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| Project | ***Annual Improvements*** **Project – 2009 - 2011 cycle** |
| Topic | **Regrouping and consistency of contingent consideration guidance** |

## Introduction

1. At its meeting in February 2010, the Board asked the Committee to provide a recommendation on how to present the guidance on contingent consideration within one standard.

## Objective of the paper

2. The objective of this paper is:

   (a) to provide an analysis on the issue,

   (b) to highlight inconsistencies and potential conflicts between IFRS 3 requirements on accounting for contingent consideration and other applicable IFRSs, and

   (c) to recommend these inconsistencies be removed by deleting references to other IFRSs from the guidance on accounting for contingent consideration within IFRS 3.

3. For ease of reference, Appendix B to this paper lists current requirements under IFRS 3 with respect to contingent consideration.

This paper has been prepared by the technical staff of the IASCF for discussion at a public meeting of the IFRS Interpretations Committee.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IFRS Interpretations Committee or the IASB. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination.

Decisions made by the IFRS Interpretations Committee are reported in IFRIC *Update*.

Interpretations are published only after the IFRS Interpretations Committee and the Board have each completed their full due process, including appropriate public consultation and formal voting procedures. The approval of an Interpretation by the Board is reported in IASB *Update*.

## Background

4. During the comment letters analysis phase for the *Improvements to IFRSs* issued in May 2010, the Committee and the Board noted that guidance on contingent consideration is included in more than one IFRS. They noted that this may give rise to divergent application practices and entail inconsistencies within IFRSs.

## Staff analysis

### *Existing guidance*

5. In the following paragraphs, the staff draws an exhaustive list of accounting requirements regarding contingent consideration on:
   (a) definition,
   (b) recognition, classification and initial measurement,
   (c) subsequent measurement, and
   (d) disclosures.
6. The aim is to give the Committee sufficient background on existing guidance to conclude on the need to make relevant changes to enhance clarity and consistent application.
7. The staff is aware that IFRS 3 was a joint project with the FASB. In this context, modifying the wording in IFRS 3 might entail departure from the wording in the corresponding guidance under US GAAP. However, the aim of the proposed changes is not to change fundamental accounting requirements but to regroup and clarify them.

#### *Definition*

8. Contingent consideration is defined in Appendix A to IFRS 3.
9. The staff notes that 'contingent consideration' is used only in the context of business combinations and mentioned only in IFRS 3.

10. The staff acknowledges contingent consideration can be of differing nature and consequently fall within the scope of different IFRSs. However, because contingent consideration only arises in business combinations, the staff believes IFRS 3 is the appropriate place for regrouping related guidance.

*Recognition, classification and initial measurement*

11. Recognition and initial measurement is addressed in paragraph 39 of IFRS 3: all contingent consideration should be recognised at fair value at acquisition date.

12. Classification is addressed in paragraph 40 of IFRS 3 and refers to different standards depending on the nature of the contingent consideration. The table below lists the references as stated in paragraph 40:

| **Contingent consideration** | **Applicable standard** | **Resulting classification** |
|---|---|---|
| **Liability**: obligation to pay | Paragraph 11 of IAS 32 | Financial liability, or Equity |
| | Other applicable IFRSs | Accordingly |
| **Asset**: right to the return of previously transferred consideration | No reference | |

13. The staff notes multiple references for recognition, classification and initial measurement.

14. One constituent raised the following issue that the staff believes is an illustration of the consequences of referring to relevant IFRSs depending on the nature of the contingent consideration for classification purposes. Entity X acquires entity Y and the consideration for the business combination includes contingent consideration that is a financial liability (X's liability) within the scope of IAS 39. Applying paragraph 40 of IFRS 3 raises the question of how to classify the liability in accordance with IAS 39.

15. The constituent highlights that a contingent consideration that is a financial liability may meet neither condition in paragraph 9 of IAS 39 to be categorised as held for trading. In addition, the constituent is of the opinion that contingent

consideration that is a financial liability is, in practice, likely not to be designated as at fair value through profit or loss upon recognition.

