



Funds in Focus 2019

Private Funds Annual Review Conference

Private Credit Trends:
Platform & Strategy Evolution;
Investor Demand & Fundraising;
Capital Deployment & Restructurings

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Proskauder»

Agenda

I. Introductions

II. State of the Market

- A. Trends in U.S. & European Institutional Demand
- B. Trends in U.S. Retail Demand
- C. Deals in the U.S. Middle Market Today

III. Platform Diversification; Accessing Retail Capital

- A. Trends in U.S. & European Structures for Institutional Investors
- B. Trends in U.S. Retail Structures
- C. Retail Investing: Build it or Buy it

IV. Deal Flow Trends; The Restructuring Cliff

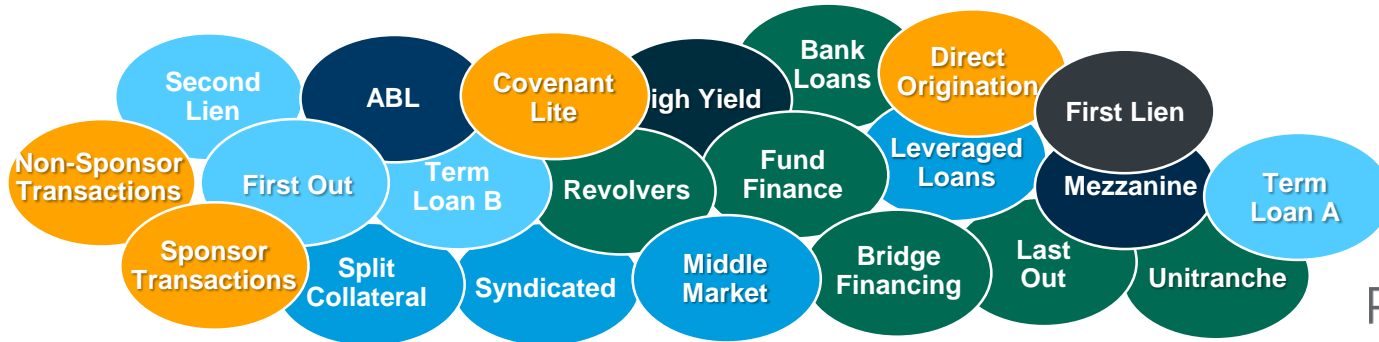
- A. Top Five Myths of Private Credit
- B. Forecasting for the Next Credit Cycle

V. Closing Remarks

II. State of the Market

State of the Market

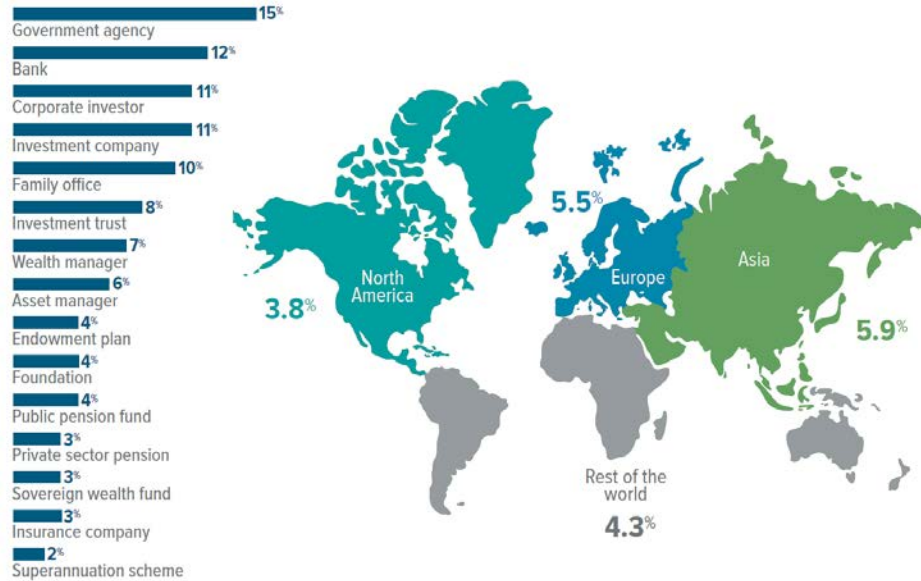
- After the global financial crisis, the reduction in bank lending boosted demand for private debt.
 - North America and Europe have dominated in recent years, but a growing number of jurisdictions have also seen an increase in demand for private debt.
- Private debt as an asset class has matured over the last decade.
 - E.g., increasing activity in the private debt secondaries market for fund stakes and loan portfolios.
- Capital is being deployed across a diversified universe of assets.



A. Trends in U.S. & European Institutional Demand

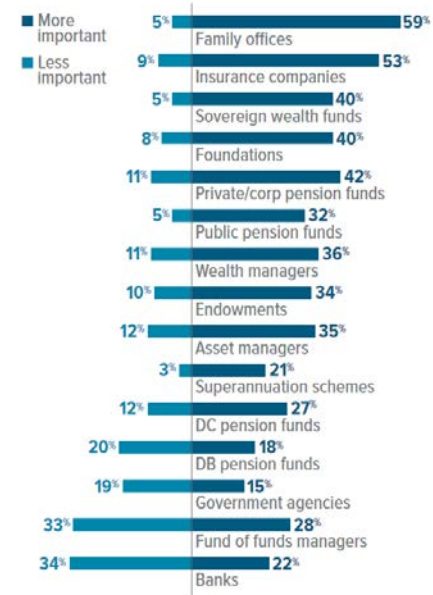
Institutional Investors

Average of Portfolio Allocation to Private Debt, 2018



Source: Preqin, Private Debt Whitepaper, Preparing for the Unknown, 2018

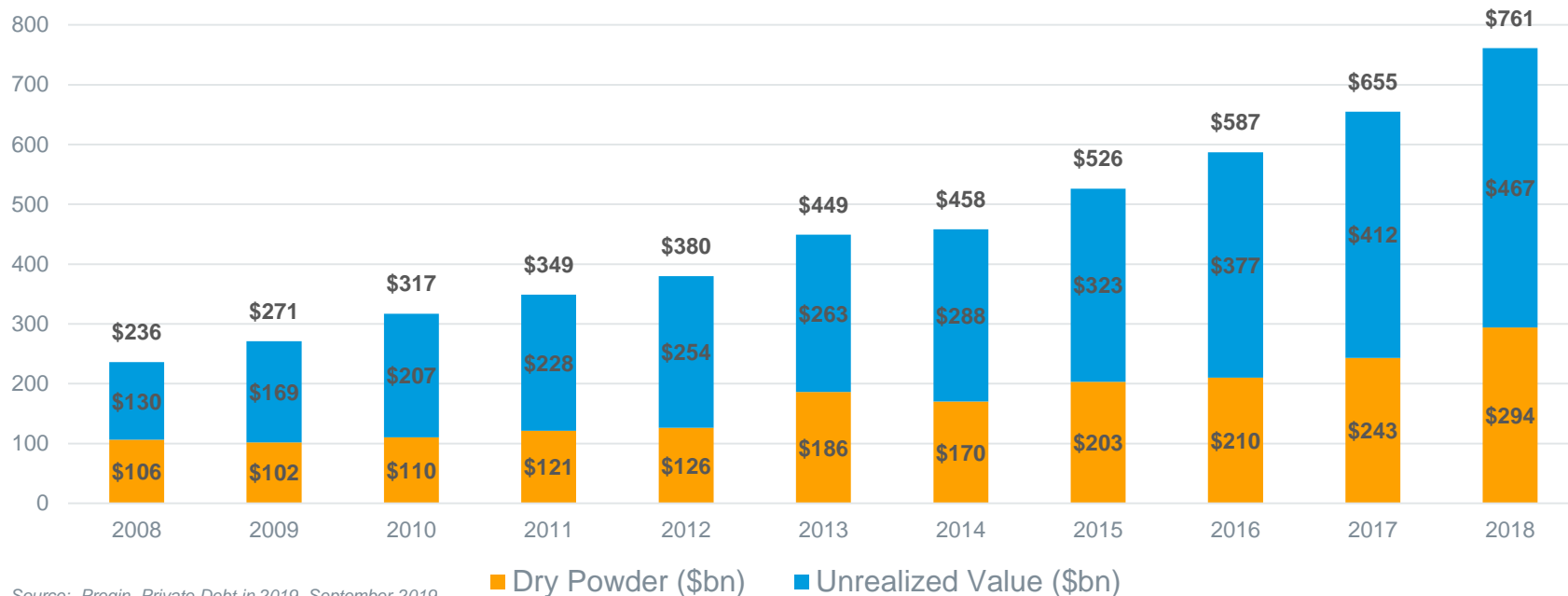
Survey of Private Debt Sponsors Responding to “How important do you think the following types of investors will be as a source of capital in 2023?”, 2018



Source: Preqin, Private Debt Whitepaper, Preparing for the Unknown, 2018

Private Debt AUM Has Increased 3x Over the Past Decade

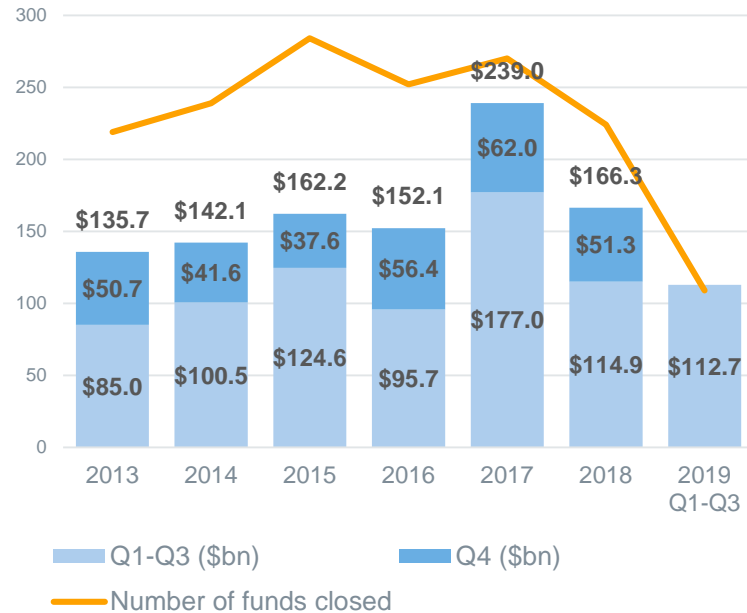
Private Debt Assets Under Management, 2008-2018



