THE STANDARD STANCE

Supplier Financing Arrangements - Insights on the Proposed Disclosure Requirements Under Ind AS

Volume 18
January 2025

BACKGROUND

The use of supplier financing arrangements has grown significantly in recent years, driven by the increasing focus on cash flow management, the use of digital platforms, and the need for businesses to navigate supply chain challenges. As such arrangements increase, it becomes increasingly important that investors have transparency over the effect on the company's liabilities, cash flows and exposure to liquidity risk.

In response to the growing prevalence of supplier financing arrangements and their implications for financial transparency, on 25 May 2023, the International Accounting Standards Board (IASB) issued *Supplier Finance Arrangements*, which amended IAS 7 *Statement of Cash Flows* and IFRS 7 *Financial Instruments: Disclosures* (the Amendments), specifically targeting disclosure requirements. Corresponding to these amendments, the Accounting Standards Board of the Institute of Chartered Accountants of India has issued an Exposure Draft on *Supplier Finance Arrangements* - Amendments to Ind AS 7 and Ind AS 107 (ED/Ind AS 7 & Ind AS 107/2023/2) vide its notification dated 25 July 2023 with actual amendments to the Indian Accounting Standards expected soon. The amendments aim to enhance the visibility of supply finance arrangements in financial statements, enabling stakeholders to better assess the financial health and liquidity risks of entities engaging in supplier financing practices.

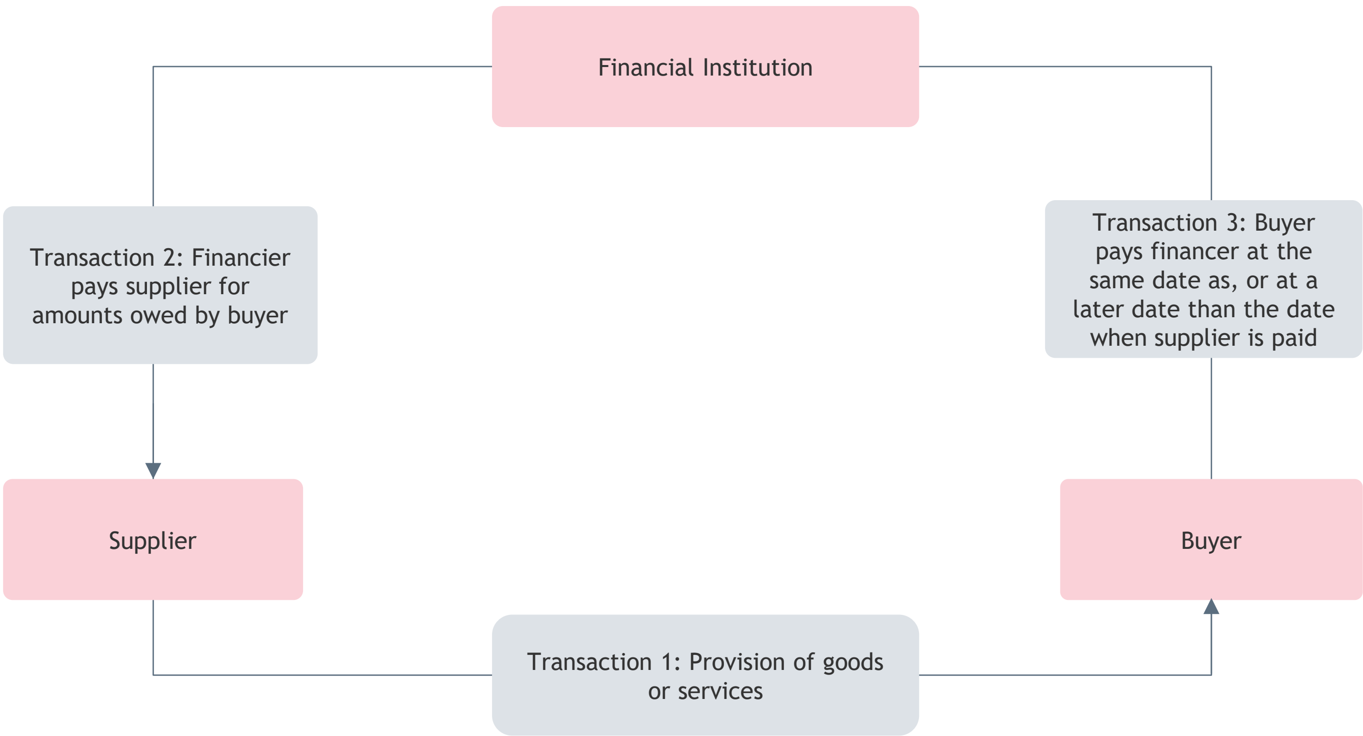
WHAT IS A SUPPLIER FINANCING ARRANGEMENT?

