

Central Bank of Ireland Letter on 2022 ESMA Common Supervisory Action on Asset Valuation

What You Need to Know

- (a) Following its 2022 review of asset valuation as part of ESMA's Common Supervisory Action, the Central Bank of Ireland ("Central Bank") has published its findings and expectations.
- (b) Four areas were highlighted where fund management companies need to improve their asset valuation frameworks.

What You Need to Do

- (a) Share the Central Bank's findings with the boards of fund management companies and take appropriate action without delay.
- (b) Conduct a review of asset valuation frameworks by the end of Q2 2024 and strengthen frameworks where weaknesses are identified.

Background

On 14 December 2023, the Central Bank issued a *Dear Chair* letter ("Letter") to fund management companies ("FMCs") regarding their 2022 review of asset valuation as part of ESMA's Common Supervisory Action ("CSA") on this topic.

The Letter summarises the Central Bank's main findings, observations and expectations following its review of FMCs' compliance with the relevant UCITS and AIFM Directives/Regulations on asset valuation, as well as their adherence to valuation principles and methodologies, including during COVID-19.

Main Findings

While the Central Bank found that the overall level of compliance with the relevant legislation was good, the Central Bank highlighted four main findings where FMCs need to improve their asset valuation frameworks:

- (a) The use of group asset valuation policies and procedures that do not reflect the local regulatory environment or the operational roles and responsibilities of the FMC;
- (b) The lack of formal asset valuation error procedures that outline the controls and escalation measures to be applied in cases of valuation errors or incorrect calculations of a fund's net asset value ("NAV").
- (c) Asset valuation policies and procedures that do not cover the valuation process in sufficient detail or are not supported by a robust governance process; and
- (d) Limited evidence of periodic reviews of asset valuation policies and procedures by senior management to ensure they remain fit for purpose and consistent across all funds under management.

The Central Bank also made two observations where FMCs should consider enhancing their asset valuation practices:

- (a) The incorporation of the results of liquidity stress testing and scenario analysis into liquidity management frameworks and decision making, risk management and risk mitigation processes; and
- (b) The clear segregation of roles and independence within the asset valuation

function to avoid potential conflicts of interest.

Key Actions

The Letter should be brought to the attention of the boards of FMCs and appropriate action taken without delay.

The Central Bank expects FMCs to conduct a review of their asset valuation frameworks by the end of Q2 2024 and to strengthen their frameworks where weaknesses are identified.

Key action items to be considered by each FMC are ensuring that:

- (a) It has documented, comprehensive and entity specific asset valuation policies and procedures which clearly outline the operational roles and responsibilities for all parties involved in the process.
- (b) Its asset valuation policies and procedures are subject to review by senior management at least annually or where required throughout the year to ensure they remain fit for purpose.
- (c) It has a formalised and comprehensive errors procedure to ensure remedial action is implemented when valuation errors or incorrect calculations of the NAV occur.

We have extensive experience in advising FMCs on asset valuation matters, including the application of the relevant regulations and principles, the design and review of policies and procedures and the management of errors and conflicts of interest. We can also assist FMCs in preparing for and responding to Central Bank supervisory engagement and inspections.

Further Information

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