



# FUND FINANCE FRIDAY

## Summertime Reflections

July 7, 2023

### Table of Contents:

- **'Fund Finance Friday: Industry Conversations' — Ares Management's Eli Appelbaum and Richard Sehayek**
- **FFF Sovereign Immunity Series – Part XII**
- **Cayman Islands Achieves Significant Milestone in Removal Process from 'AML Grey List'**
- **Wes Misson Named 'Most Effective Deal-Maker' at Southeastern Legal Awards**
- **On the Move – Dee Dee Sklar**
- **On the Move – Hamish Massie**
- **Fund Finance Hiring**

# 'Fund Finance Friday: Industry Conversations' — Ares Management's Eli Appelbaum and Richard Sehayek

July 7, 2023



By Nathan Parker  
Partner | Fund Finance



*Fund Finance Friday* was pleased to have the opportunity to speak with Richard Sehayek and Eli Appelbaum from Ares Management this week.

**Eli** is a Partner at Ares and Head of European Alternative Credit.

**Richard** is a Managing Director at Ares, with a focus on alternative credit investments. Prior to joining Ares earlier this year, Richard was a Managing Director and Global Head of Origination for Fund Financing at Credit Suisse.

Both Eli and Richard have a wealth of experience and are incredibly well placed to comment on the market. We are grateful to them for sharing their time for this piece.

*FFF: There is a lot of discussion around the growth of the fund finance market, and it is fair to say that the market has grown significantly, particularly in the PE NAV space – both in terms of participants and structures. What do you see as the main drivers for this growth?*

E&R: From our perspective there are multiple levers driving the organic growth of the fund finance market, and the example of PE NAV is helpful to illustrate this.

With the slowdown in M&A activity and the dislocation in capital markets extending portfolio realisation times, we are seeing an increasing acceptance of the advantages and usefulness of the product among both GPs and LPs as an instrument to drive value in the portfolio and manage distributions more efficiently.

There are also increasing challenges and costs associated with accessing subordinated or junior capital at the asset level, which, combined with the increased risk associated with accepting high-priced asset level financing in a high interest rate environment, make financing at a 'NAV' level more appealing. It is also worth mentioning that the growing concerns around

possible recession and stagnation in certain sectors mean the advantages to having a portfolio-wide financing solution are more pronounced.

On the distributions side of the equation, GPs are facing a complex fundraising environment. Having access to a financing facility allows GPs to expedite distributions to LPs, which can be particularly helpful where those same LPs are being asked to commit to new vehicles.

On the portfolio side, the additional liquidity afforded by NAV facilities provides both offensive and defensive advantages. Access to an additional cash resource through the NAV line allows GPs to pursue compelling add-on acquisition opportunities at portfolio level that may otherwise be beyond the capacity of the fund where the assets are held.

Defensively, the facility provides the opportunity to de-lever and de-risk underlying assets with an efficient fund-level solution.

Outside of NAV, it is also worth mentioning that the increased requirements for co-invest to achieve successful fund growth is driving GP-level solutions for debt and equity to help finance growing demands for co-invest, to finance strategic acquisitions and to allow GPs to pursue new strategies.

*FFF: With the product evolution we are seeing, it would be interesting to hear how you are viewing different structures at the moment and to get an understanding of what Ares is able to offer borrowers in terms of flexibility.*

E&R: Traditionally, the market has seen, at one end of the spectrum, bank lenders tending to offer traditional fully secured and covenant-heavy NAV structures at a lower all-in cost. While at the other end of the spectrum, particularly over the last 18 months if we think again about the PE asset class, non-bank NAV lenders have tended towards lending into more flexible, covenant-light preferred equity NAV solutions, which come with a consequent higher ticket.

This has provided choice and solutions to GPs with varying needs, including regulatory and compliance needs that have driven a number of the preferred equity structures the market has seen. It could be said that the market has been efficient in this way, ensuring that both the bank and non-bank lenders have been busy and the borrowers have choice.

Within Ares' Alternative Credit strategy, we can offer solutions across the fund capital structure, and we can consider bespoke hybrid solutions pulling to meet the exact need of the GP. Notably, Ares had approximately \$360 billion in assets under management and actively invested in over 1,750 portfolio companies, as of March 31, 2023.

*FFF: And more generally, what are you seeing in the market at the moment? What is coming across your desk?*

E&R: Demand for NAV financing facilities to these types of managers, particularly for the purposes of making acquisitions, has remained strong. We would caveat this slightly, though, as it is not uncommon for sellers of assets to offer vendor financing in an effort to expedite the transfer of assets from their balance sheet and increase the sale price. This competes with any NAV-based offering and acts as a release valve to some of the 'demand' pressure in the system.

