payables and permitting the presentation of such liabilities as trade and other payables in an agenda decision will promote diverse presentation practices.

34. Mazars says the Committee should clarify the extent to which any new liability recognised on derecognition of a financial liability subject to a reverse factoring arrangement must be classified as other financial liabilities (rather than as trade and other payables).

Staff analysis

35. The tentative agenda decision says that an entity that derecognises a trade payable to a supplier and recognises a new financial liability to a financial institution applies IAS 1 in determining how to present that new liability in its statement of financial position. An entity therefore applies IAS 1 in determining whether the new financial liability is a trade or other payable or another financial liability for the purposes of presentation in the statement of financial position. As discussed in paragraph 28 of this paper, paragraph 70 of IAS 1 and paragraph 11(a) of IAS 37 include descriptions of characteristics of trade payables.

36. In our view, the description of a trade payable in paragraph 11(a) of IAS 37 does not require the liability to be payable to the supplier. The description requires only that the financial liability be a liability ‘to pay for goods or services that have been received or supplied and have been invoiced or formally agreed with the supplier’. Therefore, in our view it would go beyond the existing requirements in IFRS Standards to state that an entity must present as other than trade and other payables *all* new financial liabilities recognised on derecognition of financial liabilities subject to reverse factoring arrangements.

37. IFRS 7 refers to loans payable only in paragraph 18—that paragraph requires particular disclosures relating to defaults and breaches of loans payable. In our view the definition of loans payable in IFRS 7 is irrelevant in determining how an entity presents financial liabilities in its statement of financial position.

Statement of profit or loss

Respondents’ comments

38. ESMA suggests that the Committee address the presentation of items relating to reverse factoring arrangements in the statement of profit or loss—in particular, whether an entity presents items relating to these arrangements as part of finance costs applying paragraph 82(b) of IAS 1 or in a different line item.

Staff analysis

39. Paragraph 82 of IAS 1 includes a list of line items an entity is required to present in its statement of profit or loss—one of those line items is ‘finance costs’. Paragraph 85 of IAS 1 requires an entity to present additional line items ‘when such presentation is relevant to an understanding of the entity’s financial performance’. Paragraph 86 of IAS 1 notes that in identifying additional line items, ‘an entity considers factors including materiality and the nature and function of the items of income and expense’.

40. IFRS Standards do not define or describe finance costs. There is therefore little that the Committee could say about the presentation of items relating to reverse factoring arrangements as finance costs or in a different line item of the statement of profit or loss. In our view, there is little benefit in adding a section to an already-long agenda

decision that would discuss more generally the presentation requirements in IAS 1 for the statement of profit or loss.

Wording of the agenda decision

41. Respondents made a number of suggestions to clarify the wording of the tentative agenda decision. These include suggestions about:

    (a) the description of a reverse factoring arrangement (paragraphs 41–45);

    (b) presentation in the statement of financial position (paragraphs 46–47);

    (c) presentation in the statement of cash flows (paragraphs 48–49); and

    (d) disclosures about liabilities subject to a reverse factoring arrangement (paragraphs 50–57).

Description of a reverse factoring arrangement

Respondents' comments

42. Deloitte says the description of a reverse factoring arrangement in the tentative agenda decision is too narrow because it is not always the case that the financial institution is paid at a date later than suppliers are paid. Deloitte therefore suggests that the description be changed as follows: 'in a reverse factoring arrangement, a financial institution agrees to pay amounts an entity owes to the entity's suppliers and the entity agrees to pay the financial institution <u>at the same or a later</u> date than suppliers are paid.'

43. BAFT says the definition of a reverse factoring arrangement in the tentative agenda decision is too wide because the agreement regarding due dates is between the entity and the supplier; it does not involve the financial institution. In other words, a reverse factoring arrangement never involves an extension to the entity's credit terms.

Staff analysis

44. BAFT and its members define reverse factoring arrangements narrowly—it considers a revere factoring arrangement to include only arrangements that do not extend the

entity's credit terms. While we acknowledge that this is how BAFT and its members define reverse factoring arrangements, we are aware from outreach that in some arrangements the financial institution offers the entity extended credit terms. BAFT members may consider this to be another type of arrangement.

45. In our view, the requirements in IFRS Standards outlined in the tentative agenda decision apply equally to arrangements in which the financial institution does (and does not) offer the entity extended credit terms. In addition, we understand arrangements in which the entity obtains extended credit terms are of particular interest to investors. We therefore recommend that the Committee continue to use the description of reverse factoring arrangements in the agenda decision.

46. We agree with Deloitte's suggestion to change the description to incorporate arrangements for which the entity might pay the financial institution on the same date as the financial institution pays the supplier. Appendix A to this paper includes a recommended change in this respect.

Presentation in the statement of financial position

47. The tentative agenda decision outlines how an entity determines—applying IAS 1—whether to present financial liabilities subject to a reverse factoring arrangement as part of trade and other payables, as part of other financial liabilities or within their own line item.

48. The table below summarises respondents' comments and our analysis and recommendations on presentation in the statement of financial position:

Respondents' comments	**Staff analysis and recommendations**
Factors an entity might consider in determining whether to present liabilities separately Petrobras suggests clarifying that the examples of factors an entity might consider are not an exhaustive list, and do not have more relevance than other facts and circumstances that might exist. ESMA and Syngenta suggest including additional examples to help entities determine whether a liability subject to a reverse factoring arrangement is not a trade or other payable. For example, ESMA suggests that if the financial institution receives compensation for any extension granted, the liability is a borrowing and not a trade or other payable Syngenta suggests using 'materially different' instead than 'substantially different' in the second factor because materiality would allow entities to base the assessment on the impact on decision-making. Syngenta says 'substantially different' may be understood differently by different preparers.	The introduction to the examples of factors in the tentative agenda decision states that an entity '..might consider factors including, for example..'. In our view, it is already clear that the factors are examples and the use of 'might consider' avoids over-emphasising their importance. In our view, ESMA's suggested example is already addressed by the second factor in the tentative agenda decision. We have been unable to identify other examples of factors that we consider appropriate to add to the agenda decision. The factor that includes 'substantially different' says the following: 'whether the terms of liabilities that are part of the arrangement are substantially different from the terms of the entity's trade payables that are not part of the arrangement'. We agree that 'substantially different' is not used in IFRS Standards and therefore may be difficult to understand. We recommend instead referring to 'sufficiently different' terms – 'sufficiently different' is the phrase used in paragraph 57 of IAS 1 in describing when an entity is required to present an item separately.
Working Capital Petrobras suggests providing more information on 'working capital'.	IFRS Standards do not define or describe working capital. Paragraph 71 of IAS 1 states that 'financial liabilities that provide financing on a long-term basis' are not part of the working capital used in the entity's normal operating cycle, which implies that working capital is short-term. However, based on existing IFRS Standards, we think there is little the Committee could add on working capital.
Application of IAS 1 EY, CVM and Mazars says the agenda decision could be read to require the application of IAS 1 in determining how	In our view, it is difficult to read the tentative agenda decision in this way—the first sentence of the section on presentation in the statement of financial position says

to present a financial liability only when the entity has derecognised a financial liability. Those respondents suggest clarifying that an entity is required to apply IAS 1 in determining the presentation of all financial liabilities, regardless of whether a previously recognised financial liability has been derecognised.	'IAS 1 *Presentation of Financial Statements* specifies requirements for the presentation of liabilities in an entity's statement of financial position'. However, we have suggested some amendments to the wording of that first sentence of the section, which we think will make this more obvious (see Appendix A).
Terminology Mazars suggests not using the phrase 'principal revenue-producing activities' when discussing the statement of financial position because it is a term used only in IAS 7 in relation to the statement of cash flows. Mazars also says the reference to the liability not being a trade or other payable because the liability represents borrowings of the entity should be in the statement of financial position section of the agenda decision, not the statement of cash flows section.	We disagree with Mazars' suggestions. We note that the phrases 'principal revenue-producing activities' and 'borrowings of the entity' are used in the tentative agenda decision only in relation to the statement of cash flows. This is because they are used in the definitions of operating activities and financing activities in IAS 7.

Presentation in the statement of cash flows

49. The section of the tentative agenda decision titled 'Presentation in the statement of cash flows' outlines how an entity determines whether the cash flows related to a reverse factoring arrangement are operating or financing cash flows applying IAS 7.

50. The table below summarises respondents' comments and our analysis and recommendations on presentation in the statement of cash flows:

Respondents' comments	**Staff analysis and recommendations**
Existence of cash flows The tentative agenda decision states that 'if a cash inflow and cash outflow occur for an entity when an invoice is factored as part of a reverse factoring arrangement, the entity presents those cash flows in its statement of cash flows. If no cash flows	We recommend no change in this respect. In our view, the tentative agenda decision faithfully depicts the requirements in IAS 7 in a neutral manner. Paragraph 6 of IAS 7 defines cash flows as 'inflows and outflows of cash and cash equivalents' but IAS 7 provides no further

are involved in a financing transaction of an entity, the entity discloses the transaction elsewhere in the financial statements in a way that provides all the relevant information about the financing activity.' PwC and the ASCG suggest clarifying that gross cash flows may exist, for example, if the financial institution acts as the entity's paying agent in a reverse factoring arrangement—they say an entity can consider there to be cash flows if the entity directs the financial institution to pay a supplier on its behalf. EY suggests clarifying the application of IAS 7 when the financial institution acts as the entity's paying agent. The UK FRC suggests removing the sentence that refers to a cash inflow and cash outflow occurring for an entity—it says the sentence could be confusing because an entity has no cash flows at the time an invoice is factored as part of a reverse factoring arrangement.	requirements to assist an entity in determining whether a cash flow exists. Providing any commentary on how an entity determines whether a cash flow exists, or on particular scenarios, would go beyond the existing requirements in IFRS Standards.
Operating cash flows The ASCG suggests improving the wording of the agenda decision to clarify that cash outflows may be operating cash flows even if they are paid to the financial institution and not to the entity's supplier.	We agree with the ASCG that cash outflows may be operating cash flows even if they are paid to the financial institution. However, we think the agenda decision does not preclude this outcome and, therefore, recommend no change to the agenda decision in this respect.
Investing cash flows EY says a reverse factoring arrangement could involve investing cash flows if the cost of the goods or services is capitalised into a longer-term asset such as property, plant and equipment or an intangible asset. This may happen in industries such as telecommunications or the extractive industries.	We agree with EY that investing cash flows are possible, if unusual. To add discussion of investing cash flows would complicate an already-long agenda decision for a relatively rare situation. We therefore suggest adding 'typically' within the statement of cash flows section of the agenda decision to address the possibly of investing cash flows arising (see Appendix A).

Link with the statement of financial position The ASCG suggests stating explicitly that there is no link between how an entity presents a financial liability in its statement of financial position and how it presents cash flows related to that liability in its statement of cash flows.	In our view, the phrase 'may help' is already clear that there is no automatic link between the statement of financial position and the statement of cash flows. We therefore recommend no change in this respect.

Disclosures about liabilities subject to reverse factoring arrangements

51. The tentative agenda decision contains a section titled 'Notes to the financial statements', which refers to a number of disclosure requirements in IFRS 7, IAS 1 and IAS 7 and explains why reverse factoring arrangements often give rise to liquidity risk.

Respondents' comments

52. Some respondents suggest additional disclosure requirements the Committee could reference in the agenda decision. For example:

    (a) PwC suggests a reference to paragraph 15 of IAS 1, which requires financial statements to present fairly the financial position, financial performance and cash flows of an entity.

    (b) EY suggests references to paragraph 112(c) of IAS 1 and paragraphs 7 and 31 of IFRS 7.

53. The ANC, Deloitte and ESMA say this section of the tentative agenda decision could be misread to limit the application of IFRS 7 to the arrangements to which the disclosure requirements in paragraph 44A of IAS 7 apply. This is because reference to paragraph 44A of IAS 7 (which applies to specific types of reverse factoring arrangements) comes immediately before reference to the requirements in IFRS 7 (which apply to all financial liabilities).

54. BAFT says reverse factoring arrangements do not 'often' create liquidity risk for the entity and suggests, instead, saying that liquidity risk 'could' arise. Deloitte says, in addition to the description in the tentative agenda decision, liquidity risk arises if an

entity becomes reliant on extended credit terms provided by the financial institution in a reverse factoring arrangement.

55. The ASCG says the reasoning in the agenda decision could benefit from focussing more on the overarching aim of improving transparency considering presentation and disclosure together, rather than focussing on specific requirements for each of the financial statements and the notes.

Staff analysis

56. Appendix A to this paper sets out our proposed changes to the wording of the tentative agenda decision. In particular, we recommend the following changes to the agenda decision having considered respondents' comments:

    (a) to move the reference to disclosure requirements in paragraph 44A of IAS 7 after the reference to disclosure requirements in IFRS 7 and IAS 1, to avoid the possible misreading identified by some respondents.

    (b) to add a reference to paragraph 31 of IFRS 7. This paragraph helps in understanding what information an entity is required to disclose about financial liabilities subject to reverse factoring arrangements.

    (c) to add that liquidity risk can arise because an entity may have become reliant on extended credit terms provided by the financial institution in a reverse factoring arrangement.

57. We note that the tentative agenda decision already refers to paragraph 112 of IAS 1, and we see little benefit in adding a reference to the general requirements about fair presentation in paragraph 15 of IAS 1.

58. Finally, in our view reverse factoring arrangements often give rise to liquidity risk. As noted earlier, BAFT and its members define reverse factoring arrangements in a specific and narrow way, whereas the tentative agenda decision describes reverse factoring arrangements more widely. We also note that even when a reverse factoring arrangement does not extend an entity's credit terms, the entity has concentrated a portion of its liabilities with one financial institution rather than a diverse group of

suppliers. This characteristic is common across all reverse factoring arrangements; we therefore recommend no change to the agenda decision in this respect.

The process

59. FCM comments on the process for dealing with requests submitted to the Committee as follows:

    (a) Agenda Paper 3 to the Committee's April 2020 meeting referred to reports on reverse factoring published by PwC and Fitch in the context of assessing the prevalence of reverse factoring arrangements. FCM notes that PwC and Fitch were the only external sources referenced in the staff papers on reverse factoring arrangements. It says the optics of only referencing those two entities in work instrumental in directing international accounting standard-setting is troubling—at a minimum, citing these reports directly, when all other research sourcing was anonymised, gives the impression of adding extra weight to these auditor and rating agency opinions and, by not providing additional sourcing information in staff papers, it is difficult for readers to evaluate independent staff research and analysis on the topic. FCM suggests that staff papers include consistent information on source references and all third parties that were consulted and that provided input to a project.

