Applying IFRS

Accounting for payments from suppliers

January 2024

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Contents

What you need to know

- IFRS accounting standards do not contain explicit guidance on a customer's accounting for payments received (or receivable) from suppliers, so judgement will be required to account for these payments received (or receivable).
- Entities need to identify whether the payment received (or receivable) is in exchange for a distinct good or service transferred to the supplier. If so, entities account for it in the same way they would other similar sales or disposals of goods or services.
- If an entity receives payment from the supplier as a discount or rebate on purchased goods or services, the payment is deducted from the cost of the purchased good or service.
- If an entity receives payment as reimbursement of costs paid on behalf of the supplier, the payment offsets the expense incurred on behalf of the supplier.

Overview

The growth of e-commerce markets, the development of new platforms and tools, and changing customer demands have all influenced the interaction between retailers and suppliers in recent years. From simple rebates or incentives to complex co-operative arrangements, there are many reasons an entity might receive payments from its supplier. For example, a supplier might pay cash to a retailer in exchange for the retailer's cooperation with, or participation in, the supplier's marketing activities.

While IFRS accounting standards specifically address payments made by an entity to its customers, there is no one standard that addresses payments received by an entity from its suppliers. Instead, there are several requirements that might be applicable, depending on the specific facts and circumstances.

This publication discusses the key steps to consider when accounting for payments received (or receivable) from suppliers, considering the requirements in the various applicable IFRS accounting standards.

The views expressed in this publication represent EY's perspectives as of January 2024. Additional issues may be identified as we continue to analyse application of the various IFRS accounting standards, and our views may evolve during that process.

1. Overview of steps to apply when assessing payments from suppliers

While IFRS 15 *Revenue from Contracts with Customers* provides requirements for consideration paid (or payable) to a customer from the supplier's perspective, there is no single IFRS accounting standard, or set of requirements, that apply to customers when payments are received (or receivable) from a supplier (sometimes referred to as 'vendor allowances'). IAS 2 *Inventories* states that discounts, rebates and similar items are deducted from the cost of inventory,[1] but provides no further guidance. Similarly, IAS 16 *Property, Plant and Equipment* and IAS 38 *Intangible Assets* also require trade discounts and rebates to be deducted from the cost of an asset.[2]

Consideration received from a supplier can take many different forms. Therefore, entities need to carefully evaluate each transaction to determine the appropriate treatment of such amounts.

1.1 Understanding the context before analysing payments from suppliers

Before determining the appropriate accounting for payments from suppliers, an entity needs to understand the context of the payment and any related contract(s). To consider that context, guidance in IFRS 15 on the following topics will be relevant:

- Combining contracts entered into at, or near, the same time with the same customer (or related parties of the customer as defined in IAS 24 *Related Party Disclosures*)[3]
- Considering the relevant rights and obligations in agreements that are oral or implied by the entity's customary business practice, not only terms that are written[4]

Considering the wider context beyond specific contractual arrangements may also be necessary, for example, if more than one supplier is involved. If payments relate to more than one supplier, entities might need to apply judgement to attribute the payments to each supplier.

1.2 Steps to apply when analysing payments from suppliers

After determining the context of any payment, an entity will need to apply judgement to account for payments from suppliers and might need to apply various IFRS accounting standards.

How we see it

While entities will need to apply judgement, we believe there are some key steps that will assist entities in considering relevant requirements in IFRS accounting standards. These steps are illustrated in the following flow chart, and each is discussed further in the sections below.