Supplier financing arrangements, often referred to as supply chain financing or reverse factoring, involve a third-party financial institution facilitating payments between a buyer and its suppliers. In such arrangements, the financial institution pays the supplier on behalf of the buyer, allowing the buyer to extend payment terms without affecting the supplier's cash flow. It is a working capital tool that allows businesses to optimise cash flow, improve working capital, and strengthen supplier relationships.

As supplier finance arrangements may evolve over time, the term has not been defined in either IAS 7 or IFRS 7 or in ED/Ind AS 7 and Ind AS 107/2023/2 because there is a risk of it becoming outdated as new practices and arrangements develop. Instead, the proposals in ED/Ind AS 7 and Ind AS 107/2023/2 describe the characteristics of a supplier finance arrangement in proposed paragraph 44G to Ind AS 7 as follows:

- One or more finance providers offer to pay amounts an entity owes its suppliers
- The entity agrees to pay the finance providers at the same date, or a later date, than when suppliers are usually paid
- Entity gets extended payment terms, or supplier gets early repayment terms, compared to the invoice payment due date
- Often referred to as 'supply chain finance', 'payables finance', or 'reverse factoring arrangements'

A typical Supplier Financing Arrangement



The proposed amendments clarify that the following are not supplier finance arrangements:

- Arrangements that are solely credit enhancements for the entity; for example, financial guarantees including letters of credit used as guarantees, and
- Instruments used by the entity to settle the amounts owed directly with a supplier; for example - credit cards

PROPOSED DISCLOSURE REQUIREMENTS IN IND AS 7

The objective of the disclosure requirements is for an entity to disclose information about its supplier finance arrangements that enables users of financial statements to assess the effects of those arrangements on the entity's liabilities and cash flows and on the entity's exposure to liquidity risk.

To meet the objectives described above, an entity shall disclose in aggregate for its supplier finance arrangements:

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

b) as at the beginning and end of the reporting period:

   (i) the carrying amounts, and associated line items presented in the entity's balance sheet, of the financial liabilities that are part of a supplier finance arrangement

   (ii) the carrying amounts, and associated line items, of the financial liabilities disclosed under (i) for which suppliers have already received payment from the finance providers

   (iii)the range of payment due dates (for example, 30–40 days after the invoice date) for both the financial liabilities disclosed under (i) and comparable trade payables that are not part of a supplier finance arrangement. Comparable trade payables are, for example, trade payables of the entity within the same line of business or jurisdiction as the financial liabilities disclosed under (i). If the ranges of payment due dates are wide, an entity shall disclose explanatory information about those ranges or disclose additional ranges (for example, stratified ranges).

c) the type and effect of non-cash changes in the carrying amounts of the financial liabilities disclosed under (b)(i). Examples of non-cash changes include the effect of business combinations, exchange differences or other transactions that do not require the use of cash or cash equivalents.

ILLUSTRATIVE DISCLOSURE

Note XX: Supplier Financing Arrangement

Qualitative information

In the ordinary course of business, the company enters into supplier financing arrangements with certain suppliers. These arrangements allow suppliers to receive early payment for their invoices through a third-party financial institution (the Financing Institution). The Financing Institution pays the supplier early at a discounted rate, and the company settles the outstanding balance directly with the Financing Institution at the end of the agreed-upon terms.

