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Family Office NAV Facilities

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As Net Asset Value ("NAV") credit facilities continue to grow in popularity, we have seen a steady increase in non-traditional borrowers utilizing NAV loans, including family office borrowers. The term "family office" is used to describe structures established by ultra-high-net worth families to manage and grow their wealth. NAV facilities allow family office borrowers to unlock liquidity required to meet their needs without selling off investments. The purpose of this article is to explore a few key features that we often see in family office NAV facilities.

<u>Asset Portfolios</u>

One characteristic of family offices that sets them apart from traditional closed-end private investment funds is that family offices typically have broad mandates and thus invest in many different types of assets, (*e.g.*, real estate, private equity, private credit, venture, hedge funds, etc.). Because family office asset portfolios are dynamic in nature and may cover a broad scope of asset classes, eligibility requirements for an asset to receive borrowing base credit may be treated differently in these facilities than in NAV facilities with more static asset portfolios. Whereas it is common in facilities with static asset portfolios to require approval for individual assets to receive borrowing base credit, family office NAV facilities may instead forego the approval requirement, which may be cumbersome for a large actively managed portfolio, and instead apply robust eligibility requirements as well as robust concentration and strategy borrowing base limits to make sure that the portfolio that a lender is underwriting does not fundamentally change over time.

<u>Intercompany Loans</u>

Because a family office is used broadly to manage the family's wealth, there is often a need for family office NAV facilities to permit borrowers to incur other indebtedness, including intercompany/affiliate loans. Intercompany loans are common features of family office facilities due to the nature of these structures. If a family office borrower has existing debt pursuant to intercompany loans, lenders may require intercompany creditors to enter into subordination agreements pursuant to which such intercompany creditors agree that the obligations of the family office borrower owing to such intercompany creditors (the "<u>Subordinated Debt</u>") shall be subordinated to the obligations of the family office borrower owing to the lenders. Lenders may also set limitations on Subordinated Debt, including (i) quantitative limitations, (ii) requiring any Subordinated Debt to be unsecured or restricting liens in connection with Subordinated Debt over certain assets or (iii) requiring Subordinated Debt to be restructured as equity.

In some instances, lenders may permit a family office borrower to make payments on Subordinated Debt while the NAV facility is still outstanding subject to certain restrictions, including requiring such family office borrower to be in compliance with all facility obligations at the time of such payment, including compliance with loan to value ratio limits.

<u>Performance Guarantees</u>

In order for lenders to ensure repayment on a family office NAV facility, it is not uncommon for such lenders to require an entity in the deal structure to enter into a performance guaranty in favor of the lenders wherein such entity (a "<u>Guarantor</u>") guarantees payment of the obligations by the family office borrower. These performance guarantees are often provided by the parent company of the borrower or an ultra-high-net worth individual, and there may be financial covenants tied to creditworthiness of the Guarantor. In some cases, these guarantees are contingent upon the borrower becoming insolvent or the borrower breaching certain key covenants in the credit facility documentation relating to the collateral, liquidity and other covenants that may impact the borrower's ability to repay the obligations.

Where the Guarantor is an ultra-high net worth individual, these credit facilities may include key person events tied to the death, incapacity or certain bad acts of the Guarantor. These provisions are typically events of default under the credit facility documentation, and any applicable cure period may require the borrower to submit a succession plan to replace the Guarantor under the credit facility.

Other Notable Features of Family Office NAV Facilities

There are several notable features of family office NAV facilities that differ from traditional NAV facilities. For example:

- **Evergreen Funds**: Unlike private equity fund borrowers, family office borrowers are typically evergreen funds with perpetual investment periods, offering greater flexibility to acquire investments without investment period limitations.
- **Valuation of Assets**: Given that family office borrowers do not always obtain audited financial statements, lenders may require the facility documentation to include a right of the lender to engage an independent auditor to value and verify the underlying assets in connection with calculating the borrowing base.
- **Use of Proceeds**: These facilities often require broad flexibility with respect to use of proceeds, and family office borrowers may use these facilities to upstream proceeds in connection with investments by related entities.

Family Office NAV Facilities Going Forward

We expect to see continued increase in family office NAV facilities as family offices continue to seek alternative leverage options and/or look for alternative sources of liquidity that lend well to bespoke structures and credit facility documentation tailored to the unique needs of each family office.