We also see GP commitment facilities – financing facilities secured against fee streams – being popular again against the backdrop of a difficult fundraising environment. Increasingly, these facilities are being used to help fund GP commitments in new vehicles given both the increase in frequency of fund launches and increased fund sizes. This has resulted in larger GP commitments.

Separately, we are seeing an increase in NAV facilities being offered on more concentrated portfolios. We believe this is partly due to the reduced availability and higher cost of subscription lines, as well as GPs feeling less certain with respect to the annual renewal process for their subscription lines. The increase of more concentrated NAV facilities is also a symptom of managers turning to portfolio-level NAV facilities earlier in the life cycle of their funds.

We are also seeing momentum outside of the traditional private equity sectors. For example, there has been a noticeable increase in interest in NAV facilities coming from real estate funds.

Financing for continuation vehicles appears to have become much more prevalent, providing an important tool to create liquidity generally by handpicking one or two high-quality assets for the vehicle.

In terms of approach across the U.S. and European markets, generally speaking LTV on NAV trades tends to be tighter in the U.S. – both in terms of what borrowers are looking for and in terms of what lenders are willing to offer compared to their EU counterparts. That said, GPs have indicated that the European markets focus more on co-invest and management holdings, which may act as a fetter on enforcement, particularly around drag/tag rights and other minority shareholder issues. This can translate into specific covenants in the loan documentation. However, in the U.S. there appears to be more flexibility around these issues, and they are less likely to be specifically addressed in the financing documentation.

Finally, partnering with banks to help recycle risk, reduce RWA and balance sheet, reduce risk and manage internal limits is becoming a bigger part of what we see.

*FFF: There is a trade-off to be had between pricing and structural flexibility. How are you seeing this play out at the moment?*

As discussed earlier, in order to offer lower pricing bank lenders have historically needed to achieve optimal capital treatment on transactions. As such, they might be constrained by requiring LTVs to remain below certain levels and have greater security restrictions. Non-bank lenders can help fill a void on the financing product spectrum as they do not have similar constraints, and so are able to be more flexible with key metrics such as LTV and security arrangements. Though this comes at higher cost to reflect the increased risk.

Increasingly, this is translating into a wider offering to GPs and managers, and with this additional flexibility – depending on what they are solving for – they should be able to find the right solution.

*FFF: And finally, one of the main points of discussion in the market at the moment is lender capacity, which is presenting its own problems but also creates the potential for market development. How are you viewing it?*

We agree. One of the biggest limiting factors at present is the availability of supply. The fund financing market is a constantly evolving ecosystem. With traditional financing routes under pressure given some lenders looking to reduce balances, de-leverage or even exit the space entirely, alternative methods of financing will have to fill in the gaps.

With this in mind, we have seen an increase in appetite coming from non-bank participants, including the insurance sector. For the most part – and subject to robust due diligence/underwriting – risk has not been at the forefront of minds, as the prevailing view has tended to be that these are low-risk, high-quality transactions. So, we don't see bank lenders reducing balances or exiting the market as a response or change of view with respect to risk but more so as a response to the availability of capital and upcoming regulatory changes.

This is what is leading to a re-pricing across the spectrum of transactions, particularly the lower-priced transactions, as supply and demand try to find an equilibrium once more.

# FFF Sovereign Immunity Series – Part XII

July 7, 2023



**By Eric Starr**  
Special Counsel | Fund Finance



**By Meghan Dobbins**  
Associate | Fund Finance

## Fund Finance Friday: U.S. States Sovereign Immunity Series



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Today we release the twelfth – and penultimate – installment of our Sovereign Immunity Series. In this part, we discuss and provide a high-level overview of how sovereign immunity is viewed specifically through the lens of fund finance transactions in the states of Utah, Vermont, Virginia, Washington and West Virginia.

As a quick recap, a state’s immunity arises from its status under the 11th Amendment of the Constitution. While there are many types of claims a state might be immune from – *i.e.*, tort, criminal, contractual, etc. – we focus on the contractual, given that it is a contractual relationship that arises from a state entity’s investment in a fund. As we have shown in previous weeks’ discussion, each state’s approach to sovereign immunity is nuanced and can vary greatly from state to state.

