



ACCOUNTING STANDARDS UPDATE

No. 2025-07
September 2025

Derivatives and Hedging (Topic 815) and
Revenue from Contracts with
Customers (Topic 606)

Derivatives Scope Refinements and Scope
Clarification for Share-Based Noncash Consideration
from a Customer in a Revenue Contract

An Amendment of the *FASB Accounting Standards Codification*®

Financial Accounting Standards Board

The *FASB Accounting Standards Codification*[®] is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

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801 Main Avenue • Norwalk, CT • 06851

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Summary

The Board is issuing this Update to address stakeholders' concerns about (1) the application of derivative accounting to contracts with features based on the operations or activities of one of the parties to the contract and (2) the diversity in accounting for share-based noncash consideration from a customer that is consideration for the transfer of goods or services. The amendments are expected to (a) reduce the cost and complexity of evaluating whether contracts with features based on the operations or activities of one of the parties to the contract are derivatives, (b) better portray the economics of those contracts in the financial statements, and (c) reduce diversity in practice resulting from the broad application of the current guidance and changing business environment. The amendments also are expected to reduce diversity in practice by clarifying the applicability of Topic 606, Revenue from Contracts with Customers, to share-based noncash consideration from a customer for the transfer of goods or services.

Issue 1: Derivatives Scope Refinements

Why Is the FASB Issuing This Accounting Standards Update (Update)?

The amendments in this Update address stakeholders' concerns that the application of the definition of a derivative is too broad and should not apply to certain contracts. Topic 815, Derivatives and Hedging, establishes accounting requirements for contracts that meet the characteristics-based definition of a derivative and are not otherwise excluded from the Topic's scope. Because of the broad application of the definition of a derivative, many types of contracts are being evaluated and potentially accounted for as derivatives.

Feedback on the 2021 Invitation to Comment, *Agenda Consultation*, indicated that questions have emerged about the application of the definition of a derivative (and the related scope exceptions) to (1) certain emerging transactions, such as bonds in which interest payments may vary based on environmental, social, and governance (ESG)-linked metrics, and (2) certain longstanding transactions, such as research and development funding arrangements and litigation funding arrangements.

A frequently cited challenge was the changing business environment and the broad application of the derivative definition and the complexity of applying scope exceptions to certain contracts with variables (referred to as “underlyings”) based on operations or activities specific to one of the parties to the contract. Some respondents noted that because those contracts relate to the performance of a party to the contract, accounting for those contracts as derivatives measured at fair value does not provide decision-useful information. Some respondents indicated that other guidance in generally accepted accounting principles (GAAP) exists to account for those contracts. Furthermore, respondents noted that because of the cost and complexity of applying the derivative guidance and the less decision-useful financial reporting that results from applying that guidance, some entities may structure those transactions in an attempt to avoid accounting for them as derivatives. The Board is issuing this Update to address the issues raised by stakeholders by expanding the scope of a current exception in Topic 815.

Who Is Affected by the Amendments in This Update?

The amendments in this Update apply to all entities that enter into non-exchange-traded contracts with underlyings based on operations or activities specific to one of the parties to the contract.

What Are the Main Provisions?

The amendments in this Update exclude from derivative accounting non-exchange-traded contracts with underlyings that are based on operations or activities specific to one of the parties to the contract. However, this scope exception does not apply to (1) variables based on a market rate, market price, or market index, (2) variables based on the price or performance of a financial asset or financial liability of one of the parties to the contract, (3) contracts (or features) involving the issuer’s own equity that are evaluated under the guidance in Subtopic 815-40, Derivatives and Hedging—Contracts in Entity’s Own Equity, and (4) call options and put options on debt instruments.

How Do the Main Provisions Differ from Current Generally Accepted Accounting Principles (GAAP) and Why Are They an Improvement?

A contract may meet the definition of a derivative in its entirety or contain

provisions or features that may be required to be accounted for separately as derivatives. Current GAAP provides certain scope exceptions from Topic 815, including for contracts that are not traded on an exchange.

The amendments in this Update expand the scope exception for certain contracts not traded on an exchange to include contracts for which settlement is based on operations or activities specific to one of the parties to the contract. This improvement is expected to result in more contracts and embedded features being excluded from the scope of Topic 815.

The amendments in this Update are expected to improve the decision usefulness of financial reporting for contracts with underlyings based on operations or activities specific to one of the parties to the contract and reduce cost and complexity for entities analyzing and applying the derivative guidance.

When Will the Amendments Be Effective and What Are the Transition Requirements?

The amendments in this Update are effective for all entities for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods. Early adoption is permitted.

An entity is permitted to apply the amendments in this Update either (1) prospectively to new contracts entered into on or after the date of adoption or (2) on a modified retrospective basis through a cumulative-effect adjustment to the opening balance of retained earnings as of the beginning of the annual reporting period of adoption for contracts existing as of the beginning of the annual reporting period of adoption.

If an entity applies the modified retrospective transition method described in the preceding paragraph, upon adoption the entity may elect on an instrument-by-instrument basis to (1) measure contracts previously accounted for as derivatives that are no longer accounted for as derivatives in their entirety under the amendments in this Update at fair value with changes in fair value recognized in earnings and (2) stop applying the fair value option for contracts that contained embedded features that otherwise would have been bifurcated but are no longer accounted for as derivatives under the amendments in this Update.

Issue 2: Scope Clarification for Share-Based Noncash Consideration from a Customer in a Revenue Contract

Why Is the FASB Issuing This Accounting Standards Update (Update)?

The Board received feedback from some stakeholders that there is a lack of clarity about which guidance an entity should apply to recognize share-based noncash consideration, such as warrants or shares, received from a customer that is consideration for the transfer of goods or services. For example, if an entity receives share-based noncash consideration from a customer that is contingent on the satisfaction of performance obligations, some stakeholders indicated that it is unclear whether that consideration (1) should be recognized at contract inception as a derivative asset under Topic 815 or an equity security under Topic 321, Investments—Equity Securities, or (2) should not be recognized until the entity satisfies its performance obligations under Topic 606. In response to this feedback, the Board decided to clarify the accounting by an entity that receives share-based noncash consideration from a customer for the transfer of goods or services.

Who Is Affected by the Amendments in This Update?

The amendments in this Update apply to all entities that enter into contracts to receive share-based noncash consideration from a customer for the transfer of goods or services.

What Are the Main Provisions?

The amendments in this Update clarify that an entity should apply the guidance in Topic 606, including the guidance on noncash consideration in paragraphs 606-10-32-21 through 32-24, to a contract with share-based noncash consideration (for example, shares, share options, or other equity instruments) from a customer for the transfer of goods or services. The guidance in other Topics (including Topic 815 on derivatives and hedging and Topic 321 on equity securities) does not apply to share-based noncash consideration from a customer for the transfer of goods or services unless and until the entity's right to receive or retain the share-based noncash consideration is unconditional under Topic 606.

How Do the Main Provisions Differ from Current Generally Accepted Accounting Principles (GAAP) and Why Are They an Improvement?

The amendments in this Update are expected to reduce diversity in the accounting for share-based noncash consideration from a customer for the transfer of goods or services by clarifying when Topic 606 and other Topics are applicable. The amendments are expected to provide investors with more comparable information and reduce accounting complexity and related reporting costs for preparers and auditors.

When Will the Amendments Be Effective and What Are the Transition Requirements?

The amendments in this Update are effective for all entities for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods. Early adoption is permitted.

An entity is permitted to apply the amendments in this Update either (1) prospectively to new contracts entered into on or after the date of adoption, including modified contracts accounted for as separate contracts in accordance with paragraph 606-10-25-12, or (2) on a modified retrospective basis through a cumulative-effect adjustment to the opening balance of retained earnings as of the beginning of the annual reporting period of adoption for contracts existing as of the beginning of the annual reporting period of adoption.

Amendments to the *FASB Accounting Standards Codification*[®]

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–14. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck out~~.

Issue 1: Derivatives Scope Refinements

Amendments to Topic 815

2. Amend paragraphs 815-10-15-10 and its related heading, 815-10-15-59, 815-10-15-74 through 15-75, 815-10-15-98, 815-10-55-2 and its related heading, 815-10-55-43, and 815-10-55-136 through 55-137 and their related headings, supersede paragraphs 815-10-15-61 and 815-10-55-44 and its related heading, and add paragraphs 815-10-55-143A through 55-143S and their related headings, with a link to transition paragraph 815-10-65-8, as follows:

Derivatives and Hedging—Overall

Scope and Scope Exceptions

> Instruments

• > Instruments ~~Within~~ within Scope

815-10-15-10 The guidance in the General Subsections of this Subtopic applies to all derivative instruments, as that term is defined in paragraph 815-10-15-83, unless explicitly excluded by this Subsection (see paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-82). The General Subsections of this Subtopic also identify incremental guidance that applies specifically to **forward commitment dollar rolls**.

- > Instruments Not within Scope

- • > Certain Contracts That Are Not Traded on an Exchange

815-10-15-59 Contracts that are not exchange-traded are not subject to the requirements of this Subtopic if the underlying on which the settlement is based is any one of the following:

- a. A climatic or geological variable or other physical variable. Climatic, geological, and other physical variables include things like the number of inches of rainfall or snow in a particular area and the severity of an earthquake as measured by the Richter scale. (See Example 13 [paragraph 815-10-55-135].)
- b. The price or value of a nonfinancial asset of one of the parties to the contract provided that the asset is not readily convertible to cash. This scope exception applies only if both of the following are true:
 1. The nonfinancial assets are unique.
 2. The nonfinancial asset related to the underlying is owned by the party that would not benefit under the contract from an increase in the fair value of the nonfinancial asset. (If the contract is a call option, the scope exception applies only if that nonfinancial asset is owned by the party that would not benefit under the contract from an increase in the fair value of the nonfinancial asset above the option's strike price.)
- c. The fair value of a nonfinancial liability of one of the parties to the contract provided that the liability does not require delivery of an asset that is readily convertible to cash.
- d. Specified volumes of sales or service revenues of one of the parties to the contract. (This scope exception applies to contracts with settlements based on the volume of items sold or services rendered, for example, royalty agreements. This scope exception does not apply to contracts based on changes in sales or revenues due to changes in market prices.)
- e. An underlying that is based on operations or activities specific to one of the parties to the contract. This scope exception applies to underlyings based on the financial operating results (or components of those results) of one of the parties to the contract. This scope exception also applies to underlyings based on the occurrence or nonoccurrence of an event specific to the operations or activities of one of the parties to the contract (such as obtaining regulatory approval, achieving a product

development milestone, or achieving a greenhouse gas emissions reduction target). When evaluating whether operations or activities are specific to one of the parties to the contract, an entity does not need to consider whether the outcome is within its control. This scope exception does not apply to any of the following:

1. Underlyings that are based on a market rate, market price, or market index (including those in paragraph 815-10-15-88(a) through (f)). (See Example 14A—Case F [paragraph 815-10-55-143K] and Case I [paragraphs 815-10-55-143P through 55-143Q] that illustrate the application of this exclusion to the scope exception.)
2. Underlyings that are based on the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract. For example, the scope exception does not apply to underlyings based on (i) a rate of return or a default rate on a pool of loans held by one of the parties to the contract or (ii) the occurrence or nonoccurrence of an event of default or other credit event by a borrower (or reference entity) on a loan held by one of the parties to the contract. (See Example 14A—Case J [paragraphs 815-10-55-143R through 55-143S] that illustrates the application of this exclusion to the scope exception.)
3. Contracts involving an entity's own equity that are subject to paragraph 815-10-15-74(a) and Subtopic 815-40.
4. Call options and put options on debt instruments that are subject to paragraphs 815-15-25-41 through 25-43.

Solely for purposes of applying the scope exception in (e), the term *party to the contract* includes the parent, subsidiaries, or other entities consolidated by the parent for both consolidated financial statements and the standalone financial statements of individual entities within the consolidated group.

