SUBSCRIPTION-SECURED FINANCINGS:

ENFORCEMENT VS. PERFECTION (EUROPEAN DEALS EDITION)

Haynes and Boone, LLP and Ogier

haynesboone

TABLE OF CONTENTS

SUBSCRIPTION-SECURED FINANCINGS: ENFORCEMENT VS. PERFECTION (EUROPEAN DEALS EDITION)

INTRODUCTION

This article is intended to complement an article entitled "**Subscription-Secured Financings: Enforcement vs. Perfection**" authored by Ellen McGinnis, Timothy Powers and Deborah Low in 2018 which related to the position of enforcement and perfection in the US (with a focus on the State of New York). In this article we will focus on subscription finance deals in the European market and what steps are required to protect a secured lender. As the majority of funds that we see as borrowers in the European market are domiciled in a number of offshore jurisdictions, this article considers what is required to perfect security in the Cayman Islands, the Channel Islands and Luxembourg, as well as England and Wales.

ENGLAND AND WALES

Emma Russell and Emily Fuller (**Haynes and Boone, LLP**)

A typical collateral package for a subscription-secured financing will consist of (i) the obligations of investors in a fund to make capital contributions, and (ii) the bank account into which such capital contributions are paid.

There are a number of provisions to consider including in the finance documents in order to protect a secured lender. These range from negative pledges, which require obligors to refrain from granting any additional security over, or disposing of, the assets which are secured under that financing, to addressing issues of subordination. We have not considered subordination in depth in this article as whether this is required will be a question of the borrower fund's structure. Where a fund uses SPVs to hold assets at a lower level in the structure, it may be that additional debt (e.g. NAV facilities) will not sit at the same level as a subscription-secured facility anyway. Due to the different uses for subscription-secured facilities and NAV facilities, it is common for a fund to have both in place. As the collateral package for a subscription-secured facility looks up the structure, and the collateral package for a NAV facility typically looks down a structure, this should not be an issue if both are documented properly but lenders should be clear as to who has priority of repayment.

PERFECTION

Where a subscription-secured financing is structured as a borrowing base facility, a lender's liability under the facility agreement should never be greater than the value of the collateral pool. This is because security should be granted over all investors' undrawn commitments on day 1, and by definition inclusion in the borrowing base will mean an included investor has not transferred, withdrawn, redeemed etc their interest in the fund and as such should be secured. This means that whatever the lender's liability to lend is under the facility agreement (based on how much of the commitments of the included investors remain uncalled), the lender should have 'pound for

pound' or 'dollar for dollar' value of collateral against its liability. Due to most included investors having an advance rate of less than 100% applied against them, there is also headroom to cover interest and fees etc.

But what is required under English law to ensure that this security interest is perfected?

Under an English law governed security agreement, a security interest over the investors' obligation to make capital contributions is created by granting an assignment by way of security over the fund's and general partner's (in the case of a fund structured as a limited partnership) or manager's right to issue call down notices to investors. In order to perfect this security and create priority, notice must be given to the relevant third parties. In relation to the assignment of the right to issue call down notices, this means giving notice to the investors. Notice of such security should be given as soon as possible after entry into the security agreement in order to gain priority; ideally on the same day. If a period of time passes between the security agreement being entered into and the notices being served (for example, in the event that notices are sent with the next investor quarterly reports rather than on day 1), then there is a risk to the lender that the investors (who are unaware of the security) could withdraw from the fund before they receive notice and as such the value of the lender's collateral will reduce.

In respect of security granted over the bank account into which capital call proceeds are paid, security can be taken either by way of assignment or a charge. Where the account bank is also the lender, security should be taken by way of a charge (and such charge should be registered (see below)). Where security is granted over an account held with a third party account bank, notice of such charge/assignment should be given to the account bank. It is market standard to also require the applicable account bank to provide a written acknowledgement of such notice. Although acknowledgment is not required for perfection, it does provide evidence that notice has been duly served. Many account banks have their own form of notice and acknowledgement which they are reluctant to negotiate. As such, borrowers should liaise with their account banks as early on in the transaction as possible in order to avoid delays in the transaction.

Where the grantor of the security is an English corporate fund (or the general partner/manager of a limited partnership fund is a corporate) and a registrable charge is created by that security agreement, the particulars of such charge should be registered with Companies House pursuant to section 878 of the Companies Act 2006. For companies the applicable form is MR01 and for limited liability partnerships it is LL MR01. Such forms should be filed within 21 days of the charge being created.

