IFRS

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STAFF PAPER

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IASB® meeting

Project	**Supplier Finance Arrangements**
Paper topic	Feedback Summary—Examples added to disclosure requirements

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Objective and structure

1. As discussed in Agenda Paper 12A, this paper summarises respondents' comments on examples proposed in the Exposure Draft *Supplier Finance Arrangements* to be added to disclosure requirements in IAS 7 *Statement of Cash Flows* and IFRS 7 *Financial Instruments: Disclosures*. The Exposure Draft proposed to add supplier finance arrangements as an example within paragraph 44B of IAS 7 (which requires an entity to disclose information about changes in liabilities arising from financing activities) and paragraphs B11F and IG18 of IFRS 7 (which requires an entity to disclose information about its exposure to liquidity risk).

2. This paper includes:

   (a) background (paragraphs 4–8);

   (b) summary of feedback (paragraphs 9–20); and

   (c) questions for the IASB.

3. Some respondents made wording suggestions that we will consider in drafting but are not summarised in this paper.

Background

Changes in liabilities arising from financing activities—non-cash changes

4. As explained in paragraph BC16 of the Basis for Conclusions on the Exposure Draft, users of financial statements (investors) find it difficult to understand the effects of supplier finance arrangements on an entity's operating and financing cash flows. To help in this respect, the IASB decided to add supplier finance arrangements as an example in paragraph 44B of IAS 7 to highlight the importance of providing information about non-cash changes in liabilities arising from financing activities that arise from supplier finance arrangements. Such non-cash changes may not be apparent to investors without the disclosure highlighted by the proposed amendments to paragraph 44B.

5. In the Exposure Draft, the IASB proposed to add sub-paragraph (da) to paragraph 44B of IAS 7 as follows [new text is underlined]:

> 44B To the extent necessary to satisfy the requirement in paragraph 44A, an entity shall disclose the following changes in liabilities arising from financing activities:
>
> …
>
> <u>(da) non-cash changes arising from supplier finance arrangements (as described in paragraph 44G), for example when future cash outflows will be classified as cash flows from financing activities; and</u>…

Quantitative liquidity risk disclosures

6. As explained in paragraphs BC21–BC22 of the Basis for Conclusions on the Exposure Draft, reverse factoring arrangements often give rise to liquidity risk because, by entering into such an arrangement, an entity typically has concentrated a portion of its liabilities with one or a few finance providers (rather than a diverse group of suppliers). Investors need information to help them assess the effect of supplier finance arrangements on an entity's exposure to liquidity risk and risk management. The liquidity risk disclosure

requirements in IFRS 7—which apply to recognised and unrecognised financial instruments—are already comprehensive. The IASB decided that there is no need to add to them as part of this project but instead decided to add supplier finance arrangements as an example within the liquidity risk disclosure requirements in IFRS 7 to highlight the importance of providing liquidity risk information about these arrangements.

7. In the Exposure Draft, the IASB proposed to amend sub-paragraph (a) and add sub-paragraph (j) to paragraph B11F of IFRS 7 as follows [new text is underlined]:

> B11F Other factors that an entity might consider in providing the disclosure required in paragraph 39(c) include, but are not limited to, whether the entity:
>
> (a) has committed borrowing facilities (eg commercial paper facilities) or other lines of credit (eg stand-by credit facilities or supplier finance arrangements (as described in paragraph 44G of IAS 7)) that it can access to meet liquidity needs;
>
> …
>
> (j) has supplier finance arrangements (as described in paragraph 44G of IAS 7) that provide the entity with extended payment terms or that provide the entity's suppliers with early payment terms.

8. The IASB also proposed to amend paragraph IG18 of IFRS 7 as follows [new text is underlined, deleted text is struck through]:

> IG18 Paragraph 34 requires disclosure of quantitative data about concentrations of risk. For example, concentrations of credit risk may arise…
>
> Similar principles apply to identifying concentrations of other risks, including liquidity risk and market risk. For example, concentrations of liquidity risk may arise from the repayment terms of financial liabilities, sources of borrowing facilities~~, or~~ reliance on a particular market in

which to realise liquid assets, or supplier finance arrangements (as described in paragraph 44G of IAS 7) resulting in the entity concentrating with finance providers a portion of its financial liabilities originally owed to suppliers….