815-10-15-60 If a contract has more than one underlying and some, but not all, of them qualify for one of the scope exceptions in paragraph 815-10-15-59, the application of this Subtopic to that contract depends on its predominant characteristics. That is, the contract is subject to the requirements of this Subtopic if all of its underlyings, considered in combination, behave in a manner that is highly correlated with the behavior of any of the component variables that do not qualify for a scope exception.

815-10-15-61 Paragraph superseded by Accounting Standards Update 2025-07. ~~A contract based on any variable that is not specifically excluded by paragraph 815-10-15-59 is subject to the requirements of this Subtopic if it has the other two characteristics (initial net investment and net settlement) identified in this Subsection.~~

• • > **Certain Contracts Involving an Entity's Own Equity**

815-10-15-74 Notwithstanding the conditions of paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-139, the reporting entity shall not consider the following contracts to be derivative instruments for purposes of this Subtopic:

[The remainder of this paragraph is not shown here because it is unchanged.]

815-10-15-75 The scope exceptions in paragraph 815-10-15-74 do not apply to either of the following:

- a. The counterparty in those contracts. For example, the scope exception in (b) in ~~the preceding paragraph 815-10-15-74~~ related to share-based compensation arrangements does not apply to equity instruments (including stock options) received by nonemployees as compensation for goods and services.
- b. A contract that an entity either can or must settle by issuing its own equity instruments but that is indexed in part or in full to something other than its own stock. That contract can be a derivative instrument for the issuer under paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-139, in which case it would be accounted for as a liability or an asset in accordance with the requirements of this Subtopic. For example, a forward contract that is indexed to both an entity's own stock and currency exchange rates does not qualify for the exception in (a) in ~~the preceding paragraph 815-10-15-74~~ with respect to that entity's accounting because the forward contract is indexed in part to something other than that entity's own stock (namely, currency exchange rates).

> **Definition of Derivative Instrument**

• > **Initial Net Investment**

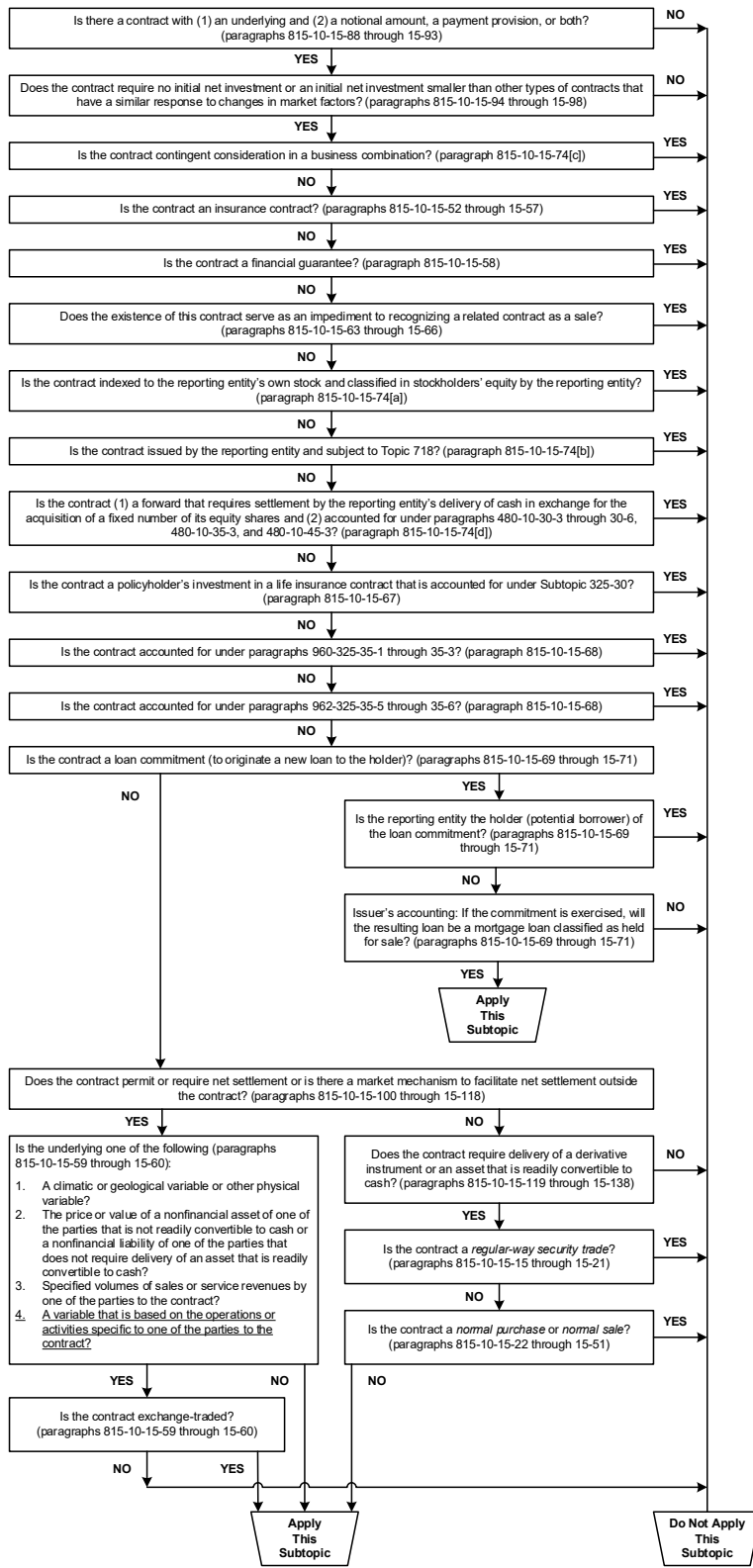
815-10-15-98 The phrase *initial net investment* is stated from the perspective of only one party to the contract, but it determines the application of this Subtopic for both parties. Even though a contract may be a derivative instrument as described in paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-139 for both parties, the scope exceptions in paragraphs 815-10-15-74 through 15-75 apply only to the issuer of the contract and will result in different reporting by the two parties. The normal purchases and sales scope exception (beginning in paragraph 815-10-15-22) also may apply to one of the parties but not the other.

Implementation Guidance and Illustrations

> Implementation Guidance

- > **Determining Whether a Contract Is within the Scope of This this Subtopic**

815-10-55-2 The following diagram depicts the process for determining whether a **freestanding contract** is within the scope of this Subtopic. The diagram is a visual supplement to the written standards Sections. It shall not be interpreted to alter any requirements of this Subtopic ~~nor shall it be or be~~ considered a substitute for the requirements. The relevant paragraphs are identified in the parenthetical note after the question.



• > **Scope Application to Certain Contracts**

815-10-55-43 This guidance illustrates the application of Section 815-10-15 in the following situations:

- a. ~~Subparagraph superseded by Accounting Standards Update No. 2025-07. Contract with payment provision~~
- b. Credit derivatives
- c. Equity options issued to employees and nonemployees
- d. Subparagraph superseded by Accounting Standards Update No. 2018-07.
- e. Repurchase agreements and wash sales
- f. Short sales (sales of borrowed securities)
- g. Take-or-pay contracts.

••> **Contract with Payment Provision**

815-10-55-44 ~~Paragraph superseded by Accounting Standards Update No. 2025-07. If the contract contains a **payment provision** that requires the issuer to pay to the holder a specified dollar amount based on a financial variable, the contract is subject to the requirements of this Subtopic. [Content amended and moved to paragraph 815-10-55-137]~~

> **Illustrations**

• > **Example 13: Certain Contracts ~~That that~~ Are Not Traded on an Exchange—Distinguishing between ~~Between~~ Physical and Financial Variables**

•• > **Case A: Contract Containing both ~~Both~~ a Physical Variable and a Financial Variable**

815-10-55-136 A contract's **{add glossary link}**payment provision**{add glossary link}** specifies that the issuer will pay to the holder \$10,000,000 if aggregate property damage from all hurricanes in the state of Florida exceeds \$50,000,000 during the year 2001.

815-10-55-137 If the contract contains a **{remove glossary link}**payment provision**{remove glossary link}** that requires the issuer to pay to the holder a specified dollar amount based on a financial variable, the contract is subject to the requirements of this Subtopic. **[Content amended as shown and**

moved from paragraph 815-10-55-44] In this Case, the payment under the contract occurs if aggregate property damage from all hurricanes in the state of Florida exceeds \$50,000,000 during the year 2001. The contract contains 2 underlyings—a physical variable (that is, the occurrence of at least 1 hurricane) and a financial variable (that is, aggregate property damage exceeding a specified or determinable dollar limit of \$50,000,000). Because of the presence of the financial variable as an underlying, the derivative instrument does not qualify for the scope exclusion in paragraph 815-10-15-59(a).

• > Example 14A: Certain Contracts That Are Not Traded on an Exchange—Underlyings Based on Operations or Activities Specific to One of the Parties to the Contract

815-10-55-143A The following Cases illustrate application of the scope exception in paragraph 815-10-15-59(e):

- a. Research and Development Funding Arrangement—Underlyings based on the occurrence of regulatory approval and achieving an earnings target (Case A)
- b. Monetization Transaction—Underlyings based on the occurrence of regulatory approval and achieving a sales target (Case B)
- c. Sustainability-Linked Bond—Underlying based on the failure to meet a greenhouse gas emissions reduction target (Case C)
- d. Litigation Funding Arrangement between Litigant and Funder—Underlying based on the occurrence of a successful litigation outcome (Case D)
- e. Litigation Funding Arrangement between Law Firm and Funder—Underlying based on the occurrence of a successful litigation outcome (Case E)
- f. Commodities-Based Arrangement—Underlying based on a market price of gold (Case F)
- g. Variable Payment Arrangement—Underlying based on the occurrence of regulatory approval (Case G)
- h. Earnout Arrangement—Underlying based on earnings activity (Case H)
- i. Variable Payment Arrangement—Underlying based on stock price differential (Case I)
- j. Credit Default Swap Arrangement—Underlying based on the occurrence of a credit event by the reference entity (Case J).

**• • > Case A: Research and Development Funding Arrangement—
Underlyings Based on the Occurrence of Regulatory Approval and
Achieving an Earnings Target**

815-10-55-143B Entity A and Entity B enter into a research and development funding arrangement. Under the arrangement, Entity B provides funding of \$50 million so that Entity A may develop and commercialize a drug compound. The arrangement has no clawback feature. Upon regulatory approval of the drug, Entity A pays \$20 million to Entity B. Once the drug is commercialized, Entity A pays an additional \$80 million to Entity B when gross profit related to the drug exceeds \$500 million.

815-10-55-143C The arrangement contains 2 underlyings: the occurrence of regulatory approval and an earnings measure (gross profit related to the drug exceeding \$500 million). Because the occurrence of regulatory approval and gross profit relate to the drug that Entity A is developing, both of the underlyings are based on the operations or activities of Entity A. Whether the occurrence of regulatory approval is within the control of Entity A does not impact the conclusion that the underlying qualifies for the scope exception. Neither underlying is based on a market rate, market price, market index, or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract as described in paragraph 815-10-15-59(e)(1) and (e)(2). Also, the exclusions related to contracts involving an entity's own equity or call options and put options on debt instruments as described in paragraph 815-10-15-59(e)(3) and (e)(4) do not apply. Therefore, those two underlyings each qualify for the scope exception in paragraph 815-10-15-59(e).

**• • > Case B: Monetization Transaction—Underlyings Based on the
Occurrence of Regulatory Approval and Achieving a Sales Target**

815-10-55-143D Entity A licenses its intellectual property to a third party to develop and commercialize a drug compound. While Entity A is not involved in the development and commercialization activities of the drug compound, the third party has agreed to pay Entity A (a) \$20 million upon regulatory approval of the drug and (b) future royalties based on sales of the drug once the drug is commercialized. Entity A separately enters into an arrangement with Entity B. Under this arrangement, Entity B pays \$50 million to Entity A in exchange for the right to receive a portion of both the (a) \$20 million payment upon regulatory approval of the drug and (b) future royalties based on sales of the drug. Entity B is involved in the arrangement solely for investment purposes and is not

involved in the development and commercialization of the drug.

