

Private fund limited partnerships.

An Introduction to the new legal form



Background

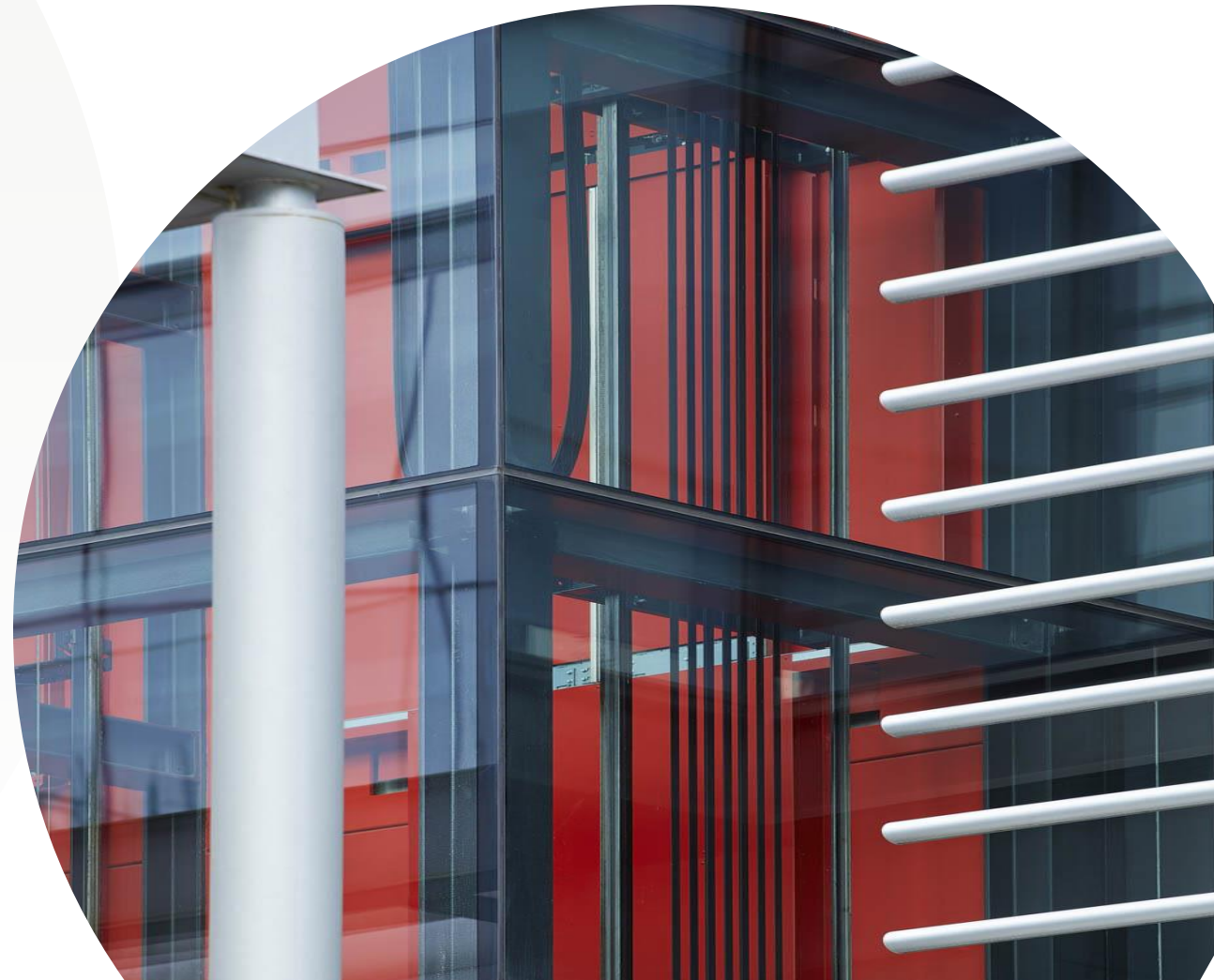
HM Treasury has published the Legislative Reform (Private Fund Limited Partnerships) Order 2017 (the "Order") which significantly amends the Limited Partnership Act 1907 (the "Act") and which introduces a new form of limited partnership - the private fund limited partnership ("PFLP").

