

## Fund Finance Friday



### NAV Facility Valuation Challenge Rights

November 14, 2025



By **Susan Bumgardner**  
Associate | Fund Finance

In the context of NAV facilities, one item that we often see heavily negotiated is the lender's right to challenge the borrower's valuations of its investment portfolio. In this article, we will explore a few key aspects of the lender's valuation challenge rights and how we typically see these points negotiated between lenders and borrowers in credit facility documentation. For purposes of this article, NAV loans refer to loans to private equity funds that are underwritten based on the value of the assets of such private equity funds.

NAV facilities typically measure risk level using the ratio of the loan principal to the value of the eligible assets supporting the borrower's loan obligations (the "LTV Ratio"). Credit facility documentation for NAV loans generally include mandatory prepayments, cash sweep requirements, financial covenants and events of default that are tied to the borrower maintaining certain LTV Ratios. Given the importance of asset valuations in these facilities, lenders are understandably focused on ensuring that reported asset valuations from borrowers are accurate and up-to-date. The valuation challenge right is one tool that lenders can use to address any concerns that may arise in connection with this reporting.

As discussed in a [previous article](#), common asset valuation approaches differ between loans to primary private equity funds ("Primary Facilities") and loans to secondary private equity funds ("Secondary Facilities"). Primary Facilities typically use the values that the borrower assigns to its private company investments on its own books and records. Lenders will diligence the borrower's valuation policies prior to closing of the facility to get comfortable with those policies and will include restrictions in the loan documents for any changes to the borrower's valuation policies. Secondary Facilities, on the other hand, commonly use the lesser of the value of the interest provided to the borrower from the underlying fund and the value that the borrower has assigned to the interest on its own books and records (which value will then be adjusted to account for the borrower's capital contributions to the underlying fund and distributions from the underlying fund to the borrower, each since the date of reporting). This "lesser of" approach is helpful to prevent the asset from being valued based on the value reported by the underlying fund where the borrower's own valuation policies require the asset to be written down, or from being valued at, e.g., cost of acquisition where the underlying fund reports a lower valuation.

Given that valuation reporting is typically provided by the borrowers on a quarterly basis, generally well beyond the end of the applicable fiscal quarter (and even longer with respect to Secondary Facilities given that the borrowers must wait to receive valuations from the underlying funds), market conditions may have changed by the time the LTV Ratio is updated to reflect the most recent valuation reporting. Additionally, market conditions generally may have changed that might bring into question whether a borrower's underlying sponsor's approach to valuation in the first place is still accurately capturing the value of the relevant investment. Valuation challenge rights can help lenders make certain that asset valuations reflect any material changes in the asset's value in these circumstances. Probably the best relatively recent example of this is the first few months of the COVID pandemic, during which there was a general industry-wide concern that asset valuations may not reflect current market conditions. Without the ability to challenge those valuations, a lender could potentially have been required to provide additional advances based on an LTV Ratio that did not reflect real-world market conditions. Lenders may also prefer to have a valuation challenge right where regular independent valuations are not required pursuant to the borrower's valuation policies (or where those policies only provide for a portion of the investment portfolio to be subject to independent valuations).

Below are a few key items that we often see negotiated in credit facility documentation for NAV loans in connection with valuation challenge rights.

### Triggers and Frequency

The frequency with which a lender may challenge a borrower's reported asset valuation and what triggers may permit a lender to make an asset valuation challenge will vary from deal to deal. Lenders may negotiate to have a valuation challenge right at all times, on a periodic basis or upon the occurrence of certain triggers (or any combination thereof).

Lenders may also have periodic valuation challenge rights (for example, lenders may be permitted to challenge reported valuations once per calendar quarter, a certain number of times per year, etc.). However, lenders and borrowers often agree to allow additional valuation challenges following a default under the credit facility. These limitations may also be disappplied to the extent that a valuation is challenged and the new valuation is found to be materially lower than the reported value or if the new valuation would result in different treatment under the credit agreement (such as a higher percentage of cash sweep) (such valuation, a "Successful Challenge Valuation").

Alternatively, lenders may negotiate for valuation challenges to be triggered by events of default, breach of certain financial covenants, such as LTV Ratio breaches, or an asset's reported value changing from its most recently reported value by an agreed percentage.

### Consultation Periods

In some instances, borrowers may negotiate to include a period of time for consultation with the lenders before any formal valuation challenge process begins or any third party valuation agent is engaged. These consultation period limitations should be negotiated carefully because if the consultation period is too long, any updated valuations may only be received shortly before new valuation reporting is due from the borrowers. Borrowers may also wish to negotiate a time limit after the lenders receive required reporting within which the lenders may initiate a valuation challenge or within which a valuation challenge must be completed. These temporal limitations should also be carefully reviewed to avoid agreeing to a timeline that is too short for a valuation agent to provide its valuation report.

### Scope

Typically, lenders may challenge the reported valuation for certain assets in the asset pool or the entire asset pool, and the permitted scope will be pre-agreed in the credit facility documentation (e.g., challenge rights may be limited to only assets that do not have available market pricing).

Additionally, parties may negotiate limits to what valuation methodologies may be used for purposes of the challenge (e.g., limiting to the methodology used by the borrower or underlying fund to value the assets in connection with the initially reported valuation or other certain common valuation approaches, such as discounted cash flow analysis, price-to-earnings market multiples, and/or any relevant market pricing data).

### Successful Challenge Valuation Duration

When a valuation challenge has resulted in a Successful Challenge Valuation, such Successful Challenge Valuation will be used for purposes of calculating the LTV Ratio for a negotiated time period. Often, this time period will extend beyond the existing quarterly reporting period. The extended time period avoids quickly reverting to the same initial borrower valuation following the exercise of valuation challenge rights.

### Who Can Challenge?

In a syndicated credit facility where there is more than one lender, each lender may have the right to dispute the reported asset valuation, but more commonly the administrative agent will have the right to challenge the valuation, or the valuation challenge right will require a certain percentage of lenders to vote for the valuation challenge.

### Third Party Valuation Agents

In order to address lender concerns about lack of independent asset valuations, we commonly see agreements to appoint a third party valuation agent. Often, the lenders and borrowers pre-agree a list of approved valuation agents and the lenders can choose from this list upon exercising valuation challenge rights.

Lenders may also negotiate the ability to value positions themselves in connection with a valuation challenge. Where this approach is used, lenders may be required to provide supporting evidence of their valuation to the borrowers upon

request and is more common where the lender may have significant expertise with a specific market or asset class.

### Borrower Counter-Challenge Rights

Borrowers may also wish to negotiate for the right to counter-challenge where a lender's valuation challenge has resulted in a Successful Challenge Valuation. The lenders and borrowers will agree in the credit facility documentation which values will be used to calculate the LTV Ratio if the counter-challenge results in a different valuation than the Successful Challenge Valuation. The lenders and borrowers may agree to use the borrowers' valuation if the difference between the two valuations exceeds a certain materiality threshold, or the lenders and borrowers may agree to use the median of the two valuations to calculate the LTV Ratio.

### Who Pays?

When a third party valuation agent is engaged, lenders and borrowers will negotiate how costs will be shared. While it is common for borrowers to reimburse lenders for expenses incurred in administering loans, borrowers often negotiate to put some limits on these expenses for valuation challenges. For example, the parties may agree to limit the borrower's obligation to cover these expenses to a number of valuation challenges during a specified period of time (and may only be required to pay for any additional valuation challenges following a default under the credit facility) or alternatively, borrowers may only be required to pay for any third party valuation that results in a Successful Challenge Valuation.