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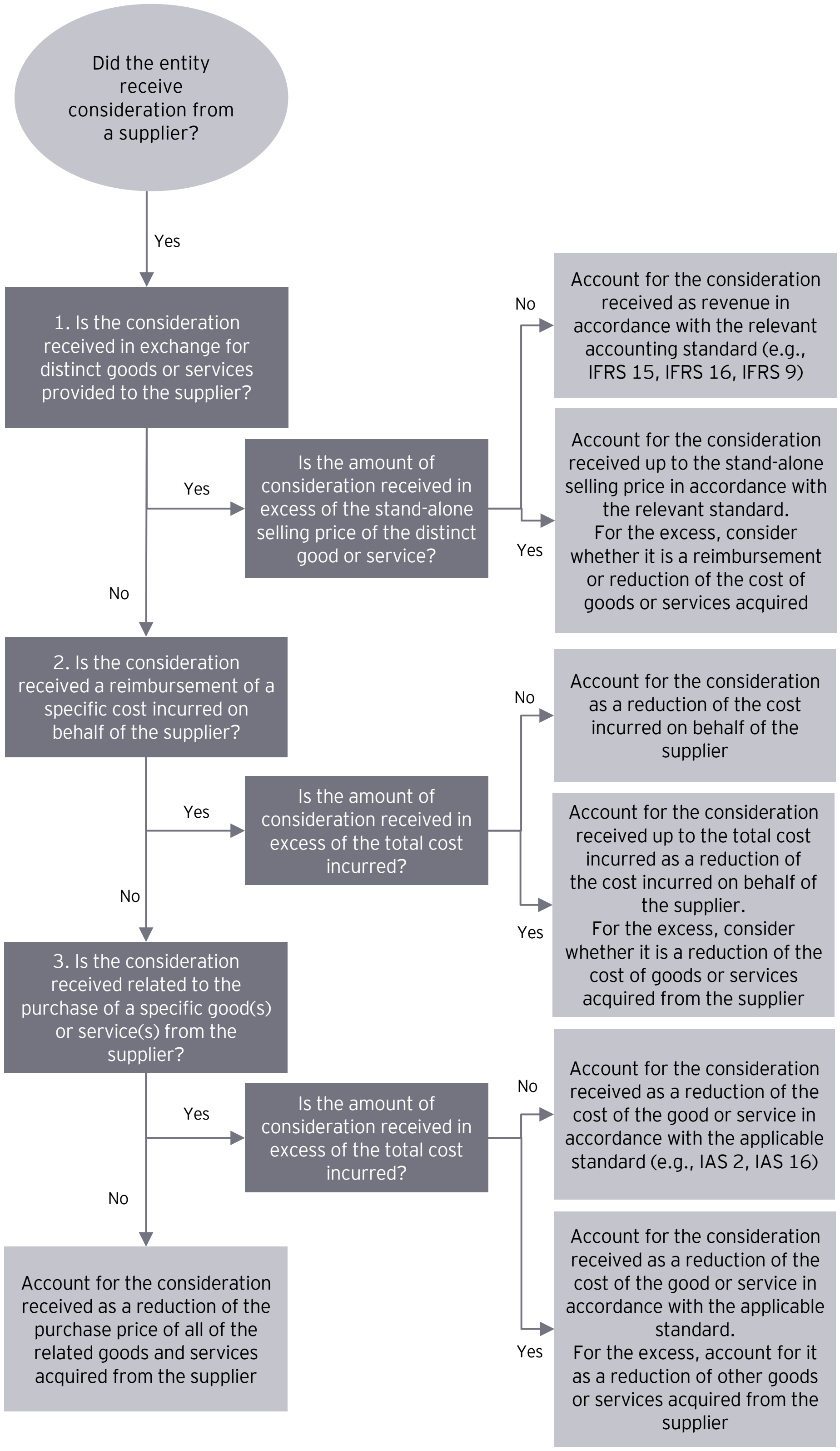
1 IAS 2.11.
2 IAS 16.16(a) and IAS 38.27(a).
3 IFRS 15.17.
4 IFRS 15.10.



As noted in these steps, the nature of a payment received from a supplier might not be clear or might be for more than one reason. Therefore, judgement may be needed based upon careful consideration of the nature of the payment and the contractual relationship between the parties.

1.3 Examples of payments received from suppliers

Some common examples of consideration received from a supplier include:

- *Co-operative advertising arrangements* — In some arrangements, an entity is reimbursed for a portion of the costs incurred to advertise the supplier's products. The determination of whether the payment from the supplier is in exchange for a distinct good or service transferred (see section 2 below) to the supplier at the stand-alone selling price will depend on a careful analysis of the facts and circumstances of the contract. In co-operative advertising arrangements that require the entity to incur a separate cost on behalf of the supplier related to advertising the supplier's products, the entity might be able to account for the consideration as a reduction of the costs incurred on behalf of the supplier (see section 3 below) instead of a reduction of the costs of products purchased from the supplier.
- *Slotting fees* — Retailers will commonly receive fees to place a supplier's goods prominently on store shelves. Slotting fees will generally be characterised as a reduction of the costs of goods purchased from the supplier once recognised in the income statement (see section 4 below) because the entity generally will be unable to demonstrate that it has provided a distinct good or service to the supplier that is separable from its purchase of the supplier's products, or that the consideration is the reimbursement of a separate cost incurred to sell the supplier's products.
- *Buydowns or margin/price protection* — A supplier might reimburse an entity up to a specified amount for shortfalls in the sales price received by the entity for the supplier's products. Buydowns generally do not provide a distinct good or service to the supplier, nor do they reimburse the entity for a separate cost incurred on behalf of the supplier. Accordingly, such payments will usually be accounted for as a reduction of the purchase price of goods or services acquired from the supplier (see section 4 below).
- *Coupons and rebates* — An indirect customer of a supplier (or end-customer) may receive a rebate or refund of a portion of the purchase price of a good or service acquired either by returning a form or coupon to the entity or the supplier. The entity may receive a payment from the supplier to reimburse the entity for any rebates or refunds provided to the end-customer. Similar to buydowns, payments to an entity as a reimbursement for coupons and rebates generally do not provide a distinct good or service to the supplier, nor do they reimburse the entity for a separate cost incurred on behalf of the supplier. Accordingly, such payments will usually be accounted for as a reduction of the purchase price of goods or services acquired from the supplier (see section 4 below).
- *'Pay to play' arrangements* — In some arrangements, an entity might receive an upfront fee from a supplier prior to, or in conjunction with, entering into a contract with the supplier. In most cases, these payments do not provide a distinct good or service to the supplier, nor do they reimburse the entity for a separate cost incurred on behalf of the entity. Accordingly, applying the requirements in IFRS 15 for consideration payable to a customer by analogy, such payments will usually be accounted for as a reduction of the purchase price of goods or services acquired from the supplier (see section 4 below).

2. Step 1: Does the entity provide something distinct in exchange for the payment from the supplier?

The first step is for an entity to assess whether the payment received (or receivable) from suppliers is in exchange for a distinct good or service transferred to the supplier. This is consistent with the requirements for consideration payable to a customer in IFRS 15.[5]

How we see it

Since IFRS 15 provides guidance on consideration paid (or payable) to a customer from the supplier's perspective, we believe it is appropriate for an entity, considering the requirements in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, to apply the requirements by analogy to payments received (or receivable) from suppliers from the customer's perspective.

2.1 Determining whether the payment is for a distinct good or service

To determine whether the payment is in exchange for a distinct good or service that the entity transfers to the supplier (in this instance, the supplier is seen as the customer), an entity first needs to determine whether it has promised anything in exchange for the payment it has received. For example, an entity might promise to provide goods or services (e.g., a research service to the supplier or a lease of equipment that is used in the manufacturing process of the supplier's products to be purchased by the entity). Conversely, it might perform administrative tasks that do not transfer a good or service to the supplier, and, therefore, there is no distinct good or service.

It is important for entities to identify all promised goods or services, including both explicit and implied promises or those included in other contracts or side agreements.

These promises might not be explicitly stated in the supply contract. That is, it is important for entities to first identify all promised goods or services, including those explicitly stated in the contract, as well as promises implied by customary practice and/or promises included in other contracts or side agreements. If they are not explicitly stated in any contract, an entity needs to consider all facts and circumstances to determine whether the supplier, has a valid expectation that the entity is promising to provide a good or service to the supplier.

If the entity identifies promised goods or services, applying the IFRS 15 requirements, it applies a two-step process for determining whether the promised good or service (or a bundle of goods or services) is distinct:[6]

- Consider at the level of the individual good or service whether the supplier (as a customer of the entity) can benefit from the good or service on its own or with other readily available resources (i.e., the good or service is capable of being distinct)
- Consider whether the good or service is separately identifiable from other promises in the contract (i.e., the promise to transfer the good or service is distinct within the context of the contract)

[5] IFRS 15.70-72.

[6] IFRS 15.27. Applying the requirements in IFRS 15 to determine distinct goods or services from a customer perspective is supported by the IFRS Interpretations Committee's March 2021 agenda decision on *Configuration or Customisation Costs in a Cloud Computing Arrangement*. See March 2021, *IFRIC Update*, available on the IFRS Foundation's website.

Both of these must be met to conclude that the good or service is distinct. If they are met, the individual good or service is accounted for as a separate unit of account, as discussed further in section 2.2 below.

An entity might need to apply significant judgement to evaluate whether a distinct good or service is identifiable. For example, in some cases, any goods or services transferred to the supplier might be used by the supplier to provide goods or services to the entity, and, therefore, might not be distinct (e.g., an entity provides a tool, mould or component part to the supplier that is used to manufacture goods that the supplier sells to the entity).

