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Things to Consider When Your Guarantor Is a Fund

By **Steven M. Herman**
Partner | Real Estate

By **Matthew S. McManus**
Associate | Real Estate

Here are some practical points to consider when the guarantor of a loan is a fund.

(1) *The Lifespan of the Fund*

Most funds have a finite lifespan. This fact can be problematic if the fund is scheduled to wind down or liquidate during the loan term. Consequently, such term should be ascertained to determine if the eventual wind-down of the proposed guarantor will result in the inability of such entity to satisfy its potential obligations under a guaranty during the term of the loan. The diligence required here is a review of the organizational documents related to the proposed guarantor, which many sponsors are reluctant to share due to confidentiality concerns. Many sponsors will provide redacted documentation but, if not, lenders can consider relying on certain third-party opinions, which are addressed in more detail below.

(2) *Calculating the Net Worth and Liquidity of Guarantor*

When a guarantor is required to maintain a minimum net worth and/or liquidity during the term of the loan, the lender is ensuring that the guarantor, at all times, has the necessary capital to satisfy the potential liabilities that may arise under a guaranty. If the proposed guarantor is a fund, the lender should consider how it is calculating such entity's net worth and/or liquidity. Specifically, the lender should consider whether to include uncalled capital commitments in calculating the guarantor's net worth and/or liquidity.

If such capital commitments are pledged to secure credit facilities, earmarked for specific investments or are contingent upon conditions unrelated to the loan, they should not be counted toward the guarantor's net worth or liquidity. Additionally, some lenders count only uncalled capital commitments which are from individuals or entities which would be considered "institutional investors" according to standards set forth by the lender, which may include ratings requirements and

other eligibility requirements. In addition, if the limited partners of the fund are not large institutional investors but are only “accredited investors,” the lender should consider the creditworthiness of such individuals and/or entities as well.

(3) *Third-Party Opinions*

To the extent that a review of organizational documents is limited or unavailable, a third-party opinion may serve to give the lender comfort (i) as to the organizational structure of the guarantor and enforceability of the guaranty, (ii) that the guaranty does not violate or contravene the proposed guarantor’s organizational documents, and (iii) that the execution, delivery and performance of the guaranty has been properly authorized.

If the fund is foreign-based or has substantial foreign investors, the lender should include provisions in the guaranty that the guarantor has submitted to U.S. jurisdiction with respect to the enforcement of the guaranty and that any judgment and amounts recovered under the guaranty will be in U.S. dollars. In addition, the lender typically would get an opinion in each applicable foreign jurisdiction that such provisions are enforceable and that a foreign court would honor a U.S. judgment.

(4) *Replacement or Supplemental Guarantor*

While a replacement or supplemental guarantor provision may be requested by a borrower in connection with its flexibility concerning transfers and assumptions, lenders should consider these provisions in the context of a fund guarantor to potentially solve some of the issues identified above. Including mechanisms to require a replacement or supplemental guarantor may prove to be a simple solution.