

Early Impressions

FASB's Accounting Standards Update ASU 2026-01

Equity (Topic 505): Initial Measurement of Paid-in-Kind Dividends on Equity-Classified Preferred Stock



EXECUTIVE SUMMARY

On April 23, 2026, the Financial Accounting Standards Board (FASB) issued ASU 2026-01, introducing a single, standardized approach for the initial measurement of paid-in-kind (PIK) dividends on equity-classified preferred stock. This update addresses long-standing diversity in practice and improves comparability across entities.

Historically, U.S. Generally Accepted Accounting Principles (GAAP) did not provide explicit guidance in this area, resulting in varied approaches—ranging from fair value at declaration date to stated rates or effective debt-like interest methods. In some cases, entities also differentiated based on whether dividends were discretionary or nondiscretionary. This inconsistency reduced comparability and increased reliance on judgment.

The new guidance mandates measurement based on the stated PIK dividend rate in the preferred stock agreement for in-scope arrangements. This approach aligns accounting with the underlying economics, reflects prevailing market practice, and enhances operability. Certain arrangements, including those involving fixed monetary amounts settled in variable shares, remain outside the scope.

The amendments are effective for reporting periods beginning after December 15, 2026, with early adoption permitted.

In this *Early Impressions* publication, we highlight what has changed, why it matters, and the key considerations for finance leaders.

We hope you find this publication valuable and welcome further discussion.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective



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BACKGROUND

Why PIK dividends matter

Preferred stock is a hybrid instrument that combines debt and equity-like features, typically providing contractual dividends, priority in liquidation, and, in some cases, conversion or redemption rights. Dividends may be paid in cash or settled in kind through the issuance of additional shares or increases in liquidation preference (PIK dividends).

PIK dividends are widely used across private equity-backed structures and growth-stage companies where investors seek predictable returns with downside protection. While these instruments enable issuers to defer cash outflows without compromising investor economics, their accounting has historically lacked consistency, resulting in diverse practices and reduced comparability.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

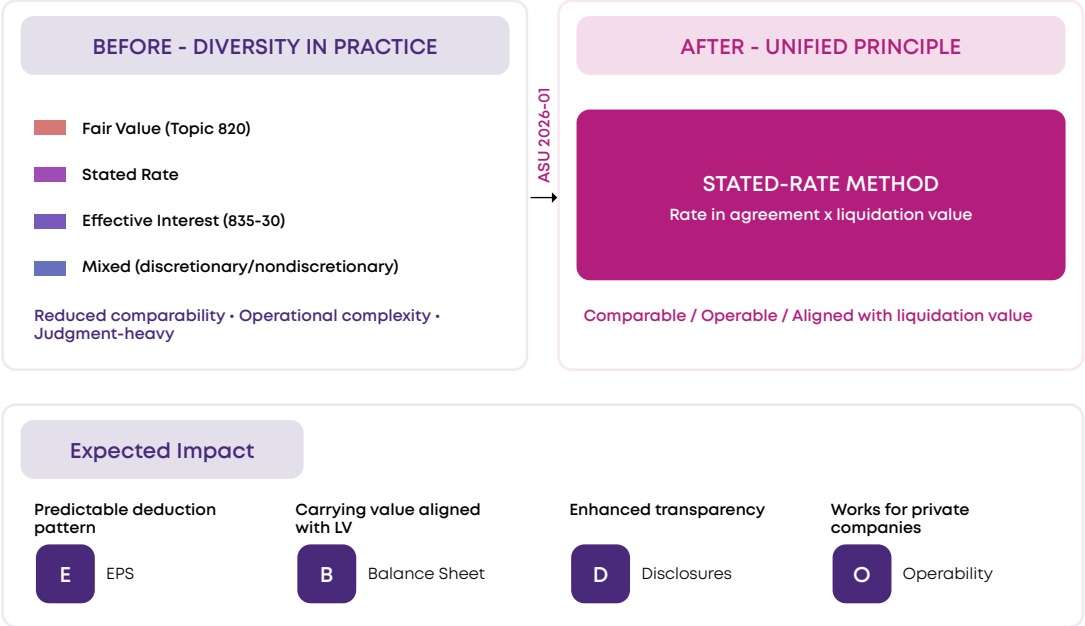
The diversity-in-practice problem

Prior to this ASU, U.S. GAAP did not prescribe a specific approach for the initial measurement of PIK dividends on equity-classified preferred stock. In the absence of clear guidance, entities relied on analogies in GAAP, resulting in inconsistent methods applied in practice— fair value, stated rate, effective interest, or combinations thereof (often differentiated between discretionary and nondiscretionary dividends).

- **Fair value method** — measuring the PIK dividend at the fair value of the additional preferred shares issued (or of the increase in liquidation value) as of the dividend declaration or issuance date, drawing on Topic 820, Fair Value Measurement.
- **Stated-rate method** — measuring the PIK dividend using the PIK dividend rate stated in the preferred stock agreement applied to the liquidation value (or liquidation preference) of the outstanding preferred stock.
- **Effective interest rate method** — applying a constant-yield approach analogous to the guidance in Subtopic 835-30, Interest — Imputation of Interest, which gradually accretes the preferred stock to its ultimate redemption or liquidation value.
- **Mixed methods** — applying fair value to discretionary PIK dividends (i.e., those declared at the board's option) and the stated rate or effective interest method to nondiscretionary PIK dividends (i.e., those that accrue automatically under the contract).