Source: Preqin, Private Debt in 2019, September 2019

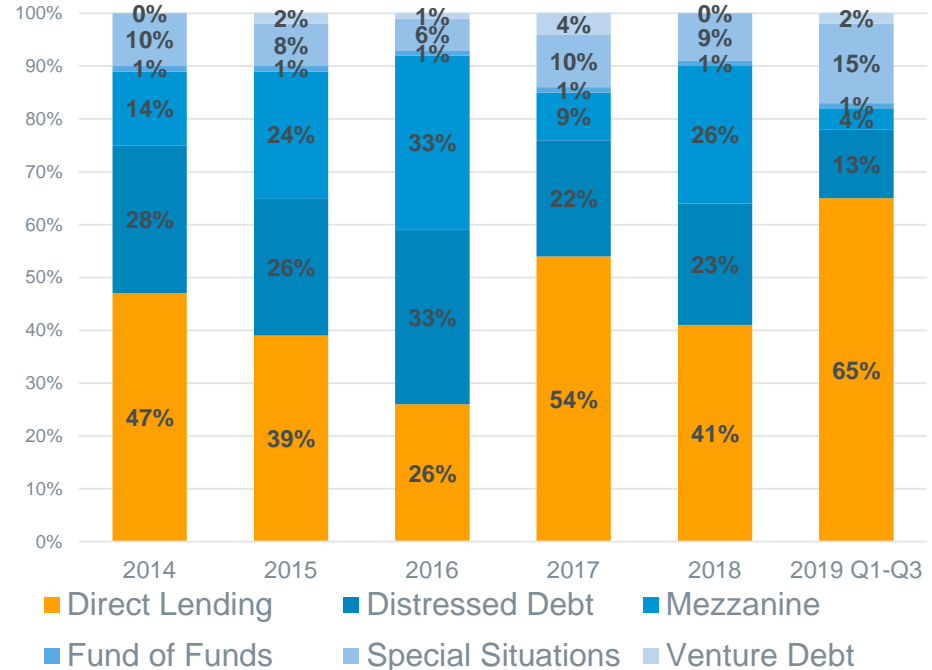
Private Debt Fundraising

Amount of Capital Raised by Number of Fund Closings, 2013-2019 Q1-Q3



Source: Private Debt Investor, Fundraising Report H1 2019

Proportion of Aggregate Capital Raised by Strategy, 2014-2019 Q1-Q3



Source: Preqin, Private Debt in 2019, September 2019

Trends in U.S. Institutional Demand

- The U.S. has consistently been a popular destination for investor capital.
 - Continued appetite (e.g., non-U.S. institutional investors, insurance companies).
- Huge expansion in existing asset management platforms.
- Newly established credit managers.
- Continued trend of Separate Accounts and Funds-of-One in addition to traditional pooled funds.
 - Highly negotiated, specialized terms.
 - Sponsor's desire to fit within the overall platform and expertise must be balanced with the investor's desire to customize for specific assets, geography and return profile.
- Continued pressure on fees, even as demand for customization grows.
- Growing interest in evergreen structures.

Trends in European Institutional Demand

- Upward trajectory over the last decade as the European industry matures.
 - However no full business cycle in the market yet.
- Institutional demand growing, especially from local authority pension plans and U.S. and Asian investors.
- Huge expansion in new and existing sponsors—ranging from those creating a debt arm of their business, to spin outs starting first-time credit funds and to established credit sponsors expanding their credit strategies.
- Large wall of capital available for deployment in a borrower-friendly market.
- Push in different directions of the capital structure in search for yield—for example, venture debt and increasingly larger deals where fewer sponsors operate.

Sponsor Conflicts of Interest

- Conflict matters generally arise more often with diversified credit managers.
 - Conflicts with other products (overlapping or not)
 - Allocation of deals and expenses
 - Priority of allocations and disclosure
 - Impact of growing SMA businesses on commingled fund mandates and other investors
- Considerations:
 - Contract (e.g., organizational documents and side letters)
 - Regulatory (e.g., client consent and disclosures as required under the Investment Advisers Act)
 - Fiduciary duties under law
 - Investment adviser's allocation policy
 - Offering document disclosures

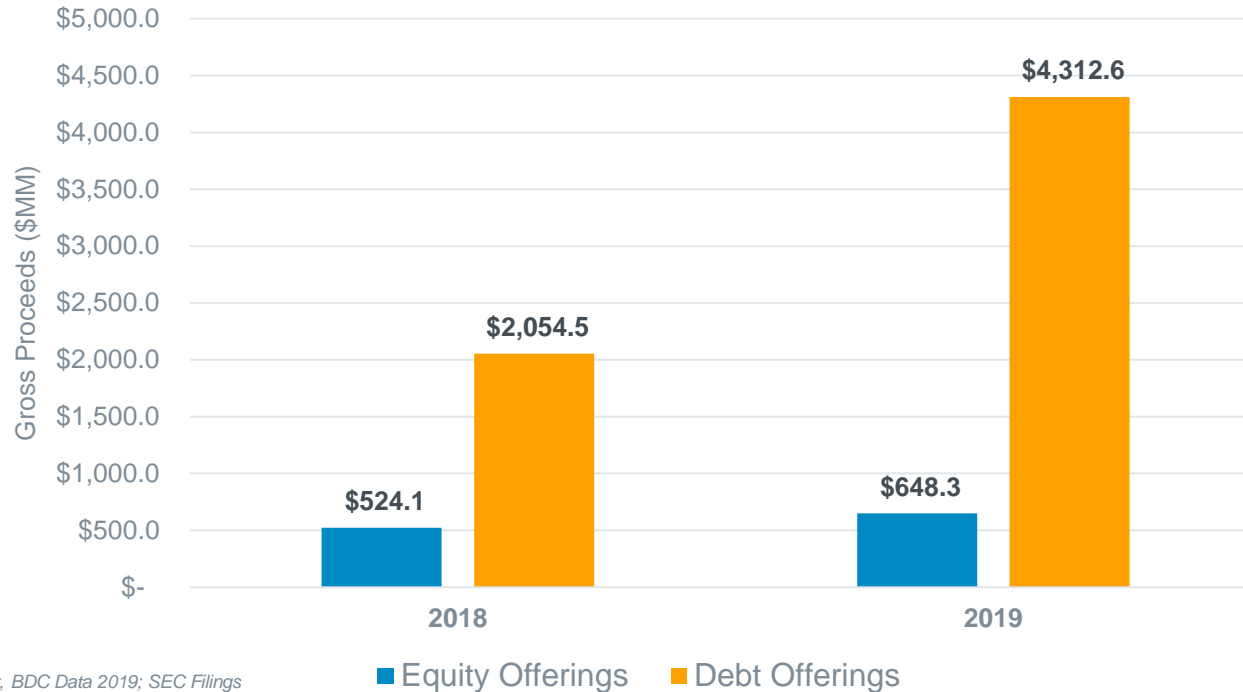
B. Trends in U.S. Retail Demand

Retail Investors

- Retail investors are typically viewed as being divided into 4 categories based on having investable assets (excluding primary residence, collectibles, etc.) of:
 - \$100 thousand - \$1 million (aka “mass affluent”),
 - \$1 million - \$5 million (aka “accredited investors”),
 - \$5 million - \$30 million (aka “mid-tier HNWIs”), and
 - \$30+ million (aka “ultra HNWIs”).
- As of the end of 2018, HNWIs (i.e., accredited investors, mid-tier HNWIs and ultra HNWIs) globally represented \$68.1 trillion of wealth (\$19.6 trillion in North America).
- Retail investors represent a diversified and—compared to the institutional investor base—underpenetrated segment of the potential investor universe.
- Popular structures for accessing retail capital include Business Development Companies (“**BDCs**”) (listed*, non-listed or private) and Registered Closed-End Funds (“**CEFs**”) (tender offer or interval funds).

Trends in Listed BDC Offerings

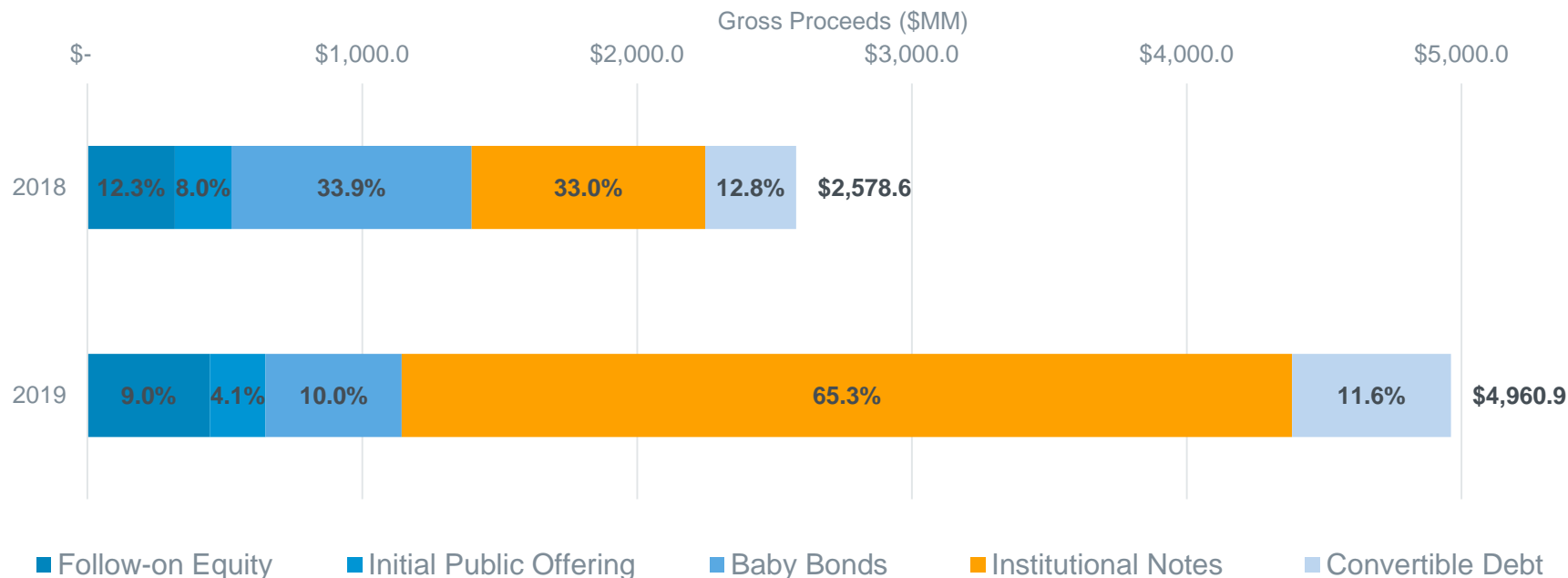
Aggregate Amount Raised in Equity vs. Debt Listed BDC Offerings by Year, 2018-2019 Q1-Q3



Source: Proskauer, BDC Data 2019; SEC Filings

Trends in Listed BDC Offerings (cont'd)

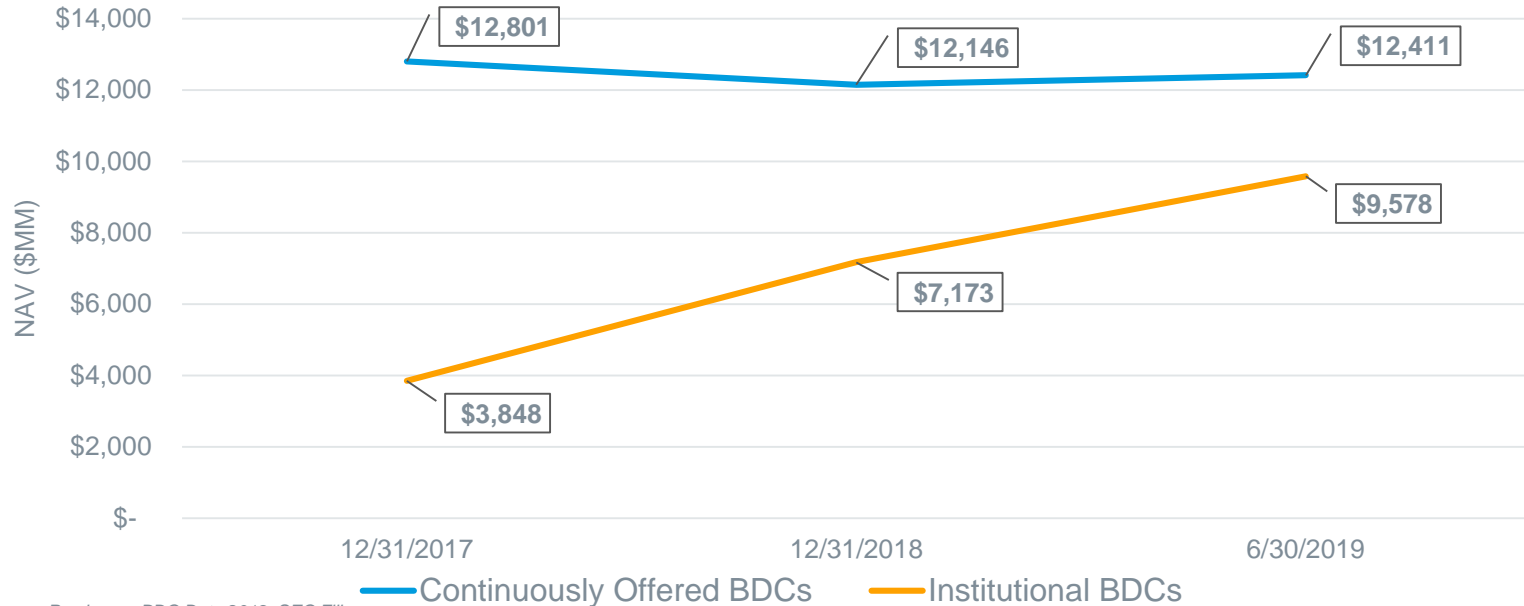
Aggregate Amounts Raised by Type of Listed BDC Offering, 2018-2019 Q1-Q3