16. Paragraph 40 of IFRS 3 brings about consistency issues on classification when contingent consideration is a financial instrument that falls within the scope of IAS 39. The staff presents below two ways of dealing with this inconsistency and highlights consequences for each:

    (a) Approach A: require that contingent consideration is classified following the guidance in IAS 39 / IFRS 9. Following this approach would result in some contingent consideration balances being classified as at amortised cost, but this would conflict with the requirement in paragraph 58 of IFRS 3 for such balances to be subsequently measured at fair value.

    (b) Approach B: do not require contingent consideration balances to be classified in accordance with IAS 39 / IFRS 9. Instead, require contingent consideration balances to be subsequently measured at fair value.

17. The staff believes that no classification requirement for contingent consideration that is a financial instrument would simplify initial recognition and subsequent accounting. Therefore the staff recommends paragraph 40 of IFRS 3 be amended to reflect this view.

*Subsequent measurement - overview*

18. The staff notes that subsequent measurement requirements are also included in more than one IFRS.

19. For a clear overview, the table below summarises the existing requirements and references:

<table>
<tr><th>Nature of adjustments</th><th>When do they occur?</th><th>Applicable IFRSs</th><th>Measurement and presentation requirements</th></tr>
<tr><td rowspan="2">Measurement period adjustments[1]</td><td>During the measurement period</td><td>IFRS 3.45-49</td><td>Fair value re-measurement.<br>Adjustments booked against goodwill.<br>Restatement of comparative information.</td></tr>
<tr><td>After the measurement period</td><td>IFRS 3.50<br>IAS 8.41-49</td><td>Accounting for errors.<br>Fair value re-measurement.<br>Adjustments booked to profit or loss for the relevant period.<br>Restatement of comparative information.</td></tr>
<tr><td rowspan="3">Non measurement period adjustments</td><td rowspan="3">Any time from the date of acquisition</td><td>Contingent consideration classified as equity<br>IFRS 3.58(a)</td><td>No re-measurement.<br>Subsequent settlement accounted for within equity.</td></tr>
<tr><td>Contingent consideration classified as a financial instrument<br>IFRS 3.58(b)(i)<br>IAS 39/IFRS 9</td><td>Fair value re-measurement.<br>Resulting gain or loss in<br>✓ P&L, or<br>✓ OCI.<br>Appropriate disclosures from IFRS 7.</td></tr>
<tr><td>Other contingent consideration<br>IFRS 3.58(b)(ii)<br>IAS 37<br>Other IFRSs</td><td>Measurement:<br>✓ best estimate, or<br>✓ in accordance with appropriate IFRSs.<br>Appropriate disclosures from IAS 37 or other IFRSs.</td></tr>
</table>

[1] Some changes in the fair value of contingent consideration that the acquirer recognises after the acquisition date may be the result of additional information that the acquirer obtained after that date about facts and circumstances that existed at the acquisition date. Such changes are measurement period adjustments in accordance with paragraphs 45–49 of IFRS 3.

***Subsequent measurement - contingent consideration that is a financial instrument – paragraph 58(b)(i)***

20. Paragraph 58(b)(i) requires that contingent consideration that is a financial instrument within the scope of IAS 39/IFRS 9 be accounted for at fair value, with resulting gains or losses recognised either in profit or loss or in other comprehensive income (OCI).

21. The staff believes that this requirement is a departure from the requirements in IAS 39/IFRS 9 that provide for some instruments (eg loans, receivables, financial liabilities) to be accounted for at amortised cost. As a consequence, the measurement requirements in IFRS 3 are not fully consistent with those in IAS 39/IFRS 9.

22. The staff notes that in most cases contingent consideration is a derivative to which fair value measurement applies in accordance with IAS 39/IFRS 9. However, paragraph 58 of IFRS 3 refers to other applicable IFRSs, hence acknowledging that contingent consideration could be a non-financial asset or a non-financial liability.

