Financial Instruments Consultative Group meeting

Date	**July 2026**
Project	**Amortised Cost Measurement**
Topic	**Measurement of financial liabilities arising from contingent settlement provisions**
Contacts	**Karen Robson** (karen.robson@ifrs.org) **Iliriana Feka** (ifeka@ifrs.org) **Riana Wiesner** (rwiesner@ifrs.org)

Introduction

- The Amortised Cost Measurement project aims to make targeted improvements to IFRS 9 *Financial Instruments* to address application issues that are widespread and have a material effect on companies' financial statements.
- In April 2026, the IASB added a further topic to this project. Specifically, the IASB decided that stakeholder feedback on measuring financial liabilities arising from contingent settlement provisions might be better addressed in the Amortised Cost Measurement project rather than in the Financial Instruments with Characteristics of Equity (FICE) project.
- At this meeting, the IASB is seeking FICG feedback on a potential way forward for responding to stakeholder concerns about measuring financial liabilities arising from contingent settlement provisions.

Contents

Questions for FICG members

Questions for FICG members

1. In your view, would Approach 1 or Approach 2 better address the challenges identified in applying the proposed amendment in the FICE Exposure Draft (see pages 7–19)?

2. In particular, regarding Approach 2 (see pages 16–19):
    a. for users of financial statements, would the significant subjectivity involved in estimating the probability and expected timing of a contingent event, such as a non-viability event, reduce the usefulness of information resulting from this measurement approach?
    b. for preparers of financial statements, would you expect to be able to reliably estimate the probability and expected timing of a contingent event, such as a non-viability event? Would making that estimate involve significant cost and effort?

3. Have you identified any alternatives that might address those challenges? If so, how would that alternative address stakeholder concerns about faithful reflection of the obligation arising from a contingent settlement provision and provide useful information to users of financial statements?

Previous IASB proposals and stakeholder feedback

Proposals in the FICE Exposure Draft

Paragraph 25 of IAS 32 *Financial Instruments: Presentation* requires a financial instrument that is settled in cash upon the occurrence of an uncertain future event, that is beyond the control of both the issuer and the holder of the instrument, to be classified as a financial liability.

Example	Proposed amendment (related to measurement) in the FICE Exposure Draft
Contingent convertible instrument: • issued at par • convertible into variable number of shares to the value of fixed par amount if CET 1 ratio breached • no maturity date • discretionary dividends	• Financial instruments with contingent settlement provisions could be compound instruments • The financial liability portion is measured at the **present value of the settlement amount**, on initial recognition and subsequently • Settlement amount is discounted, assuming settlement will occur at the **earliest possible settlement date** specified in the contract • Any gains or losses on remeasurement are recognised in profit or loss • The **probability and estimated timing** of occurrence or non-occurrence of the contingent event **have no effect** on the initial or subsequent measurement

Overall stakeholder feedback

Overall, stakeholders had opposing views to the measurement proposals: some agreed with the proposals, while others strongly disagreed

- Those who agreed, viewed the proposal as an appropriate and pragmatic solution that:
    - provides a faithful reflection of liquidity risk;
    - is simpler to apply because it avoids the complexities and costs associated with the periodic remeasurement of financial liabilities in accordance with IFRS 9;
    - balances the interests of investors and preparers; and
    - aligns with the requirements in IAS 32 for measuring obligations to purchase own equity instruments at the present value of the redemption amount (paragraph 23 of IAS 32)
- However, stakeholders asked for some clarification of the proposals (see page 10)

Agenda Paper 5B for the April 2026 IASB meeting includes further details

Overall stakeholder feedback (cont.)