Source: Proskauer, BDC Data 2019; SEC Filings

Continuously Offered & Institutional BDCs

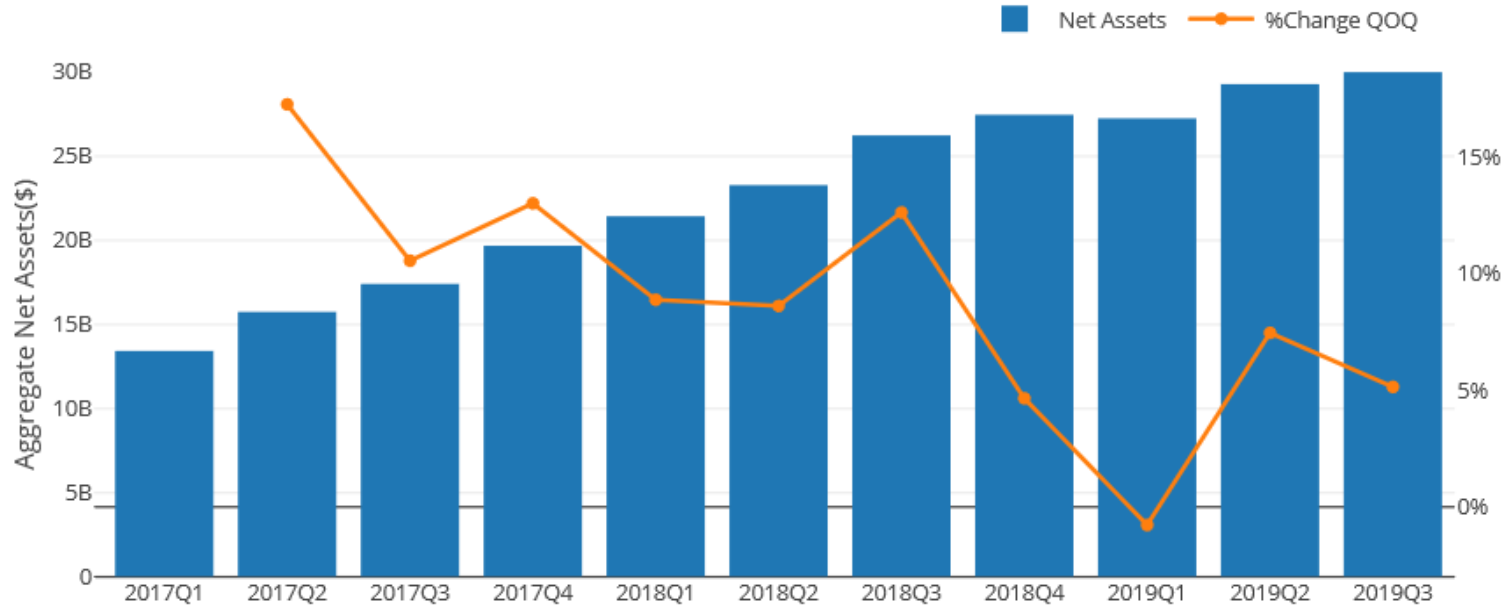
NAV of Continuously Offered & Institutional BDCs as of December 31, 2017, December 31, 2018 and June 30, 2019



Source: Proskauer, BDC Data 2019; SEC Filings

Interval Funds Net Asset Growth

Interval Fund NAV, Q1 2017-Q3 2019

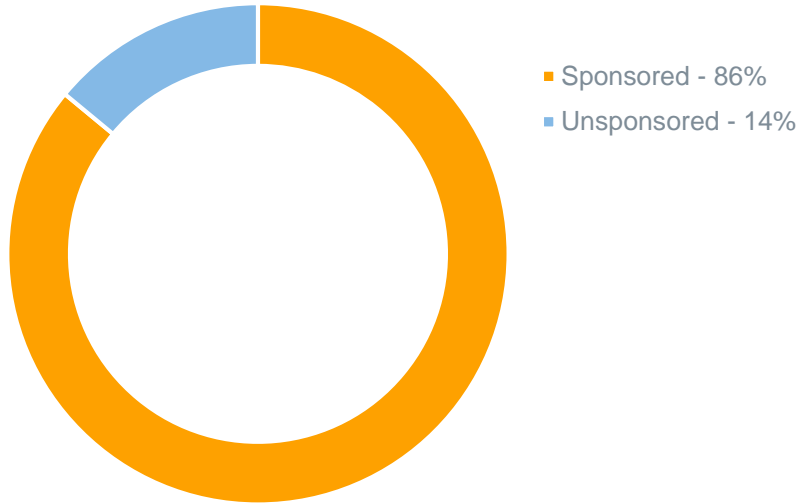


Source: Interval Fund Tracker

C. Deals in the U.S. Middle Market Today

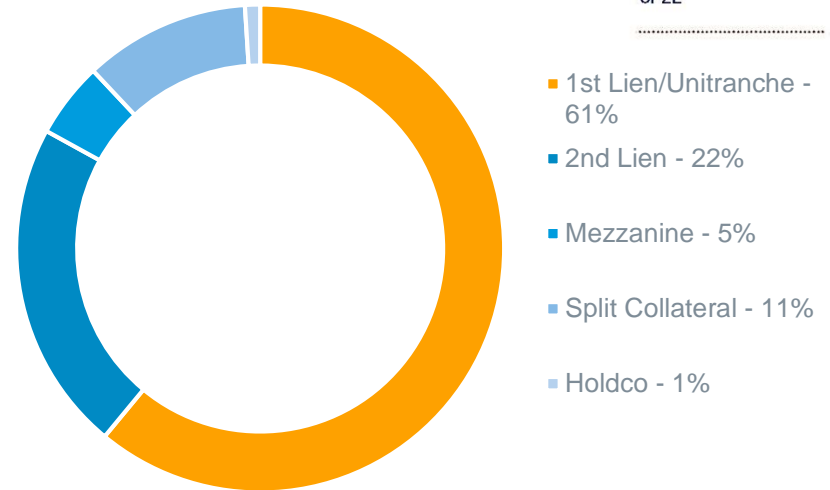
U.S. Deal Structures

Sponsored vs. Unsponsored Deals (2018)



Source: Proskauer, 2018 Private Credit Insights

Deal Type (2018)



Source: Proskauer, 2018 Private Credit Insights

III. Platform Diversification; Accessing Retail Capital

A. Trends in U.S. & European Fund Structures for Institutional Investors



U.S. Structuring Trends

- Structuring for U.S. investors requires minimal effort.
- Marketing abroad invites a cost-benefit analysis, as structuring for U.S. tax consequences to non-U.S. investors drives complexity and cost.*
 - Continued dominance of horizontal “season and sell” structures
 - Increasingly common to use treaty structures for senior debt funds
 - Increased use of leveraged blockers

* Refer to Appendix A for an overview of structuring solutions and tax considerations for U.S. direct lending funds.

Tax Considerations for U.S. Direct Lending Funds

Why are U.S. direct lending funds different than other credit or private equity funds?

- A non-U.S. person that is engaged in a U.S. trade or business (directly or through a partnership) is: (1) subject to U.S. federal income tax on a net-income basis on any income effectively connected with the business (“**ECI**”), (2) required to file U.S. income tax returns, and (3) may be subject to state and local taxes and filing obligations.
- There is a safe harbor under which a non-U.S. person (that is not a dealer) is not treated as engaged in a trade or business within the United States as a result of “trading in stocks and securities” for its own account.
 - However, the IRS takes the view that funds that originate loans and have U.S. managers do not qualify for the trading safe harbor and are engaged in a trade or business in the United States.
- As a result, non-U.S. investors in funds with U.S. managers that originate loans are potentially subject to U.S. federal income tax on ECI as high as 44.7% (21% corporate rate and 23.7% branch profits tax).

Popular Structures for U.S. Direct Lending Funds*

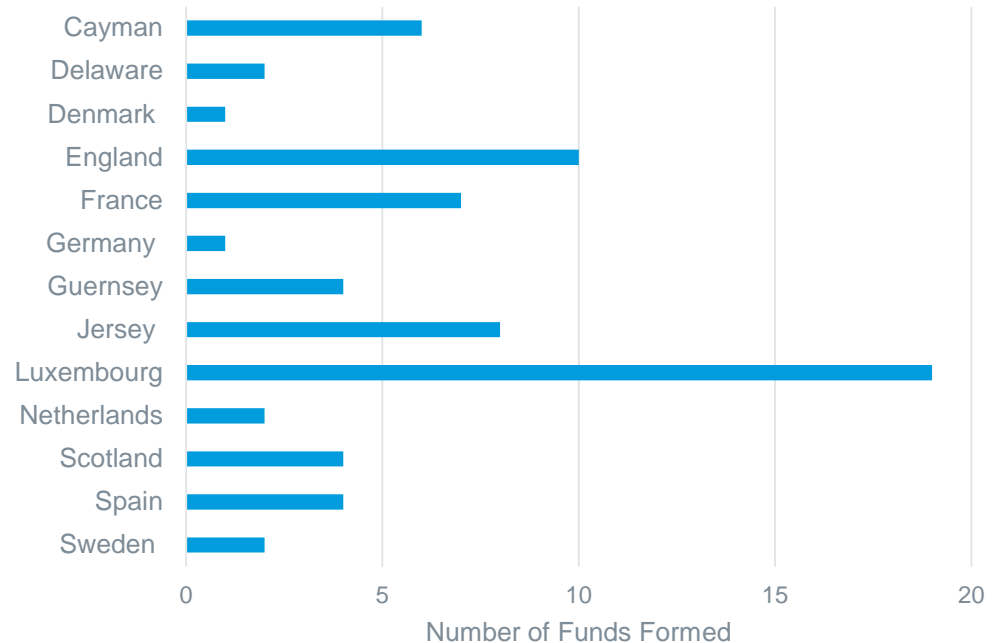
- “Treaty” funds (or “independent agent” funds):
 - “Bring your own treaty”
 - Established in a treaty jurisdiction (Luxembourg or Ireland)
- “Season and sell” structures:
 - Horizontal Seasoning
 - Vertical Seasoning
- Leveraged blockers
- BDCs/ CEFs

* Refer to Appendix A for an overview of structuring solutions and tax considerations for U.S. direct lending funds.

