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To the Point

FASB — final guidance

FASB requires disclosures about supplier finance program obligations

The guidance addresses the lack of transparency about the use of supplier finance programs.

What you need to know

- The FASB issued final guidance that requires entities to disclose the key terms of supplier finance programs they use in connection with the purchase of goods and services along with information about their obligations under these programs, including a rollforward of those obligations.
- The guidance does not affect the recognition, measurement or financial statement presentation of supplier finance program obligations.
- The guidance requires retrospective application to all periods in which a balance sheet is presented, except for the rollforward requirement, which will be applied prospectively.
- The guidance is effective for all entities for fiscal years beginning after 15 December 2022, including interim periods in those fiscal years, except for the rollforward requirement, which is effective for fiscal years beginning after 15 December 2023. Early adoption is permitted.

Overview

The Financial Accounting Standards Board (FASB or Board) issued **final guidance**[1] that requires entities that use supplier finance programs in connection with the purchase of goods and services to disclose the key terms of the programs and information about their obligations that are outstanding at the end of the reporting period.

Building a better working world

The guidance is intended to address requests from stakeholders for information about an entity's use of supplier finance programs and their effect on the entity's working capital, liquidity and cash flows. Stakeholders have observed an overall increase in the use of these programs but said the use of these programs was generally not apparent in financial statements or notes to the financial statements because there were no explicit disclosure requirements in US GAAP.

Companies seeking to maximize working capital sometimes negotiate extended payment terms with their suppliers and enter into supplier finance programs with third-party intermediaries, such as financial institutions or financial technology companies. While the terms vary, the programs generally involve a third-party intermediary processing an entity's payments for purchases from suppliers. The programs typically allow an entity to pay its invoices when due (under the extended terms negotiated with a supplier) and give the supplier the option to accelerate collection through a factoring arrangement it negotiates with the third-party intermediary.

The guidance does not affect the recognition, measurement or financial statement presentation of supplier finance program obligations, which are classified as either trade payables or bank debt, depending on the terms of the program.[2] The guidance also does not affect the accounting or disclosures by suppliers or third-party intermediaries involved in such a program.

Key considerations

Scope

The guidance applies to all entities that use supplier finance programs in connection with the purchase of goods and services. It describes a supplier finance program (which may also be referred to as reverse factoring or vendor payables financing) as an arrangement between what it refers to as a buyer party and a finance provider or intermediary that would allow the buyer's suppliers to request early payment from the finance provider or intermediary for invoices that the buyer has confirmed as valid. In the Background Information and Basis for Conclusions, the Board notes that such confirmation can be either positive or negative. That is, a buyer can confirm an invoice by saying it is valid or by not responding to the request for confirmation.

To determine whether a supplier finance program has been established, the guidance requires an entity to consider all available evidence, including arrangements between the entity and both (1) the finance provider or intermediary and (2) suppliers whose invoices have been confirmed as valid. Under the guidance, a buyer's commitment to pay a party other than the supplier for confirmed invoices "without offset, deduction or any other defenses to payment" is an indicator that the entity may have a supplier finance program, but it would not be determinative.

In the Basis for Conclusions, the Board notes that the guidance does not apply to credit card agreements because the supplier would have an option to request early payment from the finance provider in a supplier finance program, while a credit card agreement directs the finance provider to pay the supplier. Similarly, the guidance does not apply to payment processing arrangements because these arrangements do not result in suppliers having an option to request early payment. It also does not apply to normal factoring arrangements, because the buyer is typically not involved in the establishment of the arrangement with the finance provider and does not have to confirm the validity of invoices.

How we see it

The FASB said it decided to describe supplier finance programs generally and provide an indicator of when a program may exist rather than a prescriptive definition because the programs are relatively new and continue to evolve. As a result, entities will likely need to use judgment when determining whether they are parties to arrangements that are in the scope of the guidance. Management also will need to have processes and controls in place for making that determination.