815-10-55-143E The evaluation of the scope exception in this Example focuses on the arrangement between Entity A and Entity B. That arrangement contains two underlyings: the occurrence of regulatory approval and sales of the drug. Both of the underlyings are based on the operations or activities of Entity A because in this arrangement Entity A licenses the intellectual property and receives licensing income for both the regulatory approval payment and the royalties from sales of the drug. Whether the occurrence of regulatory approval is within the control of Entity A does not impact the conclusion that the underlying qualifies for the scope exception. Neither underlying is based on a market rate, market price, market index, or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract as described in paragraph 815-10-15-59(e)(1) and (e)(2). Also, the exclusions related to contracts involving an entity's own equity or call options and put options on debt instruments as described in paragraph 815-10-15-59(e)(3) and (e)(4) do not apply. Therefore, those two underlyings each qualify for the scope exception in paragraph 815-10-15-59(e).

• • > Case C: Sustainability-Linked Bond—Underlying Based on the Failure to Meet a Greenhouse Gas Emissions Reduction Target

815-10-55-143F On July 1, 20X1, Entity A issues a five-year fixed-rate bond. If Entity A's parent entity, Parent Company, fails to meet a specified greenhouse gas emissions reduction target that includes both direct and indirect greenhouse gas emissions (including upstream and downstream emissions) at the consolidated group level by June 30, 20X3, the fixed interest rate on Entity A's bond increases by 0.25 percent for the remaining term. Entity A and Parent Company are committed to meeting the target and taking actions to reduce greenhouse gas emissions. The bond is a hybrid instrument that contains an embedded feature that is required to be evaluated for bifurcation. The embedded feature contains one underlying: the failure to meet a greenhouse gas emissions reduction target at the consolidated group level. Because Entity A is a subsidiary of Parent Company, the failure to meet the greenhouse gas emissions reduction target at the consolidated level is considered an activity specific to one of the parties to the contract for the purposes of both Entity A's standalone financial statements and Parent Company's consolidated financial statements. The underlying is not based on a market rate, market price, market index, or the price or performance (including default) of a financial asset or

financial liability of one of the parties to the contract as described in paragraph 815-10-15-59(e)(1) and (e)(2). Also, the exclusions related to contracts involving an entity's own equity or call options and put options on debt instruments as described in paragraph 815-10-15-59(e)(3) and (e)(4) do not apply. Therefore, the underlying qualifies for the scope exception in paragraph 815-10-15-59(e).

• • > Case D: Litigation Funding Arrangement between Litigant and Funder—Underlying Based on the Occurrence of a Successful Litigation Outcome

815-10-55-143G Entity A, a litigant seeking to recover patent infringement damages, enters into a funding arrangement with Entity B. Under the arrangement, Entity B provides \$1 million to fund Entity A's litigation. The arrangement has no clawback feature. Upon a successful litigation outcome, Entity A will pay Entity B 50 percent of the settlement amount that it receives from the resolution of the litigation.

815-10-55-143H The arrangement between Entity A and Entity B contains one underlying: the occurrence of a successful litigation outcome. The settlement amount (and the percentage of this amount) received from the resolution of the litigation is a payment provision. Because Entity A is engaged in the legal proceeding, the underlying is based on the operations or activities of Entity A. The underlying is not based on a market rate, market price, market index, or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract as described in paragraph 815-10-15-59(e)(1) and (e)(2). Also, the exclusions related to contracts involving an entity's own equity or call options and put options on debt instruments as described in paragraph 815-10-15-59(e)(3) and (e)(4) do not apply. Therefore, the underlying qualifies for the scope exception in paragraph 815-10-15-59(e).

• • > Case E: Litigation Funding Arrangement between Law Firm and Funder—Underlying Based on the Occurrence of a Successful Litigation Outcome

815-10-55-143I Entity C, a law firm, has been engaged to represent a litigant whereby legal fees are calculated as 30 percent of the final judgment (the settlement amount). Entity C separately enters into a funding arrangement with Entity B. Under the arrangement, Entity B provides funding of \$1 million so that Entity C may hire additional staff to perform research related to the litigant's

legal proceeding. The arrangement has no clawback feature. Upon a successful litigation outcome, Entity C will pay Entity B 50 percent of the legal fees received from the litigant.

815-10-55-143J The evaluation of the scope exception in this Example focuses on the arrangement between Entity C and Entity B. That arrangement contains one underlying: the occurrence of a successful litigation outcome related to the litigant that Entity C is representing. The settlement amount (and the percentage of this amount) received by the litigant is a payment provision. Because Entity C is engaged to represent the litigant in the legal proceeding, the underlying is based on the operations or activities of Entity C. The underlying is not based on a market rate, market price, market index, or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract as described in paragraph 815-10-15-59(e)(1) and (e)(2). Also, the exclusions related to contracts involving an entity's own equity or call options and put options on debt instruments as described in paragraph 815-10-15-59(e)(3) and (e)(4) do not apply. Therefore, the underlying qualifies for the scope exception in paragraph 815-10-15-59(e).

• • > Case F: Commodities-Based Arrangement—Underlying Based on a Market Price of Gold

815-10-55-143K Entity A buys and sells gold as part of its operations. Entity A enters into a contract with Entity B whereby Entity A receives an upfront payment in exchange for a specified percentage of a price increase in the market price of gold. The arrangement contains one underlying: the market price of gold. The underlying is based on a market price as described in paragraph 815-10-15-59(e)(1). Therefore, the underlying does not qualify for the scope exception in paragraph 815-10-15-59(e).

• • > Case G: Variable Payment Arrangement—Underlying Based on the Occurrence of Regulatory Approval

815-10-55-143L Entity A, a pharmaceutical company, acquires Entity B, a biotechnology start-up company that does not meet the definition of a business. As part of the transaction, Entity A and the sellers of Entity B enter into a variable payment arrangement whereby Entity A will pay the sellers of Entity B an additional \$2 million upon regulatory approval of a drug compound that Entity B is developing.

815-10-55-143M The arrangement contains one underlying: the occurrence of regulatory approval. The occurrence of regulatory approval relates to the drug that Entity B is developing as part of its operations. The underlying is not based on a market rate, market price, market index, or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract as described in paragraph 815-10-15-59(e)(1) and (e)(2). Also, the exclusions related to contracts involving an entity's own equity or call options and put options on debt instruments as described in paragraph 815-10-15-59(e)(3) and (e)(4) do not apply. Therefore, the underlying qualifies for the scope exception in paragraph 815-10-15-59(e).

• • > Case H: Earnout Arrangement—Underlying Based on Earnings Activity

815-10-55-143N Entity A acquires a patent from Entity B. As part of the transaction, Entity A and Entity B enter into an earnout arrangement whereby Entity A will pay Entity B \$3 for each \$1 that earnings before interest, taxes, depreciation, and amortization (EBITDA) associated with the manufacturing and sale of products that rely on that patent is in excess of \$1 million on the 1-year anniversary of the purchase date. If EBITDA associated with the manufacturing and sale of products using the patent does not exceed \$1 million, Entity A does not owe Entity B any amounts under the earnout arrangement.

815-10-55-143O The arrangement contains one underlying: an earnings measure (EBITDA) related to the manufacturing and sale of products that rely on the patent acquired by Entity A. The underlying is not based on a market rate, market price, market index, or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract as described in paragraph 815-10-15-59(e)(1) and (e)(2). Also, the exclusions related to contracts involving an entity's own equity or call options and put options on debt instruments as described in paragraph 815-10-15-59(e)(3) and (e)(4) do not apply. Therefore, the underlying qualifies for the scope exception in paragraph 815-10-15-59(e).

• • > Case I: Variable Payment Arrangement—Underlying Based on Stock Price Differential

815-10-55-143P Entity A acquires Entity B (which does not meet the definition of a business) in exchange for two million shares of Entity A's common stock. As part of the acquisition agreement, Entity A agrees to pay cash to the sellers of Entity B if the quoted market price of Entity A's common stock is less than \$100 on the 1-year anniversary of the acquisition date. Specifically, if the quoted market price of Entity A's common stock is less than \$100 on the 1-year anniversary of the acquisition date, the total amount paid in cash to the sellers of Entity B is equal to \$100 minus Entity A's common stock price on the 1-year anniversary of the acquisition date multiplied by 2 million shares.

815-10-55-143Q The arrangement contains 1 underlying: the common stock price differential (\$100 less Entity A's common stock price at the 1-year anniversary of the acquisition date). The underlying is based on a market price as described in paragraph 815-10-15-59(e)(1). Therefore, the underlying does not qualify for the scope exception in paragraph 815-10-15-59(e).

• • > Case J: Credit Default Swap Arrangement—Underlying Based on the Occurrence of a Credit Event by the Reference Entity

815-10-55-143R Entity A holds a debt instrument issued by Entity C. Entity A separately enters into a credit default swap arrangement with Entity B to obtain credit protection on its debt investment in Entity C (the reference entity). As part of that arrangement, Entity A makes periodic premium payments to Entity B, and, in exchange, Entity B agrees to make a cash payment to Entity A if the reference entity defaults on the debt instrument.

815-10-55-143S The arrangement contains one underlying: the occurrence of an event of default by the reference entity. While the underlying is not based on a market rate, market price, or market index as described in paragraph 815-10-15-59(e)(1), the underlying is based on the price or performance (including default) of a financial asset of one of the parties to the contract (the debt instrument held by Entity A) as described in paragraph 815-10-15-59(e)(2). Therefore, the underlying does not qualify for the scope exception in paragraph 815-10-15-59(e).

3. Add paragraph 815-10-65-8 and its related heading as follows:

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 2025-07, Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606): Derivatives Scope Refinements and Scope Clarification for Share-Based Noncash Consideration from a Customer in a Revenue Contract

815-10-65-8 The following represents the transition and effective date information related to Accounting Standards Update No. 2025-07, *Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606): Derivatives Scope Refinements and Scope Clarification for Share-Based Noncash Consideration from a Customer in a Revenue Contract*:

Effective date and early adoption

- a. All entities shall apply the pending content that links to this paragraph for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods.
- b. Early adoption of the pending content that links to this paragraph is permitted in both interim and annual reporting periods in which financial statements have not yet been issued or made available for issuance. If an entity early adopts the pending content that links to this paragraph in an interim reporting period, it shall apply the pending content as of the beginning of the annual reporting period that includes that interim reporting period. If an entity early adopts the pending content that links to this paragraph, it also shall early adopt the pending content that links to paragraph 606-10-65-3 simultaneously.

Transition method

- c. An entity shall apply the pending content that links to this paragraph using one of the following transition methods:
 1. Prospectively to new contracts entered into on or after the date of adoption.
 2. On a modified retrospective basis through a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the beginning of the annual reporting period of adoption for contracts existing as of the beginning of the annual reporting period of adoption.

d. If an entity applies the transition method in (c)(2) and the entity had contracts or embedded features that were accounted for as derivatives but are no longer accounted for as derivatives as a result of applying the pending content that links to this paragraph, the entity has an option as of the beginning of the annual reporting period for which the pending content is adopted to elect to apply the fair value option on an instrument-by-instrument basis and measure the contract in its entirety at fair value with changes in fair value recognized in earnings if that instrument is within the scope of paragraph 825-10-15-4. For financial liabilities, an entity shall present separately in accumulated other comprehensive income the portion of the total change in the fair value of the liability that results from a change in the instrument-specific credit risk. If an entity had previously elected the fair value option for contracts that contained embedded derivatives that otherwise would have been bifurcated but are no longer required to be bifurcated as a result of applying the pending content that links to this paragraph upon adoption, the entity has an option on an instrument-by-instrument basis to revoke the fair value option as of the beginning of the annual reporting period for which the pending content is adopted and measure the contract in accordance with other generally accepted accounting principles. For those instruments for which the entity elects or revokes its election of the fair value option, the effects of initially complying with the pending content that links to this paragraph shall be reported as a cumulative-effect adjustment directly to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the beginning of the annual reporting period in which the pending content is adopted.

