

CADWALDER

Popularity of Subscription Facilities Drives Changes for Global Investment Performance Standards

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The Global Investment Performance Standards (“GIPS,” or the “Standards”) published by the CFA Institute (“CFA”) have long been a set of self-regulated guidelines for investment managers, aimed at promoting standardized and ethical investment reporting to investors. The Standards, while voluntary, are immensely popular with both investors and investment managers. According to CFA, 84 of the top 100 asset managers have adopted the Standards and claim compliance for at least part, if not all, of their business. So what does this have to do with subscription finance?

The current Standards, published in 2010, are now stale. Since 2010, the use of subscription lines of credit has become widespread and, frankly, common for investment managers. Given the extended debate in the industry regarding the lack of transparency and consistency in subscription facility reporting over the past couple of years, the CFA took notice. CFA issued a new draft for comment in August 2018. The proposed new Standards would require: that GIPS-compliant managers disclose the purpose, size, and outstanding amounts of any subscription lines; that IRR calculations include the cash flows, values, and associated costs for the subscription line; and that managers disclose whether composite IRR reporting includes subscription line usage. The exposure draft also includes a requirement that the manager present investors with the composite since-inception money-weighted return both with and without including the subscription line activity.

The comment period on the exposure draft expired at the end of 2018. CFA expects to publish the final version on June 30, 2019, with an effective date for CFA-compliant managers of January 1, 2020. The comments are public and available for review on the CFA website (see link at the end of the article). There are quite a few familiar names in the list of commenters. Many commenters argue that managers should, at the very least, report the existence, usage, amount, and basic terms of any subscription line, but that the performance report should also reflect the actual investment returns. A requirement to report both the levered and unlevered returns could be confusing to investors and would be onerous to the managers, they say. Several of the commenters express the opinion that a subscription line is no different from any other use of leverage by the manager, so if there is a requirement to provide an unlevered report, it should be exclusive of all leverage of the fund, not just a subscription line.

On the other hand, a number of commenters indicate support for the additional reporting requirements. They take the view that such reporting would increase overall transparency and make it easier for potential investors to compare investment managers on an apples-for-apples basis.

Now that the commenting period is over, it will be interesting to watch for the final draft of GIPS to examine the changes to the exposure draft proposals based on the comments. By 2020, the result will likely become commonplace in the industry.

CFA, the provider of the well-regarded Chartered Financial Analyst Program, among other professional certifications, initially published the Standards in 1999. Given the 10-year gap since the last update to the Standards in 2010, it is likely that the 2020 Standards will remain in place for some time.

The full set of comments to the exposure draft can be found [here](#).

Problems with 'Promptly'

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In commercial arrangements under English law, it is vital that the times allowed for a party to perform its obligation are clear. This is especially true in facility/credit agreements and other financial contracts. Lack of clarity results in mismatched expectations between counterparties and uncertainty as to whether counterparties are in compliance with an agreement.

In an ideal world, a contract will specify precisely how much time is allowed for each obligation to be fulfilled or step to be taken. Wherever practicable, this should be the general approach in preparing agreements. Unsurprisingly, however, contracting parties are often reluctant to commit to hard deadlines for certain obligations which they consider to be less important in the context of the overall transaction. Hard deadlines bring certainty but also create the possibility of default resulting from minor delays beyond a party's control. Borrowers, in particular, are sensitive to this because a Lender's remedies for a default, regardless of the cause or severity of the default, usually include the ability to accelerate an entire facility.

For these reasons, it is common for contracts to specify that certain actions must be taken within less precise timeframes. Contracts, including the LMA standard templates, frequently state that actions must be taken "promptly," "as soon as is reasonably practicable," or "as soon as possible." Such terms are useful, but parties must be aware of the sometimes significant uncertainties that they create.

Where an obligation must be performed within a "reasonable time" or "promptly" or "immediately," the question of what precisely these expressions mean will, under English law, depend on the particular facts and circumstances. It is impossible to establish clear rules as to exactly what those terms will mean in practice. For example, courts have previously held that an action taken within four or five days was not taken "promptly," but also, in very different circumstances, that an action taken after almost two months was taken "promptly."