For further guidance on determining whether a good or service is distinct, refer to *International GAAP® 2024*, Chapter 27, sections 4.1 and 4.2, available on ey.com/IFRS.

Significant judgement might be needed to determine whether a distinct good or service is provided in exchange for any payments received from suppliers.

2.2 A distinct good(s) or service(s) is identified

If one or more distinct goods or services are identified, an entity needs to determine whether the consideration paid by the supplier exceeds the stand-alone selling prices of the goods or services provided:

- To the extent that the consideration is less than or equal to the stand-alone selling prices of the goods or services, the entity accounts for the sales or disposals of the goods or services in the same way that it accounts for provision of those goods or services to other customers or third parties, in accordance with the applicable IFRS accounting standard(s).

  If the entity provides those goods or services as part of its ordinary activities, accounting standards such as IFRS 9 *Financial Instruments*, IFRS 15 and IFRS 16 *Leases* might apply. For example, payments received from suppliers for the right to use one of the customer's assets for a period of time might be within the scope of IFRS 16, while payments for the issuance of financial instruments might be within the scope of IFRS 9.

  If the distinct goods or services are not part of the entity's ordinary operating activities, they could be disposals of property, plant and equipment or intangible assets, for example, which would be accounted for in line with IAS 16 or IAS 38, respectively.

- For any excess above the stand-alone selling prices, entities need to perform further analysis to determine whether that excess represents a reimbursement of costs incurred on behalf of a supplier (see section 3 below) or is a reduction of the purchase price of any goods or services acquired from the supplier (see section 4 below).

Illustration 2-1 — Market research service

Retailer A enters into an agreement to perform a significant amount of market research for Supplier B related to the launch of a new product. Supplier B believes that it is paying for the expertise and knowledge available from Retailer A. Retailer A believes Supplier B is electing to purchase its knowledge of the market rather than internally developing such knowledge. Retailer A regularly offers such services to its customers (including non-suppliers).

Based on an evaluation of the circumstances, the cash consideration received is in return for Retailer A providing distinct services to Supplier B. That is, using the guidance in IFRS 15 for identifying performance obligations, the market research services are determined to be capable of being distinct (because the market research is regularly sold separately to

Illustration 2-1 — Market research service

non-suppliers), as well as sufficiently separable (or distinct within the context of the contract), from Retailer A's purchases of Supplier B's goods.

Retailer A determines that the market research is distinct within the context of the contract because of the following:

- Retailer A is not providing a significant service of integrating the market research with the purchases of Supplier B's goods because the promises to Supplier B do not represent a bundle of integrated goods or services that represent a combined output.
- The market research provided by Retailer A does not modify or customise the purchases of Supplier B's goods. The market research and the purchases of goods are not being assembled together to produce a combined output.
- The market research is not highly interrelated or interdependent with the purchases of Supplier B's goods because the market research is not needed in order for Retailer A to purchase and then resell the goods. That is, there is not a two-way dependency between the promises.

The cash consideration received from Supplier B therefore needs to be accounted for as revenue in accordance with IFRS 15, provided that the cash consideration received does not exceed the stand-alone selling price of the distinct services received by Supplier B.

If the amount of cash consideration paid by Supplier B exceeds the stand-alone selling price of the distinct services, Retailer A would need to perform further analysis to determine whether that excess represents a reimbursement of costs incurred on behalf of Supplier B (see section 3 below) or is a reduction of the purchase price of any goods or services acquired from Supplier B (see section 4 below).

2.3 No distinct good or service is identified

If the entity does not identify a promised good or service in exchange for the payment from the supplier (either because there is no promise or because it is not distinct), it considers whether the supplier is reimbursing the entity for costs incurred on its behalf (see section 3 below) or the payment is a discount or rebate on goods or services purchased from the supplier (see section 4 below).

Illustration 2-2 — Slotting fees

A supermarket receives fees to place a supplier's goods prominently on its shelves (and not a particular shelf). Such fees are often referred to as slotting fees. The supermarket is not required to provide the supplier with any other goods or services in exchange for the payment.

The supermarket concludes the payment it has received is not in exchange for a distinct good or service it provides to the supplier. Therefore, it moves to Step 2 to determine whether the supplier is reimbursing the entity for costs incurred on its behalf (see section 3 below) or the payment is a discount or rebate on goods or services purchased from the supplier (see section 4 below).

