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In Practice

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Trends in funds finance: co-investment, general partner and manager support facilities

Over the last few years, there has been a significant increase in demand from general partners and managers of funds for general partner co-investment facilities and manager support facilities, in addition to any capital call facilities which are provided to the funds themselves. More banks are looking to expand this product and take advantage of the opportunity to build and strengthen their relationships with such funds and their principals.

STRUCTURE

Facilities to a general partner or a manager are usually structured as revolving credit facilities lent directly to the general partner or the manager or key individual employees of a fund. Facilities to a general partner usually finance a portion of its commitment to the fund. Facilities to a manager provide it with working capital, effectively bridging the gap between the manager's expenses in providing investment management, advisory and operational services to the fund, and the periodic incoming management fees.

INCREASING IMPORTANCE

Although these facilities are usually seen as more risky than traditional capital call facilities, lending to the general partner or manager or principals has become increasingly attractive for both banks and funds for a variety of reasons.

From a lender's perspective, pricing is usually higher than capital call facilities, allowing lenders to generate an additional revenue stream from fees and interest. Lenders may also be interested in the opportunity to obtain the account business of a general partner or manager.

More importantly, lenders are using general partner and manager support facilities as an opportunity to develop a relationship with the principal investors in the fund, particularly in the context of large successful international funds. Such facilities are sometimes provided through the private wealth divisions of banks.

From a general partner's or manager's perspective, such facilities enable them to leverage their income stream (management fees) and to make a larger contribution to the fund as would otherwise be the case. There is a recent trend for limited partners calling for general partners and principals involved in the fund to make a larger contribution in the fund (the so-called "skin in the game") and this has consequently led to general partner support and co-investment facilities becoming increasingly in demand.

From an operational perspective, such facilities are attractive because they provide the general partner or manager with working capital to manage its respective cashflows and bridge the gap between the future income revenue stream from fees and the ongoing expenses

for services they provide to the fund.

The larger funds and managers with a proven track record of steady management fees are better suited to such facilities. This is because lenders typically base their credit decision on the underlying success of the fund (and the credit worthiness of the principals if personal guarantees are given).

KEY FEATURES OF GENERAL PARTNER AND MANAGER SUPPORT FACILITIES

- **Security package:** the facilities do not usually benefit from security over the commitments of the investors or limited partner base in the fund. The overall security package may extend to other assets of the general partner or the manager in addition to the general partner's profit share and the management fees (eg a debenture over all assets of the manager, general partner and carried interest vehicles of key individuals involved in the fund).
- **Repayment:** repayment from distributions of income comes in the form of management fees for the manager, carried interest and priority profit share of the general partner. Facilities may also provide for a minimum level of fees to be received by the general partner or manager or for such fees to exceed a specific percentage of the aggregate commitments of the investors/limited partners in the fund.
- **Guarantees:** for facilities of certain quantum, it would not be unusual for the principals to give personal guarantees in favour of the lenders.

CONCLUSION

The increase in facilities provided to general partners and managers demonstrates that the European funds finance market is moving towards that of the US funds finance market, which offers a wider range of fund finance products. In particular, as more US based investors are investing in European funds, "skin in the game" is becoming an increasingly important factor, meaning these facilities have greater strategic importance for funds, general partners and managers. ■

Biog box

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