

FUND FINANCE FRIDAY

Subscription Finance Loan Agreement Series Part 5 — Investor Commitments and Available Commitments

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A topic that should be fairly straightforward this week, but as always, with a couple of twists. Given that the ultimate recourse under a capital call / subscription facility is to the Investors, it is very important to be clear about the nature and extent of the commitments which Investors have undertaken to the Fund which are available to repay the Lenders – and it is the Investors' commitments which are the primary building blocks of the borrowing base or leverage against which the Lenders will provide to the Facilities.

How these commitments are constituted will vary considerably depending on the nature and jurisdiction of the Fund. In a Fund which is a traditional English law limited partnership, historically the commitments will be provided by a mix of “capital” and “loan” commitment (with the majority of the commitment (99.99%) being in the form of loan commitments). In other jurisdictions this may or may not be the case. For example, commitments under a Delaware law limited partnership will generally be by way of capital commitment only (there will be no “loan” element). In Luxembourg, Investor Commitments may be constituted similarly to those in English limited partnerships but they may also, depending on the specific nature / type of Fund, be more akin to capital or equity commitments.

In assessing the quantum of any Facility, the Lenders will want to retain sufficient headroom between the Investor Commitments which are available for repayment and the amount of the Facility that can be drawn. In deciding what Investor Commitments are in this sense “available” to them, Lenders will be keen to ensure that there are no obstacles to those available commitments being called to repay the Facility. In doing this, Lenders should carefully consider the following:

- The way in which “available” commitments are defined (most commonly in terms of those commitments being “uncalled”) in the underlying Limited Partnership Agreement or other relevant constitutional documents of the Fund.
- Whether there are any specific conditions to those payments being made, and if there are, whether it will always be within the Lenders' power to satisfy those conditions. For example, where the commitment is in the nature of a subscription for shares, then Lenders must be satisfied that either (i) the obligation to pay in the commitment is not conditional on the issue of share certificates or registration of the new shareholder in the books of the Fund; and / or

ii) that such issue or registration will occur without any preconditions (even on a Fund's insolvency). In most jurisdictions a Fund's insolvency (and perhaps other events) can restrict or prevent shares being issued or registered, so the better course in most circumstances is to look to ensure that the commitments are unconditional.

- Whether the availability of commitments (either generally or for specific purposes including perhaps repayment of debt) is time limited (for example, by reference to the Fund's investment period).
- What other factors might affect the level of that available commitment. For example, unless specifically excluded in the Fund's constitutional documents, it may be that there are rights of set off or counterclaim as between the Investors and the Fund which could reduce the amount of the available commitment, or an Investor could be excused from honouring its commitment in respect of a particular type of Investment. In both those cases, the Lenders will consider whether those Commitments should be removed from what are counted as "available" commitments.
- And finally, how to deal with "recallable" commitments in this context. These are commitments which arise (or are preserved) as a result of Investors being refunded or repaid usually as a result either of (i) Investors being asked to pay in commitments which for whatever reason are not actually utilised and therefore are returned to them unused once a defined period has elapsed (often around 60 or 90 days) or (ii) Investors receiving repayments out of Investment proceeds where the Limited Partnership Agreement (or equivalent) specifically provides that either an amount equal to these repayments (or some proportion of that amount) will be added back to that Investor's "available" commitments, often for a defined period after receipt. In legal terms, (provided the applicable provisions of the Limited Partnership Agreement are properly reflected) these commitments are as "available" as any others but Lenders may consider whether, particularly where Investment proceeds have already been returned to Investors, Investors may find it more difficult in practice to return these to repay debt.

All of the above should always be matched with the results of what should always be a very full due diligence process to ensure that what is written into the Facility Agreement properly reflects the way in which the commitments and their availability work through the Fund's constitutional documents and any investor subscription agreements / side letters.