These differences were not merely technical. Measurement outcomes varied significantly depending on the method applied, particularly when preferred stock traded at a premium or discount to its liquidation value, or when assumptions about redemption timing were embedded. As a result, key metrics—including earnings per share, net income available to common shareholders, and capital structure indicators—lacked comparability, prompting calls for standard-setting intervention.

Pre-ASU Diversity vs. ASU 2026-01 Unified Approach



Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective



ASU 2026-01: SUMMARY AT A GLANCE

ASU 2026-01 is narrowly scoped, introducing a single measurement principle for PIK dividends on equity-classified preferred stock. The infographic below highlights the key dimensions of the amendment.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

Objective

Eliminate diversity in practice in the initial measurement of PIK dividends on equity-classified preferred stock by prescribing a single, operable measurement basis.

Scope

Applies to PIK dividends on **equity-classified preferred stock** (including temporary equity) when the PIK feature varies based on additional shares issued or an increase in liquidation value (or liquidation preference).

Measurement principle

PIK dividends within scope are **initially measured using the PIK dividend rate stated in the preferred stock agreement**, applied to the liquidation value of the outstanding preferred stock.

Scope Exclusions

Variable shares with fixed monetary amount; deemed dividends; dividends payable in a different class of equity (e.g., common stock); PIK dividends on liability-classified preferred stock.

Transition

Entities may apply (1) the prospective method to PIK dividends declared after the effective date, or (2) the modified retrospective method with a cumulative-effect adjustment to opening retained earnings.

Effective Date

All entities: annual periods beginning after December 15, 2026, and interim periods within those annual periods. Early adoption permitted.

In practical terms, ASU requires entities to debit retained earnings (or an equivalent equity account) and credit the preferred stock carrying amount (or the additional paid-in capital relating to the preferred stock) for the stated-rate PIK dividend amount when the dividend is declared. For temporary-equity classified preferred stock, the credit is reflected in the mezzanine section consistent with SEC Staff Announcement 480-10-S99-3A (classification and measurement of redeemable securities).

Journal Entry for PIK Dividend Declaration

PIK Dividend = Stated PIK Rate × Accreted Liquidation Value

Dr Debit

Retained Earnings
(or Additional Paid-in Capital
if deficit exists)

XX,XXX

=

Cr Credit

Preferred Stock
(or related Additional Paid-in
Capital)

XX,XXX

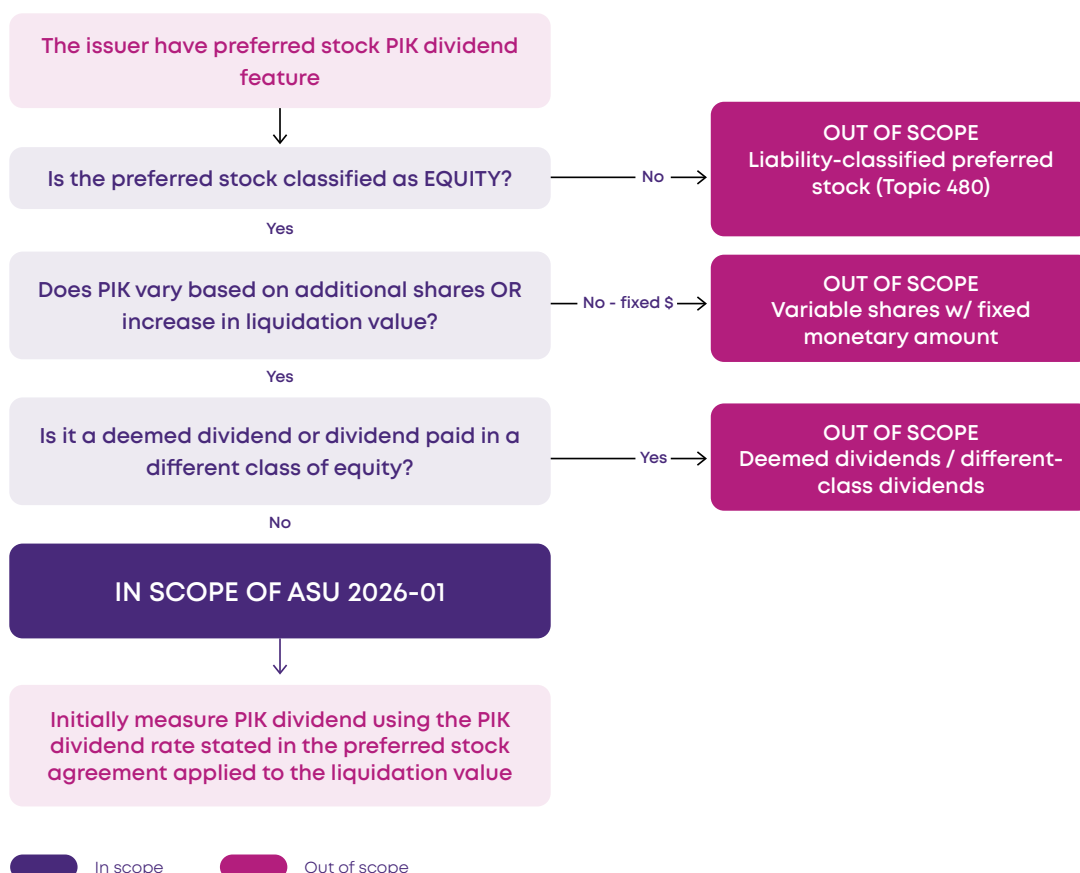
For temporary-equity classified preferred stock, the credit is recorded in the mezzanine section (per 480-10-S99-3A)