Transition disclosures

- e. An entity that applies the transition method in (c)(1) shall disclose the nature of and reason for the change in accounting principle in both the interim reporting period and the annual reporting period in which the entity adopts the pending content that links to this paragraph.
- f. An entity that applies the transition method in (c)(2) shall disclose the following in both the interim reporting period and the annual reporting period in which the entity adopts the pending content that links to this paragraph:
1. The nature of and reason for the change in accounting principle

2. The cumulative effect of the change on retained earnings or other components of equity or net assets in the statement of financial position as of the beginning of the annual reporting period of adoption and a description of the financial statement line items affected by the adjustment.

4. Amend paragraphs 815-20-25-8 and 815-20-55-115 through 55-116, with a link to transition paragraph 815-10-65-8, as follows:

Derivatives and Hedging—Hedging—General

Recognition

> Eligibility of Hedged Items and Transactions

• > Hedged Item and Transaction Criteria Applicable to both Fair Value Hedges and Cash Flow Hedges

• • > Normal Purchases or Normal Sales as Hedged Items or Transactions

815-20-25-8 In emphasizing the conditions in the definition of a **derivative instrument** in paragraphs 815-10-15-83 through 15-139, paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-82 essentially exempt contracts that meet the definition of a derivative instrument from the requirements of Subtopic 815-10 applicable to derivative instruments. However, paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-82 are not intended to preclude such contracts from being subject to the requirements of Subtopic 815-10 applicable to the hedged item in a fair value hedge.

Implementation Guidance and Illustrations

> Illustrations

• > Example 8: All-in-One Hedges

• • > Case A: Purchase of a Nonfinancial Asset

815-20-55-115 Entity A plans to purchase a nonfinancial asset. To fix the price to be paid (that is, to hedge the price), Entity A enters into a contract that meets the definition of a firm commitment with an unrelated party to purchase the asset at a fixed price at a future date. Assume that the terms of the contract (such as net settlement under the default provisions) or the nature of the asset cause the contract to meet the definition of a derivative instrument and the contract is not excluded by paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-82 from the scope of the Derivatives and Hedging Topic. As such, Entity A has entered into a derivative instrument under which it is expected to take delivery of the asset. Entity A may designate the fixed-price purchase contract (that is, the derivative instrument) as a cash flow hedge of the variability of the consideration to be paid for the purchase of the asset (that is, the forecasted transaction) even though the derivative instrument is the same contract under which the asset itself will be acquired.

• • > **Case B: Purchase of a Financial Asset**

815-20-55-116 Entity B plans to purchase U.S. government bonds and expects to classify those bonds in its available-for-sale portfolio. To fix the price to be paid (that is, to hedge the price), Entity B enters into a contract that meets the Derivatives and Hedging Topic's definition of a firm commitment with an unrelated party to purchase the bonds at a fixed price at a future date. Assume the contract meets the definition of a derivative instrument and is not excluded by paragraphs 815-10-15-13 through 15-60 and 815-10-15-62 through 15-82 from the scope of this Topic. As such, Entity B has entered into a derivative instrument under which it is expected to take delivery of the asset. Entity B may designate the fixed-price purchase contract (that is, the derivative instrument) as a cash flow hedge of the variability of the consideration to be paid for the purchase of the bonds (that is, the forecasted transaction) even though the derivative instrument is the same contract under which the asset itself will be acquired.

Issue 2: Scope Clarification for Share-Based Noncash Consideration from a Customer in a Revenue Contract

Amendments to Topic 606

5. Add paragraphs 606-10-15-3A and 606-10-55-250A through 55-250D and the related heading and amend paragraphs 606-10-55-93(i) and 606-10-55-247 and the heading preceding paragraph 606-10-55-248, with a link to transition paragraph 606-10-65-3, as follows:

Revenue from Contracts with Customers—Overall

Scope and Scope Exceptions

> Transactions

606-10-15-3A An entity shall apply the guidance in this Topic, including the guidance on noncash consideration in paragraphs 606-10-32-21 through 32-24, to a contract with share-based noncash consideration (for example, shares, share options, or other equity instruments) from a customer for the transfer of goods or services. The guidance in other Topics (including Topic 815 on derivatives and hedging and Topic 321 on equity securities) does not apply to share-based noncash consideration from a customer for the transfer of goods or services unless and until the entity's right to receive or retain the share-based noncash consideration is unconditional under this Topic. To assess whether the right is unconditional under this Topic, only the contract terms that relate to the entity's performance obligations (or a specific outcome of the entity's performance) within the scope of this Topic are evaluated. The determination of whether the right is unconditional is consistent with the guidance in paragraph 606-10-45-4, which states that a right to consideration is unconditional if only the passage of time is required before payment of that consideration is due.

Implementation Guidance and Illustrations

> Illustrations

606-10-55-93 The Examples are organized as follows:

- i. Noncash Consideration
 - Example 31—Entitlement to Noncash Consideration
 - Example 31A—Share-Based Noncash Consideration

• > **Noncash Consideration**

• • > **Example 31—Entitlement to Noncash Consideration**

606-10-55-247 Example 31 illustrates the guidance in paragraph 606-10-15-3A on share-based noncash consideration from a customer for the transfer of goods or services and the guidance in paragraphs 606-10-32-21 through 32-24 on noncash consideration. In addition, the following guidance is illustrated in this Example:

- a. Paragraph 606-10-25-14 on identifying performance obligations
- b. Paragraphs 606-10-32-11 through 32-13 on constraining estimates of variable consideration.

~~• • > **Example 31—Entitlement to Noncash Consideration**~~

[Paragraphs 606-10-55-248 through 55-250 of Example 31 are not shown here because they are unchanged.]

• • > **Example 31A—Share-Based Noncash Consideration**

606-10-55-250A Example 31A illustrates the guidance in paragraph 606-10-15-3A on share-based noncash consideration from a customer for the transfer of goods or services and the guidance in paragraphs 606-10-32-21 through 32-24 on noncash consideration. In addition, the following guidance is illustrated in this Example:

- a. Paragraph 606-10-25-14 on identifying performance obligations
- b. Paragraph 606-10-32-4 on determining transaction price
- c. Paragraphs 606-10-32-5 through 32-14 on variable consideration
- d. Paragraphs 606-10-32-28 through 32-41 on allocating transaction price to the performance obligations in the contract
- e. Paragraph 606-10-45-4 on an unconditional right to consideration.

606-10-55-250B On January 1, 20X7, an entity enters into a contract with a customer to sell 5,000 units of Product A. The customer will pay \$100 for each unit upon delivery. If the entity delivers all 5,000 units within 2 years from contract inception, the customer promises a performance bonus of 100 warrants for the customer’s common stock. The estimated fair value of the 100 warrants at contract inception is \$100,000. At contract inception, the entity concludes that each unit is a performance obligation that is satisfied at a point in time. Based on its experience, the entity expects that all 5,000 units will be

delivered to the customer before the end of 20X8. Accordingly, it concludes that the variable consideration related to the 100 warrants is not constrained and the transaction price is \$600,000 ([5,000 units × \$100] + \$100,000 estimated fair value of 100 warrants at contract inception). Accordingly, the transaction price allocated to each unit is \$120 (\$600,000/5,000 units).

606-10-55-250C During 20X7, the entity delivers 3,000 units to the customer. At the end of 20X7, the entity continues to expect that the remaining 2,000 units will be delivered to the customer before the end of 20X8. Therefore, the transaction price determined at contract inception is unchanged. For 20X7, the entity recognizes revenue of \$360,000 (3,000 units × \$120), cash of \$300,000, and a contract asset of \$60,000 (\$100,000 estimated fair value of 100 warrants at contract inception × [3,000 delivered units/5,000 units]). The entity does not reflect any changes in the fair value of the 100 warrants in the transaction price. However, the entity assesses the related contract asset for impairment.

606-10-55-250D During 20X8, the entity delivers the remaining 2,000 units to the customer. For 20X8, the entity recognizes revenue of \$240,000 (2,000 units × \$120), cash of \$200,000, and a contract asset of \$40,000 (\$100,000 estimated fair value of 100 warrants at contract inception × [2,000 delivered units/5,000 units]). The entity does not reflect any changes in the fair value of the 100 warrants in the transaction price. However, the entity assesses the related contract asset for impairment. When all 5,000 units have been delivered, the entity concludes that its right to receive or retain the 100 warrants is unconditional under this Topic. At that point, the entity derecognizes the contract asset and applies the guidance in other Topics to account for the 100 warrants.

6. Add paragraph 606-10-65-3 and its related heading as follows:

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 2025-07, Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606): Derivatives Scope Refinements and Scope Clarification for Share-Based Noncash Consideration from a Customer in a Revenue Contract

606-10-65-3 The following represents the transition and effective date information related to Accounting Standards Update No. 2025-07, *Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606): Derivatives Scope Refinements and Scope Clarification for Share-Based Noncash Consideration from a Customer in a Revenue Contract*:

Effective date and early adoption

- a. All entities shall apply the pending content that links to this paragraph for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods.
- b. Early adoption of the pending content that links to this paragraph is permitted in both interim and annual reporting periods for which financial statements have not yet been issued or made available for issuance. If an entity early adopts the pending content that links to this paragraph in an interim reporting period, it shall apply the pending content as of the beginning of the annual reporting period that includes that interim reporting period. If an entity early adopts the pending content that links to this paragraph, it also shall early adopt the pending content that links to paragraph 815-10-65-8 simultaneously.

Transition method

- c. An entity shall apply the pending content that links to this paragraph using one of the following transition methods:
 1. Prospectively to new contracts entered into on or after the date of adoption, including modified contracts accounted for as separate contracts in accordance with paragraph 606-10-25-12
 2. On a modified retrospective basis through a cumulative-effect adjustment to the opening balance of retained earnings (or other appropriate components of equity or net assets in the statement of financial position) as of the beginning of the annual reporting period of adoption for contracts existing as of the beginning of the annual reporting period of adoption.

Transition disclosures

- d. An entity that applies the transition method in (c)(1) shall disclose the nature of and reason for the change in accounting principle in both the interim reporting period and the annual reporting period in which the

entity adopts the pending content that links to this paragraph.

- e. An entity that applies the transition method in (c)(2) shall disclose the following in both the interim reporting period and the annual reporting period in which the entity adopts the pending content that links to this paragraph:
1. The nature of and reason for the change in accounting principle
 2. The cumulative effect of the change on retained earnings or other components of equity or net assets in the statement of financial position as of the beginning of the annual reporting period of adoption.

Amendments to Subtopic 610-20

7. Add paragraph 610-20-15-3A, with a link to transition paragraph 606-10-65-3, as follows:

Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets

Scope and Scope Exceptions

> Transactions

610-20-15-3A An entity shall apply the guidance in this Subtopic, including the guidance on noncash consideration in paragraphs 610-20-32-3(a)(4) and 610-20-32-4, to a contract with share-based noncash consideration (for example, shares, share options, or other equity instruments) from a counterparty for the transfer of nonfinancial assets or in substance nonfinancial assets. The guidance in other Topics (including Topic 815 on derivatives and hedging and Topic 321 on equity securities) does not apply to share-based noncash consideration from a counterparty for the transfer of nonfinancial assets or in substance nonfinancial assets unless and until the entity's right to receive or retain the share-based noncash consideration is unconditional under this Subtopic. To assess whether the right is unconditional under this Subtopic, only the contract terms that relate to the entity's transfer of nonfinancial assets or in substance nonfinancial assets (or a specific outcome of the entity's transfer) within the scope of this Subtopic are evaluated. The determination of whether the right is unconditional is consistent with the guidance in paragraph 606-10-45-4, which states that a right to consideration is unconditional if only the

passage of time is required before payment of that consideration is due.