Nevertheless, parties should be aware of certain general principles:

- There is no material legal difference between "immediate" and "forthwith." Both mean that something must be done as soon as possible in the circumstances, with the nature of the act being taken into account.
- "Directly" means speedily, or at least as soon as practicable.
- "On" or "upon" may mean simultaneously with the related act, or within a reasonable time after it, according to the circumstances.
- "Within a reasonable time" does not impose any specific timeline.
- "Promptly," as above, can mean almost any period of time, depending on the particular circumstances.

Accuracy and certainty in relation to time periods are of particular importance in finance transactions. While it will not always be appropriate to specify absolute deadlines for every action to be taken under a contract, parties should be aware of the inherent uncertainties of many terms that are frequently included in their place so that appropriate decisions can be taken about what terms are appropriate to use.

The Triago Quarterly on Subscription Line Financing

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Triago, a private equity placement agent, portfolio sales agent and strategic advisor, last week published *The Triago Quarterly*, which included a round table “on subscription line financing abuse and what should be done about it.” The participants included Andrea Auerbach of Cambridge Associates, Gael Le Clec’h of CNP Assurances, Abhik Das of Golding Capital Partners, and Ben Griffiths of MUFG Investor Services. The primary “abuse” described in the article seems to be that certain funds are holding investments out on their subscription lines for longer periods to “inflate” their returns (although there was no mention of funds exceeding the tenor restrictions for borrowings agreed to with investors in their partnership agreements, so query how this is an “abuse”). The article is available [here](#).

Credit Funds Eye Fund Finance

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Credit funds, according to an article in *Private Equity International*, are increasingly interested in lending to funds. Rather than competing head-on with banks, the story is one of carving out a niche where expertise and returns align. Crestline Investors and Validus Risk Management are among the firms highlighted by *PEI*. Based on our book of business, we estimate that about 11% of U.S. fund finance facilities originated in 2018 paid margins of 200 bps or more over LIBOR. The full *PEI* article is available by subscription [here](#).

Private Debt Investor Article on Subscription Lines

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On February 1st, *Private Debt Investor* published an article titled “Walking a fine sub-line.” The article focuses on the growth of the private debt markets and the resulting growth of subscription finance. Jeff Johnston of Wells Fargo was quoted extensively. The subscription-required article can be accessed [here](#).

ING Posts Associate/VP Opening in London

- ING has opened a search for an Associate or VP in its Investment Industry Finance (IIF) Group. The job posting is available [here](#). The bank's IIF group originates and executes lending transactions to European funds and oversees the portfolio management of the existing book. The candidate should bring at least four years' experience in structuring funds finance transactions and an established track record in deal execution. Qualified candidates may contact Lester Deeble for more information at lester.deeble@ing.com.

Square 1 Bank Equity Funds Job Posting

- Square 1 Bank is looking for a Portfolio Analyst to join its Equity Funds Group in Venturing Banking in its Durham, NC office. The job posting is available [here](#). Square 1 Bank, a division of Pacific Western Bank, provides full-service financial services to entrepreneurs and their investors.

Commonwealth Bank of Australia Fund Finance Job Posting

- Commonwealth Bank of Australia is looking for a Risk Executive to join its Risk Management, Institutional & Business Banking division in its New York office to work on private equity transactions. The job posting is available [here](#).

SMBC Subscription Secured Finance Job Posting

- SMBC is looking for an Associate to join its Subscription Secured Finance department in its New York office. The job posting is available [here](#). SMBC's Subscription Secured Finance team provides fund finance to global private sponsors, manages lines of credit from origination to closing, and provides ongoing monitoring.

Cadwalader Seeks Fund Finance Associate

- Cadwalader's Charlotte and New York offices seek an Associate for the Fund Finance practice. Qualified candidates will have 3-7 years of experience in syndicated lending, commercial lending, leverage finance, fund formation, CLOs or other relevant experience. Candidates must possess excellent academic credentials and solid law firm or in-house legal experience as well. Anyone interested, please email Wes Misson directly at Wesley.Misson@cwt.com.

