

Cayman Court clarifies the winding up regime applicable to exempted limited partnerships

In a recent judgment in *In the matter of Padma Fund LP*, Parker J held that the Court does not have jurisdiction to make a winding up order against an exempted limited partnership (“ELP”) on a creditor’s petition and that the remedy of a creditor is to commence proceedings against the general partner for an unpaid debt. The judgment clarifies the winding up regime applicable to ELPs including the statutory gateway by which a limited partner can petition to wind up an ELP.

ELPs are a popular choice for investment fund and private equity structures in the Cayman Islands and the judgment provides important clarification on the rights and remedies of investors and creditors alike.

[Liam Faulkner](#) of Campbells acted for the general partner of Padma Fund LP in successfully opposing the Petition.

The Petition

The Petitioners presented a winding up petition against Padma Fund LP (the “**Partnership**”) seeking an order that the Partnership be wound up pursuant to section 92(d) of the Companies Act (2021 Revision) (the “**Companies Act**”), as applied by section 36(3) of the Exempted Limited Partnership Act (2021 Revision) (the “**ELP Act**”), on the ground that the Partnership was unable to pay its debts having failed to satisfy a statutory demand served on the Partnership for payment of an arbitral costs award for approx. US\$14 million.

The Partnership, acting by its General Partner, opposed the Petition on five grounds:

- the Petition was procedurally defective and the Court had no jurisdiction to make the orders sought;
- the Statutory Demand relied upon to evidence insolvency was defective and invalid due to (i) its failure to comply with the applicable rules and (ii) it having been served on the Partnership which has no legal personality;
- the Petition debt was disputed *bona fide* on substantial grounds;
- the Partnership (acting by its General Partner) has a cross-claim against the Petitioners for approx. US\$1.4 billion which exceeded the amount of the alleged petition debt; and
- the Petition had been presented for a collateral and improper purpose and was an abuse of process.

Whilst the Court heard submissions on all five grounds, the Court only considered it necessary to determine the jurisdiction argument, ruling in the General Partner’s favour and dismissing the Petition as an abuse of process.

Statutory Framework applicable to an ELP

A limited partnership is a variation on the general partnership. The formation, operation and termination of ELPs in the Cayman Islands is governed by the ELP Act and by certain provisions of the Partnership Act (2013 Revision) (the “**Partnership Act**”), certain principles of common law and the provisions of the limited partnership agreement entered into between the parties.

The principal distinction between “exempted” and “ordinary” limited partnerships is that, pursuant to section 4 of the ELP Act, an exempted limited partnership is prohibited from trading in the Cayman Islands except in furtherance of its business outside the Islands.

Section 3 of the Partnership Act stipulates that a partnership is the relation which subsists between two or more persons carrying on a business with a view to profit. Section 4(2) of the ELP Act modifies this stipulation by providing that to be an ELP, the partnership must consist of:

- at least one person, called the general partner, who in the event that the assets of the ELP are inadequate, is liable for all of the debts and obligations of the ELP; and
- at least one person, called the limited partner, who shall not be liable for the debts or obligations of the ELP in excess of the capital contributed by that person to the ELP, save as provided for in the partnership agreement or otherwise in the limited circumstances specified in sections 20(1) and 34(1) of the ELP Act.

An ELP is not an entity with separate legal personality and cannot own property in its own right. Pursuant to section 16(1) of the ELP Act, any rights or property of every description of an ELP shall be held or deemed to be held by the general partner upon trust as an asset of the ELP in accordance with the terms of the partnership agreement.

The business carried on by an ELP is conducted by its general partner who has the authority to enter into all letters, contracts, deeds, instruments or documents whatsoever on behalf of the ELP: *section 14(2) of the ELP Act*. By contrast, section 14(1) of the ELP Act restricts a limited partner from conducting any business on behalf of the ELP in its capacity as a limited partner except in certain limited circumstances.