Amendments to Topic 321

8. Add paragraph 321-10-15-7, with a link to transition paragraph 606-10-65-3, as follows:

Investments—Equity Securities—Overall

Scope and Scope Exceptions

> Instruments

321-10-15-7 An entity shall not apply the guidance in this Topic to share-based noncash consideration from a customer for the transfer of goods or services unless and until the entity’s right to receive or retain the share-based noncash consideration is unconditional under Topic 606 in accordance with paragraph 606-10-15-3A. Similarly, an entity shall not apply the guidance in this Topic to share-based noncash consideration from a counterparty for the transfer of nonfinancial assets or in substance nonfinancial assets unless and until the entity’s right to receive or retain the share-based noncash consideration is unconditional under Subtopic 610-20 in accordance with paragraph 610-20-15-3A.

Amendments to Topic 815

9. Amend paragraph 815-10-25-5 and add paragraphs 815-10-25-16A through 25-16B and their related headings, with a link to transition paragraph 606-10-65-3, as follows:

Derivatives and Hedging—Overall

Recognition

815-10-25-5 The remainder of this Section addresses the following matters:

- a. Unit of accounting for recognition purposes
- b. Subparagraph not used.
- c. Forward commitment dollar rolls
- d. Derivative financial instruments subject to a **registration payment arrangement**.

- e. Share-based noncash consideration from a customer for the transfer of goods or services under Topic 606
- f. Share-based noncash consideration from a counterparty for the transfer of nonfinancial assets or in substance nonfinancial assets under Subtopic 610-20.

> Share-Based Noncash Consideration from a Customer for the Transfer of Goods or Services under Topic 606

815-10-25-16A An entity shall not apply the guidance in this Topic to share-based noncash consideration from a customer for the transfer of goods or services unless and until the entity’s right to receive or retain the share-based noncash consideration is unconditional under Topic 606 in accordance with paragraph 606-10-15-3A.

> Share-Based Noncash Consideration from a Counterparty for the Transfer of Nonfinancial Assets or In Substance Nonfinancial Assets under Subtopic 610-20

815-10-25-16B An entity shall not apply the guidance in this Topic to share-based noncash consideration from a counterparty for the transfer of nonfinancial assets or in substance nonfinancial assets unless and until the entity’s right to receive or retain the share-based noncash consideration is unconditional under Subtopic 610-20 in accordance with paragraph 610-20-15-3A.

Amendments to Status Sections

10. Amend paragraph 321-10-00-1, by adding the following item to the table, as follows:

321-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
321-10-15-7	Added	2025-07	09/29/2025

11. Amend paragraph 606-10-00-1, by adding the following items to the table, as follows:

606-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
606-10-15-3A	Added	2025-07	09/29/2025
606-10-55-93	Amended	2025-07	09/29/2025
606-10-55-247	Amended	2025-07	09/29/2025
606-10-55-248	Amended	2025-07	09/29/2025
606-10-55-250A through 55-250D	Added	2025-07	09/29/2025
606-10-65-3	Added	2025-07	09/29/2025

12. Amend paragraph 610-20-00-1, by adding the following item to the table, as follows:

610-20-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
610-20-15-3A	Added	2025-07	09/29/2025

13. Amend paragraph 815-10-00-1, by adding the following items to the table, as follows:

815-10-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Update	Date
815-10-15-10	Amended	2025-07	09/29/2025
815-10-15-59	Amended	2025-07	09/29/2025
815-10-15-61	Superseded	2025-07	09/29/2025
815-10-15-74	Amended	2025-07	09/29/2025

815-10-15-75	Amended	2025-07	09/29/2025
815-10-15-98	Amended	2025-07	09/29/2025
815-10-25-5	Amended	2025-07	09/29/2025
815-10-25-16A	Added	2025-07	09/29/2025
815-10-25-16B	Added	2025-07	09/29/2025
815-10-55-2	Amended	2025-07	09/29/2025
815-10-55-43	Amended	2025-07	09/29/2025
815-10-55-44	Superseded	2025-07	09/29/2025
815-10-55-136	Amended	2025-07	09/29/2025
815-10-55-137	Amended	2025-07	09/29/2025
815-10-55-143A through 143S	Added	2025-07	09/29/2025
815-10-65-8	Added	2025-07	09/29/2025

14. Amend paragraph 815-20-00-1, by adding the following items to the table, as follows:

815-20-00-1 The following table identifies the changes made to this Subtopic.

Paragraph	Action	Accounting Standards Board	Date
815-20-25-8	Amended	2025-07	09/29/2025
815-20-55-115	Amended	2025-07	09/29/2025
815-20-55-116	Amended	2025-07	09/29/2025

The amendments in this Update were adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Richard R. Jones, *Chair*
Hillary H. Salo, *Vice Chair*
Christine A. Botosan
Frederick L. Cannon
Susan M. Cospers
Marsha L. Hunt
Dr. Joyce T. Joseph

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

BC2. The following paragraphs are organized by issue. This organization mirrors the amendments to the Codification section.

BC3. The amendments in this Update address stakeholders' concerns about (a) the application of derivative accounting to contracts with features based on the operations or activities of one of the parties to the contract and (b) the diversity in accounting for share-based noncash consideration from a customer that is consideration for the transfer of goods or services. The amendments are expected to (i) reduce the cost and complexity of evaluating whether contracts with features based on the operations or activities of one of the parties to the contract are derivatives, (ii) better portray the economics of those contracts in the financial statements, and (iii) reduce diversity in practice resulting from the broad application of the current guidance and changing business environment. The amendments also are expected to reduce diversity in practice by clarifying the applicability of Topic 606 to share-based noncash consideration from a customer for the transfer of goods or services.

BC4. On July 23, 2024, the Board issued the proposed Accounting Standards Update, *Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606): Derivatives Scope Refinements and Scope Clarification for a Share-Based Payment from a Customer in a Revenue Contract*, for public comment with the comment period ending on October 21, 2024. The Board received 34 comment letters in response to the proposed Update. Overall, comment letter respondents supported the objective of both (a) the Board's principles-based scope exception to exclude from the scope of Topic 815 arrangements with underlyings based on the operations or activities specific to one of the parties to the contract and (b) the Board's efforts to clarify

the applicability of Topic 606 to share-based noncash consideration from a customer for the transfer of goods or services. Comment letter respondents also provided suggestions on various areas for further improvement or clarification. The Board considered stakeholder feedback on areas for further improvement or clarification in reaching the conclusions in this Update, as discussed in each issue below.

Issue 1: Derivatives Scope Refinements

Background Information

BC5. Subtopic 815-10 provides guidance on evaluating whether a financial instrument or other contract must be accounted for as a derivative instrument. Specifically, in FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*, which was issued in 1998, the Board provided a definition of a derivative instrument based on three distinguishing characteristics rather than referring to specific classes of instruments. However, when Statement 133 was issued, the Board did not want certain transactions that otherwise met the definition of a derivative to be accounted for as derivative instruments; therefore, the standard provided a list of scope exceptions. In addition to the original scope exceptions in Statement 133, which was codified as Topic 815, others have been added through subsequent amendments to the Codification.

BC6. A contract may not meet the definition of a derivative in its entirety but contains a provision or feature that could modify the cash flows of a contract based on a change in an underlying. That provision or feature is required to be bifurcated from the host contract and accounted for separately as a derivative if it meets certain criteria. In theory, this provides investors and other allocators of capital with transparency and allows them to understand the effects of embedded features. Accordingly, Subtopic 815-15, *Derivatives and Hedging—Embedded Derivatives*, provides guidance on evaluating those features for potential bifurcation from the host contract.

BC7. The Board received feedback indicating that entities experience challenges in applying the definition of a derivative and derivative scope exceptions to certain emerging transactions, such as bonds in which interest payments may vary based on ESG-linked metrics. In addition, emerging and

sometimes inconsistent scope interpretations have resulted in challenges in evaluating longstanding transactions such as research and development funding arrangements and litigation funding arrangements. Some stakeholders stated that, in their view, if derivative accounting were applied to those arrangements, it may lead to unintuitive accounting outcomes and may not be the best reflection of the economics of those contracts; therefore, they supported excluding those contracts from the scope of Topic 815.

BC8. Stakeholders noted that they incur significant costs to assess contracts under the scope of Topic 815 and to evaluate whether a contract qualifies for a scope exception. Furthermore, when those contracts qualify as a derivative, some stakeholders indicated that applying the derivative guidance is complex, which has led to diversity in practice. Some stakeholders observed that the potential application of derivative accounting has resulted in certain entities avoiding those types of contracts, which has limited certain types of activities altogether. As a result, the Board decided to refine the scope of Topic 815 specifically to exclude certain contracts from derivative accounting.

Benefits and Costs

BC9. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC10. The amendments in this Update result in removing certain contracts from the scope of derivative accounting. The Board observed that accounting for certain contracts as derivatives may not result in decision-useful information because the contracts relate to the performance of one of the parties to the contract. The Board also noted that, in many instances, derivative accounting and the requirement to measure derivatives at fair value require using complex

valuation models. In addition, accounting for those derivatives at fair value often results in assets and liabilities being recorded at amounts that would be unlikely to be realized or settled at, further reducing their predictive value for investors. Often, derivative accounting also results in a liability being recorded when the related asset fails to meet the recognition requirement under GAAP, which is viewed as not reflective of the economics of those contracts by many investors because it results in accounting for a portion of the overall, but not the entire, transaction. For example, the application of derivative accounting may result in fair value measurement of a funding mechanism when the related asset is not recognized. It may also effectively override the accounting guidance that was specifically created for certain types of transactions, such as those evaluated under Subtopic 730-20, Research and Development—Research and Development Arrangements.

BC11. The Board also considered the costs of implementing the amendments in this Update. These amendments are not expected to result in contracts not currently accounted for as a derivative being accounted for as a derivative under Topic 815. Therefore, because other current guidance applies if those contracts are not accounted for as derivatives, the implementation costs likely would not be significant. The Board acknowledged that costs may be incurred (a) to establish new controls and accounting policies for contracts that are no longer accounted for as derivatives or embedded derivatives (for example, establishing accounting policies for the recognition of interest income or interest expense for ESG-linked financial instruments) and (b) for education on the amendments. However, the Board observed that those incremental costs would be nonrecurring.

BC12. The Board also considered the benefits of implementing the amendments in this Update. The Board concluded that applying derivative accounting to the types of contracts affected by the amendments may lead to accounting results that do not reflect the economics of those contracts. Therefore, investors will receive more decision-useful information if derivative accounting is not applied. In addition, entities will benefit from a reduction in costs because they do not have to navigate and apply derivative accounting to those excluded contracts or embedded features.

BC13. Overall, the Board concluded that the expected benefits of the amendments in this Update justify the expected costs.

Basis for Conclusions

Scope Exception for Contracts with Underlyings Based on Operations or Activities Specific to One of the Parties to the Contract

BC14. An underlying, along with either a notional amount or a payment provision, determines the settlement of a derivative instrument. An underlying is defined as a specified interest rate, security price, commodity price, foreign exchange rate, index of prices or rates, or other variable (including the occurrence or nonoccurrence of a specified event such as a scheduled payment under a contract). The occurrence or nonoccurrence of a specified event was added to the definition of an underlying when FASB Statement No. 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities*, was issued in April 2003. After the issuance of Statement 149, some stakeholders noted that, in practice, the definition of a derivative may have been applied more broadly by some than may have been intended by the Board.

BC15. The Board decided to refine the scope of Topic 815 by incorporating a scope exception for contracts with underlyings based on operations or activities specific to one of the parties to the contract. For example, this scope exception generally captures underlyings based on earnings before interest, taxes, depreciation, and amortization (EBITDA), net income, and expenses. This scope exception also generally captures the occurrence or nonoccurrence of an event related to operations or activities specific to one of the parties to the contract, such as an entity obtaining regulatory approval, achieving a product development milestone, or achieving a greenhouse gas emissions reduction target. The Board observed that the various contracts described by stakeholders such as research and development funding arrangements, ESG-linked financial instruments, and litigation funding arrangements have the common characteristic that their contractual payments are based on an entity's own performance. The Board also received feedback that accounting for those contracts as derivatives may be inconsistent with the economics of these contracts.

