

CADWALDER

Getting Personal — Lending to Fund Executives

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Funds in Europe are increasingly calling on their traditional subscription finance lenders for the purpose of providing credit lines to management and executives of the fund. In one form or another, these facilities have existed in the market for some time, but an increase in the size, number and lenders willing to make these facilities available is leading to an increased focus on their (often quite technical) requirements.

Although the structure used to implement executive facilities can vary, their purpose tends to primarily be financing capital calls made against the executives in their capacity as LPs in co-invest funds.

In general terms, these facilities provide financing for the payment of subscription amounts owed by the executives and are supported by security granted by the executives over their entitlement to receive distributions from the fund, often requiring these distributions to be paid directly into a secured account.

Depending on the timing and size of expected distributions, the security package may be enhanced by the executives providing additional collateral (in the form of cash or eligible securities) and, in some circumstances, other fund entities (such as the manager or GP) may be asked to provide security over that entity's entitlement to management or GP fees.

Each borrower will generally be subject to financial covenants – for example, where collateral over cash or securities is granted the executive may be required to ensure compliance with LTV coverage requirements.

The facility may be made available directly to the executives (with security being granted by the executive to the security agent (or lender, where the facility is bilateral)). In other cases, the lender may extend credit to a fund vehicle (often an SPV or limited purpose entity) that then on-lends the proceeds to the executives. In this case, a typical structure would require the executive to grant security to the SPV lender and the SPV lender, in turn, to grant security over its rights under that security to the security agent – effectively creating an upward "cascade."

As the loan is being made to an individual, there are some key considerations and due diligence matters that need to be resolved to ensure the facility is enforceable and that the making of the loans does not result in a breach of law. As you might expect, the covenants, representations and events of default also need to be tailored so as to be applicable to individuals rather than funds or corporates, and consideration will need to be given to executive departure provisions in the LPA – particularly in a "bad leaver" scenario.

In terms of due diligence, a primary concern is the application of consumer credit legislation to the facility, and an analysis of the relevant consumer credit legislation will require an understanding of the borrower and lender location as well as the location of any assets (such as accounts) that are subject to security (as well as any other factors that create a nexus to consumer credit legislation in a particular jurisdiction). It is unusual for a borrower, lender, the collateral and governing law of a facility to all be in the same jurisdiction, and so it may be necessary to consider the consumer credit requirements of more than one jurisdiction in connection with any one borrower or loan.

The consequences of failure to comply with consumer credit legislation vary across the jurisdictions and, for example, breach of the consumer credit requirements may result in the loan and/or security being unenforceable and/or a lender being subject to regulatory or criminal sanction. In some jurisdictions (particularly those regarded as "offshore" jurisdictions in the fund finance market), it may be that there is very limited consumer credit regulation (e.g., Jersey and Guernsey) or that the regime is more permissive than in "onshore" jurisdictions (for example, in our experience, the Luxembourg regime is easier to navigate in the context of these types of facilities than the regime in the UK). However, as mentioned above, the laws of more than one jurisdiction may be applicable to a loan to a borrower.

Structuring the facility as a loan to an SPV (with the SPV on-lending to the individuals) so as to avoid making a loan to an individual does not necessarily remove the need to consider consumer credit legislation as that SPV may, as lender, be subject to consumer credit requirements. Therefore, although it may reduce the risk of regulatory or criminal sanction for the bank lender to the SPV, it does not solve potential unenforceability issues in respect of the loan and security between the SPV and the individual (over which the bank lender would ordinarily look to take cascading security as described above). In this context, lenders should also be mindful of aiding and abetting offences.

Another consideration is the application of privacy legislation to the transaction. GDPR can be relevant depending on the nature of the information provided by the individuals (particularly in security documents which may contain address, passport numbers, email and account information) and its anticipated use. It may be necessary for the fund and/or the lender to obtain GDPR consents from the individual borrowers.

In most cases, it is possible to structure the facility so that it is compliant with privacy and consumer credit legislation. Looking back at the last 12 months we have structured transactions for executives in jurisdictions across Europe, including Jersey, Guernsey, Luxembourg, Germany, Poland and the UK, as well as North America, and have seen, for example, reliance on high net worth exceptions and loans being exempt for being in excess of a certain amount. It is also possible that lenders (or affiliates) may have appropriate permissions in place to make consumer loans available.

Available exemptions may require third-party involvement (such as a third-party verification of high net worth status or there may be a requirement that individuals receive independent legal advice). These requirements can add to cost and may also lead to delays in implementing the transaction and so identifying the relevant consumer credit and privacy laws and identifying a structure that complies with these requirements as soon as possible in the life of a transaction is key.

