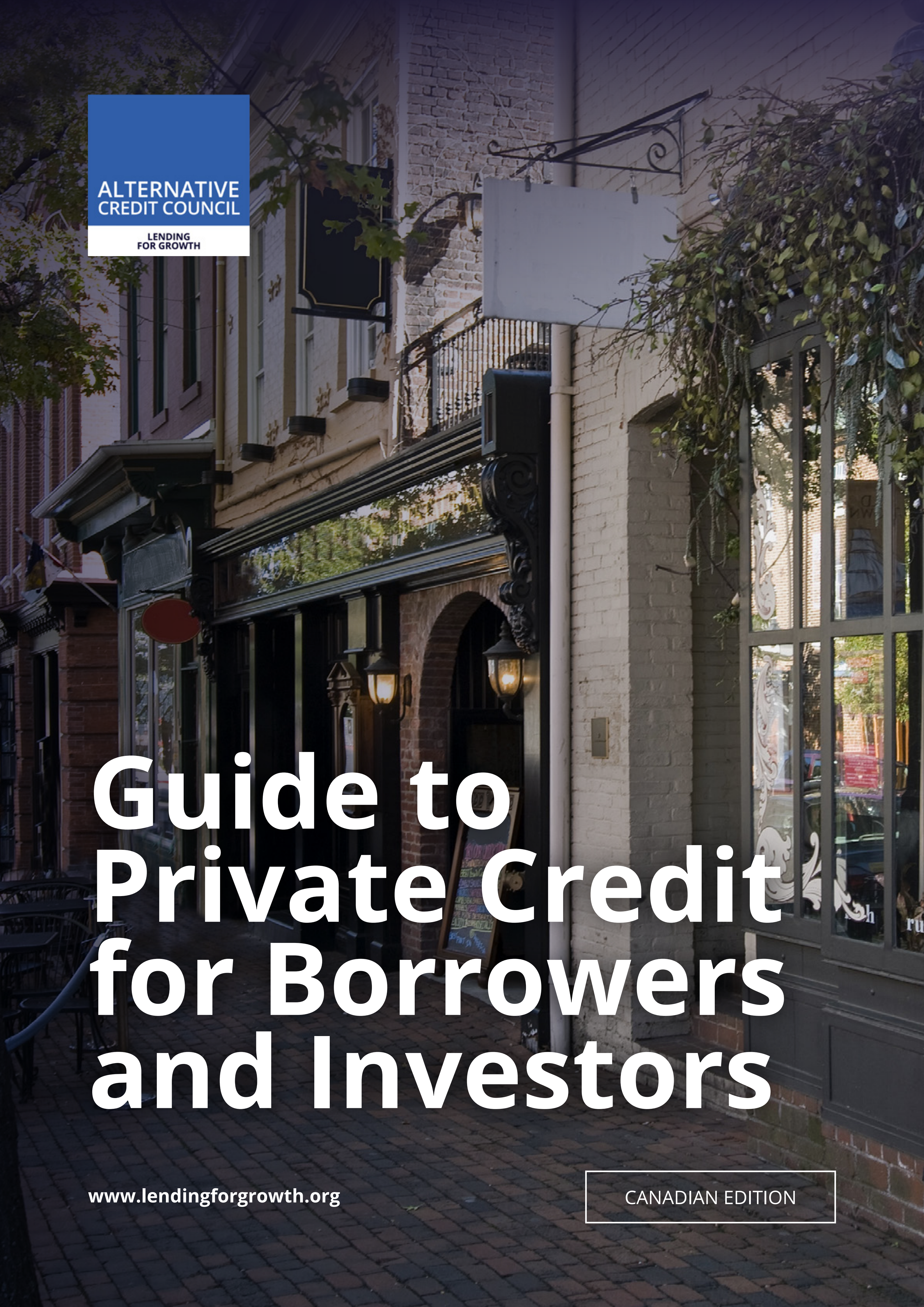


ALTERNATIVE CREDIT COUNCIL
LENDING FOR GROWTH

Guide to Private Credit for Borrowers and Investors

www.lendingforgrowth.org

CANADIAN EDITION

Foreword

Jiří Król
Global Head of the Alternative Credit Council

The success of Small and Medium Enterprises (SMEs and mid-sized businesses) is vital to the functioning of the local and global economies. It remains crucial for these businesses to have access to the finance they need to invest, grow and provide jobs across the country. Private credit managers offer an increasingly important source of funding for Canadian businesses, with several dozen local lenders providing billions in financing to our economy. Furthermore, private credit forms a key part of Canadian institutional investor portfolio allocations, with CPP Investments, for example, investing over $35B in the asset class globally.[i]

Looking ahead, access to finance is likely to be a critical factor for SMEs and mid-sized businesses as they adapt and modernise in response to COVID-19 as well as newer trends in customer demand and behaviour. With traditional bank lending more difficult to secure, private credit works to fill this financing gap. It is therefore essential to cultivate more sources of capital to support businesses across Canada.

As well as increasing the availability of capital, it is necessary to diversify the type of capital which is available. This will support SMEs and mid-sized businesses whose financing needs fall outside the risk appetite of existing capital providers, despite being viable businesses. It will also provide businesses with greater choice and support competitive finance markets.

Private credit managers pride themselves on offering loans that work with the specific needs and circumstances of the borrower. This allows these businesses to invest in their future, create jobs and compete in a global marketplace. Lenders often specialise in certain business sectors and are therefore able to offer tailored solutions based on a bilateral relationship created with borrowers. In addition, private credit lenders are well placed to support underperforming businesses in the sustainable return to viability and growth. Rehabilitation, rescue and recovery of an organisation facing decline protects economic value and preserves jobs. This is especially important as businesses continue to adjust to the changing economic circumstances as a result of the global pandemic.

Despite the growth of the private credit industry in Canada during the past decade, many business owners remain unfamiliar with this group of lenders and the lending solutions they can offer.

This introductory guide offers an overview of who private credit lenders are, how they lend and work in partnership with businesses to help them succeed. It outlines whether private credit might be the right fit for a business, how these lenders conduct due diligence, what to expect in a loan agreement and what to expect once a loan has been extended. In addition, it includes a glossary of key terms as well as case studies that provide real life examples.

The value of this type of long-term finance is well-recognised by both businesses and policymakers. The Alternative Credit Council (ACC) is pleased to support expanded capacity and sustainable growth in the real economy while educating investors, borrowers, policymakers and others on benefits and trends impacting the private credit sector. It is our hope that this guide will complement that work by raising awareness among Canadian businesses and demonstrating that private credit is an established and viable financing option for them to invest in their business.

The Alternative Credit Council Canada Committee hopes this guide will assist both borrowers in considering private credit as a viable option to support the growth of their businesses, as well as investors seeking to learn more about the asset class.

Contents

Executive summary

What is private credit?

'Private credit' is the umbrella term used to describe loans to businesses originated by lenders other than banks. It typically involves lending to companies on a bilaterally negotiated basis, with financing sizes ranging between $1 million and $250 million. Private credit lenders engage with borrowers via direct relationships which helps support their understanding of the borrower's business. This allows lenders to offer flexible and tailored finance solutions to match the unique needs of each borrower.

What businesses do they lend to?

Private credit firms generally lend to Small and Medium Enterprises (SMEs) and mid-market businesses across all sectors of the economy. Businesses use this type of finance for a variety of purposes such as acquisition and expansion plans, improving working capital and refinancing existing debt.

What types of private credit loans are available?

Private credit managers will work with businesses to find the right type of finance for their needs. This means they may lend across a range of maturities and repayment profiles, take into account different types of security, collateral or levels of seniority compared to existing debts. In addition, lenders often specialise in providing finance that is aligned with the needs and circumstances of specific sectors.

How do private credit lenders make investment decisions?

Private credit firms will engage in considerable due diligence and typically invest in only a small percentage of the businesses they assess. This ensures that both the lender and borrower are the right fit for each other. Factors a firm would typically analyse may include a business's sector and key markets, financials, corporate governance, collateral, management culture and, increasingly Environmental, Social and Governance (ESG) factors.

Why is ESG important to private credit lenders?

Private credit managers need to provide their investors with ESG information about the businesses they are lending to. This means that they will ask businesses questions about things such as their energy use, adherence to labour standards and corporate governance. This supports their understanding of how a business is being managed alongside more traditional financial metrics.

Are private credit managers secure counterparties?

Private credit firms are regulated as asset managers and the funds they manage are subject to ongoing regulatory supervision and oversight. Businesses benefit from the same safeguards and borrower protection rules when working with private credit lenders as they would do with any other finance provider.

What does a loan agreement look like?

A loan agreement should stipulate the purpose of the finance sought, the term of the loan, and the conditions of repayment such as interest rates. Loan agreements will also include undertakings or covenants, outlining the terms borrowers agree to comply with and upon which the provision of the loan is conditioned. An example term sheet can be found on **page 33** of this guide.

What happens if a business experiences distress?

The direct relationship between a borrower and private credit manager means that any periods of stress or challenging circumstances are likely to be identified early. This provides more time for both parties to proactively engage and address any issues. The individuals working with a business to mitigate the stress will often be the same people who were involved in the initial lending process. This means they will have a detailed understanding of the business and its market to better inform how to get back on track.

Private credit managers offer an increasingly important means of funding small to mid-sized businesses, with over $100bn of new loans extended globally in 2020.

Alternative Credit Council. 2020.
[Financing the Economy 2020.]

Private credit and its role in financing businesses

Defining private credit

Private credit is an increasingly important source of finance for borrowers, enabling them to invest in their businesses and support job creation and innovation. Much of the overarching terminology used to describe private credit is applied interchangeably with phrases such as 'direct lending', 'alternative lending', 'non-bank lending' and 'private credit' all part of the common parlance. 'Private credit' is the umbrella term used to describe all forms of credit provided by non-bank lenders.

Private credit typically involves lending to companies or projects on a directly negotiated basis, with typical financing sizes ranging between $1 million and $250 million. It is not publicly traded, as is the case with many corporate bonds, and is originated or held by lenders other than banks. Private credit takes various legal forms including loans, bonds, notes or private securitisation issues.

The direct and tailored nature of private lending is often the core element that distinguishes private credit from other forms of financing.

Many firms view themselves as a partner to the businesses they have lent to, and have business models which rely on the ongoing success of their borrowers.

Borrowers use private credit loans for a variety of purposes such as pursuing acquisition and expansion plans, improving working capital and refinancing. Among the most popular borrowers of private credit are SMEs and mid-market companies, however, many private credit firms cater to larger businesses.

Key advantages of private credit

Obtaining financing through private credit lenders offers three key advantage to borrowers:

01 / Direct Relationship

Private credit firms distinguish themselves through the collaborative relationship maintained with companies in their portfolio. Businesses tend to engage with the same individuals throughout the due diligence process and lifecycle of the loan. The relationship that is created is one built on trust and a deep understanding of the borrower's business on the part of the lender. It is this long-term relationship which is at the epicentre of why many businesses prefer to obtain financing through private credit lenders. Having provided the borrower with a loan tailored to his or her business, private credit lenders are better equipped to handle any periods of uncertainty which may arise throughout the lifecycle of the loan. Due to the close relationship established between borrowers and private credit lenders, renegotiating terms and making adjustments is based on stronger foundations and deeper knowledge.

02 / Tailor-made solutions

In recent years, private credit has increasingly provided an alternative means of finance to markets which are being underserved by traditional sources of finance, such as SME lending, speciality finance, real estate, trade finance and infrastructure debt. This development of such niche finance solutions more readily matches the needs of the borrower and the interests of the lender. Moreover, borrowers appreciate private credit lenders' ability to navigate the more complex financing situations required by some businesses to meet their lending needs.

03 / Speed

Despite the in-depth due diligence processes employed by private credit lenders, loan decisions are made quickly and efficiently. This enables borrowers to take advantage of time-sensitive market opportunities.

How do private credit managers lend?

Private credit managers pride themselves on offering loans that work with the specific needs and circumstances of the borrower. This means they can provide loans to borrowers using several different methods – for example, using different types of security or collateral, and at different levels of seniority compared to existing debts.

Figure 1 provides an overview of the typical structure of loans and equity that a business may offer to investors. The capital stack is a ranked representation of the order in which debt and equity holders are given access to a company's assets in the case of default. Typically, senior debt holders rank highest whereas common equity holders rank lowest.

Private credit managers pride themselves on offering loans that work with the specific needs and circumstances of the borrower

Case study

Next Edge Capital supports metal fabrication company in turnaround

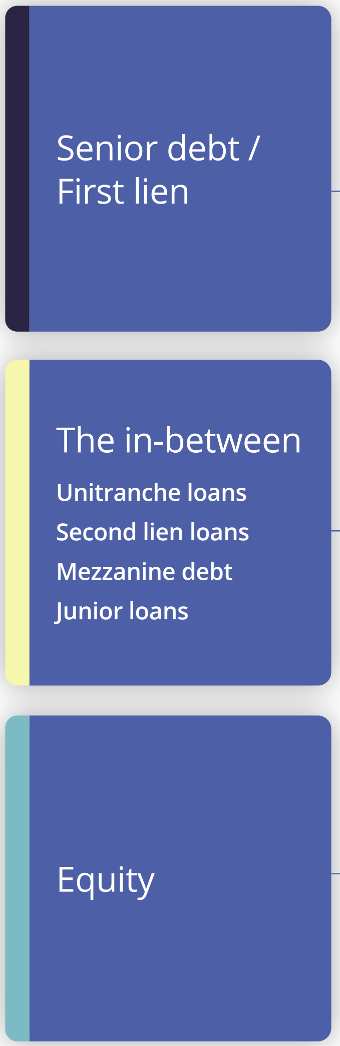
In Q1 2021 a transaction was closed for a metal fabricator in the US (the "Company"). Our financing supported a buy-out of the Company by the incumbent management team who are focussed on enhancing profitability and turning the Company around following a period of losses.

The Company experienced difficulties transitioning its clients to a different product line which caused a string of consistent losses from 2017 to 2020. The management team created a turnaround plan to move into a more lucrative and higher margin product lineup that has created an achievable breakeven point and a sightline to Company profitability. A significant consideration in the turnaround of this business included a key domestic competitor closing its doors during the pandemic which will significantly increase the Company's domestic business. In addition, lower-cost international competitors do not offer the same product lines as the Company.