    (b) FCM suggests that the Committee's process be more nuanced, with higher standards applied when considering requests from opinion-providing entities (such as audit fims and rating agencies). FCM suggests that requests for broad-based standards changes or guidance from entities such as audit firms and rating agencies go through additional scrutiny, including a public review of the request by the Board before any research project is undertaken.

Staff analysis

60. In the April 2020 staff paper, we (as staff) summarised all information we had obtained or observed about the prevalence of reverse factoring arrangements—that included information obtained in outreach responses, from our own research of information provided by entities in their financial statements and in the reports by PwC and Fitch (both of which are publicly available). Our objective was to ensure that we provided all information to the Committee that we have obtained and that we think might to relevant to the Committee's assessment of whether the request submitted has widespread effect. The reports were referred to only in the context of assessing the prevalence of reverse factoring arrangements and, therefore, assessing whether the accounting for and reporting of information about such arrangements could have widespread effect. When we refer to information that is publicly available in our papers, we often include references to source documents—this enables Committee members and others reading the paper who are interested in the materials to refer to them—whereas we do not when we obtain information at meetings or in outreach requests on an informal basis.

61. The *Due Process Handbook* requires that we treat all requests submitted to the Committee in the same way, irrespective of who the submitter is. It is the nature of the submission that is important, not its source. The process is designed to ensure that there are no barriers to stakeholders informing us about matters that may lead to inconsistent application of IFRS Standards. The process applied to requests submitted is thorough, ensuring that a standard-setting project is added only after evidence is obtained of the need for such a project and it is possible to develop a solution. Ultimately it is the Board that makes the decision to undertake standard-setting, and any such decision will be subject to comment by stakeholders through an exposure draft. Agenda decisions are also subject to due process before publication, including publishing a draft for comment and approval by the Board.

Possible standard-setting

Respondents' comments

62. Ten respondents support undertaking a narrow-scope standard-setting project on reverse factoring arrangements to improve the information provided to investors about such arrangements.

63. FCM suggests undertaking standard-setting that would address both presentation of liabilities subject to reverse factoring arrangements and disclosures. FCM suggests that entities be prohibited from presenting financial liabilities that are part of a reverse factoring arrangement as trade and other payables if:

    (a) the contractual obligations between the entity and the financial institution create secured legal asset encumbrances for the entity; or

    (b) the entity is involved in defining the terms of the reverse factoring arrangement between the financial institution and the entity's suppliers.

64. In its letter, FCM also outlines disclosures that it suggests an entity with liabilities subject to a reverse factoring arrangement make.

65. ELFA says all liabilities payable to a financial institution should be classified as other financial liabilities (and not as trade and other payables) because ELFA members consider all such liabilities to be 'debt-like' liabilities. ELFA suggests that the scope of any standard-setting project include both factoring as well as reverse factoring—in its letter, ELFA provides reasons for its suggestions, noting the experience of its members with respect to disclosures entities currently provide about factoring and reverse factoring arrangements and the consequences for financial statement analyses when entities disclose insufficient information about those arrangements.

66. Eumedion suggests introducing a requirement to disclose the net amount of credit the financial institution provides to the entity as a consequence of the reverse factoring arrangement, explaining the benefits for investors of such a disclosure.

67. The ANC notes that, in discussing possible narrow-scope standard-setting, the June 2020 staff paper and IFRIC Update referred to 'arrangements entered into to fund

payables to suppliers'. The ANC suggests further clarification of the scope of any standard-setting project to avoid misunderstanding of that scope.

68. Some other respondents provide specific suggestions about disclosures the Board could consider and some suggest considering widening the scope of any standard-setting project beyond that discussed in the June 2020 staff paper, for example:

(a) Deloitte and the UK FRC suggest including disclosure requirements about the presentation of reverse factoring arrangements in the statement of cash flows. Deloitte also suggests that such a disclosure requirement covers both factoring and reverse factoring arrangements.

(b) IDW suggests clarifying (i) the interaction between the derecognition requirements in IFRS 9 and the presentation of financial liabilities in the statement of financial position, and (ii) the meaning of 'working capital'.

Next steps regarding a possible standard-setting project

69. We have received input regarding a possible standard-setting project on supply chain financing arrangements from a number of sources as follows:

(a) Outreach meetings held with investors and others from February to May 2020—the staff paper discussed by the Committee in June 2020 summarised that input.

(b) The Committee meeting in June 2020 at which Committee members provided their views.

(c) Feedback received in the comment letters on the tentative agenda decision, summarised above in paragraphs 61–67.

70. We plan to bring all of this input and feedback to the Board for its consideration at a future Board meeting. That input and feedback will help the Board decide whether to add a narrow-scope standard-setting project to the work plan on supply chain financing arrangements and, if so, the possible scope of that project.

Staff recommendation

71. We recommend finalising the agenda decision, with changes to the tentative agenda decision as suggested in Appendix A to this paper. If the Committee agrees with our recommendation, we will ask the Board whether it objects to the agenda decision at the first Board meeting at which it is practicable to present the agenda decision.

Question for the Committee

Does the Committee agree with our recommendation to finalise the agenda decision as explained in paragraph 70 of this paper?

Appendix A—Proposed wording of the agenda decision

A1. We propose the following wording for the final agenda decision (new text is underlined, and deleted text is struck through).

Supply Chain Financing Arrangements—Reverse Factoring

The Committee received a request about reverse factoring arrangements. Specifically, the request asked:

(a) how an entity presents liabilities to which reverse factoring arrangements relate (ie how it presents liabilities to pay for goods or services received when the related invoices are part of a reverse factoring arrangement); and

(b) what information about reverse factoring arrangements an entity is required to disclose in its financial statements.

In a reverse factoring arrangement, a financial institution agrees to pay amounts an entity owes to the entity's suppliers and the entity agrees to pay the financial institution at the same date as or a date later than suppliers are paid.

Presentation in the statement of financial position

IAS 1 *Presentation of Financial Statements* specifies requirements for how an entity presents its ~~the presentation of~~ liabilities in ~~an entity's~~ the statement of financial position. Paragraph 54 requires an entity to present 'trade and other payables' separately from other financial liabilities. 'Trade and other payables' are sufficiently different in nature or function from other financial liabilities to warrant separate presentation (paragraph 57 of IAS 1).

Paragraph 11(a) of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* states that 'trade payables are liabilities to pay for goods or services that have been received or supplied and have been invoiced or formally agreed with the supplier'. Paragraph 70 of IAS 1 explains that 'some current liabilities, such as trade payables… are part of the working capital used in the entity's normal operating cycle'. The Committee therefore concluded that an entity presents a financial liability 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.

Paragraph 29 of IAS 1 requires an entity to 'present separately items of a dissimilar nature or function unless they are immaterial'. Paragraph 57 specifies that line items are included in the statement of financial position when the size, nature or function of an item (or aggregation of similar items) is such that separate presentation is relevant to an understanding of the entity's financial position. Accordingly, the Committee concluded that, applying IAS 1, an entity presents:

a) other payables together with trade payables only when those other payables have a similar nature and function to trade payables—for example, when other payables are part of the working capital used in the entity's normal operating cycle.

b) liabilities that are part of a reverse factoring arrangement separately when the size, nature or function of those liabilities makes separate presentation relevant to an understanding of the entity's financial position. In assessing whether to present such liabilities separately (including whether to disaggregate trade and other payables), an entity considers the amounts, nature and timing of those liabilities (paragraphs 55 and 58 of IAS 1).

The Committee observed that an entity assessing whether to present liabilities that are part of a reverse factoring arrangement separately might consider factors including, for example:

a) whether additional security is provided as part of the arrangement that would not be provided without the arrangement.

b) whether the terms of liabilities that are part of the arrangement are ~~substantially~~ sufficiently different from the terms of the entity's trade payables that are not part of the arrangement.

Derecognition of a financial liability

An entity assesses whether and when to derecognise a liability that is (or becomes) part of a reverse factoring arrangement applying the derecognition requirements in IFRS 9 *Financial Instruments*.

An entity that derecognises a trade payable to a supplier and recognises a new financial liability to a financial institution applies IAS 1 in determining how to present that new liability in its statement of financial position (see 'Presentation in the statement of financial position').

Presentation in the statement of cash flows

Paragraph 6 of IAS 7 *Statement of Cash Flows* defines:

a) operating activities as 'the principal revenue-producing activities of the entity and other activities that are not investing or financing activities'; and

b) financing activities as 'activities that result in changes in the size and composition of the contributed equity and borrowings of the entity'.

An entity that has entered into a reverse factoring arrangement typically determines whether to classify cash flows under the arrangement as cash flows from operating activities or cash flows from financing activities. The Committee observed that an entity's assessment of the nature of the liabilities that are part of the arrangement may help in determining the nature of the related cash flows as arising from operating or financing activities. For example, if the entity considers the related liability to be a trade or other payable that is part of the working capital used in the entity's principal revenue-producing activities, the entity presents cash outflows to settle the liability as arising from operating activities in its statement of cash flows. In contrast, if the entity considers that the related liability is not a trade or other payable because the liability represents borrowings of the entity, the entity presents cash outflows to settle the liability as arising from financing activities in its statement of cash flows.

Investing and financing transactions that do not require the use of cash or cash equivalents are excluded from an entity's statement of cash flows (paragraph 43 of IAS 7). Consequently, if a cash inflow and cash outflow occur for an entity when an invoice is factored as part of a reverse factoring arrangement, the entity presents those cash flows in its statement of cash flows. If no cash flows are involved in a financing transaction of an entity, the entity discloses the transaction elsewhere in the financial statements in a way that provides all the relevant information about the financing activity (paragraph 43 of IAS 7).

Notes to the financial statements

~~Paragraph 44A of IAS 7 requires an entity to provide 'disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes'. The Committee noted that such disclosure is required for liabilities that are part of a reverse factoring arrangement if the cash flows for those liabilities were, or future cash flows will be, classified as cash flows from financing activities.~~

Paragraph 31 of IFRS 7 *Financial Instruments: Disclosures* requires an entity to provide information that enables users of its financial statements to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed. IFRS 7 defines liquidity risk as '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'. The Committee observed that reverse factoring arrangements often give rise to liquidity risk because:

a) the entity has concentrated a portion of its liabilities with one financial institution rather than a diverse group of suppliers. The entity may also obtain other sources of funding from the financial institution providing the reverse factoring arrangement. If the entity were to encounter any difficulty in meeting its obligations, such a concentration would increase the risk that the entity may have to pay a significant amount, at one time, to one counterparty.

b) the entity may have become reliant on extended payment terms or the entity's supplier may have become accustomed to, or reliant on, earlier payment under the reverse factoring arrangement. If the financial institution were to withdraw the reverse factoring arrangement, that withdrawal could affect the entity's ability to settle liabilities when they are due, particularly if the entity were already in financial distress. ~~some suppliers may have become accustomed to, or reliant on, earlier payment of their trade receivables under the reverse factoring arrangement. If the financial institution were to withdraw the reverse factoring arrangement,~~

~~those suppliers could demand shorter credit terms. Shorter credit terms could affect the entity's ability to settle liabilities, particularly if the entity were already in financial distress.~~

Paragraphs 33-35 of IFRS 7 require an entity to disclose how exposures to risk arising from financial instruments including liquidity risk arise, the entity's objectives, policies and processes for managing the risk, summary quantitative data about the entity's exposure to liquidity risk at the end of the reporting period (including further information if this data is unrepresentative of the entity's exposure to liquidity risk during the period), and concentrations of risk. Paragraphs 39 and B11F of IFRS 7 specify further requirements and factors an entity might consider in providing liquidity risk disclosures.

An entity applies judgement in determining whether to provide additional disclosures in the notes about the effect of reverse factoring arrangements on its financial position, financial performance and cash flows. The Committee observed that:

a) assessing how to present liabilities and cash flows related to reverse factoring arrangements may involve judgement. An entity discloses judgements that management has made in this respect if they are among the judgements made that have the most significant effect on the amounts recognised in the financial statements (paragraph 122 of IAS 1).

b) reverse factoring arrangements may have a material effect on an entity's financial statements. An entity provides information about reverse factoring arrangements in its financial statements to the extent that such information is relevant to an understanding of any of those financial statements (paragraph 112 of IAS 1).

The Committee noted that making materiality judgements involves both quantitative and qualitative considerations.

Paragraph 44A of IAS 7 requires an entity to provide 'disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes'. The Committee noted that such disclosure is required for liabilities that are part of a reverse factoring arrangement if the cash flows for those liabilities were, or future cash flows will be, classified as cash flows from financing activities.

The Committee concluded that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine the presentation of liabilities that are part of reverse factoring arrangements, the presentation of the related cash flows, and the information to disclose in the notes about, for example, liquidity risks that arise in such arrangements. Consequently, the Committee ~~[~~decided~~]~~ not to add a standard-setting project on these matters to ~~its standard-setting agenda~~ the work plan.

Appendix B—Comment letters

Ms Sue Lloyd
Chair, IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD

14 September 2020

Dear Ms Lloyd:

Tentative agenda decision — Supply Chain Financing Arrangements - Reverse Factoring

We are pleased to respond to your invitation to comment on the tentative agenda decision – Supply Chain Financing Arrangements - Reverse Factoring —published in June 2020, on behalf of PricewaterhouseCoopers.

Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of member firms who commented on the tentative agenda decision. “PricewaterhouseCoopers” refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

Subject to our specific comments below, we generally agree with the Committee’s analysis of the submission and its conclusions regarding presentation in the statement of financial position, derecognition principles and relevant disclosures for supply chain financing arrangements. We also agree with the Committee’s tentative decision not to take the issue of presentation onto its agenda. We further support the committee in continuing to explore whether specific disclosure requirements would provide transparency over these arrangements and improve a user's understanding of an entity's reliance on these arrangements.

We have the following specific comments on the tentative agenda decision.

Assessment of whether the arrangement gives rise to cash flows for an entity on the factoring of an invoice

In the analysis of the classification of cash flows in the cash flow statement, the tentative agenda decision notes "If a cash inflow and cash outflow occur for an entity when an invoice is factored…" (emphasis added). We believe it should be made clear in the analysis supporting the tentative agenda decision that before determining the classification of cash flows in the cash flow statement, an entity first needs to determine whether factoring an invoice actually results in a cash flow for the entity. We acknowledge that a detailed analysis of whether there is a cash flow for the entity when an invoice is factored is beyond the scope of this agenda decision and would have far reaching consequences for many other transactions, however we believe it is an important first step for entities to consider in order to apply the agenda decision.

