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BDC Strategic Transactions

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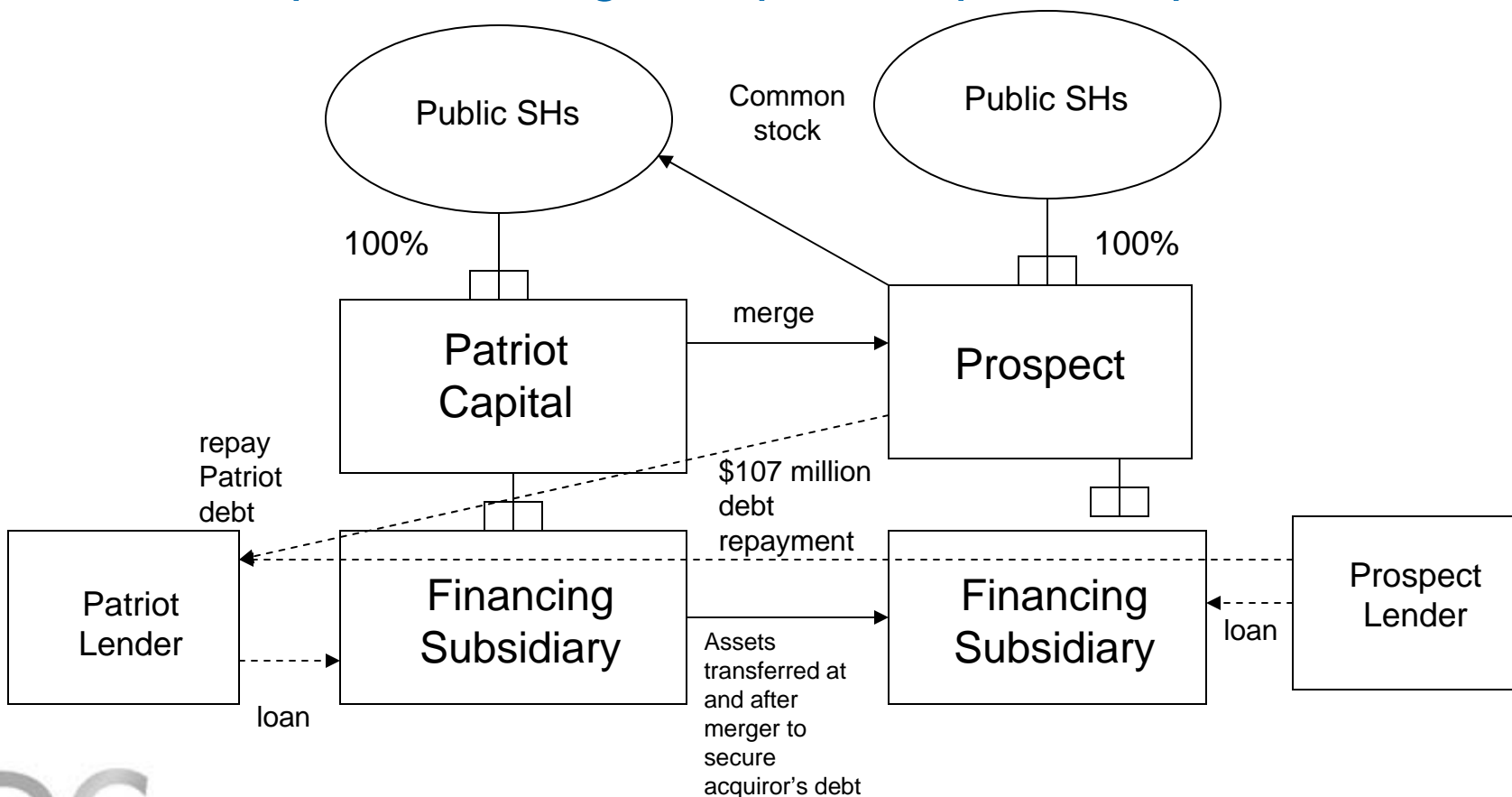
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- Recent Transactions

- Patriot Capital Funding, Inc./Prospect Capital Corporation
 - Forward merger of Patriot into Prospect
- Ares Capital Corporation/Allied Capital Corporation
 - Merger of Allied Capital into Ares Capital
- Saratoga Investment Advisors/GSC Investment Corp.
 - Capital injection; debt repayment; appointment of new investment adviser/administrator to BDC