U.K./European Structuring Trends

- Brexit planning slowed formations of U.K. vehicles.
- Large uptick in European funds being formed in Luxembourg, especially for larger sponsors (sizeable cost considerations).
- Fund jurisdiction heavily impacted by anticipated investor profile.

Domicile of European Funds Formed in 2019



Source: Proskauer, *Under the Microscope: Fundraising Terms and Trends*, March 2019

Why Luxembourg?

- The Luxembourg limited partnership (SCSp) is designed to operate in a similar way to English, Cayman and Delaware limited partnerships.
 - Tax transparent
 - Onshore for regulatory purposes
- Luxembourg S.à r.l is also common in direct lending strategies.
- Investor preference for onshore EEA AIFs with an E.U. AIFM.
- Sponsor preference for continued use of AIFMD marketing passport.

B. Trends in U.S. Retail Structures

Business Development Companies (BDCs)

What Is a BDC?

A type of closed-end fund that elects to be subject to certain provisions of the Investment Company Act of 1940 (Sections 55-65) (“**1940 Act**”).

- Created by Congress in 1980 to provide capital to small/middle market companies and restructuring companies.
- BDCs are not required to adopt a particular investment strategy, although most tend to be credit-focused.
- Managed internally or externally.
- Listed, unlisted or private.
- Typically operated as a “RIC” under Subchapter M of the Internal Revenue Code.
- Hybrid of an investment company and operating company—subject to Securities Exchange Act of 1934 (“**1934 Act**”) reporting (e.g., 10-K, 10-Q and 8-K) instead of 1940 Act reporting (e.g., N-CSR, N-PORT).

What Is a “Public”/“Listed” BDC?

A BDC that lists its common equity on a national securities exchange (e.g., the NYSE or Nasdaq).

- Being listed on an exchange means:
 - Subject to the applicable exchange’s corporate governance requirements.
 - Unlike CEFs, BDCs are not exempt from most of the exchange’s governance requirements (other than ability to use 1940 Act definition of “interested person” in lieu of the exchange’s definition of “independence”).
 - Any retail investor can purchase shares of the BDC (no suitability requirements).
 - The investment in the BDC is liquid (although, trading volumes of a number of BDCs—particularly those with smaller market capitalizations—may be limited).
- The trading price is subject to market forces and may be volatile.
- Listed BDCs often trade at a discount to net asset value (i.e., the price at which the shares are sold on the exchange is less than the value of the BDC ascribed to such shares), which can limit ability to access equity capital markets.

What Is a “Non-traded”/“Continuously Offered” BDC?

Offering registered under the Securities Act of 1933 (“**1933 Act**”); shares are not listed on a national securities exchange, but issued on a continuous basis.

- Suitability requirements for investors.
 - Gross annual income of at least \$70,000 and net worth of at least \$70,000 OR net worth of at least \$250,000.
 - Higher requirements imposed by certain states.
- Continuously offer shares (with closings generally occurring every 2 weeks) at a price that approximates (but is at least as high as) net asset value per share.
- Generally offer liquidity to investors by:
 - Offering to repurchase up to a certain percentage of shares each quarter, and
 - Seeking to complete a liquidity event within 5 to 7 years after terminate offering (e.g., merger, IPO/listing, etc.).

What Is a “Non-traded”/“Continuously Offered” BDC? (con’t)

- Not exempt from “blue sky” regulations.
- Distribution is typically through independent broker-dealers (e.g., LPL/Ameriprise) or RIA channels, which often require the BDC to clear “blue sky” requirements in 40 states before admission to the platform.
- Less popular structure given changes to FINRA rules a few years ago.

What Is a “Private” BDC?

- Typically sponsored by large private equity/credit firms with an existing investor base.
 - Focus on existing institutional investors with whom manager has relationships and/or individuals who are on HNW platforms of certain financial institutions (e.g., Morgan Stanley, Merrill Lynch)
- Offering not registered under 1933 Act.
 - Common stock is sold in reliance on private placement exemptions (typically Reg. D).
 - No blue sky registration.
- File a Form 10 to register under 1934 Act.
- Securities not listed on a national securities exchange.
- Typically feature drawdown structure that minimizes cash drag.
- Generally expect to pursue a liquidity event within a certain number of years (often 5 to 7 years after initial closing) and/or have a limited term.
- Formation transactions can be a means to raise initial capital, but must be completed prior to BDC election.

Are BDCs the Right Option?

- Depends on
 - Type of sponsor
 - Well-suited for sponsors that are SEC-registered with a developed compliance infrastructure.
 - Targeted investor base
 - Anchor, foreign, tax sensitive, yield demand
 - Type of investments (i.e., broadly syndicated vs. originated)
 - Implications on broader credit platform
 - E.g., 1940 Act-affiliated transaction restrictions
 - Cost and risk appetite
 - Consider regulatory, valuation and litigation risk.
- Limited number of IPOs since 2014, as fundraising has largely been focused on private BDCs. Only 3 in the last 4 years—each was an IPO of a private BDC.

Benefits of BDCs

- No requirement that investors be “accredited investors” or “qualified purchasers”
- Access to “permanent capital” in the public capital markets
- Flow-through tax treatment and ECI/UBTI blocker with RIC election
- “Private fund”-like performance fees (i.e., base management and incentive fees)
- Publicly available financial information through quarterly reporting
- No 25% plan asset limitation (except for private BDCs) under ERISA, unlike private funds
- Potentially more diversified portfolio
- Reduced 1940 Act burdens compared to CEFs (e.g., leverage, affiliated transactions)

Comparison – Private BDCs & Private Funds

Term	Private BDC	Private Fund
Liquidity for Investors	<ul style="list-style-type: none"> • Limited ability to sell until IPO or other liquidity event • Liquidity through distributions or built in liquidation • Limits on ability to repurchase stock 	<ul style="list-style-type: none"> • Limited ability to sell • Liquidity through distributions • Withdrawal typically only permitted if required for regulatory purposes
Typical Sponsor Economics	Management fee plus incentive fee (income and capital gains)	Management fee plus incentive fee or allocation of carried interest
1940 Act	Registered – subject to multiple regulatory restrictions (i.e., leverage, eligible investments & capital structure)	<ul style="list-style-type: none"> • Exempt – no regulatory limitations around use of leverage or eligible investments • Must comply with an exemption under Section 3(c) (e.g., 3(c)(1)/(7))
1934 Act	Subject to typical public reporting requirements under the 1934 Act	No required public reporting
1933 Act	Exempt – generally, offerings made under Reg. D to accredited investors	Same as private BDC

Comparison – Private BDCs & Private Funds

(cont'd)

Term	Private BDC	Private Fund
Timing	<ul style="list-style-type: none">• Relatively quick launch to closing, but may take longer to educate investors on product• Requires SEC filing of Form 10	Relatively quick launch to closing
Cost	High, including at start-up and ongoing	Medium
Affiliate Transactions	Limitations on joint investing and principal transactions with other accounts and funds managed by the same adviser	Few regulatory limitations; must have appropriate disclosure/consents
Domicile	Must be U.S.	Can be U.S. or non-U.S., which may be helpful for marketing in Europe

B. Trends in U.S. Retail Structures

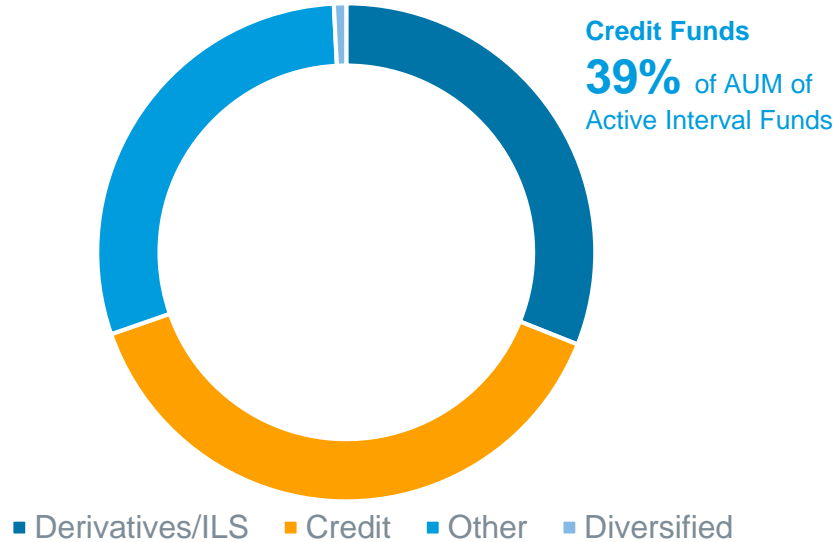
*Registered Closed-End Funds (CEFs) – Interval Funds
& Tender Offer Funds*

What is an Interval Fund?

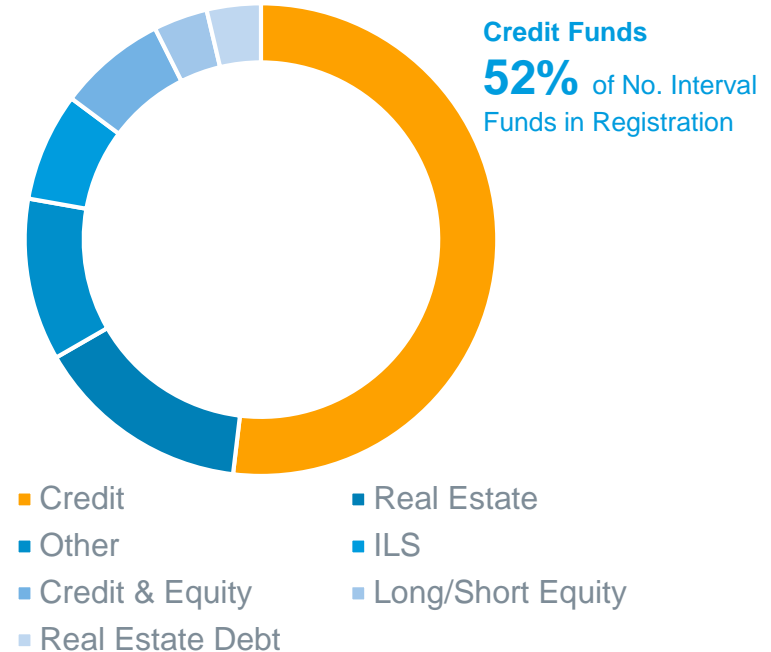
- An interval fund is registered under the 1940 Act as a continuously offered, closed-end investment company.
 - Files a registration statement with the SEC on Form N-2
 - Separate trust/corporate entity
 - Issues 1099s to investors (if elect “RIC” tax status)
 - Subject to the requirements of the 1940 Act
 - Often can be registered under the 1933 Act
 - Exempt from ERISA investor limitations (i.e., the “plan asset rule”)
- Interval funds operate in accordance with Rule 23c-3 under the 1940 Act, which requires the fund to engage in a mandatory, periodic repurchase offer to buy back shares at NAV.
 - Most undertake quarterly repurchase offers, but there is considerable variance regarding the percentage of shares offered to be repurchased at each interval.
- More than half have been granted or have applied for SEC exemptive relief to offer multiple share classes.