SCOPE APPLICABILITY

The amendments add new scope paragraphs to Subtopic 505-10, Equity — Overall, that identify the instruments and arrangements to which the measurement principle applies.

Is ASU 2026-01 Applicable? — Scope Decision Flow



Scope of application

The ASU applies to PIK dividends on preferred stock where two conditions are met:

- **The preferred stock is classified as equity** — that is, classified in permanent equity or as temporary (mezzanine) equity under SEC Staff Announcement 480-10-S99-3A. Preferred stock classified as a liability under Topic 480, *Distinguishing Liabilities from Equity*, is outside the scope.
- **The PIK dividend varies based on either (a) the number of additional preferred shares issued, or (b) the increase in the liquidation value (or liquidation preference) of the outstanding preferred stock.** In other words, the amount the issuer owes under the PIK feature is denominated in additional preferred shares or in liquidation value, rather than in a fixed dollar amount.

The scope includes both discretionary and nondiscretionary PIK dividends. Under ASU 2026-01, a single stated-rate measurement approach applies consistently, eliminating the need to differentiate based on the nature of the dividend.

Scope exclusions

The Board deliberately excluded four categories of arrangements from the measurement principle because their economics differ from the in-scope PIK dividends or because other guidance already addresses them:

Excluded arrangement	Reason for exclusion / Applicable guidance
Variable-share dividends with a fixed monetary amount	- Where the PIK dividend is settled in a variable number of shares whose aggregate value is fixed in dollars (e.g., “dividend of \$1 million paid in a variable number of preferred shares based on fair value on the declaration date”), the economics resemble a monetary obligation rather than a share-denominated obligation. - Entities should continue to apply existing guidance (including, where relevant, the share-settled obligations guidance in Topic 480).
Deemed dividends	Deemed dividends (e.g., amounts arising from beneficial conversion features, modifications to preferred stock terms, or increases in fair value on redemption) are not contractual PIK dividends declared on outstanding preferred stock and are governed by separate guidance.
Dividends payable in a different equity class	- PIK dividends that are satisfied by issuing a different class of equity (for example, dividends paid on preferred stock by issuing common stock, or dividends paid on a senior class by issuing a junior class) are outside the scope. - These are typically measured at the fair value of the shares issued at declaration or issuance, consistent with existing practice for non-reciprocal equity transactions.
PIK dividends on liability-classified preferred stock	- Preferred stock classified as a liability under Topic 480 is accounted for under the interest-accretion model, and PIK dividends on such instruments are recognized as interest expense (not dividends). - The measurement principle in ASU 2026-01 does not apply.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

Illustrative scope examples

Illustrative Scope Example 1 — In scope

Fact pattern: Company P issues 100,000 shares of Series A preferred stock with a liquidation value of \$100 per share. The preferred stock is classified as permanent equity. The agreement provides that the board may, at its option, declare dividends of 8% per annum, payable in additional shares of Series A preferred stock.

Analysis: The preferred stock is equity-classified, and the PIK dividend varies with the number of additional preferred shares issued. The arrangement is within the scope of the ASU, and dividends declared on or after the effective date must be initially measured using the 8% stated rate applied to the liquidation value of the outstanding preferred stock on the declaration date.

Illustrative Scope Example 2 — Out of scope (variable shares, fixed amount)

Fact pattern: Company Q issues Series B preferred stock (equity-classified) with a provision stating that the issuer will pay an annual dividend of \$5 million in additional Series B shares, with the number of shares determined based on the fair value of the Series B shares on each declaration date.

Analysis: The dividend amount is fixed (\$5 million) and is settled in a variable number of shares. The arrangement does not meet the in-scope condition that the PIK dividend varies based on additional shares or on an increase in liquidation value. Accordingly, it is outside the scope of the ASU and should continue to be evaluated under existing guidance (potentially Topic 480 for share-settled obligations).



