FMA

Finanzmarktaufsicht
Liechtenstein

**FMA Communication 2020/2 – Valuation of assets in UCITS, AIFs, and investment undertakings**

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| Reference: | FMA C 2020/2 |
| Addressees: | ● Management companies under UCITSG and IUG |
| | ● Alternative investment fund managers (AIFMs) under AIFMG |
| | ● Administrators under AIFMG |
| | ● Depositaries under UCITSG, AIFMG, and IUG |
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| | ● Articles 42 - 43 AIFMG, Article 11 AIFMV |
| | ● Articles 67 - 74 Commission Delegated Regulation (EU) No 231/2013 |
| | ● Article 33 IUG, Articles 18 - 21, Article 26 IUV |

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## 1. General principles

The management company/AIFM sets out the policies for the valuation of assets and calculation of the net asset value per unit or share in the constitutive documents of each fund[1].

The assets of an alternative investment fund (AIF) and IU must be valued and the net asset value (NAV) per unit or share calculated at least once a year (Article 43(2) AIFMG; Article 18(1)(a) IUV).

For open-ended AIFs, the valuations and calculations must be made at a frequency that is appropriate in relation to the specific features of the assets and the rules for issue or subscription and redemption or cancellation of units or shares. The valuation of assets held by open-ended AIFs must take place every time the net asset value per unit or share is calculated (Article 74(1) of Commission Delegated Regulation (EU) No 231/2013).

For closed-ended AIFs, a valuation must be carried out also in the event of any increase or decrease in capital.

For UCITS, the valuation must be carried out at least every two weeks (Article 10(3) UCITSV).

## 2. Valuation policies and procedures

The valuation represents a best possible approximation of the fair value of the fund's assets, taking into account external factors such as tradability, data availability, market-based inputs, etc.

Fair value is defined as the price that would be received for an asset in an orderly transaction between market participants on the measurement date.

A hypothetical transaction should be assumed, i.e. there does not have to be an actual intention to sell the asset on the measurement date. Likewise, it is not a forced transaction (e.g. fire sale or forced liquidation). The market participants are independent, knowledgeable, and willing and able to enter into the transaction.

The valuation of assets must in principle be carried out in accordance with the following hierarchy:[2]

1. Assets must be valued using objective, observable, unadjusted quoted market prices for identical assets in active markets on the measurement date, if available. If not available, then assets should be valued using:
2. Objective, observable quoted market prices for similar assets in active markets. If not available or appropriate, then assets should be valued using:
3. Quoted prices for identical or similar assets in markets that are not active (markets in which there are few transactions for the asset, the prices are not current, or price quotations vary substantially over time and/or between market makers). If not available or appropriate, then assets should be valued based on:
4. Market-based inputs, other than quoted prices, that are observable for the asset. If not available or appropriate, then assets should be valued based on:
5. Subjective, unobservable inputs for the asset where markets are not active at the measurement date. Unobservable inputs should only be used to measure fair value to the extent that observable inputs and prices are not available or appropriate. Unobservable inputs reflect the management company's/AIFM's

[1] To improve readability, investment undertakings (IUs) under the IUG, undertakings for collective investment in transferable securities (UCITS) under the UCITSG, and alternative investment funds (AIFs) under the AIFMG are summarised under the term "fund".
Where provisions of specific laws are applicable, this is indicated in the text.

[2] Source: Global Investment Performance Standards (GIPS® Standards). www.gipsstandards.org

own assumptions about the assumptions that market participants would use in pricing the asset and should be developed based on the best information available under the circumstances.

When selecting the valuation procedure, priority is therefore given to the procedure that is appropriate and maximises the use of observable market-based inputs. The market-based inputs correspond to the market situation on the measurement date. The management company/AIFM must use independent data sources where available and reliable.

Objective, observable, unadjusted quoted market prices are always prioritised over indicative prices. Indicative prices may, however, be used in valuation models.

Fair values for assets may also be obtained from appropriate third parties (e.g. issuers, market makers, and valuers). The management company/AIFM must in principle gain an understanding of how third parties determine these fair values. The management company/AIFM must assess and document the reasonability of fair values.

The valuation policies and procedures and the designated valuation methodologies must be applied consistently and reviewed at least once a year for their appropriateness. A change in the valuation procedure must be made if doing so results in a significantly more accurate estimate of the fair value than the previous valuation procedure. The changes must be approved by the senior management of the management company/AIFM.

## 3. Special requirements for the valuation of assets in AIFs

AIFMs must establish, maintain, implement and review, for each AIF they manage, written policies and procedures that ensure a sound, transparent, comprehensive and appropriately documented valuation process. The valuation policy and procedures must cover all material aspects of the valuation process and valuation procedures and controls in respect of the relevant AIF (Article 67(2) of Commission Delegated Regulation (EU) No 231/2013).

