

Private Credit Series

Beyond the Valuation: Building a Defensible Framework for Private Credit Managers

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The private credit market continues to evolve as fund structures expand, retail participation broadens and secondary market activity develops. At the same time, questions regarding alignment between reported valuations and underlying credit fundamentals have contributed to increased focus on valuation governance documentation and process integrity.

As investors, auditors, regulators and boards place greater scrutiny on private market valuations, managers are increasingly expected to support not only valuation conclusions, but also the governance, documentation and oversight frameworks underlying those conclusions.

In the current environment, stakeholders increasingly evaluate valuations in the context of the framework supporting them.

Building that framework often involves coordination across multiple disciplines. Independent valuation analysis remains fundamental, while governance, technical accounting, financial reporting and documentation considerations continue to have an important role. In practice, valuation specialists and other professional advisors may work in tandem to help managers develop valuation frameworks that are both technically grounded and operationally sound.

Drawing on the combined experience of Valuation Research Corporation's (VRC) valuation professionals and PKF O'Connor Davies specialists in valuation governance, technical accounting, operational due diligence and financial reporting, this article explores several developments shaping expectations for valuation oversight in private credit and outlines five key building blocks of a defensible valuation framework. Each firm provides distinct services aligned with its respective professional standards.

Why Valuation Governance Is Receiving Increased Attention

Several developments are influencing expectations around private credit valuations and increasing scrutiny of the frameworks supporting them. While valuation has long been a core component of private credit investing, the current environment requires managers to demonstrate not only how valuations are determined, but also how they are governed, documented and supported.

Investors, auditors and regulators are increasingly focused on the processes underpinning valuation conclusions, particularly as private credit expands into new structures and attracts a broader investor base. Against this backdrop, three developments are having a particularly significant impact on valuation governance.

i. Retailization and Liquidity Considerations

Historically, private credit was largely the domain of institutional investors with long investment horizons and a clear understanding of illiquid assets. Today, the growth of interval funds, non-traded business development companies (BDCs), tender-offer funds and other semi-liquid structures has broadened access to the asset class.

These vehicles have expanded participation in the asset class while introducing additional considerations related to liquidity and valuation. Managers are often required to balance investor liquidity expectations with portfolios comprised of inherently illiquid investments, reinforcing the importance of transparency and consistency in valuation processes.

SEC regulatory commentary has highlighted areas of focus, including liquidity management, valuation practices, conflicts of interest and investor disclosures, as private market products become more accessible to retail investors. As a result, valuation frameworks are increasingly expected to withstand scrutiny across a broader range of stakeholders and support clear communication around portfolio value.

ii. Increased Focus on the NAV Practical Expedient

Recent developments have also drawn attention to the use of the NAV practical expedient under U.S. Generally Accepted Accounting Principles (GAAP).

As secondary market activity in private assets continues to increase, regulators and standard setters are examining situations where investments are acquired at discounts to reported net asset value (NAV). In these circumstances, managers may need to assess whether observable transactions may represent data points relevant to fair value conclusions.

This issue highlights an important reality: valuation analyses often intersect with technical accounting requirements.

Managers must be prepared to support not only their valuation methodology, but also the accounting conclusions and documentation that support reported fair values. In practice, we see managers devote increasing attention to the intersection of valuation and technical accounting, particularly where secondary market transactions, discounts to NAV, or complex fund structures introduce additional judgment. These situations often require close coordination between valuation specialists and technical accounting advisors to develop supportable fair value conclusions.

A defensible framework requires a coordinated approach that incorporates valuation expertise, technical accounting knowledge and robust supporting evidence.

iii. Bridging the Gap Between Public and Private Markets

Private credit valuations have historically exhibited lower volatility than public market securities. This is largely a function of market structure.

Public markets benefit from continuous price discovery through active trading. Private markets, by contrast, often rely on periodic valuation analyses, limited observable transactions and longer investment horizons.

While these differences are expected, they place greater emphasis on governance and process. Stakeholders increasingly want to understand how managers incorporate changing market conditions, evolving credit fundamentals and observable market evidence into their valuation analyses.

A defensible framework should demonstrate that valuation methodologies remain calibrated to market conditions and continue to reflect market participants' assumptions.

What Stakeholders Are Looking For

Across the private credit landscape, scrutiny is increasingly focused on several core components of the valuation process:

- Independence of the valuation process
- Consistency of valuation methodologies
- Quality and completeness of supporting documentation
- Governance and oversight procedures

While valuation conclusions remain important, investors, auditors and regulators are placing increasing emphasis on the process used to develop those conclusions.

Managers that invest in strong governance frameworks may be better positioned to navigate market volatility, respond to audit inquiries, address regulatory questions and maintain stakeholder confidence in reported values.

Key Components of a Defensible Valuation Framework

1. Establish a Comprehensive Valuation Framework

A written valuation policy remains the foundation of a strong valuation program, but it should form part of a broader valuation framework rather than a standalone compliance document. Effective frameworks often:

- Define valuation methodologies by asset type
- Establish valuation governance and approval procedures
- Clearly assign responsibilities for preparation, review and oversight
- Address distressed, illiquid and complex situations
- Define escalation procedures and methodology override protocols
- Incorporate calibration and back-testing requirements
- Establish standards for documentation and supporting evidence

Valuation frameworks are generally reviewed periodically to reflect portfolio complexity, market conditions and evolving regulatory expectations.