Summary of feedback

Introduction

9. Most respondents agree with the proposals, largely for the reasons set forth in the Exposure Draft, to add supplier finance arrangements as an example within the requirements to disclose information about changes in liabilities arising from financing activities and about an entity's exposure to liquidity risk. One accounting firm agrees with the proposals; that respondent observes that the disclosure requirements in IFRS 7 are principles-based and the disclosure requirement in paragraph 39(c) might already be considered to require an entity to disclose information about its use of supplier finance arrangements if their use affects how an entity manages liquidity risk. The respondent nonetheless says the inclusion of supplier finance arrangements as an example of borrowing facilities in paragraph B11F of IFRS 7 clarifies that the disclosure requirements in IFRS 7 apply to such arrangements.

10. Some respondents—including preparers and preparer bodies—disagree with adding examples to IAS 7 and IFRS 7 because, for example, they disagree with the need for the project overall, say more transaction examples would be needed to address various permutations of supplier finance arrangements, or say the examples should clarify that no disclosures would be required if the entity's payment terms remained unaffected by their use of supplier finance arrangements.

11. Many respondents make suggestions to clarify or enhance the proposals to amend paragraph 44B of IAS 7 and paragraphs B11F and IG18 of IFRS 7. This feedback is organised as follows:

(a) IAS 7: changes in liabilities arising from financing activities—non-cash changes (paragraphs 12–15); and

(b) IFRS 7: quantitative liquidity risk disclosures (paragraphs 16–2).

Changes in liabilities arising from financing activities—non-cash changes

Suggestions to clarify or amend the examples

12. Many respondents, including accounting firms, accountancy bodies, regulators, standard-setters and individuals, agree with the proposed non-cash changes example but raise questions about its applicability to operating cash flows. In particular, many respondents say paragraph 44B(da) focuses only on the effect of supplier finance arrangements on the changes in liabilities arising from financing activities; that paragraph either is unclear about, or explicitly excludes, the corresponding effect on changes in liabilities arising from operating activities. These respondents ask the IASB to clarify the scope of the example. Some of these respondents say that, without clarification, the amendments would not achieve their intended purpose or will give rise to confusion. For example, the South African Institute of Chartered Accountants says:

> Concerns were raised that it is not clear whether these disclosure requirements are only applicable when the cash flows are classified as financing cash flows rather than operating cash flows. It is suggested that this be clarified. In the case where the current proposed disclosure only captures financing cash flows, it is requested that additional disclosure be required to provide transparent and prominent disclosure of how operating cash flows are impacted by supplier finance arrangements.

13. Some respondents, including a standard-setter, an accounting firm, and an accountancy body, suggest that the IASB add a specific requirement to paragraph 44B for non-cash transactions. For example, Mazars says:

> We consider that the Board should clarify the requirement so that the entity provides quantitative information on the non-cash transactions that occurred. Such disclosure shall be required for

> each reporting period where non-cash transactions have a material effect on the statement of cash flows. It will probably be a recurring disclosure rather than a disclosure only upon the first application of a supplier finance arrangement. It should help users as well to understand the amount of cash outflows from financing activities that are in substance the final operating cash payment.

14. A few respondents, including an individual and a standard-setter, request clarification about gross versus net cash flows and whether entities should present notional cash inflows and outflows. For example, Kim Chiu Chua says:

> It is not clear whether the disclosure of this type of non-cash changes means presenting, in the statement of cash flows, a notional cash (hence 'non-cash') outflow from operating activities and a notional cash inflow from financing activities simultaneously. I suggest that the Board clarify this to promote consistent interpretation by different entities.

15. Respondents, including standard-setters, accounting firms, an accountancy body and a preparer, provide other suggestions for the IASB to clarify the non-cash changes example:

    (a) clarify whether gross cash flows may exist if, for example, the financial institution acts as an entity's paying agent in a reverse factoring arrangement;

    (b) extend the disclosure requirement for non-cash transactions in paragraph 43 of IAS 7 to supplier finance arrangements arising from operating activities;

    (c) remove the word 'non-cash' from paragraph 44B(da) because it causes confusion and supplier finance arrangements can involve cash transfers as well as non-cash transfers; and

    (d) provide the example at a more detailed level, explaining in which cases future cash outflows will be classified as cash flows from financing activities.