ENFORCEMENT

Due Diligence

Any potential obstacles to the enforcement of security should be considered at the beginning of the transaction when conducting due diligence. In respect of security over the investors' uncalled commitments, this involves assessing the creditworthiness of each investor and considering any instances in which they may have a right not to fund. In order to asses this, the limited partnership agreement ("LPA") of the fund and any side letters should be reviewed carefully. Amongst other provisions, any sovereign immunity or excuse rights (for example, in relation to any call downs for purposes not in line with that investor's investment policy) that an investor may have should be noted. Ideally, lenders will gain the utmost comfort if the LPA contains wording that investors agree to fund any call downs made from a lender directly, and that they agree to fund without defence, set-off or counterclaim. If this wording is not included in the LPA, it should be considered what rights the investors do have which would allow them to exercise such rights. For example, if investors have a right to receive distributions under the LPA and such distributions are not discretionary, it should be considered whether

an investor may have a right to set-off the amount of any due and unpaid distribution against the amount of a requested call down. It should be made clear in the finance documents that any payment obligations the fund and a general partner or manager has to investors should be subordinated in favour of repayments to the lender (in the event that such wording is not included in the LPA). Unlike in the majority of US subscription-secured financings, it is still not market standard in European deals to request investors to enter into an investor letter directly with the lender in order to provide any direct obligations of the investors to the lender in the event that such obligations are not included in the LPA. As such, unless a lender has specific rights under an LPA, on enforcement the lender will need to rely on its rights under the security documents.

If the investors have not expressly agreed to meet a call down request from a lender in the fund documents, then on enforcement a lender can exercise the irrevocable power of attorney contained in the security document to 'step into the shoes' of the general partner/manager and issue a call down notice. It is worth noting that any English law governed security document which contains a power of attorney should be executed as a deed. In order for such a power of attorney by way of security to be considered irrevocable it must satisfy the requirements of section 4 of the Powers of Attorney Act 1971.

Generally on the insolvency of an English borrower, secured creditors will take priority above any unsecured creditors and shareholders/limited partners. Enforcement against individual investors will also depend on the jurisdiction in which such investors are based.

Below Ogier also explain the perfection requirements (if any) and methods of enforcement in the Cayman Islands, Guernsey, Jersey and Luxembourg.

EMMA RUSSELL

emma.russell@haynesboone.com
+44 (0)20 8734 2807

Emma is a partner and head of the Finance Practice Group in the London office of Haynes and Boone. Emma is an experienced loan finance lawyer with extensive knowledge in global fund finance, real estate finance transactions, and structured and specialty finance, as well as more general experience in acquisition, leverage, and general corporate finance. Her practice focuses on the full range of fund lending products across all fund sectors, (including private equity, real estate, secondaries, infrastructure, and hedge) from capital call facilities, hybrid/NAV facilities, to general partner support, co-invest facilities and portfolio acquisition facilities and assisting funds with structuring. Emma has significant experience advising credit funds and their lenders in relation to leverage facilities to CLOs/CDOs and securitisation vehicles. Emma has spent significant time working in-house with various financial institutions during her career.

EMILY FULLER

emily.fuller@haynesboone.com
+44 (0)20 8734 2831

Emily is an associate in the Finance Practice Group in the London office of Haynes and Boone. Emily acts on a full range of finance transactions, with a particular focus on fund finance, including syndicated and bilateral leveraged/NAV, hybrid and capital call facilities, as well as GP lines and management fee credit facilities. Emily's practice focuses on acting for bank and non- bank lenders, sponsors and a variety of borrowers (including, SMAs, private equity, hedge, infrastructure, real estate and credit funds, corporate entities and joint ventures) and has also gained valuable experience of both open-ended and closed-ended offshore fund structures.

CAYMAN ISLANDS

Mark Santangeli and James Lydeard (**Ogier**)

The Cayman Islands is one of the leading jurisdictions in the world for the establishment of closed ended investment funds. Funds are often formed as exempted limited partnerships ("ELPs"). These funds are structured on a standalone basis or as part of a larger fund structure. For example, it is common to see non-US tax investors invest in an ELP feeder fund as part of a "master-feeder" structure. Other types of Cayman vehicle (for example, exempted companies and limited liability companies) can be, and are sometimes, used as fund vehicles depending on the circumstances but an ELP is by far the most common type of entity used. As a consequence, this section focuses solely on subscription-secured financings with an ELP as the choice of fund vehicle. Specialised advice should be obtained for other types of vehicles.

PERFECTION

An ELP is not a legal entity; it acts through its general partner. In a typical structure, the general partner is established as a company, often as a Cayman exempted company, Cayman limited liability company, Cayman exempted limited partnership, Delaware limited liability company or Delaware limited partnership. The Exempted Limited Partnership Law (Revised) provides that the right to make capital calls and receive the proceeds of them are assets of the ELP and are held upon trust for the ELP by the general partner.