The test of insolvency for an ELP

Whilst section 93 of the Companies Act provides a statutory definition of a company’s inability to pay debts, which in turn provides a statutory gateway for the Court to wind up a company under section 92(d) of the Companies Act, section 2 of the ELP Act provides that in the ELP Act:

“**insolvency of the exempted limited partnership**” means that the general partner is unable to pay the debts and obligations of the exempted limited partnership, otherwise than in respect of liabilities to partners on account of their partnership interests, in the ordinary course of business as they fall due out of the assets of the exempted limited partnership, without recourse to the separate assets of the general partner not contributed or committed to the exempted limited partnership and “**insolvent**” shall be construed accordingly”.

The defined term “insolvency of the exempted limited partnership” is used in sections 20(1) and 34(1)(b) of the

ELP Act only and the defined term “insolvent” used in sections 34(1)(a) and 43(2)(g) only.

In the event that the ELP is insolvent within the meaning of section 2 of the ELP Act, the general partner remains personally liable for the ELP’s debts and obligations pursuant to section 4(2).

Legal proceedings to be commenced against the General Partner only

Section 33(1) of the ELP Act states that subject to subsection (3), legal proceedings by or against an ELP may be instituted by or against any one or more of the general partners only, and a limited partner shall not be a party to or named in the proceedings.

Section 33(3) provides that a limited partner may bring an action on behalf of an exempted limited partnership if any one or more of the general partners with authority to do so have, without cause, failed or refused to institute proceedings.

The Petitioners sought to argue that section 33(1) governs the circumstances in which a limited partner may be named to proceedings and did not prohibit a creditor from commencing legal proceedings against an ELP. Parker J rejected this argument and held that there is no provision within the ELP Act or the Partnership Act which provides that legal proceedings may be instituted against an ELP in the name of the ELP. This is because it is through the general partner that the debts and obligations of the ELP are enforced. The business of the ELP is conducted by its general partner, the assets of the ELP are held by the general partner on a statutory trust and the general partner is personally liable for the debts of the ELP.

The Court has no jurisdiction to wind up an ELP on a creditor’s Petition

The Petitioners cited twelve different cases since 2013 where the Court had made a winding up order following the presentation of a petition against an ELP (not its general partner) on the assumption that the Court’s jurisdiction to make a winding up order under section 92 of the Companies Act applies to ELPs by virtue of section 36(3) of the ELP Act. Parker J held that the Court had erred in respect of these rulings.

Parker J held that section 36(3) of the ELP Act does not give a freestanding right for a creditor to present a winding up petition against an ELP. The prefatory words of section 36(3) are clear that Part V of the Companies Act only applies to an ELP if and to the extent that the provisions are not inconsistent with the ELP Act and that the presentation of a creditor’s petition was inconsistent with (and contrary to) section 33(1) of the ELP Act. As such, there is no jurisdiction for the court to make a winding up order against an ELP on a creditor’s winding up petition.

The scenarios in which an ELP can be wound up and dissolved

Parker J held that on a true construction of the ELP Act, an exempted limited partnership can be wound up and the partnership dissolved in one of two scenarios:

- voluntarily in accordance with the provisions of the partnership agreement pursuant to section 36(1) of the ELP Act; or
- by the Court pursuant to section 35 of the Partnership Act, which applies by virtue of section 3 of the ELP Act.

Section 36(1) of the ELP Act contains provisions for the voluntary winding up and dissolution of an exempted limited partnership upon the occurrence of two events:

- at the time or upon the occurrence of any event specified in the partnership agreement; or
- unless otherwise specified in the partnership agreement, upon the passing of a resolution of all the general partners and a two-thirds majority of limited partners.

Section 35 of the Partnership Act contains five grounds on which a court may order the dissolution of a partnership on the application by a partner and includes, at sub-section 35(d), when the business of the partnership can only be carried on at a loss and, by sub-section 35(e), whenever in any case circumstances have arisen which, in the opinion of the court, render it just and equitable that the partnership be dissolved. Section 35 of the Partnership Act is in substantially the same terms as section 35 of the English Partnership Act 1890. It was introduced into Cayman Islands law by section 36 of the Partnership Law, 1983.

