

Valuation Raised as an Issue by the OCIE

On June 23, 2020, a Risk Alert¹ was released by the SEC on behalf of the Office of Compliance Inspections and Examinations (“OCIE”) that provides an overview of compliance issues found during examinations of registered investment advisers that manage private equity or hedge funds (“private fund advisers”). The Risk Alert is intended to (i) assist private fund advisers evaluate and improve their compliance programs and (ii) provide investors with information relating to private fund adviser deficiencies. Valuations were identified as an issue by the OCIE.

Each year, the OCIE examines hundreds of private fund advisers, and is frequently asked about its observations, common deficiencies and compliance issues from these examinations. As a result of the deficiencies, investors in private funds (“investors”) (i) may have paid more in fees and expenses than required or (ii) were not informed of relevant conflicts of interest concerning the private fund adviser and the fund.

The Risk Alert discusses three general areas of deficiencies that OCIE has identified in its private fund examinations: (A) conflicts of interest, (B) fees and expenses, and (C) policies and procedures relating to material non-public information (“MNPI”).

Under section fees and expenses, valuation has been named a concern by the OCIE. During examinations, the OCIE observed that private fund advisers did not value client assets in accordance with their valuation processes or in accordance with disclosures to clients (such as that the assets would be valued in accordance with GAAP). In some cases, the staff noted that this failure to value a private fund’s holdings in accordance with the disclosed valuation process led to overcharging management fees and carried interest because such fees were based on inappropriately overvalued holdings.

How Houlihan Capital Can Help

Houlihan Capital can help with the valuation process, including reviewing or drafting your valuation policy and with the process of determining fair value of your illiquid investments. The firm has extensive experience in providing objective, independent and defensible opinions of value that meet accounting and regulatory requirements. Houlihan Capital is SOC-compliant, a Financial Industry Regulatory Authority (FINRA) and SIPC member and committed to the highest levels of professional ethics and standards.

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