Strengths of the Company and why we were able to finance the deal:

- Experienced management team in turnarounds and manufacturing.
- Solid financial reporting.
- Good inventory and strong accounts receivables to lend against.
- The closest competitors are internationally based, giving our borrower a competitive advantage in offering US customers smaller quantities and quicker delivery.
- Strong revenue projections in the first half of 2021.
- Accounts Receivables, Inventory, and Accounts Payable are all trending in a positive direction.
- No payroll or tax issues

Figure 1: Capital stack



Senior debt / First lien

First lien loans rank highest in the capital stack. This means that such loans are prioritised against most assets, often including the capital stock of the business. Inversely, the borrower is typically charged a lower amount of interest to reflect the relative security of the loan.

The in-between

There are several other positions within the capital stack ranking in priority below senior debt but above common equity, or potentially combining debt and equity positions, that private credit lenders may be willing to take. The interest rate paid is typically proportional to the level of risk associated with the loan / equity structure and the relative seniority in terms of access to capital. Borrowers may appreciate the simplification of such a structure as a 'one stop' source of financing with limited syndication risk. Examples of common terms a borrower may come across in this context are:

- **Unitranche loans:** Unitranche loans combine a senior tranche of debt and a junior tranche of debt in a single loan and provide a blended return to the lender.
- **Second lien loans:** Second lien loans usually form part of a wider senior debt package and will be lent at the same level in the structure as senior debt.
- **Mezzanine debt:** Mezzanine is a form of junior debt issued under separate documentation to the senior debt that ranks in priority behind the senior debt, but ahead of equity and is typically provided in conjunction with senior debt.
- **Junior loans:** Junior, or subordinated, loans have lower repayment priority than senior and mezzanine loans in the case of default and are closer to equity in the capital structure. As such, they run a higher risk of not getting repaid if a borrower defaults and hence pay higher coupons.

Equity

Equity represents the shares of ownership of the business. Shareholders will only be repaid after all debt commitments have been fulfilled. Therefore, equity ranks lowest in the capital stack. Direct lenders will generally not be involved in equity financing, but an equity component often finds its way as an addition to a debt portion of financing, usually in the form of equity warrants granted to the lender.

What types of private credit loans are available?

It is important to note that the universe of private credit loans is a broad one, with a selection of common strategies defined below. Within each strategy, a private credit manager may choose various loan seniorities according to the capital stack (see Figure 1).

Asset-based finance

Asset-based lending describes companies or other entities borrowing money secured against the value of assets they own. Common assets that are provided as collateral for an asset-based loan include physical assets like real estate, land, inventory, equipment and machinery, or intangible assets such as intellectual property. Asset-based lending is suited to organisations that require working capital to operate and grow, particularly in industries that might not provide significant cash flow potential.

Cash flow finance

Cash flow financing is a type of lending in which a loan made to a business is secured by a company's expected cash flows. The equity of the company to which the private lender provides the financing can therefore be considered as the collateral of the loan. The key financial metric used in assessing the creditworthiness and the amount of the loan to the business is the quality and size of its EBITDA. This is explored further in the following chapters.

Infrastructure debt

Infrastructure debt involves the financing of long-term infrastructure and industrial projects whereby repayments of the debt are funded by the cash flow generated from the completed project.

Real estate finance

Real estate finance involves the provision of credit secured against an underlying real estate asset. This type of financing may entail the funding of the initial purchase and construction phase of a commercial property, or the funding of a more general investment and enhancement strategy in existing commercial property.

Rescue finance

Rescue finance can be defined as the loans provided to companies that have filed for bankruptcy or have a significant chance of filing for bankruptcy in the near future. Rescue finance can be an opportunity to invest in a business which has the potential to use such additional funds to turnaround the company and enable renewed success.

Trade finance

Trade finance enables borrowers to purchase specific goods in both domestic and international markets. This is often transactional, with finance only being provided for specific shipments of goods and for specific periods of time. The debt is secured against the goods being financed. Until the borrower repays the debt, the goods typically belong to, or are secured in favour of, the lender.

Venture debt

Venture debt or venture lending refers to loans provided to early stage companies which enables such businesses to proactively fuel growth. As early stage companies typically do not have significant assets or cash flows, access to traditional bank loans is often restricted. Thus, venture debt can be a powerful financing tool.

Private credit and other financing sources

	Private credit	Private equity	Traditional banking	Public debt	Broadly syndicated loans
Typical relationship with borrower	Bilateral, direct	Bilateral, direct	Intermediated, often syndicated	Individual bond holders	Syndicated, banks and investment banks are key intermediaries
Typical borrower	SMEs or mid-market companies	SMEs, mid-market companies and large businesses	Larger businesses	Large, often multinational, businesses	Non-investment grade businesses on the higher end of mid-market and larger corporates
Backing	Usually secured by assets	Access to equity	Usually secured by assets	Secured and unsecured	Usually secured against lender equity
Use of ratings	Not rated	Not rated	Rated	Rated	Usually rated
Typical agreement	Bespoke and heavily negotiated	Bespoke and heavily negotiated	Standardised	Standardised	Standardised
Typical size of financing	1-250MM	Variable	Variable	500MM-5bn	250MM-1bn
Typical coupon	Floating (LIBOR+) [1]	n/a	Floating (Libor+)	Fixed	Floating (Libor+)
Typical maturity	3-7 years	n/a	Variable	Variable	3-7 years
Liquidity profile	Non-tradable	n/a	Tradable	Tradable	Tradable

1 LIBOR, which stands for London Interbank Offered Rate, serves as a globally accepted key benchmark interest rate that indicates borrowing costs between banks. Most interest rates in loan contracts are set on the basis of Libor. Libor is currently being phased out by macroprudential regulators and replaced by SONIA and SOFR (see Appendix).

Private credit and other financing sources

Banking

Private credit firms have close ties with traditional banks, and many have formed partnerships. Many companies financed by private credit have obtained bank financing either prior to or during their involvement with the private credit manager. When companies have been unable to secure bank finance, it is important to understand that this may not necessarily be due to them having a poor credit history, but rather due to a bank's risk appetite or existing exposure. An increasingly popular trend in recent years is banks and non-banks working alongside each other to provide the borrower with the best available finance option across their different business needs. Furthermore, companies are seeking to diversify their sources of funding and want to access the tailored solutions that private credit managers can provide. Private credit should be viewed as a complementary element of the financial services sector, rather than competing with traditional banking.

Corporate bonds

Bonds are public or private loans made to large organisations. These include corporations, cities, and national governments. Traditionally, corporate bonds and retail bonds are publicly traded on the stock market. They have a predetermined maturity date when the bond is redeemed, and investors are repaid their original investment. For a borrower, issuing public corporate bonds carries additional disclosure requirements. Credit rating agencies assess the quality of the company issuing bonds through a grading system according to the entity's ability to repay these loans. Due to this ratings requirement, issuing corporate bonds requires a high level of public transparency. Opting for a private loan carries the key advantage of limited disclosure, as a borrower's financial data is accessible only to the firm that is providing the loan and no public credit rating through an agency is required. Bonds are typically only available to larger companies and are not considered to be suitable for SMEs.

Private equity

Private equity describes finance provided in return for an equity stake in the company receiving the investment. Often, private equity firms aim to purchase significant shares in a business in order to exercise influence on its management. Due to this ownership dynamic, the private equity firm has a vested interest in the business's success and aim to improve its growth potential by leveraging internal expertise.

Sponsored lending is a type of private credit loan closely associated with a private equity firm which owns shares in the business seeking a loan and acts as a sponsor. Loans which do not involve sponsored lending are described as direct loans. In sponsored transactions, the private equity firm's expertise and relationship with both the borrower and private credit manager often helps to facilitate the loan. Businesses partially owned by private equity sponsors represent only a small percentage of all businesses, yet the majority of finance provided by private credit firms has involved sponsored lending.

When it comes to working without a sponsor, a private credit lender often has to invest more resources to conduct the necessary due diligence when engaging in such direct lending, which partly explains why sponsored lending remains popular. Due to the increased value and time offered to the businesses in direct lending arrangements, as well as the increased risk borne by lenders, direct lending is typically associated with higher costs for the borrowers. However, direct lending is a key area of growth and investment for private credit firms, with many predicting that this business segment will soon match sponsored lending. In addition to the wealth of opportunity in this space, private credit firms value the ability to establish a direct relationship with the borrower, as opposed to an engagement mediated by a third party.

Case study

How SocialChorus CEO Gary Nakamura used venture debt to extend his runway and ramp up growth

When Gary Nakamura joined **SocialChorus** as the company's CEO in 2017, it was because he saw an opportunity to build a great business. He knew that one of the biggest challenges large corporations face is communicating effectively with their employees, and was impressed with the workforce communications platform the company had built to solve the problem. The innovative platform offers enterprises a single place to plan, create, publish, and measure employee communications.

Today, the San Francisco-based company helps some of the biggest, best-known enterprises in the world, including Vodafone, Whirlpool, AB Inbev, and Dow. Using state-of-the-art machine learning and artificial intelligence, SocialChorus improves workforce engagement and communication to align teams around company goals so that they can work as one.

The need for creative capital

According to Gary, over its 10-year history, SocialChorus had used a combination of venture capital, private equity, and venture debt to help fuel its growth. By 2019, the company's revenue was growing quickly and approaching break-even, and Gary was eager to find creative alternatives to fund the continued momentum in the business.

"It's been a great year," says Gary. "We've seen 50 percent ARR growth and are well on our way to becoming a profitable business. Taking venture debt was the logical choice because wewanted to lock in some additional runway. Given how capital-intensive targeting and selling to our customer base is, we knew that the right credit facility would allow us to continue to grow our revenue and complete another renewal cycle with our customer base prior to a potential bigger equity raise next year."

Although SocialChorus has taken venture debt in the past, Gary was open to partnering with other lenders. "When we got introduced to Espresso Capital and got a sense for how the team works, we immediately saw an opportunity," Gary says. "Espresso not only had more competitive terms than any of the lenders we'd worked with previously, they were able to structure the facility with terms that reflected the specific needs and financial profile of our business. That flexibility was critical for us."

Using venture debt to enable ambitious growth targets

As part of its credit facility with Espresso, Gary was able to refinance SocialChorus's existing debt while adding more cash to its balance sheet. Gary plans to put the capital to good use, investing in the company's sales and marketing efforts so that it can continue to grow its revenue base by 50 percent or more, while cementing its position as category leader.

Looking ahead, Gary sees a bright future for SocialChorus. "As large global enterprises modernize their workplaces and ways of doing business, the need to communicate with their workforces is becoming critical," he says. "This represents a wealth of opportunity for us. Our solution enables enterprises to align with their workforce by helping them communicate more effectively and efficiently. Not only that, it's backed up with data and metrics so that they can see if they're being effective and whether their workforce is actually engaged."

Gary says that his experience with Espresso has exceeded expectations. That includes the due diligence process which he describes as thorough but uneventful. "It's been a very good partnership for us," says Gary. "In business, it's always all about who you work with, and Espresso has put together one of the best teams we've seen."

In July 2020, SocialChorus closed a $100 million equity investment led by Sumeru Equitiy Partners.

"Espresso not only had more competitive terms than any of the lenders we'd worked with previously, they were able to structure the facility with terms that reflected the specific needs and financial profile of our business. That flexibility was critical for us."

Gary Nakamura | CEO, SocialChorus

How is private credit regulated?

Oversight of private credit lenders

One of the most common myths about private credit firms is that they are unregulated or lightly regulated, especially when compared with traditional banking. This is incorrect. Private credit firms are regulated as asset managers and the funds they manage are subject to regulatory rules and oversight in relation to their conduct and lending activity. In addition, regulators routinely monitor and assess how a private credit manager is managing its business and any potential risks arising from its lending activity. A private credit firm is required by law to disclose information regarding the performance of its risk management function.

Moreover, the firm's investors, who are often large institutions such as insurance and pension funds, will also require similar disclosures. Should a firm fail to meet its disclosure obligations to a regulator, it will be subject to regulatory sanctions up to and including withdrawal of their authorisation.If a firm fails to meet an investor's disclosure requirements as set out in the investment mandate, it could face commercial and reputational consequences, which may include legal action. Anyone borrowing from a private credit manager will be engaging with a counterparty that is accountable to both their own investors as well as their local regulator.

Is private credit riskier than bank lending?

Businesses obtaining finance from private credit firms benefit from the same safeguards and borrower protection rules as they would with other lenders. While any borrower should always be diligent in their choice of lender, their interests are equally protected with private credit managers as they would be when choosing a traditional lender. In fact, due to the direct and close relationship between private lenders and borrowers, their interests are more closely aligned. Private credit lenders are accountable to a base of investors often representing large pension and insurance funds. These investors expect private credit managers to maintain a portfolio of successful loans and have allocated capital to them on that basis. Private credit firms therefore have no interest in being owners of businesses, but instead make loans with the intention of taking all necessary steps to help borrowers to meet the prescribed terms of the loan.

Oversight of private credit lenders in Canada

In Canada, the origination, credit analysis and lending processes generally carried out by private credit funds and their managers are not subject to specific regulatory oversight, other than laws of general application. The marketing, offering and issuance of interests by private credit funds are regulated under the securities regime established in each province or territory in Canada, with many of the applicable rules and regulations being harmonized across Canada.

Carrying on of a lending business in Canada

Generally, carrying on the business of corporate cash flow and asset-based lending, project finance, mezzanine and subordinate lending and most other traditional lending strategies are not subject to specific legislative oversight in Canada. However, a private credit fund manager should obtain advice to the extent a fund's lending strategy includes making loans in a regulated sector or industry. For example a private credit fund that is arranging, administering and funding commercial or residential mortgages may be required to register and comply with business conduct rules under applicable mortgage broker legislation or as a dealer under applicable securities laws, as required in each province and territory in Canada, and a private credit fund that is arranging, administering and funding pay-day loans will be required to comply with applicable pay-day loan legislation in each province and territory in Canada. Managers of private credit funds must also comply with laws of general application, including privacy, criminal and other laws.

Canadian securities laws applicable to private credit funds

Under Canadian securities laws, a private credit fund is required to prepare and qualify a prospectus in each province or territory where it offers securities unless an exemption from the prospectus requirement is available. The manager of the fund must consider if it is required to register under applicable securities laws and register if required, unless there is an available exemption from the applicable registration requirements. A description of the available exemptions from the prospectus and registration requirements is set out below.

