European Leveraged Finance Association Houlihan Lokey Akin

PRESS RELEASE

European Leveraged Finance Association outlines UCITS Fund limitations with potential solutions to allow collective investment in transferable securities.

London, 18 May 2023: European Leveraged Finance Association (ELFA) today issues a new report called 'UCITS Funds Participating in New Money Transactions - Obstacles and Potential Approaches' that reviews UCITS Fund limitations and considers options that would allow regulated investment funds falling under the European undertakings for the collective investment in transferable securities (UCITS) regulation ("UCITS funds") to participate in new money transactions to preserve value and allow for recoveries of distressed investments.

UCITS funds have often experienced a substantial erosion of value during restructuring transactions due to regulatory restrictions that prohibit participation in new capital contributions. In these situations, the new money providers are often able to extract enhanced economics from the restructured company, which UCITS funds are unable to participate in, impairing recovery prospects.

These restrictions can negatively impact returns for UCITS funds as they prevent UCITS funds from realising value and participating in the economics of restructuring the debt of a distressed investee company. This places investors in European retail funds at a disadvantage compared to investors in professional investor funds or in mutual funds in the United States.

Given the deteriorating market conditions, this issue is likely to become more prevalent in the near to medium term. The interests held by UCITS funds are often not large enough to allow the UCITS funds to influence the terms of the restructuring. The obstacles limiting the ability of a UCITS fund to participate in the new money of a restructuring transaction, and related implications, explored in the Insights report, include:

- **An inability to invest in new money facilities that aren't 'Transferable Securities' or 'Eligible Investments'**. In a restructuring, new money may be structured as a loan or unlisted securities as opposed to a liquid instrument, however, UCITS funds are restricted from making loans or investing in unlisted securities, which limits recovery value for distressed investments and, consequently, overall lower returns relative to funds not bound by UCITS regulations.
- **No Transferability of Participation Rights.** The right to participate in a restructuring is not generally transferable due to regulatory restrictions. Allowing UCITS funds to transfer their participation rights would allow recovery of some value from a restructuring, even if they cannot participate.
- **The inability to underwrite greater than the pro-rata share of new money.** UCITS funds are not typically able to underwrite or provide backstop facilities greater than their pro-rata share of new money, despite a willingness to do so. Current UCITS regulations prohibit funds from providing guarantees with respect to the obligations of another, consequently, UCITS funds have to forego fees for low-risk underwriting arrangements that non-UCITS funds receive.

Following discussions with its members, ELFA has analysed this topic with the support of Houlihan Lokey and Akin Gump, presenting in the Insights report three potential approaches to deal with the issue:

1. Participating in new money via a debt-issuing SPV;
2. A standardised new money structure; and
3. Transferability of new money participation rights.

These are not recommendations as they would require advance engagement with relevant regulatory authorities; however, ELFA is proposing to work with its member firms to facilitate this engagement on a co-ordinated industry basis.

Sabrina Fox, Chief Executive Officer of ELFA, commented: "The current restrictions prevent UCITS funds from realising value and participating in the economics of restructuring debt of a distressed investee company, which disadvantages investors in European retail funds compared to professional investor funds or US mutual funds. Given worsening market conditions it is time to consider solutions and engage with regulators in the interests of UCITS funds and their investors. ELFA is co-ordinating this on behalf of UCITS fund members and the wider market."

End

About ELFA
ELFA is a trade association comprised of European leveraged finance investors from over 60 institutional fixed income managers, including investment advisers, insurance companies, and pension funds. ELFA seeks to support the growth and resilience of the leveraged finance market while acting as the voice of its investor community by promoting transparency and facilitating engagement among European leveraged finance market participants. For more information, please visit ELFA's website: www.elfainvestors.com.

About Akin
Akin is a leading global law firm providing innovative legal services and business solutions to individuals and institutions. Founded in 1945 by Richard Gump and Robert Strauss with the guiding vision that commitment, excellence and integrity would drive its success, the firm focuses on building lasting and mutually beneficial relationships with its clients. Our firm's clients range from individuals to corporations and nations. We offer clients a broad-spectrum approach, with over 85 practices that range from traditional strengths such as appellate, corporate and public policy to 21st century concentrations such as climate change, intellectual property litigation and national security.

About Houlihan Lokey
About Houlihan Lokey Houlihan Lokey (NYSE:HLI) is a global investment bank with expertise in mergers and Houlihan Lokey guides clients through the complex financial and strategic challenges they face during each stage of their business lifecycle. As a leading advisory-focused independent investment bank, they are able to serve as a trusted advocate to our clients across a number of key disciplines. Through our nine dedicated industry groups and financial sponsors efforts, we provide the focused expertise to help advance our clients vision. Houlihan Lokey has the largest worldwide financial restructuring practice of any investment banking firm, with offices and experienced professionals located across the globe. Since its inception in 1988, the restructuring group has advised on more than 1,400 restructuring transactions with aggregate debt claims in excess of $3.0 trillion. With more than 250 dedicated restructuring professionals worldwide, our group has significant presence domestically and internationally. We serve clients domestically and around the world, providing extensive resources to staff each case and serve our clients. Our broad base of clients and extensive experience allow us to understand the dynamics of each restructuring situation and the needs, attitudes, and positions of all parties in interest. Please visit: https://hl.com/.

European Leveraged Finance Association
35 Ballards Lane, London N3 1XW
T +44 (0)7921 384457
E support@elfainvestors.com