Quantitative disclosures about liquidity risk

Suggestions to clarify or amend the examples

16. Some respondents, including investor bodies, an accounting firm and a standard-setter, say the proposals to amend paragraph B11F of IFRS 7 would result in no change in disclosure practices because of the way the proposed amendments are worded. For example, the Corporate Reporting Users Forum says:

> …paragraph B11F states that Supplier Finance Arrangements are one of a number of 'other factors' that an entity 'might consider in providing the disclosure required in paragraph 39C'. From an investor point of view this seems to create no obligation on boards to report on the implications for liquidity risk of SCF arrangements. It allows scope for boards to remain silent on the issue and, even when challenged, to claim that they 'considered' SCF arrangements but decided not to report on them and to do so without providing any justification for their decision.

17. Another investor body makes the same comment and suggests that the IASB change 'might consider' to 'should consider' in paragraph B11F. An accounting firm similarly suggests that the amendment to the disclosures in paragraphs B11F and IG18 should be included in a separate paragraph using the word 'should' (or 'shall') instead of 'might'.

18. Some respondents, including standard-setters, preparers, accounting firms, an investor and an accountancy body, recommend that the IASB more explicitly and specifically require quantitative liquidity risk disclosures for supplier finance arrangements. For example:

    (a) explicitly require an entity to disclose the existence of a concentration of risk to a specific supplier finance provider or providers, rather than related to supplier finance arrangements in general as referred to in paragraph IG18.

    (b) provide a more precise description of the quantitative disclosures on concentrations of liquidity risk that would be required—for example, the number of finance providers, any factoring limits granted and for which term, and the extent to which the limits were used.

(c) require disclosures regarding banks and their roles in these transactions, including the names of the banking institutions involved and any overlap in institutions that are also providers of committed credit facilities to the debtor.

(d) consider requiring disclosures by *suppliers* for the impact of supplier finance arrangements on their liquidity risk. A preparer says a supplier could suffer if such an arrangement would be withdrawn and would have to consider the disclosure requirements of paragraph B11F(a); this respondent suggests the IASB clarify this requirement because the proposals are only focused on disclosures by the customer.

19. Some respondents request other clarifications, for example:

(a) a standard-setter and a group of standard-setters ask whether the amendments to paragraph IG18 would require disclosure of a 'whole chain' of finance providers. For example, the Hong Kong Institute of Certified Public Accountants says:

> We note that in certain financing arrangements, the finance providers may be acting as a conduit or an intermediary to spread the credit risk of the reporting entity to multiple finance providers…. As the reporting entity may not know the finance provider's back-end arrangements on its debt, it may not be able to identify the ultimate finance providers in such case…. [t]he ED is not clear as to whether…paragraph IG18 would require an entity to disclose information only up to the party with whom it contracted or information that covers the whole chain of SFA. Accordingly, we suggest that the IASB clarify the extent of disclosure that is required under paragraph IG18…

(b) a preparer says the proposed amendment to paragraph B11F(a) of IFRS 7 should be revised because it implies that supplier finance arrangements are similar to credit facilities; not all supplier finance arrangements constitute lines of credit that an entity can access to meet liquidity needs.

(c) a law firm suggests that the IASB delete the amendments to paragraph B11F(a) and rely instead on the amendments to paragraph B11F(j). They view it as unhelpful to include supplier finance arrangements within a paragraph dealing with loans, possibly implying that supplier finance arrangements are akin to loans.

(d) an accounting firm questions the need for the disclosure in proposed paragraph B11F(j) of IFRS 7 given the broad description of supplier finance arrangements; all such arrangements may not affect an entity's liquidity risk.

(e) a preparer suggests that the level of detail provided in relation to an entity's supplier finance arrangements should be commensurate with the level at which the entity's risks have changed due to the arrangements, rather than requiring an entity to include a mandatory list of disclosures.

20. A few respondents make comments about other aspects of IFRS 7. For example, an accounting firm suggests the IASB emphasise that it is likely that balances resulting from supplier finance arrangements would represent a separate class (or even several classes) for disclosure purposes applying paragraph 6 of IFRS 7, even if they are presented as trade payables in the statement of financial position under IAS 1.

Questions for the IASB

Does the IASB have any questions on the feedback presented in this Agenda Paper? Are there any topics on which IASB members would like more details in future meetings?