2020 'Pink Book' Published

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By Michael Mascia
FFA Board Member

Global Legal Insights: Fund Finance 2020, commonly known as the "Pink Book," was published by Global Legal Group Ltd. (GLG) this week. This is the fourth edition of the guide, which includes 25 product-oriented chapters together with 19 jurisdictional updates. Many of the world's preeminent fund finance law firms contributed chapters, and I am extremely appreciative of their continuing support of, and contributions to, the book.

It is so cool how the fund finance legal community comes together each year to produce this resource for the market. Special thanks to GLG for their continuing support of our market; they do a sensational job. Each year, Rory Smith at GLG and I have tried to improve the book, adding chapters and contributors, and encouraging the contributors to cover new areas at greater depth. We hope the 2020 edition is a productive resource for your business. As always, we welcome feedback and suggestions on how the book should improve and evolve to remain relevant. An electronic copy of the book is available [here](#), and hard copies will be available at the 10th Annual Fund Finance Symposium in Miami in February.

London Fund Finance Team Authors Two Chapters in 2020 'Pink Book'

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By Jeremy Cross

This year the London Fund Finance team at Cadwalader authored two chapters in the 2020 Pink Book. The first chapter, being the "country" chapter for England and Wales, considers the role of English law in fund financings across Europe as well as the varied structures that have developed in the London market. The chapter looks back over the growth of the market since 2000 and also provides useful insights, current market data and possible future trends.

The second chapter, co-authored with Ian Weise at Investec, is titled: "The secondaries market: The rise of GP-led and preferred equity solutions." The chapter examines the recent rise in GP-led secondary deals and preferred equity structures, considers how these structures have evolved, and provides insight into how financing can be made available to support these structures and the evolving secondaries market.

The chapters are available on GLG's website [here](#).

The State of Play on Overcall Limitations

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By Michael Mascia
FFA Board Member



By **Wes Misson**
Partner | Fund Finance

Cadwalader provided a chapter in the 2020 Pink Book on current market trends on overcall limitations. The article is intended to be a complete resource for practitioners on all things overcall limitations: formulations of the various types in partnership agreements, data-based market prevalence, mitigants employed by lenders to reduce risk, commercial compromises making headway in the market, and partnership agreement innovations. The chapter is available on GLG's website [here](#).

Recommended Reading

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- *Bloomberg Businessweek's* "**Nobody Makes Money Like Apollo's Ruthless Founder Leon Black**" makes for an excellent read for students of private equity and financial history. The bio reminds us of the long list of Drexel Burnham Lambert alumni that includes the likes of Stephen Feinberg (Cerberus), Bennett Goodman (GSO), Josh Harris (Apollo), Mitch Julis (Canyon Partners), Ken Moelis (Moelis & Co.), Mark Atanasio (Crescent Capital) and so on. Maybe the definitive book on the Drexel culture and legacy has yet to be written.
- In its updated ***World Economic Outlook*** published this week, the IMF cited receding risks to the global economic growth outlook following a U.S.-China trade deal. At the same time, the fund downgraded its growth forecasts for 2020 and 2021.
- The IMF is not alone in its view: 62% of U.S. CEOs expect global growth to decline over the next 12 months, according to PWC's ***23rd Annual Global CEO Survey*** published this week. Only 27% of respondents reported being "very confident" in their prospects for revenue growth in 2020, a post-crisis low. We see a downgraded growth outlook and a move lower in rates as supportive to continued capital flows into private funds.
- Larry Fink is defending BlackRock's recent stance in elevating climate-related criteria in its investment processes, *Barron's*: "**Larry Fink Defends BlackRock's New Emphasis on Climate Change. What Investors Need to Know.**"
- Not entirely unrelated, index funds are either too passive, depending on your agenda, or dangerously influential given their sheer scale and common ownership of competitors. *Bloomberg Businessweek* recently recapped the ongoing debate in "**The Hidden Dangers of the Great Index Fund Takeover.**"

Fund Finance Hiring

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Fund Finance Hiring

Silicon Valley Bank is seeking to add a Director, Senior Associate and Associate to its London-based Global Funds Banking Team.

More information and the link to apply can be found [here](#) (use the following job numbers to find the roles: Director – 5362; Senior Associate – 5314; Associate – 5313).

Other opportunities within the Global Funds Banking practice across the US are also open, details of which can be found [here](#).

