BDO BULLETIN

INVESTMENT COMPANIES TO INCLUDE CONTRACTUAL SALE RESTRICTIONS IN FAIR VALUE OF EQUITY SECURITIES

SEPTEMBER 2026

SUMMARY

The Financial Accounting Standards Board (FASB) has issued Accounting Standards Update (ASU) 2026-03, *Fair Value Measurement (Topic 820): Investment Companies with Equity Securities Subject to Contractual Sale Restrictions*. The update is a narrow exception to ASC 820, *Fair Value Measurement*, applying only to investment companies within the scope of ASC 946, *Financial Services — Investment Companies*. It requires investment companies within the scope of ASC 946 to consider contractual sale restrictions when measuring the fair value of equity securities in accordance with ASC 820. (Other entities must continue to exclude contractual sale restrictions from fair value.) It also requires investment companies to disclose the amount of the discount attributable to the restriction.

KEY TAKEAWAYS

- Investment companies within the scope of ASC 946 must now apply a discount (and disclose the amount of that discount) to reflect the amount market participants would demand because of a contractual sale restriction, reversing the guidance in ASU 2022-03, *Fair Value Measurement (Topic 820): Fair Value Measurement of Equity Securities Subject to Contractual Sale Restrictions*, for these entities.
- Restrictions already reflected in the economics of another transaction, such as securities pledged as collateral in a borrowing, are excluded to avoid double counting the same economic effect.
- Transition is prospective to all equity securities, including those with restrictions already in effect, with the adoption adjustment recognized in current-period earnings and disclosed.
- Early adoption is permitted any date on or after September 9, 2026.

WHY IS U.S. GAAP CHANGING?

Under ASC 820, a contractual restriction on the sale of an equity security is not part of the security's unit of account and therefore is not considered in measuring fair value. ASC 820 also prohibits an entity from recognizing and measuring a contractual sale restriction as a separate unit of account. As a result, under ASC 820, an entity holding a contractually restricted equity security and an entity holding an identical unrestricted security issued by the same investee (and for which there are quoted prices in an active market) each measure fair value based on the market price of the unrestricted security.

Stakeholders indicated that the existing guidance produces fair value measurements that do not accurately reflect how market participants would value equity securities subject to contractual sale restrictions—a concern emphasized for investment companies because excluding the effect of those restrictions in the fair value measurement (i) overstates net asset value (NAV), (ii) might distort performance reporting and management fees, and (iii) creates different outcomes for purchasing, redeeming and remaining shareholders.

WHO DOES THIS CHANGE AFFECT?

The amendments in ASU 2026-03 only apply to investment companies within the scope of ASC 946 that have investments in equity securities that are subject to contractual sale restrictions. The amendments are a narrow exception, meaning that all other entities must continue to ignore the effect of contractual sale restrictions in the fair value measurement of equity securities, in accordance with the existing guidance in ASC 820.

BDO INSIGHT: FASB PROJECT ADDED FOR OTHER ENTITIES

Some stakeholders requested that the guidance in ASU 2026-03 apply to all entities. However, the FASB noted that the contractual sale restriction issue is particularly significant for investment companies (as discussed above), observing that it also affects the investment company’s investors who measure their investments at NAV. Accordingly, to expeditiously address the issue, the FASB limited the guidance solely to investment companies within the scope of ASC 946. The FASB added a project to the technical agenda to address the fair value measurement of equity securities subject to contractual sale restrictions for other entities.

WHAT IS CHANGING?

Measurement Exception for Investment Companies

When an investment company cannot sell an equity security on the measurement date because of a contractual sale restriction, ASU 2026-03 requires the investment company to apply a discount for the effect of the restriction in the fair value measurement of that security. Specifically, the investment company applies the discount regardless of whether the contractual sale restriction is (i) a characteristic of the reporting entity holding the security or (ii) a characteristic of the security itself. The discount reflects the amount that market participants would demand to compensate for the liquidity risk and price volatility associated with the restriction period.

The requirement does not apply to restrictions imposed on equity securities that are reflected in the economics of another transaction entered by the reporting entity (for example, a borrowing in which the reporting entity pledged those equity securities as collateral).

New Disclosure of the Discount

ASU 2026-03 requires investment companies to disclose the amount of the discount included in the fair value measurement of equity securities that is attributable to contractual sale restrictions. If an entity has multiple investments in equity securities subject to contractual sale restrictions, it considers the guidance in ASC 820-10-50-1D to determine how much to aggregate or disaggregate the disclosed information. The new disclosure is in addition to the existing fair value disclosures that equity securities subject to contractual sale restrictions are required to provide. Therefore, entities must still disclose the nature of the restrictions, the remaining duration of the restrictions, and circumstances that could cause a lapse.

BDO INSIGHT: APPLYING THE CONTRACTUAL SALE RESTRICTION GUIDANCE

ASU 2026-03 reverses course for investment companies. Previously, ASU 2022-03 required all entities to exclude the effect of contractual sale restrictions from fair value. By way of explanation, the FASB noted that companies are staying private longer and entering public markets at larger valuations, meaning that lock-up restrictions may have a more significant economic effect than they did when ASU 2022-03 was issued.

The FASB decided not to define "contractual sale restriction," noting that a new definition risked unintended consequences. However, it provided a carve-out for restrictions that are reflected in the economics of another transaction entered by the reporting entity, so that the effect of such restriction is not double-counted. The FASB noted that pledged collateral is the most common fact pattern, but it chose broad wording to enable investment companies to apply judgment based on their own facts and circumstances.

ASU 2026-03 applies only to equity securities. It does not apply, for example, to crypto assets or debt securities. However, the scope debate is likely not settled, as stakeholders noted that the same issues that apply to equity securities might arise for other assets as well.

WHEN ARE THE CHANGES EFFECTIVE?

The following table summarizes the transition for ASU 2026-03:

<table>
<tr><th></th><th>PUBLIC BUSINESS ENTITIES</th><th>ALL OTHER ENTITIES</th></tr>
<tr><td>Effective Date</td><td colspan="2">▶ Annual reporting periods beginning after December 15, 2027.
▶ Interim reporting periods within those annual reporting periods.</td></tr>
<tr><td>Early adoption</td><td colspan="2">Permitted on any date on or after September 9, 2026.</td></tr>
<tr><td>Transition</td><td colspan="2">▶ Prospective to all equity securities, including equity securities with contractual sale restrictions in effect on the adoption date. Any adjustment resulting from adoption is recognized as an adjustment to current-period earnings on the date that the investment company first applies the amendments.
▶ An investment company that early adopts applies the amendments prospectively beginning on the adoption date.
▶ An investment company must disclose the amount recognized as an adjustment to earnings in the period in which it first applies the amendments.</td></tr>
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Link to ASU 2026-03.

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