LEGAL UPDATE: VALUATION PRACTICES AND RISK MANAGEMENT PRACTICES FOR FUND MANAGEMENT COMPANIES

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I. Introduction

1. On 29 May 2026, the Monetary Authority of Singapore ("**MAS**") issued two (2) information papers that set out MAS' supervisory expectations in respect of valuation practices (the "**Valuation Information Paper**") and risk management practices (the "**Risk Management Information Paper**" and collectively, the "**Information Papers**") of fund management companies ("**FMC**"). The expectations set out in the Information Papers are based on MAS' thematic inspections of selected FMCs' investment process. In this client update, Director Ian Phung and Associate Justin Hoo summarise the key takeaways from the recent updates.

II. Valuation Practices for Fund Management Companies

2. The Valuation Information Paper provides that FMCs must ensure independent valuation of their assets under management ("**AUM**") and put in place governance structures, frameworks, policies and procedures ("**P&P**") and controls to ensure that valuation of funds' assets is appropriate and timely, and investors are treated fairly. This is because weak valuation practices can significantly impact the interests of investors in several ways, including but not limited to:

   (a) <u>Erroneous Subscription and Redemption Calculations</u>: Inaccurate valuations may result in incorrect fund unit pricing, leading investors to subscribe at unfair values or redeem units for more or less than they are truly worth;

   (b) <u>Distortion of Fund Performance</u>: Misvalued assets can misrepresent a fund's returns, potentially misleading investors about the fund's track record and risk profile;

   (c) <u>Improper Valuation of Asset Transfers</u>: This may cause mispricing between portfolios or funds during transfers, unfairly allocating value across investor groups; and

   (d) <u>Excessive Payment of Fees</u>: Management and performance fees calculated on inflated or inaccurate NAV can result in investors being overcharged.

3. The Valuation Information Paper covers four (4) key areas related to valuation: (1) governance, (2) policies and procedures, (3) ongoing price validation checks, and (4) valuation approaches and methodologies.

Governance

4. MAS observed that most FMCs engaged third-party service providers such as external valuers and/or fund administrators to perform independent valuation and reporting of net asset values ("**NAV**") to investors. Meanwhile, for FMCs that invest in private and illiquid assets, valuation was carried out in-house by a function independent of portfolio management or an entity related to the FMC. Further, FMCs either designated senior management with relevant expertise and experience or set up a dedicated committee to oversee valuation matters. Smaller FMCs were observed to not have dedicated committees and appointed senior management member(s) involved in portfolio management function to oversee the valuation of hard-to-value assets. Further, a few FMCs either did not establish terms of reference ("**TOR**") for their dedicated committees, or their existing TOR lacked coverage of key operational areas, such as composition and designation of committee members, meeting frequency and quorum requirements for decision making.

5. MAS stated that FMCs should ensure that valuation matters are overseen by senior management member(s) who are independent from the portfolio management function to avoid potential conflicts of interest ("**COI**"). For smaller FMCs where there could be a lack of independence, any potential COI should be adequately mitigated and where appropriate, disclosed to their investors. Mitigation measures would include engaging external valuers to conduct independent assessments or conduct regular external audits on valuation practices. Further, dedicated valuation committee(s) should have formal TORs in place which clearly outline their responsibilities, composition, meeting frequency, quorum requirements, and reporting line(s) for accountability.

Policies and Procedures

6. In relation to P&Ps, the P&Ps of an FMC should clearly define the roles and responsibilities of all parties involved in the valuation process, include appropriate valuation methodologies and frequency for all relevant asset classes, clearly outline escalation procedures for exceptions noted, specify corresponding record-keeping requirements, and be subject to regular and ad-hoc reviews.

7. It was noted that some FMCs' P&Ps were not adhered to when their current practices were observed, and the P&Ps did not contain sufficient guidance for certain scenarios (e.g. factors to trigger fair value assessment, timelines to resolve exceptions, and key inputs for valuation sensitivity analysis). Similarly, some FMCs failed to obtain the approval of their valuation committee and document the reason for the deviation.

Ongoing Price Validation Checks

8. In relation to ongoing price validation checks, FMCs should implement independent and ongoing price checks which are supported by well-defined exception tolerance levels, along with clear escalation protocols and approval channels. Documentation of price validation checks should be maintained and include justifications for any overrides to ensure proper record keeping and accountability.

9. MAS noted that while FMCs commonly engage third-party service providers, FMCs should be wary of how the valuer identifies and reports stale prices for securities that are not traded and has unchanged prices for consecutive days, and ensure that the reporting and review of such stale prices are done in a timely manner. Further, FMCs should align their definition of “stale price securities” with their fund administrator.