Originally a legal form used for any type of business, today the limited partnership structure is the most commonly used legal form for private equity and venture capital funds. These funds are a more modern form of business than those business which the Act was designed for, and the vital role they play in the UK economy was certainly not anticipated when the Act was drafted. Yet despite the change in its key use, and the length of time it has been around, the Act has seen very little in the way of reform.

It is the Government's aim, in introducing the PFLP, to make UK limited partnerships an attractive vehicle for private equity and venture capital funds, by reducing the administrative and financial burdens which affect these funds and, in particular, by clarifying activities that investors can undertake without risking their limited liability status. In taking this step, the Government is seeking to keep up with other jurisdictions, who have introduced or are in the process of introducing, more flexible structures for private funds.

This note sets out a brief guide to the new legal form, as anticipated in the Order.

The contents of this paper are for information only and are not intended to be construed as legal advice and should not be treated as a substitute for specific advice.



Becoming a PFLP

To be designated as a PFLP, the limited partnership must be constituted by an agreement in writing and must satisfy the conditions set out below.

New limited partnerships

New PFLPs will be designated at the point at which they register with Companies House as a limited partnership using the new Form LP7. Form LP7 will require the following:

- the partnership name;
- the name of each general partner and limited partner;
- the address of the proposed principal place of business;
- a declaration by the general partner declaring the partnership meets the PFLP conditions; and
- a signature by the general partner.

If a new limited partnership does not meet the PFLP conditions at the point of registration, it can use a revised Form LP5 to register, providing the details above without the declaration, as well as the general nature and the term of the partnership and the capital contributions of the limited partners. Once the conditions have been met, Form LP8 can be used to apply for designation as a PFLP.

Existing limited partnerships

Limited partnerships registered prior to the new legislation coming into force will be able to convert to PFLP status by providing the information set out above, as well as the registration number and date of registration of the limited partnership.

It is important to note that, once converted, a PFLP cannot return to general limited partnership status.

Certificates and names

On registration, the registrar will issue a certificate of designation as a PFLP stating the date of designation. This certificate is conclusive evidence that the limited partnership has been so designated.

For new limited partnerships, a combined certificate will be issued confirming creation of the limited partnership and designation as a PFLP.

All limited partnerships, including PFLPs, need to have a name ending with the words “limited partnership” or “LP”; there is no requirement to change the name to reflect the designation as a PFLP.

The Conditions

The concept of the PFLP is linked to the concept of a "collective investment scheme", as that term is defined in section 235 of the Financial Services and Markets Act 2000 ("FSMA"). It is worth noting that, for the purposes of the PFLP, the exemptions which otherwise apply under section 235 of FSMA will not apply.

The conditions which the PFLP must meet are as follows:

- it is an arrangement with respect to property of any description, including money, the purpose or effect of which is to enable persons taking part in the arrangements (whether by becoming owners of the property or any part of it or otherwise) to participate in or receive profits or income from the property;
- the persons who are to participate do not have day-to-day control over the management of the property, whether or not they have the right to be consulted or to give directions; and
- the contributions of the participants and the profits or income out of which payments are to be made to them are pooled and/or the property is managed as a whole by or on behalf of the operator of the scheme.

Capital Contributions

The Act currently requires a limited partner to make a contribution of capital at the time of entry into the partnership and that such contribution be registered at Companies House. The limited partner's liability is limited to the amount of their contribution and if they withdraw the capital then the limited partner is liable for the LP's debts and obligations up to the amount withdrawn. Any increase in capital contribution must be declared.

In contrast, limited partners of new PFLPs will not be required to make a capital contribution to the PFLP.

For partnerships established before the introduction of the new rules but which subsequently convert to the PFLP regime, the pre-PFLP capital contributions do not transfer and so cannot be withdrawn. If such contributions are withdrawn then the limited partner will remain liable. Such capital contributions will still need to be declared by the limited partnership. However, contributions made after the conversion to the PFLP regime will be capable of being withdrawn without liability and without declaration.