- Those who disagreed said that the proposed solution would not provide useful information because it did not consider market participants' perspective on the occurrence of the contingent event.
- In their view, the settlement amount does not reflect the economic substance of the instrument because it does not consider the probability and timing of the contingent event occurring. Therefore, they believe that:
  - liabilities might be overstated when the contingent event is remote; and
  - liabilities might be understated when later or larger settlements are more probable.
- These stakeholders said that the proposals introduce a new measurement basis for particular financial liabilities and would reduce comparability rather than improve it.
- They recommended that financial liabilities are measured applying the principles in IFRS 9, which in their view would take into account expected cash flows (ie probability and timing of the contingent event occurring).

Agenda Paper 5B for the April 2026 IASB meeting includes further details

Request for further clarification

Questions stakeholders raised about the application of the proposed measurement requirements included:

- **Day one gains or losses**—how to account for differences between the settlement amount and transaction price on initial recognition
- **Discount rate**—how to determine the discount rate for calculating the present value of the settlement amount on initial measurement, whether to adjust the discount rate subsequently and how to account for any differences arising from the adjustments
- **Settlement amount**—how to determine the settlement amount on initial recognition, and subsequently, if there are multiple contingent settlement provisions, multiple settlement dates or if the settlement amount is based on future performance targets or performance metrics of the entity
- **Embedded derivatives**—how the proposed measurement approach relates to the requirements in IFRS 9 for separating embedded derivatives from the host financial liability. Stakeholders noted that in practice, the requirements are applied differently, resulting in either recognition of a financial liability for the full amount without accounting for an embedded derivative or recognition of both a financial liability and an embedded derivative.

Agenda Paper 5B for the April 2026 IASB meeting includes further details

A potential way forward

A potential way forward

- Based on the feedback, the staff think the views described on pages 8–10 might be the only two viable options for the IASB to consider. However, because these views differ fundamentally, staff do not think a compromise between them is possible.
- The terms and conditions of contracts with contingent settlement provisions vary significantly, including across different jurisdictions.
- Consequently, identifying an approach that might achieve broad stakeholder support across jurisdictions may not be feasible.
- However, the IASB is aware of diversity in practice. Stakeholders have repeatedly requested guidance and noted that this diversity reduces the usefulness of information provided to investors. Accordingly, the IASB aims to explore potential solutions rather than maintain the status quo.
- The staff think it would be beneficial to explore whether measuring financial liabilities in accordance with IFRS 9 requirements could address some of the concerns that stakeholders identified in relation to the approach proposed in the FICE Exposure Draft

Approach 1: Recognise liability at transaction price

Initial measurement

- Paragraph 31 of IAS 32 requires the equity component of compound instrument to be assigned the residual amount after deducting from fair value of the instrument as a whole, the amount separately determined for the liability component.
- IFRS 9 requires financial instruments to be initially measured at fair value. Paragraph B5.1.1 of IFRS 9 states that **fair value is normally the transaction price** (see Appendix for further details).
- The approach in IAS 32 and in the FICE Exposure Draft was based on measuring a financial liability at the amount an entity cannot avoid paying upon occurrence of the contingent event. This approach is consistent with the definition of a financial liability. For contingent settlement provisions, the occurrence of the event is outside the control of both the holder and issuer; therefore, the issuer cannot avoid paying at least the transaction price.
- As the contingent event is outside control of the issuer, it is assumed that contingent event can occur at any time, therefore the financial liability is not discounted for the time value of money.

Subsequent measurement

- If measured at amortised cost, the carrying amount is increased via a catch-up adjustment when an entity is expected to settle the liability at an amount higher than the transaction price (paragraph B5.4.6 of IFRS 9)

Approach 1: Recognise liability at transaction price (cont.)

Other considerations

- Financial liabilities arising from contingent settlement provisions are different from other financial liabilities. For most financial liabilities there is an unconditional contractual obligation to pay an amount of cash. However, in the case of contingent settlement provisions, the obligation is conditional on the occurrence of a future event. Therefore, specific requirements for such liabilities would need to be included in IFRS 9.
- This approach would avoid any day 1 gains or losses arising and would meet the IASB's objective to have consistent measurement between initial and subsequent measurement (ie no day 2 gains would be recognised).
- In many cases the contingent event is the non-viability of the issuer (or its peers). This approach would avoid counter-intuitive effects from increasing the liability when non-viability becomes more likely.