It is not necessary to have a local law security agreement to document the security over the right to receive uncalled capital commitments and the right to make capital calls. In US subscription-secured financings, the security is often governed by US law whilst in European subscription-secured financings it is more common for a local law governed security agreement to be used. When it comes to taking security over the bank account into which capital contributions are paid, it is usual for the security document to be governed under the laws where the account is held. Typically, the account bank is not located in Cayman.

Priority of the security over the uncalled capital commitments is achieved by giving notice of the creation of the security interest to the ELP's limited partners (i.e. the investors). Aside from establishing priority, giving notice to the investors has additional benefits for lenders. Until investors receive notice of the security interest they are entitled to treat the fund/its general partner as the person to whom they are liable and to obtain a good discharge by payment to, or settlement with, the fund/its general partner. Old English case law (highly persuasive but not technically binding in Cayman) suggests that once an investor receives notice of the security interest: (a) the investor is barred from thereafter accepting a release by the fund/its general partner of its obligations or a variation of its obligations in a manner prejudicial to the secured party; and (b) the investor will not be able to set-off against its uncalled capital commitments any amounts which become due and payable to the investor (from the fund) after it has received the notice. In terms of when notice is given to investors, this is a matter of negotiation between the parties but lenders usually require that notice be served as soon as possible after closing (notice can only be sent after the security agreement is entered into and the security interest in respect of which notice is given has been created). Recently, more prominence has been given to investor notices and it is not unusual to see lenders request additional language be included in the notice that goes beyond advising investors of the mere creation of the security. For example, language may be included advising the investor that the fund/its general partner has provided an undertaking in the finance documents not to permit any reduction or cancellation of investor capital commitments.

In those rare cases where the account bank is located in Cayman, priority of the security over the bank account into which capital commitments are deposited is achieved by giving notice of the creation of the security interest to the account bank. Whilst it is also market practice to require the account bank to provide a written acknowledgement of such notice, the approach of Cayman banks in dealing with such requests varies. In some instances the Cayman bank will not be prepared to provide any acknowledgement at all.

Lastly, whilst there is no public registration regime in Cayman for security over uncalled capital commitments and the right to call capital, Cayman companies (including Cayman limited liability companies) are required under the Companies Law (Revised) to maintain a register of mortgages and charges into which details of all security interests granted must be entered. This register of mortgages and charges is an internal register only and failure to make an entry does not affect priority or validity of the security. Where a Cayman company is the general partner or ultimate general partner of a fund that has granted security, it is a commercial matter whether the general partner or ultimate general partner (as the case may be) makes an entry in its register of mortgages and charges in respect of the security interests granted by it in its capacity as general partner or ultimate general partner. There is no strict requirement to make such entries.

ENFORCEMENT

A secured party would enforce a Cayman law governed security interest using its contractual rights under the relevant security documentation and as a result, generally enforcement steps can be taken without the need for court approval. Where the security documentation is Cayman law governed, an enforcement would likely involve the secured party appointing a receiver over the collateral. The secured party would typically have the power to direct where the investors pay their capital calls, but may rely on a correlated account pledge to trap the capital call proceeds. In addition, it is common for a Cayman law governed security document to contain an irrevocable power of attorney as security for the performance of the obligations of the fund/its general partner under the finance documents. On an enforcement, this power of attorney typically permits a secured party to "step into the shoes" of the fund/its general partner and call capital from investors in the name of the fund/its general partner. Note that under the Cayman Powers of Attorney Law (Revised), a power of attorney granted by or on behalf of a fund/its general partner that is expressed to be irrevocable and which is granted to secure the performance of an obligation owed to a secured party: (a) cannot be revoked without the consent of the secured party; and (b) would survive the winding-up or insolvency of the fund, in each case for as long as the obligations to the secured party remain undischarged.

Generally on the insolvency of an ELP, secured creditors will take priority over unsecured creditors and limited partners. Enforcement against individual investors will also depend on the jurisdiction in which such investors are based.

When reviewing the LPA of the fund (and other fund documents) and assessing enforcement options, one consideration from a Cayman law perspective is the extent to which the fund documents confer upon lenders third party rights under the Cayman Contracts (Rights of Third Parties) Law (Revised) ("Third Parties Rights Law"). Under the Third Parties Rights Law, it is possible to confer third party rights on a lender which allows the lender to enforce contractual rights against the other parties to the relevant contract as if the lender had been a party to the contract. In order to cater for the needs of subscription lenders, some LPAs, especially those for funds established over the past couple of years, confer such rights upon lenders. A detailed review of the LPA is required to ascertain the nature of any such rights, but they may include the right to

require investors to fund capital commitments on an acceleration of the subscription loan. There may also be other important rights, for example, a right to enforce defaulting limited partner provisions (i.e. remedies available to the fund/its general partner where a limited partner defaults in its capital call obligations under the LPA) or a veto right with respect to reduction or cancellation of investor capital commitments.