3. Step 2: Is the supplier reimbursing the entity for costs incurred on its behalf?

An entity first needs to understand the nature of the reimbursement negotiated between the entity and the supplier and the entity should consider all facts and circumstances.

3.1 Determining whether the payment is a reimbursement

An entity could receive a payment from the supplier for reimbursement of costs incurred on the supplier's behalf. In some cases, this might indicate the entity is acting on behalf of the supplier as its agent. In other cases, an entity could enter into a contract with the supplier to pay certain amounts to end-consumers (the supplier's customers' customers) in advance and receive payments from the supplier for reimbursement of the amount it paid. Therefore, an entity first needs to understand the nature of the reimbursement negotiated between the entity and the supplier and the entity should consider all facts and circumstances.

IFRS accounting standards do not contain detailed guidance on payments received for reimbursement of costs incurred on the supplier's behalf, but factors to consider may include, but are not limited to:

- Whether there is a specific agreement with the supplier to incur the costs on their behalf and be reimbursed.
- Whether the costs to be reimbursed by the supplier are directly related to the activities that caused the costs.

  This might be clear if the costs are incremental (i.e., would not be incurred if the entity had not agreed to pay them on the supplier's behalf), but in other situations, it could require significant judgement.

  In some cases, the costs incurred might include internal costs that are directly related to the activities that are subject to reimbursement. While internal costs may be controllable costs of an entity, they might not be directly tied to consideration from the supplier. Despite this, in certain circumstances, an entity might be able to demonstrate that the internal costs would be directly related to the activities that are subject to reimbursement. For example, an entity might receive payments for making available (on a full-time basis) dedicated marketing staff to a supplier, who are instrumental in maximising the sale of the supplier's goods. If the staff's activities focus solely on goods or services provided by the supplier and a distinct good or service is not identified, the payments (or some parts of payments) might be deducted from the personnel costs recognised in the entity's financial statements.
- Whether the payment contains a margin exceeding the amount of the costs incurred. If so, this might indicate there is a service being performed or a good provided by the entity.

  In such a situation, the entity may need to reconsider Step 1 (see section 2 above) or consider whether the payment is for both a reimbursement and also in exchange for something else. For example, an entity could receive reimbursement for costs incurred in providing a good or service as the supplier's agent. On the other hand, reimbursement could be received by an entity for pass-through amounts to the customer on behalf of the supplier or the entity's margin/price protection rather than for costs incurred in the activities on the supplier's behalf.

Considering these factors, an entity needs to determine whether the payment is, in substance, a reimbursement of a supplier's cost. Often an entity may need to use judgement and this assessment should be based on the weight of evidence available.

3.2 Payments that are a reimbursement of costs incurred on behalf of a supplier

If the payments are a reimbursement of costs incurred on behalf of a supplier:

- Any payment received up to, and including, the amount of costs incurred on behalf of the supplier, would be deducted from the costs recognised in the entity's financial statements.
- Any amount exceeding the costs incurred would need to be further assessed under Step 3 to determine whether it is a discount or rebate on goods or services purchased from the supplier (see section 4 below).

Illustration 3-1 — Co-operative advertising arrangements

Supermarket A sells various products purchased from multiple suppliers. Supermarket A and some suppliers enter into a co-operative advertising arrangement to make a brochure for the upcoming holiday season to advertise specific products. Supermarket A and the suppliers agree to pay some parts of the printing and delivery costs of the brochure based on the relative space of each supplier's product in the advertisement. Supermarket A assesses the payment received in accordance with Step 1 and, considering the specific facts and circumstances, concludes that it is not providing a distinct service to the suppliers. Instead, it concludes it is a reimbursement for costs incurred on behalf of the suppliers.

When Supermarket A receives payments from the suppliers for reimbursement of the costs incurred in the co-operative advertising activities on the suppliers' behalf, these payments would be deducted from the advertising costs in the financial statements of Supermarket A. This is because the advertising costs are incurred to promote the sales of the specific products (or supplier) and the costs would not be incurred if Supermarket A and the suppliers had not entered into the arrangement.

3.3 Payments that are not a reimbursement of costs incurred on behalf of a supplier

If the payment does not represent a reimbursement, the entity would need to further assess the payment received under Step 3 to determine whether it is a discount or rebate on goods or services purchased from the supplier (see section 4 below).