Quantitative information

	End of the reporting period 31.12.20X4	Beginning of the reporting period 1.1.20X4
Carrying amount of financial liabilities that are part of a supplier finance arrangement		
Presented in trade and other payable:	10,00,000	8,50,000
- of which suppliers have received payment from the finance provider	8,50,000	7,10,000
Range of payment due dates		
Liabilities that are part of the arrangements	XX-XY days after invoice date	XZ-ZX days after invoice date
Comparable trade payables that are not part of the arrangements	YY-YX days after invoice date	YZ-ZZ days after invoice date

Notes:

1) Type and Effect of Non-Cash Changes:

During the period, the following non-cash changes occurred in the carrying amounts of financial liabilities related to supplier financing arrangements:

a) Effect of Exchange Differences

The company has recognised non-cash exchange differences in the carrying amount of financial liabilities arising from supplier financing arrangements. The following describes the effect of exchange rate fluctuations on these financial liabilities:

i. Exchange Rate Impact on Financial Liabilities: *As of the balance sheet date, the carrying amount of financial liabilities related to supplier financing arrangements denominated in foreign currencies has increased/ decreased due to changes in foreign exchange rates. The net effect of these exchange rate movements resulted in a non-cash adjustment of INR XX million, which is reflected as part of the financial liabilities.*

PROPOSED DISCLOSURE REQUIREMENTS IN IND AS 107

Application guidance of Ind AS 107 (Ind AS 107.B11F) provides examples of factors that an entity might consider in providing liquidity risk disclosures. The Amendments have added supplier finance arrangements as another factor relevant to liquidity risk.

ILLUSTRATIVE DISCLOSURE

The company also participates in a supply financing arrangement with the principal purpose of facilitating efficient payment processing of supplier invoices. Such arrangements allow the company to centralise payments of trade payables to the bank rather than paying each supplier individually. While the arrangement does not significantly extend payment terms beyond the normal terms agreed with other suppliers that are not participating, the programme assists in making cash outflows more predictable.

TRANSITION AND EFFECTIVE DATE

The Exposure Draft issued by the ICAI has proposed that an entity shall apply the amendments for annual reporting periods beginning on or after 1 April 2024. However, it should be noted that as of the date of this publication, the Ministry of Corporate Affairs has not issued any notification with respect to these amendments.

As a part of transitional relief, the proposed amendments provide exemptions from certain disclosures (the illustrative dates provided below assume an entity with a March year-end and a 30 September interim financial statement issued in accordance with Ind AS 34. It is assumed that the entity applies the Amendments for annual reporting periods beginning on or after 1 April 2024):

Reporting Period	Disclosures Not Required And Example
For any reporting periods presented before the beginning of the annual reporting period in which the entity first applies the Amendments.	Comparative information. For example, in the entity's 31 March 2025 annual financial statements, disclosures for the 31 March 2024 comparative period are not required.
As at the beginning of the annual reporting period in which the entity first applies those amendments.	▪ The carrying amounts, and associated line items, of the financial liabilities for which suppliers have already received payment from the finance providers. ▪ Range of payment due dates for supplier finance liabilities and comparable trade payables that are not part of a supplier finance arrangement. This information is not required to be disclosed for the beginning of the annual reporting period in which the entity first applies the amendments (i.e. 1 April 2024).
For any interim period presented within the annual reporting period in which the entity first applies those amendments.	The information otherwise required to be disclosed by the Amendments. Therefore, the entity is not required to disclose any of the information otherwise required by the Amendments in its interim financial statements for its half-year ended 30 September 2024. However, it should be noted that when the entity prepares its interim financial statements for the half-year ended 30 September 2025, it will be required to disclose the information as required by the Amendments for the comparative period, i.e., for 30 September 2024.

OTHER ASPECTS

There are other aspects to consider when accounting for supplier finance arrangements like presentation on the balance sheet and the cash flow statement. These aspects are not addressed in the amendments.

Presentation in the balance sheet

Liabilities that are part of a supplier finance arrangement:

- can be presented as part of 'trade and other payables' only when those liabilities have a similar nature and function to trade payables (for example, when those liabilities are part of the working capital used in the entity's normal operating cycle); and
- must be presented separately when the size, nature or function of those liabilities makes separate presentation relevant to the understanding of an entity's financial position.