MARK SANTANGELI

mark.santangeli@ogier.com
+1 345 815 1766

Mark is a partner and specialises in all types of finance and has particular expertise in fund financing. He has significant experience in representing both borrowers and lenders (including major financial institutions, multilateral international financial institutions, private equity funds and hedge funds) in all types of lending products to include subscription line facilities, margin lending, derivative based structures, bond issues and limited recourse financings.

He also has a wide range of experience in asset finance and regularly advises on the use of Cayman SPVs.

Mark is a member of the Cayman Islands Legal Practitioners Association and the Law Society of Scotland.

JAMES LYDEARD

james.lydeard@ogier.com
+1 345 815 1755

James is a senior associate and works on a wide range of banking and finance matters for both borrowers and lenders, including fund finance, real estate finance and corporate lending. James also provides regulatory advice and assists clients with a variety of general corporate matters. James has substantial experience of the onshore market, including secondments with international banking institutions.

Prior to joining Ogier, James trained and practiced at Dentons in London (2009 to 2015). During his time at Dentons he was seconded to the real estate finance team of a global financial institution and an international infrastructure firm, as well as a six-month secondment to Dentons' Muscat office.

James is a contributor to Ogier's cross-jurisdictional fund finance guides and publications.

James received his LL.B in Law and Management Studies from the University of Leeds in 2007 and his Diploma in Legal Practice from the College of Law in 2009.

GUERNSEY

Christopher Jones and Matthew Macfarlane (**Ogier**)

CREATION OF SECURITY IN GUERNSEY

Security Agreements

Guernsey law does not recognise the concept of "perfection" of security, focusing instead on the "creation" of a security interest. Under a Guernsey law governed security agreement, a security interest over the rights of the general partner or manager of the fund to make capital calls to investors (and to receive the proceeds of such capital calls) is created where the secured party (or some person on the secured party's behalf other than the debtor or some person on the debtor's behalf) has title to the collateral pursuant to a security agreement, and where that title is acquired by assignment. A security interest will be created once (i) the secured party has title (and where that title has been acquired by assignment) and (ii) notice in writing has been served on the party from whom the debtor would be able to claim the collateral (i.e. the investors). Essentially therefore, to create security over the capital call rights, the rights are assigned to the lender and notice of the assignment is given to the limited partners.

Notice in writing is required to create a security interest. Consequently, notice would typically be served on the relevant investors contemporaneously with the execution of the security agreement. Where notice is given at a later date, a security interest will not be created until the service of such notice on the investors. However, the timing of service of notice is a commercial issue and accordingly, transaction specific arrangements for the service of notice on investors are not untypical in Guernsey (for example, notice may be served by way of the inclusion of the notice in the next usual circular provided to investors following execution of the security agreement). Where such alternative methods of serving notice are proposed, the bank must be aware that a security interest is not created until notice is served on the relevant investors.

In respect of security granted over a bank account into which capital call proceeds are paid, a security interest will be created either:

(a) where the bank which holds that account for its customer is the secured party and where its customer and the debtor are one and the same person, by the secured party having control of that account pursuant to a security agreement; or

(b) where the account bank and the secured party are separate entities, once (i) the secured party has title (and where that title has been acquired by assignment) and (ii) notice in writing has been served on the party from whom the debtor would be able to claim the collateral (i.e. the account bank).

As detailed above, in respect of paragraph (b) above, a security interest is created only at the point at which notice is served and, accordingly, where security is granted over an account held with a third party account bank notice of assignment is typically given to the account bank contemporaneously with the execution of the security agreement.

It is market practice in Guernsey to also require the recipient of a notice served under a Guernsey security agreement to provide a signed acknowledgement of the receipt of such notice. An acknowledgment is not required as a matter of Guernsey law for the creation of a security interest but, given there is no concept of deemed receipt in Guernsey, an acknowledgment provides evidence that notice has been duly served. However, it is not untypical for the requirement for investors to provide a signed acknowledgment to be dispensed with given the practical and commercial difficulties inherent in expecting investors to provide an acknowledgement, particularly where the service of the notice can be evidenced in some other way (for example by counsel for the secured party being copied on an email circulating the notice to the relevant investors).