The substance of some arrangements is that the entity is directing a cash payment from the bank to the supplier and that presentation of a cash inflow to the entity (draw down on borrowing) and cash outflow to the supplier (payment of payables) may be appropriate. To illustrate, if under a factoring arrangement, when an entity factored an invoice, the bank transferred funds to a bank account for the entity, and then the entity directed the bank to pay the supplier from that bank account, this would clearly result in cash flows for the entity. However, some reverse factoring arrangements do not make use of a separate "bank account", nonetheless the bank has effectively acted as the entity's payment agent to settle the obligation to the supplier. We believe the substance of this arrangement is the same as the first arrangement where a separate bank account is used. We liken this to other circumstances when an entity directs a third party to pay an obligation on its behalf, such as a sale of a property to a third party where, upon request of the seller, a portion of the proceeds is paid by the purchaser directly to the seller's mortgage provider to settle the mortgage on the property. We believe that in such a situation, the seller should generally present a cash inflow for the sale and a cash outflow for the settlement of the mortgage. This would be true regardless of whether the cash inflow and outflow were recorded in the seller's bank account.

As noted above, we acknowledge that a detailed analysis of when a financial institution is acting as a payment agent for an entity is beyond the scope of this agenda decision. However, if the committee agrees that there *may be situations* where the financial institution can be acting as a payment agent with respect to cash flows paid to the supplier, and therefore presentation of these cash flows in the cash flow statement of the entity is appropriate, we suggest adding the following sentence to assist preparers in appropriately applying the agenda decision:

"Consequently, when an invoice is factored as part of a reverse factoring arrangement, an entity should determine whether the bank has effectively acted as the entity's payment agent to settle the obligation with the supplier as part of the arrangement. The Committee concluded that determining which cash flows in a reverse factoring arrangement are those of the entity was beyond the scope of the submission. If ~~if~~ a cash inflow and cash outflow occur for an entity…"

Fair presentation

We believe that it is important that entities consider the requirements in IAS 1 para 15 that the accounting reflects a fair presentation of the financial position, financial performance and cash flows of an entity. The tentative agenda decision is clear that for both the financial position and the cash flows there are judgements that an entity will need to make as to the substance and nature of the transactions and balances. We believe it would be helpful for the tentative agenda decision to refer to the fair presentation requirements in IAS 1.

Derecognition of a financial liability

We agree with the committee's observation that "An entity that derecognises a trade payable to a supplier and recognises a new financial liability to a financial institution applies IAS 1 in determining how to present that new liability in its statement of financial position". We believe that if the arrangements with the bank result in derecognition under IFRS 9, then the new liability would be appropriately presented as a short-term borrowing (or a similarly described line item) as opposed to trade payables or other payables. In determining the presentation in the statement of financial position under IAS 1, an entity should consider the outcome of the derecognition analysis. We believe the tentative agenda decision is not sufficiently clear on the importance of assessing derecognition and how that conclusion may impact the presentation of the financial liability. We believe the agenda decision would be more useful to stakeholders if this interaction was clarified. We propose amending the following sentence to reflect this as follows:

An entity that derecognises a trade payable to a supplier, recognises a new financial liability to a financial institution. ~~applies IAS 1 in determining how to present that new liability in its statement of financial position.~~ This new financial liability would be appropriately presented as a short-term borrowing (or a similarly described line item) as opposed to trade payables or other payables".

If you have any questions in relation to this letter please do not hesitate to contact Henry Daubeney, PwC Global Chief Accountant and Head of Reporting (+ 44 7841 569635).

Yours sincerely,

PricewaterhouseCoopers

PricewaterhouseCoopers

Building a better
working world

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INVESTOR IN PEOPLE

International Financial Reporting Standards Interpretations Committee
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E14 4HD

18 September 2020

Dear IFRS Interpretations Committee members,

Invitation to comment – Tentative Agenda Decision: *Supply Chain Financing Arrangements - Reverse Factoring (IFRIC Update* June 2020 - Agenda Paper 2)

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on the above Tentative Agenda Decision (TAD) discussed by the IFRS Interpretations Committee (the IFRS IC) in June 2020.

Overall, we support the general direction of the TAD and we believe that it provides helpful guidance for the presentation and disclosure of reverse factoring arrangements. In particular, we support the emphasis that is given on the separate presentation, where necessary, of such liabilities in the statement of financial position and the disclosure requirements to explain those arrangements. This will contribute to achieving transparency in reverse factoring arrangements.

However, we would like to share some concerns over parts of the TAD and also request certain clarifications:

Derecognition of a financial liability

The TAD clarifies that "an entity that derecognises a trade payable to a supplier and recognises a new financial liability to a financial institution applies IAS 1 *Presentation of Financial Statements* in determining how to present that new liability in its statement of financial position (see 'Presentation in the statement of financial position')". However, IAS 1 applies similarly when determining whether a trade payable should be presented as another liability in the context of a reverse factoring arrangement, even if the trade payable is not derecognised under the requirements of IFRS 9 *Financial Instruments*. Therefore, we believe that it would be helpful to clarify that an entity is required to determine how to present any such liability in its statement of financial position, regardless of whether the entity derecognised the trade payable when entering into a reverse factoring arrangement, or not.

Presentation in the statement of cash flows

We agree with the fact that an entity's assessment of the nature of the liabilities that are part of the arrangement may help in determining the nature of the related cash flows as arising from operating or financing activities. We generally believe that this is in line with what we have seen in practice.

However, we believe that the current wording in the TAD may be interpreted differently by constituents, and as such, may lead to diversity in practice. In particular, the TAD currently states the obvious, that is if no cash flows are involved, then no cash flows should be presented in the cash flow statement. However, it has been observed that certain entities consider that the relationship between themselves and the financial institution is, in substance, a principal/agent relationship. Such a conclusion would imply that the financial institution is acting as an agent of the entity and is, therefore, incurring cash flows on behalf of the entity when paying the supplier. It is unclear in the TAD as to whether such an analysis would be appropriate.

We would also like to point out that, currently, the TAD suggests that the decision is whether to classify the associated cash flows as operating or financing activities. However, we note that if the cost of the goods or services is capitalised into a longer-term asset such as property, plant and equipment, or possibly an intangible asset, the classification decision would be between investing and financing activities. This may be particularly relevant in asset intense industries such as telecommunications or the extractive industries. To avoid potential confusion, we suggest that the Committee revises the wording to reflect this consideration as well.

Notes to the financial statements

We believe that the two cases mentioned in the TAD as giving rise to liquidity risk should be mentioned as examples to avoid being misunderstood as an exhaustive list.

Finally, we believe it may not be sufficient to only point out the general disclosure requirements of paragraphs 112 and 122 of IAS 1 to emphasise the need for relevant and transparent disclosures. For example, reference to more specific paragraphs such as paragraph 112(c) of IAS 1 and the disclosure objectives in paragraphs 7 and 31 of IFRS 7 *Financial Instruments: Disclosures* would be helpful.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas at the above address or on +44 (0)20 7951 3152.

Yours faithfully

Ernst & Young Global Limited

PETROBRAS

Rio de Janeiro, September 21, 2020

CONTRIB 0045/2020

Ms. Lloyd, Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD, United Kingdom

Subject: Supply Chain Financing Arrangements—Reverse Factoring

Reference: Tentative Agenda Decision (TAD)

Dear Ms. Lloyd,

Petrobras welcomes the opportunity to comment on the IFRS Interpretations Committee's Tentative Agenda Decision - Supply Chain Financing Arrangements—Reverse Factoring. We believe this is an important opportunity for all parties interested in the future of IFRS and we hope to contribute to the progress of the Committee's activities.

We agree with the Committee's decision not to add the matter to its standard-setting agenda.

We believe that the assessment of reverse factoring arrangements presentation involves judgment and consideration of all facts and circumstances. In this sense, we ask the Committee to clarify in the final agenda decision that the factors included in the TAD to assess how to present liabilities that are part of a reverse factoring arrangement separately are not exhaustive and should not have more relevance than other facts and circumstances that may be pertinent in such assessment.

We also noted that the TAD provided a conclusion of when an entity presents a financial liability as a trade payable. In this sense, we also ask the Committee to provide further clarifications in the final agenda decision about what 'part of the working capital' means in such conclusion. It is worth mentioning that the IFRS Standards does not provide a definition for working capital.

If you have any questions in relation to the content of this letter, please do not hesitate to contact us (contrib@petrobras.com.br).

Respectfully,

/s/Rodrigo Araujo Alves
Rodrigo Araujo Alves
Chief Accountant and Tax Officer

RÉPUBLIQUE
FRANÇAISE
Liberté
Égalité
Fraternité

AUTORITÉ
DES NORMES COMPTABLES

Paris, 23 September 2020

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PDC n°29

Mrs Sue Lloyd
IFRS Interpretation Committee Chair
7 Westferry Circus, Canary Wharf
London, E14 4HD
United Kingdom

Subject: June 2020 – IFRS IC Tentative Agenda Decision: Supply Chain Financing – Reverse Factoring

Dear Mrs Lloyd, Dear Sue,

I am writing to you on behalf of the Autorité des normes comptables (ANC) to express our views on the IFRS Interpretations Committee's Tentative Agenda Decision (TAD) published June 2020 regarding the classification and disclosures requirements applicable to supply chain financing arrangements.

We agree with the Committee's conclusion that the principles and requirements in IFRS Standards provide an adequate basis for an entity to determine the presentation of liabilities that are part of such arrangements, the presentation of the related cash flows and information to disclose in the notes. However, we suggest clarifications to the wording of the TAD with regard to the scope of some disclosure requirements.

Lastly, we support the initiative of a narrow-scope amendment, to develop additional disclosure requirements for arrangements entered into to fund payables to suppliers.

- **The usefulness of publishing an Agenda Decision (AD)**

The consequences of supply chain financing arrangements on financial information are complex and far-reaching. Moreover, such arrangements are becoming widespread and cover a wide range of schemes. We agree with the Committee's tentative decision to publish an AD that sets out the applicable presentation and disclosure requirements. We think an AD may enhance the consistent application of those requirements and thus, may improve the reporting of financial information about supply chain financing arrangements.

- **Improvements to the wording of the Agenda Decision**

Albeit limited in its scope, the TAD provides useful clarifications about (i) the presentation of the sobligations to which reverse factoring arrangements relate and (ii) the applicable disclosures. We agree with Committee's analysis and conclusions but think that the scope of the disclosures requirements mentioned in the TAD could be made more explicit.

We understand that the first paragraph of the section entitled '*Notes to the financial statements*' specifically deals with disclosure requirements only applicable to financial liabilities not classified as trade payables. Accordingly, those requirements do not apply to trade payables. This is apparent from the mention in the TAD that '*such disclosure is required for liabilities that are part of a reverse factoring arrangement if the cash flows for those liabilities were, or future cash flows will be, classified as cash flows from financing activities*'. We agree that paragraph 44A of IAS 7 *Statement of Cash Flows* restricts this disclosure requirement to financial liabilities other than trade payables because that paragraph requires an entity to provide disclosures '*that enable users of financial statements to evaluate changes in liabilities arising from financing activities*'.

The following paragraph in the section goes on and outlines the requirements in IFRS 7 *Financial Instruments: Disclosures*. However, given the scope applicable to the requirements mentioned in the immediately preceding paragraph and in the absence of any clarification, we are concerned that the TAD might be read as narrowing the disclosures requirements in IFRS 7 on liquidity risk to financial liabilities other than trade payables only and thus, might imply that those disclosure would not apply to trade payables. In our view, the scope of the requirements in IFRS 7 on liquidity risk is not limited to financial liabilities other than trade payables—it also extends to trade payables (applying paragraphs 3 and 31 of IFRS 7) and to all non-derivative financial liabilities (applying paragraphs 39 of IFRS 7). Therefore, it would useful to clarify that the scope of the disclosure requirements regarding liquidity risks as presented in the TAD includes the circumstances in which the liabilities are classified as trade payables.

- **Clarifications on the scope of possible narrow-scope standard-setting**

The addendum to the TAD states that the possible narrow-scope standard-setting project would consist of developing '*disclosure requirements for arrangements entered into to fund payables to suppliers*'. For reasons similar to those mentioned in the paragraph above, we think that the scope of such project could be clarified by being more accurately defined. We agree that the addendum is not part of the Agenda Decision as such. Nonetheless, we think such clarification would avoid any misunderstanding about the types of liabilities that would be in the scope of the standard-setting project, and by extent would contribute to the understandability of the AD.

Should you wish to discuss any aspect of our comment letter, please do not hesitate to contact me.

Yours sincerely,

Kind regards.

Patrick de Cambourg

Patrick de Cambourg

IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD

28th September 2020

Dear Board Members and Staff,

Thank you for the opportunity to comment on your tentative agenda decision on reverse factoring arrangements. The European Leveraged Finance Association (ELFA) is a professional trade association comprised of European leveraged finance investors with more than 30 institutional fixed income managers, including investment advisors, insurance companies, and pension funds. ELFA seeks to support the growth and resilience of the leveraged finance market while acting as the voice of its investor community by promoting transparency and facilitating engagement among European leveraged finance market participants.

Our members view the application of current reporting standards to receivables factoring and reverse factoring as particularly problematic for the following reasons:

- Our members consider the liabilities originated by such liabilities to be debt-like liabilities because terms generally enable earlier payment to suppliers and later payment by customers. The funding gap that is so generated is bridged by a bank or other financial institutions, similar to other conventional form of funding.
- Our members find that such arrangements are frequently not disclosed in annual and quarterly reports, resulting in under-reported financial debt. This is particularly problematic for leveraged finance investors making their investment decisions based on reported financial debt, as they would be unaware of the additional leverage funded through such arrangements. Therefore, when such arrangements are not disclosed, investors may misallocate capital and misprice credit risk. This is also problematic for equity investors as under reported financial debt might translate into inflated market equity valuations.
- Default risk is a key consideration for leveraged finance investors and the risk can be exacerbated by these arrangements, which are generally short-term in nature and can be pulled at short notice. When banks pull out of these lines, the resulting working capital shock can potentially trigger a liquidity crisis that could lead to the issuer's default, without any warning sign for investors. When these arrangements are not disclosed, leverage finance investors are unaware of this additional source of default risk, compounding the capital allocation and pricing challenge described in the previous point. A number of high-profile defaults have abundantly illustrated this point.
- When these arrangements are not disclosed, banks have an asymmetrical information advantage vs. debt capital market investors which undermines a key tenet of efficient capital markets (i.e., that the same information is made available to all investors).

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Company Registration: 11850624

For these reasons ELFA supports Moody's letter to strengthen reporting standards applicable to supply chain finance arrangements. In addition to reverse factoring, ELFA would welcome tighter reporting standards for non-recourse receivables factoring as well, since all of the points raised above are also applicable to this form of funding.

