Global Legal Update[1]

By Brandon Spleen, Charles Zang and Mei Zhang

The Global Legal Update panel focused on legal developments over the past year in each of the United States, the Cayman Islands and Luxembourg. Here are our key takeaways.

- While use of a debt commitment in a private investment vehicle (including use of a rated note feeder vehicle) is not new as of the past year, panelists noted that New York and other United States jurisdictions have seen an increase in the popularity of such structures over the past three years. They noted that more fund sponsors are closing in commitments in this manner and having conversations with their lenders about including such commitments in the borrowing base. This, they noted, has resulted in an ongoing maturation and evolution of the diligence and legal provisions necessary to get such lenders comfortable advancing against debt commitments.

- As debt commitments and rated note feeders become more popular in the United States, U.S. counsel have found that certain insurance companies are rejecting the prospect of having their position converted to equity, due to regulatory concerns, even when an insolvency or default event occurs, requiring additional focus to ensure the debt commitments and note funding obligations are as close as possible to a special purpose vehicle and bankruptcy remote.

- While rated note feeders do not seem to be common in Luxembourg, the Luxembourg market has seen debt commitments utilized either with plain funds (either regulated or unregulated) or via securitization vehicles through Luxembourg law and European Union regulation. With the increase in debt commitments, Luxembourg attorneys would want to make sure they build into the fund documents conversion mechanisms whereby at the election of the lender or general partner during an enforcement scenario the debt commitment would automatically convert to equity.

- Attorneys in the Cayman Islands are seeing an increase in rated note vehicles becoming domesticated in the Cayman Islands due to investor demand. Panelists noted that such choice of domestication requires review and a thorough understanding of both the U.S. Bankruptcy Code and the Cayman Islands Insolvency Laws, and that these two insolvency regimes have fundamental differences.

- Within the U.S. market, attorneys are finding an uptick in requests for hedging mechanics built into the loan agreement governing the subscription line, as lenders are, in certain cases, expecting to provide such services to their borrower client over an outside lender. However, borrowers are pushing back on these requests and sometimes using a legal argument to do so, which is that lenders are prevented (with certain exceptions) from conditioning one financial product on another via the “anti-tying” laws.

- Cayman Islands markets are seeing an increase in private funds registering under the Cayman Islands Private Fund Act, requiring credit agreements to include additional protections, including a condition

[1] Moderated by Jad Nader, Partner at Ogier, the panel included the following: Finn Howie, Counsel at Mourant; Maude Royer, Senior Associate at Loyens & Loeff; Eric Schwitzer, Partner at Paul Hastings; and Jenna Willis, Counsel at Carey Olsen.

precedent that the Cayman entities register under this Act and an ongoing covenant for such entity to maintain its registration status.

- Luxembourg attorneys note that with the development of the Alternative Investment Fund Managers Directive, the number of parties in the fund has been increased and with it the distribution of roles amongst them (GP, alternative investment fund manager, portfolio manager, advisors, custodians and administrators, all being fund parties). This results in an increased focus on confirming the powers delegated to the alternative investment fund manager, including authorizations and powers to issue capital calls, borrowing and granting security, and making sure the right parties on the fund side are involved on a subscription deal.

- Sanctions generally cover any sanction enforceable by the U.S. government, United Nations, the European Union, and His Majesty's Treasury (U.K.). The general mitigants for sanctions risk within subscription facilities include exclusion events, ongoing covenants and events of default. Withdrawal from a fund when an investor becomes subject to sanctions has become a unique issue for Cayman Islands sanction specialists, as there is no general license to force an investor to withdraw from the fund except for extraordinary events and national security interest.

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