Approach 1 would be largely consistent with the proposals in the FICE Exposure Draft, but simplified and responsive to the requests for clarification summarised on page 10.

Advantages and disadvantages of Approach 1

Key advantages	Key disadvantages
• **Initial measurement applying existing concepts**. The financial liability arising from contingent settlement would be initially measured at transaction price, already discussed in IFRS 9 (eg see paragraph B5.1.1). • **Objectively determined financial liability amount.** Initial recognition of the financial liability at transaction price would be a factual and more objective measure, being the contractual amount agreed by the parties at issuance. • **Reflective of how these instruments are priced and invested**. Previous feedback from the FICE project indicated that investors view these instruments as more akin to debt than equity—that is, they behave like debt instruments in favourable conditions. That is also why some entities hedge interest rate and FX risks of these liabilities. • **Balanced cost-benefit outcome.** The investor benefits of reflecting expected probability and timing would not outweigh preparer costs, particularly because estimates for events such as non-viability may be unreliable. • **Improves comparability.** Measuring the liability without significant subjective judgements or arbitrary assumptions about timing or occurrence of contingent event occurring would improve comparability.	• **Disregarding the probability of the contingent event may not reflect economic substance**. Some argue that a market participant would consider the probability of the contingent event occurring and allocate some, or most, of the instrument's initial fair value to the equity component. • **Regulatory consequences**. Measuring the financial liability at transaction price could result in the reclassification of amounts from equity to liabilities on transition in some jurisdictions. This may have a consequential effect on the regulatory capital metrics, including the Common Equity Tier 1 (CET1) ratio in those jurisdictions.

Approach 2: Recognise liability based on expected value

Initial measurement

- When determining the fair value of the liability component applying paragraph B5.1.1 of IFRS 9, the issuer considers the probability and expected timing of the contingent event occurring.
- IFRS 13 *Fair Value Measurement* states that fair value measurement assumes that a financial liability remains outstanding and is transferred to a market participant and that the market participant would be required to fulfil the obligation.
- Supporters of this approach argue that, when applying a present value approach to measure the liability's fair value, the issuer would estimate future cash flows and consider possible variations in their amount and timing.

Subsequent measurement

- If measured at amortised cost, the carrying amount is adjusted for changes in the issuer's expectations about the amount and timing of the cash flows required to settle the liability (paragraph B5.4.6 of IFRS 9).

Approach 2: Recognise liability based on expected value (cont.)

Other considerations

- Under this approach, the fair value of the liability component might be very low if an entity does not expect the contingent event to occur, resulting in the remaining amount being allocated to the equity component. As a result, the carrying amount of the liability will increase as the probability of the contingent event occurring increases. In practice, the effect might be that no liability is recognised until the entity is deemed to be non-viable.
- However, some stakeholders said that, doing so would involve significant subjective judgements, for example requiring an entity to estimate the occurrence of events such as own non-viability. That subjectivity may not improve financial reporting, as it might:
    - increase operational costs to develop a reliable estimate and frequently remeasure the liability; and
    - reduce the usefulness of information due to subjective judgements which reduce comparability.
- This approach is similar to the proposal in the 2018 FICE Discussion Paper on the ‘amount feature’, which would measure the liability based on the probability of the entity entering liquidation. Stakeholders strongly disagreed with that proposal because assessing whether, or when, an entity would enter liquidation is highly subjective and could produce counter-intuitive outcomes—that is, as an entity’s financial position worsens, the liability’s carrying amount would increase.

Approach 2: Recognise liability based on expected value (cont.)

