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# Corporate Liquidation

Exempted limited partnerships (explanation of the structure, statutory framework and the statutory gateway to winding up ELPs)

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# Aims and Objective

This module aims to provide an overview of:

- the nature of an ELP
- the duties owed by a General Partner to ELPs and LPs;
- statutory “safe harbours” for LPs;
- the liquidation processes relevant to ELPs; and
- some of the relevant Cayman cases considering these issues

**Objective:** to facilitate learning on this module in order to enable you to answer (i) self-assessment questions and (ii) questions relating to this part of the Corporate Liquidation assessment.

# ELPs

- Widely used **hybrid** vehicles selected by fund sponsors setting up private equity and real estate structures, tax transparent master funds and single investor vehicles.
- Intended to be a passive investment vehicle:
  - There must be at least one (Cayman based) GP with responsibility for managing business of the ELP
  - Numerous LPs who are passive investors with limited liability
- **LPA/LPD is key**: strong emphasis on contractual relationship
- Relevant statutes: **(i)** Partnership Act (2013 Revision); and **(ii)** ELP Act (2021 Revision); and **(iii)** common law and equitable principles applicable unless inconsistent with ELP Act

# ELPs: Key features



An ELP has no separate legal personality (assets held on statutory trust)



The GP is responsible for all management (but often delegates to an Investment Manager)



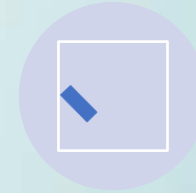
A statutory duty of good faith is owed by the GP



There is (generally) limited liability for the limited partners



But there is unlimited liability for the GP



Claims made by the ELP are generally to be brought by the GP



The liquidation of an ELP comprises two distinct stages – its winding up and its subsequent dissolution (solvent v. insolvent)

# GP duties to ELP and LPs

- **S.19 ELPA**, a GP must act at all times:
  - in good faith
  - in the interests of the ELP (unless LPA says otherwise)
- **Duty of Good Faith** – duty to display complete good faith towards co-partners in all partnership dealings and transactions (akin to a general partnership) it cannot be excluded by the LPA
- **DOGF - a fiduciary duty** – therefore an expectation of trust & confidence:
  - (i) duty of honesty in partnership dealings
  - (ii) duty of disclosure, unless modified by the LPA which carries with it a so-called “duty to speak” including disclosure of a partner’s own misconduct; and
  - (iii) an obligation not to obtain a benefit at the expense of the partnership without the other partners’ full knowledge and consent
- LPs do not (generally) owe fiduciary obligations to other partners

# GP duties (cont)

- duty to account to LPs (fundamental to any partnership)
- other typical duties (including fiduciary duties save for irreducible core) may be excluded by the terms of the LPA
- A duty in tort (ie to act with skill and care)
- A duty to keep proper books of account (cash flow, balance sheet, ELP sales and purchases of goods)
- Duty under ELPA to keep register of LPs, register of LP contributions, and a register of security interests



# LPs s.22 right to information

*Dorsey v. XIO GP (2018); GIC (2020); Abraaj (2023)*

s.22 of the ELP Law: “...each limited partner may demand and shall receive from a general partner true and full information regarding the state of the business and financial condition of the exempted limited partnership.”

- "true and full information" under s.22 broader than audited/unaudited accounts available under s.21
- necessary for express language in LPA to exclude rights under s.22
- *M&S v BNP* provides that a term can only be implied if, without the term, the contract would lack commercial or practical coherence. That was not the position here. The LPA would need to be construed as excluding the broad right to information under s.22.



## Derivative and direct claims Breach of duty

- S.33(3) ELP Act affords right to LP to bring derivative claim where GP fails or refuses to bring claim “*without good cause*”
- Aims to avoid improper stifling of claims by the GP
- No specific procedural requirements (unlike a corporate entity of ELPs elsewhere) although a limited partner must plead the facts and matters relied upon to satisfy s.33
- Is it open to an LP to bring direct claims against the GP?





Any questions re GP  
duties?