Practical Insight

- Evaluating scope is a two-step exercise. First, confirm that the preferred stock is classified as equity (permanent equity or temporary equity) not as a liability. Second, determine whether the PIK dividend is denominated in additional preferred shares or in an increase in liquidation value (in scope) or in a fixed dollar amount satisfied by a variable number of shares (out of scope).
- Entities should not assume by analogy that the measurement principle extends to deemed dividends, beneficial conversion features, or modifications of preferred stock terms. Those arrangements remain subject to their existing, separate guidance.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

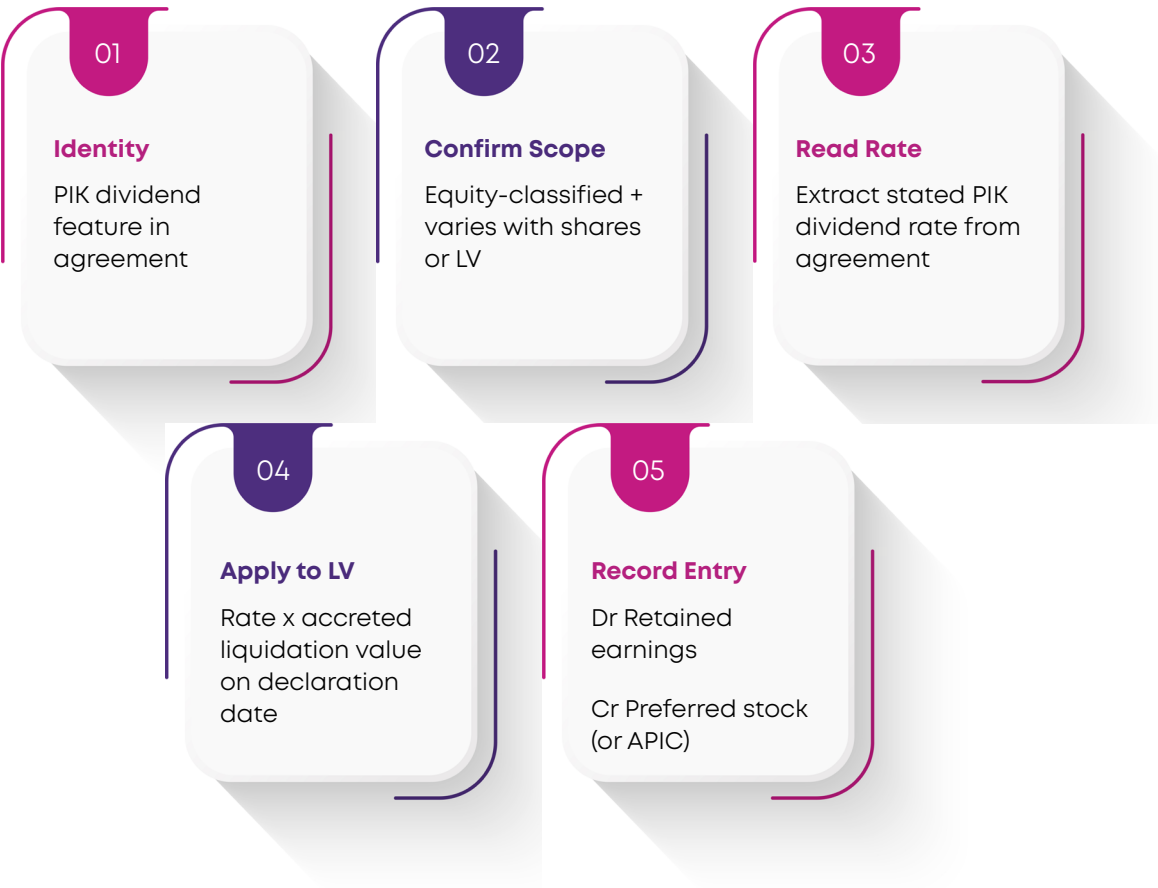
Effective Date and Transition

Uniquis Perspective

KEY HIGHLIGHTS OF THE AMENDMENT

This section walks through the substantive requirements of ASU 2026-01. The amendments to the Accounting Standards Codification (ASC) are concise: they add two new scope paragraphs (ASC 505-10-15-3 and 505-10-15-4) and one measurement paragraph (ASC 505-10-30-1), plus transition guidance in ASC 505-10-65-1. The impact, however, reaches every issuer of equity-classified preferred stock with a PIK dividend feature.

Applying the Stated-Rate Measurement — 5-Step Workflow



Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

A The core measurement principle

Paragraph 505-10-30-1 states that PIK dividends on preferred stock issued to preferred shareholders shall be initially measured based on the PIK dividend rate stated in the preferred stock agreement. In operational terms, this means:

- The measurement basis is the contractual stated rate, not a market-derived rate, not a fair value, and not an imputed effective rate.
- The rate is applied to the liquidation value (or liquidation preference) of the outstanding preferred stock as of the declaration date. Where liquidation value accretes over time (because prior PIK dividends have already increased it), the rate is applied to the current, accreted liquidation value.
- The resulting amount is recorded in retained earnings (or, if a retained earnings deficit exists, to additional paid-in capital or an equivalent equity account, consistent with existing U.S. GAAP and SEC staff practice) and credited to the preferred stock carrying amount (or to additional paid-in capital related to the preferred stock, depending on the entity's presentation policies).
- For preferred stock classified as temporary equity, the credit is recorded in the mezzanine section, following the classification and measurement guidance in 480-10-S99-3A.

The principle is straightforward: the stated rate is the primary input, the liquidation value is the base, and the resulting measurement flows through equity without a separate income statement effect (except to the extent that it reduces net income available to common shareholders for EPS purposes).