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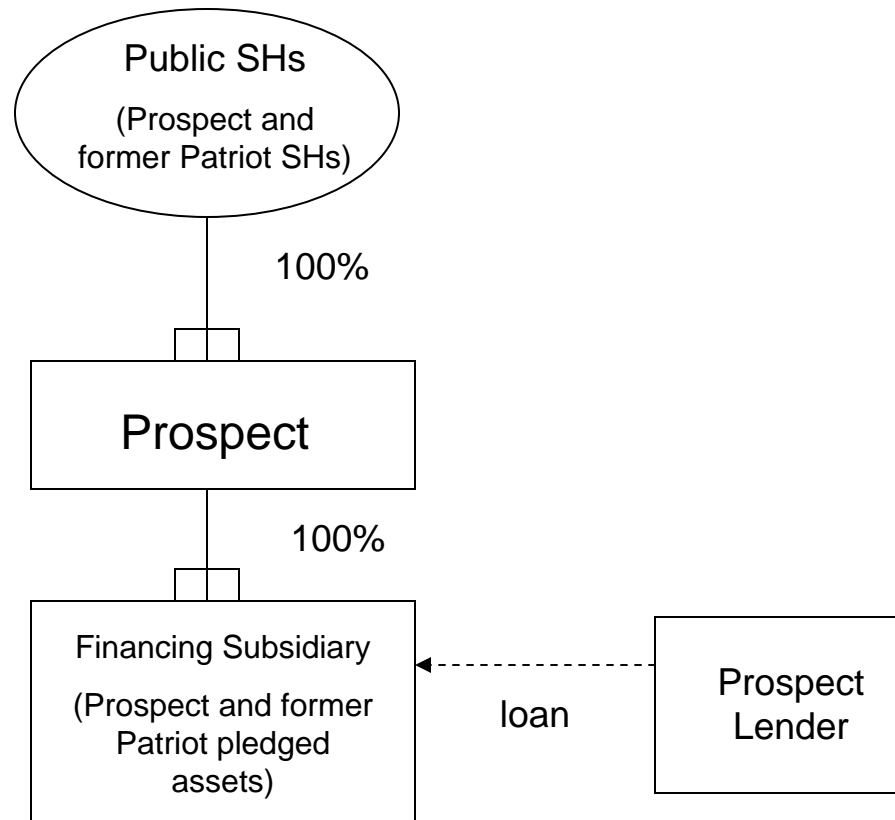
- Patriot Capital Funding/Prospect Capital Corporation



