Funds Finance

An introduction to funds finance

Czech Private Equity & Venture Capital Association

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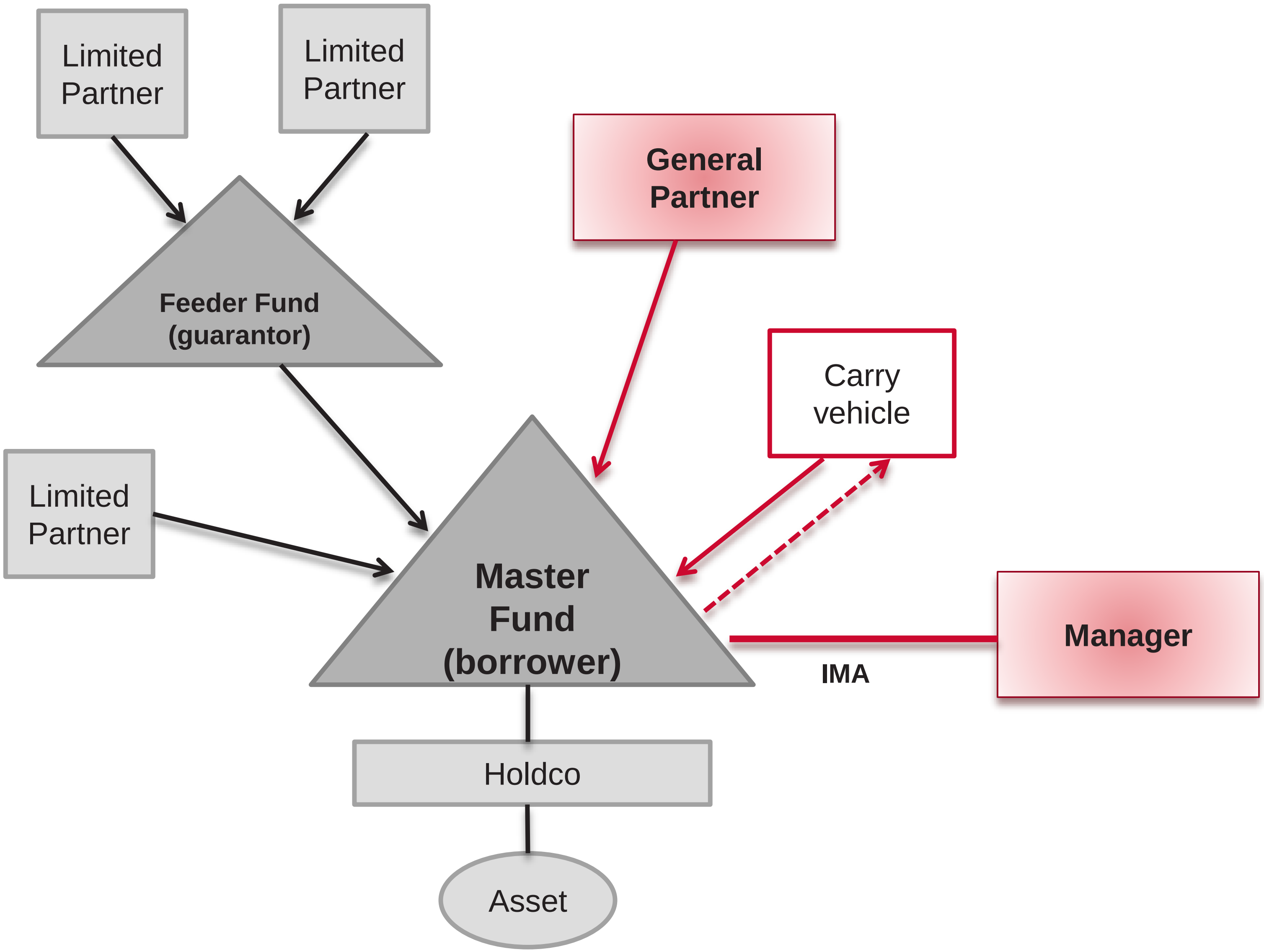
1. What is a private equity fund?

- Why are they used?
- What do they do?
- Which jurisdictions are they set up in and why?
- What is the life cycle of a private equity fund?
- Overview of the private equity market

Basic fund structure – capital call facility



2. Commercial drivers – why funds do these deals

- Administrative convenience
- Speed of execution
- FX reasons
- IRR enhancement
- Specific deal related reasons when additional financing needed

3. Commercial drivers – why banks do these deals

- Safe financing with healthy upfront fees if institution doing large quantums
- To get closer to the fund for underlying deals
- To get ancillary business like hedging and depositary function at fund level
- Ongoing lending pipeline as new funds are added to the structure (i.e. Fund 1, Fund 2, Fund 3 etc.)

4. Different types of fund financing

- Capital call facility
- Hybrid facility
- NAV facility
- SMAs (separately managed accounts)
- General partner support facilities

5. Credit analysis by banks

- External rating or sufficient information within bank to provide internal rating
- Borrowing base calculations – advance rate vs ratio of undrawn commitments to indebtedness
- Track record of fund manager
- Fund assets
- Cross collateralisation
- Post Abraaj

6. Key transaction documents

- Facility agreement
- Security package typically includes:
  - assignment of the GP's/asset manager's rights to call for capital from the investors
  - charge over bank account(s) into which capital contributions are paid
  - note there will be a slightly different security package for a GP support facility
- Legal opinions
- Other CPs
  - Corporate authorisations
  - Constitutional documents – **due diligence** (DD is paramount on a funds finance transaction)

7. Typical points of negotiation

- Financial covenants
  - Borrowing base dependent on aggregate funds raised on closing/Eligible Unfunded Capital Commitments within that
  - NAV
- Representations
  - Whether certain representations and undertakings apply to the Manager/definition of “Fund Parties”
  - Borrowing limits/authority
- Event of default triggers
  - EoD which is continuing vs acceleration/declared default
  - Umbrella facilities – cross default/fund level defaults and facility level defaults

8. Typical points of negotiation (continued)

- Investor notices
  - CP vs 1 BD after closing vs publication of quarterly report (hot topic following Abraaj)
- Due diligence
  - Confidentiality and disclosure issues
  - LPA restrictions
  - Side letters
  - Enforcement against defaulting investors
- Legal opinions
  - US vs UK approach

9. Issues to look out for

- GP, Manager or both as key obligors?
- Power to borrow and to secure
  - Ability to borrow for fund only, through subsidiaries or both
  - Ability to secure by way of assignment and account charge
- Borrowing limits – time and amount
- Perfection of security
  - Service of notices to investors
  - Service of notices to account bank and acknowledgement from bank containing waiver of set off rights
  - Local law quirks

10. Protections for lenders

- Due diligence carried out by specialist legal advisors
- Key protections in the finance documents
- Enforcement process

11. Facility Considerations for Borrowers

- LPs' perspectives and opinions regarding bridging
- Impact on MoC and IRR
- Tenor vs pricing
- How to make the facility most efficient?
- Operational Restrictions
- Transaction costs (time, counsel fees) vs efficiency

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