B The two conditions that bring an instrument into scope

New paragraph 505-10-15-3 sets out the entry test: the measurement principle applies only if both (a) the preferred stock is equity-classified, and (b) the PIK dividend varies based on additional preferred shares issued or on an increase in liquidation value. Paragraph 505-10-15-4 clarifies that the principle does not apply to:

- PIK dividends on preferred stock are classified as a liability under Topic 480.
- PIK dividends satisfied by issuing a variable number of shares equal in aggregate fair value to a fixed monetary amount.
- Deemed dividends (including increases in the fair value of redeemable preferred stock accounted for under SEC Staff Announcement 480-10-S99-3A).
- Dividends on preferred stock that are payable in a different class of equity (e.g., common stock).

Each exclusion identifies a transaction whose economics or classification differ in ways that justify separate treatment. The Board's conclusion — supported in the Basis for Conclusions — is that forcing a one-size-fits-all measurement principle over these arrangements would introduce rather than reduce complexity.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

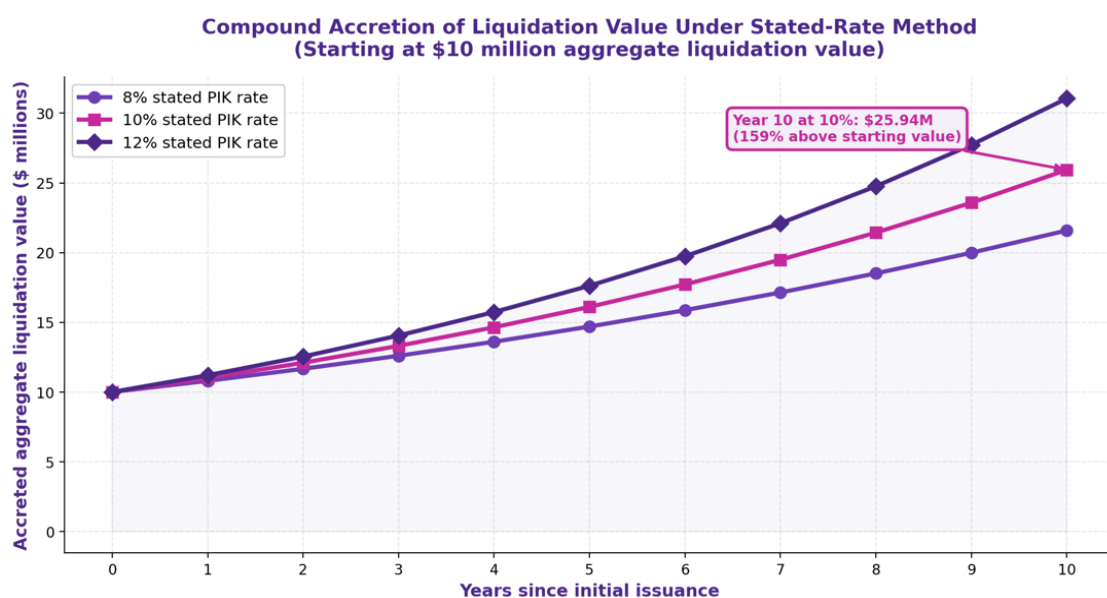
Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

ASU 2026-01 anchors the measurement of PIK dividends to the liquidation value of preferred stock, aligning accounting with how investors assess economic exposure and track returns. This ensures the resulting measurement is intuitive, comparable, and directly reconcilable to market-based metrics.

Given this approach, entities must maintain accurate tracking of liquidation value as it accretes over time. Each PIK dividend increases the base for future calculations, creating a compounding effect that should be reflected in systems and controls.



Implementation Matter

Entities should carefully review their preferred stock agreements to identify:

- (i) the stated PIK dividend rate (including whether it is fixed or floating);
- (ii) the base to which the rate is applied (per-share liquidation value, aggregate liquidation value, or an alternative formulation);
- (iii) the frequency of compounding and declaration;
- (iv) whether the PIK dividend is discretionary or nondiscretionary; and
- (v) whether the dividend is satisfied by additional shares or by an increase in liquidation value.

Each element drives the measurement outcome and, in many cases, the mechanics of tracking the preferred stock over its life. Entities should document their contractual review in a reusable accounting memo.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

Comprehensive Example — Multi-period PIK dividend measurement

Fact pattern: Company X issues 1,000 shares of Series A preferred stock at \$1,000 per share on January 1, 20X7 (aggregate liquidation value of \$1,000,000). The preferred stock is classified as permanent equity, is not redeemable, and bears a stated PIK dividend rate of 10% per annum. Dividends are nondiscretionary, accrued annually on December 31 and are satisfied by increasing the per-share liquidation value. Company X has retained sufficient earnings to cover the dividends. Company X adopts ASU 2026-01 prospectively on January 1, 20X7 (assume this is the effective date).

Period 1 — December 31, 20X7. PIK dividend = $\$1,000,000 \times 10\% = \$100,000$. Journal entry: Dr. Retained earnings \$100,000; Cr. Preferred stock \$100,000. Updated aggregate liquidation value = \$1,100,000 (\$1,100 per share).

Period 2 — December 31, 20X8. PIK dividend = $\$1,100,000 \times 10\% = \$110,000$. Journal entry: Dr. Retained earnings \$110,000; Cr. Preferred stock \$110,000. Updated aggregate liquidation value = \$1,210,000 (\$1,210 per share).