Registrants should consider the SEC staff guidance on supplier finance programs to determine whether they need to provide disclosures in MD&A.

Disclosures

The guidance requires an entity that uses supplier finance programs to disclose the following information in the annual financial statements to help users understand the nature, activity during the period, changes from period to period and the potential magnitude of the programs:

- The key terms of the programs, including (1) a description of the payment terms, such as payment timing and the basis for its determination and (2) assets pledged as security or other forms of guarantees provided for the committed payment to the finance provider or intermediary
- The amount of the obligations outstanding at the end of the reporting period that the entity has confirmed as valid to the finance provider or intermediary (i.e., the amount of obligations that the buyer has confirmed as valid that remains unpaid by the buyer), where those obligations are presented in the balance sheet and the amounts presented in each line item in the balance sheet if they are presented in more than one line item
- A rollforward of those obligations presenting, at a minimum, the amount outstanding at the beginning of the reporting period, the amount added to the program during the reporting period, the amount settled during the reporting period and the amount outstanding at the end of the reporting period

If an entity has more than one program, it can aggregate disclosures, but not to the extent that useful information is obfuscated.

In interim periods, the guidance requires entities to provide the amount of the obligations outstanding at the end of the reporting period that the entity has confirmed as valid to the finance provider or intermediary (i.e., the amount of obligations that the buyer has confirmed as valid that remains unpaid by the buyer).

Other considerations

The Securities and Exchange Commission (SEC) staff has suggested that companies consider making disclosures in management's discussion and analysis (MD&A) if the effects of a supplier finance program are material to current-period liquidity or are reasonably likely to materially impact liquidity in the future.

At the 2019 AICPA Conference on Current SEC and PCAOB Developments,[3] Lindsay McCord, then Deputy Chief Accountant and now Chief Accountant in the Division of Corporation Finance, noted that while using these programs frequently improved companies' liquidity and operating cash flows, companies did not always disclose their use of this strategy.

At the 2021 AICPA conference, Ms. McCord reminded the audience that the SEC staff mentioned the use of supplier finance programs in its **guidance**[4] on making robust and transparent disclosures about financing activities companies were undertaking in response to COVID-19.

Separately, the International Accounting Standards Board issued a **proposal**[5] in November 2021 that would require new disclosures about supplier finance arrangements to enable users of financial statements to assess the effect of these arrangements on an entity's liabilities and cash flows.

How we see it

SEC registrants should consider the SEC staff guidance on supplier finance programs to determine whether they need to provide disclosures in MD&A.

Transition and effective date

The guidance is effective for all entities for fiscal years beginning after 15 December 2022, including interim periods within those fiscal years, except for the rollforward requirement, which is effective for fiscal years beginning after 15 December 2023. Early adoption is permitted.

During the fiscal year of adoption, entities are required to disclose in each interim period the key terms of the programs and the balance sheet presentation of the program obligations. Entities apply the guidance retrospectively to all periods in which a balance sheet is presented, except for the rollforward requirement, which is applied prospectively.

Endnotes:

[1] ASU 2022-04, *Liabilities — Supplier Finance Programs (Subtopic 405-50): Disclosure of Supplier Finance Program Obligations*.

[2] For more information about financial reporting considerations for supplier finance programs, see section 5.19 of our **Financial reporting developments publication, *Issuer's accounting for debt and equity financings (after the adoption of ASU 2020-06,* Accounting for Convertible Instruments and Contracts in an Entity's Own Equity).**

[3] See discussion in our publication, ***2019 AICPA Conference on Current SEC and PCAOB Developments: Compendium of significant accounting and reporting issues***.

[4] SEC Division of Corporation Finance CF Disclosure Guidance: Topic 9A, *Coronavirus (COVID-19) — Disclosure Considerations Regarding Operations, Liquidity, and Capital Resources*.

[5] IFRS Standards Exposure Draft, *Supplier Finance Arrangements: Proposed amendments to IAS 7 and IFRS 7*.