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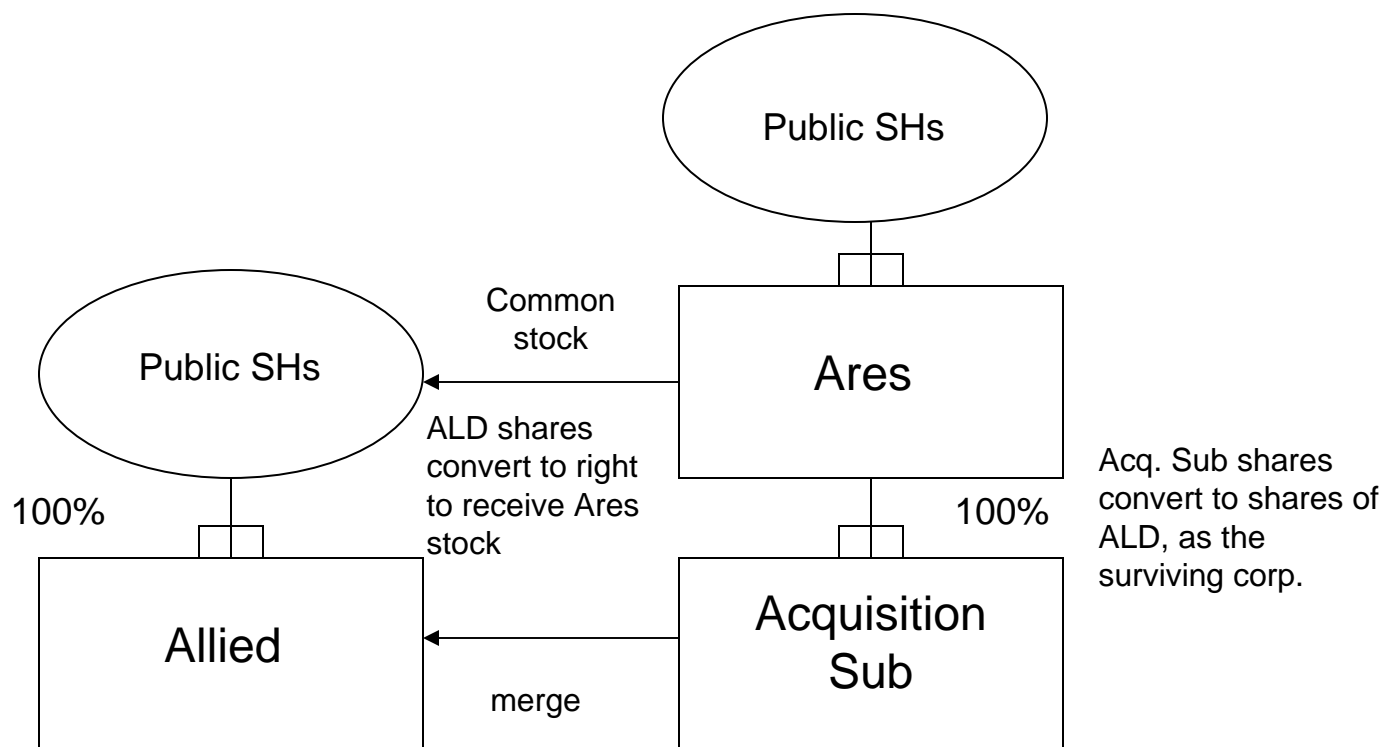
- Patriot Capital Funding/Prospect Capital Corporation
- Resulting structure:



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- Ares Capital Corporation/Allied Capital Corporation

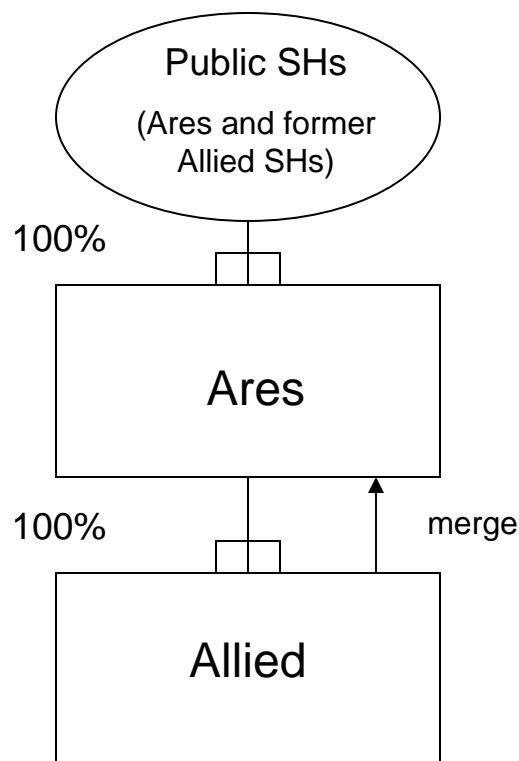
Step One:



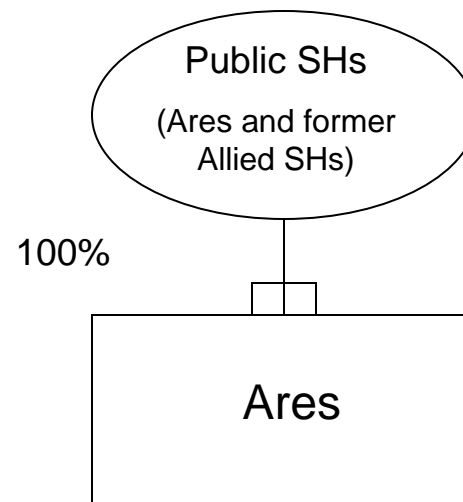
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- Ares Capital Corporation/Allied Capital Corporation

Step Two (short-form merger):