Prospectus exemptions

Private credit funds that offer securities to investors in Canada typically do so pursuant to one or more prospectus exemptions by way of private placement to sophisticated investors. The most common prospectus exemption relied on by private credit funds is the "accredited investor" exemption, which generally requires an investor to meet certain monetary thresholds regarding net income and/or net worth or be certain types of entities. The less stringent compliance and disclosure obligations under the private placement regime are cost-effective and efficient, resulting in quicker access to capital for borrowers.

Joshua Kuretzky
Partner
Davies Ward
Phillips & Vineberg

Registering as an Investment Fund Manager

An entity is required to be registered as an investment fund manager under Canadian securities laws if it is a person or company that directs the business, operations or affairs of an "investment fund". Investment funds are generally entities whose primary purpose is to invest money provided by investors other than for the purpose of seeking to exercise control of a company in which it is investing or to be actively involved in the management of the company. A mutual fund is considered an investment fund under Canadian securities laws. Canadian securities regulators have provided fairly definitive guidance in their analysis of private equity funds and the conclusion that such funds do not constitute investment funds for purposes of Canadian securities laws generally on the basis that the private equity fund invests to exercise or seek to exercise control of a company in which it is investing or to be actively involved in the management of the company. There is also guidance related to mortgage investment entities that provides the same conclusion for certain entities whose business constitutes originating, making and servicing mortgage loans. Canadian securities regulators have not provided any similar guidance with respect to private credit funds more generally, though the manager of a private credit fund that originates, makes and services loans should be able rely on the guidance provided in respect of private equity funds and mortgage investment entities on the basis that the business carried on by the private credit fund is analogous.

A separate analysis will be required to be undertaken in respect of a private credit fund that undertakes additional activities beyond the origination, making and servicing of loans as to whether it will constitute an investment fund and accordingly whether the manager of the fund will be required to register as an investment fund manager under Canadian securities laws.

Dealer registrations requirements

If a private credit fund is open-end, Canadian securities laws deem whoever markets and distributes securities of the fund to be engaged in the business of trading in securities and will require such entity to be registered as a dealer under Canadian securities laws unless an exemption is available. Typically the manager of an open-end private credit fund is responsible for its distribution and is required to comply with the registration and business conduct rules for a dealer under applicable Canadian securities laws. However, an exemption is available to an open-end fund and its manager who engage a registered dealer to distribute the fund. Most private credit funds are closed-end funds. Closed-end funds are generally able to take the position that they are not engaged in the business of trading in securities and not required to be registered as dealers or to offer securities in the fund through a registered dealer.

Debunking myths: private credit vs. bank lending

Since 2008, regulations such as Frank-Dodd (USA) and Basel III (EU) have accelerated the participation of non-bank lenders into the private credit market. However, like with many relatively new opportunities such as the rise of a new asset class and new participants into the market, there can be a circulation of misinformation and misconceptions – these are some of the myths about private credit that we are here to debunk.

Is private credit riskier than bank lending?

There is the impression that non-bank lenders are participants working in the shadows of the big banks, operating businesses with less regulation and oversight. This is certainly not the case for established lenders. Many non-bank lenders may not have the same regulation as the banks, but their level of oversight and overall underwriting process can be just as rigorous. Furthermore, most professional alternative lenders have senior/heads of underwriting that came from much larger institutions, so their calibre, experience and expertise remain just as strong.

With regards to the type of businesses they operate, lending takes many forms, some very vanilla in their structure such as traditional asset-backed lending on real estate and some more complicated and/or labour intensive, such as the constant monitoring seen in account receivables lending (otherwise known as Factoring). In areas such as Factoring, which from an investor standpoint can be viewed as an arbitrage opportunity, whereby non-bank lenders can provide a company a way to improve its cash flow cycle, productivity and overall efficiency through the purchase of their receivables. Often, through the purchase of these receivables, the end-debtor of the receivables are typically companies with higher credit-worthiness than the company receiving the loan (i.e. Fortune 500 companies). From an investors' perspective there is an inefficiency that can be exploited, creating the opportunity to charge attractive yields to the client based on their often lesser business credit, however, receiving higher levels of security due to the higher credit quality of the end debtor (receivable). In the end, most non-bank lenders are just like the entrepreneurial clientele they service, producing a service (lending) to a company that might otherwise not be able to get bank financing due to poor credit, insufficient track record/financial reporting system or historical financial mistakes – despite their receivables being of sufficient value relative to the loan amount. Even good businesses can have blips, and work throughs that can make them unattractive candidates to receive cheaper forms of financing at times, thus the connotation that the lenders to these businesses operate in a less professional manner to a bank is a misconception. In reality, the practice of private lending has existed for centuries and remains to this day, very much an essential component of trade finance.

Is competition from private lenders bad for the banks?

On the contrary, the existence of private lenders serves as a key complement to aid the banks regarding the issuance of debt and adds with the overall health of the economy. Often, non-bank lenders partner with the banks to service clientele which the bank can no longer lend to. Whether it be: deal size, the complication of the transaction, a niche market where banks are unfamiliar, or transactions that require quicker cash than the banks can offer, there is a multitude of reasons why non-bank lenders are sought out. While Private Lending may not be the cheapest option for businesses, its role is imperative to the infrastructure and overall health of the financial economy.

Rob Anton
President of Next Edge Capital Corp.

Risk return profile - Too good to be true?

By investing in private credit strategies, investors can partake and profit from increased returns relative to risk, as a result of regulatory changes, illiquidity premiums and other supply-and-demand arbitrages.

For instance, given the low-interest rate environment and the lack of yield provided by traditional fixed income, private credit has been used as an alternative to produce yield and reduce a portfolio's systematic risk. On a risk-adjusted basis, private lending has shown its ability to return equity-like returns with bond-like risk. Collateralized loans, which have been negotiated privately, and that may also be backed by personal guarantees and GSAs, allow lenders to further securitize their positions without taking on undue risk, all the while continuing to charge a premium interest rate – the perfect arbitrage opportunity for higher returns, with downside protection.

Risk is reduced due to the fact that the nature of private lending is outside of public markets. With privately negotiated terms and conditions, these loans are free from market manipulation and sensitivity, significantly reducing a portfolio's volatility. Its low correlation to the market allows investors to further enhance their diversification, a key portfolio tool to reducing downside risk, especially in times of uncertainty in the equity markets (such as in today's climate with Trump, the China-Trade Wars, and Brexit). (Wilson, 2019)[1]

Ultimately the risk-return profile is also extremely attractive in worst-case scenario situations such as a company's insolvency. Comparable to other forms of investments such as equity, when it comes to recouping your principal investment in the event of a company's default, senior and junior secured bonds are the first to be repaid on the capital stack, and it is within these two categories where most private credit fund strategies structure their loan positions.

Currently, the private lending market sits at over $1 trillion USD globally (McKinsey & Company, 2019)[2], well on its way to beat Preqin's initial assumptions in November 2018 that anticipated the private credit market would reach over $1.4T in AUM in 2023, which consequently, would also lead private credit to overtake real estate, to become the third largest alternative asset class (Preqin, 2018)[3]. These powerful expectations make private credit an exceptionally fast-growing market, especially for a relatively young and still emerging asset class. Furthermore, with the continuing influx of new money (Sambo, 2019)[4] pouring into the asset class by Canadian Investment goliaths like Canada Pension Plan Investment Board (CPPIB), Public Sector Pension (PSP) (Public Sector Pension Investment Board , 2019)[5], and Ontario Teachers' Pension Plan (OTPP) (Annual Report, 2018)[6] there is overwhelming evidentiary support for private credit place as a key portfolio component.

According to Preqin's Alternatives 2019 report, strategy asset inflows show credit strategies being among the top in 2018, and among the strategies with the least outflows in Q1 2019. (Preqin Alternatives in 2019 Report, 6.27.19)[7]. The same report also showed that among institutional investors, expectations on the performance of private credit remain largely consistent among investors, with 73% stating it matched expectations and 18% indicated that it exceeded expectations. Furthermore, according to Private credit Investor's September 2019 publication the outlook for private lending continues to be positive with global investor appetite expected to increase (Private credit Investor, 2019)[8]. Thus, for newcomers looking to deploy capital into new strategies such as private credit, learning to separate the fact from the fiction is a great start to understanding why private credit has become such a strategic piece for sophisticated portfolios over the last decade, and, more importantly, how it can further become part of yours as an investor.

1 The Growth of Private Investor Interest in Debt Structured Investments - July 13, 2019
2 The Rise and Rise of Private Markets - McKinsey Global Private Markets Review 2018
3 The Future of Private credit by Preqin
4 Canada Pension Giant CPPIB is Extending its Private Credit Wager - BNN Blomberg
5 Think. Act. Globally. Public Sector Pension Investment Board - 2019 Annual Report
6 2018 Annual Reports – All the Right Elements - Ontario Teachers' Pension Plan
7 Preqin Alternatives in 2019 Report - 6.27.19 - Manager of Investor Data - Preqin (Joseph Borda, CAIA)
8 Private credit Investor - September 2019 Report

Assessing eligibility

Understanding the investment process

Understanding how private credit firms assess whether to lend to a company is crucial to understanding whether private credit is the right finance option for you.

While each private credit firm will subscribe to a unique investment mandate according to the firm's ethos, all reputable private credit firms will engage in considerable due diligence and typically invest in only a small percentage of the businesses they assess. This ensures that both the lender and borrower are the right fit for each other. As private credit firms may specialise in one sector or geography, borrowers should consider various firms when searching for funding options. Advisors can assist borrowers with identifying suitable lenders.

The diagram opposite outlines the core process a business should expect to undergo when attempting to obtain financing through a private credit firm. The timeframe associated with these steps can take several months to be completed, however, a large number of borrowers are unlikely to be taken forward in the early stages of the process. Throughout the investment process, lenders typically consult third party experts and other external research providers.

Case study

Apollo provides CVC with bespoke capital solution to finance the acquisition and growth of System C, a UK health software leader

Apollo Global Management, Inc. (together with its consolidated subsidiaries, "Apollo" or the "Firm") announced that certain funds managed by its affiliates ("Apollo Funds") have provided debt financing to CVC for its acquisition of System C, the UK's leading provider of health and social care software and services.

The financing was comprised of a £115m unitranche facility and a further committed acquisition facility to support the company's expansion plans.

System C provides vertical software solutions for hospitals, social care, immunisation management and population health that help to improve the quality and efficiency of patient care. The bespoke financing solution provided the company and CVC with both flexibility and available capital to help deliver its ambitious growth plan.

Typical private credit investment process

1. Lender receives information on many investment opportunities through advisors, banks, private equity firms and own network
2. Borrowers are filtered according to broad criteria of investment mandate (industry, business size, geography)
3. Borrowers undergo a detailed review and pre-assessment
4. Borrower is screened by the investment committee
5. Preliminary term sheet / loan agreement is issued to the borrower
6. Complete due diligence
7. Final review by the investment committee
8. Borrower is presented with a final loan agreement / term sheet
9. Loan is issued

Due diligence - What is a 'good fit'?

Private credit firms undertake an extensive due diligence process to identify whether a business is a 'good fit' for the firm's investment mandate. It is in the best interests of private credit firms to lend responsibly and be diligent when assessing a borrower's creditworthiness and ability to repay financing. As well as being critical to the success of the private credit firm, there are regulatory and investor requirements to ensure that the firm has robust risk management systems in place.

While equity investors place great emphasis on the growth trajectory of a business in order to increase the value of their ownership stake, private credit managers seek to ascertain whether a potential borrower will be able to repay the loan and interest the business has been given. The following provides an indication of the factors a firm would typically analyse in the course of its assessment.

In which sector does the business operate?

Private credit firms often specialise in specific sectors, for example, agriculture, automotive, retail, healthcare or real estate. The private credit manager will seek to finance businesses within that space, as the firm will be able to undertake a more sophisticated analysis of the competitiveness and trajectory of the sector, as well as the ability to more accurately assess the creditworthiness of the business. In the long term, a private credit firm will be a better partner to borrowers within its chosen sectors, so this is likely to be one of the first things that determine whether or not they are a good fit for you.

Where does the business operate?

Knowledge of commercial and regulatory requirements for the countries in which the business operates enables the private credit manager to better understand and predict how the borrower's business may be affected by broader macro-economic and regulatory conditions. As a result, a borrower should expect that a private credit firm may enquire about:

- Regulatory filings, licences, permits and regulatory approvals in the jurisdictions in which it currently conducts or intends to conduct business
- The potential effect of any pending or proposed regulatory changes
- Any pending or threatened proceedings or investigations before a court or regulatory authority

> *In the long term, a private credit firm will be a better partner to borrowers within its chosen sectors*

AIMA Due Diligence Considerations for Retail Investment Advisors

Investment Manager

- What is the background and experience of investment manager & the investment team?
- What is the governance surrounding the investment manager & investment team?
- What are the features of the investment manager's compliance culture?
- What risk management frameworks are in place? For example, independent reporting lines, operational risk management, conflicts of interest, etc.?
- Are the members of senior management of the investment manager, the portfolio manager and/or the fund directors personally invested in the fund?

Strategy

- What is the fund's investment objective and principal investment strategies?
- Have the objectives of the investment strategy changed in the past 5 years?
- From where are the underlying positional data, market data and any underlying models sourced for this strategy?
- Are there position limits and what are they?
- Who makes the portfolio management decisions and how are they made?
- What is the performance history? In what type of markets would this strategy be expected to outperform or underperform?
- What method(s) does the investment manager use to measure the total risk of a portfolio using this strategy?
- How much financial leverage does the fund use on average? What are the limits? What are the sources of leverage?
- Are there any capacity constraints?
- Offering documents, subscription agreements, and process for purchases and redemptions?
- What are the fees, including performance fees and calculation methodology?
- What is the valuation policy and frequency of valuation?
- How long would it take in normal market conditions and stressed market conditions to liquidate the fund without incurring unusual costs?
- What portfolio data does the investment manager provide to investors, and with what frequency and time lag?
- Who are the outsourced service providers of the fund? For example, prime broker, auditor, custodian, administrator, legal counsel, etc.?