Given the importance to our members of strengthening current reporting standards applicable to factoring arrangements, we believe the Board should reconsider adding these matters to its standard setting agenda. We would encourage the Board to take on a narrow-scope project to add specific disclosure requirements for all factoring arrangements, whether receivables factoring or reverse factoring.

In response to your questions:

Question 1: Do you think the information already required by IFRS Standards (as explained in the tentative agenda decision) is sufficient?

Based on the experience of ELFA members we have consulted, the application of current reporting standards is not sufficient to address the issue. Our members have found that such arrangements are frequently undisclosed and sufficiently large in size to add significant credit risk. A recent annual study by the Supply Chain Finance Community and PWC (quoted by Moody's in its report "Reverse factoring is increasingly popular but can weaken liquidity at a time of stress", 19th September 2019) 49% of companies surveyed already operate a reverse factoring programme, yet fewer than 5% of the non-financial companies rated by Moody's disclose such a programme in their public accounts.

With regards to non-recourse receivables factoring (non-recourse sale of trade receivables), such lines are not included among financial liabilities in the balance sheet as they are treated as "true" sale of receivables and are frequently undisclosed in the notes to the financial statements. There is a general consensus among ELFA members that these are a debt-like facilities. In addition to the points raised above, while in theory a non-recourse sale of receivables results in a full transfer of the credit risk associated with customers' payment, in practice banks add them together with conventional debt facilities to calculate aggregate corporate exposure limits.

With regards to reverse factoring, our members find that the liabilities generated by such arrangements are generally reported as trade payables or other payables even when the terms of the liabilities that are part of such arrangement are substantially different from the terms of the companies' trade payables that are not part of the arrangement. Our members have pointed to examples were DPOs (Days Payables Outstanding) were >300 days under reverse factoring arrangements and yet such liabilities were reported as other payables.

Question 2: Is there something missing from the Standards—something the Board should add to the requirements—that is needed to facilitate companies providing useful information about these arrangements? If so, what is missing?

Our members believe that it would be helpful to classify any liability to banks and other financial institutions as financial liabilities regardless of the underlying transaction that has generated such liabilities. Under current reporting standards, a liability to a financial institution generated through supply chain financing arrangements could be classified either as trade payables or other payables even if the initial liability to a supplier is transferred to a bank or

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other financial institution. Our members believe that when a liability is transferred to a bank or other financial institution, it should be classified as financial liability.

With regards to non-recourse receivables factoring (non-recourse sales of trade receivables), our members believe these are debt-like liabilities for the reasons previously illustrated and although they do not generate a financial liability in its technical definition, they are very similar to other conventional revolving funding agreements. For these reasons our members would welcome a mandatory disclosure in the notes to the financial statements of such liabilities.

We hope that our comments will contribute to the IASB's further deliberation on this topic. Should you require any clarifications, please do not hesitate to contact us.

Your sincerely,

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September 28, 2020

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SOCPA Comments on Tentative Agenda Decision- Supply Chain Financing Arrangements—Reverse Factoring

Dear Colleagues,

The Saudi Organization for Certified Public Accountants (SOCPA) appreciates the efforts of the IFRS Interpretations Committee (Committee) and welcomes the opportunity to comment on the *Tentative Agenda Decision- Supply Chain Financing Arrangements—Reverse Factoring*.

Reverse Factoring means that the entity derecognizes a trade payable and recognizes a loan payable. According to IFRS 7, loans payable are defined to be 'financial liabilities, other than short-term trade payables on normal credit terms'. Therefore, there is no judgement involved about the amounts, nature and timing of those liabilities that allows the entity to determine whether to present such liability with trade payables or not. Allowing such judgement in the Agenda Decision will promote diverse presentation practices. Furthermore, and as we see Reverse Factoring as a loan payable, it is preferable for the Agenda decision to make reference to the IFRS 7 requirements regarding defaults and breaches on loans payable (paragraph 18), which are not requirements for trade payable. Allowing judgment about the presentation of Reverse Factoring may add to diversity in practice regarding IFRS 7 disclosure requirements about defaults and breaches on loans payable.

Please feel free to contact Dr. Abdulrahman Alrazeen at (razeena@socpa.org.sa) for any clarification or further information.

Sincerely,

Dr. Ahmad Almeghames
Secretary General

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Chair of the IFRS Interpretations Committee
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IFRS Technical Committee
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Berlin, 28 September 2020

Dear Sue,

IFRS IC's tentative agenda decision reached in its June 2020 conference call

On behalf of the Accounting Standards Committee of Germany (ASCG), I am writing to comment on the tentative agenda decision on Supply Chain Financing Arrangements taken by the IFRS Interpretations Committee (IFRS IC) as published in the June 2020 *IFRIC Update*.

We generally agree with the tentative agenda decision. However, we have identified room for improving the wording, thereby increasing clarity.

As regards presentation in the statement of cash flows, the current wording of the tentative decision implies that cash flows shall be presented *either* as operating cash (out)flows *or* as financing cash (out)flows. However, we take the view that under a reverse factoring arrangement, and in particular when applying the indirect method (IAS 7.20), it could be appropriate to present *both* operating cash (out)flows as well as financing cash (in/out)flows – which effectively represents a gross presentation. We suggest clarifying the agenda decision in this regard to ensure that a gross presentation is neither required nor precluded.

Further, in the light of the current Primary Financial Statements project, assessing the nature of cash flows should be based on a wider understanding of "operating" (ie. core/main business as well as ancillary activities). This said, cash outflows may be assessed as "operating" even though they are paid to the factor (which corresponds to a "financing agent") and not to the entity's supplier. We suggest improving the respective wording in order to address this point.

As regards the statement of financial position, the current wording suggests that assessing the nature of liabilities determines, or "may help" determining, the nature of cash flows. While we support coherence in presentation, this would neither require *identical* presentation in the statement of cash flows and the statement of financial position nor justify that a change in the nature of cash flows implies an automatic derecognition of an existing liability/trade receivable and recognition of a new (financial) liability – or vice versa. We suggest that the current wording be amended accordingly.

Lastly, we believe that the reasoning for this agenda decision could benefit from focussing more on the overarching aim of improving transparency. This aim is achieved by the aggregate of appropriate presentation of reverse factoring arrangements within the statement of financial position and the statement of cash flows as well as appropriate accompanying disclosure rather than specific requirements for each of these statements and/or disclosures.

If you would like to discuss our views further, please do not hesitate to contact Jan-Velten Große (grosse@drsc.de) or me.

Yours sincerely,

Andreas Barckow

President

IFRS Interpretations Committee
The IFRS Foundation
Columbus Building
7 Westferry Circus
London
E14 4HD

25th September 2020

By Electronic Mail: ifric@ifrs.org

Re: IFRIC Update June 2020 Tentative Agenda Decision:
Supply Chain Financing Arrangements—Reverse Factoring

Dear Members of the IFRS Interpretations Committee,

We welcome the opportunity to comment on the June 2020 tentative agenda decision, "Supply Chain Financing Arrangements – Reverse Factoring", on behalf of Fermat Capital Management, LLC.

Fermat Capital Management, LLC manages multiple investment strategies, including in investment grade trade financing transactions – known as supply chain finance or reverse factoring transactions – on behalf of regulated investors, such as U.S. insurance companies and banks. As an investment manager, we are not involved in the origination of the transactions we invest in, rather we purchase investments from bank and financial technology broker-dealers.

The topic of reverse factoring accounting and disclosure has received significant attention recently. In addition to the work of the IFRS Interpretations Committee, both FASB and the SEC are reviewing reverse factoring accounting and disclosure issues. In certain jurisdictions, including the United Kingdom and Australia, private commercial policy matters such as payment terms – in some cases related to reverse factoring – are being examined by business associations, with a particular focus on fairness for small and medium-sized enterprises. In the U.K., the behavior of a certain debtor organization was the subject of a Parliamentary inquiry, where reverse factoring and accounting was an element of the investigation. Other debtor organizations are being asked for supplemental information on their reverse factoring activities by regulators. These developments have attracted media attention on the topic, which – in some cases – has conflated accounting, individual corporate behavior and public policy issues.

We are writing this letter as we believe IAS Staff and IFRS Interpretations Committee Members erred by not recommending a narrow-scope standard-setting reverse factoring disclosure project in their most recent June 2020 meeting. In our view, Staff and Committee Members did not adequately address the two fundamental issues raised in Moody's Investor Service's submission on supply chain finance arrangements, and therefore failed to address the accounting issues highlighted. As investors we share the concerns outlined in the submission, namely, that without adequate disclosures: a) it is difficult to compare financial statements of companies that use and do not use reverse factoring, b) reverse factoring can obscure "debt-like liabilities" and, c) reverse factoring can complicate default risk assessments by obfuscating the important distinction between operating and financing cashflows.

As investors, we welcome appropriate and informative disclosures in financial statements, however, we do not believe current disclosures are sufficient. For example, investors and other financial statement users currently do not know whether a company utilizes reverse factoring unless it chooses to disclose that it does. Further, with current accounting standards, investors do not know whether there are interests in company assets associated with the use of reverse factoring facilities by the creditors, nor if the company is involved in arranging and managing the financing with those creditors, both of which have important implications for account classification.

These are critical issues, which we believe Staff did not address in their work. Without considering the full scope of reverse factoring disclosures and their complexities, particularly with respect to classification, in our view Committee Members did not have the necessary information to opine on the narrow-scope standard-setting project agenda item. This letter provides two sets of recommendations. First, specific recommendations for consideration in future IFRS deliberations regarding reverse factoring disclosure standards. Second, recommendations on how the handling of external requests for guidance on IFRS practices and subsequent responses can be improved going forward.

1) <u>Disclosure Recommendations on Reverse Factoring</u>

Disclosure regarding reverse factoring is fundamentally complex given the roles and information flows in reverse factoring arrangements. The sale of a receivable (the factoring activity in reverse

FERMAT CAPITAL
MANAGEMENT, LLC

factoring) is executed between the trade creditor and a financing agent, such as a bank. In factoring, that arrangement may or may not be disclosed to the trade debtor, *which constrains the classifications that can be made by the trade debtor.* Arrangements between trade creditors and their financing sources, just like those between trade debtors and their financing sources, are private and disclosures about the other's activities – in the case of reverse factoring, that is the activities of financing source(s) such as banks and/or the trade creditors – raises both privacy and property rights issues for trade debtors. Simply put, the activities are not the debtor's accounts to disclose.

The first challenge facing trade debtor disclosure is whether or not reverse factoring account disclosure should be classified as short-term debt or as account payables. Classification as debt is appropriate when the debtor arranges for a loan or for the issuance of bonds with a financing provider such as a bank *for its account*. Classification as trade payables is appropriate under an arrangement where goods and/or services have been sold by a creditor to the debtor for payment in the future. Banks are providers of many services to debtors, including for loans and bonds, that are classified as debt, as well as other services that are classified as payables, and there may be instances where, *under certain conditions, the bank's debt financing may have superior legal standing to that of other creditor financing (potentially involving other banks), including cross defaults to other forms of debtor indebtedness at that bank*. This possible difference *necessitates that the reverse factoring arrangement be disclosed, as a security interest may exist even though the debtor is not receiving cash in the factoring transaction*. Here additional disclosure and accurate accounting classification are critical, as the credit facility that the bank is utilizing – while it may be for the benefit of the creditors who are receiving cash through their asset sales – may be affiliated and secured by the debtor. Given that *the bank's legal and accounting classification is not disclosed to the debtor for its accounting for that indebtedness*, the debtor may not consider such stakeholder impact. *In summary, if the contractual obligations through the bank create secured legal asset encumbrances for the debtor then this disclosure is required and, in this case, the appropriate classification of such an arrangement is debt*.

The second classification challenge is understanding the extent of the involvement of the debtor in the provision of services between the finance agent and trade creditors. If the debtor is involved in defining the terms of the arrangement – beyond simply providing information about future creditor payments and necessary identification and informational disclosures about those creditors – then such involvement would suggest they are arranging financing for facility use by their creditors *as if it were for their account*. In this case, the appropriate classification of the arrangement would again be debt. However, in independent and discretionary arrangements between a trade creditor and a finance agent, the appropriate classification of such an arrangement for the debtor is payables. *In other words, if the debtor has no involvement in the arrangements between the finance agent and the creditors then the appropriate classification selecting for reverse factoring is payables.*

The fundamental assumptions referred to in paragraphs 22 and 23 of the June 2020 Staff paper – titled "Supply Chain Financing—Reverse Factoring" – that are relied upon for the subsequent classification analysis, are insufficient to address these issues. We believe financial statements must include additional qualitative debtor disclosures acknowledging: a) any reverse factoring arrangement(s), b) whether there is, or there is not, a finance agent security governing that arrangement(s) and, c) the extent of the involvement of the debtor in the reverse factoring arrangement(s). Specifically, we recommend the following additions to financial statement disclosures:

1. An affirmative statement regarding the existence of a reverse factoring arrangement(s) and an acknowledgement that the debtor believes, to the best of its knowledge, that the arrangement is not secured by the debtor's assets; if the debtor acknowledges that it does not believe this is a secured arrangement then the appropriate classification for the arrangement is payables, and;
2. An affirmative statement regarding the existence of a reverse factoring arrangement(s) and qualitative statements about the debtor's involvement in the reverse factoring arrangement(s), including:
    a. Whether or not the program is offered to all or only some creditors;
    b. Whether the debtor has exerted influence on:
        i. The size and/or pricing of the financing arrangement, and/or;
        ii. The financing agent's role, facility limit, syndication and syndication counterparties.

    If the debtor acknowledges that it is not involved in arranging the facility, nor its operating terms, operations or creditor involvement, then the appropriate classification for the arrangement is payables.

If the debtor can affirm that the reverse factoring arrangement is not secured and the debtor is not involved in arranging the facility, only these additional disclosures are required to complete the financial statements. These simple additional disclosures – known to the debtor to the best of its knowledge without requiring possible property rights or privacy violations – would enable proper classification and therefore interpretation of balance sheets and cash flow statements.

However, a reporting entity's acknowledgement that the arrangement is secured, or that it is arranging the facility or is involved in its operation, creates classification issues outside the scope of Staff research to date. We believe the Members of the IFRS Interpretations Committee should consider this omission, together with the recommendations above, and request appropriate Staff research to bring these issues forward for deliberation in a future public meeting.

2) <u>Recommendations on the Process for Handling External Requests for IFRS Guidance</u>

As observers, we believe these deliberations on supply chain financing accounting standards setting have raised important questions regarding the IFRS Interpretations Committee's policy and process with respect to handling and responding to external requests for accounting standards guidance.

