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Subscription facilities: Through the Looking Glass and into Wonderland

Jan Sysel, Jons Lehmann & Kathryn Cecil
Fried, Frank, Harris, Shriver & Jacobson LLP

Introduction

As is common wisdom, the subscription facility has evolved into a significant and global financing tool for investment funds seeking efficient access to capital. Borrowers utilise subscription facilities in a myriad of ways, ranging from short-term borrowings (used primarily to bridge liquidity needs *in lieu* of making frequent and/or irregular investor capital calls) to long-term leverage (which seeks to increase the overall fund size and serve as a permanent source of capital) as well as various combinations thereof.

Subscription facilities are the bedrock of the fund manager's arsenal to facilitate the effective management of a fund's liquidity needs. Used by a wide variety of funds, with different investment strategies, across the full range of asset classes in North America and around the globe, including Europe (in particular the UK) and Asia-Pacific, where the market has significantly expanded, the prevalence and importance of the subscription facility is unquestionable. As the use of debt financing by funds has become ubiquitous, investors are now accustomed to, and more educated about, the use of such facilities. In tandem, fund structures have evolved to offer investors a menu of levered and unlevered options and different investment currencies to choose from.

The number, size, variety and complexity of investment funds have grown over the years, and subscription facilities have adapted to the changing landscape. Fund sponsors and lenders continue to collaborate to develop financing solutions designed to address the evolving needs of borrowers and their investors. Indeed, a "cookie-cutter" subscription financing is a myth. The subscription facility market today is robust and sophisticated, continuously attracting new entrants on both the borrower and the lender side. Increasing demand and bespoke financing needs have resulted in the development of customised liquidity solutions to suit the particular profile of the underlying fund. While NAV facilities, GP financings and other products have risen further in prominence during the past year, subscription facilities have continued to dominate overall activity in the fund finance market through 2022. Investors and sponsors continue to highly value quick access to liquid capital and other related benefits in fund management and deployment. As the world slowly recovers from the longer-term effects of the global pandemic and faces the challenges of greater geopolitical uncertainty and more volatile economic conditions, the subscription facility is once again proving to be a versatile and flexible instrument. Even in an age where the structuring and negotiation of transactions is increasingly virtual, the benefits of subscription facilities are still very much tangible and real.

This chapter looks at the breadth of the types of subscription financings and trends currently in the marketplace by examining select aspects of facilities for various kinds of investment funds in the US and UK markets.

Once upon a time, long, long ago: Subscription facility fundamentals

Subscription facilities are effectively a form of "asset-based lending", where the ability to borrow is determined principally by reference to the value of certain eligible assets provided as collateral for such loan. Such assets also count towards the "borrowing base" against which a bank will advance. A subscription facility's collateral package is anchored by the commitments of the fund's investors that have not yet been funded.

These financings tend to be structured as revolving credit facilities, giving the borrower readily available access to liquidity for the purpose of making investments, without having to call equity capital and wait for the contributions to be received. The short period required to draw advances (typically one to three days) enables quick execution of underlying asset acquisitions or other investments. Such investments may include back-to-back funding arrangements in the case of debt funds, which increasingly look to offer similar products to underlying borrowers with the inherent short-term liquidity requirements. Subscription facilities also allow funds to improve cash management by avoiding inefficient holding of reserves for covering expenses, and often provide additional flexibilities, such as availability of alternative currencies and letters of credit.

Although the security package may vary depending on the fund structure and other factors, a typical security package for subscription facilities comprises security over: (i) the unfunded capital commitments of the fund's investors; (ii) the right to make capital calls from investors, and receive proceeds of such capital calls in the form of contributions; (iii) the bank accounts into which the capital contributions are funded; and (iv) certain rights related to the foregoing (including the right to enforce against such investors) pursuant to the documentation evidencing such rights (including subscription agreements of the investors and organisational documents of the fund).