Many account banks have their own form of notice and acknowledgement which they are reluctant to negotiate. Therefore, similar to the English position, borrowers should liaise with their account banks as early on in the transaction as possible in order to avoid delays in the transaction.

Notices

In respect of a notice served on investors pursuant to a Guernsey law governed capital call rights security agreement, it is important that such notice specifies that the debtor has assigned to the secured party all rights, powers and interest in the rights of the debtor in and to the relevant investors' capital contributions pursuant to the security agreement. Clear and unambiguous drafting in this regard will highlight to investors that amounts to be contributed by investors pursuant to capital calls made by the secured party following enforcement of the security will be used by the secured party to service the relevant debt under the finance documents, rather than for the purposes of making investments or such other purposes as are specified in the LPA of the fund.

Further, any notice to investors must comply both with the requirements of the LPA (see the paragraph entitled "Due Diligence", below) and with the requirements of the Security Interests (Guernsey) Law, 1993 (the "SIGL"). The SIGL provides that notice may be served on any person by delivering it to him, leaving it at his proper address or by sending it by post to him at that address. Further, the Electronic Transactions (Guernsey) Law, 2000 makes provision for the service of notice by electronic means (such as email). The requirement that notice be "served", however, will require the service of the notice on the investors rather than, for example, the notice simply being uploaded to a website which investors may log onto from time to time.

Security Registration

There is no requirement as a matter of Guernsey law that any security agreement created pursuant to the SIGL be registered with the Guernsey Companies Registry or any similar body.

ENFORCEMENT

Following an event of default under the finance documents, and upon the secured party having served written notice on the debtor specifying the event of default complained of (which is a requirement of Guernsey law), the secured party will be able to exercise the capital call rights. Where the debtor and the secured party have contractually agreed, as is customary in Guernsey, that the security may be exercised without the need for an order of the Royal Court in Guernsey, then provided that the documents are enforceable in accordance with their terms there is no requirement in Guernsey for any court order, or similar approval, in order to exercise the power of sale or application.

Enforcement would be effected through the secured party and not, for example, by a receiver appointed on his behalf (Guernsey does not have the concept of receiver or administrative receiver) nor would any administrator appointed to a company have the power to realise assets subject to the security on behalf of the secured party.

The proceeds of any sale and/or application must be applied by reference to the statutory waterfall which in principle provides for the payment of the secured debt following payment of any costs, fees and any prior secured claims.

In an insolvency scenario, the SIGL provides that, where a debtor becomes insolvent (or subject to a désastre) or his property is otherwise subject to proceedings consequent upon insolvency (or declaration of désastre), the secured party may realise or otherwise deal with the collateral as if such event had not taken place (i.e. there is no stay of enforcement proceedings). Equally, the moratorium that generally exists as a result of an administration order being made in Guernsey (under the Companies (Guernsey) Law, 2008), does not affect rights of enforcement with respect to security interests created pursuant to the SIGL.

Due Diligence

In respect of any potential obstacles to the enforcement of security in Guernsey, the LPA and ideally any side letters should be reviewed carefully to ascertain as to whether there are any provisions which may affect the ability to create or enforce the security. Amongst other provisions, the ability to assign the rights to make capital calls and to receive the proceeds therefrom must be identified and any restrictions on the assignment or exercise of such rights should be amended or removed. The LPA should not prohibit someone other than the general partner or manager from making a capital call to investors. In addition, any contractual provisions in the LPA which allow investors to claw back some or all of capital contributions made to the general partner or manager should be considered so that the scope and extent of the rights being assigned pursuant to the security agreement is clear. Similarly, the LPA should not restrict the payment of the proceeds of capital calls directly to the secured party following enforcement of the security, i.e. by way of set-off or counterclaim. As per the position in England, it should be clear in the finance documents that any payment obligations the fund and a general partner or manager has to investors should be subordinated in favour of repayments to the secured party (in the event that such wording is not included in the LPA). Any requirements in relation to the service of notice on investors should be noted and complied with.

In the event that investors have not expressly agreed to meet a capital call request from the secured party in the fund documents, the secured party can, on enforcement, exercise the irrevocable power of attorney contained in the Guernsey security document to 'step into the shoes' of the general partner or manager and issue a capital call notice. Unlike the position in England, a Guernsey law governed security document which contains a power of attorney does not require to be executed as a deed.

CHRISTOPHER JONES

christopher.jones@ogier.com
+44 1481 752337

Christopher is a partner and advises financial institutions, investment funds and corporate clients on a broad range of multi-jurisdictional transactions. He has extensive experience in respect of banking and finance, derivatives, restructuring, corporate matters, mergers and acquisitions, private equity and listings.

