

FUND FINANCE FRIDAY

When a Fund Isn't a Fund – “It's a Fund, Jim, But Not as We Know It”

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Traditionally, European fund vehicles have been established as limited partnerships with general and limited partners. Increasingly, fund clients and their lawyers are taking advantage of the variety of "fund" entities created over the last decade in Europe, resulting in an increase in corporate entities as fund vehicles.

These corporate vehicles, most commonly seen in the Irish and Luxembourg markets, do not have the usual GP/LP structure and instead, issue shares or other equity-like instruments when a capital call is made. Unlike a fund, which generally only requires the issuance of a call notice and the receipt of cash to complete an investor call, in the context of a corporate entity, additional steps may be required (such as the issuance of shares).

This has the potential to complicate enforcement of security over the right to call capital, either because the "fund" entity is insolvent and therefore prevented from issuing further shares or because the security agent is logistically unable to take the steps required (such as the issuance of shares) post-receipt of cash.

Depending on the type of entity being used as the fund vehicle, a variety of possible solutions present themselves. For example, the constitutional documents of the entity may provide for a deemed issuance of shares if capital is called for the purpose of enforcement, or there may be another mechanism to decouple the obligation of the investor to pay capital from that of the fund entity to issue shares. It may also be possible to have contractual arrangements in place with any entity that runs the administrative affairs of the fund entity, whereby they agree to issue the shares.

Issues relating to the corporate structure of the "fund" should be identified and discussed with lead and local counsel during the due diligence phase of a transaction, as the solutions may not be straightforward to implement.