

## ALTERNATIVE INVESTMENTS

# BRIDGE LOANS: ANSWERING YOUR MOST COMMON QUESTIONS

Subscription Lines, also known as Bridge Loans or Capital Call Lines, are short-term loans that can be used while emerging funds are waiting for their Limited Partners or investors to fund their capital commitment. This provides immediate cash flow to the fund managers and can be used for various purposes. Emerging managers may want to consider a Subscription Line while they raise capital for their fund as the line can assist in smoother efficiencies. Richey May has created a guide to address frequently asked questions around why and how emerging managers may want to attain a Bridge Loan and what they will need to consider if they choose to secure one.

### Who Can Secure a Subscription Line?

Funds that operate with a closed end structure are the best fit for a subscription line. This is ideal for funds who have at least \$30M in AUM. The legal expenses to secure the loan add up and don't have as great of a return for smaller funds, so larger loans and funds are a better fit.

### When would a fund use a Subscription Line?

This is ideal for when a fund comes across an opportunity and they need to move quickly, but calling on the committed capital from their investors will take some time to process and get funded for the investment. The fund can use the Subscription Line to immediately move on an opportunity and pay it back after the funding comes in.

Initially it takes around 60 days from the first meeting to be approved for the loan, more or less depending on the fund complexity and fund responsiveness. Thereafter the initial approval, a request for a subscription line can be turned around very quickly, sometimes even in the matter of a few days. Being approved for a subscription line can allow you to take advantage of more opportunities, quickly.

### What do banks look for in the approval process?

They like to see the fund manager's background to get a better idea of their experience and track record. It helps to know how long the fund manager has been doing this. They will want to get an idea of the investor base and investor roster and how much concentration of committed capital each LP already has.

As a fund manager, it is important to display your past success of managing funds and display your investor base. Be prepared for the bank to ask for a balance sheet and audited financials of the fund.

*All loans are subject to bank underwriting, due diligence and credit approval*

### What are the typical terms of a Subscription Line?

The typical term varies due to several factors, however, generally a term can be put in place to match the investment period of the Fund with the possibility for extension options.

The line can be outstanding for 6 months (on average) but in some cases up to a year. Some funds like to secure the line opportunistically to increase purchasing power and in some instances leverage.

### What are the tax implications?

In general, the tax implications for emerging funds partaking in Subscription Lines are favorable to their Limited Partners, with certain caveats. The interest expense on Subscription Lines will ultimately flow through the entity to the Limited Partners, who can in most cases use their pro-rata share of the expense as a deduction on their own tax return. The caveat, depending on the type of entity, is that the amount of this expense may be limited under the excess business interest expense limitation tax regime enacted as a result of the Tax Cuts and Jobs Act of 2017.

There is also consideration at the entity level using Subscription Lines. The use of Subscription Lines could be considered the use of leverage, which may trigger Unrelated Business Taxable Income. This type of income is not preferred for U.S. Tax Exempt Investors, as it could trigger tax liability on the income earned from the entity. It may be construed that the use of a Subscription Line is unrelated of the basis of an exempt organization's normal course of business.

In any case, it is important to speak with your tax advisor on the issues and benefits surrounding Subscription Lines before entering into an agreement.

### Other recommendations for securing a Subscription Line:

- Communicate with your Legal Counsel and mention you may consider borrowing at the Fund Level.
- Mention to your Limited Partners and Investors that the fund may pursue a Subscription Line which would smooth out capital calls.

If you have questions or need an introduction to obtain a bridge loan, please contact [Steve Vlasak](#).



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