

**APPLEBY**

# **Guide to Exempted Limited Partnerships**

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## **PREFACE**

The Exempted Limited Partnership Law (2001 Revision) (the “Exempted LP Law”) provides for an “exempted limited partnership” (an ‘Exempted LP’), as distinct from a limited partnership (an ‘ordinary LP’) registered under the Partnership Law. The Exempted LP Law seeks to meet many of the shortcomings of the Partnership Law in regard to the ordinary LP as a vehicle for offshore investment.

The ordinary LP provided for in the Partnership Law was essentially conceived as a method of allowing investors (‘limited partners’) to invest with limited liability in certain restricted businesses subject to observing certain requirements perceived to offer protection to persons dealing with the ordinary LP. Thus the ordinary LP had to be registered; its registration had to be published in the Gazette; the role of limited partners was restricted to that of ‘silent partners’ in that they could take no active part in the partnership business; a change in its constitution had to be gazetted; a limited partner’s right to share in the profits was seemingly limited to taking interest at a fixed rate payable only out of profits; and a limited partner had a perpetual exposure to contribute in the event the ordinary LP became insolvent even after he had withdrawn or transferred his interest. The ordinary LP was thus a cumbersome vehicle.

## **THE NATURE OF AN EXEMPTED LIMITED PARTNERSHIP**

A partnership registered under the Exempted LP Law has a number of novel features. Thus:

- (a) It may be formed for any lawful purpose “to be carried out or undertaken either in or from within the Islands or elsewhere” provided it does not undertake business with the public of the Islands (s.4);
- (b) It must maintain a registered office in the Islands (s.6);
- (c) At least one general partner, if more than one, must be resident here or, if a company, be registered under the Companies Law (whether by incorporation as a Cayman Islands company or registered as a foreign company having a place of business in the Islands) or if, a partnership, be registered under the Exempted LP Law (s.4(5));
- (d) Whilst a Limited Partner is precluded from taking part in the general conduct of the partnership business, a number of specific activities similar to those appearing in the U.S. Law of limited partnership, are deemed not to offend this principle (s.7(3));
- (e) The partnership is not dissolved or disrupted by a change in the identity of the partners, the assignment of a limited partnership interest or the death or bankruptcy or incapacity of a limited partner (s.7(6));
- (f) The rights to assign and to mortgage a limited partnership interest are specifically recognised (s.7(7));
- (g) Registration is accomplished by the filing with a Registrar of a statutory statement signed by the general partner (s.9(1));
- (h) The general partner has the responsibility for maintaining (or causing to be maintained) a register of partnership interests and particulars regarding the name and address and contribution of each partner, the amount of any capital returns and the dates thereof. The register must be maintained at the registered office of the Exempted LP. The register is open to public inspection and must be kept up to date (s.11);
- (i) Unless the partnership agreement provides otherwise, a limited partner may demand and shall receive accounts from the general partner (s.12);
- (j) Proceedings are instituted usually by or against the general partners and not by or against limited partners, unless limited partners take part in conduct of partnership business which is not allowed by s.7(3) (s.13);

- (k) The return of capital contributions made by limited partners is permissible so long as the partnership is solvent immediately following such return but there is a contingent liability to repay such returned contribution to the extent necessary to settle debts if the return of capital to the limited partner is not justified and the partnership is insolvent within 6 months of the return of the contribution (s.14);
- (l) A partner or creditor can apply to the court for an order for dissolution on just and equitable principles. The death, bankruptcy or incapacity of the last remaining general partner by law determines the partnership unless the limited partners take steps to replace him (s.15);
- (m) The Governor can grant a Tax Exemption Undertaking to an Exempted LP and in respect of the interests of the partners thereto (s.17);
- (n) The general partner is required to make an annual return to the Registrar regarding compliance with the Exempted LP Law and to pay an annual return fee (s.19);
- (o) A partner can deal with the partnership in which he has an interest in the same way as if he were dealing with any other third party but any right to repayment of a debt must be subordinated to all other creditors (s.20); and
- (p) A limited partnership registered under the Partnership Law is unaffected by the Exempted LP Law but it may be re-registered as an exempted limited partnership under the Exempted LP Law if it so chooses (s. 21).

The Exempted LP Law makes no pronouncement to indicate that a partnership registered under the Exempted LP Law is a separate legal entity. Rather, the contrary seems to be the case in so far as s.21(2) of the Exempted LP Law provides that re-registration of a limited partnership (first registered under the Partnership Law) shall not have the effect of creating a new entity. It is therefore safe to say that an Exempted LP is not a juridical entity but a set of contractual obligations affecting the partners inter se where a general partner is vested with certain powers and obligations in relation to a business and the assets of the business. Sections dealing with the right to contract and to institute proceedings reinforce this notion.