Because the collateral for a subscription facility is intrinsically tied to the obligation of the investors to make capital contributions (rather than the fund's underlying assets), lenders closely scrutinise the investor base of the fund and the legal relationship between the investors and the fund. The types of investors and the life-cycle stage of the fund will influence and help determine the optimal approach for calculating the borrowing base against which the loan will be advanced.

Investors are generally considered eligible, and typically categorised as either an "included investor" (usually institutional investors with a specific rating and/or sufficient financial strength) or a "designated investor" (other investors meeting relevant criteria). Certain investors may be ineligible due to restrictions on their ability to fund in particular situations, for example, due to regulatory reasons, or those for whom a lender lacks sufficient financial information. It is important to note that the uncalled commitments of ineligible investors still form part of the collateral package granted to lenders, typically leading to some element of over-collateralisation. Further, an otherwise eligible investor may subsequently become ineligible and its commitments disregarded due to certain specified exclusion events, such as a decline in its financial condition (including bankruptcy).

After determining the basic composition of investors that will be included in the borrowing base of the subscription facility, the parties negotiate appropriate advance rates and any applicable concentration limits in respect of these investors. Advance rates are the basic measure of the amount of credit a lender will allow a borrower, and are generally expressed as a percentage of the included investors' (up to 90–95%) and designated investors' (up to 65–70%) uncalled capital commitments.

We now commonly see further bifurcation of advance rates, depending on additional criteria. For example, there may be a higher advance rate afforded from the moment in time at which capital commitments over a certain threshold (sometimes referred to as a "hurdle") have already been funded. This feature caters to the natural cycle of an investment fund because, as capital is drawn, the amount of credit support available for a subscription facility decreases. However, a higher advance rate may alleviate or even equalise these consequences. From a lender's perspective, the diminished uncalled capital is counterbalanced by the investors having more "skin in the game". Another similar feature is a fluctuation of the advance rate based on the value of assets in the fund, when, as the value of fund assets increases over time, so does the percentage applied to uncalled commitments.

There are other potential approaches to categorising investors – for example, a now common segment of the US market functions on the basis of a "simplified" borrowing base with a (typically somewhat lower) "flat" advance rate against an aggregate investor pool. In this structure, the borrowing base generally encompasses all of a fund's investors, regardless of eligibility criteria or exclusion triggers (which is similar to the "coverage ratio" principle traditionally used in subscription lines in the UK market).

Concentration limits present a further refinement of how the overall borrowing base credit is distributed among various classes of investors, and are generally determined based upon the makeup of a particular fund's investor pool. Lenders often look to reduce their risk exposure through diversification and thus aim to calibrate the classes of investors within the borrowing base. This is done in order to ensure that, from their perspective, a disproportionate amount is not advanced against the uncalled capital commitment of a particular class, either individually or in the aggregate for such class. Historically, there has been focus on limiting the amount of credit that is attributed to investor categories such as individuals (natural persons) and their tax and estate planning vehicles. However, we have seen an increase in lenders' willingness to lend against such investor commitments.

A variation of this principle that we have seen banks propose is that they seek to ensure that the largest investor (no matter what class or category it would have otherwise been in) does not constitute more than a certain percentage of the overall fund commitments. On the other hand, in order to increase flexibility, lenders may consider holidays or waivers in respect of concentration limits (e.g. not apply them during a "ramp up" period during the fundraising stage after the first, but before the final, fund closing, when the initial investor pool is less diverse than it ultimately will be) or the upward flexing of applicable percentages to relax such requirements for a specified period.

From a legal perspective, sponsors and lenders alike pay attention to the organisational documents of the fund, which (within the statutory framework applicable to the particular entity in question) set forth the contractual obligation of the investors to fund capital if and when called. In addition to the general powers of the fund, certain express provisions authorising the borrower (or its general partner, manager or other controlling person) to incur debt and grant liens (including, importantly, a pledge of the uncalled capital commitments) without further consent or action by the investors are expected. Also commonly included are a host of other ancillary acknowledgments and consents for the benefit of subscription lenders (often as express third-party beneficiaries), which can provide additional comfort.