Period 3 — December 31, 20X9. PIK dividend = $\$1,210,000 \times 10\% = \$121,000$. Journal entry: Dr. Retained earnings \$121,000; Cr. Preferred stock \$121,000. Updated aggregate liquidation value = \$1,331,000 (\$1,331 per share).

Observations. The PIK dividend amount increases each period because the liquidation value base compounds. After three years, the aggregate liquidation value has grown by \$331,000 (33.1%) — a classic compound-interest profile. Each PIK dividend reduces net income available to common shareholders for EPS purposes by the full amount recorded in that period.



Practical Insight

The stated-rate approach introduces a “mechanical” cadence to PIK dividend accounting that is simpler than fair value or effective interest approaches, but it still demands disciplined tracking. Key items to embed in a PIK-dividend workbook: (i) the stated rate (and its floor/ceiling if applicable); (ii) the liquidation value roll-forward; (iii) the PIK dividend declarations calendar; (iv) the corresponding credits to preferred stock or additional paid-in capital; (v) the reconciliation to net income available to common shareholders; and (vi) the periodic comparison to redemption amount under 480-10-S99-3A (for temporary equity).

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

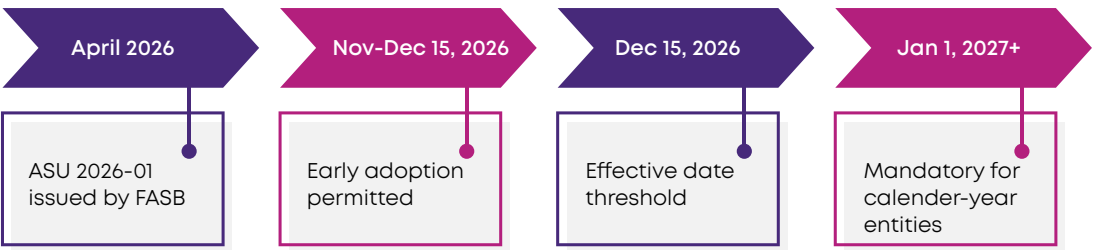
EFFECTIVE DATE AND TRANSITION

Effective date

The amendments are effective for annual periods beginning after December 15, 2026, including interim periods, with early adoption permitted.

Entities already applying a stated-rate approach are expected to transition with minimal impact. Those using fair value, effective interest, or hybrid methods should plan for a more structured transition.

Effective date & adoption timeline

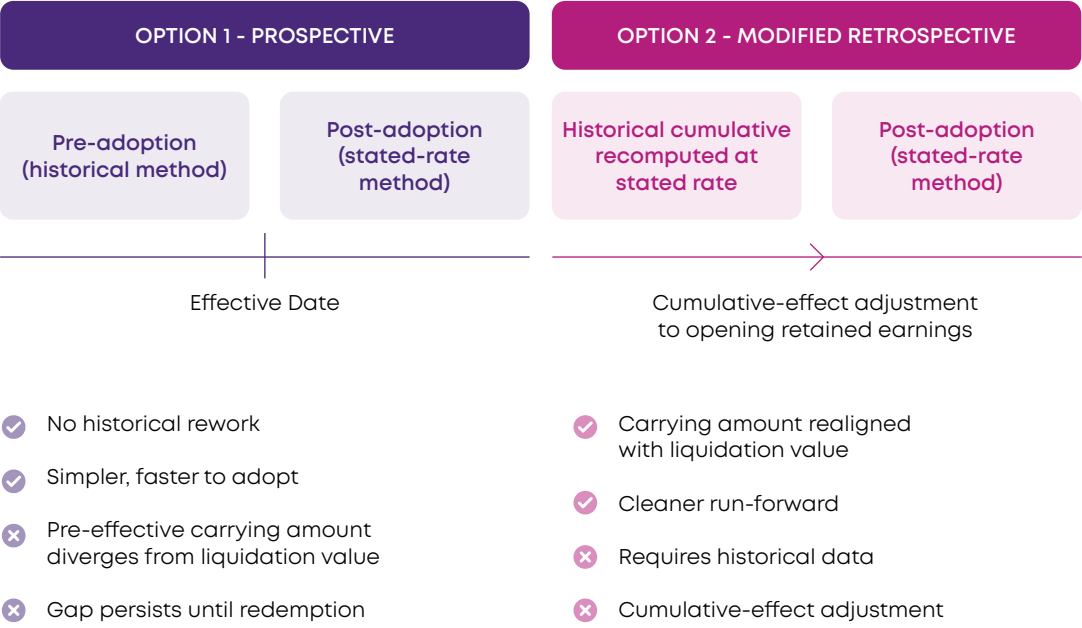


Applies to all entities (PBEs and non-PBEs) - annual periods beginning after December 15, 2026, and interim periods within those annual periods.

Transition methods

The ASU offers two transition options. An entity must select one method and apply it consistently across all PIK dividends within the scope of the ASU.

Transition methods - at a glance



Under the prospective method, the entity applies the measurement principle only to PIK dividends declared on or after the effective date (or early-adoption date). PIK dividends that were declared and recorded before the effective date are not remeasured. The carrying amount of the preferred stock as of the effective date (whether previously measured at fair value, the effective interest amount, or any other basis) is carried forward unchanged. This approach is simple and preserves prior-period comparability as historically reported.

