Schulte Roth & Zabel

Alert

Private Funds — Impact of the Wuhan Novel Coronavirus on January NAV Calculations: Challenges for Private Fund Managers

January 31, 2020

While the financial impact of the Wuhan Novel Coronavirus is still incalculable (as, of course, is the human cost), many private fund managers may find themselves forced to perform some kind of assessment.

As today is the end of the month, many managers are required to calculate a net asset value that will serve as the basis for investor reporting, management fee calculations and subscription or redemption prices. With China's equities and futures exchanges closed (reports indicate that most Chinese exchanges are scheduled to open on Monday, Feb. 3, 2020, albeit with reduced staffing), managers with funds and client accounts that are exposed to China need to consider how this impacts their valuation obligations. This situation will have different levels of impact: Advisers to Asia-focused funds are more likely to be substantially affected by these closures, while other managers may be able to determine that there is no material effect on their funds.

For those managers who need to cut a month-end NAV, we expect that they will find that they need to rely on a "fair value" valuation process for assets that are otherwise considered (under applicable accounting rules) to be Level 1 or Level 2 assets (and which are typically valued by reference to exchange-quoted prices), especially bearing in mind there has been no trading on such markets since they closed for the Lunar New Year on Jan. 25, 2020.

Such managers should consider the full range of options available and the various sources of data that might be employed in undertaking a fair value pricing, which might include — among others — Monday's opening prices (if there is an orderly opening on Monday), activity in China- and Asia-focused futures contracts that are actively trading in non-Chinese marketplaces, trading of Chinese names on secondary exchanges, trading of comparable non-Chinese securities and bespoke or industry models. Managers also should consider evaluating their options with their auditors. Of course, for funds with material exposure to suspended markets, it may make sense to defer February subscriptions (although this does not help in terms of previously scheduled redemptions) or even to push back the valuation point to Monday (assuming an orderly opening on Monday).

While there are numerous options to consider, managers should start by reviewing their existing obligations, and consider whether any of the following steps are appropriate:

- Review constitutional documents or other client agreements (including side letters) and disclosure documents to ascertain what options are available and, in particular, what requirements might apply in respect of a fair value calculation;

- Perform a similar exercise with the adviser's valuation policy and any desk policies to isolate the specific requirements and constraints on any fair valuation process; and
- Consider reviewing the proposed course of action with on and offshore counsel, as well as the fund auditors, external administrator and fund/GP board of directors (as applicable).

If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel.

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