Private Credit Strategy

- How does the investment manager source potential borrowers? Direct relationships with the borrower (e.g. in-house advisory), private equity sponsors, banks, via corporate debt advisors (e.g. audit firms/lawyers, consultants etc.), marketplace lending platforms?
- What is the typical target range of maturities sought?
- How are repayment terms on originated loans typically structured?
- Describe the investment manager's credit assessment and due diligence process.
- What types of representations, warranties and covenants are the borrowers required to give and what collateral is required? How is this monitored?
- What is the investment manager's policy towards impaired/stressed loans or bad debts and what track record does they have?

Assessing the balance sheet

There are three key concepts which underpin a private credit manager's assessment of your business:

1. **EBITDA:** The key measure used to assess a business's financial performance is EBITDA which stands for **E**arnings **B**efore **I**nterest, **T**axes, **D**epreciation and **A**mortisation. In practice, EBITDA is a metric of a business's profits that can be used to showcase a firm's financial performance without accounting for its capital structure. Despite its widespread use, EBITDA is not part of the Generally Accepted Accounting Principles (GAAP) or International Financial Reporting Standards (IFRS) due to considerable differences in how the figure is calculated. This is further complicated by the concept of adjusted EBITDA and add backs. **Adjusted EBITDA** differs from the standard EBITDA measure in that it is used to normalise income and expenses, as companies may have unique expense items such as redundant assets, bonuses paid to owners, rentals and other one-off costs. These items are referred to as **'add backs'** as they are added back to the net profit value of the company. It is commonplace for private credit managers to look at adjusted EBITDA as it more accurately reflects the financial position of a business.

2. **Leverage ratios:** A leverage ratio is a financial ratio that indicates the level of debt held by a business against other measures in its balance sheet, income statement or cash flow statement. The debt / EBITDA ratio measures a company's ability to repay its debts. A high ratio may indicate that a business's debt load is too high to consider advancing further loans. Other types of leverage ratios include:
   - Debt-to-Assets Ratio =
     Total Debt / Total Asset
   - Debt-to-Equity Ratio =
     Total Debt / Total Equity
   - Debt-to-Capital Ratio =
     Total Debt / (Total Debt + Total Equity)
   - Debt-to-EBITDA Ratio =
     Total Debt / Earnings Before Interest Taxes Depreciation & Amortisation (EBITDA)
   - Asset-to-Equity Ratio =
     Total Assets / Total Equity

3. **Loan-to-Value (LTV):** The LTV ratio compares the size of a loan to the value of the asset on which the loan is based. The LTV ratio is an important metric that assesses the risk a lender carries by providing the loan to a borrower. Difficulty may arise if the value of the loan is significantly higher than the value of the asset, as this reflects a risk for the lender in the event of a default.

In addition to the above key criteria, a private credit firm may also request additional information, such as:

- Current and past balance sheets, income statements, cash flows and liquidity
- Current budgets and projections including business plans and projections for product sales and cost of sales
- Projected financials for the term of the requested loan (e.g. five-year term = five-year forecast)
- Latest accounts receivable, accounts payable, aged debtors and creditors reports
- All local and foreign tax returns
- Current debt schedule (including payment history)
- Seniority structure for existing debt
- Existing material charges
- Any auditor's letters and reports to management
- Insurance policies

Collateral

Assessing a company's value requires an overview of its assets, of both physical assets and intellectual property. Collateral is the most common way to mitigate the risk a lender takes on when providing a borrower with a loan. It acts as a security, should the borrower be unable to repay the lender. This is particularly relevant for loans that are not primarily reliant on a company's cash flow but rather its assets. As part of the lender's due diligence process, independent evaluations of collateral are usually commissioned to ensure an objective assessment of its value. Collateral, in the case of secured lending, by itself should not be a predominant criterion for approving a loan and cannot by itself justify the approval of any loan agreement.

Management and employees

Effective management is crucial for a business to continue to function throughout the lifecycle of the loan. Private credit managers will assess the leadership of a business according to tangible and intangible factors. Examples of relevant factors include experience, education, team size and advisors. Due to the direct and bilateral relationship established in the process of obtaining private credit financing, trusting the borrower's management team is a crucial part of the firm's decision-making process.

Therefore, a business may be asked to provide:

- Corporate management organisation chart including titles and backgrounds of all senior officers
- Employee handbooks and policy manuals
- Employment agreements and consulting agreements, severance and collective bargaining agreements, and confidentiality and non-disclosure agreements
- Summaries of all threatened, outstanding and concluded litigation and arbitration proceedings

How sustainable is the business?

ESG criteria have become firmly established as standard in the financial sector to answer the question of how sustainable a business may be in the long term.

As a long-term investor, a private credit lender will therefore screen borrowers according to ESG criteria to assess the longevity of the business.

How each private credit lender interprets and values ESG considerations is different. However, a manager may broadly distinguish between positive and negative ESG screenings or look to make investments according to 'impact' driven objectives.

1. Positive ESG screening

This describes the use of environmental, social, and governance factors when assessing a potential borrower. Fundamentally, ESG integration is predicated on the notion that ESG factors can be financially material to investment performance and can, in turn, lead to superior financial performance. The notion that a well-run company tends, on balance, to deliver better financial performance than one which is run poorly is relatively uncontroversial. ESG factors can also be thought of as risk factors, such as the risk that a company's practices may not be sustainable in the long term due to the environmental degradation they cause, or an unrepresentative leadership team may represent a limited viewpoint or ineffective internal governance of the business.

Responsible investment should not be viewed as a rigid one size fits all model or checklist of issues to be considered in isolation, but instead as an overarching framework tailored to each business. Naturally, expectations of compliance with key ESG considerations are proportionate to business size and capabilities. As the importance of ESG grows, it is prudent to consider how a business may perform against the factors a private credit manager is likely to consider when making lending decisions. It is often the case that businesses are already taking actions which would be considered in line with ESG criteria, so it may simply be a matter of adequately recording and reporting existing measures.

2. Exclusionary / negative screening

This approach focuses on doing no harm and involves the exclusion of certain sectors from investment based on products or services, or certain behaviours that an investor deems undesirable for moral reasons which have a detrimental impact.

3. Impact investing

More rigorous forms of responsible investing, going beyond the above, are known as impact investing, which requires a company to invest capital in order to create measurable social or environmental goods. In many ways, impact investing bridges the gap between traditional investing and philanthropy, by deliberately creating societal benefits whilst also generating profits.

Table 1: United Nations Principles for Responsible Investment (abridged) [ii]

The below table is an example of the questions a private credit manager may ask as part of their approach to responsible investing.

Overall	Does your business have an ESG policy?
	Does your business track and monitor ESG initiatives?
Environment	Does your business have an environmental policy?
	Are you able to estimate the CO_2 footprint of the business?
	What is the water or energy consumption of the business?
	Does your business operate a waste recycling policy?
Social	Are you planning to create further jobs through the expansion of this business?
	Do you enforce a diversity and inclusion policy?
	Do you follow fair labour practices?
	Describe your recruitment process and average retention rates
	Do you abide by an equal opportunities policy?
	Do you maintain a data security and privacy policy?
	Do you abide by the Modern Slavery policy?
Governance	Does the business have independent member(s) of its board?
	Does the business abide by a corporate code of ethics?
	Do specific committees exist and what are they tasked with?
	Do you engage in systemic risk management?
	Do you maintain transparency of payments?

Loan agreements and monitoring

Understanding loan agreements

While it is highly advisable to seek professional advice when negotiating the terms of a loan agreement, this section offers a basic introduction to the key issues to keep in mind when reaching this stage in the process. From a private credit manager's perspective, documentation is a crucial element of maintaining a rigorous investment process as loan documentation should appropriately reflect the risks identified in the due diligence process. A detailed overview of common terms included in loan agreements can be found in the Appendix.

Case study

LendInvest steps in with a $3.6m Development Exit loan following Covid delays

As a result of Covid, an experienced developer working on a 9 unit scheme in Surrey experienced delays which pushed completion behind schedule and meant planned sales were delayed.

Approaching practical completion with a development facility but needing to wait longer to sell the units, they were introduced to LendInvest to refinance onto a Development Exit facility to secure the completed properties while they were sold.

This refinancing gave them the breathing space of further time to sell remaining units, settle anxious investors during an uncertain period and clear outstanding debt. The loan was structured at a loan-to-value of 69%.

1. Purpose and loan term

A loan agreement should stipulate: (a) the purpose of the finance sought; (b) the term of the loan; and (c) the conditions of repayment such as interest rates. It is important for the borrower to clarify and define which type of finance is most appropriate for the needs of the business.

2. Interest rate

Another key concept to understand is the type of interest rate a lender may charge. Generally, a loan agreement will stipulate interest rates as either fixed or floating/variable. Fixed interest rates remain the same throughout the lifecycle of the loan, and the floating/variable rate will change in line with a reference rate. This reference rate has typically been LIBOR (London Interbank Offered Rate), which is currently being phased out. An explanation of alternative rates is included in the Appendix.

3. Covenants

Loan agreements are generally composed of undertakings or covenants, outlining the terms borrowers agree to comply with and upon which the provision of the loan is conditioned. Covenants are split into positive, negative and financial duties.

Types of financial covenants

Financial undertakings, or covenants, govern the financial position and health of the borrower and set out the parameters within which the borrower must operate. Financial covenants can be grouped into two broad categories – incurrence and maintenance covenants. An incurrence covenant only takes effect if the borrower is taking a specified action, meaning that they must be met only at the time of incurrence, whereas a maintenance covenant requires the borrower to maintain a certain level of activity and is typically tested at regular intervals. Common covenants include:

- Coverage: requires the borrower to maintain a minimum level of cash flow or earnings relative to specified expenses, most often interest, debt service and fixed charges;
- Leverage: sets a maximum level of debt relative to either equity or cash flow, with total debt-to-EBITDA level being the most common;
- Current ratio: requires the borrower to maintain a minimum ratio of current assets to current liabilities;
- Tangible net worth (TNW): requires that the borrower has a minimum level of TNW, often with a build-up provision, which increases the minimum by a percentage of net income or equity issuance; and
- Maximum capital expenditure: requires the borrower to limit capital expenditure to a certain amount in a given period.

Types of non-financial covenants

Non-financial covenants are promises made by the borrower that are not financial but tend to be operational, legal, tax or insurance related in nature. Loan agreements tend to contain both positive and negative non-financial covenants.

Positive covenants prescribe the conditions necessary to maintain the stability of the borrower's business. Examples include:

- Requirement to maintain the corporate existence
- Requirement to maintain insurance policies
- Requirement to request permission from the lender when the entity is considering some form of change of ownership

Negative covenants list various activities that the borrower may not engage in without the lender's consent, while allowing enough flexibility to carry out their business. Examples include:

- Restriction on merger or acquisition deals without lender consent;
- Restrictions on substantial changes within the borrower's business;
- Restriction on investment activities without the lender's permission;
- Restriction on dividend distribution; and
- Restriction on the sale of assets without consulting the lender.

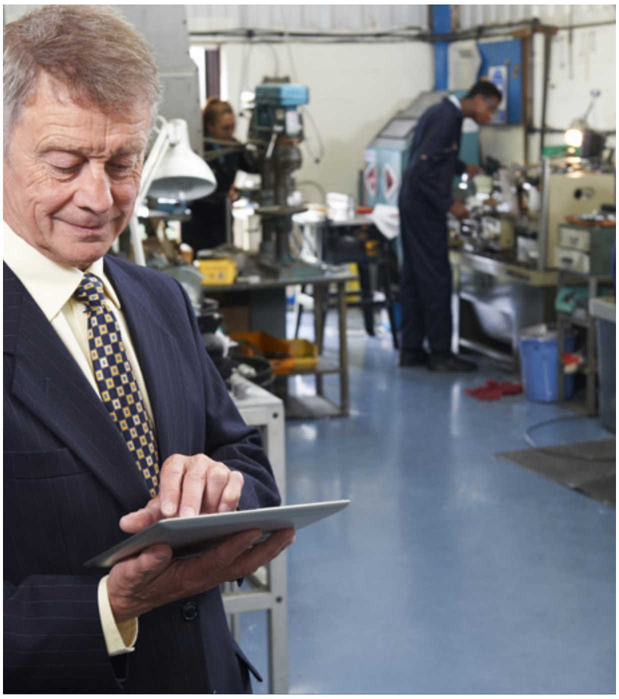
Sample term sheet

The below offers a broad overview of key components a borrower may encounter in a private credit loan agreement. The appendix includes examples of term sheets for a first lien as well as second lien loan which are specific to Canadian private credit managers.

Borrower	Borrowers includes all group companies which may need access to the loan or the working capital element. Consideration should also be given including target companies being acquired with the funds provided.
Guarantors	Guarantors includes the borrower group or company and all operating subsidiaries of the company.
Obligors	Obligors includes all legal parties who owe or undertake an obligation to another through the loan contract.
Purpose	A borrower must disclose the purpose for which the business intends to deploy the financing provided.
Maturity	This designates the length of time after which the borrower must return the principal loan amount.
Ranking	As noted in the capital stack, each loan held by a business is ordered in priority of seniority in terms of repayments and access to assets.
Margin / Interest	The margin denotes the extra percentage rate of interest charged by lenders over the relevant basis rate reflecting the credit quality of the borrower. Most interest rates in loan contracts are set on the basis of LIBOR. However, LIBOR is currently being phased out by macroprudential regulators and replaced by SONIA (see Appendix).
Cash Sweep	A cash sweep mandates the borrower to use any excess free cash flows to pay outstanding debt rather than distribute it to shareholders.
Security	In secured lending arrangements, a lender requires a 'security' or collateral for cases in which the borrower may be unable to repay the loan. Such securities may include: First-ranking pledge over the shares in the borrower; First-ranking fixed and floating security over all the assets and undertakings of the borrower and its subsidiaries; and Guarantees from each of the holding companies of the borrower and their respective subsidiaries subject to confirmation of structure.
Voting	Should a borrower hold multiple loans with separate lenders, voting arrangements determine what amendments may be made to the loan agreement with the consent of only one lender, and which require the agreement of other lenders to the business.
Governing Law / Jurisdiction	The governing law is the law of the jurisdiction in which the loan will be agreed. Often the parties select the jurisdiction where the lender resides.

What happens after I receive the loan?

Once a loan has been extended, a borrower's relationship with the private credit firm does not end. In fact, the firm's investment professionals should engage in regular dialogue with company management to monitor performance. There are several ways for lenders to continue monitoring the credit during the tenure of the loan.