We note that PwC and Fitch – a global accounting firm and rating agency respectively – were the only external sources referenced in the Staff work published on the topic. Ratings agencies and auditors provide opinions on financial statement classifications and disclosures, or on credit worthiness, in forms that are directly and indirectly utilized by regulators and investors. Auditors or ratings agencies are not risk-takers in the use of these opinions, but their market roles are extraordinarily complex, and their opinions have a significant impact on investments and on investment prices. Given the potential for the appearance of conflicts, the optics of only referencing two such entities in a piece of work instrumental in directing international accounting standards setting are troubling. At a minimum, citing these materials directly, when all other research sourcing was anonymized, gives the impression of adding extra weight to these auditor and rating agency opinions and, by not providing additional sourcing information in the written report, it is difficult for readers to evaluate independent Staff research and analysis on the topic. We are aware, however, that Staff consulted with a much broader array of experts and materials when conducting their work. In our view, standards setting papers and reports should include consistent information on source references and all third parties that were consulted and that provided input to a project. Such a simple step would promote transparency in the deliberation process and would demonstrate that IFRS development considers a sufficiently broad and independent range of inputs.

Second, we believe IFRS Interpretations Committee's policy should be more nuanced, with higher standards applied when considering requests from opinion providing entities given their roles and potential influence on the application of broad-based accounting standards, such as the matter in question. As noted above, auditors and ratings agencies have complex roles and potential conflicts exist between opinion provision and how that information is used by investors and regulators. To manage concerns on possible influence on standards and policy setting, we suggest that the IFRS Interpretations Committee consider a revision to their policy on responding to public inquiries and recommend that requests for broad-based standards changes or guidance from entities such as raters and auditors go through additional scrutiny, including a public review of the request by the full Board before any research project is undertaken. In our view, such a revision will, again, promote transparency in the IFRS setting process and will contribute to better outcomes for all interested parties.

We hope that the Committee will examine the issues we outline in this letter and we are available for additional information or any required clarifications.

Yours faithfully,

Adam L. Dener
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European Securities and Markets Authority

THE CHAIR

Date: 24 September 2020
ESMA32-61-418

Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD
United Kingdom

Ref: The IFRS Interpretations Committee's June 2020 tentative agenda decision

Dear Ms Lloyd,

The European Securities and Markets Authority (ESMA) would like to thank you for the opportunity to respond to the IFRS Interpretations Committee's (IFRS IC) publication of a tentative agenda decision in the June 2020 IFRIC Update relating to *Supply Chain Financing Arrangements — Reverse Factoring.* We are pleased to provide you with the following comments with the aim of improving the consistent application and enforceability of IFRSs.

ESMA has considered the IFRS IC's tentative decision not to add to its standard-setting agenda the request to clarify how an entity presents liabilities arising from supply chain financing – reverse factoring arrangements and what related information an entity is required to disclose in its financial statements.

ESMA notes that the IFRS IC concluded that the principles and requirements in existing IFRS provide an adequate basis for an entity to determine the accounting for such arrangements. ESMA agrees with the Committee's conclusions.

ESMA is conscious that, in the absence of standard-setting activity by the IASB to address the specificities of reverse factoring arrangements, some diversity in practice may still persist especially for the degree of judgement involved in the approach to the classification of liabilities relating to these transactions, their presentation and the related disclosures. Therefore, until such a specific standard-setting solution is developed by the IASB, ESMA agrees with the usefulness of the proposed agenda decision and supports its finalisation subject to the following comments.

Firstly, ESMA would deem it useful that the IFRS IC spells out more clearly which considerations issuers should make in determining the nature of the liabilities that are part of a reverse factoring arrangement. As the tentative agenda decision indicates, this determination is necessary in order to identify the type of cash flows – whether operating or financing – that shall be presented pursuant to IAS 7 *Statement of Cash Flows*. For example, it may be helpful that the IFRS IC clarifies under which circumstances a liability is not a trade or other payable, but rather it represents borrowings of the entity and, therefore, it has to be presented as a financial liability, in accordance with paragraph 54 of IAS 1. Amongst others, potential indicators that can be considered are, for instance, the fact that the maturity of the liability to a financial institution is significantly longer than the initial maturity of the liability to the supplier and the fact that the financial institution receives compensation for the extension granted, as indicated in Decision EECS/0117-06 of ESMA's 21st *Extract from the EECS's Database of Enforcement*[1].

Secondly, ESMA supports the examples provided in the tentative agenda decision of factors that an entity might consider when assessing whether to present separately liabilities that are part of a reverse factoring arrangement. However, ESMA regrets that the tentative agenda decision does not address the presentation of items relating to reverse factoring arrangements in the statement of profit or loss and other comprehensive income. ESMA encourages the Committee to address this aspect to clarify, for example, whether the items relating to these arrangements should be classified as part of finance costs in accordance with paragraph 82(b) of IAS 1 or in a different line item. In this respect, ESMA also highlights the importance of ensuring consistency in the operating or non-operating classification across the primary statements of the different components stemming from these arrangements.

Thirdly, ESMA welcomes and agrees with the conclusion made by the Committee on the usefulness of the disclosure requirements in IAS 1 *Presentation of Financial Statements*, IAS 7 and IFRS 7 *Financial Instruments: Disclosures*. ESMA recalls that in its 2015 Statement[2] it encouraged issuers to disclose: (i) the accounting policy applied to the classification of reverse factoring arrangements; (ii) the judgements made by the management; (iii) the relevant provisions of those arrangements; (iv) the quantitative impact on their financial statements; and (v) how the arrangements are used to manage their liquidity needs. ESMA suggests that, when finalising its agenda decision, the IFRS IC makes reference to the importance of disclosing such aspects and, in particular, the judgments made and the accounting policies applied to these types of transactions.

Lastly, ESMA notes that the tentative agenda decision may be read as limiting the applicability of the disclosures in IFRS 7 to the cases where changes in liabilities arising from financing activities occur, as per the disclosure requirements in IAS 7. ESMA therefore encourages the Committee to: (i) clarify this aspect so to avoid any misunderstanding in the scope of the IFRS 7 disclosures; (ii) and consider recommending the IASB making narrow-scope amendments to the requirements in IFRS 7 to more explicitly address these transactions. In addition, when taking forward its project on *Primary Financial Statements*, ESMA encourages the IASB to

[1] ESMA32-63-334 – Report, 21st Extract from the EECS's Database of Enforcement, 31 October 2017

[2] 2015/ESMA1608 – Public Statement, European common enforcement priorities for 2015 financial statements, 27 October 2015

provide a specific example on the application of the principles for aggregation and disaggregation that can illustrate the presentation of items relating to reverse factoring transactions.

In case you have any questions or comments regarding this letter, please do not hesitate to contact me or Evert van Walsum, Head of the Investors and Issuers Department (Evert.vanWalsum@esma.europa.eu).

Yours sincerely,

Steven Maijoor

September 29, 2020

Ms Sue Lloyd,
Chair, IFRS Interpretations Committee,
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Sue,

Subject: Comments of the Institute of Chartered Accountants of India (the ICAI) on Tentative Agenda Decision (TAD) issued by IFRS Interpretations Committee on Reverse Factoring Arrangements

The Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India (ICAI) welcomes the opportunity to comment on above referred Tentative Agenda Decision of IFRS Interpretations Committee.

We agree with the overall conclusions in the TAD with regard to presentation and disclosures regarding liabilities involving reverse factoring arrangement in the statement of financial position and statement of cash flows. While deliberating the TAD, some of the ASB members highlighted the following issues:

1) The TAD specifies that where an arrangement involves reverse factoring, the entity shall present the liabilities as other payables together with trade payables if those payables have nature and function similar to trade payables. The TAD also prescribes that the said liability shall be presented separately (including disaggregation of trade and other payables) considering their size, nature or function. It was argued that since the entity has entered into a reverse factoring arrangement, nature of such liabilities is sufficiently different requiring separate presentation irrespective of the fact whether any additional security is provided or not and whether the terms of the liabilities that are part of the arrangement are substantially different or not compared to the terms of other trade payables of the entity.

2) TAD also specifies that if the trade payable is discharged, cancelled or expires as a result of entering into the reverse factoring arrangement, an entity derecognises the trade payable and recognises a financial liability payable to the financial institution and the same shall be presented applying IAS 1. Applying IAS 1, such liability may get presented as 'trade or other payables' or as 'other financial liability'. However, in such a situation, since the liability related to trade payable has been derecognised and the entity is no more liable to pay to the provider of goods and services and now the entity owes to the financial institution, the TAD may clarify that this liability should be presented as other financial liability and not as 'trade and other payables'.

IFRS Interpretations Committee may address the above concerns.

With kind regards,

CA. M.P. Vijay Kumar
Chairman
Accounting Standards Board
Institute of Chartered Accountants of India

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Sue Lloyd
Chair of the IFRS Interpretations Committee
Columbus Building
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Canary Wharf
London E14 4HD
United Kingdom

29 September 2020
602/636

Dear Ms Lloyd

Re.: Tentative Agenda Decision: Supply Chain Financing Arrangements – Reverse Factoring

The IDW appreciates the opportunity to comment on the above-mentioned Tentative Agenda Decision of the IFRS Interpretations Committee from June 2020.

We welcome the Committee's decision to provide guidance on reverse factoring arrangements, as this kind of transaction has become increasingly widespread in recent years. We would also support a standard-setting project regarding issues arising from such transactions, as we believe that such an approach could target the issues far more specifically than an agenda decision is able to. Moreover, any standard-setting project should not only address the disclosures necessary in the case of reverse factoring agreements, but also the interaction with the derecognition requirements in IFRS 9.

The key discussions we have been party to in this context concern the presentation of those payables subject to a reverse factoring arrangement. More specifically: whether such payables still be presented as trade payables. We appreciate the Committee's effort to clarify this issue. Nevertheless, we are concerned about a key aspect of the clarification, which is the reference to 'working capital'.

The Tentative Agenda Decision indicates that trade payables are 'part of the working capital used in the entity's normal operating cycle'. Although the term 'working capital' is also used in several IFRS, there is no clear and consistent definition in place. We are concerned that a decision as to whether payables are part of the working capital is likely to be highly judgemental and thus this reference might introduce further uncertainty into the accounting for supply chain financing arrangements. Therefore, we believe that the IASB should provide a framework for identifying working capital in order to ensure a common understanding and comparability between information reported by different entities. As we expect that the application of such a framework will still require significant judgement, we propose that – should this approach be pursued further – entities should be required to disclose their definition of working capital.

However, in our view, a more specific reference to the derecognition guidance in IFRS 9 and an explanation of the interaction with the presentation of the liability in accordance with IAS 1 could provide a basis for a more robust reporting approach for such transactions. It would be necessary to focus on legal extinguishment as well as on substantial modifications. In respect of substantial modifications, the quantitative test would generally not lead to derecognition, whereas a targeted qualitative assessment may nevertheless warrant the derecognition of the trade payables. Any recognised 'new' payable could then not be classified as a 'trade payable'. We recommend some specific guidance be given concerning how the qualitative assessment should be conducted for trade payables – that generally have an effective interest rate of zero. For example, the introduction of an element of interest may lead to the derecognition of the trade payables and trigger the recognition of a payable depicting a financing transaction.

We would be pleased to answer any questions that you may have or discuss any aspect of this letter.

Yours sincerely

Bernd Stibi
Technical Director
Reporting

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29 September 2020

Sue Lloyd
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Dear Ms Lloyd

Tentative agenda decision – Supply Chain Financing Arrangements – Reverse Factoring

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the June 2020 IFRIC Update of the tentative decision not to take onto the Committee's agenda the request for clarification on how to present liabilities to which reverse factoring arrangements relate and what information is required to be disclosed in relation to these arrangements in the financial statements.

We agree that the IFRS Interpretations Committee's conclusions regarding supply chain financing arrangements reflect the requirements of IFRS Standards.

We agree that the outcome of applying these requirements will lead to different presentations in the statement of financial position, within trade payables, other payables or in other financial liabilities depending on the terms of the arrangement and the relative similarity of the nature and function of the liability under the arrangement with more conventional trade payables. Whilst we agree with this outcome, we are concerned that users are not benefiting from a fuller understanding of these arrangements given the lack of specific disclosures required by IFRS 7. The Board may wish to consider adding to its agenda a project to improve disclosures in this area, potentially through illustrative examples, due to the increasing prevalence of alternative financing models such as these, and the move away from obtaining finance from a broad range of suppliers to a more concentrated approach with a single or small number of financial institutions or other funding vehicles. In particular, specific disclosures about the extent to which amounts are owed to parties other than the original supplier, irrespective of whether the amounts are included in trade or other payables, and the relative concentration of such amounts would provide users with information that currently is often not disclosed. Such disclosure would also counterbalance the fact that the term 'working capital', that is critical in determining whether a balance is a trade payable, is not defined.

Where an amount payable to an entity other than the supplier remains presented in trade and other payables, we would suggest additional disclosures including:

Deloitte.

- a description of the entity's approach to presentation of the arrangement and the judgements made in applying the policy;
- the carrying amount of the liabilities and the line items in which they are presented;
- how the entity manages and monitors these arrangements including any impact on the viability of the business; and
- changes to the arrangement in the period, or subsequently, that would impact presentation or result in a change of liquidity risk.

Whilst we agree that the conclusion reached by the IFRS Interpretations Committee regarding the classification of cash flows is consistent with the requirements in IAS 7 Statement of Cash Flows, we note that the application of these requirements to factoring and reverse factoring arrangements may distort the determination of cash flows from operations. We therefore agree that disclosure of such non-cash movements will be important in understanding how the arrangement is accounted for. In a reverse factoring arrangement where the liability has been classified as a borrowing in the statement of financial position the Committee's approach will result in a single financing cash outflow in the cash flow statement without any corresponding financing inflow or operating outflow. This will reflect the treatment in the statement of financial position but not that in profit or loss where there will be an operating expense. We draw to the attention of the Committee that this issue is not unique to reverse factoring, but also applies to trade receivables factoring. When an entity does not derecognise trade receivables and the factor receives the cash directly from the customer, if the transferor only recognises a financing cash inflow from the failed sale borrowing from the factor, it will have no cash outflow for the repayment of the deemed borrowing nor any cash inflow from its customers even though it has recognised revenue as an operating item. Similar to our suggestion that the Board should consider the need for additional disclosures to support the presentation in the statement of financial position, we would suggest that the Board also considers the need for additional disclosure to help users understand the effect of factoring and reverse factoring transactions on the statement of cash flows. This could include consideration of whether the guidance in IAS 7.43-44 should be expanded, for example by including factoring and supplier financing arrangements as examples of when disclosures of non-cash transactions may be relevant.