Illustration 3-2 — Buydowns or margin/price protection

Manufacturer B agrees to reimburse Supermarket A up to a specified amount for shortfalls in the sales price received by the entity for Manufacturer B's products. Buydowns generally do not provide a distinct good or service to Manufacturer B, nor do they reimburse Supermarket A for a directly related cost incurred in selling Manufacturer B's products. Accordingly, such payments would be a reduction of the purchase price of goods or services acquired from Manufacturer B (see section 4).

4. Step 3: Is the payment a discount or rebate on goods or services purchased from the supplier?

Appropriately identifying which goods or services the payment relates to is important.

If the payment is not in exchange for a distinct good or service (see section 2 above) or a reimbursement of amounts paid on behalf of a supplier (see section 3), the payment will generally be part of a transaction in which the entity is purchasing something from the supplier – that is, a discount or rebate on a previous or upcoming purchase.

Appropriately identifying which goods or services the payment relates to is important in determining whether an IFRS accounting standard(s) specifically applies to such a payment, and the appropriate timing of recognition in profit or loss.

Payments should be:

- Linked to the specific purchase(s) to which it relates, if known

  Or

- Allocated to purchases from suppliers on a reasonable and consistent manner, to the extent that the consideration cannot be linked to a specific good(s) or service(s).

In some cases, purchases may relate to more than one supplier (e.g., co-operative advertising), and, therefore, specific attribution or allocation on a reasonable and consistent basis will be necessary.

Accounting for supplier consideration as a reduction of the cost of the purchased goods or services (applying the requirements in IFRS 15 for consideration payable to a customer by analogy) could result in delayed recognition in the income statement until the related goods or services are recognised in the income statement. In some arrangements, judgement may be required in order to apply payments from suppliers to the purchased goods or services. For example, if the level of purchases is initially unknown, an entity might need to estimate the expected purchases in the future in order to allocate the payments appropriately.

If a payment is specifically linked, or allocated to a recognised asset, a number of standards may be relevant. IAS 2, for example, applies to inventories an entity purchases from its suppliers. IAS 2.11 states that trade discounts, rebates and other similar items are deducted in determining the costs of purchase for the inventory. Even though payments from suppliers to customers are not explicitly addressed, the paragraph should also be understood to include cash incentives and other payments from suppliers. Such payments could come in various forms, including incentives paid that can be offset against future purchases and payments related to a specific purchase. To the extent that such payments relate to inventories that have been sold, the entity would account for them as a reduction of cost of sales.

However, in its November 2004 agenda decision, the IFRS Interpretations Committee clarified that "rebates that specifically and genuinely refund selling expenses would not be deducted from the cost of inventories"[7] (see section 3). As such, an entity receiving a payment from a supplier cannot default to treating any payment from a supplier from whom it purchases inventories as a reduction. Instead, it needs to determine the nature of the payment, which might require judgement.

[7] *IFRIC Update*, November 2004, available on the IFRS Foundation's website.

Illustration 4-1 — Discounts on inventories

Consider the fact pattern in Illustration 2-2 above, in which a supermarket concludes that slotting fees received are not received in exchange for a distinct good or service.

Assume that the master supply arrangement with supplier offers the supermarket discounted prices in exchange for prominence on store shelves. This discount is achieved through monthly payments and depends on the shelf position in a given month.

The supermarket determines that the nature of the payment is a discount on inventories. On that basis, it accounts for the payment as a reduction of the costs of purchase of inventories, or as a reduction of costs of sales if the inventories have already been sold.

Another accounting standard that could be applicable is IAS 16, which requires an entity to deduct trade discounts and rebates from the cost of an asset within the scope of that standard.[8] Similarly, IAS 38 also requires an entity to deduct trade discounts and rebates from the cost of intangible assets.[9]

If an entity concludes that the payment represents a rebate or discount on the purchase of an asset, care is needed if the payment is variable or contingent. This may be particularly challenging if the reason for the payment being variable or contingent is not within the entity or supplier's control. Further discussion is included in *International GAAP® 2024*, Chapters 17 and 18, available on ey.com/IFRS.

How we see it

Significant judgement will often be needed to appropriately attribute, or allocate, payments to good(s) or service(s) purchased from supplier(s). This is key to the timing of recognition. Given the judgement involved, entities may need to disclose additional information for material payments received from suppliers to assist users of financial statements.

[8] IAS 16.16(a).
[9] IAS 38.27(a).

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