Covenants

During the due diligence and loan origination process, appropriate loan covenants will have been agreed in the document. Loan covenants are often incorporated into loan agreements to allow the lenders to exercise additional control over the borrowers in times of stress or poor performance, with the aim of minimising any losses to the fund. Examples include:

- **Reporting covenants** in the credit agreement which require the borrower to provide regular certified financial information, notice requirements for material events, litigation and defaults. The frequency of ongoing monitoring should be agreed in advance.
- **Financial analysis** in conducting the monitoring of the borrower, a lender will engage in an analysis of financial statements, as it serves as an early indicator of changes in a borrower's risk profile.
- **Inspection rights** granted to the lenders in the credit agreement with respect to locations, books and records.
- **Review of collateral** through field examinations to assess potential value erosion.
- **Annual certifications** by the borrower as to no defaults that require a borrower to review its operations.
- Right to take a **board observer seat**.

What happens if I cannot pay back my loan?

If a borrower undergoes periods of stress or challenging circumstances, it is in the private credit manager's best interest to work with the business to find an effective solution.

This will typically involve working with the borrower to understand the situation and identify how best to get back on track. Such measures are tailored to the unique circumstances of each borrower but can range from enhanced monitoring, offering temporary forbearance or developing a new business plan. The following sections provide further detail on what such steps may look like.

Enhanced monitoring

If a heightened risk of default is revealed during routine monitoring, the private credit manager will place the borrower on its watchlist. Often this is due to adverse operating trends, ill-proportioned balance sheets, or adverse economic or market conditions. Non-financial considerations may also include management issues, pending litigation or other material structural weaknesses. For the borrower this means that the private credit partner will likely request more frequent access to financial information and other monitoring tools.

What does forbearance look like?

Forbearance refers to instances where a lender conditionally agrees to refrain for a limited time (the forbearance period) from exercising its rights under a defaulted loan agreement while the borrower seeks to refinance, restructure or otherwise repay its debts. A forbearance agreement often requires the borrower to make certain concessions and undertake new actions. This may include adopting substantive amendments to the loan documents that go into effect immediately and guide how the credit facility will operate during the forbearance period.

The main benefit of this approach is to give a borrower more time to meet its obligations under the loan agreement. In instances where the borrower is facing a temporary period of stress but its long-term creditworthiness remains strong, this approach can allow the borrower to ride out this period of stress whilst ultimately meeting the terms of the credit agreement.

Forbearance measures could include:

- Entering into a standstill agreement with the borrower to alleviate any immediate insolvency concerns;
- The private credit manager working with the borrower to develop a remedial or recovery plan;
- Securing alternative sources of funding;
- Payment holidays / moratorium on interest;
- Payment holidays / moratorium on principal;
- Conversion of cash payments to PIK;
- Principal reduction; and
- Debt / equity swaps or similar restructurings.

What happens in the event of default?

In circumstances where all measures implemented to assist a business with managing its adverse conditions may not be working or are proving more challenging, it may be appropriate for the private credit manager to exert more control. The degree and method by which such control may be exercised can vary. Examples could include taking an active role in the borrower negotiations with their suppliers or customers. Where appropriate, a private credit manager may also use the powers under the loan agreement to appoint lender representatives to the borrower's governing body to support the proposed rescue measures.

As a final measure, the private credit manager, like any lender, may seize the collateral provided by the borrower. However, a firm will explore all other possibilities before doing so, as a defaulting business is not in the interest of any reputable private credit firm which will seek to prevent this undesirable outcome.

Restructuring: The direct lender's way

Payment defaults are an inherent risk in lending. Companies can fail for many reasons but when a firm is unable to meet its debts when they come due or its operating performance continuously falls due to an unsustainable business model, a financial or business restructuring is usually necessary. Restructuring options fall on a spectrum ranging from amendments to interest rates or repayment terms in the lending agreement to formal insolvency proceedings, which in the worst case involves liquidation. Irrespective of the scenario, direct lending managers need to be adroit at managing the restructuring process if they are to withstand cycle turns and economic crisis when high leverage and poor business fundamentals conspire to raise the volume of defaulted loans. Loan workouts are highly entrepreneurial endeavors characterized by creativity, unpredictability, and extraordinary challenge.

This article explores loan restructuring options and explains how direct lending managers can add real value to the restructuring process by enabling the distressed debtor to become rehabilitated and reward investors, workers, and the rest of society. The right solution will depend on the circumstances. No two restructurings are the same and there is no standard template. This article attempts to provide context and themes for a successful loan restructuring in the manner a direct lender would.

Informal vs formal

The destruction of companies, assets, and products is often the price of progress. This is how Joseph Schumpeter (1883-1950), acclaimed Austrian economist and author of "Capitalism, Socialism and Democracy", describes "creative destruction." The extinction of firms that cannot keep pace is desirable because it helps reallocate capital and human resources to better uses. However, this reallocation is not always efficient or necessary when failure is self-inflicted by a bad management team or capital structure rather than caused by a technological or market evolution. While firms in terminal decline should be culled out of business to make room for more productive companies, other distressed firms that can be turned around through better management, business model, or capital structure, should be rescued. Restructuring is about fixing distressed companies, either through deleveraging the balance sheet (a financial restructuring) or by improving operations and therefore cash flows (a business restructuring).

When a borrower faces financial distress, it will first resort to negotiating with its creditors through an informal restructuring. If affected parties engage in good faith negotiations with genuine intentions to achieve an amicable resolution, then the savings in time and expense versus a formal restructuring can be significant. It also avoids the likely loss of confidence from stakeholders in the borrower's value chain (especially suppliers and customers) and the attendant interruption in operations. The stigma of a formal restructuring, conducted through a statutory insolvency regime[1], may unfairly create the perception of greater risk of failure of the borrower, and result in vendors and customers avoiding credit extensions, preferring upfront cash payments or delivery before payment. Where possible, lenders should pursue an out-of-court, informal restructuring to save resources and preserve value in the distressed business.

Informal restructuring best functions where the creditors are either few in number or share a common goal of seeing the restructuring through. Coordinating the response of creditors to ensure

1 In Canada, the two primary pieces of bankruptcy legislation are the Bankruptcy and Insolvency Act (the "BIA") and the Companies' Creditors Arrangement Act (the "CCAA"). The BIA is the principal federal legislation in Canada applicable to insolvencies. It governs both voluntary and involuntary bankruptcy liquidations as well as debtor reorganizations. The CCAA is specialized companion legislation designed to assist larger corporations to reorganize their affairs and is similar to Chapter 11 of the United States Bankruptcy Code. The CCAA provides a company in restructuring with greater flexibility and greater creativity in conducting its reorganization

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Third Eye Capital

they can reach a consensus towards supporting a debtor out of crisis is difficult. Not all creditors are willing to exercise restraint in the face of default and there is little incentive to share in the benefits and burdens of a business rescue if not all creditors are going to provide additional financing or be willing to cooperate with the debtor to achieve a turnaround plan. For example, a secured lender willing to forbear from enforcing on its collateral in connection with a defaulted loan or making a distressed debt-to-equity exchange, will expect similar concessions from other lenders. Without agreement among all creditors, even the best laid restructuring plans are at risk of being derailed.

The increased participation by private credit funds in recent years in credit markets traditionally dominated by banks, will drive the trend toward fewer informal restructurings of distressed debtors. This is because of more transactional (as opposed to relationship-based) mandates by private credit funds that place primacy on financial self-interests rather than community or social goals (to which banks are more sensitive). When multiple banks are the senior creditors of a distressed debtor, there are self-enforcing norms that encourage lenders to cooperate. In a bank syndicated loan, for instance, if one bank becomes overly-absorbed with maximizing its own utility, even at the expense of the other banks or the successful restructuring of the distressed business, it would be putting itself in a position to be censured by the other banks through the imposition of informal sanctions. The dissenting bank risks not being "invited" into future syndications and would be left out of the opportunity to partake in profitable loans. Such moral suasion works when there are only a handful of like-minded participants in a given credit market (like Canada's bank oligopoly). Informal restructurings can be effective in such circumstances. However, since any informal restructuring depends on the willingness of lenders to alter their pre-distress rights, private credit funds and other non-bank lenders that are almost exclusively financially motivated and indifferent to their future relations with other creditors will engage in aggressive game-theoretic arguments, making settlement more difficult. In an informal restructuring, there is no way to bind a dissenting creditor who wants to hijack the rehabilitation of a distressed borrower. Despite the savings in time and resources, informal restructurings can be usurped by the whims of a single creditor. Given that the number of non-bank lenders in Canada has more than doubled in the past ten years, particularly private credit and credit-focused hedge funds, the willingness of lenders to settle on a restructuring plan without court involvement has become impractical.

A sound insolvency regime is crucial to settle disagreements among management, owners, lenders, suppliers, and other stakeholders. Coordination problems, contract defects, and information asymmetries often occur in a negotiated, informal process, making it difficult to facilitate an efficient and orderly restructuring of a distressed debtor. There are competing interests at play which fall on the spectrum between desire for immediate repayment (usually through an expeditious liquidation of the business or assets) to the need to make compromises to facilitate the survival of the business. During the period when the distressed debtor is suspected of being insolvent or considers commencing a restructuring, some creditors for varying reasons may be unwilling to either remain invested in the debtor or provide further capital. Some lenders may simply want to "move on" by rapidly enforcing their individual claims or selling their defaulted debt, even if it results in a reduction in the total value recovered. A formal restructuring is sometimes necessary to prevent or "stay" the improvident actions of creditors and to bring all affected parties to the table in order to facilitate a resolution.

2 Over the past two decades, Arif has led complex business turnarounds and managed several successful problem loan workouts of middle-market borrowers in Canada..

Going formal

Formal restructuring in markets with established insolvency laws has the advantage of binding all relevant stakeholders, particularly creditors, to a court-approved plan. It offers the distressed business the opportunity to not only restructure its debts but emerge and continue to operate as a going concern. Courts encourage the financial reorganization of a distressed debtor rather than liquidation. At the heart of every formal restructuring is the maximization of value for the creditors and the rehabilitation of the distressed business. Expectation that the business can be restored to financial health, continue to provide jobs, and remain a going concern motivates a turnaround over a liquidation. A hastened liquidation of the business may best serve the interests of senior creditors protected by security over the assets of the borrower, especially where asset values are depleting, but courts will scrutinize the consequences of allowing a sale based on its utilitarianism. Liquidations are most practical when the business has no prospects of being a going concern and management has conceded to such view (often implicitly by way of abandonment).

The CCAA framework in Canada allows distressed companies to liberate from legacy costs, remove burdensome contracts, and eschew obsolete business models. It gives a debtor "breathing room" through an interim "stay" (or moratorium) on enforcement of actions or claims against its assets, which can be co-opted as a tool to ensure that the debtor is able to maintain the liquidity necessary for running the distressed business pending negotiation of a restructuring plan. Faced with financial distress, a company will be permitted to continue using its assets to facilitate a restructuring. It means pre-distress creditors, including secured lenders, may not remove assets (even assets that have liens in favor of the lenders) if they are necessary for the continued operation of the business, until management devises and implements a viable plan for the restructuring. This plan is the crucible of a formal restructuring and can be approved even against the objection of some creditors, thereby resolving the cooperation and coordination issues that impede informal restructurings.

A successful formal restructuring requires participation from a broad set of actors including management, directors, creditors, shareholders, investors, regulators, administrators (including monitors, receivers, and trustees), and courts. However, the determination of who manages the distressed business has implications on outcomes. The most common option is to have the current management remain in place to run the day-to-day affairs of the business and lead development of a restructuring plan. At the other extreme is replacing existing management with a new team, which signals to observing constituencies a lack of confidence with previous operators. An in-between option is appointing an external person, such as a "Chief Restructuring Officer" to supervise the management of the distressed business as the restructuring is negotiated and a plan is put in place.

One of the strongest arguments in support of retaining the distressed debtor's management as the business commences restructuring, is their experience and knowledge. The formal restructuring regimes in Canada and the U.S. support a debtor-in-possession ("DIP") concept, which keeps existing management in place and the debtor in control of its assets while the restructuring is underway. In addition to the knowledge and experience which is brought to bear, retaining the management of the distressed business preserves relationships with key stakeholders such as customers and suppliers and may be a critical step to ensuring that the restructuring of the distressed business starts as soon as the signs of distress become evident. Early intervention, when the debtor presumably still has valuable operations, can hasten the successful exit from a costly, court-supervised formal restructuring.

Existing management's retention of control of a distressed business is not an absolute privilege. A management team that has defrauded, or has been dishonest in its dealings, will not be afforded the room to continue in its fraud at the expense of the creditors of the business. A DIP must act as a fiduciary and is duty bound to protect the interests of creditors too. That is why the CCAA provides for a mechanism for an independent insolvency professional to monitor the distressed company's ongoing operations and assist with reporting to the court and stakeholders on viability of the business and progress on the restructuring plan. A monitor's mandate includes the power to take financing initiatives, such as borrowing new money by granting super-priority security to lenders during the period of restructuring (commonly referred to as DIP financing).

Even in light of this, TEC notes that the bar to displace management is very high. Merely evidencing incompetency, mismanagement or imprudent decision making on the part of management is not enough. Fraud and gross negligence have to be proven to compel a restructuring court to oust existing management. Private credit managers can be successful in motivating untrustworthy management teams to resign by threatening to increase management's potential exposure to certain liabilities. The monitor has the power to challenge transactions undertaken by the management of the now distressed business which it considers to be disadvantageous to creditors and request a court order for them to be clawed back into the estate of the debtor. Such fraudulent conveyance cases tend to be highly contested and are typically not pursued unless the underlying amounts are significant.

Direct lending managers affected by a formal restructuring will have varying influence on the plan of restructuring depending on their lien position and scope of collateral. Direct lenders that are pre-petition secured creditors should consider providing DIP financing in a formal restructuring so that they can exercise better control over collateral and position themselves for a higher recovery of their pre-filing exposure. In some cases, the DIP financing can be used to repay the pre-petition debt. DIP financing is critical for distressed debtors that do not have sufficient cash for working capital to maintain ongoing business including for the payment of rent, wages, inventory, maintenance, professional fees, and other critical expenses. Through the use of covenants, such as the achievement of timely restructuring milestones and certain expense caps (e.g., management salaries), a direct lending manager can use the DIP financing to ensure the preservation of going concern value while keeping the debtor's management team aligned and accountable. A DIP financing also positions a direct lender as future owner of the business by potentially converting the financing into a major equity stake when the firm exits the formal restructuring with a plan (a plan surely influenced by the direct lending manager).