In terms of the drafting of the tentative agenda decision we believe that the current wording reflecting the definition of a reverse factoring arrangement is too narrow as it is not always the case that the financial institution is paid at a date later than suppliers are paid. As such, we would suggest the following editorial change (underlined):

"In a reverse factoring arrangement, a financial institution agrees to pay amounts an entity owes to the entity's suppliers and the entity agrees to pay the financial institution ***<u>at the same or a later</u>*** *date than suppliers are paid."*

In addition to the liquidity risks mentioned in the tentative agenda decision, we would suggest an additional risk be mentioned which is that an entity may become reliant on the extended financing terms provided by reverse factoring arrangements to manage liquidity risk through the option to pay the financial institution later than it would have paid the supplier(s). If a financial institution were to withdraw the arrangement this could adversely affect the entity's ability to settle liabilities, particularly if the entity were already in financial difficulties.

Finally, we would suggest that clarification be added to the paragraph commencing *'Paragraphs 33-35 of IFRS 7 require...'* that this applies in all cases and is not dependent upon the presentation in the statement of financial position as trade payables, other payables or other financial liabilities.

Deloitte.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0) 20 7007 0884.

Yours sincerely

Veronica Poole
Global IFRS Leader

September 29, 2020

IFRS Interpretations Committee
IFRS Foundation
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Canary Wharf
London E14 4HD
United Kingdom

Via Electronic Submission

Re: IFRS Open for Comments Document / Tentative Agenda Decision and comment letters: Supply Chain Financing Arrangements—Reverse Factoring

Dear Members of the IFRS Interpretations Committee:

BAFT (the Bankers Association for Finance and Trade) respectfully submits this letter in response to the IFRS Open for Comments Document / Tentative Agenda Decision and comment letters: Supply Chain Financing Arrangements—Reverse Factoring.

BAFT is an international financial services industry association whose membership includes nearly 300 financial institutions and solution providers throughout the global community. As a worldwide forum for analysis, discussion, and advocacy in international financial services, BAFT provides support to members that are active in trade finance and many of them actively engaged in providing supply chain finance solutions to their clients globally. As demonstrated during the COVID pandemic, such programs have proven essential for international commerce and a fully functioning global economy.

We are highly supportive of the IFRS Interpretations Committee's having taken up a review of the SCF Reverse Factoring (aka Payables Finance) technique that represents a significant and growing supply chain product for member banks and their clients globally.

BAFT developed a supply chain finance committee in 2013 to provide a forum for member banks focused on supply chain finance activities to have the opportunity to discuss challenges and best practices related to these products without antitrust related concerns. Additionally, in late 2019 BAFT set up a Supply Chain Finance Working Group to provide a framework to help clarify the use and structuring of payables finance programs. Please refer to this document entitled *Payables Finance Principles* which has recently been published.

It is with this backdrop that BAFT, on behalf of our member banks, advises you of our strong support for and endorsement of the IFRS Tentative Agenda Decision on Reverse Factoring published in June 2020. We offer some thoughts below on the wording contained in the Tentative Agenda Decision to not add Reverse Factoring to the IFRS standard setting agenda.

Under subheading Tentative agenda decision

> The language in final paragraph of this section does not reflect the actual arrangement. We therefore recommend that it be amended to read, "In a reverse factoring arrangement, a financial institution agrees to pay amounts an entity owes to the entity's suppliers in advance if elected by the supplier, and the entity agrees to pay the financial institution on the original due date."
>
> Please note that the commercial arrangement regarding due dates is between the entity and its supplier and does not include or concern the financial institution. The financial institution will separately offer to discount the invoice payment if requested to do so from the supplier without the knowledge of the entity.

Under Notes to the financial statements

> In the second paragraph beginning:
>
> "IFRS 7 *Financial Instruments: Disclosures* defines liquidity risk as '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'. The Committee observed that reverse factoring arrangements often give rise to liquidity risk because..:"
>
> We observe that the word "often" creates the impression that reverse factoring creates additional liquidity risk which should not be a predetermined assumption when taking into consideration the fundamentals of a Reverse Factoring Program. We therefore recommend that the word "often" be replaced by "could" in the sentence cited above to read:
>
>> "The Committee observed that reverse factoring arrangements could give rise to liquidity risk because…"

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At a time of increasing global liquidity concerns, BAFT and its member firms recognize the benefits of this trade finance product as an important source of liquidity for businesses of all sizes, especially to small and medium- sized enterprises and reaffirm our support for continued discipline relating to financial reporting and disclosure.

We thank you for the opportunity to provide comments. If you have any questions, please contact Stacey Facter, Senior Vice President, Trade Products at sfacter@baft.org.

Very truly yours,

Tod R. Burwell

Tod R. Burwell
President and Chief Executive Officer

MASB MALAYSIAN ACCOUNTING STANDARDS BOARD
LEMBAGA PIAWAIAN PERAKAUNAN MALAYSIA

30 September 2020

Ms. Sue Lloyd
Chair
IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Ms. Lloyd,

Tentative Agenda Decision: Supply Chain Financing Arrangements – Reverse Factoring

The Malaysian Accounting Standards Board (MASB) welcomes the opportunity to provide comments on the above Tentative Agenda Decision.

We agree with the Interpretations Committee's reasons set out in the Tentative Agenda Decision for not adding these items onto its agenda.

If you need further clarification, please contact the undersigned by email at beeleng@masb.org.my or at +603 2273 3100.

Thank you.

Yours sincerely,

TAN BEE LENG
Executive Director

Unit 13A-1, Menara MBMR, No. 1, Jalan Syed Putra, 58000 Kuala Lumpur.
Tel : (603) 2273-3100 Fax : (603) 2273-9400 Email : masb@masb.org.my Website : www.masb.org.my

IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4DG

Submitted electronically

30 September 2020

Dear Committee Members

Tentative Agenda Decision: Supply Chain Financing Arrangements—Reverse Factoring

I am writing on behalf of the UK Financial Reporting Council (FRC) to provide comments on the IFRS Interpretations Committee's Tentative Agenda Decision *Supply Chain Financing Arrangements—Reverse Factoring*, issued in June 2020[1].

We thank the Committee for its contribution to this important topic and the publication of the tentative agenda decision. After the collapse of a significant UK construction business in 2018, the reporting of supply chain financing arrangements has received much attention in the UK, and we are very clear that addressing any reporting weaknesses in this area is in the public interest.

Our research suggests that reverse factoring is a significant funding alternative for certain industry sectors. Nevertheless, we find a gap between the apparent prevalence of these transactions and the information disclosed in financial statements.

In September 2019 the Financial Reporting Lab of the FRC issued a report on *Disclosures on the sources and uses of cash*,[2] which also addressed reverse factoring. Our analysis showed that good reporting in this area is rare. To drive improvements, we provided practical guidance around the presentation and disclosure of these transactions in our report, which overlaps with the tentative conclusions reached by the Committee. We are, therefore, largely supportive of the content of the tentative agenda decision. Nevertheless, we have doubts whether guidance on existing requirements alone, will be sufficient to improve the quality if reporting.

The Committee discussed the merits of a possible narrow-scope standard setting project. We support a disclosure project to develop clear and specific disclosure requirements that focus the attention of preparers and auditors, provide additional information to users and facilitate effective enforcement. We urge the Committee to make this recommendation to the Board and would support the Committee and the Board in developing the proposals.

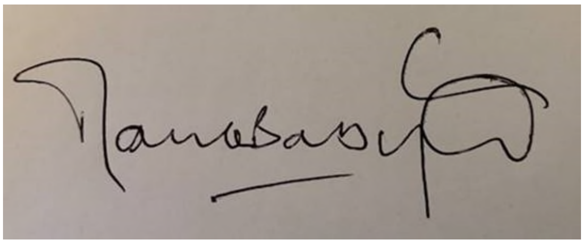
1 The views expressed by the FRC in this letter are separate from and will not necessarily affect the conclusions of any UK endorsement assessment of any new or amended International Accounting Standard.

2 https://www.frc.org.uk/getattachment/0689ba0c-2a23-4850-b0b9-8bec52938cce/Disclosures-on-the-sources-and-uses-of-cash-Final.pdf

Our detailed response to the tentative agenda decision is included in the Appendix to this letter.

If you would like to discuss these comments, please contact me or Susanne Pust Shah (s.pustshah@frc.org.uk).

Yours sincerely,



Mark Babington
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Appendix:

Presentation in the statement of financial position
IAS 1 *Presentation of Financial Statements* specifies requirements for the presentation of liabilities in an entity's statement of financial position. Paragraph 54 requires an entity to present 'trade and other payables' separately from other financial liabilities. 'Trade and other payables' are sufficiently different in nature or function from other financial liabilities to warrant separate presentation (paragraph 57 of IAS 1). Paragraph 11(a) of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* states that 'trade payables are liabilities to pay for goods or services that have been received or supplied and have been invoiced or formally agreed with the supplier'. Paragraph 70 of IAS 1 explains that 'some current liabilities, such as trade payables… are part of the working capital used in the entity's normal operating cycle'. The Committee therefore concluded that an entity presents a financial liability 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. Paragraph 29 of IAS 1 requires an entity to 'present separately items of a dissimilar nature or function unless they are immaterial'. Paragraph 57 specifies that line items are included in the statement of financial position when the size, nature or function of an item (or aggregation of similar items) is such that separate presentation is relevant to an understanding of the entity's financial position. Accordingly, the Committee concluded that, applying IAS 1, an entity presents: a. other payables together with trade payables only when those other payables have a similar nature and function to trade payables—for example, when other payables are part of the working capital used in the entity's normal operating cycle. b. liabilities that are part of a reverse factoring arrangement separately when the size, nature or function of those liabilities makes separate presentation relevant to an understanding of the entity's financial position. In assessing whether to present such liabilities separately (including whether to disaggregate trade and other payables), an entity considers the amounts, nature and timing of those liabilities (paragraphs 55 and 58 of IAS 1). The Committee observed that an entity assessing whether to present liabilities that are part of a reverse factoring arrangement separately might consider factors including, for example: a. whether additional security is provided as part of the arrangement that would not be provided without the arrangement.

b. whether the terms of liabilities that are part of the arrangement are substantially different from the terms of the entity's trade payables that are not part of the arrangement.

A1 We concur with the Committee's analysis and descriptions of the existing requirements in IFRS. In addition, our outreach has shown that users need clarity on where amounts subject to supplier funding arrangements have been included and the respective balances, but such disclosure is often lacking because not specifically required.

Derecognition of a financial liability
An entity assesses whether and when to derecognise a liability that is (or becomes) part of a reverse factoring arrangement applying the derecognition requirements in IFRS 9 *Financial Instruments*. An entity that derecognises a trade payable to a supplier and recognises a new financial liability to a financial institution applies IAS 1 in determining how to present that new liability in its statement of financial position (see 'Presentation in the statement of financial position').

A2 We concur that, although a complex area, IFRS provides adequate accounting requirements on derecognition for reverse factoring transactions.

Presentation in the statement of cash flows
Paragraph 6 of IAS 7 *Statement of Cash Flows* defines: a. operating activities as 'the principal revenue-producing activities of the entity and other activities that are not investing or financing activities'; and b. financing activities as 'activities that result in changes in the size and composition of the contributed equity and borrowings of the entity'. An entity that has entered into a reverse factoring arrangement determines whether to classify cash flows under the arrangement as cash flows from operating activities or cash flows from financing activities. The Committee observed that an entity's assessment of the nature of the liabilities that are part of the arrangement may help in determining the nature of the related cash flows as arising from operating or financing activities. For example, if the entity considers the related liability to be a trade or other payable that is part of the working capital used in the entity's principal revenue-producing activities, the entity presents cash outflows to settle the liability as arising from operating activities in its statement of cash flows. In contrast, if the entity considers that the related liability is not a trade or other payable because the liability represents borrowings of the entity, the entity presents cash outflows to settle the liability as arising from financing activities in its statement of cash flows. Investing and financing transactions that do not require the use of cash or cash equivalents are excluded from an entity's statement of cash flows (paragraph 43 of IAS 7). Consequently, if a cash inflow and cash outflow occur for an entity when an invoice is factored as part of a reverse factoring arrangement, the entity presents those cash flows in its statement of cash flows. If no cash flows are involved in a financing transaction of an entity, the entity discloses the transaction elsewhere in the financial statements in a way that provides all the relevant information about the financing activity (paragraph 43 of IAS 7).

A3 We concur with the Committee's analysis of the requirements for the presentation of reverse factoring arrangements in the cash flow statement.

A4 A clear analysis of cash generation and spending in an entity is vital for users, especially when the economy is under strain and liquidity risk is increased. To assess the quality of disclosures of cash flows and liquidity risks, in December 2019 the FRC announced a new Thematic Review – *Cash flows and liquidity disclosures*[3]. As part of this project we will review disclosures of supplier financing arrangements, when they are material. This work will inform us of progress made in terms of quality of disclosure of the impact of reverse factoring arrangements on cash flows and liquidity risk.

A5 We acknowledge that some prefer a grossed-up presentation of reverse factoring arrangements and hence would include cash flows in operating activities, even if they are notional amounts, ie amounts economically similar to inflows and outflows of cash, rather than actual cash in or outflows of the entity. However, a cash flow statement is a statement of cash in and outflows of the entity and the inclusion of notional amounts, even if that may seem useful, could obscure the "real" cash flows and thereby have a detrimental effect on the relevance of information.

A6 We prefer that non-cash transactions are transparently reported in the financial statements, for example through a reconciliation between cash flows and profit from

[3] https://www.frc.org.uk/getattachment/1336c2d2-718e-48f7-9eea-644d208e174f/CRR-Press-notice-CF-thematic.pdf

operating activities. IAS 7 limits the requirement to present non-cash transactions to investing and financing activities, although, as demonstrated for reverse factoring, they could also affect operating activities. We would therefore support extending the disclosure requirement in IAS 7 paragraph 43 to operating activities.[4]

A7 We also wanted to highlight where we believe the drafting of the agenda decision could be clarified. It currently reads:

Investing and financing transactions that do not require the use of cash or cash equivalents are excluded from an entity's statement of cash flows (paragraph 43 of IAS 7). Consequently, if a cash inflow and cash outflow occur for an entity when an invoice is factored as part of a reverse factoring arrangement, the entity presents those cash flows in its statement of cash flows. If no cash flows are involved in a financing transaction of an entity, the entity discloses the transaction elsewhere in the financial statements in a way that provides all the relevant information about the financing activity (paragraph 43 of IAS 7).