In general the Exempted LP Law goes some distance to bring into our Law a concept of partnership akin to the U.S. Uniform Limited Partnership Act 1987; certainly some of the features of the Exempted LP resemble those of that Act.

## **THE ADVANTAGES OF AN EXEMPTED LP OVER AN ORDINARY LP**

The following is a summary of the differences between the two types of limited partnerships available in the Cayman Islands.

## **1. Mutations & Transfers**

An Exempted LP is not disrupted by a change in the composition or character of the limited partners. There is also no obligation to report to the Registrar immediately on a change in limited partners nor to advertise in the Gazette any change in general partner as is the case with an ordinary LP. Instead, the general partner of an Exempted LP must keep a register of partnership interests, which must be up-dated periodically within 25 days of the change, and any change in general partners must be notified to the Registrar. Whilst the register of partnership interests is public, this shortcoming may be circumvented by use of nominees. All filings with the Registrar in respect of an Exempted LP are public. The right to transfer and to mortgage a limited partnership interest is specifically recognised though a general partner has a statutory power of veto (s.7(7)).

## **2. Withdrawal of Contributions and Distributions of Capital Gains & Profits (s.14)**

Whereas under an ordinary LP there is a virtual prohibition against the return of contributions made by a limited partner and the limited partner remains perpetually accountable to the partnership, under the Exempted LP Law contributions can be returned to a limited partner. This has two features, namely that not only can the limited partnership interest be returned (ie. the position be liquidated) but also by virtue of the definition of a "contribution" it means also that a capital growth or other profit can be distributed with impunity if the partnership agreement so provides.

The restriction now on "returning the contribution" is that the Exempted LP remains solvent immediately following the return and will continue to be solvent for 6 months after the return. The limited partner's liability is limited to the repayment of such contribution if the partnership becomes insolvent within that period.

The concept of "profit sharing" is innovative. Under an ordinary LP, in theory, a limited partner had to content himself with "interest" on his contribution. Various devices were invented to circumvent this structure. Under the Exempted LP Law there are no statutory provisions regulating profit-sharing and the definition of "partnership interest" recognises the concept of profit as an entitlement of a limited partner.

## **3. Ability to Conduct Foreign and Other Business (s.4)**

It is recognised that an Exempted LP can undertake all types of business including business abroad: indeed offshore enterprise must be the principal purpose of an Exempted LP. This was not clearly within the purview of the Partnership Law when incorporating the provisions for ordinary LPs. It is to be noted, however, that in so far as the promoters of an Exempted LP may seek to offer limited liability protection to investors in limited partnership interests, they would be well advised to register

the Exempted LP as a limited partnership in such jurisdictions abroad as they contemplate doing business or otherwise to register a limited liability company as the vehicle through which trading is carried on in those jurisdictions. Cayman will not recognise a foreign limited partnership as such (it must register here to be recognised here) and in the absence of such recognition of foreign limited partnerships by the Cayman Courts, in all probability a Cayman Exempted LP would not be recognised if not registered in the foreign jurisdiction in which it carries on business.

Under s.4(1) it is still possible to register an Exempted LP which would have as its primary purpose investment in a Cayman non-resident company. S.4(1) allows of "any lawful purpose ... to be carried out or undertaken either in the Islands or ..." and the proviso against undertaking business with the public in the Islands would not apply to the taking of shares in a non-resident company under a private offering. Thus an Exempted LP may have special attractions to investors resident in jurisdictions the tax laws of which offer advantages to investors in partnerships that are not available to investors in companies.

#### **4. Local Presence (ss. 4, 5 & 6)**

As the concept of the Exempted LP is to cater for the offshore investor, it is necessary to give the Exempted LP a 'local presence'. The Exempted LP Law does this by requiring that at least one general partner, whether an individual, a company or itself a partnership, be 'resident' here. This is not the case with an ordinary LP. While attorneys generally advocated that at least one general partner should be resident so as to give an ordinary LP some causal connection with the Islands there is no express provision under the Partnership Law to this effect.

Local presence is a logical requirement so that Cayman courts may be vested with jurisdiction over the partnership and so that the partners are rendered more readily accountable to the provisions of the Exempted LP Law and thus giving the concept legitimacy.

#### **5. Limited Partner's Role Expanded (s.7)**

The U.S. Limited Partnership Act recognises that a limited partner may act as agent for the general partner without violating its limited liability. Now under the Exempted LP Law we have express statutory confirmation that this duality is permissible under our Law in the case of an Exempted LP.

## **CONCLUSION**

The Exempted LP is an innovative vehicle for meeting the needs of offshore investors, particularly as an alternative to corporate mutual funds and unit trusts. There is provision for re-registering an existing ordinary LP as an Exempted LP and serious regard should be given to this possibility in the case of each ordinary LP now used in the offshore investment community.

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For more specific advice on exempted limited partnerships in the Cayman Islands, we invite you to contact one of the following in the Corporate and Commercial Practice Group:

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