As the sophistication of market participants grows, much more attention is paid to subtle nuances and technical drafting of the fund documentation (typically the limited partnership agreement). This is true particularly in respect of certain provisions that have come to be increasingly negotiated between the funds and investors. These include investment "excuse" provisions (allowing an investor not to participate in a particular investment due

to regulatory, tax or other considerations specifically applicable to it) and other important elements with regard to the mechanics of funding, such as "overcall" provisions (which mitigate risk of another investor funding default) or any entitlement of the fund to "recycle" capital (such as to recall certain amounts previously distributed to the investors).

As a result of these developments, "investor letters" (i.e. separate bilateral arrangements between the lenders on the one hand, and the investors on the other hand, which would establish direct contractual privity between the lender and the investor) are now only rarely used. We will address certain situations in which obtaining such letters may be beneficial for structuring the subscription facility from both the borrower and lender perspective in more detail below.

The variations of fund structures and underlying investor pools can result in differing considerations, and typically require custom and complex loan documentation in each specific case. Below, we illustrate the need for bespoke tailoring in the context of: (i) funds of one and/or separately managed accounts (which may have only a single investor); (ii) complex commingled vehicles (which may have hundreds or more investors and utilise numerous entities that are part of one fund family); and (iii) by comparison, funds in the UK market.

Cinderella goes to the ball: The separately managed account

As discussed above, the investor composition of a fund is a key factor for lenders in establishing the borrowing base for a subscription facility. When there is only one investor, as is the case for "funds of one" or "separately managed accounts" (SMAs), certain unique considerations arise, including those stemming from an increased concentration risk. In our experience, the number of SMAs has continued to dramatically increase in recent years, as large institutional investors (including state and private pension funds, educational endowment funds, insurance companies and sovereign wealth funds) have been keen to put their capital to work faster than managers have raised a commingled fund. SMAs may also allow such investors to take advantage of customised structures, which can accommodate unique tax and/or regulatory requirements or investment objectives.

While, from a financing perspective, SMAs present some specific challenges, there are also certain advantages. Indeed, it appears that as the number of SMAs in the marketplace has increased, so too have subscription facilities available for these investment products, and lenders appear to be increasingly willing to extend credit to SMAs. Like any other fund, the terms of the organisational documents of an SMA must satisfy the general requirements of the subscription facility lender, but enhanced due diligence may often underpin a bank's SMA lending decision.

Many lenders view the facility as akin to making a loan to the underlying investor and so, as an alternative (or in addition) to incorporating certain provisions in the organisational documents, lenders may request that the investor in the SMA enters into an investor consent letter. The primary benefit of such letter is generally to establish a direct privity of contract between the investor and the lender. Such a letter might also address any other specific considerations that may arise in a particular context (for example, as many investors in SMAs are government pension plans, there may be sovereign immunity issues that lending against such investors might potentially present to banks). In the context of SMAs in particular, investor letters may be coupled with additional credit support documentation to the extent that an investor is utilising one or more intermediate entities through which it invests. This often takes the form of a "comfort letter" under which the ultimate creditworthy parent undertakes to keep the vehicle (which is the direct limited partner in the fund) sufficiently capitalised to meet capital calls.

Understandably, the treatment of such issues requires a highly individualised analysis that needs to be performed on a case-by-case basis. As compared to subscription facilities for multiple-investor funds, advance rates for the single-investor SMAs tend to be more customised and negotiated. While banks generally lend based on the creditworthiness of each investor, and would thus be expected to assign an advance rate for an investor in an SMA that is substantially equivalent to the advance rate such investor would receive if it were investing in a commingled fund, other factors may necessitate a different approach. For example, in an SMA scenario, lenders cannot rely upon a diversified investor base that, in the aggregate, reduces their exposure to an individual investor's funding failure. Further, as noted above, in many commingled fund facilities there are investors who do not qualify for inclusion in the borrowing base, but their uncalled capital commitments are still pledged as collateral and so effectively provide for "over-collateralisation".