The successful restructuring of a distressed business depends vitally on a stay of creditor action and enforcement, a plan and means of enforcing that plan (even against the volition of dissenting creditors), and a management structure to implement the restructuring. Informal restructuring has advantages but its reliance upon cooperation among the parties (primarily the creditors) limits achievement of the foregoing vital components necessary for success. A formal restructuring is the only sure way to ensure legal certainty of a plan and a direct lender with exposure to the distressed debtor must know how it will empower itself before entering such a process.

Direct lenders to the rescue

The declining risk appetite of banks in the face of rising defaults and insolvencies is paving the way for private credit funds to play a greater role in distressed company restructurings. Banks prefer conservative paths to resolve problems and tend to become too closely attached towards standard litigation options when they decide to enforce rights and remedies against defaulted borrowers. Banks are not inclined to incur more operational costs or make additional investments in distressed debtors even if it could lead to the likelihood of higher recoveries. When a debtor's financial prospects deteriorate, with the possibility of default, regulators require bank lenders to make reserves for the likelihood of default. Such provisioning by a bank means that it has more capital tied up in a debt for which repayment is uncertain. While the imposed regulatory adjustments may better facilitate prudence, for bankers, these adjustments do not make economic sense for bank profitability. In such situations, it makes even less economic sense for banks to provide additional financing to distressed debtors.

Private credit funds, which do not have the same regulatory pressures and capital charges faced by banks, have the unique opportunity to add value to a restructuring. When providing new money to a distressed business (whether in the form of DIP financing during a formal restructuring, as discussed above, or funding the exit from court proceedings), direct lenders will have immense latitude to monitor the progress of the business and exert pressure on management to make certain decisions to drive value. Direct lenders can also orchestrate a change in management especially where the company failure was attributable to poor leadership or the lack of entrepreneurial creativity on the part of the extant management team. Through its activism, direct lenders are able to unlock value which had been previously unharnessed or ignored by the distressed business. This is beneficial to the debtor, other stakeholders, and the economy as a whole: the direct lender serves as a source of liquidity that can revitalize the struggling business, channel funds towards healthier undertakings, and preserve if not increase jobs.

Direct lenders will take direct steps to improve prospects of the businesses in which they invest. They are incentivized to seek the highest possible returns on the investments made in distressed situations. It makes sense for distressed firms to have their debt in the hands of creditors whose interests align with the interests of the firm as a whole. The process of financial restructuring often goes hand in hand with a business restructuring. Direct lending managers encourage the distressed debtor to look more closely at its business model, and to make the necessary operational changes and determine the most appropriate combination of assets that will allow the firm to succeed going forward. Banks rarely possess the expertise to profit from distress. Private credit funds, however, can support, for instance, a distressed debtor's plan to divest non-core assets in favor of focusing financial and managerial resources on the core business, even if that might lead to higher fixed costs in the short-term. Direct lenders have been shown to not only cooperate with other stakeholders but are motivated, through their own self-interest and profit-maximizing objectives, to support the revitalization of a debtor in restructuring.

Of course, any rescue efforts must depend on the possibility that the distressed firm is viable. Making this determination is not always an easy call but sophisticated and experienced private credit managers are better placed to determine which firms are viable and worthy of a rescue endeavor than their bank peers. Direct lending managers not only provide financing to the distressed business, but also provide the intelligence to guide the restructuring in a way that increases returns to their investors and other stakeholders of the company. Private credit funds play a critical role in ensuring managerial accountability and efficiency in the conduct of a distressed business.

Given the interests of the private credit fund in the business, there is an increased likelihood that the intervention of such investors can prevent a liquidation of the distressed debtor. For some lenders, absent any legal basis for constraining their desire to quickly liquidate the borrower, that option is the first recourse, taking advantage of the financial pressures of the debtors, to extract value for themselves. This was the case in one contentious formal restructuring in which the author's firm was involved whereby another secured lender vehemently opposed a restructuring plan, instead preferring a speedier liquidation of the debtor's assets. The author's firm sought the cooperation of several other stakeholders, including local government and labour unions, to drive negotiations in the direction of a successful restructuring of the business, providing initial new financing, and preserving thousands of jobs and taxes for the community as a result.

The reputation of non-bank direct lenders in the restructuring of companies has been that of a "vulture", which has been coloured by the emotions of losing management teams and sensationalized by the media. In the current crisis environment, direct lending managers are increasingly present at the negotiating table in formal restructurings. Empirical evidence shows that participation of such investors in a formal restructuring help distressed companies successfully emerge as going concerns[3]. In that respect, private credit firms are the "phoenix" for the reorganization process contributing, among other things, substantial resources in the form of capital, business and financial acumen, and expertise.

Conclusion

The global pandemic has exposed weaknesses in credit underwriting, loan documentation and collateral management. The pandemic should have wiped out some companies and unmasked warts on troubled businesses, but bank forbearance and formidable government stimulus successfully bridged cash flow gaps and staved off a widespread massive credit default crisis. The actual creditworthiness of leveraged borrowers today is very likely overstated. The number of heavily indebted companies in the U.S. that cannot cover their debts with operating income and thus continuously rely on low interest rates and more capital to survive, has now grown to ~20%, according to Axios Research[4]. These so-called "zombie companies" have been able to postpone an inevitable restructuring. However, when the indiscriminate fiscal and monetary support comes to an end, the winds of creative destruction will be allowed to blow again, and there will be unprecedent opportunities for private credit funds to bring life back to those zombie companies that can be restructured.

3 Wei Jiang et al., Hedge Funds and Chapter 11, 67 J. FIN. 513, 513 (2012)
4 **https://www.axios.com/zombie-companies-us-e2c8be18-6786-484e-8fbe-4b56cf3800ac.html**

Conclusion

SMEs and mid-market businesses will always be central to the success of the UK economy. This ‘Borrowers Guide to Private Credit’ provides these vital businesses with an introduction to the financing alternatives that are available to them. This will support their ability to invest, grow and support job creation.

This guide has demonstrated how private credit managers are well-established providers of finance that are ideally suited to supporting UK Businesses, and provided SMEs with insight into what to expect when partnering with them.

It is our hope that this guide will support the expansion of private credit in the UK and its role supporting growth and innovation by UK businesses.

To learn more, visit **lendingforgrowth.org** or **canada.aima.org** for investor education resources, thought leadership content and annual research.

How to get in touch with a private credit lender

Canada is home to a variety of private credit lenders catering to different business sectors and sizes.

CLICK HERE

to contact the private credit firm of your choice to discuss next steps today.

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Third Eye Capital

Appendix

Glossary of Terms	
Arrangement fee	An arranger is typically a bank or other financial institution responsible for originating a syndicated loan. The small fee charged to the borrower is the arrangement fee.
Baskets	**Baskets** refers to negotiated exceptions to the loan agreement's prohibition on restricted payments. Baskets are either capped or scalable (allowing it to fluctuate with EBITDA).[iii]
	General restricted payment basket: In its simplest form, a restricted payments covenant in a loan agreement limits the borrower's ability to make payments such as dividends, distributions, equity redemptions and repurchases to its equity holders. The provision ensures that equity holders are not paid before the loans are repaid, apart from limited exceptions. Other types of payments to parties that are not equity holders may also be covered in a restricted payments provision, such as payments to holders of the borrower's subordinated debt.
	Ratio debt basket: A ratio debt basket typically allows the borrower to incur debt secured on a senior secured basis subject to a maximum senior secured leverage ratio, and unsecured debt subject to a maximum total leverage ratio.
	Available amount starter baskets: In a building basket (or ratio-based basket), a "starter amount" is sometimes made available which permits the borrower to make restricted payments up to a fixed dollar amount even before the basket has begun to build (or without meeting the financial ratio test).

Glossary of Terms

Borrower	Borrower in the context of a loan agreement should encompass all group companies which require access to the loan. This should include any target companies which the borrower may intend to acquire with the funds provided.
Certain funds period	Certain funds provisions are required when the loan proceeds may be used to fund an acquisition governed by the City Code on Takeovers and Mergers. The provision obliges funding to be provided to the borrower in order to complete the cash payment of an acquisition within a specified amount of time. The certain funds period is typically set at four to six months from the signing of a loan agreement.[iv]
Clean down	A clean down is a provision applicable to a working capital or overdraft facility to ensure that the borrower is not using that facility as long-term debt. Such a clause will specify that the working capital or overdraft facility must be undrawn for a specified number of consecutive days in each of the borrower's financial years or other specified period.[v]
Closing leverage	Closing leverage describes the ratio of funded debt as of the closing date to closing date EBITDA.
Commitment / ticking fees	A commitment fee refers to the fee charged by a lender to a borrower as compensation for its commitment to lend, since the lender has set aside the corresponding funds for the borrower but is not yet earning interest. Thus, such fees typically are associated with unused credit lines or undisbursed loans.
Cross default threshold	Cross default thresholds are in place to mitigate risks associated with lending money to businesses who have also borrowed from other lenders. A default in the payment of other loans of the borrower or of any member of the borrower group would also trigger a default under the second loan agreement containing a cross default threshold provision.
Default	A loan agreement will contain a standard provision to cover the conditions under which a borrower is considered to be in default, or potential default.
Delayed draw term loan	Delayed draw term loans (DDTLs) refers to bespoke arrangements allowing borrowers to request additional funds after the initial loan term period has already ended. This extended draw period is typically offered to borrowers with good credit ratings.

Glossary of Terms

Equity cure / EBITDA cures	Providing 'cures' refers to private equity sponsors injecting additional funds into a borrower in which it owns equity, in order to enable the business to meet its financial covenant test when it otherwise would not have. As cures should not be used to mask an underlying problem with the borrower's business but rather to address a short-term performance dip, loan agreements typically contain limitations on the cure right. The most common limitation on cure rights is a hard cap on both the total number of times a cure right can be exercised during the life of the loan, and the maximum permitted frequency of such cure.
Excess cash flow sweeps	A cash sweep obliges the borrower to use excess free cash flows to settle outstanding debts to lenders. Therefore, the excess cash cannot be distributed to shareholders.
Governing law	The governing law is the law of the jurisdiction in which the loan will be agreed. Typically, the lender's resident jurisdiction is selected.
Incremental facilities 'Accordion' feature	Under incremental facilities, borrowers can request for an existing loan to be increased, or that a new loan be provided under its existing loan agreement at any point in the future. This increased loan will still rely on existing collateral. **Free and clear basket**: This sets out the amount of incremental facility loans that a borrower may draw upon without having to demonstrate renewed compliance with a financial ratio test. It will either be 'hard capped' at a set amount, or can be 'soft capped' as a percentage of EBITDA. **Ratio test**: This allows the borrower to utilise incremental facilities in excess of the free and clear basket, provided that the borrower's leverage ratio or other financial ration remains below a fixed level. **"No worse off"** concept has often been included, which enables the borrower to incur the additional debt so long as its leverage ratio would not increase as a result (irrespective of how high its resulting leverage ratio is in absolute terms).[vi]
London Interbank Offered Rate (LIBOR)	LIBOR, which stands for London Interbank Offered Rate, serves as a globally accepted key benchmark interest rate that indicates borrowing costs between banks. Most interest rates in loan contracts have been set on the basis of LIBOR. LIBOR is currently being phased out by macroprudential regulators and replaced by alternative benchmarks such as SONIA and SOFR (see below).
Margin	The margin refers to the additional percentage rate of interest charged by lenders over the relevant basis rate. This typically reflects the credit quality of the borrower and will be adjusted to the relative risk inherent to the loan provided.

Glossary of Terms

Material adverse effect	Material adverse effect is used to define the seriousness of an event which may determine when the lender will request a borrower to remedy a breach of the agreement or take action on a default. Typically, this encompasses any event or change in circumstance that would significantly affect the assets, liabilities or cash flow of the borrower in a negative manner.
Most favoured nation	If an incremental facility provision is included in a loan agreement, a 'most-favoured-nation' clause (MFN) will often be found. The primary purpose of an MFN is to protect the value of the initial debt in the secondary market. By allowing the borrower to incur additional pari passu debt under the same loan agreement, the lenders run the risk that the terms of that additional debt are less favourable than the original, which will make the existing loans harder to sell on the secondary market. The solution for the lender is to allow incremental facilities to be put in place but only if certain key terms of the incremental facility fall within set parameters. This will prevent the incremental facility from being significantly more attractive to lenders than the existing facilities. Such parameters may include: The **yield** payable on the incremental facility cannot be more than the yield on the existing facility by more than a certain buffer amount. The **maturity date** for the incremental facility cannot be earlier than a specified date. There can be **no amortisation** of the incremental facility (or, if there is amortisation of the existing facilities, the weighted average life to maturity of the incremental facility must not be shorter than the existing facility). It is now increasingly common for any MFN provisions to include a sunset period of 6 to 24 months following which such pricing limitations will cease to apply.[vii]
Mitigation	Mitigation refers to a provision which obliges the lender to take into account and mitigate the effect of any circumstances giving rise to increased costs.
Origination fee	An origination fee refers to the initial fee charged by a lender for processing a new loan application, as compensation for putting the loan in place.
Pari passu	Pari passu is a Latin term that means 'on equal footing' or 'ranking equally'. If a business's debts are pari passu, they are all ranked equally, so the borrower would pay each lender the same amount in insolvency.