Illustrative Transition Example 1 — Prospective method

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

Facts: Company A issued 10,000 shares of Series B preferred stock on January 1, 2024, with an initial aggregate liquidation value of \$10,000,000 and a stated PIK dividend rate of 9% per annum. Through December 31, 2026, Company A measured PIK dividends using a fair value approach, recognizing an average of \$950,000 per year (totaling \$2,850,000).

As of December 31, 20X6:

- Carrying amount of preferred stock: **\$12,850,000**
- Accreted liquidation value: **\$12,950,029** ($\$10,000,000 \times 1.09^3$)

Transition. Company A adopts the ASU prospectively on January 1, 2027. The existing carrying amount of \$12,850,000 is carried forward with **no cumulative-effect adjustment**.

First post-transition period. For the year ended December 31, 2027, the PIK dividend is measured using the stated rate applied to the accreted liquidation value:

- $\text{PIK dividend} = \$12,950,029 \times 9\% = \mathbf{\$1,165,503}$

Journal entry:

- Dr. Retained earnings \$1,165,503
- Cr. Preferred stock (or APIC) \$1,165,503

The accreted liquidation value increases to **\$14,115,532**.

Observation. Because no adjustment is recorded at transition, a **permanent difference** remains between the carrying amount of preferred stock (\$14,015,503) and its accreted liquidation value (\$14,115,532). Entities should continue to track both amounts, particularly for comparison with the redemption value, where applicable.

Option 2

Modified retrospective transition

Under the modified retrospective method, the entity applies the measurement principle as if it had always been in effect for outstanding preferred stock with an in-scope PIK dividend feature. The cumulative effect of transitioning from the entity's historical method (e.g., fair value or effective interest) to the stated-rate method is recorded as an adjustment to opening retained earnings (or other equivalent equity account) as of the beginning of the annual reporting period of adoption. Prior periods are not restated; only the carrying amount of the preferred stock and the opening retained earnings of the adoption period are adjusted.

Illustrative Transition Example 2 — Modified retrospective method

Facts: Same facts as Example 1. As of December 31, 2026, the carrying amount of the Series B preferred stock is **\$12,850,000** (measured using a fair value approach). Had the stated-rate method been applied since issuance, the carrying amount would equal the accreted aggregate liquidation value of **\$12,950,029**.

Transition adjustment. Company A adopted the ASU using the modified retrospective method on January 1, 2027. A cumulative-effect adjustment of **\$100,029** (\$12,950,029 – \$12,850,000) is recorded to align the carrying amount with the stated-rate basis.

Journal entry (January 1, 2027):

- Dr. Retained earnings \$100,029
- Cr. Preferred stock (or APIC) \$100,029

Following the adjustment, the preferred stock carrying amount equals its accreted aggregate liquidation value.

First post-transition period. For the year ended December 31, 2027, the PIK dividend is measured using the stated rate:

- $\text{PIK dividend} = \$12,950,029 \times 9\% = \mathbf{\$1,165,503}$

The carrying amount of preferred stock (\$14,015,503) and its accreted liquidation value (\$14,115,532) remain aligned in subsequent periods.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

Required transition disclosures

Entities are required to provide clear disclosures in the period of initial adoption (including interim periods, where applicable), tailored to the chosen transition approach.

For **prospective adoption**, disclosures should include:

- The nature of the change in accounting principles and a description of the new measurement approach
- The method of transition applied

For **modified retrospective adoption**, in addition to the above, entities should disclose:

- The cumulative-effect adjustment to retained earnings or other equity components at the beginning of the earliest period presented
- The impact on income available to common shareholders, other affected financial statement line items, and per-share amounts for the current and any retrospectively adjusted periods