BC16. The Board observed that guidance exists in GAAP on how to account for these contracts if they are not accounted for as derivatives. The Board determined that applying the current guidance would provide investors with more decision-useful information than accounting for those contracts as derivatives and would narrow the diversity associated with how those arrangements are accounted for in practice, even if some diversity remains.

BC17. As an alternative to the scope exception in this Update based on operations and activities, the Board considered amending the definition of a derivative in Topic 815, including the definition of an underlying. However, some stakeholders stated that other areas of GAAP (such as Topic 460, Guarantees) reference the term *underlying* in the Master Glossary. In addition, those definitions have been applied in practice for many years and are well understood. The Board concluded that an amendment to the definition of a derivative (including the definition of an underlying) would require significant effort to evaluate and identify how the amendments would affect other areas of GAAP. Moreover, some stakeholders noted that amending the definition may make assessing whether contracts are included within the scope of Topic 815 more complex. For those reasons, the Board decided not to amend the definition of a derivative in this Update, but instead to create a derivative scope exception. The Board concluded that having a clear derivative scope exception would maximize the potential for cost savings because entities typically first review the list of scope exceptions when evaluating a contract and subsequently evaluate whether the contract meets the definition of a derivative if it does not qualify for a scope exception.

BC18. In developing the scope exception, the Board considered the definition of a derivative in International Financial Reporting Standards (IFRS) 9, *Financial Instruments*. In IFRS 9, a contract with an underlying that is a nonfinancial variable that is specific to a party to the contract is not considered a derivative. The Board observed that certain contracts and embedded features that stakeholders raised in the 2021 Invitation to Comment are not currently accounted for as a derivative by entities that apply that definition. The Board concluded that the concept of “specific to a party to the contract” is a relevant and useful concept and, therefore, incorporated that concept into the amendments in this Update. However, the Board decided not to incorporate the exact same guidance in IFRS 9 because the term *nonfinancial variable*, which is included in IFRS 9, is not defined in GAAP. The Board was concerned that employing an existing term from IFRS 9 in GAAP could create confusion

in practice and that some may interpret the term *nonfinancial variable* to exclude certain financial statement metrics, such as net income or EBITDA.

BC19. The Board also considered introducing scope exceptions for certain types of contracts such as research and development funding arrangements, ESG-linked financial instruments, and litigation funding arrangements rather than including a principles-based scope exception based on operations or activities specific to one of the parties to the contract. However, the Board decided that defining these types of contracts may not be feasible and that scope exceptions for certain types of contracts may be more susceptible to structuring and may result in economically similar contracts being accounted for differently. Also, in the absence of a common principle, determining which contracts should be excluded from or included within the scope of Topic 815 could be more challenging. The Board decided that a principles-based scope exception would be more durable because it will address a broad population of existing and emerging types of contracts. In contrast, adding scope exceptions for certain types of contracts may result in ongoing requests for additional standard setting as new types of contracts emerge.

BC20. Comment letter respondents supported a principles-based scope exception rather than amending the definition of a derivative or creating instrument-specific scope exceptions for research and development funding arrangements, ESG-linked financial instruments, and litigation funding arrangements. Also, stakeholders supported that the principles-based scope exception excludes from the scope of Topic 815 contracts with underlyings based on operations or activities specific to one of the parties to the contract.

Underlyings and Contracts Not Eligible for the Principles-Based Scope Exception

BC21. Because of the broad nature of the principles-based scope exception, the Board concluded that certain underlyings should not be eligible for that scope exception. Specifically, the Board determined that underlyings based on (a) a market rate, market price, or market index, including those in paragraph 815-10-15-88(a) through (f), or (b) the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract should not be captured by the scope exception in paragraph 815-10-15-59(e). This exclusion captures instruments commonly understood to be and accepted as derivatives (such as interest rate swaps and commodity forward contracts).

BC22. The Board observed that the exclusion related to underlyings based on a market price currently exists in the specified volumes of sales or service revenues scope exception in paragraph 815-10-15-59(d). Similar to the current interpretations of the specified volumes of sales or service revenues scope exception in paragraph 815-10-15-59(d), the exclusion in paragraph 815-10-15-59(e) was not intended to preclude an entity from applying the scope exception to payment provisions that are based on a combination of variables, rather than solely based on a market price.

BC23. The Board also concluded that an underlying based on the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract (for example, certain guarantee contracts in which the payoff depends on the performance of a financial asset or financial liability [such as loans and debt] of one of the parties to the contract) should not be captured by the scope exception in paragraph 815-10-15-59(e). Without this exclusion, that type of contract would meet the scope exception in that paragraph because that scope exception is more expansive than the financial guarantee contracts scope exception in paragraph 815-10-15-58. Furthermore, this exclusion is necessary because similar instruments such as credit default swaps are commonly understood to be derivatives and should be accounted for as derivatives.

BC24. Some comment letter respondents questioned whether certain income statement metrics such as metrics based on interest income, interest expense, and credit losses would be considered underlyings based on the performance of financial assets or financial liabilities (for example, a financial institution that has assets and liabilities that give rise to those income statement items) and, therefore, would not be eligible for the scope exception in paragraph 815-10-15-59(e). Generally, the determination of whether a financial statement metric will qualify for the scope exception in paragraph 815-10-15-59(e) would be a matter of judgment, similar to the application of the current scope exception in paragraph 815-10-15-59(d). The Board believes that many financial statement metrics will qualify for the scope exception.

BC25. The Board notes that the exclusion related to the price or performance of a financial asset or financial liability applies to underlyings rather than the contracts themselves. That is, this exclusion is not intended to preclude contracts that meet the definition of a financial asset or financial liability from qualifying for the scope exception. For example, even though a litigation

funding arrangement with a contingent payment meets the definition of a financial asset, the scope exception would apply because the underlying is based on the occurrence of a successful litigation outcome rather than the price or performance of that financial asset.

BC26. During initial deliberations, the Board observed that the principles-based nature of the scope exception captures not only the types of transactions that the Board originally intended (such as research and development funding arrangements, ESG-linked financial instruments, and litigation funding arrangements), but also certain types of debt instruments with well-established accounting guidance. Specifically, under current GAAP, (a) issuers of convertible debt evaluate whether the conversion feature meets the derivative scope exception related to certain contracts involving an entity's own equity in paragraph 815-10-15-74(a) to determine whether the conversion feature should be bifurcated from the debt host contract and (b) entities generally evaluate paragraph 815-15-25-42 (originally issued as Statement 133 Implementation Issue No. B16, "Embedded Derivatives: Calls and Puts in Debt Instruments") to determine whether call options and put options should be bifurcated from the debt host contract. In the proposed Update, the Board decided not to restrict those instruments from qualifying for the proposed scope exception. For example, a conversion option embedded in a contingently convertible debt instrument would have been evaluated under two derivative scope exceptions (the exception in paragraph 815-10-15-74(a) for certain contracts involving an entity's own equity and the exception in paragraph 815-10-15-59(e) for non-exchange-traded contracts), and if the conversion option qualified for either of the scope exceptions, it would not be accounted for as a derivative.

BC27. Comment letter respondents noted that including these instruments or embedded features in the scope exception would increase the complexity of accounting for those instruments. In addition, some respondents noted that if these instruments or embedded features were eligible for the scope exception, it could create different accounting outcomes for freestanding financial instruments and hybrid instruments with comparable features. For example, certain embedded features may fail to qualify for the scope exception related to certain contracts involving an entity's own equity but would qualify for the scope exception in paragraph 815-10-15-59(e) and, therefore, would not be required to be bifurcated. However, if the same feature were a freestanding contract, it may be required to be classified as a liability and measured at fair value under Subtopic 815-40 even if it qualifies for the scope exception in

paragraph 815-10-15-59(e).

BC28. Stakeholders generally indicated that there is current guidance for those instruments and embedded features and therefore provided feedback that those contracts and embedded features should be excluded from the scope exception. Because of that comment letter feedback, the Board decided to exclude (a) contracts involving an entity's own equity that are subject to Subtopic 815-40 and (b) call options and put options on debt instruments that are subject to paragraphs 815-15-25-41 through 25-43 from qualifying for the scope exception in paragraph 815-10-15-59(e).

BC29. The Board observed that under the amendments in this Update, certain contracts, including deal-contingent interest rate swaps and ESG-linked interest rate swaps, will likely need to be evaluated under the predominant characteristics assessment to determine whether they are subject to derivative accounting because they include one underlying that would be eligible for the scope exception and one underlying that would not. The Board observed that if those contracts are not accounted for as derivatives at contract inception because they meet the scope exception in paragraph 815-10-15-59(e), they would likely be recognized as derivatives at a later date after the contingency related to an entity's own operations or activities is resolved.

BC30. During initial deliberations, the Board considered (but rejected) an alternative approach whereby a contract would have been accounted for as a derivative if any individual underlying did not qualify for any of the scope exceptions in paragraph 815-10-15-59. During redeliberations, the Board considered a similar alternative approach that would have excluded contracts from qualifying for the scope exception if any of the underlyings in the contract were a market rate, market price, or market index or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract. This alternative approach would have excluded not only contracts involving an entity's own equity and certain call options and put options on debt instruments (for example, a put feature embedded in a bond that is contingently exercisable if the issuer has an initial public offering) but also other contracts such as deal-contingent interest rate swaps and ESG-linked interest rate swaps from qualifying for the scope exception because they generally involve a market-based underlying.

BC31. The Board rejected this alternative approach during redeliberations. The Board concluded that (a) this alternative approach would have resulted in more contracts being accounted for as derivatives than intended by the Board and (b) excluding the specific contracts or features discussed in paragraph BC28 requires less judgment and, therefore, will result in less diversity in practice and be easier for entities to apply.

Operations or Activities Specific to One of the Parties to the Contract

BC32. The Board considered whether the phrase *party to the contract* should be limited to the legal entity that entered into the contract. Stakeholders indicated that some contracts may reference activities at the consolidated level or parent-entity level rather than at an individual reporting entity level and limiting “party to the contract” to the legal entity that entered into the contract may narrow the application of the expanded scope exception. In initial deliberations, the Board decided that the scope exception should capture not only the activities of the legal entity that is the party to the contract but also the activities of the parent, subsidiaries, and other entities consolidated by the parent for the purposes of both consolidated financial statements and the standalone financial statements of individual entities within the consolidated group. Comment letter respondents generally supported the broader interpretation of the phrase *parties to the contract* (including parties outside the reporting entity) to incorporate various types of contracts that exist in practice. Some respondents indicated that this broader interpretation is different from how current practice treats other contracts in standalone financial statements under other Topics. Therefore, the Board decided during redeliberations to clarify that this concept should be applied solely for purposes of applying the scope exception in paragraph 815-10-15-59(e) (that is, an entity should not apply the party to the contract concept by analogy in other areas of GAAP).

BC33. The Board considered whether an entity would need to determine whether the “activity” is within the control of one of the parties to the contract. Stakeholders provided examples of underlyings that may be subject to operations or activities specific to one of the parties to the contract but the outcomes of those underlyings may not be fully within the control of the entity, such as regulatory approval and favorable litigation outcomes. In response to stakeholder feedback, the Board decided that when evaluating whether operations or activities are “specific to one of the parties to the contract,” an

entity does not need to determine whether the outcome is within the control of an entity because stakeholders noted that a control-based principle would be subjective, be challenging to apply, and potentially create diversity in practice. In addition, including a control-based principle would significantly narrow the application of the scope exception.