Recent transactions include advising Wells Fargo Bank International in respect of the amendment to a €215 million term facility made available to the Shurgard Self Storage Group. Christopher also regularly advises global investment banks in respect of industry standard documentation produced by the International Swaps and Derivatives Association, the International Capital Market Association and the International Securities Lending Association.

Christopher is an advocate of the Royal Court of Guernsey, a solicitor in England and Wales and a member of the Bar of New York.

MATTHEW MACFARLANE

matthew.macfarlane@ogier.com
+44 1481 752242

Matthew is a senior associate and advises a variety of financial institutions and companies on a wide range of banking, derivatives, corporate, finance and restructuring transactions, predominantly of a multi-jurisdictional nature.

A Scottish qualified solicitor, Matthew is a prize-winning graduate from the University of Edinburgh with a particular focus on corporate and finance transactions. With a background in commercial litigation and general corporate work, Matthew assists on a wide variety of banking, corporate transactions, predominantly of a multi-jurisdictional nature, including acquisition, real estate and asset financing.

*Not admitted in Guernsey

JERSEY

Katrina Edge and Kate McCaffrey (**Ogier**)

CREATION OF SECURITY IN JERSEY

Security Interest Agreements

For a subscription facility, we would typically expect security to be taken over (i) rights of the general partner or manager to make capital calls to investors under the LPA (the "Capital Call Security"); and (ii) the bank account(s) into which capital call proceeds are paid (the "Account Security"). If the limited partnership is a Jersey limited partnership and the relevant bank account is in Jersey, this security package can be combined into one Jersey security interest agreement.

Capital Call Security

In Jersey, security created under a Capital Call Security will be perfected by way of registration of a financing statement on the Jersey Security Interests Register ("SIR") maintained by the Jersey Financial Services Commission ("Registration").

Account Security

Security granted over any Jersey bank account into which capital call proceeds are paid, will be perfected either by:

(a) control, by:

(i) the deposit account being transferred into the name of the secured party with the written agreement of the grantor and the account bank;

(ii) the grantor, the secured party and the account bank agreeing in writing that the account bank will comply with instructions from the secured party directing the disposition of funds in the deposit account;

(iii) the deposit account being assigned (by way of security) to the secured party by instrument in writing signed by or on behalf of the grantor and notice is given in writing to the account bank; or

(iv) the secured party being the account bank,

(together, "Control"); or

(b) Registration.

Notices

Capital Call Security

There is no requirement to send notification to or obtain acknowledgment from investors to create or perfect security over the uncalled investor commitments in Jersey. However, we would advise a secured party to require that the fund give notice of the creation of such security to its investors either contemporaneously with the execution of the security interest agreement or with the next communication sent to the investors after completion/the first drawdown. Ideally, key or large investors would also acknowledge such notice and provide certain funding confirmations directly to the secured party but this would depend on the relative negotiating positions of the bank and the borrower.

Account Security

Account security perfected by way of Control, will have priority over security perfected by Registration only. As such, although Registration alone would be sufficient to achieve a perfected security interest, given the priority implications, we recommend that perfection by way of Control is achieved in addition to Registration.

Control over deposit accounts held with a third-party account bank, is created and perfected by sending a notice to the third party account bank which satisfies limbs (ii) and (iii) of the definition of Control (above), signed by the grantor and the secured party, and the secured party receiving an acknowledgement signed by the third party account bank wherein the account bank agrees to, amongst other things, comply with

instructions from the secured party directing the disposition of funds in the account. The notice should also contain a confirmation from the third party account bank that it has not received any prior notices of any security interest over the bank account(s).

Most account banks have their own form of notice and acknowledgement which they are reluctant to negotiate. Therefore, similar to the English position, borrowers should liaise with their account banks as early on in the transaction as possible in order to avoid delays in the transaction.

Security registration

As discussed above, it is market practice to perfect Jersey security interests by Registration (even if the security is also perfected by another means such as control).

ENFORCEMENT

The power of enforcement in respect of a security interest created under Jersey law may be exercised following (i) an event of default under the finance documents (or relevant negotiated trigger in the security interest agreement); and (ii) the secured party having served written notice on the grantor specifying the event of default complained of. A secured party has wide enforcement powers under the Security Interests (Jersey) Law 2012 ("SIJL") including the power to:

(a) appropriate the collateral;

(b) sell the collateral; or

(c) take any of the following actions:

(i) take control or possession of the collateral;

(ii) exercise the rights of the grantor in relation to the collateral;

(iii) instruct any person who has an obligation in respect of the collateral to carry out such obligation for the benefit of the secured party; or

(iv) apply any remedies provided for by the security agreement to the extent that such remedies do not conflict with the SIJL.