While many states have, in some form or another, waived their immunity through case law or legislative action, we must also review any applicable side letter. An investor’s side letter is often critical when making the determinations regarding sovereign immunity – or lack thereof.

### UTAH

Utah has preemptively waived its sovereign immunity with regard to any contractual claims. Traditionally, there are notice requirements and steps a claimant must take in order to bring a suit against a government entity; however, in Utah, if such claim is contractual, those notice requirements are waived.

While the notice requirement has been waived, under Utah's Rules of Civil Procedure, to bring a claim, a plaintiff is required to submit to the Court: (i) a short statement showing that such plaintiff is entitled to relief and (ii) demand for judgment for specified relief (including the amount demanded). In addition, a plaintiff has to give notice of the "nature and basis or grounds of the claim" and the type of claim generally to the state entity that action is being brought against.

## **VERMONT**

Vermont, unlike Utah, has not waived or eliminated sovereign immunity as a defense against any contractual claims. Specifically, the Supreme Court of Vermont has laid out that the state *may* waive immunity, and any waiver of the state's immunity must be expressly accomplished by state statute – something the Legislature has not expressly done (at least not for contractual claims). As such, the investor documents for any Vermont public entity should be carefully reviewed by counsel to ensure that sovereign immunity can be, and has been, properly waived prior to inclusion in a borrowing base. There are some positive signs that this might change in the future. Further, the legislature has already waived immunity in the case of tort claims and in the event a municipal corporation purchases insurance.

## **VIRGINIA**

You've probably heard that Virginia is for Lovers (of enforceable contractual commitments). Virginia courts have maintained that sovereign immunity is not applicable in suits that are based on valid contracts "entered into by duly authorized agents of the government." In so holding, courts have recognized that the Commonwealth and its agents may not use sovereign immunity as a shield against liability in an action which is based on a validly executed contract. The qualifier here, that a contract must be validly executed, demonstrates the importance of careful due diligence to confirm, among other things, *all* applicable documents are validly executed by *all* parties.

Notwithstanding the noted waiver, there are a few steps that have to be taken before a claim can be brought in court. Namely, the claim must first be presented "to the head of the department, division, institution or agency of the Commonwealth responsible for the alleged act or omission which, if proved, gives rise to the claim." Only once the claim is presented to the applicable department or agency, and such department refuses to allow the claim, can the claim proceed in a circuit court in Virginia.

## **WASHINGTON**

Washington, like many of its cohorts we've discussed here, has expressly waived its contractual sovereign immunity. In doing so, they have delegated the authority to waive any immunities to the State Legislature. The State Constitution lays out that "Any person or corporation having any claim against the state of Washington shall have a right of action against the state in the superior court." While immunity has been expressly waived, there are a

few limitations on where the action must be brought. Specifically, the action must be brought in the superior court in:

1. the county of the residence or principal place of business of the plaintiff;
2. the county where the cause of action arose;
3. the county in which the real property that is the subject of the action is situated;
4. the county where the action may be properly commenced by reason of the joinder of an additional defendant; or
5. Thurston County, Washington.

## **WEST VIRGINIA**

West Virginia has gone a step further than its similarly-named eastern neighbor (Virginia) and created a specific court to handle all claims against the state. In creating the Court of Claims, West Virginia has waived its contractual sovereign immunity for claims in which the state should in equity and good conscience discharge and pay. The legislature stated: “[a]ny monetary claims against an agency of the State which is immune from suit is within the jurisdiction of the Court of Claims.”

Similar to other states, the West Virginia State Code lays out the steps that must be followed in order to bring a claim: “The claimant shall give notice to the clerk that he or she desires to maintain a claim. Notice shall be in writing and shall be in sufficient detail to identify the claimant, the circumstances giving rise to the claim, and the state agency concerned, if any. The claimant shall not otherwise be held to any formal requirement of notice and after the close of the hearing the court shall consider the claim and shall conclude its determination, if possible, within sixty days.”

## **Conclusion**

In our next and final installment of our Sovereign Immunity Series, we will round out our discussion of the status of sovereign immunity in two states (Wisconsin and Wyoming) and provide closing thoughts to complete this series.



# Cayman Islands Achieves Significant Milestone in Removal Process from 'AML Grey List'

July 7, 2023



**By Michael O'Connor**  
Partner | Conyers



**By Derek Stenson**  
Partner | Conyers

While the Cayman Islands' current inclusion on the FATF "Grey List" and the EU "Black List" for AML purposes is not of material relevance to transactions in the fund finance world, the Cayman Islands recently received some very positive news when FATF confirmed at its June meeting that the Cayman Islands has now met all 63 of its recommended actions regarding the jurisdiction's AML framework.

