



OMNIGENCE ASSET MANAGEMENT

**Eliminating PE NAV  
Distortion: How \$1 Par  
Pricing and Cash Sweeps  
Improve Transparency  
and Alignment**

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## EXECUTIVE SUMMARY:

Traditional private equity structures rely on periodically marked Net Asset Values (NAVs), which can create governance challenges, distort asset allocation models, and obscure real performance, especially in volatile or illiquid markets. This white paper presents a structural alternative: a \$1 par pricing model with no reliance on NAVs, where all distributable cash flows are swept to investors. This model prioritizes realized economic performance over paper gains and enhances alignment, liquidity, and transparency for institutional allocators. This approach is gaining traction as it eliminates NAV smoothing, simplifies risk management, reduces bid-ask spreads in secondaries, and improves portfolio construction clarity. It is best suited for cash-generative strategies such as lower mid-market consolidation, income-oriented secondaries, and preferred equity structures.

## INTRODUCTION TO THE NAV PROBLEM IN PRIVATE EQUITY:

Private equity was designed for long-term, patient capital, but the industry's reliance on subjective, lagged NAVs introduces a persistent tension between accounting representation and economic reality. Especially during drawdowns or illiquid market environments, GPs often resist marking down assets, creating artificially stable or inflated NAVs that mislead asset allocation models, distort portfolio construction, and obscure true performance. The result is mispriced secondaries, governance challenges, and fund performance that can diverge materially from economic outcomes. A 2024 Preqin study found that 43% of LPs believe GP-reported NAVs are materially overstated during market stress, and 57% expressed concern that stale marks delayed rebalancing decisions during the 2022–2023 correction. NAV smoothing, deliberately or structurally, has become endemic, and pension plans are rethinking how to access private equity exposure without compromising transparency or governance integrity.

## STRUCTURAL SOLUTION:

A \$1 par unit with no NAV and full, non-discretionary cash sweeps is a potential solution. Rather than relying on subjective NAV updates, this alternative structure allows investors to enter and exit the vehicle at a fixed par price (e.g., \$1/unit) and instead receive all net distributable cash flows (income + realized gains) through non-discretionary cash sweeps. The key elements of this model include:

- Fixed \$1 par entry and redemption price
- No reported NAV or internal valuation fluctuations
- All free cash flow swept to investors monthly or quarterly
- Unrealized gains retained until monetized

This structure fundamentally reorients the vehicle's economics around actual cash returns, not paper appreciation.

## OVERALL ADVANTAGES:

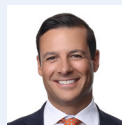
This structure increases transparency, alignment and return clarity.

- True Economic Returns Over Paper IRRs. The cash sweep model ensures that investors are paid only from realized performance. There is no incentive or ability to inflate returns through unrealized gains. Performance is measured in real-time, through cash-on-cash returns (DPI) and annualized yield, not paper IRRs or TVPIs. According to Cambridge Associates, DPI now accounts for over 55% of realized value in mature PE portfolios (>8 years), yet many LPs still anchor on IRR, despite its sensitivity to interim valuations and exit timing.
- Removes NAV-Based Mispricing and Gaming. Because investors always transact at \$1, the manager has no incentive to manipulate NAV to influence subscriptions, redemptions, or fund rankings. This also reduces bid-ask spreads in secondaries, since pricing is anchored to cash flow expectations rather than discounted or inflated NAVs.



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Recent data from Setter Capital shows that secondary market discounts to GP-reported NAVs widened to 17% in 2023, largely due to concerns about stale or optimistic valuations.

- Simplifies Portfolio Rebalancing. Fixed unit pricing eliminates denominator effects as plan sponsors no longer see artificial increases or decreases in portfolio weights due to NAV swings. This simplifies rebalancing, stress testing, and regulatory reporting. In a 2024 survey by State Street, 38% of pension CIOs cited denominator effect distortions as a top challenge in PE portfolio management post-2022.