# Restrictions on LPs

- **S. 14 ELPA** – LPs must not conduct business of ELP
- LPA usually forbids such LP participation
- **S.20(1) ELPA** states that if an LP takes part in the conduct of the business of an ELP in its dealings with persons who are not partners the LP is liable, in the event of the insolvency of the ELP, for all debts and obligations of that ELP incurred during the period that it participated in the conduct of the business as though it was, for that period, a GP
- **However**, the LP is only rendered liable to a person who transacts business with the ELP during that period with actual knowledge of his participation and who then reasonably believed the LP to be a GP

# LP safe harbours

- **S.20(2) ELPA** provides for an extensive, non-exhaustive list of safe harbours, which do not amount to taking part in the conduct of the business of an ELP such as
  - approving or disapproving an amendment to the LPA
  - consulting with and advising a GP with respect to the business of the ELP
  - presentation of a winding up petition
  - acting as surety or guarantor for the ELP
  - involvement with the constitution and operation of boards and committees of the ELP (eg typical advisory committees as well as involvement on portfolio company boards)

Any questions re LP safe  
harbours?

# Commencement of winding up

- under ELPA there are four types of ELP winding up:
  - (i) **pursuant to LPA** (ie voluntarily) s. 36(1)(a)
  - (ii) **by resolution of partners** (2/3 of LPs and all GPs) unless LPA provides otherwise
  - (iii) **automatically** s.36(7) to (9) following event of withdrawal of GP being:
    - (a) the death; or (b) the commencement of liquidation, bankruptcy or dissolution proceedings; or (c) the withdrawal, removal or making of a winding up or dissolution order; in relation to the GP **unless** new GP appointed within 90 days
  - (iv) **by the court** – (a) s. 36(3) ie application of Part V CA; and (b) s.36(3)(g) ELPA preserves the power of the court, on the application of a partner, creditor or liquidator of an ELP, to make orders and give directions for the winding up and dissolution of an ELP as may be just and equitable.

# Priority of claims

- ELPA incorporates express provisions relating to the application and distribution of an ELP's property on winding up
- s. 140 of the CA (appropriately amended) applies to ELPs
- ELP's property is to be applied in satisfaction of its liabilities, and any such application is required to take into account any applicable subordination agreements, contractual set off or netting arrangements (bilateral or multi-lateral) and any other agreements for the deferral, postponement or waiver of creditors' claims.
- s.140(2) provides that the collection in and application of assets without prejudice to and after taking into account and giving effect to the rights of preferred and secured creditors



# Priority (cont)

- As for secured creditors, section 36(4) ELPA expressly recognises that a secured creditor is entitled to enforce his security without the leave of the court and without reference to the GP or any liquidator appointed to wind up the ELP
- Any surplus remaining after satisfaction in full of all the ELP's liabilities is distributed to the partners in accordance with their rights under the LPA

# Recoverable payments

- Payments to LPs
  - S.34 ELPA certain distributions to LPs may be clawed back in the event of 'insolvency of the ELP' (as defined in s.2 ELPA)
  - if an LP receives a payment representing a return of any part of its contribution or is released from a continuing obligation in respect of its commitment to make a capital contribution; and
  - LP had actual knowledge of the insolvency of the ELP
  - vulnerability period: 6 months following payment or release
  - LP liable if repayment/ performance necessary to discharge a debt or obligation of the ELP incurred during the period that the contribution or commitment represented an asset of the ELP
  - approach now closely aligned to Delaware position
  - Impact? significantly reduces likelihood that distributed amounts will be capable of being clawed back





# Recoverable payments (cont)

- **Voidable preferences**

- s.145 CA applies to ELPs.
- a conveyance or transfer of property, or a charge thereon, and any payment obligation and judicial proceeding, made, incurred, taken or suffered by an ELP in favour of any creditor at a time when the ELP was unable to pay its debts, with a view to giving such creditor a preference over the other creditors of the ELP, is invalid, if made, incurred, taken or suffered within six months immediately preceding the commencement of the winding up of the ELP
- payments to related party creditors deemed to have been made to give that creditor a preference (a related party “controls”/ has significant influence over the ELP in making financial and operating decisions)

# Dispositions at an undervalue

- A disposition at an undervalue by an ELP has always been capable of being set aside, under the Fraudulent Dispositions Act (1996 Revision) at the instance of a creditor thereby prejudiced, to the extent necessary to satisfy the obligation to that creditor
- s.146 CA deals with avoidance of dispositions at an undervalue under Part V of that Act. s.146 does not apply to a voluntary winding up of an ELP under section 36(1) of the ELP Act
- Where s.146 does apply to an ELP, a disposition at an undervalue may now be set aside in full. However, since it may be set aside only at the instance of an official liquidator, this provision will be relevant only if the relevant ELP is wound up by, or subject to the supervision of, the court.
- In any other circumstances, the FDA will continue to be applicable.

