

# Fund Finance Friday



## The Liquidity Lifeline - How Subscription Lines Help BDCs and Interval Funds Navigate Redemption Pressures

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By **Chad Stackhouse**  
Partner | Fund Finance



By **Karina Velez**  
Associate | Fund Finance

Subscription credit facilities have long been a staple of traditional private equity fund finance, but their application to business development companies (“BDCs”) and interval funds deserves fresh attention, particularly now, as the private credit market confronts a liquidity environment that few participants anticipated even twelve months ago. With redemption pressures mounting across privately-held BDCs and interval fund structures, the subscription line has quietly reemerged as one of the most practical liquidity tools available to fund sponsors.

This article explores the basics of how subscription lines to BDCs and interval funds address withdrawals, why a fund benefits from maintaining a subscription credit facility, and what additional sources of comfort lenders should, and increasingly do, look for when underwriting these credits.

### The Basics: BDCs vs. Interval Funds

BDCs and interval funds are both closed-end vehicles regulated under the Investment Company Act of 1940, but they operate under distinct leverage frameworks.

A BDC invests primarily in the debt and equity of middle-market companies. Following the passage of the Small Business Credit Availability Act in 2018, BDCs may elect to lower their asset coverage requirement from 200% to 150%, effectively permitting up to a 2:1 debt-to-equity leverage ratio, up from the previous 1:1 limit. This expanded capacity has driven meaningful growth in the BDC credit facility market.

Unlike a traditional closed-end fund, an interval fund continuously offers shares at NAV pricing and commits to periodically repurchase a stated percentage of outstanding shares (typically between 5% and 25%) at regular intervals, most commonly quarterly. Interval funds are subject to a 300% asset coverage requirement under the 1940 Act, meaning total assets must equal at least three times outstanding borrowings, which effectively caps debt at one-third of total assets (a roughly 0.5:1 debt-to-equity ratio). This is considerably more restrictive than the BDC leverage framework but still accommodates meaningful borrowing capacity when structured thoughtfully.

What unites both structures is their ability to raise capital through subscription programs. Uncalled investor commitments form the foundation of the borrowing base for a subscription credit facility, making these vehicles natural candidates for subline support.

### How Subscription Facilities Address Withdrawals

A key distinction between BDCs and interval funds lies in how they manage investor liquidity.

BDCs typically offer periodic tender offers, often capped at around 5% of outstanding shares. These tender offers are discretionary, as the BDC’s board retains the authority to reduce or suspend repurchases entirely, and many offering

documents expressly reserve this right. This discretionary gating mechanism is a meaningful structural protection for subscription lenders, because it means that even in a period of elevated redemption demand, the fund is not obligated to return capital to investors at a pace that would impair the lender's collateral base.

Interval funds, by contrast, are legally required to conduct periodic repurchase offers once the fund has adopted a fundamental policy setting the repurchase interval and the minimum repurchase amount. However, the board retains discretion over the amount of each repurchase offer (within the 5%–25% range), and the fund is required to maintain liquid assets sufficient to meet the full amount of any announced repurchase offer. From a subscription lender's perspective, this creates a predictable, limited liquidity obligation rather than an open-ended one. The lender can model the maximum periodic outflow and ensure that the borrowing base provides adequate coverage after accounting for the liquidity obligation.

For lenders, this distinction matters. BDCs present a more flexible, sponsor-driven liquidity model, while interval funds introduce a defined liquidity profile. In both cases, subscription facilities provide a mechanism to fund redemptions without forcing asset sales. Borrowing base dynamics also remain self-correcting, as investors redeem and their remaining commitments decline, borrowing availability under the credit facility correspondingly shrinks.

### **Why Funds Benefit from Having a Subscription Line in Place**

The current private markets environment has only increased the value of having a subscription facility in place. Private credit platforms are operating in a market where execution, speed, liquidity management, and investor confidence all matter more than ever. A subscription line gives sponsors a practical way to meet liquidity needs without forcing asset sales at unfavorable times or interrupting investment activity.

Just as importantly, it supports portfolio construction. Rather than holding excess cash to fund anticipated redemptions or capital needs, sponsors can preserve dry powder and deploy capital more efficiently. That can be especially valuable in private credit, where the ability to act quickly on attractive opportunities may be a meaningful competitive advantage.

### **Sources of Lender Comfort**

For lenders, the borrowing base remains essential, but it is only part of the analysis. A lender looking at a BDC or interval fund will also focus on the broader structure of the vehicle, including the quality and concentration of the investor base, the fund's gating and repurchase mechanics, the financial strength and reputational commitment of the sponsor, and the level of disclosure around portfolio performance and valuation. The regulatory framework under the 1940 Act also provides an important layer of discipline through reporting requirements, audited financials, and leverage limits.

### **Looking Ahead**

As BDCs and interval funds continue to grow as private credit platforms, subscription facilities are likely to become even more embedded in the core infrastructure supporting these vehicles. For sponsors, that means greater flexibility in managing capital and deploying it in new opportunities. For lenders, it means a credit product that remains attractive, but one that requires close attention to the underlying fund structure, investor liquidity mechanics, and sponsor support.