There may be other terms in SMA subscription facilities for which lenders may seek a different regime, as compared to commingled fund subscription facilities. For example, certain exclusion events (i.e. events that, if they were to occur with respect to an investor, would trigger removal of such investor from the borrowing base) under a commingled fund subscription facility may be characterised as events of default (i.e. events that give the lender a right to accelerate the amounts outstanding under the facility and pursue remedies) under an SMA subscription facility.

Another approach to mitigating the increased risk profile of an SMA is that certain exclusion events that might otherwise be afforded a grace period, allowing the investor, the borrower and the lender to work out a potentially problematic situation, are either immediate breaches or the period is reduced. There is rationale for this approach; for instance, if the SMA investor defaults on its obligation to fund a capital call, the lack of any other investor commitments to fall back on makes it reasonable to characterise such an occurrence as an event of default. However, if the same failure to fund capital were to occur in a commingled fund, the typical subscription facility would simply no longer give credit for such investor's commitment in the borrowing base. Only if investors with material capital commitments (above agreed-upon thresholds) defaulted would an event of default be triggered under a commingled fund's facility, in most cases.

In a similar vein as the exclusion events, investor transfer restrictions may also be tightened in the credit documentation for an SMA.

Focusing on potential advantages, sponsors with multiple SMAs may be able to utilise the straightforward nature of the single-investor vehicle in order to achieve greater efficiency with respect to the facility documentation. Indeed, some sponsors have found that SMAs are generally well suited for employing the so-called "umbrella" technology, pursuant to which the same lender provides individual and separate loan commitments to multiple borrowers under one credit agreement.

Under these instruments, many of the terms are shared by all of the SMAs party to the loan document, but investor-specific terms (such as the pricing, the advance rate and the loan amount) can be different for each SMA. Importantly, each SMA remains severally (and not jointly) liable for its own borrowings and the distinct facilities are not cross-defaulted or cross-collateralised. This means that potential issues under one SMA's facility will not impact another SMA's facility, even if both are party to the same credit agreement. Umbrella facilities may allow sponsors to streamline negotiations into essentially a single set of documentation while putting multiple facilities in place.

The time and cost efficiencies of umbrella facilities has also prompted commingled funds to consider implementing such an approach, and the number of them employing this technology has increased. More and more managers are seeking to combine a number of subscription facilities for different funds (whether that be of different strategies or vintages) within one overarching framework. This promotes closer alignment of terms with the benefit that reporting and covenant regimes are kept consistent across a number of separate facilities, mitigating the monitoring and compliance burden that would result from diverging standards.

The town musicians of Bremen: Large commingled funds

At the other end of the spectrum, there are pooled investment fund vehicles with diverse investor bases, which may include a variety of institutional investors, as well as private wealth management clients (such as high-net-worth individuals and their family offices) and, at times, the sponsor's management and employees. Depending on the composition of the investor base, such funds often require, due to various tax, regulatory and other considerations, multiple entities through which the investors can access the underlying investments, resulting in structures that can be quite complex.

A frequently used technology is a multi-tiered structure, sometimes referred to as the "master-feeder" structure. This arrangement utilises two or more separate entities on top of each other; investors contribute capital through a "feeder" fund, which then passes on ("feeds") the capital to a "master" fund, which in turn makes investments, either directly or indirectly, through subsidiaries. In certain circumstances, there may be some investors who invest through the feeder fund, and other investors who invest into the master fund.