A well-designed framework should be sufficiently robust to adapt to these developments while maintaining consistency and transparency.

2. Strengthen Governance and Independent Oversight

Governance has an important role in supporting defensible valuation conclusions and the broader valuation framework. As portfolios become more complex and transactions between affiliated vehicles receive greater scrutiny, independent challenge and oversight become increasingly important. Effective governance helps demonstrate that valuation conclusions are subject to appropriate review and are not unduly influenced by investment performance objectives.

Common practices may include:

- Independent valuation committees
- Clear separation between investment teams and valuation oversight functions
- Documented challenge and review procedures
- Consistent application of methodologies across portfolios
- Periodic independent assessments of valuation processes

Many managers also engage external advisors to provide additional expertise, independence and perspective. PKF O'Connor Davies provides operational due diligence, governance and financial reporting advisory services to assist managers in evaluating whether valuation governance structures, oversight processes and documentation practices are aligned with industry expectations and capable of withstanding investor, audit and regulatory scrutiny.

3. Anchor Valuations to Observable Market Evidence

While private credit investments may not benefit from the same level of price transparency as public markets, managers should seek to ground valuations in observable market evidence where available. As investors, auditors and regulators place greater emphasis on supportability, valuations that rely heavily on unobservable inputs without sufficient market corroboration may receive increased scrutiny.

Periods of market volatility can amplify differences in valuation approaches and assumptions. In these environments, it becomes increasingly important to demonstrate how current market conditions, comparable transactions and evolving credit fundamentals are incorporated into the valuation process.

Key considerations may include:

- Prioritizing observable market inputs
- Regularly reassessing discount rates, spreads and assumptions
- Benchmarking against comparable transactions and market evidence
- Conducting scenario analysis for distressed or complex investments
- Performing periodic calibration and back-testing exercises

Independent valuation professionals can provide valuable market insight and benchmarking support, particularly for difficult-to-value assets or complex capital structures. VRC valuation professionals assist managers in assessing market participant assumptions, benchmarking valuation inputs and evaluating how changing market conditions may be reflected within the broader valuation framework.

4. Prioritize Documentation and Supportability

In many cases, valuation challenges arise not because a conclusion is unreasonable, but because supporting documentation is incomplete or inconsistent.

Documentation is often a key factor in whether a valuation conclusion is accepted or subject to challenge.

A defensible framework should provide a clear record of:

- Key assumptions and judgments
- Alternative scenarios considered
- Sources of market data
- Governance review and challenge procedures
- Methodology selections and any changes applied
- Supporting evidence available at the valuation date

Documentation should be prepared with auditors, investors, regulators and valuation committees in mind. It should clearly demonstrate not only the conclusion reached, but also the process employed to arrive at that conclusion, including how key judgments and inputs were evaluated.

5. Leverage Independent Expertise Across Disciplines

As private credit markets evolve, valuation oversight often involves multiple disciplines.

Independent third-party valuation professionals can provide technical depth in valuation analyses, market benchmarking and methodology support, while also contributing an additional layer of objectivity. As valuation cycles in some structures move beyond a quarterly cadence to align with monthly or daily fund subscription and redemption activity, internal teams may face capacity constraints or require additional specialized expertise to value illiquid private credit assets.

However, valuation expertise alone may not address every challenge managers face. Technical accounting considerations, valuation governance, financial reporting requirements, operational controls and stakeholder scrutiny often require additional support from specialists with complementary expertise.

By combining independent third-party valuation expertise with governance, technical accounting and operational diligence capabilities, managers can strengthen the overall framework supporting valuation conclusions. Increasingly, private credit managers are seeking integrated support to address not only valuation methodology, but also the governance, reporting and documentation processes that support those conclusions.

Looking Ahead

Valuation governance extends beyond the development of a reasonable estimate of value. It is about establishing a defensible framework that supports valuation conclusions through robust governance, independent oversight, consistent methodologies and comprehensive documentation.

As private credit continues to evolve and attract increased attention from investors, auditors and regulators, managers should view valuation as one component of a broader governance framework rather than an isolated quarterly exercise.

Organizations that proactively strengthen valuation governance may be better positioned to navigate complexity, respond to scrutiny and support confidence in reported values.

How VRC and PKF O'Connor Davies Support Private Credit Managers

Building a defensible valuation framework often requires expertise across multiple disciplines.

VRC delivers independent valuation services for private market portfolios, including analyses across equity, debt, structured credit, asset-based finance, real assets and complex securities. VRC's specialized direct lending and private credit team has deep experience in credit underwriting, capital structures and sector-specific performance drivers. By partnering with fund managers, valuation committees and boards, the firm enhances efficiency, strengthens documentation and increases transparency across the valuation process.

PKF O'Connor Davies complements these capabilities through valuation governance assessments, operational due diligence, technical accounting support, fair value advisory, audit readiness assistance and broader financial reporting support.

Together, these services help private credit managers strengthen the processes, controls and governance supporting their valuation conclusions and build greater confidence among investors, auditors, boards and regulators.

Contact Us

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