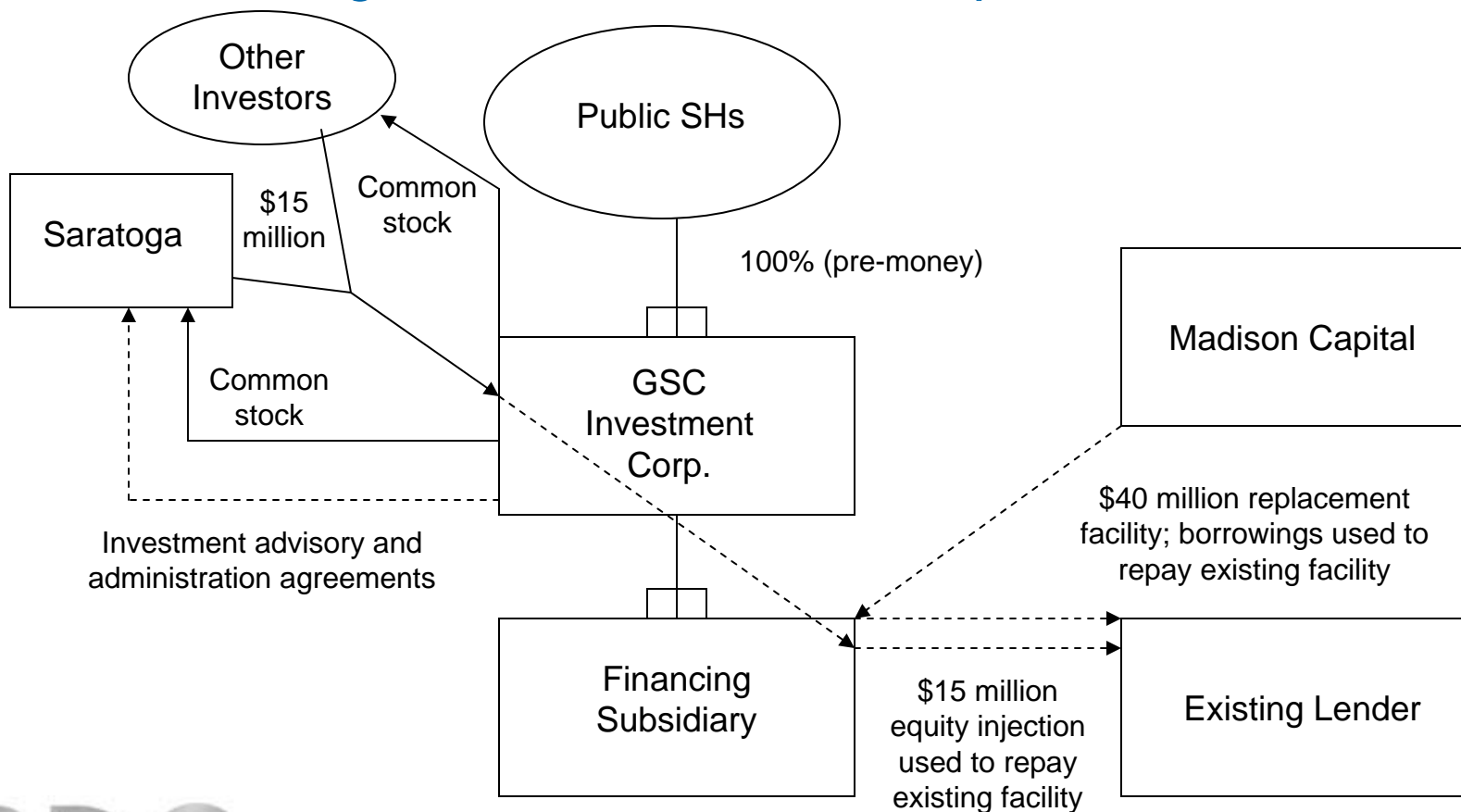


Resulting structure:



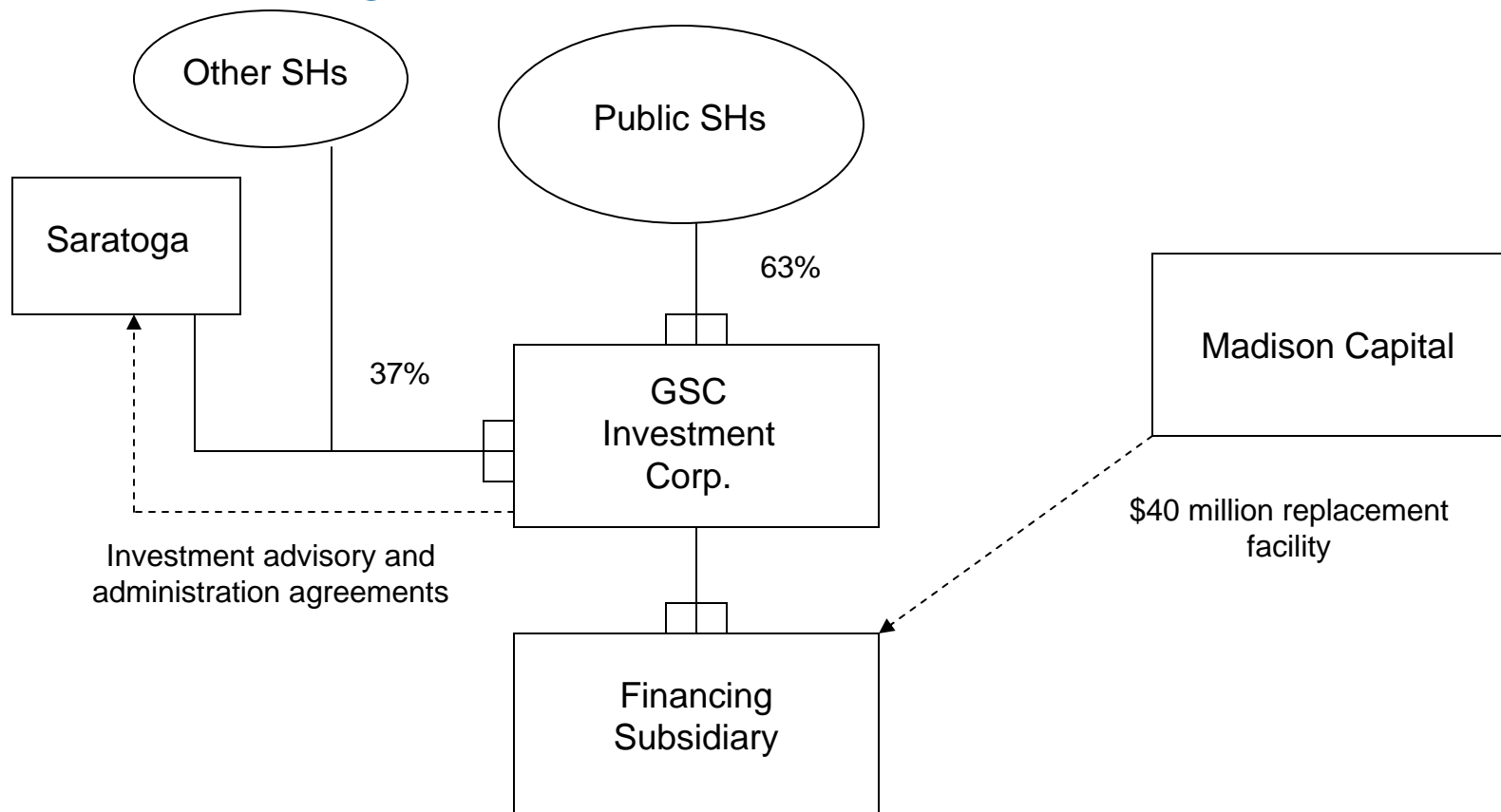
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- Saratoga/GSC Investment Corp.



BDC Strategic Transactions

- Saratoga/GSC Investment Corp.



- What are some of the General Issues to Consider?
 - Transaction structure issues
 - Taxable/tax-free nature of transaction
 - Change of Control issues
 - Does Revlon (or another state's equivalent) apply?
 - No shop, fiduciary out, "superior proposal", matching rights and termination fees
 - Shareholder approval matters under state law and exchange listing requirements
 - Issues arising under existing financing arrangements of acquired and acquiring BDC

- What are some of the BDC-Specific Issues to Consider?
 - Transaction structure issues:
 - BDC cannot own a BDC
 - No “fund” can hold greater than 3% of BDC
 - Final Dividend
 - Shareholder approval matters
 - New Advisory and other agreements
 - Compensation matters