### **GOVERNANCE ADVANTAGES FOR FIDUCIARIES:**

Traditional NAV-based private equity structures create significant governance friction for institutional investors. Subjective valuations, inconsistent reporting methodologies, and complex audit trails introduce recurring fiduciary challenges, especially during periods of market stress. By contrast, the \$1 par + cash sweep model streamlines governance and reduces risk across multiple dimensions:

- Eliminates Valuation Conflicts: NAV disputes between GPs, auditors, valuation committees, and consultants can absorb significant time and introduce fiduciary liability. With no interim NAV marks, the par model bypasses these debates entirely, relying instead on audited financials and realized performance. This simplifies internal oversight and reduces exposure to valuation-related litigation or audit exceptions.
- Enhances Fiduciary Clarity: Under this structure, returns are reported in real time via distributions (DPI and annualized yield), aligning economic performance with what LPs actually receive. This removes the ambiguity of IRR-based approaches and helps fiduciaries meet transparency obligations to boards, beneficiaries, and regulatory bodies.
- Reduces Oversight Burden: Without the need for quarterly NAV reporting, subjective discount rates, or complex fair value models, the governance burden on staff, consultants, and investment committees drops materially. Fiduciaries can focus on evaluating realized outcomes and cash-generating potential, rather than debating interim marks.
- Improves Auditability: Distributions are grounded in actual cash flow, not estimated appreciation, creating a cleaner audit trail and simplifying both internal and external audits. This model also minimizes back-and-forth with auditors and reduces valuation-related footnotes or compliance disclosures.
- Strengthens Alignment and Accountability: Since performance fees and carry (if structured appropriately) are tied to realized returns, not NAV accretion, the model reduces agency risk and aligns manager compensation with investor outcomes. This mitigates headline and reputational risk associated with “phantom gains” or paper-driven carry payments.

### **USE CASES:**

This structure fits exceptionally well in many contexts:

- Cash-Flowing Lower Mid-Market PE: Serial, evergreen consolidation strategies, especially those with high monthly EBITDA generation and strong DPI potential.
- Secondary and Income-Oriented PE: Strategies with built-in yield, such as preferred equity, structured credit, or income-oriented secondaries.
- Pension Plan Liquidity Sleeves: Par or pension investors seeking predictable distributions and low-volatility PE exposure aligned with benefit obligations.

### **CONSIDERATIONS AND TRADEOFFS:**

This structure does not fit certain strategies.

- Growth-oriented PE May Not Fit: Venture capital or deep value turnaround strategies with long duration and back-ended return profiles are less compatible.

- Requires Consistent Cash Flow: Portfolio companies must generate consistent and distributable cash flows to support ongoing sweeps.
- Incentive Realignment: Carried interest models may need adjustment to reward realized, distributable performance instead of NAV accretion. Some funds now use a “realization hurdle” (e.g., DPI > 1.0x) before carry is paid.

### NEXT STEPS FOR LPS:

Institutional allocators interested in evaluating or adopting the \$1 par + cash sweep model can consider the following phased approach:

- Pilot with Income-Focused Mandates: Start with a modest allocation to a cash-generative PE strategy, such as lower mid-market consolidation or structured secondaries, where DPI and yield are the natural drivers of value. Use this as a testing ground for performance tracking, governance processes, and operational mechanics.
- Include in Liquidity Sleeve Planning: Integrate the structure into your pension plan’s liquidity sleeve or short-duration alternatives bucket. It offers steady distributions and fixed-value simplicity without compromising long-term private market exposure.
- Revise Benchmarking Approaches: Shift performance evaluation from IRR/TVPI to cash-on-cash (DPI) and annualized yield metrics. This enables a more transparent comparison of cash-generative PE vs. yield-focused credit or infrastructure.
- Engage GPs on Structural Flexibility: Where alignment exists, request GPs to consider sidecar vehicles or new funds using the par/cash-sweep approach, especially for existing high-DPI strategies. LPs can also negotiate realization hurdles tied to DPI to encourage alignment with this model.
- Incorporate into Governance Policy: Update investment policy statements and internal reporting frameworks to allow for non-NAV-based valuation methods. Highlight how fixed pricing enhances compliance clarity, reporting efficiency, and liquidity management.

### CONCLUSION:

As institutional investors demand more transparency, liquidity, and alignment in private markets, the traditional NAV-based PE model is being reexamined. A \$1 par unit structure with cash sweeps eliminates NAV distortion and restores private equity’s economic fundamentals:

Feature	Traditional NAV-Based PE	\$1 Par + Cash Sweep PE
Entry/Exit Pricing	Based on GP-determined NAV	Always \$1/unit
Valuation Frequency	Quarterly (subjective)	Not applicable
Distribution Basis	Discretionary or reinvested	100% of net distributable cash swept
Return Metric	IRR / TVPI (includes unrealized)	DPI / Yield & Gains (realized only)
Denominator Risk	High (NAV-based volatility)	None (fixed unit value)
Governance Burden	High (valuations, audits, disputes)	Low (cash accounting)
Secondary Pricing	Often discounted vs. NAV	Typically par or yield-based

For pension plans and long-term allocators seeking dependable, real returns—not just accounting optics—this model may represent the future of operationally-aligned, investor-first private equity.

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