23. The staff lists two paths forward to remove the inconsistency highlighted in paragraph 19 above:

    (a) View A: contingent consideration that is a financial instrument within the scope of IAS 39/IFRS 9, and that would not be measured at fair value under these standards, should be measured at fair value in accordance with the provisions in paragraph 58 of IFRS 3. References to IAS 39/IFRS 9 would then need to be removed. In addition, accounting for the resulting gain or loss would need to be assessed. The staff is aware that assessing that it should be recognised through profit or loss is a change from what is currently required in paragraph 58(b)(i) of IFRS 3. However, it would improve comparability by requiring one accounting treatment only.

    (b) View B: contingent consideration that is a financial instrument within the scope of IAS 39/IFRS 9, and that would not be measured at fair value under these standards, should follow the measurement provisions

set out in IAS 39/IFRS 9. The guidance in IFRS 3 would then need to be amended to permit this accounting.

24. The staff acknowledges that view A is consistent with the principle in IFRS 3 for measuring consideration transferred at fair value. The staff also believes this was the intent of the Board when issuing IFRS 3 for measuring contingent consideration regardless of its nature.

25. The staff acknowledges this creates differences in the measurement requirements of financial instruments depending on whether or not they are contingent consideration arising from a business combination. Introducing a new measurement basis based on the circumstances in which an item arises (a business combination) can be seen as rule-based and departing from a principle-based measurement approach.

26. In addition, one may question practicability when requiring fair value measurement for an item that is part of a category of items that in principle is not measured at fair value.

27. However, the staff thinks that choosing view B and changing the basis of accounting for this type of contingent consideration would go beyond an *Annual Improvement*.

28. In the light of the above findings, the staff believes that view A is consistent with IFRS 3 and would address the perceived conflict between guidance in the different standards. The staff thinks that for the sake of clarification the rationale for favouring consistency with IFRS 3 over the consistency with IAS 39 should be explained within the standard or in the Basis for Conclusions.

***Subsequent measurement - contingent consideration that is not a financial instrument – paragraph 58(b)(ii)***

29. The staff notes that the guidance specifically points to IAS 37 *Provisions, Contingent Liabilities and Contingent Assets* for contingent consideration classified as an asset or a liability that is not within the scope of IFRS 9 or IAS 39.

30. The staff can envisage situations when a contingent consideration is a non-financial liability, for example contingent consideration relating to a lawsuit in progress at the date the contingent consideration is measured. However, since IAS 37 measurement basis is the 'best estimate' and not 'fair value', the staff thinks reference to IAS 37 provides inconsistent guidance. The staff also notes that paragraphs 27 to 30 of IAS 37 address contingent liabilities and require they not be recognised. The staff believes referring to IAS 37 for a contingent consideration that is a non-financial liability - that IFRS 3 requires to recognise - may entail confusion with respect to the use of the word 'contingent'.

31. In addition, the staff notes that the first part of paragraph 58 of IFRS 3 refers to changes in fair value for contingent consideration irrespective of its nature. The staff believes it is inconsistent in the same paragraph to:

    (a) mention changes in fair value of an item, and

    (b) require this item be measured in accordance with standards that do not require fair value as a measurement basis.

32. The staff is of the opinion that similarly to the analysis for contingent consideration that is a financial instrument, two paths forward exist:

    (a) specifically require fair value measurement for items that are contingent consideration, delete reference to applicable IFRSs and acknowledge in the Basis for Conclusions that fair value measurement requirement departs from the 'normal' accounting that would apply if these items were not contingent consideration, or

(b) change the accounting for contingent consideration to retain relevant individual measurement principles in other IFRSs. The staff thinks that view B goes beyond *Annual Improvements* because it would represent a change in accounting principles.

33. The staff recommends a path that ensures consistency with the requirements in IFRS 3 and in particular the solution in paragraph 32(a) above.

