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# INNOVATIVE RATED NOTE STRUCTURES SPUR INSURANCE INVESTMENTS IN PRIVATE EQUITY

*This article discusses how insurance investments in private equity are typically structured via collateralized fund obligations and rated feeders and key regulatory and other trends relating to the same.*

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As insurance companies look for opportunities to invest in a diversified portfolio of funds, and funds look for ways to access additional capital, there is increasing demand for innovative rated note structures. Such investments are typically structured in one of two ways: (1) through a rated note feeder fund for investment in a single fund or (2) through a special purpose vehicle structure for investment in a portfolio of funds, creating a fund of funds structure. For investment in a single fund, the master fund typically creates a feeder fund that issues rated debt and equity through which the insurance company can participate as a debt-only investor or as a debt and equity investor, depending on the structure of the deal. For investment in a portfolio of funds, the special purpose vehicle is typically structured to include one or several tranches of rated debt supported by limited partnership ("LP") interests in the underlying funds that comprise the investment portfolio and a tranche of equity commitments (structured as straight equity or subordinated notes), which, as the first-loss tranche, is important for the ratings analysis. Although insurance regulators have proposed changes to the investment classification and/or regulatory capital requirements for the equity tranches and notes issued by these structures, we expect interest in these structures to continue even as market conditions tighten.

This article reviews how these investments are typically structured, some important parameters that need to be determined in their structuring, the current regulatory environment, and recent trends.

## KEY CHARACTERISTICS

- *Basic Single-Fund Structure*: Structured notes obligations invested in a single master fund usually take the form of a feeder fund that issues one or more tranches of debt and equity. Typically, the investor purchases debt and equity, with the substantially larger commitment taking the form of debt (for example, 80% debt and 20% equity). This structure relies on the ability to map steady cash flows from the master fund for the ratings analysis and we therefore usually see this structure used to invest in debt funds. If the sponsor needs the ability to adapt terms for the rated debt that would not be

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