Glossary of Terms

Participation fee / Front end fee	Participation fees or front end fees refer to fees paid to the lender upon signing the loan agreement, at the beginning of the loan transaction.
Payment	The price of a loan is comprised of the interest rate margin which will be set out in the private credit offer letter and term sheet, and is calculated on the basis of the relative riskiness of the loan. There are several options for the method of repayment: **Specific periodic amounts:** The borrower will make a specified payment to the lender at regular intervals. **Bullet loan / Lump sum payment:** The borrower pays nothing to the lender until the end of the note term, at which time the borrower repays the entire note in one payment. **Interest only:** The borrower makes regular payments to the lender that are put towards paying off the interest on the principal amount only, with no portion of the payment going towards the principal amount itself. **Interest and principal:** The borrower makes regular payments to the lender that are put towards paying off both the principal amount and the interest as it is compounded. At the end of the term of the loan agreement, there will be no outstanding balance to be repaid. **Payment in Kind (PIK):** A credit arrangement whereby interest is not paid on borrowings in cash between the funding date and maturity of the debt product, but instead is added to the principal balance of the loan. **Voluntary prepayment** means a prepayment of principal to the extent that such prepayment reduces the scheduled instalments. Voluntary prepayment is only possible if stipulated in the loan agreement.
Permitteds	Loan agreements typically seek to accommodate the need for operational flexibility by allowing for certain categories of “leakage” to be permitted. Thus, a loan agreement usually contains a specified list of permitted exceptions from the covenants that prohibits the borrower from making restricted payments. These Permitteds typically fall within three broad categories: Market-standard and universally accepted as being necessary in order for any business to operate effectively; Business-specific and are accepted by the lenders on the basis that they are justifiable leakages; or Broad general baskets (see Baskets) for leakages not falling within a specific permitted under the first two categories but with which lenders are comfortable.[viii]

Glossary of Terms	
Portability	A portable loan is debt for which a change in control of the business would not trigger the early repayment of the debt.
Pro forma	Pro forma, a Latin term meaning 'as a matter of form', refers to the process of presenting financial projections for a specific time period in a standardised format to allow for comparison and analysis.
Revolving credit facility margin	A revolving loan is a flexible financing tool allowing for repayment and re-borrowing of the funds. A revolving credit facility margin provides the borrower with the ability to withdraw funds, repay, and withdraw again.
Secured Overnight Financing Rate (SOFR)	The secured overnight financing rate, or SOFR, is an interest rate that banks use to price U.S. dollar-denominated derivatives and loans. The daily SOFR is based on transactions in the Treasury repurchase market, where investors offer banks overnight loans backed by their bond assets. SOFR has been published since April 2018 as part of the process to replace LIBOR.
Step downs on margin ratchet	The margin ratchet is a mechanism whereby the initial margin interest rate a lender charges can be reduced if the borrower achieves a better financial position. If that financial position subsequently worsens, the margin will return to its original level.[ix]
Sterling Overnight Indexed Average (SONIA)	The Sterling Overnight Indexed Average (SONIA) measures the rate paid by banks on overnight funds. It is calculated as a trimmed mean of rates paid on overnight unsecured wholesale funds.
Unrestricted and restricted subsidiaries	A typical covenant package will limit a corporate group from taking certain actions by applying restrictions to a borrower and its 'restricted subsidiaries'. By default, all subsidiaries of the borrower will be part of the restricted group unless they are specifically designated as 'unrestricted'. The purpose of these provisions is to avoid a 'leakage' of collateral, meaning the transfer of the assets of a business to a subsidiary which is not included in the initial loan agreement.

Endnotes

i CPP Investments. 2021. **Annual Report**.
ii United Nations Principles for Responsible Investment. 2021. **Responsible investment DDQ for private credit investors**.
iii. UK Practical Law. 2021. **Glossary Basket.**
iv. Linklaters. 2021. **Certain Funds.**
v. UK Practical Law. 2021. **Glossary Clean-down clause.**
vi. Clearly Gottlieb. 2021. **Market Wrap - Loan Transferability**.
vii. ibid.
viii. Osborne Clarke. 2021. **'Grower baskets': untangling the weeds**.
ix. UK Practical Law. 2021. **Margin Ratchets.**

Sample Term Sheet - First Lien Loan

DATE

COMPANY

Attention: NAME(S) and TITLE(S)

COMPANY NAME (hereinafter referred to as the “**Company**” and “**you**”) have requested that **LENDER NAME** (hereinafter referred to as “**LENDER**”, “**us**” and “**we**”) express our level of interest in providing financing for the repayment of existing debt, and to provide working capital for the operations of the Company. We have reviewed the information presented to us to date and are willing to suggest the following financial structure.

The purpose of this letter is to advise you of the basic terms and conditions which we envision, and will require, should you wish to pursue the subject financing. This letter should only be used as reference for discussion. This is NOT a Commitment Letter.

Borrowers:	COMPANY (or JOINT AND SEVERAL BORROWERS)
Corporate Guarantors:	XXXXX
Personal Guarantors:	NAME OF PERSON(S) (IF APPLICABLE)
Key Person’s Life:	IF APPLICABLE (AND NAME OF PERSON(S))
Primary Facility:	$XXXX Senior Secured Revolving Line of Credit
Secondary Facility:	$XXXX Senior Secured Term Loan Credit Facility / Accordion (if applicable)
Purpose:	To repay certain existing secured debt, and to provide additional working capital for day-to-day operations + OTHER AS REQUIRED (IE: REPAYMENT OF SHAREHOLDER LOANS / ACQUISITION etc.)
Term:	# of Months, plus an option to renew for up to # of additional months, as mutually agreed.
Interest Rate:	[%.] annual rate, payable monthly
Closing Fee:	[%] of Total Credit Facility or $XXXX
Monitoring Fee:	[$.] per month payable in advance (dependent on complexity)
Early Termination Fee:	A Make Whole Fee equal to [%.] (or [%.] for US$) per annum on the current out standing facility for the balance of the term of the loan.
Unused Line Fee:	[%]per annum, calculated daily and payable monthly, on the unused portion of the Facility.
Advance Rate:	Up to [%.] of Eligible Investment Grade Accounts Receivable of the Company, as suming that Dilution is not greater than 5%. Up to [%.] of Eligible Non-Investment Grade Accounts Receivable of the Company, assuming that Dilution is not greater than 5%. Up to [%]of the Net Orderly Liquidation Value (“NOLV”) of Eligible Inventory of the Company, valued by an Appraiser acceptable to the Lender, and expressed as a function of Cost.

	Up to [%.] of Net Orderly Liquidation Value ("NOLV") of Eligible Machinery & Equip ment **OR Up to [%] of the NET / FORCED LIQUIDATION VALUE ("NFLV" or "FLV")** of the Company, valued by an Accredited Appraiser acceptable to the Lender. Up to [%.] of the unencumbered Fair Market Value ("FMV") of Eligible Commercial Property held by the Company, valued by an Accredited AACI Appraiser acceptable to the Lender.
Monitoring:	Springing Lock Box with Blocked Account Agreement. Monthly Collateral reporting submitted by EOB Day 5. Monthly financial reporting submitted by EOB Day 15. Monthly Compliance Certificate by EOB Day 15. **OTHER MONITORING AS PER STRUCTURE**
Priority Reserves:	Will be reserved from the eligible margined collateral.

Conditions of Closing:

All obligations of the Company and any guarantees will be secured by a first security interest and lien upon all present and future assets of the Company and any corporate guarantors, including all accounts, contract rights, general intangibles, chattel paper, Blocked Account Agreement, documents, instruments, deposit accounts, inventory, equipment, and real property, trademarks and patents and all products and proceeds thereof.

Insurances will be assigned to the Lender, as required and discussed in further detail below in Other Items and Conditions (item g).

The Company agrees to pay all reasonable legal and closing expenses, including filing and search fees, appraisal fees, field examinations, and all other due diligence expenses incurred by LENDER, whether or not this transaction closes. All such expenses shall be paid as advances on account. This section shall survive the expiration or termination of this letter.

Subsequent to the completion of this transaction, the Company further agrees to pay for all out-of-pocket expenses and administration charges incurred from time to time during the course of our financing arrangements, including without limitation expenses for recurring field examinations, and appraisals.

Deposits:

As evidence of our mutual good faith and in consideration of our having incurred and continuing to incur certain expenses in the expectation of establishing the financing arrangements between us and the Company, we request that the Company make an initial deposit to LENDER in the amount of [$.   ] against our field examination, financial analysis and due diligence, and appraisal expenses.

After these are completed, and if the findings are acceptable and the decision is made by LENDER to proceed to legal's, a further deposit of **$XXXX** will be required to apply against legal and closing expenses.

These deposits will be:

a) Returned to the Company less the cost of our field examinations, financial analysis and appraisals, legal fees and other expenses directly related to the loan application and credit review, if our credit review of the proposed facility is not positive;

b) Retained by us and credited to the loan account of the Company, less the expenses described in paragraph (a) above, if the loan is approved and funded;

c) Retained by us as a fee in addition to expenses payable by the Company as set forth above, if our credit approval of the proposed financing is approved but the transaction does not close within 30 days from the date of such approval, whether as the result of your election not to do business with LENDER or a failure to fulfill any of the conditions of the proposed financing as approved by us; and

d) Retained by us as a fee in addition to expenses payable by the Company as set forth above if at any time during the loan and credit review the Company intentionally misleads us or intentionally fails to disclose material information which, if disclosed, would have had a material impact on the loan approval.

Other Information and Conditions:

This proposal does NOT represent a commitment to lend. Our proposal is expressly subject to a review of certain other information, satisfactory completion of our field examinations, credit investigations and management background checks. Once approval is given, it will be contingent upon a closing taking place on or before **DATE (PER ESTIMATED CLOSING)**, provided we mutually agree to take all reasonable actions to expedite the closing of the transaction as counsel for each party may advise.

The closing of the credit facility will be subject to the satisfaction, in a manner acceptable to us, of the following:

a) The Company continuing to furnish Lender with all financial information, projections, budgets, business plans, cash flows and such other information as we reasonably request from time to time. We shall have received current agings of receivables, current perpetual inventory records and/or roll forwards of account receivables and inventory through the date of closing, current listing of machinery and equipment (if applicable) with supporting documentation, and other documents and information that will enable us to accurately identify and verify the eligible collateral at or before closing in a manner satisfactory to us. Lender may require weekly reporting of collateral information from the Company.

b) Satisfactory legal review of the terms of the credit facility and its structure by our counsel and execution and delivery of loan documents, all in a form and substance satisfactory to us. The loan documents will include, among other documents, a Loan Agreement, Security Agreements, PPSA financing statements, and opinion from counsel. Such loan documents will contain provisions, representations, warranties, conditions, covenants and events of default satisfactory to us and our counsel.

c) The Company will be required to maintain Earnings Before Interest, Taxes, and Depreciation & Amortization (“EBITDA”) at a level to be mutually agreed upon, calculated on a rolling twelve-month basis for the duration of the loan and any additional extensions.

d) The Company will be required to maintain a Tangible Net Worth in an amount to be mutually agreed upon. No distributions, other than normal management fees, salaries, wages and dividends that are fully set out in projections and do not put the Company in default, will be allowed without our prior consent.

e) No material adverse change in the business, operations, profits or prospects of the Company or in the condition of the assets of the Company shall have occurred since the date of the last field examination.

f) We shall require landlord waivers upon all Company facilities where applicable. Such waivers shall be under term and conditions satisfactory to the Lender. In the event a waiver is not obtained, a reserve in the minimum amount of three months’ rent will be taken against the collateral pool.

g) We shall require the Company to maintain adequate insurance and agree that all funds received from the insurance pursuant to a major claim will be immediately paid to LENDER who will be named in the policy as first loss payee on all the assets of the Company, as well as on the personal property that has been pledged a part of this structure.

h) At all times the funds advanced to the Company must be less than the margined collateral pool (less prior charges) securing the advances. For clarity, the margined collateral pool is represented by Eligible Accounts Receivables, and Eligible Inventory at the advance rates stated above.

i) ADDITIONAL CONDITIONS / COVENANTS AS PER STRUCTURE (IE: OTHER MONITORING ETC.)

The Terms and Conditions described in this Proposal Letter are intended as an outline only and this Proposal Letter does NOT purport to include or summarize all of the terms, conditions, covenants and other provisions which will be contained in the loan documents.

The Lender and or its Agent may use the names, logos and other insignia of the Company in any "tombstone" or comparable advertising on its website or in other marketing materials.

Unless accepted by the Company and as accepted, received by Lender by the close of business on **DATE (TYPICALLY ONE (1) WEEK FROM ISSUANCE)** with the deposit referred to above, this Proposal shall expire at that time.

This Proposal is solely for your benefit and is not to be relied on by any third party.

We look forward to working with you on this transaction.

Yours truly,

LENDER

____

NAME OF LENDER SENIOR OFFICER

COMPANY NAME HERE

We acknowledge and agree to all the terms and conditions as of this _____ day of ____________, 2020.

____

ADDRESSEE / PROSPECTIVE CLIENT'S SENIOR OFFICER NAME

Sample Term Sheet - Second Lien Loan

PROPOSAL LETTER

[Date]

[Borrower Name]

[Address]

Dear ________

You have provided us with certain information and have discussed with us the current and future needs for financing of [ ] and its divisions or subsidiaries (the "Borrower").

In connection therewith, [ ] (the "Lender") is pleased to confirm its interest in providing up to [$] of Second Lien Term Loan (the "Financing") to the Borrower to replace existing debt and for future working capital purposes (the "Transaction"), on general terms and conditions outlined in the attached Summary of Proposed Terms. Except as otherwise indicated, all references herein to "$" and "dollars" shall be Canadian dollars.

Please understand that this Proposal Letter indicates interest and does not constitute a commitment or undertaking to provide financing. This proposal is subject to review of certain other information, satisfactory completion of our, credit investigations, analysis, and approval by Lender's credit committee.

So that we may begin our legal and business due diligence, please sign and return this letter, along with a good faith deposit of [$] (the "Good Faith Deposit"), on or before [Date]. Lender will charge the Good Faith Deposit for fees and expenses to be reimbursed. If Lender should approve and close the financing within [.] days of approval, Borrower's remaining Good Faith Deposit (net of fees and expenses) would be applied towards fees due at closing. If Lender should not approve the transaction substantially on these terms or otherwise acceptable to you (for any reason other than your acceptance of financing from another lender or your termination of Lender's efforts hereunder), then the balance of the Good Faith Deposit (net of fees and expenses) shall be returned. In all other circumstances, Lender will retain the remaining Good Faith Deposit.

We sincerely look forward to working with you and your colleagues to close the proposed transaction.