***Disclosures***

34. The staff notes that paragraph B64 of IFRS 3 provides guidance with respect to required disclosures (see Appendix B to this paper).

35. The staff also notes that paragraph 58 of IFRS 3 provides guidance for the accounting for contingent consideration by reference to applicable IFRSs. Some believe that when contingent consideration is in the scope of a relevant IFRS it should be subject to all the disclosure requirements of that IFRS in addition to the requirements in paragraph B64 of IFRS 3.

36. The constituent who raised the issue presented in paragraph 14 above is also concerned with the application of paragraph 8(e)[2] of IFRS 7 *Financial Instruments: Disclosures* to contingent consideration that is a financial liability. Because such contingent consideration is not classified in practice in accordance with IAS 39, the constituent is of the opinion that it would be difficult to apply paragraph 8(e) of IFRS 7.

37. The staff is of the opinion that the information provided in accordance with paragraph B64 is useful and sufficient information. This is also illustrated by Illustrative Example IE72 where disclosures on contingent consideration do not show disclosure requirements from other applicable IFRSs.

38. Therefore the staff believes that for contingent consideration that is a financial instrument IFRS 7 disclosures do not need to be given.

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[2] This paragraph requires disclosure of financial liabilities at fair value through profit or loss showing separately (i) those designated as such upon initial recognition and (ii) those that meet the definition of held for trading.

## Conclusion and staff recommendation

### *Recommendation*

39. The review of existing guidance shows:

    (a) the extent to which guidance to account for contingent consideration is included in more than one IFRS, and

    (b) inconsistencies in classification, measurement and disclosure requirements, that could be removed either by:

        (i) deleting references to other IFRSs within IFRS 3, or

        (ii) changing the accounting requirements.

40. The staff believes that removing inconsistencies in accounting for contingent consideration within the guidance provided in IFRS 3 would meet the set objective of regrouping guidance as well as enhancing the quality of the standards.

### *Inclusion in Annual Improvements*

41. The staff is of the opinion that deleting references to other IFRSs in paragraphs 40 and 58 of IFRS 3 leads to the appropriate accounting for contingent consideration and also removes disclosure inconsistencies. In addition it is straight forward and feasible in a reasonable timeframe as part of the *Annual Improvements* project.

42. Therefore the staff suggests the Committee recommends the Board amends paragraphs 40 and 58 of IFRS 3 through the *Annual Improvements* project to remove references to other IFRSs. In addition, paragraph 58(b) of IFRS 3 would be amended to assert that resulting gains and losses from changes in fair value should be recognised in profit or loss.

### *Transition provisions*

43. The staff believes that the effects of the proposed changes should be accounted for prospectively from the date the improvement is effective in order to avoid unduly burdensome changes.

### *Consequential amendments*

44. The staff believes that a consequential amendment of the proposed modification would be the exclusion of contingent consideration from the scopes of IAS 39/IFRS 9 and of IFRS 7. However, distinction between financial liability and equity would need to remain in paragraph 40 of IFRS 3. The staff notes that the proposed amendment will not change the different accounting in paragraph 58 of IFRS 3 for contingent consideration that is equity in accordance with paragraph 11 of IAS 32 - the equity contingent consideration is not to be remeasured.

### *Proposed drafting*

45. Appendix A to this paper sets out draft wording to reflect the proposed changes. Consequential amendments will be drafted at a later date.

## Questions to the Committee

| Question 1 – Need for improvement |
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| Does the Committee agree that removing existing inconsistencies would improve clarity in accounting for contingent consideration? |

| Question 2 – Removing inconsistencies in measurement and disclosure requirements |
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| Does the Committee agree with the staff's recommendation to delete the references to other IFRSs in paragraph 58 of IFRS 3 for the reasons set out in paragraphs 18 to 38? |

| Question 3 – Draft wording proposed in Appendix A |
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| Does the Committee agree with the wording proposed in Appendix A? |

# Appendix A – Drafting for proposed amendment

This appendix includes proposed drafting of the proposed amendment. It is based on the text included in the Bound Volume as of 1 January 2010. New text is underlined and deleted text is struck through.