In other situations, a separate fund structure may be formed for different types of investors without there being an aggregating master fund, which is sometimes referred to as a "parallel fund" structure. For US-based sponsors, an initial fund is often formed as a Delaware or Cayman Islands limited partnership that is treated as a "pass-through entity" for US federal income tax purposes and typically includes taxable US investors. When the investor pool includes non-US investors and/or certain tax-exempt US investors, one or more separate "offshore" funds, which are treated as non-US corporations (or non-US limited partnerships) for US federal income tax purposes, are often formed in various jurisdictions (frequently the Cayman Islands, British Virgin Islands and Bermuda, and increasingly also European domiciles such as Luxembourg, Ireland and Scotland as well as the Channel Islands of Guernsey and Jersey).

The general trend appears to be that the complexity of fund structuring continues to evolve and increase as more investors are exploring different or new asset classes, and the regulatory and tax environment keeps developing. It is not unusual for a large fund with a widely diversified investor base to employ multiple parallel vehicles at the same time as they also utilise several layers of feeder funds. This often results in creating a complex web of dozens (or even hundreds) of entities, which requires a good understanding of the structure by both sponsors and lenders.

Regardless of jurisdiction and/or legal form, all of the entities in these types of structures are part of one fund family, and are managed by a common investment manager – such management can be accomplished in a variety of ways, including by utilising multiple affiliated entities and/or independent managers. Each of the various vehicles is typically a separate legal entity, though the exact characteristics may depend on how the relevant legal forms of the vehicles are treated in their applicable jurisdictions. In some cases, they may be statutorily required to act through another entity (for example, a Cayman Islands limited partnership acts through its general partner).

The considerations that determine the characteristics of each entity can contribute to the complexity of the structures in terms of which entities need to be party to the subscription facility documentation. Most multi-tiered funds need to ascertain at which level borrowings will be made (in other words, which entity will be the borrower under the subscription facility). This choice may be affected by any number of different factors, including tax and regulatory considerations, administrative ease and the operational requirements of the sponsor (for example, the ability to accommodate other creditors within the structure, whether that be for the provision of hedging, or structural leverage). To the extent that investor capital commitments are not made directly to the borrowing entity, consideration must be given as to how to mechanically ensure that a security interest in the collateral has been granted, directly or indirectly, for the lenders' benefit.

A "cascading pledge" structure is one potential method utilised to assure that lenders have an appropriate "path" to the ultimate source of capital commitments. In this scenario, the upper-tier feeder fund pledges the capital commitments of its investors to the lower-tier master fund, in order to secure such feeder fund's obligations to make capital contributions into the master fund. The lower-tier master fund then, in turn, pledges the capital commitments of its "investors" (i.e. the upper-tier feeder funds), and any rights under the pledge from the upper-tier feeder funds, to the lenders to secure such master fund's obligations as a borrower under the subscription facility.

Other possible alternatives include an arrangement where (if permissible from a regulatory and tax perspective) the feeder fund may become a party to the subscription facility agreement and/or security agreement with the lender. Under this approach, the feeder fund may become a co-borrower of the loans, become a guarantor of the indebtedness incurred by the master fund, or just provide a "naked" pledge of the investors' capital commitments directly to the lender.

There are situations where it may not be possible to have multiple parallel entities within a fund structure jointly and severally liable for repayment of the loans and, in some instances, the "onshore" and "offshore" entities may be required to enter into separate credit agreements. Another example is a dual "levered" and "unlevered" silo structure, where one fund silo does not incur debt at all, or only takes advantage of a subscription facility to manage cash-flows, but the other fund silo also obtains asset-based leverage.

If separate credit agreements are put in place, they may or may not be permitted to be cross-collateralised, whether for tax and/or regulatory reasons or because of an understanding with the investors in the separate vehicles. This effectively means that each of the parallel vehicles must rely on a borrowing base comprising only capital commitments of its own investors. As banks typically provide different advance rates and concentration limits for different investors based on their underwriting criteria, the borrowing capacity of one silo may be different from the borrowing capacity of the other silo(s). Since sponsors ordinarily aim to manage borrowings on a consistent level across the various vehicles in a fund family, the ability to borrow might then be dictated by the vehicle with the lowest borrowing capacity.