Interval Fund Strategies

Assets Under Management of Active Interval Funds by Strategy (Nov. 2019)



Number of Interval Funds in Registration by Strategy (Nov. 2019)



Trends in Interval Fund Formation

- In 2018, a record number of new funds launched in 2018, and total net assets in interval funds increased 41% to reach approximately \$27.5 billion.
 - Most recently, interval fund net assets topped \$30 billion in Q3 2019 with over 75% of active funds reporting net asset increases.
- Strong performance has driven solid fundraising—3 new interval funds launched in Q3 2019, and there are currently 25 interval funds pending with the SEC in registration.
- Long/Short Equity, Real Estate, and Credit strategies are all included in the list of fastest growing funds.
- Over the past two years, interval fund registrations have surpassed more “traditional” retail alternative structures such as non-traded REITs and BDCs.

What is a Tender Offer Fund?

Conduct continuous offerings, similar to interval funds, but operate under different federal securities laws.

- 1940 Act-registered closed-end fund.
 - No election to operate under Rule 23c-3.
- Shares continuously offered on “shelf” registration statement under Rule 415 under 1933 Act.
 - Pending SEC rulemaking on offering reform would streamline shelf registration statements for CEFs, including tender offer funds.
- Discretionary repurchases conducted pursuant to Section 23(c)(2) of 1940 Act and issuer tender offer rules under 1934 Act (Rule 13e-4).
- FINRA review standards vary (exemptive relief available).

Comparison – Interval Funds, Tender Offer Funds & Private Funds

General Terms

	Interval Fund	Tender Offer Fund	Private Fund
Investor Suitability Thresholds	No. Any investor (assuming 1933 Act registration)	Same as interval fund	Yes. Only “Accredited investors” and/or “qualified purchasers”
Limitation on Number of Investors	No	Same as interval fund	3(c)(1) funds: 100; 3(c)(7) funds: Unlimited (subject to a 2,000-investor cap to avoid 1934 Act reporting)
Performance Fees	Yes—to an extent. Permitted on income; also permitted on capital gains if offering limited to “qualified clients”	Same as interval fund	Yes
Multiple Share Classes	Yes, but only with SEC exemptive relief	Same as interval fund.	N/A. Side letters may provide preferential rights to certain investors.

Comparison – Interval Funds, Tender Offer Funds & Private Funds (cont'd)

Repurchase Offers

	Interval Fund	Tender Offer Fund	Private Fund
Liquidity Requirements	Maintain liquid assets sufficient to meet repurchase offers during period of time between each notice to repurchase and the repurchase pricing date	None	None
Frequency of Repurchases	Repurchases must occur on the interval period selected by the fund (e.g., 3, 6 or 12 months) absent shareholder approval	At the discretion of the fund's board (generally follow offering document disclosure, but not-binding)	N/A. Withdrawal typically only permitted if required for regulatory purposes.
Payment Delay	No. Payment deadline is 7 days after the repurchase pricing date	Yes (consistent with offering documents)	N/A. Distributions must be consistent with organizational documents.

Comparison – Interval Funds, Tender Offer Funds & Private Funds (cont'd)

SEC/FINRA Filings & Other Regulatory Matters

	Interval Fund	Tender Offer Fund	Private Fund
SEC Process for Updating Offering Documents	Annual filing to update financial statements pursuant to Rule 486(b). Filing will go effective automatically.	Annual filing for updating of financial statements, which is subject to SEC review and effectiveness. Can file for SEC no-action relief to rely on Rule 486(b).	N/A (other than Reg. D filings)
FINRA Review and Compensation Limits	Subject to Rule 2341	Subject to Rule 5110 (can seek relief) if 1933 Act registered offering	Generally N/A
Exempt from ERISA “Plan Asset” Regulation?	Yes	Same as interval fund	No
1099 Eligible?	Yes (assuming can satisfy Subchapter M rules)	Same as interval fund	No

C. Retail Investing: Build it or Buy it

Types of Consolidation Transactions

- Acquire BDC/CEF
- Acquire investment adviser to BDC/CEF
- Externalize investment advisory function
- Internalize investment advisory function
- Enter into investment advisory agreement with a new manager

Factors Contributing to Current Consolidation Environment

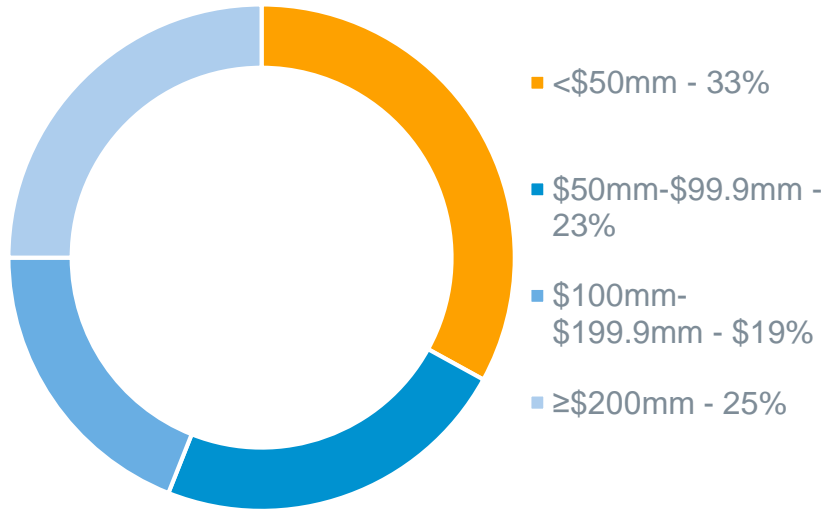
- BDCs/CEFs remain interesting vehicles to participate in credit assets.
- Organic growth of existing BDCs/CEFs can be difficult.
- Continued pressures to reduce cost structures
- Continued pressures on smaller managers
- Access to existing pools of capital (and new investors)
- Succession planning and robust multiples for financial services transactions
- Potentially lower cost option to enter market

IV. Deal Flow Trends; The Restructuring Cliff

A. Top Five Myths of Private Credit

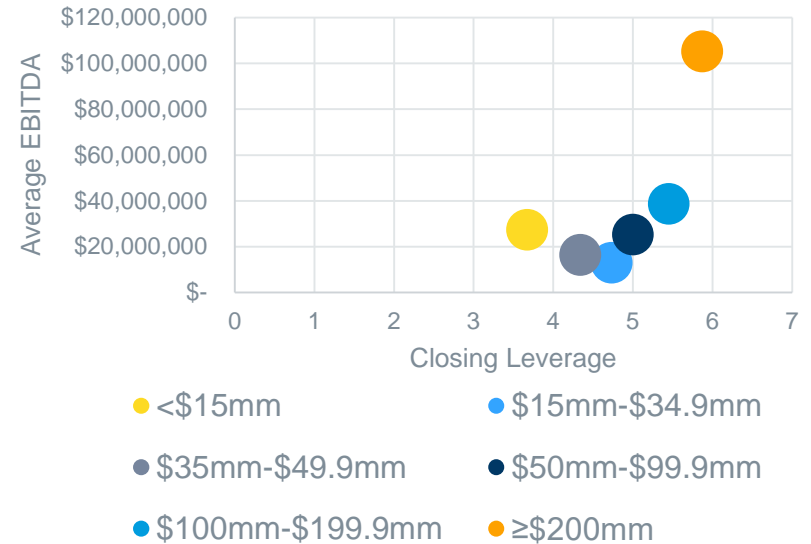
1. It's a Middle Market Solution.

Deal Size (2018)



Source: Proskauer, 2018 Private Credit Insights

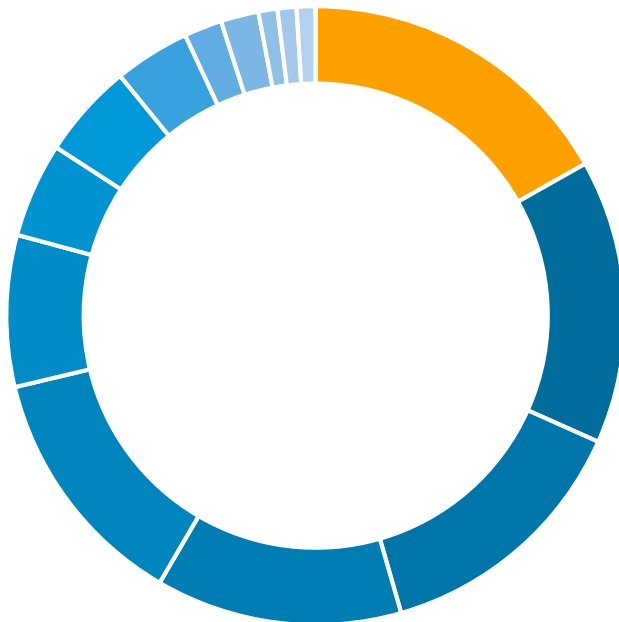
Average EBITDA & Closing Leverage by Deal Size (2018)



Source: Proskauer, 2018 Private Credit Insights

2. It's for Out-of-Favor Industries.

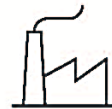
Type of Industry (2018)



- Manufacturing - 17%
- Health Care - 15%
- Business Services - 14%
- Consumer - 13%
- Software & Technology - 13%
- Food & Beverages - 8%
- Construction - 5%
- Other - 5%
- Education 4%
- Financial Services - 2%
- Real Estate - 2%
- Energy & Utilities - 1%
- Franchise, Sports & Rec' - 1%
- Media, Entertainment & Arts - 1%
- Automotive - 0%
- Transportation - 0%

Top Industry 2018:
Manufacturing

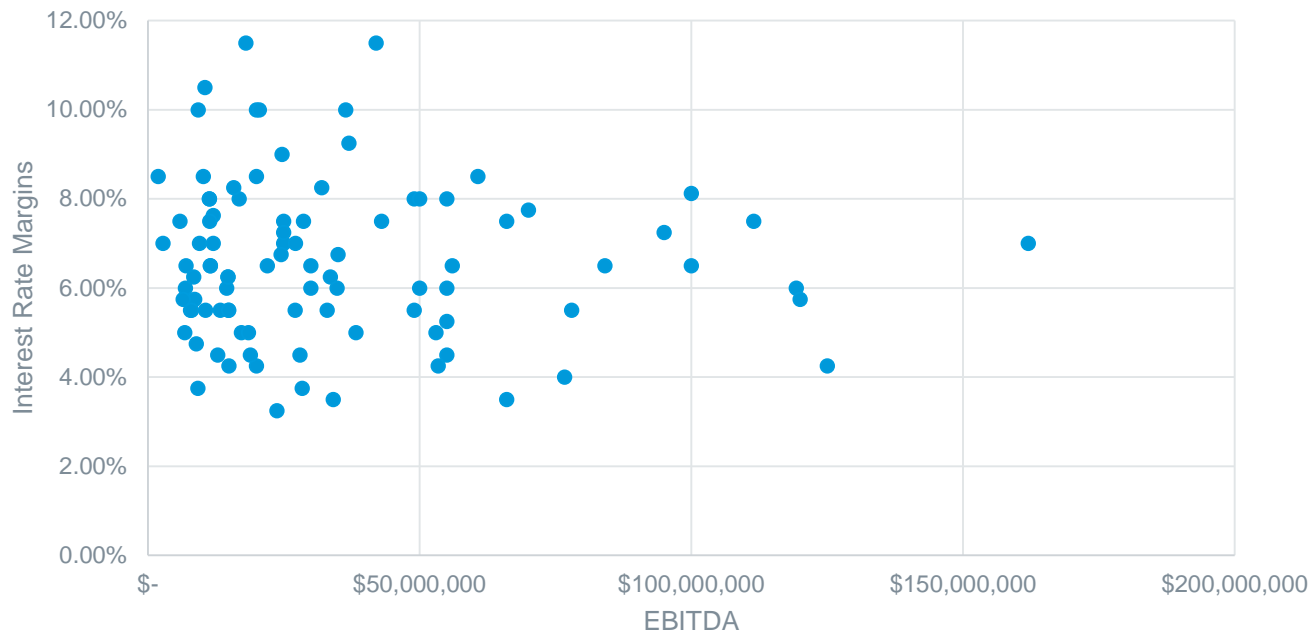
17%



Source: Proskauer, 2018 Private Credit Insights

3. Pricing Can't Compete with the Syndicated Market.

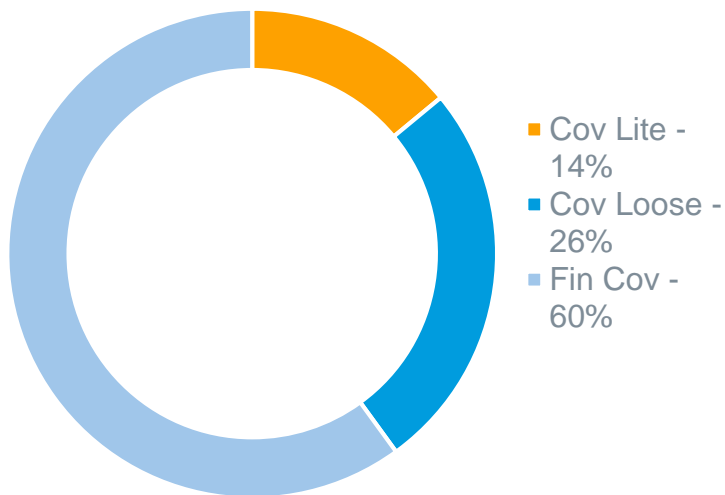
EBITDA vs. Interest Rate Margins (2018)



