



In This Issue

- [Overview](#)
- [Background](#)
- [Main Provisions](#)
- [Proposed Effective Date and Transition](#)
- [Contacts](#)

FASB Proposes Guidance on Measurement of Paid-in-Kind Dividends on Equity-Classified Preferred Stock

Overview

On September 30, 2025, the FASB issued a [proposed ASU](#)¹ that would amend ASC 505² to add guidance on how an issuer should measure paid-in-kind (PIK) dividends on equity-classified preferred stock. Under the proposed amendments, entities would be required to measure such dividends by multiplying the PIK dividend rate by the liquidation preference of the shares.

The proposal is limited to the measurement of PIK dividends and does not address recognition. By providing clear guidance on how to measure PIK dividends, the Board expects that comparability between entities will improve.

Comments on the proposed ASU are due by October 27, 2025.

Background

The proposed guidance began as a project of the Emerging Issues Task Force (EITF) on the measurement of PIK dividends on equity-classified preferred stock. Under current GAAP, there is no guidance on how an issuer should measure PIK dividends on such stock; accordingly, there is diversity in practice related to the accounting for these transactions.

¹ FASB Proposed Accounting Standards Update (ASU), *Equity (Topic 505); Initial Measurement of Paid-in-Kind Dividends on Equity-Classified Preferred Stock*.

² FASB Accounting Standards Codification (ASC) Topic 505, *Equity*.

At its [March 25, 2025](#), meeting, the EITF voted to recommend (1) improvements to the accounting requirements and (2) that the FASB add a project on this issue to its technical agenda, which the Board did on April 30, 2025.

Main Provisions

Scope

Under the proposed ASU, ASC 505-10-15 would be amended to:

- Define PIK dividends as “dividends that an issuer satisfies either by delivering to the holder additional preferred stock with the same terms as the original preferred stock or . . . by increasing the original preferred stock’s liquidation value.”
- State that the proposed guidance applies to PIK dividends on preferred stock classified as equity, including preferred stock classified as temporary equity in accordance with the SEC staff announcement in ASC 480-10-S99-3A.³
- Clarify that the guidance applies when the monetary value of the PIK dividends varies on the basis of the value of the preferred stock issued (i.e., when the issuer does not satisfy dividend obligations by issuing a variable number of shares with a fixed monetary value).

The proposal does not provide guidance on when an entity should recognize PIK dividends. Accordingly, the guidance in the proposed ASU would apply only after an entity has concluded that it meets the conditions for recognition and therefore must determine how to measure such dividends. See [Section 10.3.4.2](#) of Deloitte’s Roadmap *Distinguishing Liabilities From Equity* for guidance on dividend recognition.

Measurement

The proposed ASU would add to U.S. GAAP ASC 505-10-30-1, which would require entities to measure PIK dividends on the basis of their “rate stated in the preferred stock agreement.” Such agreements often specify this rate as a percentage of the liquidation preference or stated value of the preferred stock, although these designations may vary. This liquidation value reflects the amount owed to the holder of the preferred stock upon certain liquidation or deemed liquidation events or upon conversion into another class of equity (e.g., common stock).

Often, the liquidation preference is initially equal to the original issuance price of preferred stock; however, if the preferred stock was issued at a discount, the original issuance price may differ from the liquidation preference. An entity should evaluate the specific terms and features of its preferred stock to determine the amount to which to apply the stated dividend rate.



Connecting the Dots

Under current GAAP, an entity commonly assesses whether PIK dividends are discretionary or nondiscretionary when determining its PIK dividend measurement approach. Under the proposed ASU, there would be no distinction between the measurement of PIK dividends that are discretionary or nondiscretionary.

³ Originally issued as EITF Topic D-98, “Classification and Measurement of Redeemable Securities.”

The examples⁴ below explain the application of the proposed ASU in various scenarios.

Example 1

An entity issues 1 million shares of convertible preferred stock with a stated liquidation preference of \$10 per share. The shares are issued for \$10 per share for total proceeds of \$10 million ($\$10 \times 1 \text{ million} = \10 million). Dividends accrue quarterly to the liquidation preference of the preferred stock, whether or not declared, and must be paid in kind. The stated annual dividend rate is 6 percent of the liquidation preference (or 1.5 percent per quarter).

At the end of the first quarter, the entity recognizes total PIK dividends of 15,000 shares:

- $\$10 \text{ million [liquidation preference]} \times 1.5\% \text{ [quarterly dividend rate]} = \$150,000$.
- $\$150,000 \div \$10 \text{ [liquidation preference per share]} = 15,000 \text{ [preferred shares]}$.

The entity would therefore recognize a PIK dividend amount of \$150,000 (15,000 shares \times \$10 per share liquidation preference).

Example 2

Assume the same facts as in Example 1, except that in exchange for the \$10 million proceeds, the entity issued both preferred stock and equity-classified warrants. The warrants and the preferred stock each represent freestanding financial instruments. The preferred stock is initially recorded with a carrying value of \$9 per share ($\$9 \times 1 \text{ million} = \9 million) since \$1 million of proceeds was allocated to the warrants.

In this scenario, the entity would also recognize a PIK dividend amount of \$150,000 (15,000 shares \times \$10 per share liquidation preference). That is, the recognition of an issuance discount on the preferred stock does not affect the measurement of the PIK dividends as they accrue or are declared.

Example 3

Assume the same facts as in Example 1, except that dividends that are paid in kind accrue at the rate of 8 percent of the liquidation preference (2 percent per quarter). Dividends declared and paid in cash would be paid on the basis of a dividend rate of 6 percent of the liquidation preference (or 1.5 percent per quarter).

At the end of the first quarter, if the entity has not declared cash dividends, the entity recognizes total PIK dividends of 20,000 shares:

- $\$10 \text{ million [liquidation preference]} \times 2.0\% \text{ [quarterly PIK dividend rate]} = \$200,000$.
- $\$200,000 \div \$10 \text{ [liquidation preference per share]} = 20,000 \text{ [preferred shares]}$.

In this scenario, the entity would therefore recognize a PIK dividend amount of \$200,000 (20,000 shares \times \$10 per share liquidation preference).

Proposed Effective Date and Transition

An entity would be permitted to apply the amendments on either (1) a prospective basis or (2) a modified retrospective basis for equity-classified preferred stock instruments that are outstanding as of the initial application date. Early adoption would be permitted for interim and annual periods for which financial statements have not been issued or made available for issuance. An entity adopting the amendments in an interim period would be required to adopt them as of the beginning of the annual reporting period that includes that interim period.

The effective date will be determined after the FASB considers stakeholder feedback on the proposed ASU.

⁴ Examples 1 and 2 are adapted from paragraphs 36 through 41 of the EITF's March 25, 2025, [Issue Summary No. 1](#).

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