FATF has confirmed that the next step will be an on-site visit to the Cayman Islands (a standard and expected final step in the process which will take place in the coming months) and, assuming the inspection proceeds as expected, the Cayman Islands will be eligible for removal from the FATF "Grey List" in October of 2023.

Removal from the corresponding EU AML list is subject to the approval of the EU authorities, but it is expected that this process will begin following the Cayman Islands' removal from the FATF list.

While it is still a little early to say that this chapter has been fully written, the above news is a very important and positive milestone which demonstrates that the Cayman Islands continues to prove itself as a sophisticated jurisdiction with a robust and effective AML framework. We look forward to bringing further positive news on this topic in the coming months.

## Wes Misson Named 'Most Effective Deal-Maker' at Southeastern Legal Awards

July 7, 2023

2023 ALM  
SOUTHEASTERN  
LEGAL AWARD  
WINNER



Cadwalader U.S. fund finance head Wes Misson was named a “Most Effective Deal-Maker” at last month’s 2023 ALM Southeastern Legal Awards in Atlanta.

In its selection, ALM referenced Wes as being “the most prominent lender-side fund finance lawyer in the industry,” noting that “over the past 15 years of successfully delivering on innovative and precedent-setting client work, [he] has helped shape this important realm of the private lending markets.” In a published profile following Wes’s selection, ALM wrote: “Wes has served as lead counsel on thousands of transactions, including many of the largest and most sophisticated fund financings ever consummated. Over the past two years alone, he has advised more than 40 banks as lead or syndicate lender in transactions valued in excess of \$200 billion in terms of lender commitments and, in 2022 alone, Wes closed 15 transactions with lender commitments totaling at least \$3 billion each.”

Wes credited his mentor, Mike Mascia, for shaping him and provided some great advice on client relationships. He said: “It really is a relationship business. You have to make sure your client knows their counterparty and is comfortable moving forward despite the issues. If something goes wrong, how are they going to react? Will they be cooperative and reasonable? If the answer to those questions are not satisfactory after considering all the factors with the relationship, then it may be a situation where you ask the client if they are better off passing. It’s rare, but sometimes no deal is better than regretting doing a bad deal later. Also, it should go without saying, but if there are any ethical concerns, then it is always better to walk. You need to feel good about the relationship. Client selection is the best protection against a bad deal.”

You can read Wes’s full profile [here](#).

In addition, Cadwalader real estate finance partner Chris Dickson and special counsel Molly Lovedale were named “On the Rise” honorees. Chris was recognized for his work “as lead counsel to the lenders in transactions valued in the billions or hundreds of millions on a wide range of hospitality and other commercial real estate properties across the U.S.” Molly’s profile noted her participation as a senior team member “in representing the lenders on multiple significant transactions – totaling \$7.3 billion – across a range of high-value real estate asset classes.” You can read about Chris and Molly [here](#).

## On the Move – Dee Dee Sklar

July 7, 2023

On the Move



**Dee Dee Sklar**

Coller Capital

**Dee Dee Sklar** has joined **Coller Capital** as a Senior Advisor.

Dee Dee has worked with Coller over many years as a client relationship and said she is very pleased to take on this new role. With a career spanning asset management and banking, Dee Dee most recently worked as Vice Chair, Subscription Finance for Wells Fargo after serving as Global Head of the Funds Subscription Finance business. Dee Dee is the Global Chair of **Women in Fund Finance** and holds business development roles for the **Fund Finance Association**. She has numerous Board and Advisor positions across the fund finance industry.

## On the Move – Hamish Massie

July 7, 2023

On the Move



Hamish Massie has joined Bridgepoint as a Vice President in the London office.

He will be focusing on Fund Finance as part of the Portfolio Financing & Structuring team within Bridgepoint Credit. Hamish was previously at Bank of Ireland, where he was a Deputy Manager on the Subscription Finance team.

# Fund Finance Hiring

July 7, 2023

Fund Finance Hiring

Investec Bank is looking to hire legal counsel to join its market-leading Fund Solutions business in London.

This is a high-profile and technically rewarding role embedded in the business and would suit a lawyer with 5-7 years post-qualification experience gained on a banking and finance team at a leading international law firm or investment bank. The role will involve working on a wide range of financing transactions supporting funds and their managers in the UK and internationally.

For more information, please visit [here](#).