One potential solution may be (where this is acceptable from a commercial perspective and permitted under the applicable fund documents) to provide for a "limited" cross-collateralisation (by certain assets only), cross-guarantee and/or cross-default between the individual credit agreements. This might allow the borrowing base to be calculated on an aggregate basis for all the silos. Another approach may be to utilise "investor letters", which, by giving an increased level of comfort to the lenders, may allow for higher advance rates and/or concentration limits.

The golden goose: The European lands of magic

Over time, the internationalisation of the subscription finance market has influenced the documentation and transaction terms of subscription facilities in the European market. US-based sponsors have been expanding their investment activities across the Atlantic and continue to seek subscription facilities similar to what they have been accustomed to in the US. In addition, European and US-based lenders have increasingly offered subscription facility terms similar to those seen in the US market.

Nevertheless, despite a trend for convergence of the terms, broadly speaking, certain differences persist due to differing approaches to credit evaluation and local law requirements with respect to the creation and perfection of security interests in collateral.

The relatively recent trend for ESG-linked financings in the European finance market is also increasingly becoming a feature incorporated within subscription facilities in the US market, where a number of sponsors have sought to incorporate ESG-driven financing terms. While Europe may have adopted ESG principles earlier than the US and Asia, those considerations have very quickly picked up steam in those markets as well and are now becoming commonplace.

Subscription facilities in the UK market were historically almost exclusively the product of "relationship" deals, with lenders primarily focusing on the track record of the larger sponsor group and success of their earlier vintages when determining whether to offer a subscription facility to an individual fund. This difference in approach used to be reflected in some of the terms typical of subscription facilities in the UK market. For example, traditionally, subscription facilities in the UK market frequently used the "coverage ratio" to limit the amount that may be drawn under the facility at any given time.

The coverage ratio is the ratio of the uncalled capital commitments of the included investors to the aggregate indebtedness of the fund, and is typically set at no less than 1:1. Notably, the coverage ratio approach does not typically involve applying advance rates to the uncalled capital commitments of included investors, meaning that once an investor is deemed an "included investor", the borrower receives credit for 100% of that investor's uncalled capital commitment.

In recent years, the coverage ratio approach has become less common in the UK market and is frequently substituted by a US-style borrowing base model. Parallel to the development of the borrowing base methodology, investor exclusion events have also been refined. These events are typically narrower in scope for facilities that apply a borrowing base methodology, but are often tailored to particular investors and address a greater number of specific events that would result in a reduction of the borrowing base. Lenders are increasingly focused on the exclusion event definitions – a trend that goes hand in hand with the increased focus on, and diligence of, organisational and fund-related documents.

Irrespective of the internationalisation of the subscription finance market and the convergence of certain terms of subscription facilities in US and European markets, the granting of security interests in respect of a borrower's obligations under a subscription facility remains specific to the jurisdiction applicable to the relevant fund entity. Granting and perfecting security interests over the uncalled capital commitments of the funds' investors, the rights to call capital commitments, and the bank accounts into which any capital contributions are funded, represent the cornerstone on which the collateral base of the subscription facilities are built.

In the US market, to perfect the security interest and enforce the lender's rights against third parties, generally a UCC-1 financing statement should be filed (and a control agreement entered into with respect to pledged accounts). Under English law, however, the security interest of lenders in the rights to call capital is typically created pursuant to an assignment by way of security, which is perfected by notification to the investors in the fund. To manage and protect the relationship with their investors, borrowers often seek to negotiate the timing for the delivery of the notices to investors, and are also highly sensitive to the form of any such notifications. This process is balanced against the lenders' desire to obtain a perfected security interest reasonably promptly after the facility is made available.

A happy ever after? The story continues…

In a record 2021 for the fund financing market, we have again witnessed a sustained and steady increase in the volume and size of subscription facilities, and overall other fund financing transactions more broadly. A key driver behind the market's solid growth has been the willingness of sponsors and investors to work with lenders on devising and implementing customised solutions addressing all parties' needs and requirements. Thus, market participants have been successful in developing products flexible enough to adapt to evolving fund structures and prospective new investors as well as liquidity solutions for the "long run" that can cater to the different stages of the life of a fund.