Section 3 of the ELP Act provides that the rules of equity and of common law applicable to partnerships as modified by the Partnership Act, but excluding sections 31, 45 to 54 and 56 to 57 shall apply to an ELP, except where they are inconsistent with the express provisions of the ELP Act. At the time of introducing the ELP Act into law, the legislature chose not to dis-apply or modify section 35 of the Partnership Act.

When considering the true construction of section 36(3) of the ELP Act, the Court is required to identify “*the mischief that it was concerned to redress by the statutory provision*”. Parker J held that the intention of the legislature could not have been to enable a partner of an ELP to apply to wind up and dissolve the partnership on just and equitable grounds pursuant to section 92(e) of the Companies Act as the jurisdiction to do so already existed under section 35(e) of the Partnership Act. As the remedy already existed, there was no “mischief” to redress.

Indeed, the Court’s jurisdiction to dissolve an ELP on the application of a partner under section 3 of the ELP Act and section 35 of the Partnership Act is broader than under section 92 of the Companies Act. Parker J held that it could not have been the intention of the legislature to narrow the Court’s jurisdiction by replacing section 35 of the Partnership Act (which specifically applies to partnerships) with section 92 of the Companies Act.

In reaching this conclusion, Parker J respectfully differed from the Court’s previous findings in *XIO Diamond LP* and held that the court was in error in that case as to the proper jurisdictional basis for winding up an ELP on the petition of a partner.

A copy of the judgment can be found here: [Judgment – In The Matter of Padma Fund L.P. FSD 201 OF 2021 \(RPJ\)](#).

Commentary

An ELP is a different legal structure to a company. A company has legal personality and can own assets in its own right. When a company is wound up the company retains the legal title to the assets with the beneficial interest automatically vesting in the liquidators. In the case of an ELP, it is the relationship between the partners that is being wound up with a liquidator being appointed over its assets and undertakings. When an ELP commences

voluntary liquidation, the default position is that the general partner acts as voluntary liquidator with the effect that it continues to hold legal title to the partnership's assets on a statutory trust albeit in a different capacity. When someone other than the general partner is appointed to act as liquidator, legal title to the partnership's assets should not remain with the general partner but instead be transferred to the new liquidator, by court order if necessary, who in turn holds those assets on a statutory trust and should proceed to discharge his function by winding down the partnership's affairs in an orderly manner similar to the function of a liquidator of a company. In the event of a shortfall, the general partner remains personally liable and the liquidator has a claim against the general assets of the general partner for any shortfall.

The remedy of any creditor of an ELP is to commence proceedings against the general partner. In the event that a winding up order is made against the general partner, any liquidator appointed will continue to hold the assets of the ELP on a statutory trust to be distributed to the creditors of the ELP in accordance with the statutory scheme. In the event of a shortfall in the partnership assets, the liquidator has a claim against the separate assets (if any) of the general partner and such claim would constitute an unsecured claim in any liquidation of the general partner which ranks *pari passu* with the claims of other creditors of the same class who have an unsecured claim against the general assets of the general partner. The solvency of a general partner is therefore highly relevant to the ability of a creditor to enforce a debt against an ELP.

About Campbells

Campbells has one of the largest insolvency, restructuring and litigation teams in the Cayman Islands and has particular expertise in connection with all aspects of the restructuring and winding up of companies, investment funds, exempted limited partnerships and structured finance entities as well as complex investment fund litigation.

Recent instructions include acting for the joint official liquidators of ABRAAJ Investment Management Limited following the collapse of what was once the world's largest emerging markets private equity group with US\$14 billion AUM and acting for the joint provisional liquidators of Luckin Coffee Inc., in a high profile restructuring case.

Should you have any queries or require advice on issues relating to litigation, insolvency or restructuring in the Cayman Islands then please contact us directly.



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