Source: Proskauer, 2018 Private Credit Insights

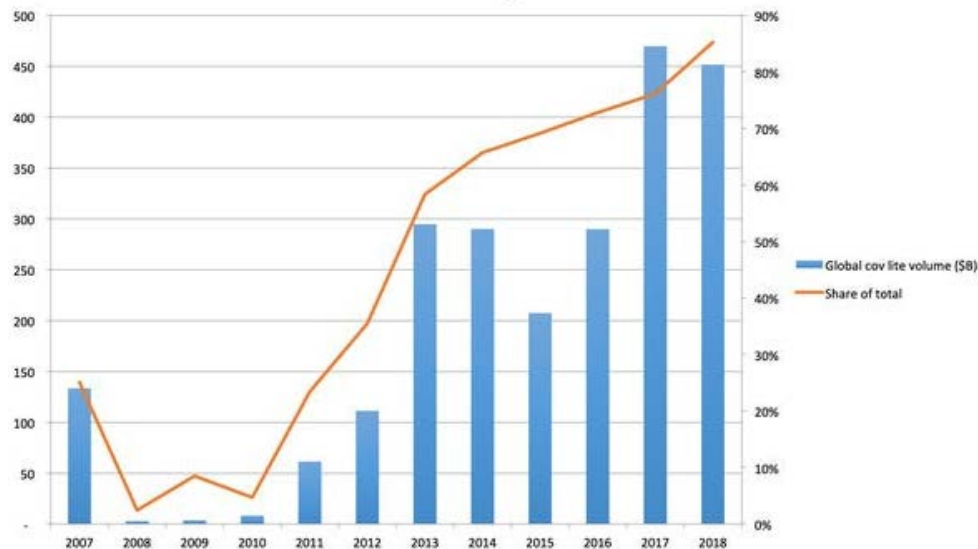
4. The Majority of Deals Are “Cov-lite.”

Financial Covenants (2018)



Source: Proskauer, 2018 Private Credit Insights

Global Middle Market Covenant-Lite Volume (\$bn)



Source: Business Insider

5. There Are Only a Handful of Large Players.



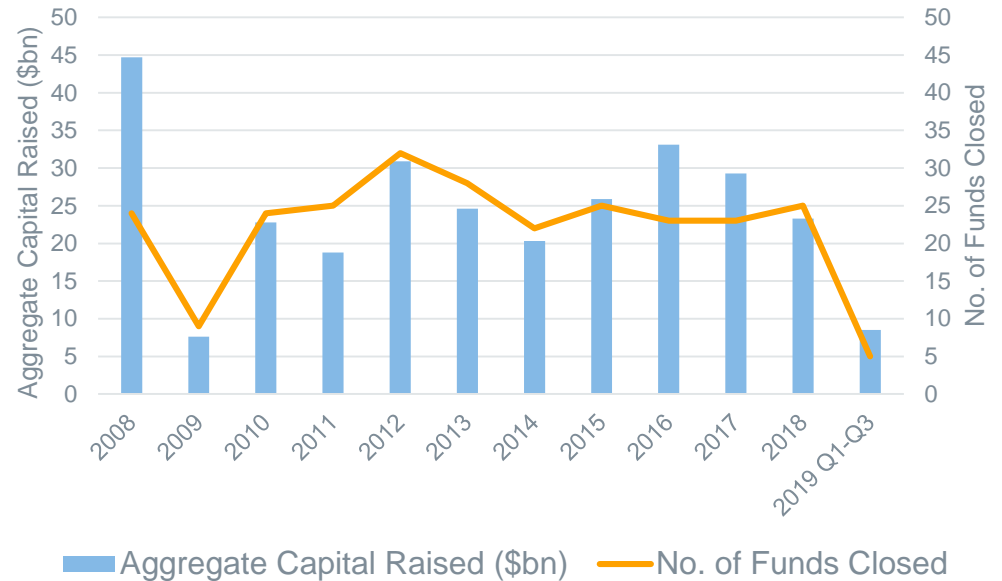
Source: Growth Cap Advisory
Source: Private Debt Investor

B. Forecasting for the Next Credit Cycle

Fundraising for Distressed Strategies

- Following a slow 18 months of little activity, distressed fundraising rose again in the first half of 2019.
- The average fund size in 2019 is \$1.3 billion, as compared to \$911 million in 2017.
- 53% of funds in market with distressed strategies as of Q3 2019 were focused on North America.

Global Distressed Debt Fundraising, 2016-2019 Q1-Q3



Source: Private Debt Investor, H1 Fundraising Report 2019, Q3 Fundraising Report, 2019

Continued Effects of Tax Reform

- Increased collateral available to lenders to U.S. multinational companies due to changes in U.S. international tax regime and Section 956.
 - However, some borrowers are still able to resist having CFCs guarantee their debt, and being required to pledge their CFC's stock.
- Section 163(j) currently limits business net interest expense deductions to 30% of EBITDA.
 - Generally little effect on leverage incurred by credit funds because all income is interest income.
 - We had expected to see a decrease in corporate borrowers issuing debt and an increase in preferred stock. However, we haven't seen this happen.
 - But, beginning in 2022, net business interest expense will be deductible only up to 30% of EBIT. Much greater limitation than EBITDA.
- Corporate tax rate reduced from 35% to 21%.
 - U.S. corporate leveraged blockers are starting to be used by funds with non-U.S. investors.
 - Will leveraged blockers continue to make sense if corporate tax rates increase in the future?

Borrower-Friendly Documentation

- “Cov-lite” and “cov-loose”
- EBITDA addbacks
- Less restrictive negative covenants
- Fewer defaults

Risks

- Collateral Leakage (e.g., J Crew, PetSmart, etc.)
- Layering/ up-tiers
- Non-pro rata exchanges
- Unequal treatment of lenders
- Unencumbered collateral
- Cross-over lending

Considerations For Fundraising

- Access to follow-on capital
- Diligence restructuring expertise
- Consider exposure to borrower-friendly documentation
- Understand conflict management of cross-over lenders

V. Closing Remarks

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Proskauer: One-Stop Shop for Private Credit

Investment Management Expertise

- Represent U.S. and European sponsors in structuring and formation of 30+ credit funds and separate accounts, representing over \$8.6 billion in equity commitments since 2015.
- Integrated Tax and Regulatory specialists assist in creating bespoke structuring solutions.
- Cutting edge insight into market trends, developments and terms and conditions.
- Active practice in establishing and advising BDCs.

Transactions

- Exclusively represent 75+ providers of private credit, including private debt funds, BDCs, insurance companies, asset managers, finance companies, family offices and other sources of private debt capital in the U.S. and European markets.
- ~ 250 deals closed per year.
- Active in the market for 20+ years, and have participated in the evolution of a number of credit products.

Proprietary Databases

- **Funds Data:** Tracks terms of 1,600+ funds (and growing daily) across all strategies and jurisdictions, providing us access to the most current market data and allowing us to anticipate and resolve issues raised by investors quickly and efficiently.
- **Deal Data:** Identifies market trends in middle-market lending and provides real-time intelligence on the state of the credit markets. Includes 200+ searchable deal terms across various product lines.
- **Intercreditor/AAL Data:** Tracks terms of hundreds of intercreditors and AAL.

Corporate Counsel

- Act as outside general counsel to investment managers with a particular emphasis on ongoing fund management matters.
- Advise on acquisitions of alternative investment managers as well as joint ventures and other strategic transactions.
- Leverage expertise to develop a deep understanding of clients' businesses.
- Counsel clients on operational, compliance and regulatory matters.

One Center of
Expertise

Proskauer's Global Presence



Appendix A: Overview of Structuring Solutions & Tax Considerations for U.S. Direct Lending Funds

Bring Your Own Treaty (“BYOT”) Structures

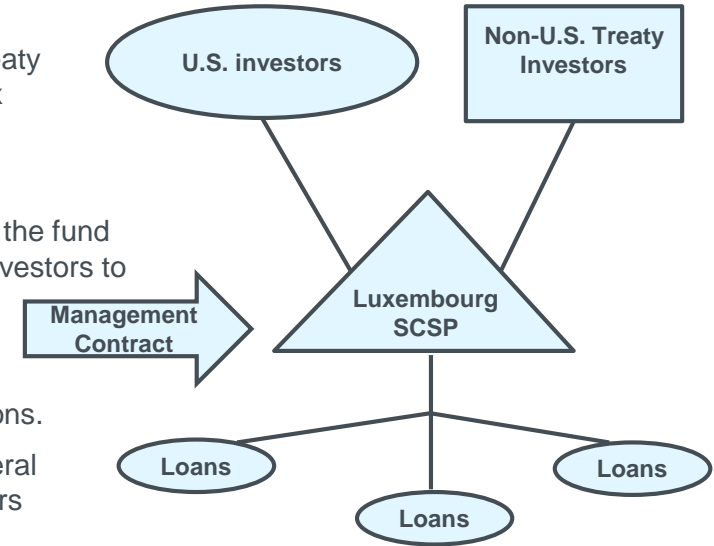
- **Independent agent:** Manager must qualify as an “independent agent”.

- **Ownership:**

- Non-U.S. investors must qualify for the benefits of an income tax treaty between the U.S. and the jurisdictions in which the investors are tax resident.
- Taxable U.S. investors may invest.
- Tax-exempt U.S. investors may invest, but will be subject to UBTI if the fund is leveraged. In that case, it may be possible for tax-exempt U.S. investors to invest through a parallel Luxembourg or Irish treaty vehicle.