Enforcement would be effected through the secured party and not, for example, by a receiver appointed on his behalf (Jersey does not have the concept of receiver or administrative receiver) nor would any administrator appointed to a company have the power to realise assets subject to the security on behalf of the secured party.

The proceeds of any sale and/or appropriation must be applied by the secured party by reference to a statutory waterfall which in principle provides for the payment of the secured debt following payment of any costs and fees, with any surplus to be distributed in accordance with the provisions of the SIJL.

In an insolvency scenario, where a grantor becomes insolvent (or subject to a désastre) or its property is otherwise subject to proceedings consequent upon insolvency (or on a declaration of désastre), the secured party may realise or otherwise deal with the collateral as if such event had not taken place (i.e. there is no stay of enforcement proceedings).

Power of attorney

It is usual practice for Jersey law security interest agreements to contain an irrevocable security power of attorney. Such power of attorney (a) survives the insolvency of the grantor; and (b) has effect, notwithstanding any statute which vests the property of the grantor in any other person on insolvency; the secured party shall be entitled to act as if the power of attorney had been given also by the person in whom the property vests.

Due Diligence

In respect of any potential obstacles to the enforcement of security in Jersey, the LPA and any side letters should be reviewed carefully to ascertain as to whether there are any provisions which may affect the ability to create or enforce the security. Amongst other provisions, the ability to assign the rights to make capital calls and to receive the proceeds therefrom must be identified and any restrictions on the assignment or exercise of such rights should be amended or removed. Further, the LPA should not prohibit someone other than the general partner or manager from making a capital call to investors. In addition, any contractual provisions in the LPA which allow investors to claw back some or all of capital contributions made to the general partner or manager should be considered so that the scope and extent of the rights being assigned pursuant to the security agreement is clear. Similarly, the LPA should not restrict the payment of the proceeds of capital calls directly to the secured party following enforcement of the security, i.e. by way of set-off or counterclaim. As per the position in England, it should be clear in the finance documents that any payment obligations the fund and a general partner or manager has to investors should be subordinated in favour of repayments to the secured party (in the event that such wording is not included in the LPA). Any requirements in relation to the service of notice on investors should be noted and complied with.

In the event that investors have not expressly agreed to meet a capital call request from the secured party in the fund documents, the secured party can, on enforcement, exercise the irrevocable power of attorney contained in the Jersey security document to 'step into the shoes' of the general partner or manager grantor and issue a capital call notice. Unlike the position in England, a Jersey law governed security document which contains a power of attorney does not require to be executed as a deed.

KATRINA EDGE

katrina.edge@ogier.com
+44 1534 514192

"She has always been on top of her game". Clients rate Katrina Edge, a partner in Ogier's Jersey banking and finance team for her expertise, responsiveness and focus on what really matters in a transaction.

Katrina has extensive experience advising on a wide range of financing and corporate transactions. Katrina advises a broad range of local and international financial institutions, investors and borrowers. She has particular expertise in secured lending, property financing and restructuring transactions and also has extensive experience advising clients on the establishment of real estate holding structures and the acquisition and disposal of such structures.

Katrina's specialist areas include finance, corporate (with a focus on advising in connection with the establishment, acquisition and disposal of real estate holding structures) and restructuring.

KATE MCCAFFEREY

kate.mccaffrey@ogier.com
+44 1534 514355

Kate is a managing associate and is a corporate and banking specialist advising on a wide range of high-value international transactions. She acts for international finance institutions, investors and corporate borrowers in relation to complex, multi- jurisdictional bilateral and syndicated facilities, refinancing and restructurings. Kate has significant experience in relation to the financing of investment funds and the real estate finance sector.

Kate has a strong reputation for her ability to deal with complex transactions and providing succinct, practical commercial legal advice. Client feedback is that Kate is, 'a pleasure to work with.'

Kate trained as an English solicitor at the London office of Paul Hastings. Prior to joining Ogier in August 2018 she spent eight years at another leading law firm in Jersey. Kate is qualified as a solicitor in England and Wales and was educated at the University of Durham.

LUXEMBOURG

Daniel Richards and Catharina von Finckenhagen (**Ogier**)

Perfection and enforcement under the laws of the Grand Duchy of Luxembourg

Like in the UK, the security package granted by the fund in a subscription credit facility will generally include:

- a pledge over the rights of the general partner to call the uncalled capital commitments of the investors and to enforce any associated rights; and
- a bank account pledge over the deposit account into which the investors deposit the proceeds of the capital calls.