A8 The sentence starting "Consequently, if …" is confusing as it may be read to imply that a cash in or outflow might arise at the time an invoice is factored, when in practice we would not expect a cash in or outflow for the recipient of the services. We suggest that this sentence is deleted or the Committee clarifies in what instances it would expect cash in or outflows.

[4] In the FRC Discussion Paper *Improving the Statement of Cash Flows* published in 2016, we outlined some of the issues and possible solutions to the presentation of reverse factoring arrangements in the cash flow statement. https://www.frc.org.uk/getattachment/99748001-ddfb-4789-918b-569552416070/-;.aspx

Notes to the financial statements
Paragraph 44A of IAS 7 requires an entity to provide ‘disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes’. The Committee noted that such disclosure is required for liabilities that are part of a reverse factoring arrangement if the cash flows for those liabilities were, or future cash flows will be, classified as cash flows from financing activities. IFRS 7 *Financial Instruments: Disclosures* defines liquidity risk as ‘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’. The Committee observed that reverse factoring arrangements often give rise to liquidity risk because: a. the entity has concentrated a portion of its liabilities with one financial institution rather than a diverse group of suppliers. The entity may also obtain other sources of funding from the financial institution providing the reverse factoring arrangement. If the entity were to encounter any difficulty in meeting its obligations, such a concentration would increase the risk that the entity may have to pay a significant amount, at one time, to one counterparty. b. some suppliers may have become accustomed to, or reliant on, earlier payment of their trade receivables under the reverse factoring arrangement. If the financial institution were to withdraw the reverse factoring arrangement, those suppliers could demand shorter credit terms. Shorter credit terms could affect the entity’s ability to settle liabilities, particularly if the entity were already in financial distress. Paragraphs 33-35 of IFRS 7 require an entity to disclose how exposures to risk arising from financial instruments including liquidity risk arise, the entity’s objectives, policies and processes for managing the risk, summary quantitative data about the entity’s exposure to liquidity risk at the end of the reporting period (including further information if this data is unrepresentative of the entity’s exposure to liquidity risk during the period), and concentrations of risk. Paragraphs 39 and B11F of IFRS 7 specify further requirements and factors an entity might consider in providing liquidity risk disclosures. An entity applies judgement in determining whether to provide additional disclosures in the notes about the effect of reverse factoring arrangements on its financial position, financial performance and cash flows. The Committee observed that: a. assessing how to present liabilities and cash flows related to reverse factoring arrangements may involve judgement. An entity discloses judgements that management has made in this respect if they are among the judgements made that have the most significant effect on the amounts recognised in the financial statements (paragraph 122 of IAS 1). b. reverse factoring arrangements may have a material effect on an entity’s financial statements. An entity provides information about reverse factoring arrangements in its financial statements to the extent that such information is relevant to an understanding of any of those financial statements (paragraph 112 of IAS 1). The Committee noted that making materiality judgements involves both quantitative and qualitative considerations.

A9 We concur with the Committee’s observations regarding the required disclosures in the notes. However, we have doubts whether this list, although helpful, will drive the improvements we are seeking. We therefore support a narrow scope disclosure standard setting project.

A10 As noted in Staff Paper 2 of the Committee’s meeting in June 2020, users of financial statements look for additional information when reverse factoring arrangements are material, but they are missing because they are not explicitly required. We support disclosures around the items listed in paragraph 57 (a) to (d) of that paper, which include:

(a) the total amounts subject to reverse factoring arrangements;

(b) where, and how, an entity has classified associated amounts in the statements of financial position and cash flows;

(c) the nature of reverse factoring arrangements, including any credit term extensions, the effect of the arrangement on the entity’s days payable ratio and the duration of that effect (for example, to understand whether improvements in the ratio is one-off or expected to occur in future periods); and

(d) the risks to which the entity is exposed, for example liquidity risks from reverse factoring arrangements and how the entity manages those risks.

Kirsten Elce
Head of Group Accounting,
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Chair, IFRS Interpretations Committee
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30 September 2020

Dear Ms Lloyd,

Tentative agenda decision – Supply Chain Financing Arrangement – Reverse Factoring

In response to your invitation to comment, and as a preparer of accounts under International Financial Reporting Standards, I am pleased to provide our comments on the Committee's tentative agenda decision.

While we broadly agree with the tentative agenda decision, we suggest that examples be provided to assist preparers in determining what factors should be considered when assessing whether liabilities under reverse factoring arrangements are substantially different from trade payables that are not part of such arrangements.

An important application issue regarding the IFRS 9 Financial Instruments de-recognition criteria for financial liabilities is whether interest charged by the financial institution, implicitly or explicitly, should be considered in the assessment of whether the liability arising from a reverse factoring arrangement is 'substantially different'. Does it make a difference if the previous terms with the suppliers did not include an interest charge if the payable was settled within the agreed payment terms? Can the IFRIC provide examples of how the IFRS 9 de-recognition criteria should be applied? How does an entity measure 'substantially different' in the context of trade payables?

The use of the phrase 'substantially different' is unhelpful because it does not set a meaningful threshold and therefore there is a risk that preparers with the same circumstances could report a similar transaction differently leading to diversity in application. Could the IFRIC consider using 'materially different', which would allow entities to base the assessment on the impact on decision-making?

Kirsten Elce
Head of Group Accounting, Reporting & Internal Audit

To the members of the IFRS Interpretations Committee (IFRIC)

Submitted electronically

Subject: Eumedion response to IFRIC's tentative agenda decision on Supply Chain Financing Arrangements

Ref: B20.18

The Hague, 30 September 2020

Dear members of IFRIC,

Eumedion appreciates the opportunity to respond to the IFRIC's tentative agenda decision on Supply Chain Financing (SCF) arrangements. Eumedion is the dedicated representative of the interests of 50 institutional investors, all committed to a long term investment horizon. Eumedion aims to promote good corporate governance and sustainability in the companies our participants invest in. We regard accounting standards as a critical part of a global financial infrastructure, especially since investors are dependent on the quality of accounting standards for allocating their own and entrusted capital. Together our participants invest over € 6 trillion of capital in equity and corporate non-equity instruments.

We are supportive of the tentative agenda decision. We observe rather infrequent disclosures on and separate presentations of SCF arrangements, while financial institutions do actively provide such services to listed entities. There is a risk that investors are often not informed of material SCF arrangements. Although this could well be an enforcement issue, we do expect that the tentative agenda decision will contribute to the proper application and enforcement of the Standards.

However, even with the agenda decision in place, an important characteristic of SCF liabilities for investors is likely to remain unreported. The economic substance of SCF liabilities will be interpreted by many investors as being partly in-substance payables and partly in-substance financial liabilities owed to a financial institution. This is especially true for SCF arrangements that increase the payment terms for the reporting entity. Doubling the payment term can be interpreted as a significant change in payment terms and thereby result in classification of the entire amount as an SCF financial liability. However, for many investors, halve of that amount would be regarded by many as an in-substance payable, and not an in-substance financial liability. If the payment terms for the reporting entity were 12 months, up from one month; only an approximate 8.3% (1/12th) of the reported SCF liability would be interpreted by many as an in-substance payable.

We therefore suggest that IFRIC complements its final agenda decision with a call on the IASB to introduce a requirement to disclose in the notes the actual net amount of credit that the financial institution provides to the reporting entity as a consequence of the SCF arrangement on the reporting date; i.e. the amount that the financial institution owes from the reporting entity under the SCF arrangement less the amount the financial institution owes to the suppliers of the reporting entity under the SCF arrangement on the reporting date.

A requirement to disclose this amount helps investors making several better assessments. Such requirement allows investors to continue to track how working capital requirements are developing over time. With an unknown part of the in-substance payables in financial liabilities, tracking working capital becomes either meaningless or requires time-consuming and likely quite inaccurate judgments.

From a valuation perspective, there is an intrinsic difference between a payable and a financial liability, even though both are liabilities. Payables contribute to a lower working capital. The lower or even the more negative working capital is, the less financial liabilities or equity an entity needs to finance its growth. Generally, the more the growth of the company can be financed by its suppliers, i.e. the more negative working capital is, the higher the market valuation of the equity such entity is. This argument reverses for financial liabilities: the more a company depends on financial liabilities to finance its growth, the lower the equity valuation of a company is. The suggested requirement allows for a more accurate valuation of a company.

There is also a liquidity dimension. Suppliers tend to be much more lenient towards their clients in their terms for providing credit, than financial institutions are. Unlike financial institutions, the margins of individual suppliers on the products and services sold generally provide a buffer against some debtors' inability to pay. Generally, listed entities don't go bankrupt because they fail to pay their suppliers, but because they fail to secure (re-)financing at financial institutions. If a financial institution cancels a supply chain finance arrangement, the milder short term consequence is that the entity will need to renegotiate new payment terms directly with its suppliers. It is likely that the payment terms that the suppliers agreed to through the original arrangement will be a starting point for such negotiations. The potentially major consequence is that the entity will need to repay or refinance the in-substance financial liability. The in-substance financial liability is the amount that resulted from the actual difference in the payment term of the entity to the financial institution and the payment term of the financial institution to the suppliers. So for liquidity and continuity assessments, a disclosure requirement that allows investors to calculate a split of the SCF liability in a payables and a financial liability is also relevant.

Without the requested disclosure requirement, many investors are likely to assume that all of the reported SCF liabilities are in-substance financial liabilities, which would in many cases be overly pessimistic.

If the members of IFRIC would like to discuss our views in further detail, please do not hesitate to contact us. Our contact person is Martijn Bos (martijn.bos@eumedion.nl, +31 70 2040 304).

Yours sincerely,

Rients Abma

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***Subject**: Tentative Agenda Decision and comment letters: Supply Chain Financing Arrangements—Reverse Factoring*

Dear colleagues ,,

I would like to thank you all , for the bright recognized efforts you performed in the *Tentative Agenda Decision and comment letters: Supply Chain Financing Arrangements—Reverse Factoring*.

You may find my responses to the exposure draft on pages (2-4)

Kindly , if any additional further explanation is needed , in relation to the responses or suggested comment , it will be my pleasure to respond to you using below contact.

Thanks

Your sincerely ,,

Shady Mehelba

Chartered public accountant -Egypt

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Comment :-

I agree with committee in relation to its response of using IAS 1 par.29 , with some points in relation to derecognition and classification in IFRS 9 that I configured that may be enhanced by more deliberations and more analysis , although IAS 1 deals with presentation in financial statements (Par .29) which more relevant to the issue regard aggregating or disaggregating the liabilities arise from reverse factoring

Finally , the user present in financial statement(accordance to IAS 1) items such meet the appropriate classification as per IFRS 9 , accordingly I think giving more analysis to different forms of reverse factoring or limited the response to situation of factoring invoice for received goods with determined fixed price with different credit terms will be of more benefit in decision

IFRS 9 has separate section for reclassification of financial assets . on the other hand for the financial liabilities essence , the financial liability can not be reclassified Par. 4.4.2 , accordingly the issue relate to derecognition and recognition not presentation or separation from payable , that may need the criteria referred to under the derecognition of financial liability section in IFRS 9 to be adequately met and carefully assessed against liabilities that would have been generated by reverse factoring arrangement

I believe that The depth analysis and further deliberation with other comments may enhance the following point of views :-

1- The different position to debtor and financial institution in such arrangements

The committee, when referred to derecognition of financial liability ,may support its response using criteria as indicated in Par B3.3.4 IFRS 9

"If a debtor pays a third party to assume an obligation and notifies its creditor that the third party has assumed its debt obligation, the debtor does not derecognise the debt obligation unless the condition in paragraph B3.3.1(b) is met. If the debtor pays a third party to assume an obligation and obtains a legal release from its creditor, the debtor has extinguished the debt. However, if the debtor agrees to make payments on the debt to the third party or direct to its original creditor, the debtor recognises a new debt obligation to the third party."

In such paragraph , we can find clear cut requirement for the debtor to recognize a new debt obligation when the debtor is obliged to third party based on the information that third party assumed the liability

Also Based on such Paragraph , I did not find reference to core of reverse factoring in relation to its type which may take several forms , one of the forms is the assumption of liability by financial institution or other third parties and other may take form of just assignment of liability or agency relationship with financial institution

In some instances, the debtor still guarantees to financial institution payment from specific account within specific period

while such arrangements may take several forms of imputed goods finance , letter of credits issued by financial institution to finance purchase or direct invoice factoring , in fact principle stated by committee is stabilizing the treatment as if it takes one form, accordingly more analysis and deliberations are required regard the situation whether the payment by financial institution is before receiving goods and service according to authorized or approved proforma or represent specific financial institution terms in its substance that may result in different presentation through payable ,overdrafts and cash and cash equivalents that meet such obligation

The different terms of each type of reverse factoring including degree of assumption/assignment /payment and guarantee of payment to third party will affect depend on whether the characteristics of cashflow will be materially different under the new arrangement

As a consequence we may find financial institution act only as intermediate party with finance or admin minimum charge or may assume the liability , we may in future find a way after deliberating the other comments to separate such two situation with appropriate classification criteria that affect presentation

2- The financial institution arrangement and process of handling cashflow of arrangement

Taking into account that the assignment of liability to financial institution may include ordering of purchase by its client with approving specific purchase invoice which mean that payment of debt occurred prior to receiving goods which formulate pure borrowing or under some jurisdictions when agreed to be with specific amount above purchase price and although it may represent time value of money it may represent morabha in Islamic finance if the terms were adequately conform with such definition .

And although credit period may not vary or exceed one year the finance charge is imposed at rate probably if company heavily use such agreement will be material , and accordingly even shorter in term is essential when financial institution evaluate for such customer credit facilities

From the other side , the customer of financial institution when have charges will have undue cost and effort to split those relate to normal characteristics of previous account and those differ from it , (for ex. Payment prior to receiving goods for 6 month to vendor as advance is not the same as payment vendor six moth later from receiving goods, working as agent for customer of financial institution not as working by substitution) these leave a scope of variety of presentation and may affect representation faithfulness if no adequate guide exist

Accordingly different terms may lead also to different presentation , using even feeding cash account as per agreement of financial institution may even affect presentation under certain agreement and require to offset debit account with overdraft of reverse factoring with such debit account if criteria is met in such agreement . Especially if specific collection were linked to such agreement in case of corresponding factoring of specific customers' receivable contract collection.