- **Other Considerations:**

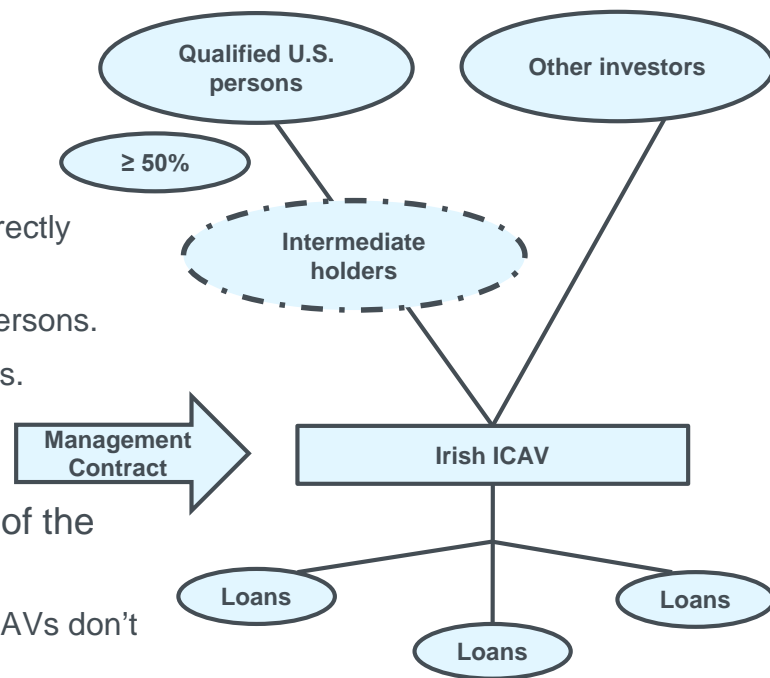
- Investors may be subject to state taxes and tax return filing obligations.
- A feeder fund that elects to be treated as a corporation for U.S. federal income tax purposes may be established to shield non-U.S. investors from direct state tax and tax filing obligations.
- The fund (including any feeder fund) and any SPV through which the fund holds assets must be transparent for purposes of the investors’ tax laws.



Treaty Structures: Ireland or Luxembourg

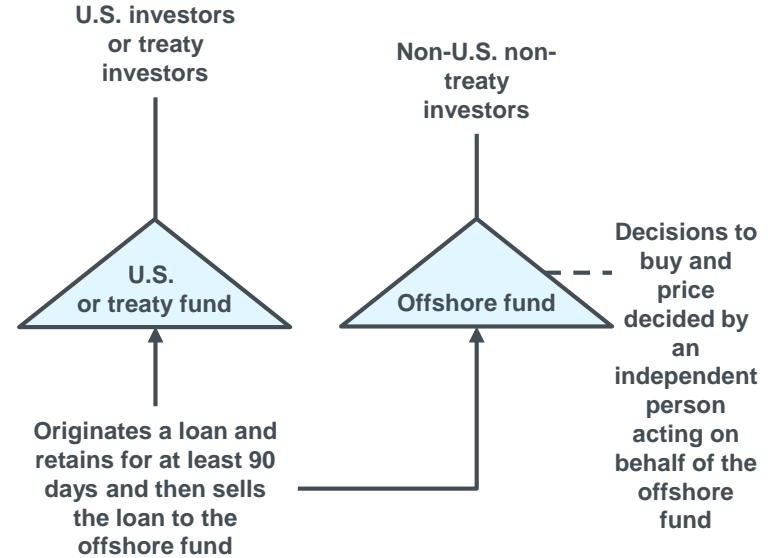
The Irish Collective Asset Management Vehicle (ICAV)

- **Independent agent:** Manager must qualify as an “independent agent”.
- **Ownership:**
 - $\geq 50\%$ of the ICAV’s vote and value must be directly or indirectly owned by “qualified U.S. persons”.*
 - Intermediate holders are not required to be qualified U.S. persons.
 - Useful for U.S. parent with subs located in other jurisdictions.
- **Base Erosion Test:** Amounts that are deductible for Irish tax purposes and are paid or accrued to investors other than qualified U.S. persons may not exceed 50% of the ICAV’s gross income.
 - The base erosion test doesn’t apply to an ICAV because ICAVs don’t deduct payments for Irish tax purposes.



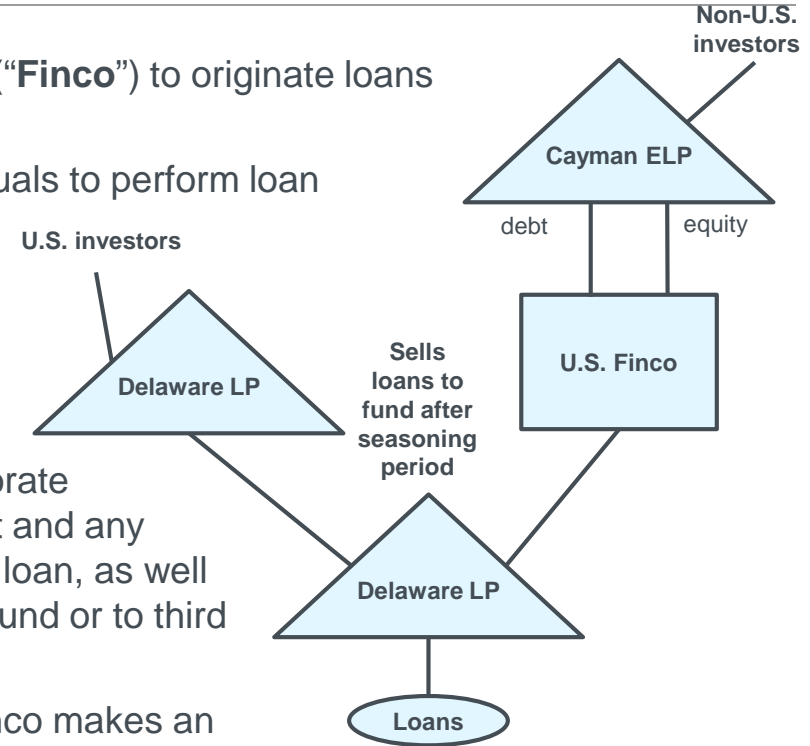
Season & Sell (Horizontal Seasoning)

- U.S. or treaty fund originates loans.
- After “seasoning” period (90 days), the U.S. or treaty fund offers to sell the loan to the offshore fund.
- The decision to purchase is made by a person who is entirely independent of the U.S./treaty fund and the manager, who represents the offshore fund, and has full discretion to purchase or not purchase and to negotiate price.
- Independent valuation of each loan.
- U.S. or treaty fund must be prepared to hold or sell to third party if the offshore fund does not purchase the loan.



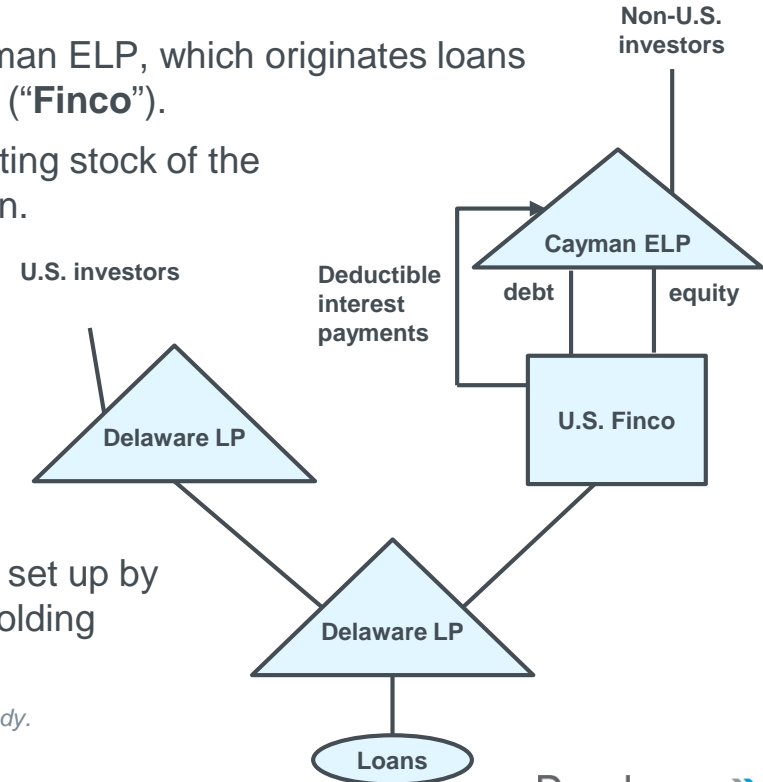
Season & Sell (Vertical Seasoning)

- Fund organizes a U.S. corporate finance subsidiary (“**Finco**”) to originate loans to third parties.
- Finco must employ an appropriate number of individuals to perform loan origination and servicing activities, and those employees will have use of an office and equipment.
- Finco must be adequately capitalized in accordance with the reasonable needs of a lending business (including possibly debt capitalization).
- Finco is subject to U.S. federal, state and local corporate income tax on its net income, which includes interest and any origination or other fees earned with respect to each loan, as well as gain recognized upon the sale of any loan to the fund or to third parties.
- After a “seasoning” period (180 days? 90 days?), Finco makes an offer to sell each loan to the fund.



Leveraged U.S. Blocker

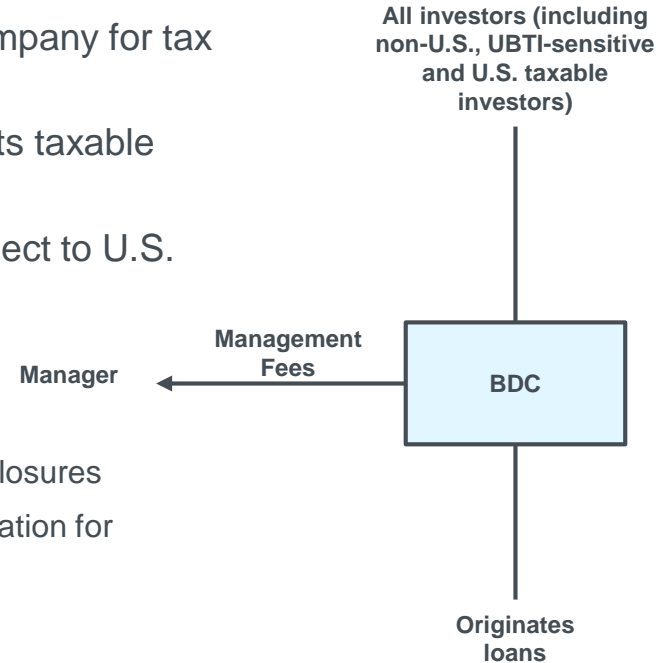
- Permits ECI-sensitive investors to invest through Cayman ELP, which originates loans through a leveraged U.S. corporate finance subsidiary (“**Finco**”).
- No non-U.S. investor can own $\geq 10\%$ or more of the voting stock of the Finco indirectly through the partnership or by attribution.
- Finco pays U.S. federal income tax and applicable state tax. Deductible interest payments reduce amounts of income subject to taxation.
 - At 70% leverage, with a return of 10% and interest expense at 8%, the effective federal tax rate would be 9.24% $((100 - 56) \times 21\%)$, assuming all net income reinvested in the U.S. business until final liquidation.*
- Repeal of Section 958(b)(4) has caused U.S. blockers set up by sovereign wealth funds to be subject to 30% US withholding tax on portfolio interest.