Once a partnership established after the introduction of the new rules converts to the PFLP regime, any capital contributions made before the PFLP regime will transfer so that all capital contributions of the PFLP can be withdrawn and do not require to be declared.

Changes to the Partnership

As is already the case, any changes to the details of the partnership, or changes to the liability of any partner will need to be notified to the registrar using Form LP6.

A PFLP will not need to publish a Gazette notice when a limited partner transfers its interest in the PFLP. This reduces an administrative burden for PFLPs. Correspondingly, section 36(1) of the Partnership Act 1890 is disappplied in relation to PFLP; that section provides that a person dealing with the firm is entitled to treat a former partner as continuing to be a partner until they receive notice (by way of the Gazette) that the person is no longer a partner of the partnership.

Where a general partner ceases to be a partner of a PFLP, a gazette notice will still be required in order to ensure the departing general partner does not continue to be treated as a partner of the PFLP.

The White List

In terms of the Act, a limited partner may not take part in management of the limited partnership's business without becoming liable for the LP's debts incurred for the period during which they were involved in the management.

The Order introduces a new, non-exhaustive, "white list" of activities that a limited partner in a PFLP may undertake without being considered to be taking part in the management of the business.

It is important to remember that the white list does not give the limited partners in a PFLP the right to undertake these actions, as that is a matter to be dealt with in the partnership agreement. However, it is hoped this white list will help partners to understand which activities they can undertake without risking their limited liability, reflecting their role in the PFLP.

The white list includes taking part in a decision about:

- the variation of the partnership agreement;
 - whether to allow:
 - investment by the partnership;
 - the participation by the limited partner in an investment by the partnership; and
- the incurring, extension or discharge of debt or other obligation owed by the partnership;
- whether the general nature of the partnership business should change;
- whether to dispose of the partnership business or to acquire another business;
- whether a person should become or cease to be a partner;
- whether the partnership should be dissolved or wound up; and
- changes in the persons responsible for the day-to-day management of the partnership.

The white list includes taking the following actions:

- enforcing rights under the partnership agreement (unless those rights are to carry out management functions);
- approving the accounts of the partnership;
- approving the valuation of the partnership's assets;
- entering into a contract with the partnership or a general partner in the partnership (unless the contract requires the limited partner to take part in management functions);
- acting as a director, member, employee, officer or agent of, or a shareholder or partner in a general partner or another person appointed to manage or advise the partnership in relation to the affairs of the partnership; and
- discussing the prospects of the partnership business.

Winding up a PFLP

In terms of the Act, a limited partnership must be wound up by its general partner. Where there is no general partner remaining, a court order must be obtained in order to wind up the limited partnership.

In contrast, the PFLP can be wound up, either by a general partner or by another person, agreed between the partners, to carry out the winding up. A PFLP which has no general partner can be wound up by a person appointed by the limited partners. The appointment of the person to wind up the PFLP would be covered by the White List activities, so would not risk the limited liability status of the limited partner.

This is a useful development as it avoids the lengthy court process if there is no general partner remaining in the limited partnership. Further, it allows the partners to appoint an insolvency practitioner, where expert knowledge may be required. It is especially useful where the general partner cannot in reality act to wind up the partnership.

Other Matters

The duties of partners under Sections 28 and 30 of the Partnership Act 1890 apply to partners of limited partnerships. These are the duty of partners to render accounts and information of all things affecting the partnership to any partner and the duty not to compete with the partnership. In practice, the limited partnership agreement will disapply these duties. The Order creates a statutory basis that these duties do not apply to a limited partner in a PFLP

What Next?

If adopted, the Order will come into force on 6 April 2017. The Order is being introduced using the affirmative resolution process, which means it will be adopted in its entirety or not at all. The likelihood is that the Order will be adopted and that the PFLP will become part of UK law very soon.

THANK YOU.



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