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Private lending funds, often called private credit vehicles, are an increasingly attractive option for deploying capital in commercial lending outside traditional banking channels. These funds pool investor money to originate or acquire loans — typically secured by real estate or other assets — for businesses and projects that banks may pass on. Unlike banks, they do not take deposits and are not subject to the same heavy banking regulations, but they operate within a framework of securities laws and investor protections.

For business owners, founders exploring structured financing, lenders, or attorneys entering this space, understanding the economics is critical. Launching a fund is achievable, but it demands thoughtful planning around legal structure, documentation, compliance, and operations. Underestimating the infrastructure, especially documentation, can quickly erode returns or create enforceability risks. Modern tools are changing that equation, making professional-grade processes more accessible and cost-effective.

Common Legal Structures

Most private lending funds are structured as **Limited Liability Companies (LLCs)** or **Limited Partnerships (LPs)**, often formed in Delaware for its flexible laws and investor familiarity. In an LP, a general partner (GP, often the fund sponsor or manager) handles operations and investment decisions, while limited partners (LPs, the investors) provide capital with limited liability.

Fund-of-funds arrangements or parallel vehicles may be used for tax efficiency or to accommodate different investor types. The choice depends on tax considerations, investor preferences, and strategy (e.g., real estate-focused lending). Professional legal counsel is essential early to tailor the structure and minimize tax leakage or conflicts.

Investor Eligibility and Fundraising

Funds typically rely on **Regulation D** exemptions under the Securities Act of 1933, most commonly Rule 506(b) or 506(c). This allows raising unlimited capital from *accredited investors* — individuals with a net worth over \$1 million (excluding primary residence) or income exceeding \$200K (\$300K joint) in recent years — without full SEC registration.

Rule 506(b) permits up to 35 non-accredited investors (with restrictions) and relies on pre-existing relationships, while 506(c) allows general solicitation but requires verified accredited status. Funds may also qualify under Investment Company Act exclusions like 3(c)(1) (≤ 100 investors) or 3(c)(7) (qualified purchasers).

These rules keep things private but impose limits on marketing and require careful compliance to avoid "bad actor" disqualifications or rescission risks.

Essential Legal Documentation

Documentation forms the legal infrastructure of the fund and its deals. Key documents include:

- **Fund formation docs:** Operating Agreement or Limited Partnership Agreement (LPA) outlining governance, fees, capital calls, distributions, and GP/LP rights.
- **Private Placement Memorandum (PPM):** Discloses strategy, risks, fees, and terms (not always required but highly recommended for transparency).
- **Investor Subscription Agreements:** Formalize commitments and representations.
- **Loan documents:** Promissory notes, security agreements, mortgages, guarantees, etc., for each lending transaction. These must be precise for enforceability.

High-quality drafting directly impacts speed, cost, risk of disputes, and outcomes in default. Poorly prepared documents can lead to delays, higher legal fees in workouts, or unenforceable terms. This is where technology shines: automated platforms can generate consistent, customizable loan docs rapidly, reducing reliance on manual drafting while maintaining compliance and quality.

Regulatory Considerations

Private lending funds are generally not required to be licensed as lenders in many jurisdictions if they avoid taking deposits or engaging in certain banking activities. However, they are not unregulated. Securities laws (Reg D filings via Form D), anti-money laundering (AML) rules, and potential state lending or usury laws apply. If the manager advises the fund, Investment Advisers Act considerations or registration may

arise for larger operations.

Ongoing obligations include investor reporting, tax filings (e.g., K-1s), and compliance monitoring. Working with experienced counsel helps navigate this without overkill.

Setup and Ongoing Costs: The Real Numbers

Many underestimate upfront costs.

Setup costs for a modest fund (e.g., \$20M+ target) often range from \$100,000 to \$500,000+ in organizational expenses, including:

- Legal fees for formation, PPM, and LPAs
- Compliance, tax structuring, and filings
- Marketing materials and initial administrative setup

These are often capped (e.g., 0.5–1% of commitments) and borne by the fund/investors once closed, but sponsors front them initially.

Ongoing overhead includes management fees (typically 1–2% of committed or invested capital to cover operations), fund administration, auditing, investor reporting, loan servicing, and compliance. Third-party administrators, loan servicers, and software add costs but reduce internal burden. Performance fees ("carry," often 10–20% above a hurdle) align incentives.

Documentation is a recurring pain point. Manual processes inflate legal and review costs per loan. Automation tools—like those streamlining commercial lending docs—dramatically lower this overhead, speeding closings, minimizing errors, and improving scalability. Better processes mean lower costs and stronger infrastructure.

When Does a Lending Fund Make Economic Sense?

A fund makes sense if you can raise sufficient capital (often \$20M+ minimum for efficiency), have a repeatable deal flow, and manage costs to deliver competitive net returns to investors after fees. It suits operators with lending expertise, networks for sourcing deals, and the ability to handle administration or outsource it effectively.

It may *not* make sense for one-off deals, very small scales, or those without compliance bandwidth. Syndication, joint ventures, or direct lending platforms could be simpler. Scale, strategy, and execution determine viability. With efficient documentation and operations, the economics improve significantly, allowing focus on origination and portfolio performance rather than paperwork.

Building for Success

Establishing a private lending fund requires real investment in legal, operational, and technological infrastructure. The rewards — flexible capital deployment, attractive yields, and diversification — can be substantial when done right. Documentation isn't mere paperwork; it's the foundation that protects enforceability, controls costs, and drives outcomes.

At **Farley Law**, we help clients navigate these intersections of law, lending, and technology. Whether you're exploring fund formation, optimizing loan documentation, or scaling operations, experienced guidance paired with practical tools positions you for success in the evolving private credit space. Contact us to discuss how to make the economics work for your goals.