The valuation policies and procedures also include escalation channels for resolving differences in values or other problems in the valuation of the assets. Pursuant to Article 71(2) and (3) of Commission Delegated Regulation (EU) No 231/2013, a review process for the individual values of assets must also be defined, where a material risk of an inappropriate valuation exists.

Under Article 43(5) AIFMG, the valuation may be carried out by the AIFM itself or delegated to an external valuer meeting the requirements set out in Article 44 AIFMG.

If the AIFM appoints an external valuer, the procedures for the exchange of information between the AIFM and the external valuer must be set out in the valuation policies and procedures. However, the AIFM remains responsible for ensuring a proper valuation. Any exclusion of liability vis-à-vis the AIF and the investors is ineffective. The appointment of an external valuer must be notified to the FMA.

Under Article 43(6) AIFMG, the FMA may, if the AIFM carries out the valuation itself, also require the AIFM to have its valuation procedures and/or valuations inspected by an external valuer or auditor.

If a model is used to value assets, the main features must be presented in the valuation policies and procedures. The AIFM must take into account the characteristics of the financial instrument and the information available to it for the valuation. When applying the model, the following aspects in particular must be documented in a detailed and comprehensible manner:

- the reason for the choice of the model
- the underlying data
- the assumptions used in the model and the rationale for using them
- the limitations of the model-based valuation

A valuation model must always be based on a recognised and appropriate methodology.

Before a valuation model is used, it must be validated by a person with sufficient expertise who was not involved in the process of building the model. The valuation must be approved by the senior management of the AIFM before it is used.

## 4. Valuation of investments in private equity and private debt

Private equity refers to investments in the form of equity interests in companies that are not traded on a trading venue or for which the immediate intention is to delist this company from the trading venue after the investment is made.

Private debt refers to the provision of debt capital to companies by non-banks via a non-publicly traded market.

Hybrid financial instruments may also exist which have both equity and debt characteristics.

Due to the lack of market prices as a result of the non-listing of private equity and private debt, these investments fall under point 4 and especially point 5 of the valuation hierarchy.

For the valuation of investments in private equity and private debt, the FMA recommends applying the International Private Equity and Venture Capital Valuation Guidelines (IPEV Guidelines).[3]

Application of the IPEV Guidelines or other recognised valuation guidelines must be documented in the valuation policies and procedures of the AIF.

### 4.1 Valuation of investments in private equity

The management company/AIFM must select the most appropriate valuation model to determine the fair value of the investment in private equity.

The management company/AIFM must take into account factors such as the equity interest (majority or minority interest), the characteristics of the financial instrument and the invested company, and the availability and appropriateness of company-specific data and market-based inputs.

The management company/AIFM must in particular assess, with the appropriate care, the life cycle of the company (start-up, established company), the impact of different accounting standards, and the usability of book values and forecasted figures.

The IPEV Guidelines provide assistance in selecting and applying appropriate valuation models.

### 4.2 Valuation of investments in private debt

The management company/AIFM must select the most appropriate valuation model to determine the fair value of the investment in private debt.

[3] www.privateequityvaluation.com

For the valuation of investments in private debt, the management company/AIFM must take into account market-based inputs, where available and appropriate. Other factors to be taken into account by the management company/AIFM include the issuer's default risk, the coupon rate and the maturity of the financial instrument, as well as any collateralization.

The nominal value of the debt instrument is not automatically fair value, but both values can be identical depending on market conditions and the characteristics of the instrument. This is the case if the coupon rate of the debt instrument is in line with the market on the measurement date.

If no appropriate market-based inputs are available for the valuation, the management company/AIFM should base the valuation exclusively on the issuer's company-specific data in accordance with the valuation hierarchy. The management company/AIFM must periodically review the appropriateness of the valuation procedure and the existence of market-based inputs. The management company/AIFM must determine an appropriate and comprehensibly documented procedure for any write-downs and write-ups relating to the debt instrument.

For short-term investments with a term to maturity of less than 397 days, a valuation at the current market price can be omitted and the investments can be recognised at nominal value.

The IPEV Guidelines provide assistance in selecting and applying appropriate valuation models.

## 5. Data protection

The FMA processes personal data exclusively in accordance with the general data processing principles of the General Data Protection Regulation (Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC) as well as in line with Liechtenstein data protection law.

All information regarding the processing of personal data, as well as details about the processing purpose, the data controller and the rights of data subjects can be found in the FMA Privacy Policy: https://www.fma-li.li/en/fma/data-protection/fma-privacy-policy.html

## 6. Entry into force

This Communication was approved by the Executive Board of the FMA on 9 December 2020 and enters into force on 1 January 2021.

The FMA is happy to answer any questions.
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