Predominant Characteristics Assessment

BC34. When a contract (or an embedded feature in a hybrid instrument) has more than one underlying and some, but not all, of them qualify for the scope exception in paragraph 815-10-15-59, an entity must perform a predominant characteristics assessment, which is a correlation assessment. That assessment is needed to determine whether the freestanding contract (in its entirety) or an embedded feature (in a hybrid instrument) qualifies for the scope exception. Stakeholders indicated that the correlation assessment can be challenging to apply in practice and would become more common under the proposed amendments.

BC35. In the proposed Update, the Board proposed replacing the current correlation assessment with a fair value assessment. That fair value assessment would have required that an entity assess how each underlying affects the fair value of the contract and determine which underlying would have the largest expected effect on changes in the fair value of the contract (or an embedded feature). The underlying that had the largest expected effect on fair value would be considered the predominant underlying, and whether the predominant underlying qualifies for the scope exception in paragraph 815-10-15-59 would determine the accounting for the contract or embedded feature. The Board expected that the proposed fair value assessment would have been more operable than the current correlation assessment and would have resulted in more consistent application of the guidance.

BC36. However, comment letter respondents expressed concerns about the costs and complexity of performing the proposed fair value assessment, especially because more instruments would be subject to the predominant assessment based on the amendments as proposed. Furthermore, comment letter respondents noted that the proposed fair value assessment would pose many of the same challenges that exist under the current correlation assessment. Specifically, the predominant characteristics assessment would continue to be difficult for an entity to apply in practice when a contract has one

underlying that depends on another underlying. For example, in the case of a bond that is contingently puttable upon the occurrence of an initial public offering, the contract has one underlying that depends on another underlying because it involves exercising a contingent feature or “trigger” for cash flows or settlements under the contract to occur.

BC37. In response to those concerns, the Board considered alternatives to revise the proposed fair value assessment. For example, the Board considered an alternative approach that would create a principle for assessing predominance. Under that alternative approach, an underlying would have been considered the predominant underlying if it had the largest expected effect on the value of the contract or an embedded feature. This alternative approach was intended to provide entities with flexibility in evaluating predominance based on the nature of the contract or embedded feature and would not have required a detailed fair value assessment. However, the Board rejected this alternative approach because it was concerned that the approach would have created diversity in application and narrowed the application of the scope exception in paragraph 815-10-15-59(e) in a way that was not consistent with the Board’s intent.

BC38. In light of comment letter feedback and other changes made in redeliberations (particularly related to the scope of the scope exception), the Board decided to retain the current correlation assessment. Because the Board decided that contracts on an entity’s own equity in Subtopic 815-40 and call options and put options on debt instruments do not qualify for the scope exception, the Board expects that the correlation assessment will apply to a limited number of contracts and embedded features. The Board observed that the current correlation assessment is applied in practice to certain contracts. Therefore, the Board determined that the current correlation assessment can be applied to contracts and embedded features that have an underlying that qualifies for the scope exception in paragraph 815-10-15-59(e). In addition, the Board considered that if this assessment were changed, entities that apply the current correlation assessment would have incurred additional costs to transition to a new method to assess predominance. Therefore, the Board determined that the costs of amending the current predominant characteristics assessment outweigh the benefits and decided to retain the current correlation assessment.

Effective Date and Transition

BC39. The amendments in this Update are effective for all entities for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods. This effective date is consistent with comment letter feedback that an effective date of at least one year from the issuance date of a final Update would be sufficient and is based on the Board's expectation that the implementation costs of applying the guidance likely will not be significant. Noting that entities other than public business entities also will benefit from the guidance and will have an approximately two-year time period between the issuance of this Update and when they are required to apply the guidance, the Board determined that the effective date should be the same for all entities. Early adoption is permitted. If early adoption is elected in an interim reporting period, the amendments should be applied as of the beginning of the annual reporting period that includes that interim reporting period.

BC40. The Board decided to allow an entity to apply the amendments for Issue 1 in this Update either (a) prospectively to new contracts entered into on or after the date of adoption or (b) on a modified retrospective basis through a cumulative-effect adjustment to the opening balance of retained earnings as of the beginning of the annual reporting period of adoption for contracts that exist as of the beginning of the annual reporting period of adoption. The Board notes that the transition method that an entity elects for Issue 1 may be different from the transition method that it elects for Issue 2.

BC41. For entities that apply the amendments in this Update on a modified retrospective basis, the Board decided to provide, upon adoption, an instrument-by-instrument option to elect to measure certain contracts in their entirety at fair value with changes in fair value recognized in earnings. A contract that is within the scope of paragraph 825-10-15-4 that is no longer accounted for as a derivative because of applying the amendments in this Update is eligible for this option. The option is intended to permit entities that otherwise would have applied the fair value option at contract inception to apply the fair value option upon adoption. For financial liabilities, an entity should present separately in other comprehensive income the portion of the total change in the fair value of the liability that results from a change in the instrument-specific credit risk. Furthermore, the Board decided to provide, upon adoption, an instrument-by-instrument option to stop applying the fair

value option for contracts that contain embedded features that otherwise would have been bifurcated but are no longer accounted for as derivatives because they qualify for the scope exception.

BC42. For those instruments for which an entity elects or stops applying the fair value option, the adoption date effects of complying with the amendments in this Update should be reported as a cumulative-effect adjustment in the opening balance of retained earnings (or other appropriate components of equity or net assets) as of the beginning of the annual reporting period in which the amendments are adopted.

BC43. The Board decided to require certain disclosures in accordance with Topic 250, Accounting Changes and Error Corrections. All entities should disclose in the period of adoption the nature of and reasons for the change in accounting principle. Additionally, an entity that elects the modified retrospective transition method is required to disclose (a) the cumulative effect of the change in retained earnings or other components of equity or net assets as of the beginning of the annual reporting period of adoption and (b) a description of the financial statement line items affected. An entity that issues interim financial statements should provide the required disclosures in the financial statements of both the interim reporting period and annual reporting period of adoption.

Issue 2: Scope Clarification for Share-Based Noncash Consideration from a Customer in a Revenue Contract

Background Information

BC44. In 2023, the FASB staff received a technical inquiry about how an entity should account for warrants granted by a customer as consideration for a revenue contract when the warrants vest upon the entity's satisfaction of its performance obligation. This question was later raised at the November 10, 2023 public roundtable meeting on FASB's Post-Implementation Review (PIR) of Topic 606.

BC45. Some stakeholders noted that, in their view, there is a lack of clarity about which guidance an entity should apply to recognize share-based noncash consideration, such as warrants or shares, received from a customer

that is consideration for the transfer of goods or services. As a result, there are differing interpretations in practice about whether Topic 815 or Topic 321 should be applied to share-based noncash consideration that has not yet been earned and recognized in a revenue contract. For example, if an entity receives share-based noncash consideration from a customer (the grantor) when providing goods or services and that share-based noncash consideration is contingent on the satisfaction of a performance obligation, some stakeholders indicated that it is unclear whether that share-based noncash consideration (a) should be recognized at contract inception as a derivative asset under Topic 815 or an equity security under Topic 321 or (b) should not be recognized until the entity satisfies its performance obligation under Topic 606.

BC46. In response to that feedback, the Board decided to clarify the accounting by an entity that enters into contracts to receive share-based noncash consideration from a customer for the transfer of goods or services. The Board included this clarification, which addresses the applicability of derivative accounting in Topic 815, in this Update because it aligns with the objective of this Update to reduce the cost and complexity of evaluating whether certain contracts are subject to derivative accounting.

Benefits and Costs

BC47. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC48. The amendments in this Update clarify the applicability of Topic 606 to share-based noncash consideration from a customer for the transfer of goods or services. This clarification is expected to reduce diversity in practice and enhance consistency in the accounting for revenue contracts with different

forms of consideration. Accordingly, the Board expects that investors will receive more consistent information on revenue contracts with different forms of consideration and more comparable information across different entities.

BC49. The amendments in this Update are expected to reduce financial reporting compliance costs by simplifying the accounting for share-based noncash consideration from a customer for the transfer of goods or services. Although some entities may incur one-time transition costs, the Board expects that those costs will not be significant. In addition, the Board expects that entities that currently apply the guidance in other Topics, such as Topic 815 or Topic 321, to account for share-based noncash consideration from a customer for the transfer of goods or services may experience a reduction in recurring costs. This is because those entities will no longer need to apply derivative or equity security accounting to share-based noncash consideration each reporting period until their right to receive or retain the share-based noncash consideration is unconditional under Topic 606.

BC50. Overall, the Board expects that the amendments in this Update will provide investors with more relevant, consistent, and comparable information while reducing costs for preparers and auditors. Comment letter respondents generally agreed that clarifying the application of the guidance would reduce complexity and diversity in practice. Therefore, the Board concluded that the expected benefits of the amendments justify the expected costs.

Basis for Conclusions

Accounting under Topic 606

BC51. Some stakeholders asserted that the increase in revenue contracts with share-based noncash consideration (such as warrants or shares) from customers has resulted in a growing need to clarify the accounting for those revenue contracts. The Board's intent has been for entities to apply Topic 606 to account for share-based noncash consideration from customers for the transfer of goods or services. Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, added the guidance in paragraph 505-50-05-2A to clarify that an entity should apply Topic 606 to a share-based payment in a revenue contract with a customer. Subsequently, Subtopic 505-50, *Equity—Equity-Based Payments to Non-Employees*, including paragraph 505-50-05-2A, was superseded by Accounting Standards Update No. 2018-07, *Compensation—Stock Compensation (Topic 718)*:

Improvements to Nonemployee Share-Based Payment Accounting. Nevertheless, the Board's intent for an entity to apply Topic 606 to account for share-based noncash consideration from a customer in a revenue contract did not change.

BC52. The Board acknowledges that the current guidance in Topic 606 is not as explicit as the guidance in superseded paragraph 505-50-05-2A. The lack of clear guidance has contributed to diversity about which guidance (that is, Topic 606 or other Topics, such as Topic 815 and Topic 321) should be applied.

BC53. Therefore, the Board decided to clarify in Topic 606 that an entity should apply the guidance in Topic 606, including the guidance on noncash consideration in paragraphs 606-10-32-21 through 32-24, to a contract with share-based noncash consideration from a customer for the transfer of goods or services before the guidance in other Topics (including Topic 815 and Topic 321) is applied.

BC54. Comment letter respondents generally supported the Board's additional clarification. They noted that the clarification would align with the current revenue recognition principles, better reflect the economics of these types of transactions, and provide investors with decision-useful information. Additionally, comment letter respondents expected the clarification to simplify accounting assessments, reduce diversity in practice, and create consistent guidance for revenue contracts with different forms of consideration.

BC55. The Board decided to use the term *share-based noncash consideration* to describe noncash consideration in the form of a share-based payment received from a customer for the transfer of goods or services. That term is consistent with the Board's intent, is well understood by stakeholders, and enhances consistency with the current noncash consideration guidance in Topic 606.

BC56. The amendments in this Update require that share-based noncash consideration from a customer for the transfer of goods or services in a revenue contract be subject to Topic 606 unless and until an entity's right to receive or retain the share-based noncash consideration is unconditional under Topic 606.

BC57. The Board's decision to account for share-based noncash consideration from a customer under Topic 606 until the right to receive or retain it is unconditional under Topic 606 is consistent with how a receivable (which is an entity's right to consideration that is unconditional) is defined in paragraph 606-10-45-4. This is an asset-focused approach because it emphasizes that the share-based noncash consideration received from a customer should be accounted for in a manner that is consistent with how other assets that result from revenue transactions are accounted for. Therefore, this approach is consistent with Chapter 5, *Recognition and Derecognition*, of FASB Concepts Statement No. 8, *Conceptual Framework for Financial Reporting*. Under this approach, share-based noncash consideration from a customer in a revenue contract is expected to be accounted for in the same periods and in a similar manner to cash consideration and other forms of noncash consideration. For example, under the amendments in this Update, noncontingent or nonrefundable share-based noncash consideration received upfront as a prepayment for the transfer of goods or services should be accounted for in a similar manner as a prepayment in cash. The amendments do not affect how revenue should be accounted for under Topic 606.