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective



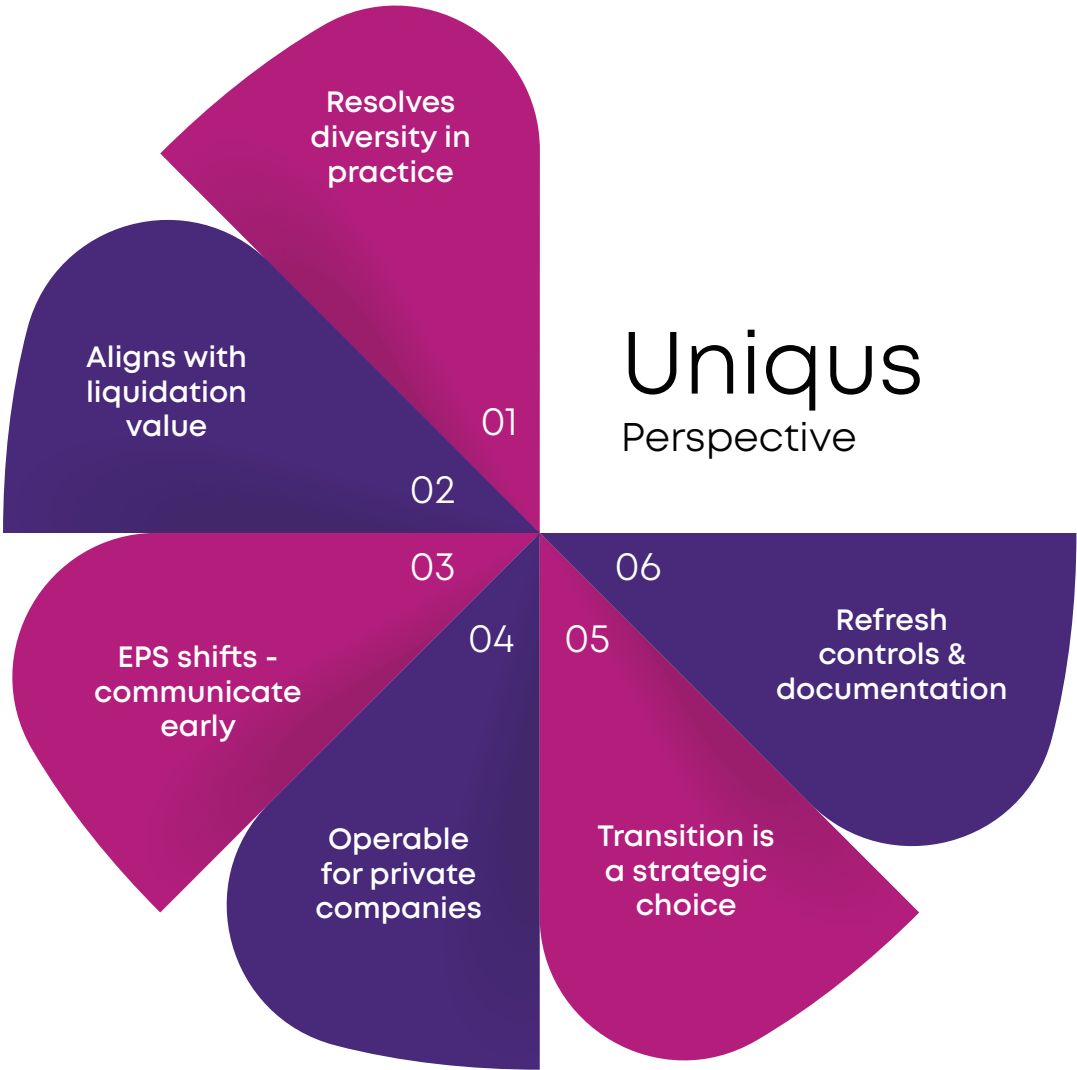
Implementation Matter

- Transition choice is a strategic decision. Prospective transition minimizes complexity but causes the preferred stock carrying amount to diverge from the accreted liquidation value (which may raise questions from sophisticated users).
- The modified retrospective method realigns the two measures — resulting in a cleaner run-forward — at the cost of developing historical computations at the stated rate.
- Entities should evaluate: (i) materiality of the cumulative-effect adjustment; (ii) data availability (particularly for long-outstanding preferred stock); (iii) impact on debt covenants, EPS, and peer comparability; and (iv) preferences of the audit committee, auditor, and regulators.



UNIQUS PERSPECTIVE

ASU 2026-01 is a narrow-scope standard with broad implications for how PIK dividends are recorded, reported, and communicated. Below, we share our view of the most important takeaways for issuers, audit committees, and other stakeholders — distilled from our work with clients across private equity portfolio companies, real estate, technology, energy transition, and other sectors where preferred stock with PIK features is common.



Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquus Perspective



Resolution of a long-standing diversity is a clear win for comparability

ASU 2026-01 eliminates a widely cited practice issue, enabling consistent measurement of in-scope PIK dividends. This enhances comparability across entities and removes the need for investors to normalize key metrics such as EPS and returns to common shareholders.



Alignment with liquidation value reinforces the “preferred stock as capital stack” lens

By anchoring measurement to liquidation value, the ASU aligns accounting with how investors evaluate preferred stock within the capital structure, improving the relevance and usability of reported information in valuation and capital allocation decisions.



EPS and capital structure metrics will shift — communicate early and proactively

The revised measurement will directly impact net income available to common shareholders and EPS. Entities should proactively communicate expected changes to investors, audit committees, and lenders, particularly where equity-based metrics influence covenants or valuations.



Private-company operability was a decisive factor — and it matters

The stated-rate approach simplifies application, particularly for private and pre-IPO entities that may lack robust fair-value capabilities, thereby reducing operational complexity and implementation burden.



Transition is a strategic choice, not a clerical exercise

The choice between prospective and modified retrospective transition has broader implications. Entities should evaluate materiality, operational feasibility, and impacts on covenants, tax, and compensation, supported by robust governance and documentation.



The standard should prompt a broader refresh of preferred stock controls and documentation

Adoption provides an opportunity to refresh accounting policies, systems, and controls. Entities should update documentation, ensure accurate tracking of liquidation value, and align close and disclosure processes with the new requirements.

For more information on the proposed Accounting Standard Update, see the [press release](#) on the FASB's website.

Executive Summary

Background

ASU 2026-01: Summary at a Glance

Scope Applicability

Key Highlights of the Amendment

Effective Date and Transition

Uniquis Perspective

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