3- The change in terms which represent by change in cashflow characteristics

The reverse factoring's different terms from the original invoice terms are not specifically stated within the paragraphs of derecognition of financial liability Par 3.3.1-5 , although Par.3.3.2 refer to change of terms among lender and borrower , this paragraph finalized by conclusion of recognition of new liability and extinguish of old liability , although reference

to change in terms of any financial liabilities whether to lender or vendor may lead to same conclusion

In further deliberations it may be suggested to add sub paragraph to Par. 3.3.2 that describe such situation of exchanging cashflow terms and characteristics under reverse factoring of payable invoiced to describe whether the case represent transfer of contractual obligation to deliver cash flow to vendor that resulted in different characteristics cash flow or providing guide how to assess such change in characteristics

PO Box 1411
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30 September 2020

Ms Sue Lloyd
Chair IFRS Interpretations Committee
International Accounting Standards Board
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Online submission: https://www.ifrs.org/projects/work-plan/supply-chain-financing-arrangements-reverse-factoring/

Dear Sue

Tentative agenda decision - Supply Chain Financing Arrangements—Reverse Factoring

I am pleased to make this submission on the above Tentative Agenda Decision (TAD) relating to Supply Chain Financing Arrangements—Reverse Factoring.

I have extensive experience in accounting advice on International Financial Reporting Standards across a wide range of clients, industries and issues in the for-profit, not-for-profit, private and public sectors.

My clients have included listed companies, unlisted and private companies, charitable and not-for-profit organisations, federal, state and local government departments and agencies in the public sector, and government owned corporations (government business enterprises). I also have some commercial, standard setting and academic experience.

Overall

I agree broadly with the TAD, and with the IFRS Interpretations Committee not adding the issue to its agenda. I do not believe that standard setting is required.

I note the issue submission refers to the significant and widespread failure to provide sufficient information on these arrangements.

I found the TAD and staff papers well researched and explained. However, I did not find anything significant that preparers and their auditors could not have found themselves. I see no reason for the widespread failure of preparers to apply (and their auditors to enforce) existing standards.

Definition of Trade Payables.

I do not agree with the restrictions in the TAD applied to classifying a financial liability as a trade payable. In particular, I do not believe that a liability is required to be to the original supplier, or that the liability is required to be due within 12 months (if the operating cycle is 12 months).

Obligation to a supplier

The TAD refers to the reference in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* to trade payable as being to a supplier:

> trade payables are liabilities to pay for goods or services that have been received or supplied and have been invoiced or formally agreed with the supplier.

While I would agree with the reference as a good summary, I do not believe that the reference should be considered comprehensive and exclusive. The reference appears almost as a throw-away line in a standard not related to financial liabilities.

I believe that many obligations to pay for supplies that are refinanced by a financial institution, or other entity, remain in the nature of trade payables. In particular, if the only change to the obligation is that the obligation is to a different entity and for a later date. The underlying obligation is still linked to the original purchase, and the due date is also linked to the original purchase date, even if later. The balance of the obligation to the new lender will be an accumulation of multiple amounts, with multiple due dates.

For example:

- An obligation for $1,100,000 for goods delivered on 15 April, supplier to be paid 15 May, amount due to financier 15 July (Invoice 01)
- An obligation for $2,200,000 for goods delivered on 20 May, supplier to be paid 20 June, amount due to financier 20 August (Invoice 02)

  As at 30 June, the balance owing is:

$1,100,000	Due 15 July (Invoice 01)
$2,200,000	Due 20 August (Invoice 02)

- An obligation for $3,300,000 for goods delivered on 25 July, supplier to be paid 25 August, amount due to financier 25 October (Invoice 03)

  As at 31 July, the balance owing is:

$2,200,000	Due 20 August (Invoice 02)
$3,300,000	Due 25 August, then later 25 October (Invoice 03)

This balance (an accumulation of individual “drawdowns” and varying due dates) contrasts to the usual bullet payment due date of borrowings.

Treating the reverse factoring obligation as a trade payable would also have some advantages:

- it would likely result in any cash flows being treated as operating cash flows – consistent with traditional arrangements of paying a supplier.
- arrangements where there is a direct drawdown of funds by a supplier, with the obligation to repay being incurred by the reporting entity, would be treated similarly to when a supply invoice was sent to the reporting entity and then refinanced.

As noted in the TAD, presentation of a separate line item because of the amount being a different nature (e.g. for interest bearing trade payables) may be warranted/

An implication of including outstanding reverse factoring balances as trade payables will be that an interest cost will be recognised on amounts that are not classified as debt. Additional information, as required under existing standards, can be made to avoid any confusion.

Being part of working capital

The TAD requires that for an obligation to be part of trade payables, that the obligation is "part of the working capital used in the entity's normal operating cycle".

While working capital is not defined in IFRSs, it is commonly defined as current assets less current liabilities.

I do not agree that trade payables are required to be payable within 12 months (the usual length of a company's operating cycle). While trade payables are commonly due within 12 months, like inventory and trade receivables, I do not agree with a bright line excluding items from trade payables (or inventory or trade receivables), if the cash flow is not expected within 12 months.

Future standard setting

As I stated above, I see no reason for the widespread failure of preparers to apply (and their auditors to enforce) existing standards. I do not believe that additional standard setting will provide benefits exceeding the costs.

Hopefully, the issue of the TAD will provide sufficient impetus for preparers and auditors to comply with current requirements and provide sufficient information for users to understand these arrangements.

Yours sincerely,

David Hardidge
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Ms Sue Lloyd
Chair of the IFRIC

Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

30 September 2020

REF: TAD Supply Chain Financing Arrangements – Reverse Factoring

The Office of the Chief Accountant of the Securities and Exchange Commission of Brazil – CVM welcomes the opportunity to respond to the TAD Supply Chain Financing Arrangements – Reverse Factoring.

We are a division of the national securities regulator engaged in the study and development of accounting standards, interpretations and guidance for Brazilian listed companies and investment funds. By endorsement of CVM, the accounting standards issued by the Brazilian Accounting Pronouncements Committee – CPC become mandatory for these issuers.

One of the legal mandates of CVM is to stimulate savings and its application in securities through the efficient and regular functioning of capital markets. To stimulate permanent investment in shares of publicly held companies and investment funds we are convinced that a good quality set of accounting standards play a central role in achieving these objectives.

If you have any questions about our comments, please do not hesitate to contact us at snormas@cvm.gov.br

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The Office of the Chief Accountant welcomes the opportunity to comment on the IFRIC's TAD related to Supply Chain Financing Arrangements – Reverse Factoring.

Overall, we generally support the analysis drawn in the TAD and its conclusions regarding derecognition, presentation and the relevant disclosures to be included in the notes to the financial statements. We think requirements in current standards give an adequate basis to preparers about how to account for liabilities that were subject to reverse factoring. All relevant facts and circumstances should be taken into account in analysing whether the liability should be derecognised and whether the trade payable should be presented as another liability in the statement of financial position. Therefore, we also agree with Committee's conclusion not to add this matter to its standard-setting agenda.

Nevertheless, we would like to share our concerns about some parts of the TAD that may have unintended consequence of possible misintepretation by entities when entering into a reverse factoring arrangements. Our concern is related to the following passage of the TAD:

> **Derecognition of a financial liability**
>
> An entity assesses whether and when to derecognise a liability that is (or becomes) part of a reverse factoring arrangement applying the derecognition requirements in IFRS 9 *Financial Instruments*.
>
> An entity that derecognises a trade payable to a supplier and recognises a new financial liability to a financial institution applies IAS 1 in determining how to present that new liability in its statement of financial position (see 'Presentation in the statement of financial position').

We would like to highlight that IAS 1 should be applied to determine how to present a liability that was subject to a reverse factoring arrangement irrespective of whether that liability was derecognised according to IFRS 9. Consequently, we ask the Committee to better clarify this aspect in the TAD, making it clear that an entity should apply IAS 1 to determine how to present a liability in the statement of financial position when such liability is subject to a reverse factoring arrangement, even though the liability is not derecognised according to IFRS 9.

Yours sincerely,

Paulo Roberto Gonçalves Ferreira
Chief Accountant

FINANCIAL REPORTING COUNCIL OF NIGERIA
Federal Ministry of Industry, Trade and Investment

September 29, 2020

The IFRS Review Team
IFRS Foundation
Columbus Building
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Canary Wharf, London
E14 4HD
United Kingdom

Dear Sir/Madam,

Comment Letter on IFRS Interpretations Committee Tentative Agenda Decision on Supply Chain Financing Arrangements - Reverse Factoring

The Financial Reporting Council of Nigeria (FRC) hereby avails its input alongside its constituents in Nigeria on the IFRS Interpretations Committee (Committee) Tentative Agenda Decision on Supply Chain Financing Arrangements - Reverse Factoring

In view of the responses received from the constituents in Nigeria, the Council wish to comment that we align with the Committee that the principles and requirements in IFRS Standards, particularly IAS 1 *Presentation of Financial Statements, IFRS 7 Financial Instruments Disclosures, and IAS 37 Provisions, Contingents Assets and Contingents Liabilities* offer adequate bases for entity to determine the presentation and disclosures of liabilities which are part of reverse factoring arrangements.

More so, the Council, in agreement with its constituents align with the decision of the Committee not to add the matter to its standard-setting agenda. This is because the Council believes there are no accounting issues/challenges in respect of the presentation and disclosures of liabilities which are considered to be part of a reverse factoring arrangement.

If you require any further information or clarification, do not hesitate to contact the Head, Directorate of Accounting Standards (Private Sector) on:
teosawe@financialreportingcouncil.gov.ng

Yours faithfully,

Titus E. Osawe
Head, Directorate of Accounting Standards – Private
For:Executive Secretary/CEO

MAZARS

Mrs Sue Lloyd

IFRS Interpretations Committee Chair

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La Défense, 30 September 2020

Tentative Agenda Decisions – IFRS- IC Update June 2020

Re: Supply chain financing arrangements – reverse factoring (IAS 1 Presentation of Financial Statements)

Dear Sue,

MAZARS is pleased to comment on the abovementioned IFRS Interpretations Committee Tentative Agenda Decision, published in the June 2020 IFRIC Update.

We welcome the attempt of the Committee to provide guidance on this topic, that has been the focus of many questions in the past few years in relation with the increase in the number of this kind of arrangements.

Regarding the **presentation in the statement of financial position**, we think that the key distinction many users would like to see clarified is whether reverse factoring (RF) liabilities should be classified as "trade and other payables" or as "financial liabilities" line items, according respectively to IAS 1 § 54 (k) and (m). We therefore appreciate the objective of the Committee to provide criteria in order to decide whether RF liabilities are to be presented separately but would suggest the Committee clearly states that their purpose is to help distinguishing between these two classifications.

We do support the principle set out by the Committee, namely that the classification of the Reverse Factoring (RF) liability should depend on **whether its terms are substantially different from the usual terms of trade payables**, taking into account the entity-specific environment.

Nevertheless, we think the proposed criteria may not always be operational, because they either may not be discriminating enough, or they rely on concepts not defined by the standards, such as working capital. We acknowledge that the application of any set of criteria to RF transactions will require a significant amount of judgment given the wide diversity of contracts, jurisdictions, local regulations and practices that exist in this area. Therefore, we think it should be complemented by adding and enhancing disclosures in the notes to the financial statements, in line with the proposals of the Committee.

Regarding the **derecognition** of the financial liability, we agree that an entity that derecognises a trade payable to a supplier and recognizes a new financial liability to a financial institution applies IAS 1 in determining how to present that new liability in its statement of financial position. However, we think the Committee should clarify the interaction between the derecognition analysis and the presentation according to IAS 1. For example, to what extent the derecognition of a RF liability should entail that the new liability is classified as an "other financial liability" (IAS 1.54(m))?

Another frequent situation is when the maturity of a trade payable included in a RF arrangement can be significantly extended beyond that of usual trade payables in the economic environment of the entity, without triggering the derecognition of the financial instrument. In this case, we would suggest reclassifying the RF trade payable as an "other financial liability" starting from the date where its maturity starts to exceed that of usual trade payables. For that purpose, we would encourage the Committee to clarify that a reclassification of a financial instrument may be required even if the transaction does not meet the conditions required for the derecognition of the financial instrument.

Regarding the **presentation in the statement of cash flows (SCF)**, we support the objective of the Committee to promote consistency of classification between SCF and Statement of Financial Position (SFP) in relation to the RF liability and agree that the SFP presentation should drive the SCF presentation. In this respect, we would suggest that a consistent wording should be used across the agenda decision for both purposes, such as "working capital" and "normal operating cycle", and to avoid using the criterion of "principal revenue-producing activities" , which is specific to SCF, for SFP presentation purposes. Besides, while we agree with the Committee that when "the liability represents borrowings of the entity, it should not be presented as a trade payable", we think this statement should be better positioned in the SFP part of the decision.

Regarding the impact of non-cash transactions, we agree that "Investing and financing transactions that do not require the use of cash or cash equivalents are excluded from an entity's statement of cash flows". In RF arrangements, a (kind of) non-cash transaction may arise upon reclassification of a RF liability from "trade and other payables" to "other financial liabilities", which would occur on the date when its maturity starts to exceed those of usual trade payables. This could be considered as giving way to an operating cash outflow and a financing cash inflow. Since these cash flows cannot be reflected in the SCF due to the scope exclusion of IAS 7 § 43, we support the Committee's view that "the entity discloses the transaction elsewhere in the financial statements in a way that provides all the relevant information about the financing activity", which could be here to describe the implicit cash flows related to this reclassification.

MAZARS

We nevertheless question the relevance of a SCF that would only include few cash outflows from operating activities, on the basis that the settlement of the liabilities for buying materials, goods or services is finally classified within cash flows from financing activities due to RF arrangements. Therefore, we believe that the Committee should refer that issue to the Board, so that it could examine whether the SCF should include some non-cash transactions in order to improve its relevance.

Regarding the **notes to the financial statements,** we approve the objective of the Committee to enhance disclosures in the notes to the financial statements, in relation to RF liabilities. We believe indeed that IFRS 7 already provides room for relevant disclosure on liquidity risk. In this respect we suggest that for trade payable included in RF arrangements, a maturity analysis should be disclosed , according to IFRS 7 § 39 a) and § B11, at a more granular level than for banking liabilities, using for example time bands such as 1-3, 3-6, 6-9, or 9-12 months.

In addition, we fully support the development of specific and targeted disclosure requirements within a **narrow-scope standard-setting project**, as it might indeed help bridging the expectation gap expressed by many users regarding financial information on RF arrangements and more generally supply chain financing arrangements.

Should you have any questions regarding our comments on the tentative agenda decisions, please do not hesitate to contact Edouard Fossat (+33 1 49 97 65 92).

Yours faithfully,

Michel Barbet-Massin

Edouard Fossat