## Proposed amendments to IFRS 3 *Business Combinations* (as revised in 2008)

Paragraphs 40 and 58 are amended. Paragraph 64D is added. Paragraph B64 is reproduced for ease of reference and paragraph B64A is added.

### The acquisition method

#### Consideration transferred

*Contingent consideration*

40 The acquirer shall classify an obligation to pay contingent consideration as a liability or as equity on the basis of the definitions of an equity instrument and a financial liability in paragraph 11 of IAS 32 *Financial Instruments: Presentation*~~, or other applicable IFRSs~~. <u>Contingent consideration that is a financial instrument in accordance with the definitions in IAS 32 is not in the scope of IAS 39 or IFRS 9 and shall follow the requirements in this standard.</u> The acquirer shall classify as an asset a right to the return of previously transferred consideration if specified conditions are met. Paragraph 58 provides guidance on the subsequent accounting for contingent consideration.

### Subsequent measurement and accounting

#### Contingent consideration

58 Some changes in the fair value of contingent consideration that the acquirer recognises after the acquisition date may be the result of additional information that the acquirer obtained after that date about facts and circumstances that existed at the acquisition date. Such changes are measurement period adjustments in accordance with paragraphs 45–49. However, changes resulting from events after the acquisition date, such as meeting an earnings target, reaching a specified share price or reaching a milestone on a research and development project, are not measurement period adjustments. The acquirer shall account for changes in the fair value of contingent consideration that are not measurement period adjustments as follows:

(a) Contingent consideration classified as equity shall not be remeasured and its subsequent settlement shall be accounted for within equity.

(b) Contingent consideration classified as an asset or a liability ~~that:~~

~~(i) is a financial instrument and is within the scope of IAS 39~~ shall be measured at fair value<u> at each reporting date</u>, with any resulting gain or loss recognised ~~either~~ in profit or loss<u> for the period</u>~~ or in other comprehensive income in accordance with that IFRS~~.

~~(ii) is not within the scope of IFRS 9 or IAS 39 shall be accounted for in accordance with IAS 37 or other IFRSs as appropriate.~~

## Effective date and transition

### Effective date

64D *Improvements to IFRSs* issued in [date] amended paragraphs 40 and 58 and added paragraph B64A. An entity shall apply those amendments for annual periods beginning on or after 1 January 2012. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact. Application should be prospective from the date the amendments are effective.

# Appendix B

# Application guidance

## Disclosures (application of paragraphs 59 and 61)

B64 To meet the objective in paragraph 59, the acquirer shall disclose the following information for each business combination that occurs during the reporting period:

(a) …

(g) for contingent consideration arrangements and indemnification assets:

(i) the amount recognised as of the acquisition date;

(ii) a description of the arrangement and the basis for determining the amount of the payment; and

(iii) an estimate of the range of outcomes (undiscounted) or, if a range cannot be estimated, that fact and the reasons why a range cannot be estimated. If the maximum amount of the payment is unlimited, the acquirer shall disclose that fact.

B64A For contingent consideration, an entity shall not apply the disclosure requirements set out in IFRS 7 *Financial Instruments: Disclosures*.

# Basis for Conclusions on proposed amendments to IFRS 3 *Business Combinations* (as revised in 2008)

*This Basis for Conclusions accompanies, but is not part of, the proposed amendment.*