BC58. The Board decided on the asset-focused approach in paragraphs BC56 and BC57 in response to feedback from some comment letter respondents about the amendments in the proposed Update, which would have required recognition of share-based noncash consideration from a customer in a revenue contract upon the satisfaction of a performance obligation. Those respondents questioned whether the proposed amendments would be appropriate in more complex arrangements in which the share-based noncash consideration vests or is exercisable upon a contingent event other than the satisfaction of a performance obligation, such as achieving a specified milestone (for example, selling a certain number of units or completing performance in a certain period of time). Some respondents observed that if share-based noncash consideration was recognized based on the satisfaction of a performance obligation, it may lead to the share-based noncash consideration being accounted for under other Topics before the variability related to the transfer of goods or services is fully resolved under Topic 606. Compared with the proposed amendments, the asset-focused approach in the amendments in this Update better interacts with the current guidance in Topic 606, including the variable consideration guidance and the guidance on recognizing a contract asset, and better addresses more complex situations. The Board also added a new example to help stakeholders better understand

the Board's intent and provide clarity to support consistent application.

BC59. The Board acknowledges that there could be situations in which share-based noncash consideration vests or is exercisable upon multiple contingent events, some of which are related to an entity's performance obligation (or a specific outcome of the entity's performance) and others that are not. To address those situations, the Board decided that when assessing whether an entity's right to receive or retain share-based noncash consideration from a customer in a revenue contract is unconditional under Topic 606, the entity should evaluate only contract terms that relate to its performance obligations (or a specific outcome of the entity's performance) within the scope of Topic 606. Once those performance-related contingencies have been resolved, an entity's right to receive or retain share-based noncash consideration from a customer is unconditional (other than by the passage of time) under Topic 606, and the entity should begin accounting for the share-based noncash consideration under other Topics. A contingent event that is unrelated to an entity's performance obligation (or a specific outcome of the entity's performance) will not prevent the entity from accounting for share-based noncash consideration under other Topics.

BC60. The Board acknowledges that judgment may be needed in assessing whether a contingent event relates to an entity's performance obligation (or a specific outcome of the entity's performance) under Topic 606. However, the Board expects that this clarification will be helpful and operable for stakeholders because it identifies the types of contingent events that need to be resolved before share-based noncash consideration can be accounted for under other Topics and because it provides a principle for entities to assess how a contingent event should be evaluated. The Board also observes that because the assessment of whether an entity's right to receive or retain share-based noncash consideration is unconditional under Topic 606 is based on contingencies that are related to the entity's performance (or a specific outcome of the entity's performance) under the contract terms, it is generally consistent with the definition of *vest* in the Master Glossary (because, for example, market conditions do not affect vesting). As a result, this approach is expected to improve the symmetry with the grantor's accounting under Topic 718, Compensation—Stock Compensation.

BC61. Some comment letter respondents questioned how the probability of vesting of share-based noncash consideration should be considered under Topic 606. Those comment letter respondents asked whether the probability of

vesting should be included in the estimated fair value of the share-based consideration at contract inception or whether the probability of vesting should instead be incorporated into the assessment of variable consideration. The Board observed that the current guidance in Topic 606, specifically the guidance on variable consideration and noncash consideration, indicates that when the probability of vesting of share-based noncash consideration is related to an entity's performance obligation (or a specific outcome of the entity's performance) under Topic 606, it should be included in the assessment of variable consideration. This treatment also is consistent with how a grantor measures a share-based payment award at grant date under Topic 718.

BC62. The Board concluded that applying an asset-focused approach to account for share-based noncash consideration from a customer in a revenue contract under Topic 606 aligns with the Board's intent, is consistent with the guidance in Topic 606, and is expected to result in a more consistent accounting for revenue contracts with different forms of consideration. In addition, the amendments will improve symmetry with the grantor's accounting under Topic 718 and will not affect convergence between Topic 606 and IFRS 15, *Revenue from Contracts with Customers*.

BC63. The Board considered an alternative view held by some stakeholders that share-based noncash consideration from a customer in a revenue contract should be recognized at contract inception under Topic 815 or Topic 321 because it meets the definition of *financial instrument* in the Master Glossary. However, the Board observed that the definition of *financial instrument* states that some financial instruments may not be recognized because they fail to meet some other criterion for recognition. Furthermore, the Board observed that this alternative view could result in consideration and revenue in a revenue contract with share-based noncash consideration from a customer being recognized in different periods and in a different manner than a revenue contract with cash consideration. The Board questioned the decision usefulness of this differential effect on entities' financial statements.

Consequential Amendments

BC64. Noting that the guidance in Subtopic 610-20, Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets, refers to the revenue recognition principles in Topic 606, including the guidance on recognition and measurement, the Board included a question in the proposed

Update about whether a clarification similar to that in paragraph 606-10-15-3A should be added to address the applicability of Subtopic 610-20 and other Topics to share-based noncash consideration from a noncustomer for the transfer of nonfinancial assets. Generally, comment letter respondents agreed that a similar scope clarification should be provided in Subtopic 610-20 and did not identify any unintended consequences of providing that clarification. Considering the existing alignment in the accounting for similar transactions between Subtopic 610-20 and Topic 606 and comment letter respondents' general support, the Board decided to include this scope clarification.

BC65. In addition, the Board decided to clarify in Topic 815 and Topic 321 that the guidance in those Topics does not apply to (a) share-based noncash consideration from a customer for the transfer of goods or services before Topic 606 is applied or (b) share-based noncash consideration from a counterparty for the transfer of nonfinancial assets or in substance nonfinancial assets before Subtopic 610-20 is applied. Comment letter respondents generally supported the Board's decision and observed that Topic 815 and Topic 321 are the most common Topics that interact with Topic 606 and Subtopic 610-20 and the clarification added in those Topics would help enhance clarity.

BC66. Some comment letter respondents observed that other Topics, such as Topic 323, Investments—Equity Method and Joint Ventures, Topic 805, Business Combinations, and Topic 810, Consolidation, also could apply to share-based noncash consideration received from a customer in a revenue contract. They suggested that the Board add consequential amendments to those Topics similar to the clarifications in Topic 815 and Topic 321. The Board acknowledges that there are other Topics besides Topic 815 and Topic 321 that may interact with Topic 606 or Subtopic 610-20 in accounting for share-based noncash consideration from a customer for the transfer of goods or services or to share-based noncash consideration from a counterparty for the transfer of nonfinancial assets or in substance nonfinancial assets. However, observing that Topic 815 and Topic 321 are likely to be the most common Topics that interact with Topic 606 and Subtopic 610-20, the Board concluded that it is unnecessary to make consequential amendments to all other Topics that may relate to the accounting for share-based noncash consideration.

Other Feedback

BC67. Some stakeholders, including comment letter respondents, requested that the Board address certain measurement issues related to share-based noncash consideration from a customer in a revenue contract, including measurement of the estimated fair value of share-based noncash consideration at contract inception, subsequent measurement of contract assets that are related to share-based noncash consideration (such as the impairment of contract assets), and the initial measurement of share-based noncash consideration once it is accounted for under other Topics.

BC68. The Board acknowledges those stakeholders' feedback that the current guidance may not be sufficient to address those measurement issues. However, the Board observes that those measurement issues are not unique to revenue contracts with share-based noncash consideration from a customer. Additionally, those issues are not a result of the amendments in this Update.

BC69. Furthermore, the Board notes that it addressed measuring the estimated fair value of noncash consideration in the basis for conclusions (paragraph BC39) of Accounting Standards Update No. 2016-12, *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*. That paragraph explains why the Board decided not to specify how the fair value of noncash consideration should be measured. Paragraph BC40 of that Update addresses the subsequent accounting under other Topics for changes in fair value of noncash consideration after contract inception. That paragraph states that if the guidance in other Topics related to the form of the noncash consideration requires that asset to be measured at fair value, an entity should recognize a gain or loss (outside of revenue) upon receipt of the asset if the fair value of the noncash consideration has increased or decreased since contract inception. That paragraph further explains that for situations in which an entity performs by transferring goods or services to a customer before the customer pays the noncash consideration or before payment of the noncash consideration is due, the entity is required to present the noncash consideration as a contract asset, excluding any amounts presented as a receivable and assess the contract asset or receivable for impairment. The Board did not receive any new information that would cause the Board to revisit its decision in that Update.

BC70. Because those measurement issues relate to all forms of noncash consideration (not just share-based noncash consideration) and are generally broader than the scope of this project, the Board decided not to further address those issues in this project.

BC71. Some comment letter respondents suggested that if the Board decides not to address the subsequent measurement of contract assets related to share-based noncash consideration, it could consider requiring additional disclosures about changes in the fair value of share-based noncash consideration that is accounted for under Topic 606. The Board observes that requiring that information to be disclosed may be as complex and costly as accounting for the share-based noncash consideration as a financial instrument at contract inception. The Board also views that the current disclosures in Topic 606 are sufficient to provide investors with relevant information. Therefore, the Board decided not to add any new disclosure requirements.

BC72. The Board also decided not to address the accounting for certain other economically similar contracts and arrangements raised by some stakeholders, such as (a) revenue contracts with noncash consideration in the form of crypto assets or in the form of other financial instruments or (b) purchase contracts with share-based noncash consideration received from vendors that are within the scope of Subtopic 705-20, Cost of Sales and Services—Accounting for Consideration Received from a Vendor. The Board concluded that those contracts and arrangements are not pervasive and are beyond the scope of this project.

Effective Date and Transition

BC73. The amendments in this Update are effective for all entities for annual reporting periods beginning after December 15, 2026, and interim reporting periods within those annual reporting periods. Early adoption is permitted. The Board decided to require the same effective date and permit early adoption for both Issue 1 and Issue 2 of this Update, because of the similar comment letter feedback it received (see paragraph BC39 for details). Furthermore, the Board clarified that if an entity early adopts the amendments of Issue 2, it should early adopt the amendments of Issue 1 at the same time.

BC74. The Board decided to allow an entity to apply the amendments of Issue 2 in this Update either (a) prospectively to new contracts entered into on or after the date of adoption, including modified contracts accounted for as separate contracts in accordance with paragraph 606-10-25-12, or (b) on a modified retrospective basis through a cumulative-effect adjustment to the opening balance of retained earnings as of the beginning of the annual reporting period of adoption for contracts that exist as of the beginning of the annual reporting period of adoption. The Board notes that the transition method that an entity elects for Issue 2 may be different from the transition method that it elects for Issue 1.

BC75. In response to the feedback from comment letter respondents, the Board decided to allow an option for prospective transition. Although most comment letter respondents agreed that the transition method in the proposed Update (paragraph 606-10-65-3(c)(2) of this Update) was clear and operable, some comment letter respondents noted that the proposed transition method may be costly or not operable for certain entities. To ease the potential complexity of adopting the amendments in this Update, the Board decided to provide a prospective transition option. Because the number of entities that have revenue contracts with share-based noncash consideration may be limited, the Board expects that providing transition options will not significantly affect the comparability of financial information provided to investors.

BC76. The Board decided to require certain transition disclosures in accordance with Topic 250, which were generally supported by comment letter respondents. All entities should disclose in the period of adoption the nature of and reasons for the change in accounting principle. Additionally, an entity that elects the modified retrospective transition method is required to disclose the cumulative effect of the change in retained earnings or other components of equity or net assets as of the beginning of the annual reporting period of adoption. An entity that issues interim financial statements should provide the required disclosures in the financial statements of both the interim reporting period and annual reporting period of adoption.

Amendments to the GAAP Taxonomy

The amendments to the *FASB Accounting Standards Codification*[®] in this Accounting Standards Update require improvements to the GAAP Financial Reporting Taxonomy and SEC Reporting Taxonomy (collectively referred to as the “GAAP Taxonomy”). Those improvements, which will be incorporated into the proposed 2026 GAAP Taxonomy, are available through [GAAP Taxonomy Improvements](#) provided at www.fasb.org, and finalized as part of the annual release process.