**Actual leverage levels and interest rate on the debt would be subject to a transfer pricing study.*

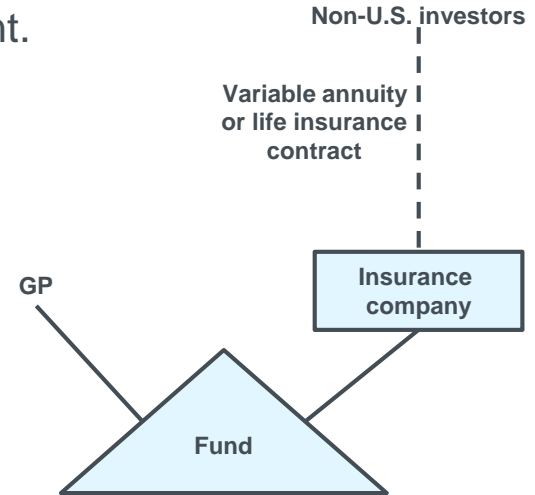
BDC or CEF

- BDC/CEF elects to be taxable as a regulated investment company for tax purposes.
- BDC/CEF annually distributes $\geq 90\%$ (and preferably all) of its taxable income to avoid a corporate-level tax.
- Distributions of “qualified” interest income should not be subject to U.S. withholding tax.
- BDC/CEF needs a separate board.
- Leverage ratio limitations:
 - BDC: 2:1 leverage ratio limitation with certain approvals and disclosures
 - CEF: 1:2 leverage ratio limitation for debt; 1:1 leverage ratio limitation for preferred stock



Insurance Dedicated Fund (IDF)

- Investor control doctrine prevents investor involvement.
- Diversification.
- Subject to taxes and expenses including:
 - 1% federal DAC tax.
 - State premium tax.
 - Broker expense.
 - Underwriting expense (insurance only).
 - Annual cost of insurance/mortality & expense.
- Total cost:
 - 40bps – 125bps (annuity)
 - 75bps – 150bps (insurance)



Overview of Structuring Solutions for U.S. Direct Lending Funds

Structure	Primary Positive Attributes	Primary Limitations
BYOT	<ul style="list-style-type: none"> Increasingly common structure for senior debt funds Permits 100% participation by all investors in all economics of underlying loans Can be combined with season & sell structures 	<ul style="list-style-type: none"> Need >50% U.S. investor ownership Marketing focused on “good” treaty investors Movement to increase substance requirements Concerns about Lux or Irish tax Manager must qualify as an independent agent
Treaties (Lux/Irish)	<ul style="list-style-type: none"> Increasingly common structure for senior debt funds Permits 100% participation by all investors in all economics of underlying loans Simpler than BYOT structure Can be combined with treaty and season & sell structures 	<ul style="list-style-type: none"> Marketing focused on treaty-eligible investors Manager must qualify as an independent agent
Season & Sell: Horizontal	<ul style="list-style-type: none"> The most widely accepted structure in the market Tend to be less complex 	<ul style="list-style-type: none"> “Capacity issues” Returns for offshore fund are lower than the onshore fund due to up-front fees Fiduciary issues for affiliated trades between onshore and offshore funds
Season & Sell: Vertical	<ul style="list-style-type: none"> Eliminates fiduciary issues for affiliated trades 	<ul style="list-style-type: none"> Not widely used Operationally intensive Reduced returns during seasoning period for offshore fund Less tax comfort
Leveraged Blocker	<ul style="list-style-type: none"> No marketing restrictions or balancing of investors Simplest structure Sponsors are considering increased use 	<ul style="list-style-type: none"> Reduced returns due to tax leakage
BDC/CEF	<ul style="list-style-type: none"> Single vehicle solution for all types of investors 	<ul style="list-style-type: none"> Regulatory tax Need for separate board Restriction on future season and sell
IDF	<ul style="list-style-type: none"> Favored by high net worth investors/private banks Solution for all types of investors 	<ul style="list-style-type: none"> Not widely utilized Increased costs: Annuity + Insurance Investor control doctrine prevents investor involvement

Overview of Tax Considerations for U.S. Direct Lending Funds

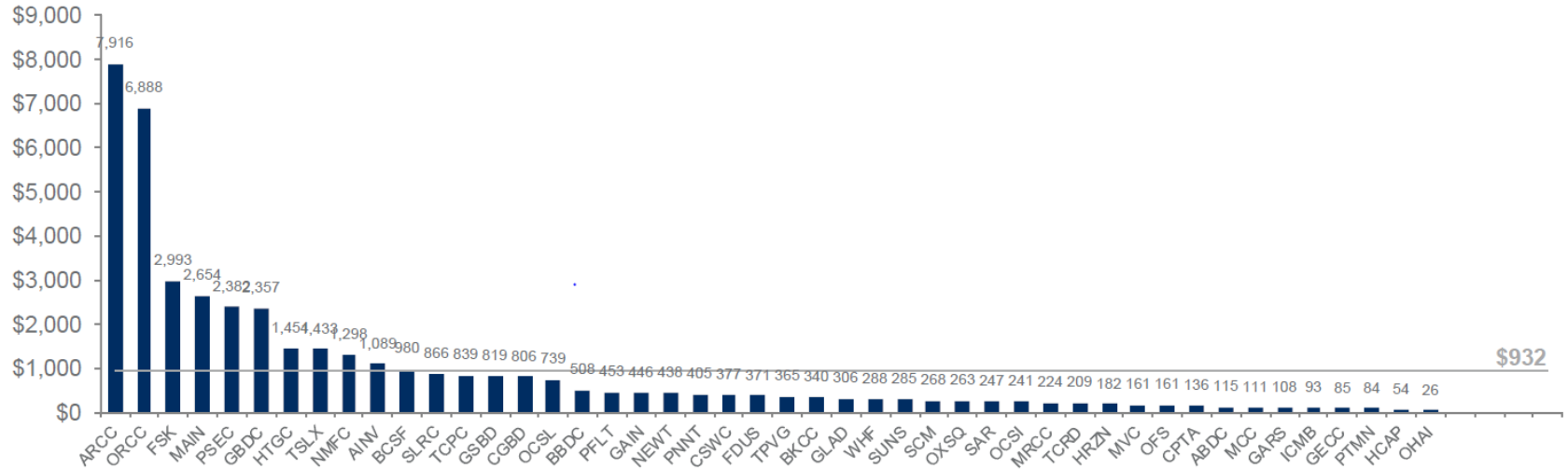
Structure	UBTI for Tax-Exempts from Use of Leverage	ECI for Non-U.S. from Loan Origination
Treaty Position – BYOT & Treaties (Lux/Irish)	No UBTI	No ECI
Season and Sell – Horizontal & Vertical	No UBTI, but lose some yield	No ECI, but lose some yield
Leveraged Blocker	No UBTI	No ECI
BDC/CEF	No UBTI, but leverage is limited	No ECI
IDF	No UBTI	No ECI

Appendix B:

Public BDC Market Data

Public BDC Market — General Data

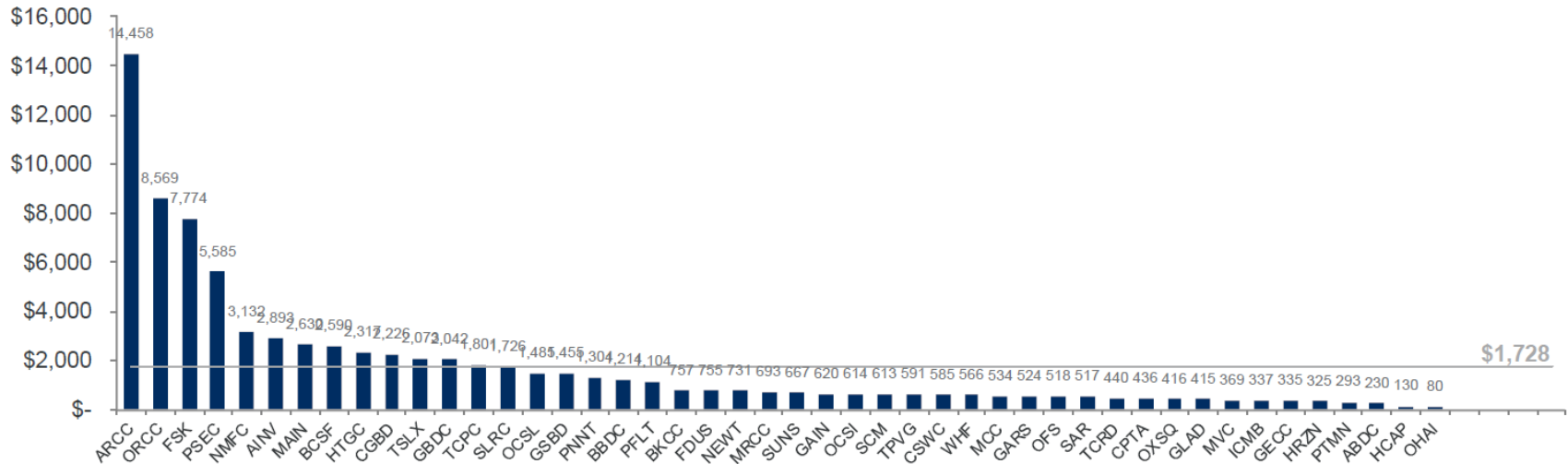
Market Capitalization (\$MM) as of November 8, 2019



Source: Raymond James

Public BDC Market — General Data (cont'd)

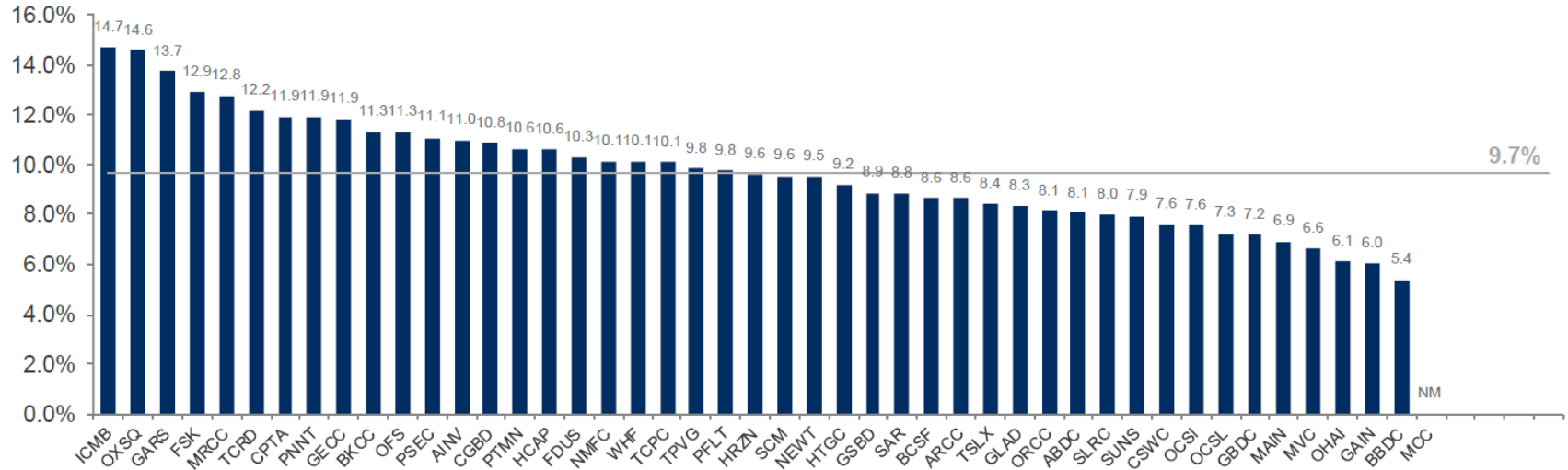
Assets (\$MM) as of November 8, 2019



Source: Raymond James

Public BDC Market — General Data (cont'd)

Current Dividend Yield as of November 8, 2019



Source: Raymond James

Dividend rate uses current dividend annualized.

MAIN includes supplemental dividend.



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