Proskauer

FCA's Private Market Valuations Review – Good Practice but Room for Improvement

Regulatory & Compliance on **March 10, 2025**

Background

On 5 March 2025, the United Kingdom's Financial Conduct Authority ("**FCA**") published the findings of its multi-firm review of valuation processes for private market assets (the "**Review**"). The Review covered firms operating in range of private asset classes, including: venture capital, infrastructure (equity and debt), private equity and private debt.

As detailed by the FCA, private market assets are not subject to external valuations that are typically carried out within the public markets (that are subject to frequent trading and pricing). The Review set out to analyse whether private market firms had robust valuation processes in place, to ensure fairness and confidence in the industry.

The FCA noted that firms generally demonstrated good practice, but there is room for improvement.

Key Findings

The key findings from the Review are:

1. **Governance arrangements**

Whilst nearly all firms reviewed had specific governance arrangements in place for valuations (with many incorporating valuation committees responsible for valuation decisions), the FCA noted that in some cases, there were inadequate records to note how these valuation decisions were reached and that valuation committee members could not describe examples in practice.

Key Recommendation: Firms should have a clear accountability regime for valuations, including detailed record-keeping of how valuation decisions are reached.

2. **Conflicts**

While firms identified conflicts in their valuation process around fees and remuneration, and in many cases had limited these through fee structures and remuneration policies, other potential conflicts were only partly identified and documented.

The FCA noted that conflicts could arise where valuations are linked to investor fees and employee remuneration. In addition, firms are incentivised to determine favourable valuations as part of investor marketing, asset transfers (such as continuation funds) and secured borrowing arrangements (such as NAV facilities).

Key Recommendation: Firms should consider if these valuation-related conflicts are relevant and if they are, for firms to document and take steps to mitigate or manage them.

3. **Functional independence and expertise**

The FCA observed that whilst some firms demonstrated functional independence (citing the use of a dedicated function to lead on valuations, preparing models and recommendations) that other firms demonstrated insufficient expertise in their functions (citing the inability to describe assets, valuation models and the structure of the valuation committee voting membership).

Key Recommendation: Firms should assess whether they have sufficient independence in their valuation function and the voting membership of their valuation committees are measured to ensure effective control and expert challenge.

4. **Policies, procedures and documentation**

The FCA focused on appropriate policies and procedures relating to valuation policies, valuation models, auditors and back-testing. They found that whilst all firms had valuation policies outlining the process, some firms did not provide further detailed rationale for selecting specific methodologies and safeguards for functional independence.

Key Recommendation: Firms should ensure that their valuation policies are sufficiently comprehensive and clear. Moreover, the FCA also advised that firms should consider whether they can make investments in technology to improve consistency and reduce the risk of human error in their valuation processes.

5. **Frequency and Ad hoc valuations**

The FCA noted that less frequent valuations could risk a “stale” valuation, which does not accurately reflect the condition of an investor’s holdings.

For most alternative assets, the industry has predominantly converged to quarterly valuation cycles, although debt assets also had monthly valuation cycles. Firms reviewed by the FCA argued those frequencies were usually appropriate, given the resource-intensive nature of valuing private assets, the alignment with financial reporting frequency and infrequent changes to the value of the underlying asset.

Key Recommendation: Firms should incorporate a defined process for ad hoc valuations which would mitigate the risk of “stale” valuations.

6. **Transparency to investors**

The FCA found that reporting varied across firms, but that most firms were providing regular quantitative and qualitative updates to investors.

Key Recommendation: Firms should consider where they can improve their reporting to and engagement with investors in relation to valuations, including providing detail on fund-level and asset-level performance to increase transparency and investors’ confidence.

7. **Application of valuation methodologies**

The FCA reported that methodologies varied across asset classes, with the most common methodologies being:

- **Market approach:** which uses prices and other relevant information that have been generated by market transactions that involve identical or comparable assets. This can involve valuation multiples derived from quoted prices of public companies or prices from merger and acquisition transactions.
- **Income approach:** which converts future amounts (for example, cash flows or income and expenses) to a single current (discounted) amount. When the income approach is used, the fair value measurement reflects current market expectations about those future amounts.

The FCA found that the challenges most firms faced was inconsistency. Some firms discussed the challenge of identifying comparable companies or assets, particularly when the portfolio company or asset had unique attributes and firms also had different approaches to reflect public market volatility.

Key Recommendation: Firms should apply valuation methodologies and assumptions consistently, and to make valuation adjustments solely on the basis of fair value. Where relevant, firms should consider using industry guidelines to ensure their approach is in line with standard market practice.

8. **Use of third-party valuation advisers**

The FCA noted that third-party valuation advisers can provide additional independence and expertise, although sufficient oversight is required.

Key Recommendation: When using a third-party valuation adviser, they should be appropriately overseen, and potential commercial conflicts need to be identified and managed. Firms should consider the strengths and limitations of the service provided and disclose the nature of the services used to investors.

Next Steps

Following the Review, the FCA will engage with firms and industry bodies to discuss the challenges faced by the industry and potential opportunities to further enhance valuation practices within private markets. They also note that the findings from the Review will be considered as they assess the Alternative Investment Fund Managers Directive ("**AIFMD**"), as currently onshored in the United Kingdom.

Key Takeaway for Non-UK Fund Sponsors

Although the findings from the Review are aimed at firms regulated by the FCA, the United States Securities and Exchange Commission ("**SEC**") has regularly commented issues relating to the valuation processes of firms within their remit over the last few years. The findings from the Review and the associated recommendations are valuable for non-FCA regulated fund sponsors as well, as it provides a baseline as to common, good practice across the private assets market, which the SEC may look to when determining whether or not to cite a U.S. fund manager's valuation policies and procedures for a deficiency.

View orginal.

Related Professionals

- **John Verwey**
  Partner
- **Michael Singh**
  Associate
- **Rachel E. Lowe**
  Partner
- **Sulaiman I. Malik**
  Associate