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DUE DILIGENCE IN FUND FINANCE TRANSACTIONS

This article provides a summary of key considerations for lenders and lenders' counsel when conducting due diligence for fund finance transactions. The principal documents for review are detailed, with practical tips for avoiding common pitfalls in performing due diligence in subscription line facilities and net asset value facilities.

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The due diligence process in a fund finance transaction can often be the most time-consuming part of the transaction. To that end, this article sets forth some of the fundamental elements of the process, noting that each transaction is unique and has its own considerations. The first step is determining what type of transaction is being structured. Subscription lines or capital call facilities are typically revolving lines of credit based on the remaining amount of outstanding capital calls from the investors in the fund. Due to this concept, subscription lines are typically used in the earlier part of a fund's life cycle. On the other hand, net asset value facilities ("NAV") facilities are credit facilities based on the value of the investments held by the fund. Hybrid facilities combine elements of both subscription lines and NAV facilities, but this article will be limited to just subscription lines and NAV facilities. As part of the diligence process for any of these facilities, it is important to start the diligence process as early as possible in order to identify any potential concerns.

The initial diligence request for all fund finance facilities should consist of the fund's structure chart, all organizational documents, and the private placement memorandum. Communicating with the lender client will shape the due diligence process; depending on the makeup of the fund's investors, lenders will also want to review (or have lender's counsel review) investor subscription agreements, side letters, and may also require investor letters (pursuant to which an investor confirms its capital commitment and acknowledges a lender's rights and obligations when stepping into the GP's shoes) or evidence that a certain percentage of capital calls have already been made.[1] Typically, the lender will want its lawyers to conduct more diligence with subscription lines than with NAV facilities, as much of the investment-level diligence for a NAV

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[1] Anastasia N. Kaup and Louise Melchor, Duane Morris LLP, *Fund Finance: How to Mitigate Risk and Facilitate Financing* (Dec. 30, 2021), https://www.duanemorris.com/articles/fund_finance_how_to_mitigate_risk_facilitate_financing_1221.html.