Perfection of security

The pledge of the right to call capital from investors in respect of their uncalled capital commitments is perfected under Luxembourg law by the mere conclusion of the pledge agreement listing the pledged capital commitments between the fund and the security agent. However, an investor may nevertheless validly discharge his payment obligation under the subscription agreement as long as he has no notice of the security interest. Notification of the pledge is therefore highly recommended, and market standard, even if not strictly required for security perfection purposes. The notice should be provided by the fund on the date of closing or as soon as possible thereafter to ensure the priority of the security interest.

To perfect the bank account security under Luxembourg law, the account bank must be notified of the pledge and asked to relinquish any rights of set off, combination of accounts or first ranking pledge in the respect of the account collateral which would otherwise apply in standard account bank terms and conditions. When the account bank is the lender itself, the perfection requirements can be dealt with in the security agreement directly.

Enforcement of security

Under Luxembourg law, enforcement may be carried out by the lender as a secured party by way of private action, without requiring any court order or the involvement of any public or judicial officer or notary.

Upon enforcement, the secured party will be able to deliver drawdown notices to the investors in lieu and place of the fund's general partner (or manager, depending on the fund documents).

In addition to the right to call capital, a secured party will also be granted the right to enforce the obligations of the investors to fund the capital commitments.

Finally, the secured party will be able to take control of the collection account pursuant to the bank account pledge agreement.

To facilitate the enforcement process, the Luxembourg law of 5 August 2005 on financial collateral arrangements (the 2005 Law) disapplies the Luxembourg civil law requirement for a formal default notice (mise en demeure) to be served prior to enforcement, although the contractual facility agreement terms will often entail a notice of acceleration and demand in any event. Certainty is further enhanced by the 2005 Law's disapplication of the laws of both Luxembourg and other jurisdictions relating to bankruptcy, liquidation, reorganisation or similar measures and from any civil, criminal or other judicial attachment or confiscation court order. All legal risks of nullity of the security or unenforceability against third parties, arising from such matters, are thus disapplied except in relation to civil liability for conspiracy to defraud and in relation to an insolvency cause of action pursuant to a fraud on creditors. Accordingly, in the absence of fraud, the relevant Luxembourg security and its enforcement provisions are binding on any insolvency office-holders and the secured assets fall outside the bankruptcy estate of the grantor, and is enforceable by private action of the secured party despite the opening of any bankruptcy

proceedings against the grantor, and, importantly, is not vulnerable to being set aside by reason of any hardening period (période suspecte). The result is an attractive, secure legal framework that strongly benefits the secured finance parties in transactions involving Luxembourg entities granting security, and consequently, fund promoters seeking investment financing solutions.

DANIEL RICHARDS

daniel.richards@ogier.com
+352 2712 2011

Daniel is a partner and Luxembourg Advocate, Jersey Advocate and English Solicitor.

Daniel co-founded Ogier's Luxembourg office in 2012, leading Ogier's Luxembourg finance and private equity teams, prior to becoming practice partner in 2018. He has extensive experience in all aspects of international investment structuring and related financing in Luxembourg, Jersey and UK.

Having read law at Cambridge University, Daniel qualified as an English solicitor in 1999, practicing at a major international law firm's London office 1997-2002.

Since moving to Jersey in 2002 and to Luxembourg in 2012, Daniel has acted for fund managers and banks in relation to the establishment, financing and portfolio investment by, regulated and non-regulated international investment structures across the broad range of alternative asset classes, including: private equity, real estate, infrastructure, infrastructure finance, credit and special opportunities.

He is frequently nominated in legal industry directories for his highly regarded client service.

CATHARINA VON FINCKENHAGEN

catharina.vonfinckenhagen@ogier.com
+1 345 815 1802

Catharina is a senior associate and specialises in fund finance, advising global lending institutions and borrowers on multi-jurisdictional subscription finance facilities.

With extensive corporate finance, banking and investment funds experience, she advises an international client base on general corporate and banking matters and all aspects of investment funds, including formation, restructuring, corporate governance and operational matters.

Catharina is a member of 100 Women in Finance, Women in Fund Finance and the Cayman Islands Legal Practitioners Association. Catharina is fluent in English, French, Italian, Norwegian, Swedish and Spanish.

Prior to joining Ogier, Catharina worked as a corporate finance and funds lawyer at Norton Rose Fulbright in London, Hong Kong and the Kingdom of Bahrain, specialising in various open and closed-ended fund formations, including Shariah compliant structures, international private equity offerings, public and private mergers and acquisitions, restructurings and joint ventures.

She joined a leading offshore law firm as an associate in Singapore before moving to the Cayman Islands in 2015.