10. Key takeaways for ongoing price validation checks also include:

    (a) adjusting exception tolerance levels according to the characteristics of each asset class and financial instrument;
    (b) putting in place appropriate processes to detect inconsistent valuation practices for the same asset class or financial instrument across different funds managed;
    (c) ensuring timely review and follow-up on all pricing exceptions noted;
    (d) using independent alternative price sources to investigate exceptions;
    (e) establishing appropriate escalation processes and forums for exceptions handling;
    (f) establishing clear criteria or thresholds for challenging third-party service providers’ valuations; and
    (g) maintaining proper records of all price validation checks performed, investigations conducted, and follow-up actions taken to resolve pricing issues, including any approvals obtained.

Valuation Approaches and Methodologies

11. For the purposes of transparency, FMCs should clearly disclose to investors the names and use of third-party valuation service provider(s) and their specific roles and responsibilities, any material involvement by the FMC in the valuation process, and include a high-level description of the valuation approach and a summary of the valuation methodologies applicable to the different asset classes and financial instruments that their funds can invest in. More detailed information regarding valuation approaches and methodologies could be set out in an FMC’s P&Ps, to be made available to investors upon their request.

12. FMCs should be aware of the unique challenges that certain asset classes pose such as private credit and digital assets. The valuation of private credit involves a certain degree of subjective judgement, such as when to designate a borrower as being in default, the extent of recoverability and valuation adjustments, where personal guarantees or collateral have been obtained but uncertainty remains regarding the timing and outcome of enforcement actions. As for digital assets, FMCs should note that for such markets which operate 24/7, it will require a pre-defined cut-off time for pricing to ensure consistency and comparability across reporting periods, the volatility inherent in such assets which cause price fluctuations, fragmented trading environments leading to inconsistent price discovery, and illiquidity risk arising from limited trading activity.

13. FMCs should also ensure that there are established frameworks and processes, which are duly approved by the relevant authority (e.g. valuation committee or senior management) to identify assets that require fair value review in a timely and consistent manner, and apply appropriate valuation methodologies. Assets that are assigned fair values should be subject to ongoing

monitoring to ensure their valuations remain appropriate, and the criteria for triggering a reassessment should be clearly set out, and performed assessments should be appropriately documented.

III. Risk Management Practices for Fund Management Companies

14. The Risk Management Information Paper states that FMCs are required to put in place a risk management framework to identify, address and monitor the risks associated with their assets under management.[1] The Risk Management Information Paper also sets out MAS' supervisory expectations for effective governance structures, frameworks, P&Ps, and controls for overseeing and managing the FMCs' investment process. FMCs are expected to consider the principles set out in the applicable MAS Guidelines on Risk Management Practices and Guidelines on Licensing and Conduct of Business for Fund Management Companies [SFA 04-G05]. The Risk Management Information Paper covers: (1) governance, (2) policies and procedures, (3) new fund launches and changes to existing funds, (4) investment due diligence, and (5) ongoing monitoring of investments.

Governance

15. MAS expects the board and senior management to put in place appropriate governance structures, frameworks, P&Ps, and controls for (i) new fund launches and investment changes to existing funds, (ii) investment due diligence and (iii) ongoing monitoring of investments. COI should be identified and effective controls and segregation of duties should be implemented to mitigate such COI and where appropriate, disclosed to customers. The board and senior management should also keep apprised of investment matters on a timely and regular basis, with appropriate escalation procedures established to highlight significant issues or concerns for action to be taken in a timely manner.

Policies and Procedures

16. MAS expects FMCs to establish comprehensive P&Ps that cover all aspects of their fund management activities and operations. The roles and responsibilities of all parties (including third-parties) should be clearly identified and defined. The P&Ps should cover the relevant frameworks, methodologies, processes and controls for identifying and managing risks associated with each asset class and the investment strategy employed by the FMC. Escalation procedures for exceptions, including limit breaches and anomalies detected should also be clearly outlined in the P&Ps. Further, the P&Ps should be subject to regular and ad-hoc reviews to incorporate best practices and emerging industry standards on a timely basis.

17. Some FMCs only established relevant investment P&Ps after the funds were launched, and some FMCs did not update their P&Ps to reflect ongoing practices or were not sufficiently detailed to provide guidance in specific areas. Relevant P&Ps should be in place prior to launching new funds and there should be a fixed frequency for regular reviews and triggers for ad-hoc reviews should be specified. P&Ps should provide guidance to deal with any deviations

[1] Regulation 13B(1)(a) of the Securities and Futures (Licensing and Conduct of Business) Regulations.

from the approved P&Ps and the reasons for such deviations should be adequately justified and properly documented and approved.