## Accounting for contingent consideration

BC1 The Board proposes to clarify the accounting for contingent consideration arising from business combinations. The Board noted that requirements on classification in paragraph 40 of IFRS 3 are inconsistent with requirements on subsequent measurement in paragraph 58 of IFRS 3 for contingent consideration that is a financial instrument within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* when compared with the accounting requirements of IAS 39. Because paragraph 40 of IFRS 3 refers to 'other applicable IFRSs' a contingent consideration that is a financial liability might be classified as at amortised cost. This would conflict with the requirement in paragraph 58 of IFRS 3 that such contingent consideration be subsequently measured at fair value. Therefore, the Board proposes to delete the reference to 'other applicable IFRSs' in paragraph 40 of IFRS 3. The reference to paragraph 11 of IAS 32 *Financial Instruments: Presentation* would remain because such distinction is relevant for the subsequent measurement requirements in paragraph 58(a) of IFRS 3, ie no re-measurement for contingent consideration classified as equity. The proposed amendment entails a consequential amendment to IAS 39 to exclude contingent consideration from its scope.

BC2 As a consequence of not requiring classification of contingent consideration that is a financial instrument in accordance with IAS 39, the Board proposes to delete the option in paragraph 58(b) of IFRS 3 to recognise resulting gain or loss from changes in fair value through other comprehensive income. All changes in fair value of the financial instrument would therefore be recognised in profit or loss.

BC3 The Board also noted that the subsequent measurement requirements for contingent consideration that is not a financial instrument in paragraph 58(b) of IFRS 3 conflict with measurement in other applicable IFRSs. The conflict lies in that paragraph 58(b) of IFRS 3 refers to changes in fair value of contingent consideration and requires contingent consideration be measured in accordance with standards that do not require fair value as a measurement basis. Therefore the Board proposes to delete the reference to 'IAS 37 or other IFRSs as appropriate' from paragraph 58(b) of IFRS 3. The proposal therefore maintains fair value as the subsequent measurement basis for contingent consideration. The Board acknowledges this is a change from the accounting that would apply if these items were not contingent consideration.

BC4 In addition, the Board proposes to clarify that the information provided in accordance with paragraph B64 of IFRS 3 is useful and sufficient information. Disclosures in IFRS 7 *Financial Instruments: Disclosures* should not need to be given for contingent consideration that is a financial instrument. The proposed amendment entails a consequential amendment to IFRS 7 to exclude contingent consideration from its scope.

# Appendix B – Existing guidance and relevant IFRS literature

The current guidance on accounting for contingent consideration is reproduced below for ease of reference.

## Definition – IFRS 3 Appendix A

Usually, an obligation of the acquirer to transfer additional assets or equity interests to the former owners of an acquiree as part of the exchange for control of the acquiree if specified future events occur or conditions are met. However, contingent consideration also may give the acquirer the right to the return of previously transferred consideration if specified conditions are met.

## Nature of contingent consideration – IFRS 3 paragraph IN12

IN12 In general, an acquirer measures and accounts for assets acquired and liabilities assumed or incurred in a business combination after the business combination has been completed in accordance with other applicable IFRSs. However, the IFRS provides accounting requirements for reacquired rights, contingent liabilities, contingent consideration and indemnification assets.

## Recognition – IFRS 3 paragraphs 39 and 40

39 The consideration the acquirer transfers in exchange for the acquiree includes any asset or liability resulting from a contingent consideration arrangement (see paragraph 37). The acquirer shall **recognise** the acquisition-date fair value of contingent consideration as part of the consideration transferred in exchange for the acquiree.

40 The acquirer shall classify an obligation to pay contingent consideration as a liability or as equity on the basis of the definitions of an equity instrument and a financial liability in paragraph 11 of IAS 32 *Financial Instruments: Presentation*, or other applicable IFRSs. The acquirer shall classify as an asset a right to the return of previously transferred consideration if specified conditions are met. Paragraph 58 provides guidance on the subsequent accounting for contingent consideration.

## Measurement – IFRS 3 paragraphs 50, 54 and 58

50 After the measurement period ends, the acquirer shall revise the accounting for a business combination only to correct an error in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

54 In general, an acquirer shall subsequently measure and account for assets acquired, liabilities assumed or incurred and equity instruments issued in a business combination in accordance with other applicable IFRSs for those items, depending on their nature. However, this IFRS provides guidance on subsequently measuring and accounting for the following assets acquired, liabilities assumed or incurred and equity instruments issued in a business, combination:

(a) reacquired rights;

(b) contingent liabilities recognised as of the acquisition date;

(c) indemnification assets; and

(d) contingent consideration.