Other considerations (continued)

- Furthermore, as discussed at the IASB's June 2025 meeting, preparers have reported that, for financial instruments with contingent terms affecting the contractual interest rate, estimating the probability and timing of a contingent event on initial recognition is often not feasible. Any resulting estimate would be unreliable because it would require significant judgement and would not be based on reasonable and supportable information available.
- The IASB was previously asked to provide application guidance on how to reflect the probability of contingent events in the expected cash flows for the purpose of determining the effective interest rate on initial recognition of a financial instrument with contingent terms.
- In September 2025, the IASB concluded that prescribing a method may be arbitrary and may not appropriately reflect the substance of different types of contingent contractual cash flows. At the time, the IASB tentatively decided to take no further action on this matter.

IFRS Accounting

Advantages and disadvantages of Approach 2

Key advantages	Key disadvantages
• **Reflects the expected obligation**. Taking into account the expected probability and timing would help avoid overstating liabilities when the contingent event is remote and understating them when larger or later settlement amounts are more likely. • **Consistent with a market participant perspective**. This approach better aligns with fair value—that is, the price paid to transfer a liability in an orderly transaction between market participants at the measurement date. • **Usefulness of information.** Might be reflective of economic substance; therefore, resulting in decision useful information. However, the significant subjectivity involved may also undermine the usefulness of information.	• **Relies on subjective estimates and probability-weighted outcomes.** This would increase costs for preparers and reduce comparability of information for users of financial statements. • **May produce counter-intuitive outcomes.** The measurement effect would be similar to own credit risk in fair value measurement: the higher the probability of the contingent event, such as non-viability, the higher the liability amount and related losses recognised in profit or loss. • **Lack of transparency**. Because the liability is likely to have an immaterial carrying amount in favourable conditions, users may have limited visibility of the potential for a significant liability to be recognised in 'bad' times.

Appendix—A reminder of measurement requirements in IFRS 9

Reminder of IFRS 9 approach—initial measurement

- There is one approach in IFRS 9 for measuring financial liabilities on initial recognition—at **fair value** adjusted for some transaction costs (see paragraph 5.1.1 of IFRS 9)
- Paragraph B5.1.1 of IFRS 9 states that the fair value of a financial instrument at initial recognition is normally the **transaction price** (ie the fair value of the consideration given or received, see also paragraph B5.1.2A and IFRS 13). However, if part of the consideration given or received is for something other than the financial instrument, an entity shall measure the fair value of the financial instrument
- Paragraph B5.1.2A of IFRS 9 requires that if an entity determines that the fair value at initial recognition differs from the transaction price, the entity accounts for that instrument at that date as follows:
    - at the measurement required by paragraph 5.1.1 if that fair value is evidenced by a quoted price in an active market for an identical asset or liability (ie a Level 1 input) or based on a valuation technique that uses only data from observable markets. An entity recognises the difference between the fair value at initial recognition and the transaction price as a gain or loss
    - in all other cases, at the measurement required by paragraph 5.1.1, adjusted to defer the difference between the fair value at initial recognition and the transaction price. After initial recognition, the entity shall recognise that deferred difference as a gain or loss only to the extent that it arises from a change in a factor (including time) that market participants would take into account when pricing the asset or liability

Reminder of IFRS 9 approaches—subsequent measurement

Amortised Cost	Fair Value
The amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the **effective interest method** of any difference between that initial amount and the maturity amount *[Defined in IFRS 9]*	The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date *[Defined in IFRS 13]*
Interest expense recognised in profit or loss using the effective interest rate (EIR)	Changes in fair value generally recognised in profit or loss
Remeasured when estimated contractual cash flows change. By **adjusting the EIR** (as per paragraph B5.4.5) or by adjusting the amortised cost of the liability through a catch-up adjustment (as per paragraph B5.4.6 of IFRS 9).	Financial liability remeasured to **fair value** at each reporting date

IFRS
Accounting

Follow us online

ifrs.org

@IFRSFoundation

IFRS Foundation

International Accounting Standards Board