New Fund Launches and Changes to Existing Funds

18. In respect of the launch or distribution of new funds, FMCs should consider the funds' investment objective and/or strategies, target investor segments, risk-return profiles, redemption terms and liquidity tools. They should also consider the service providers' experience and expertise, controls, systems and infrastructure, and the legal and regulatory requirements. Where models and their outputs are used in selecting investments and/or managing the associated risks, FMCs should perform due diligence on the models and understand the models' data requirements, assumptions and limitations, and perform model validations. For changes to existing funds, FMCs should review the impact of the changes on the abovementioned factors, as applicable, and communicate the change to relevant stakeholders, where necessary.

19. FMCs should ensure that relevant fund documents and marketing materials are appropriately prepared or updated, and that they are accurate and not misleading. Further, such fund documents should be reviewed and approved by the relevant approving authority and the assessments, discussions, and decisions should be documented to ensure accountability.

20. FMCs were generally observed to have formalised processes for new products, which will be documented in, among other things, a new fund launch checklist or template to be submitted to the relevant authority for review and approval. However, some FMCs did not evaluate the merits of the investment, and assess the investment's return and risk profile prior to the launch of the new fund. Smaller FMCs should also ensure that the portfolio managers for a new fund have adequate investment management experience to manage the fund, taking into account their experience with the relevant asset classes and investment strategy of the fund. Where service providers are concerned, FMCs should also assess the suitability of service providers to provide the services for the asset classes concerned (e.g. digital assets).

Investment Due Diligence

21. MAS expects that FMCs conduct sufficient due diligence on every potential investment. The due diligence process should include an assessment of the authenticity and suitability of the investment, and an evaluation of the reasonableness of its projected risk-return profile vis-à-vis the fund's stated investment objective and strategy using quantitative and/or qualitative methods. The nature and extent of due diligence required would depend on the specific investment/asset class. Therefore, FMCs should devote sufficient attention to understand the legal characteristics of each investment, along with the associated risks and expected cashflows from the assets.

22. Where investments are made indirectly (e.g. fund of funds), FMCs should assess the governance structure, competency and expertise of the entities directly managing the underlying investments, to have a more comprehensive understanding of the associated risks.

23. To the extent that FMCs rely on third-party information advice, opinions and/or reports, they should have a clear understanding of the underlying assumptions, methodology and basis behind them and maintain sufficient means and expertise to assess and where appropriate, challenge the conclusions presented. FMCs are reminded that they remain accountable and have the responsibility to make informed decisions based on the information obtained. FMCs should also ensure that investment recommendations are approved by the relevant approving authority, and documentation of due diligence performed should be properly maintained for audit and accountability purposes.

Ongoing Monitoring of Investments

24. MAS expects FMCs to put in place appropriate frameworks, procedures, controls and systems to support the ongoing monitoring and management of funds' investments and their appointed service providers. FMCs should adopt a structured and systematic approach to identify, monitor and assess: (1) material risks affecting the funds' performance and risk profile, including market, credit, counterparty, liquidity and operational risks, (2) relevant developments concerning the funds' underlying investments, such as changes in macroeconomic conditions, industry trends, issuer/borrower-specific events and regulatory developments, and (3) performance and resilience of the service providers, including fund administrators, custodians, investment managers, and other outsourced parties.

25. Where models and their outputs are used for ongoing monitoring and risk management, FMCs should put in place robust procedures and controls to ensure that the models' assumptions, inputs and outputs remain valid, appropriate and reliable over time. This includes implementing ongoing monitoring of model performance, conducting periodic validation and back testing, and promptly addressing any deficiencies or limitations identified. Any overrides or suppression of model outputs should be subject to appropriate oversight and governance. The circumstances under which such actions are taken and the rationale for doing so, should be appropriately documented and approved by the relevant approving authority. In situations where greater reliance is placed on human judgement, FMCs should ensure that such decisions are supported by a transparent decision-making framework, with proper accountability and audit trail in place.

26. FMCs should ensure that there is sufficient clarity on the matters requiring reporting and escalation to the relevant approving authority. Documentation of ongoing monitoring efforts (including reviews of documents or inputs from third-party service providers), discussions and decisions should be systematically maintained to demonstrate rigour in the monitoring process and ensure accountability.

27. FMCs should provide information to investors that accurately reflect the current state, nature and types of risks borne by the fund, to ensure a clear understanding and enabling informed decision making.

IV. Conclusion

28. In conclusion, the Information Papers set out MAS' supervisory expectations in relation to the valuation practices and risk management practices of FMCs. FMCs should glean from the

observations, the better observed practices and the areas of improvement set out in the Information Papers, and consider reviewing and addressing any deficiencies in their own governance structures, frameworks, P&Ps and internal controls.

29. Please feel free to reach out if you have any queries on the abovementioned updates.

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