Paragraph B63 provides related application guidance.

58 Some changes in the fair value of contingent consideration that the acquirer recognises after the acquisition date may be the result of additional information that the acquirer obtained after that date about facts and circumstances that existed at the acquisition date. Such changes are measurement period adjustments in accordance with paragraphs 45–49. However, changes resulting from events after the acquisition date, such as meeting an earnings target, reaching a specified share price or reaching a milestone on a research and development project, are not measurement period adjustments. The acquirer shall account for changes in the fair value of contingent consideration that are not measurement period adjustments as follows:

(a) Contingent consideration classified as equity shall not be remeasured and its subsequent settlement shall be accounted for within equity.

(b) Contingent consideration classified as an asset or a liability that:

(i) is a financial instrument and is within the scope of IFRS 9 or IAS 39 shall be measured at fair value, with any resulting gain or loss recognised either in profit or loss or in other comprehensive income in accordance with IFRS 9 or IAS 39 as applicable.

(ii) is not within the scope of IFRS 9 or IAS 39 shall be accounted for in accordance with IAS 37 or other IFRSs as appropriate.

## Disclosures - IFRS 3 Appendix B

B64 To meet the objective in paragraph 59, the acquirer shall disclose the following information for each business combination that occurs during the reporting period:

(a) …

(g) for contingent consideration arrangements and indemnification assets:

(i) the amount recognised as of the acquisition date;

(ii) a description of the arrangement and the basis for determining the amount of the payment; and

(iii) an estimate of the range of outcomes (undiscounted) or, if a range cannot be estimated, that fact and the reasons why a range cannot be estimated. If the maximum amount of the payment is unlimited, the acquirer shall disclose that fact.

## Basis for Conclusions

BC354 The boards observed that many obligations for contingent consideration that qualify for classification as liabilities meet the definition of derivative instruments in IAS 39 or SFAS 133. To improve transparency in reporting particular instruments, the boards concluded that all contracts that would otherwise be within the scope of those standards (if not issued in a business combination) should be subject to their requirements if issued in a business combination. Therefore, the boards decided to eliminate their respective provisions (paragraph 2(f) of IAS 39 and paragraph 11(c) of SFAS 133) that excluded contingent consideration in a business combination from the scope of those standards. Accordingly, liabilities for payments of contingent consideration that are subject to the requirements of IAS 39 or SFAS 133 would subsequently be measured at fair value at the end of each reporting period, with changes in fair value recognised in accordance with whichever of those standards an entity applies in its financial statements.

BC355 In considering the subsequent accounting for contingent payments that are liabilities but are not derivatives, the boards concluded that, in concept, all liabilities for contingent payments should be accounted for similarly. Therefore, liabilities for contingent payments that are not derivative instruments should also be remeasured at fair value after the acquisition date. The boards concluded that applying those provisions would faithfully represent the fair value of the liability for the contingent payment of consideration that remains a liability until settled.

BC356 The boards also considered whether subsequent changes in the fair values of liabilities for contingent consideration should be reflected as adjustments to the consideration transferred in the business combination (usually in goodwill). Some respondents to the 2005 Exposure Draft favoured that alternative because they thought that changes in the fair value of contingent consideration effectively resolve differing views of the acquirer and the former owners of the acquiree about the acquisition-date fair value of the acquiree. The boards acknowledged that a conclusive determination at the acquisition date of the fair value of a liability for contingent consideration might not be practicable in the limited circumstances in which particular information is not available at that date. As discussed in more detail in paragraphs BC390–BC400, the boards decided that the revised standards should provide for provisional measurement of the fair value of assets acquired or liabilities assumed or incurred, including liabilities for contingent payments, in those circumstances.