Presentation in cash flow statement

- If the entity considers the related liability to be a trade or other payable, cash outflows to settle the liability can be presented as arising from operating activities in its statement of cash flows.
- If the entity considers that the related liability is not a trade or other payable because the liability represents borrowings of the entity, cash outflows to settle the liability can be presented as arising from financing activities in its statement of cash flows.

CONCLUDING REMARKS

The proposed amendments under Ind AS on supplier financing arrangements represent a significant step towards improving financial statement transparency. By shedding light on these arrangements, the standard setters aim to provide stakeholders with a clearer understanding of a company's financial obligations and liquidity position, fostering better decision-making and market confidence.

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CONTACT US

For any content related queries, you may please write to the service line experts at accountingadvisory@bdo.in

For any other queries or feedback, kindly write to us at marketing@bdo.in

BDO IN INDIA OFFICES

Ahmedabad
Westgate Business Bay, Floor 6
Office No. 601, Block A, S.G. Highway
Makarba, Ahmedabad 380051, INDIA

Bengaluru - Office 1
Prestige Nebula, Floor 3
Infantry Road
Bengaluru 560001, INDIA

Bengaluru - Office 2
SV Tower, No. 27, Floor 3 & 4
80 Feet Road, 6th Block, Koramangala
Bengaluru 560095, INDIA

Bhopal
Floor 3, Pradhan Business Center
Ansal Pradhan Enclave, E 8 Arera
Colony Near Dana Pani Square,
Bhopal 462026, INDIA

Chandigarh
Plot no. 55, Floor 5
Industrial & Business Park
Phase 1, Chandigarh 160002, INDIA

Chennai
Olympia Cyberspace, Floor 10, Module 4
No: 4/22 Arulayiammanpet, SIDCO Industrial
Estate Guindy, Chennai 600032, INDIA

Coimbatore
Pacom Square, Floor 3, 104/1, Sakthi
Main Road, Bharathi Nagar, Ganapathy
Coimbatore 641006, INDIA

Delhi NCR - Office 1
Magnum Global Park, Floor 21, Archview
Drive, Sector 58, Golf Course Extn Road
Gurugram 122011, INDIA

Delhi NCR - Office 2
Windsor IT Park, Plot No: A-1
Floor 2, Tower B, Sector 125
Noida 201301, INDIA

Goa
BIZ – Nest, Floor 7
A Wing, Sunteck Corporate Park
Opp. Shram Shakti Bhavan, Patto
Panaji, Goa 403001, INDIA

Hyderabad
1101/B, Manjeera Trinity Corporate
JNTU-Hitech City Road, Kukatpally
Hyderabad 500072, INDIA

Kochi
XL/215 A, Krishna Kripa
Layam Road, Ernakulam
Kochi 682011, INDIA

Kolkata
Floor 4, Duckback House
41, Shakespeare Sarani
Kolkata 700017, INDIA

Mumbai - Office 1
The Ruby, Level 9, North West &
South East Wings, Senapati Bapat Marg
Dadar (W), Mumbai 400028, INDIA

Mumbai - Office 2
601, Floor 6, Raheja Titanium, Western
Express Highway, Geetanjali Railway
Colony, Ram Nagar Goregaon (E),
Mumbai 400063, INDIA

Mumbai - Office 3
Floor 20, 2001 & 2002 - A Wing, 2001-
F Wing Lotus Corporate Park, Western
Express Highway, Ram Mandir Fatak Road,
Goregaon (E) Mumbai 400063, INDIA

Pune - Office 1
Floor 6, Building No. 1
Cerebrum IT Park, Kalyani Nagar
Pune 411014, INDIA

Pune - Office 2
Floor 2 & 4, Mantri Sterling, Deep Bunglow
Chowk, Model Colony, Shivaji Nagar
Pune 411016, INDIA

Vadodara
1008, Floor 10, "OCEAN", Sarabhai
Compound, Nr. Centre Square Mall,
Dr. Vikram Sarabhai Marg Vadodara
390023, INDIA