This is evidenced by a growing number of combinations of subscription facilities and asset-based facilities (collateralised by the underlying fund investments). Such financing can take the form of hybrids (with a collateral package that consists of both uncalled capital commitments and underlying investment assets) or other bespoke instruments (for example, where a traditional subscription-based borrowing base is enhanced by a component based on the value of the underlying investment assets, but without a corresponding pledge). Indeed, by coupling the components of a subscription facility with those of asset-based financings, a solution can be tailored to support the fund's ongoing liquidity requirements beyond the termination of the investment period while balancing the different risk profile at that stage of the fund life. This trend is likely to continue and expand as fund products evolve further, in particular in the light of the increased interest in semi-liquid fund products and continuation funds.

Additional products, such as capital provided in the form of preferred equity, GP/management fee financing solutions, and employee loan programmes continue to be widely utilised and developed. Moreover, there has been a convergence of the fund financing market with the larger bond and capital markets where we are observing an increasing appetite for syndicated facilities that can take the form of rated notes and even incorporate features historically seen in securitisations. We believe that the future of these products and markets is intrinsically tied together and, for certain types of deals, they will eventually combine.

As ESG-compliant investments in general become more prevalent, the broader loan market is developing financing products that include ESG-linked criteria to reward positive performance of borrowers in the related key metrics. European regulatory requirements to classify funds under the Sustainable Finance Disclosure Regulation as either not investing in accordance with sustainability factors (article 6), promoting sustainability (article 8) or having sustainability as an investment objective (article 9) have led to an increase in funds identifying as sustainable. Legislation in this area, to be implemented in England and Wales next year, is likely to further shape the fund finance market. While, in the US, the regulation

of ESG is in its nascent stages, the Securities and Exchange Commission (as one of the key regulators of the financial investment and advisory industry) has taken a keen interest in the top and published a voluminous proposal for future rulemaking.

In credit facilities in particular, a margin adjustment – either a discount if certain ESG-related performance criteria are met or a premium if the criteria are not met – may be used to incentivise the borrower to meet certain ESG-related thresholds. Likewise, in the fund finance market, there is a noticeable and accelerating trend towards ESG criteria, including facilities where the interest rate is determined by a ratchet mechanism based on agreed key performance indicators referencing the fund's portfolio companies (or, in the case of debt funds, the performance or percentage of their own loans with such criteria), or external third-party ratings, in each case tested on a periodic basis. The variety of ESG metrics is also developing and covers areas from renewable energy investments to gender and race equality on management boards of portfolio companies.

While a number of the foregoing investment strategies and debt products are as yet relatively new developments, we expect the market to evolve and align over time, gravitating towards increased consistency in principles and reporting standards.

We believe that the popularity of subscription facilities is driven in part by the strong performance these loans have demonstrated over extended periods of time, and the strength of the alternative asset sector, as well as the continued ability of sponsors and lenders to craft solutions that meet the growing needs and complexities of today's investment fund structures. Despite the broader markets encountering some tumultuous times in 2022, with significant geopolitical developments as well as unexpected economic challenges (with a sudden and significant increased global inflation), the fund financing space has remained largely stable and terms of the underlying financing documents generally consistent.

We remain optimistic about the outlook for the industry, which, due to the versatility of its products and adaptability of market participants, has shown its resilience to difficult conditions and the capacity to weather challenges so far.

* * *

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The Legal 500 UK recognises Jons in Investment Funds: Fund Finance and Acquisition Finance, Bank Lending: Investment Grade Debt and Syndicated Loans. The publication quotes a client praising Jons for "offering practical advice" and bringing "innovative legal solutions and market experience to their work". Jons is also recognised by *IFLR1000* in the Banking category.



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