Sincerely,

[LENDER]

By:________________________ Its:________________________

AGREED AND ACCEPTED THIS ________ DAY OF _____________, [DATE]

[BORROWER]

By: ___________________ Its: ___________________

SUMMARY OF PROPOSED TERMS

$MM Second Lien Term Loan for

[Borrower]

[Date]

Borrower:	[ ] the ("Company")
Lender:	[ ] the "Lender"
Guarantors:	Material subsidiaries, as applicable.
Amount:	[$] million
Facility:	Senior Secured Term Debt ("2nd Lien")
Purpose:	For general working capital purposes
Interest Rate:	[%] per annum fixed, payable monthly in arrears
Default Rate:	[%] in excess of the applicable rate
Maturity:	[ ] ( ) years from the date of closing
Availability:	The entire amount of the Facility will be available for drawdown at closing subject to compliance with the conditions precedent as stated herein.
Repayment:	No principal payments for the first [ ](.) months after closing. Thereafter, monthly principal payments of [$.] for following [ ] ( ) months.
Prepayment:	Prepayment in whole or in part is permitted, at any time, in minimum amount of [$] but will be subject to a prepayment fee of [%] of the amount prepaid during the first [.] ( ) months after closing and a [%.] prepayment fee during the third year of closing. No prepayment penalty will be applicable after [.] (.) months after closing.
Mandatory Prepayment:	No mandatory prepayments required so long as senior lender requires such mandatory pre payments apply first to senior debt.
Warrants:	At the closing of the transaction, the Lender will receive detachable and freely transferable warrants which provide an equivalent equity value in the Company (the "Warrants") to acquire [%] of the fully diluted stock or value in the Company at closing. The Warrants will have a nominal exercise price, anti-dilution protection, r egistration rights, exercise mechanisms and put/call provisions to be agreed upon.
Observer Rights:	Lender will be allowed to send two observers to all regular and special meetings of the Board of Directors of the Company.
Closing Fees:	A Closing Fees of [%]of the Amount is to be paid to the Lender upon closing of the transaction.
Expenses:	All out of pocket costs and expenses incurred by the Lender including, without limitation, travel expenses and fees and disbursements of legal counsel and other advisors, will be for the account of the Borrower whether or not the transaction contemplated herein is completed. Borrower hereby grants a security interest to Lender in respect of all such amounts Borrower may be owing.

Security: Fully perfected charge over all assets of the Borrower, second only to senior lender and customary permitted liensincluding (i) pledge of shares of borrower, subject only to the senior lender; (ii) assignment of adequate all risk insurance with the Lender specified as named insured and loss payee subject only to the first interest of the senior lender; and (iii) any other security Lender or its legal counsel may reasonably require; (iv) any and all covenants, waivers, estoppels, acknowledgments

Financial and Other Covenants: Standard covenants are to apply including, without limitation, the following (these covenants are subject to further due diligence and may be amended):

1. Unencumbered inventory value reported to senior lender less borrowings from senior lender not less than [$.   ] million at all times, measured monthly.
2. Limitations on indebtedness, material changes, change of control, liens, restricted payments and investments, asset sales, capital expenditures, changes in nature of business, share issuance, granting of guarantees, mergers, acquisitions, dividends, and others which are customary for transactions of this nature;
3. Minimum Fixed Charge Coverage Ratio (EBITDA divided by the aggregate of interest expense, scheduled repayments of indebtedness, cash taxes, and unfunded capital expenditures) shall not be less than [TBD] measured on a rolling four-quarter basis;
4. Funded Debt (all interest bearing debt including the 2nd Lien debt) to EBITDA (defined as earnings before interest, taxes, depreciation and amortization and before extraordinary items including any gains or losses on disposition of assets) ratio to be measured on a rolling four quarter basis, of not greater than [TBD];
5. Limitation of Capital Expenditures;
6. Payments of dividends, withdrawals of shareholders' advances or any other withdrawals of capital or material changes in management compensation are not permitted without the prior written consent of the Lender;
7. Priority payables to remain current at all times;
8. Customary reps & warranties for transaction of this nature

Reporting Requirements: Borrower will furnish the following reports, including, but not limited to:

1. Audited financial statements on an annual basis and unaudited financial statements on a monthly basis, within 90 and 30 days respectively after the end of the respective fiscal period, both to be accompanied by borrowing base certificate provided to the senior lender, chain wide inventory report, payment schedule of all priority payables with supporting documents, compliance certificates respecting reps and warranties, covenants and events of default;
2. Detailed annual financial projections with supporting assumptions ("Business Plan") to the Lender 30 days prior to the end of the fiscal year;
3. Annual inventory appraisal report completed by an appraiser acceptable to Lender;
4. Any other information on a timely basis as may be reasonably requested by the Lender.

Conditions Precedent:	Standard conditions to closing will include, without limitation, the following: 1. Review of three years financial projections of the Borrower including supporting assumptions; 2. Review of final sources and uses statement for this transaction and pro-forma opening consolidated balance sheet of the Borrower; 3. Inspection of stores and operations and discussions with senior management; 4. Review of all material contracts including, without limitation employment contracts with key members of management; 5. Satisfactory insurance coverage; 6. Satisfaction with the terms and conditions of the senior debt and other indebtedness; 7. No material adverse change in respect of the business, results of operation, condition (financial or otherwise), value, prospects, liabilities, or assets of the Company; 8. Satisfactory legal documentation, including inter-creditor agreement with senior lender, as applicable, which shall not contemplate any payment block prior to a default and standstill for more than 90 day period, provided no insolvency event or enforcement by senior lender 9. No event of default shall be in existence; 10. Usual and customary representations and warranties for transaction of this nature, all satisfactory to Lender; 11. Owners of the Company will enter into customary non-compete and non-solicitation agreements.
Events of Default:	The usual and customary events of default are to apply determined by the Lender and its legal counsel, including cross default to senior debt and material agreements.
Assignment:	The Lender reserves the right to syndicate, participate, sell or assign a portion or all of the Facility.
Governing Law:	Province of Ontario
Publicity:	The Lender shall be entitled following closing to publicize its involvement in providing the Facility to the Borrower by way of “tombstone” advertising or otherwise and report such involvement in banking and investment surveys and reports without the prior written consent of the Borrower.
Confidentiality:	This proposal is delivered to you on the understanding that the Borrower and Lender agree that it is to be kept confidential. the Borrower shall not make any disclosure of this proposal or the terms hereof to any third party, other than their legal counsel or other professional advisors, without the prior written consent of the Lender, except as required by applicable law.
Break Fee:	In the event the Borrower accepts a committed offer to finance from the Lender and fails to complete the drawdown of funds for any reason, a break fee of [$.] shall be paid to the Lender.
Indemnity:	You agree that you will, except in the case of gross negligence or willful misconduct, indemnify and hold harmless the Lender and its directors, officers, employees, consultants, agents and attorneys from and against any and all claims, damages, liabilities and expenses (including, without limitation, fees and disbursements of Lender’s counsel) incurred by or asserted against the foregoing in connection with or arising out of any investigation, litigation or proceeding related to this transaction.

ACC and AIMA Canada members

ABERDEEN STANDARD INVESTMENTS (CANADA) LIMITED

ACCELERATE FINANCIAL TECHNOLOGIES INC

AGF INVESTMENTS INC.

ALBERTA INVESTMENT MANAGEMENT CORP

ALBERTA TEACHERS' RETIREMENT FUND

ALBOURNE PARTNERS (CANADA) LIMITED

ALGONQUIN CAPITAL CORPORATION

ALLIANZ GLOBAL INVESTORS (CANADA)

APEX FUND SERVICES (CANADA) LTD.

ARROW CAPITAL MANAGEMENT

AUSPICE CAPITAL ADVISORS LTD.

AVANTFAIRE CANADA LTD.

AVENUE LIVING ASSET MANAGEMENT

AYAL CAPITAL ADVISORS LTD.

BAKER MCKENZIE

BANK OF AMERICA MERRILL LYNCH

BLACKROCK ASSET MANAGEMENT CANADA LIMITED

BLAKE, CASSELS & GRAYDON LLP

BLOOM BURTON INVESTMENT GROUP INC.

BMO NESBITT BURNS INC.

BORDEN LADNER GERVAIS LLP

BRK CAPITAL

BROADRIDGE FINANCIAL SOLUTIONS, INC.

BT GLOBAL GROWTH INC.

CACHET CAPITAL INC.

CAISSE DE DEPOT ET PLACEMENT DU QUEBEC

CENTURION ASSET MANAGEMENT INC.

CI INVESTMENTS

CIBC CAPITAL MARKETS

CIBC MELLON GLOBAL SECURITIES SERVICES COMPANY

CIBC WOOD GUNDY

CITCO (CANADA) INC

CONVERIUM CAPITAL INC.

CORNERSTONE GROUP

CORTLAND CREDIT GROUP INC.

CREDIT SUISSE ASSET MANAGEMENT CANADA

CREDIT SUISSE PRIME SERVICES

DAVIES WARD PHILLIPS & VINEBERG LLP

DELPHIA ASSET MANAGEMENT INC.

DESJARDINS INVESTMENTS INC.

DYNAMIC FUNDS

EDGEPOINT INVESTMENT GROUP

EHP FUNDS

ENTERPRISE CASTLE HALL ALTERNATIVES INC.

ESPRESSO CAPITAL LTD.

EVOVEST

EY - CANADA

EZE SOFTWARE CANADA INC.

FORGE FIRST ASSET MANAGEMENT INC.

FORMULA GROWTH LIMITED

FUNDATA CANADA INC.

GAPINSKI CAPITAL MANAGEMENT LLC

GOLDMAN SACHS CANADA INC.

GROUNDLAYER CAPITAL INC.

HARMONIC FUND SERVICES CANADA INC.

HAZELVIEW INVESTMENTS INC.

HEALTHCARE OF ONTARIO PENSION PLAN

HGC INVESTMENT MANAGEMENT INC.

HIGHSTREET ASSET MANAGEMENT INC.

HILLSDALE INVESTMENT MANAGEMENT INC.

HORIZONS ETFS MANAGEMENT (CANADA) INC.

ICM ASSET MANAGEMENT INC.

IHS MARKIT

INDEPENDENT REVIEW INC.

INNOCAP INVESTMENT MANAGEMENT

INTERNATIONAL FUND SERVICES

INTERTRUST GROUP

INVESTMENT MANAGEMENT COMPANY OF ONTARIO

INVESTMENT PARTNERS FUND INC.

JM FUND MANAGEMENT INC.

JODDES LIMITED

KPMG LLP

LAWRENCE PARK ASSET MANAGEMENT LTD.

LEITH WHEELER INVESTMENT COUNSEL LTD.

LIONGUARD CAPITAL MANAGEMENT INC.

LYNWOOD CAPITAL MANAGEMENT INC.

LYSANDER FUNDS LIMITED

MACKENZIE FINANCIAL CORPORATION

MAPLES FUND SERVICES (CANADA) INC.

MARRET ASSET MANAGEMENT INC.

MCMILLAN LLP

MONTRUSCO BOLTON INVESTMENTS INC.

MUFG FUND SERVICES (CANADA) LIMITED

NATIONAL BANK FINANCIAL INC.

NATIONAL BANK INDEPENDENT NETWORK

NEUBERGER BERMAN

NEXT EDGE CAPITAL CORP.

NINEPOINT PARTNERS LP

NOAH CANADA WEALTH MANAGEMENT LIMITED

OGAM LTD.

OMERS ADMINISTRATION CORPORATION

ONTARIO TEACHERS' PENSION PLAN

OPTRUST - OPSEU PENSION PLAN TRUST FUND

PENDERFUND CAPITAL MANAGEMENT LTD.

PERISCOPE CAPITAL INC.

PH&N INVESTMENT MANAGEMENT

POLAR ASSET MANAGEMENT PARTNERS INC.

PWC- TORONTO

PRIME QUADRANT

PSP INVESTMENTS

Q CAPITAL MANAGEMENT LTD.

RBC GLOBAL ASSET MANAGEMENT

RBC GROUP RISK MANAGEMENT (GRM) WHOLESALE CREDIT RISK

RESOLVE ASSET MANAGEMENT

RICHARDSON WEALTH

RP INVESTMENT ADVISORS

RSM CANADA

SCOTIA GLOBAL ASSET MANAGEMENT

SCOTIA GLOBAL BANKING & MARKETS

SGGG FUND SERVICES INC.

SHORELINE WEST ASSET MANAGEMENT INC.

SKYLINE WEALTH MANAGEMENT INC.

SOCIETE GENERALE CAPITAL CANADA INC.

SS&C TECHNOLOGIES

STATE STREET

STIKEMAN ELLIOTT LLP

SUMMERWOOD CAPITAL CORP.

TACTEX ASSET MANAGEMENT INC.

TD SECURITIES

TD WEALTH

THE AUDRA GROUP

THE CANADIAN MEDICAL PROTECTIVE ASSOCIATION

THIRD EYE CAPITAL

TORONTO TRANSIT COMMISSION PENSION PLAN

TRANS-CANADA CAPITAL INC.

TURTLE CREEK ASSET MANAGEMENT INC.

UNIVERSITY OF TORONTO ASSET MANAGEMENT CORPORATION (UTAM)

VISION CAPITAL CORPORATION

WARATAH CAPITAL ADVISORS LTD.

WAYPOINT INVESTMENT PARTNERS

WELLINGTON MANAGEMENT CANADA ULC

WESTCOURT CAPITAL CORPORATION

WILLIS TOWERS WATSON

XIB ASSET MANAGEMENT INC.

YTM CAPITAL ASSET MANAGEMENT LTD.

About the ACC

The Alternative Credit Council (ACC) is the global body representing asset management firms in the private credit and direct lending space. It currently represents over 200 members that manage $450bn of private credit assets. The ACC is an affiliate of AIMA (the Alternative Investment Management Association). It is governed by its own board which ultimately reports to the AIMA Council. ACC members provide an important source of funding to the economy. They finance mid-market corporates, SMEs, commercial and residential real estate developments, infrastructure and the trade and receivables business. The ACC provides guidance on policy and regulatory matters, supports wider advocacy and educational efforts and produces industry research to strengthen the sector's sustainability and economic and financial benefits. Alternative credit, private credit or direct lending funds have grown substantially in recent years and are becoming a key segment of the asset management industry. The ACC seeks to explain the value of private credit by highlighting the sector's wider economic and financial stability benefits.

www.lendingforgrowth.org

About AIMA

The Alternative Investment Management Association (AIMA) is the global representative of the alternative investment industry, with around 2,000 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than $2 trillion in hedge fund and private credit assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. The ACC currently represents over 200 members that manage $450bn of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors).

www.aima.org