# Fraudulent trading

- Section 147 CA applies to the winding up of any ELP, irrespective of whether or not it is a voluntary winding up (s. 36(3)(d) ELPA)
- Thus, if in the course of the winding up of an ELP it appears that any of its business has been carried on with intent to defraud the ELP's creditors or creditors of any other person or for any fraudulent purpose, the court may, upon application by the liquidator, declare that any persons who were knowingly parties to the carrying on of the business in that manner are liable to make such contributions, if any, to the ELP's assets as the court thinks proper.
- For the purpose of section 147, 'intent to defraud' means an intention to wilfully defeat an obligation owed to a creditor.

# Liquidating ELPs: other relevant cases

- **Rhone Holdings** (2015): non petition clauses in the LPA will be upheld
- **Grand State** (2021): winding up petitions may be stayed if established that the debt is bona fide disputed on substantial grounds where dispute ought to be resolved by arbitration
- **ECM Straits Fund** (2023): power under s.36(3)(g) to bring the voluntary liquidation of an ELP under court supervision if thought “just and equitable”

# Conflicting decisions: can an ELP be wound up on the basis it is insolvent?

- in **XIO Diamond** (2020) Justice Kawaley formed the view, obiter, that the Court has jurisdiction under s.92 (e) of the CA to wind up an ELP including in respect of a creditor's petition on the ground of insolvency

- S.36(3) provides:

*“Except to the extent that the provisions are not consistent with this Act, and in the event of any inconsistencies, this Act shall prevail, and subject to any express provisions of this Act to the contrary, the provisions of Part V of the Companies Act (2021 Revision) and the Companies Winding Up Rules, 2018 shall apply to the winding up of an exempted limited partnership and for this purpose...”*

# Padma

- in **Padma** (2021) Justice Parker held that the Court has no jurisdiction to consider a creditor's winding up petition against an ELP, and he expressly disapproved of decision in XIO Diamond.
- Instead, Justice Parker stated that a creditor where an ELP is insolvent is to present a petition against the GP of the ELP, not against the ELP itself (as the GP has unlimited liability)
- This represents a considerable departure from prior practice in the Cayman Islands where creditors' petitions to wind up ELPs have been routinely presented against the ELP itself (and not the GP) in those circumstances

# Formation Group

- in **Formation Group** (2022) Justice Kawaley addressed the conflict between XIO Diamond and Padma concerning standing to issue a winding up petition against an ELP as opposed to its GP
- Whilst both XIO Diamond and Formation concerned petitions to wind up an ELP on the just and equitable ground (whereas Padma concerned a creditor's petition to wind up an ELP on the ground of insolvency)....
- Justice Kawaley concluded that Padma “*was wrong in finding that s.33(1) as read with s.36(3) of ELPA does not permit the presentation of a winding-up petition against an ELP alone because only the general partner may be sued*”

# Alternative to winding up



An ELP is not dissolved until notice of dissolution signed by GP or liquidator is filed with the Registrar (s.36(2) ELPA)



s. 37(3) ELPA permits striking off without dissolution where no liquidator is acting or the affairs of the ELP are fully wound up



a partner or creditor can object to the striking off within 10 years and seek ELP's reinstatement



striking off does not extinguish the liability of any GPs or LPs which continue





Questions re ELP  
winding up?

# Conclusions

Thank you for listening!

Presentation has provided an overview of:

- the nature of an ELP
- the duties owed by a General Partner to ELPs and LPs;
- statutory “safe harbours” for LPs;
- the liquidation processes relevant to ELPs; and
- some of the relevant Cayman cases considering these issues