- What type of disclosure is required?
 - Merger requires combined proxy statement/registration statement on Form N-14
 - N-14 gets reviewed by Division of Investment Management
 - Solicitation Issues
 - Press releases
 - Road shows
 - ISS presentation
 - Pro Forma financial statement issues
 - Fair Value adjustments
 - New Advisory and other agreements

- **What Issues are Raised at the Portfolio Company Level?**
 - Eligible Portfolio Cos. Acquiring BDC will need to determine whether the Portfolio Cos of target BDC are “eligible” Portfolio Cos
 - Nature of Income. Acquiring BDC will need to review the nature of the target BDC Portfolio Cos and their respective sources of income.
 - Change of Control Triggers; Transfer Restrictions, Joinders Requirements, etc.
 - Portfolio Co employment agreements
 - Portfolio Co incentive plans
 - Portfolio Co credit agreements
 - Equity ownership rights of management (e.g., tag-along, drag-along, etc.)

- **What Issues are Raised by BDC Debt Repayment/Replacement?**

- Borrowing Base: which assets will qualify as part of the “borrowing base” under the acquiring BDC’s new or existing facility?
- Financing Subsidiary: may need to combine assets of two separate financing subsidiaries into a single financing subsidiary
 - New security: previously un-pledged assets may need to be transferred to financing subsidiary, which might require consent, joinders, etc.
 - Covenants: Need to diligence target for compliance
- “Subsidiary” vs “Portfolio Company”: Portfolio Cos are typically excluded from definition of “Subsidiary” for most or all purposes under a BDC Credit Agreement.
 - Covenants: fewer restrictions imposed on the operations of the Portfolio Companies as compared to Subsidiaries; but significant Portfolio Cos may be treated the same
- Use of C Corp Blockers: If C Corp blockers are used, consider their status under credit facility

- What are Some of the Unique Issues Relating to Asset Management Portfolio Cos?
 - Ownership Issues:
 - Section 12(d) prohibits ownership of a registered investment adviser by a BDC without exemptive relief
 - If an unregistered asset manager is acquired, as the business grows, need to be sensitive to the number of funds (*i.e.*, “clients”) it manages.
 - Special attention needs to be paid to other asset manager Portfolio Cos of the acquired BDC so that all “clients” are not combined for purposes of determining whether registration is required.
 - Dodd-Frank is likely to dramatically change the landscape and require registration of most asset managers, which will be a significant issue for BDCs with asset management Portfolio Companies
 - Management fee income is typically viewed as “bad” RIC income, so blocker or other arrangement needs to be utilized

- What are Some of the Unique Issues Relating to Asset Management Portfolio Cos?
 - Contract Issues
 - Anti-Assignment/Change of Control Triggers.
 - If the fund management agreements include garden variety anti-assignment clauses, typically no “assignment” of the agreement would be deemed to occur upon a change of control of the BDC
 - Many fund management agreements bootstrap the Advisers Act definition of “assignment” into the anti-assignment clause.
 - Anti-assignment provisions in fund management agreements that use the Advisers Act definition of assignment could be triggered upon a change of direct or indirect control of the asset manager and would require the requisite consents
 - Consents. If consents are required under a fund management agreement, in many cases the consent process will be challenging, and may involve obtaining consent of the issuer/fund, consent of the controlling class of noteholders and/or equity of the issuer/fund, and confirmation from the relevant rating agencies that the transaction will not result in a downgrade of the rated classes of notes.
 - Key Person” Triggers. Consider acquiring BDC’s plans for keeping management on and/or the plans of management to continue; departures could result in “key person trigger”
 - Timing. If consents under fund management agreements are conditions to closing, the consent process can affect timing; if not conditions to closing, consider the impact of the BDC transaction occurring prior to obtaining fund consents

- What are Some of the Unique Issues Relating to Asset Management Portfolio Cos?
 - BDC Deal-Level Issues:
 - Required Consents. Depending upon the importance of the managed fund business, acquiring BDC may want the requisite consents to be conditions to closing
 - Certainty of Closing. Requiring such third party consents is also in conflict with the typical public company deal model, which is typically designed to close in the absence of a “material adverse effect” or “material adverse change” to the target company
 - Pre-Closing Dispositions. If the number of funds under management gives rise to adviser registration concerns, or if the managed funds are not consistent with the acquiring BDC’s business model, the acquired BDC may try to sell the managed fund business prior to closing of the BDC level deal