

Limited Partnerships in Jersey

Introduction

The Limited Partnerships (Jersey) Law 1994 (the 'Law') provides a comprehensive statutory framework for the establishment and operation of limited partnerships in Jersey.

A limited partnership may be an appropriate structure for a number of different purposes. A principal use will be to provide an additional form of investment vehicle for mutual funds, in particular for the venture capital industry, and in this regard it is noticeable that it is possible to list limited partnership interests on the Dublin Stock Exchange and this should equally be possible on the Channel Islands Stock Exchange. A limited partnership will also be an attractive structure for various tax planning purposes, for instance as a method of holding assets situated in another jurisdiction. It may also provide an attractive method of trading as a partnership where it is desirable to have the flexibility to introduce partners as passive investors on a limited liability basis.

Tax Treatment

In most cases, the principal attraction of the limited partnership for the partners will be its tax transparency. The effect of this is that profits and losses of the limited partnership are attributed to the partners themselves who will be taxed according to their proportionate share of such profits and losses.

There are two particular advantages to a partner of this tax treatment. First, the partner is able to set off his share of any losses of the limited partnership against profits from other investments, something which is not possible in the case of an investment fund company. Secondly, the profits and losses of the limited partnership which are attributable to the partner will be treated for these purposes as arising in the country in which the investments of the limited partnership are made, which can enable a partner to take advantage of double tax treaties between the country of his residence and that of the investment.

The Income Tax (Jersey) Law 1961 has been amended to deal specifically with limited partnerships and the Comptroller of Income Tax has issued an explanatory booklet on the subject. This confirms that the limited partnership itself will not be subject to assessment for income tax and that a non-resident partner will not be liable to Jersey income tax except on Jersey source income (but excluding by long standing concession, bank deposit interest). The Comptroller of Income Tax has also confirmed that he would not treat management fees or profit share received by a general partner as Jersey source income.

Hence, provided a limited partnership has no Jersey resident partners (a general partner with exempt status is treated as non-resident for these purposes) and no Jersey source income, no tax return is required to be submitted.

Where the general partner of a limited partnership is a Jersey incorporated company, the preferable tax status for the general partner is likely to be either Exempt Company status or International Business Company status. Either of these will enable a general partner to pay interest on loans to the partnership, made either by the limited partners or third parties, without being liable to make a deduction in respect of withholding tax. A fully tax resident general partner will not have this benefit and may have to make an appropriate withholding.

Regulation

The consent of the Financial Services Commission is required to the creation of partnership interests under the Control of Borrowing (Jersey) Order 1958 (the 'Order'). An application for a consent under the Order must include certain prescribed information in relation to the general partner of the limited partnership (although not in relation to the limited partners). If the general partner is an existing Jersey incorporated company, the Financial Services Commission will merely require confirmation that the relevant information previously provided remains accurate.

Limited partnerships which constitute collective investment funds will be subject to the licensing regime under the Collective Investment Funds (Jersey) Law 1988, so that permits will be required by functionaries of the limited partnership where partnership interests are to be offered to the public. The general partner as the manager of the partnership will undoubtedly require a permit, as will any other functionaries providing services to the limited partnership in or from within Jersey.

Establishing a Limited Partnership

In order to establish a limited partnership the following steps will need to be taken:-

(i) An application must be submitted to the Financial Services Commission under the Control of Borrowing (Jersey) Order 1958, for consent to the creation of interests in the limited partnership. As partnership interests will be created on the execution of the limited partnership agreement, this consent will need to be obtained prior to execution of the partnership agreement.

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(ii) An application for the approval of the proposed name of the limited partnership should be submitted to the Registrar of Limited Partnerships. The Registrar has a discretion to refuse to register a limited partnership if he disapproves of the name and a system has been established by the Financial Services Commission for the prior approval of proposed names.

(iii) A declaration in the prescribed form signed by each general partner must be delivered to the Registrar of Limited Partnerships together with the prescribed fee of £500. The declaration must state the name of the partnership, the address of the registered office of the partnership (which must be in the Island), the full name and address of each general partner (or in the case of a company, the place where it is incorporated and its registered or principal office), the duration of the partnership and such other particulars as may be prescribed (none have been prescribed as yet). There is no requirement to file the partnership agreement and no requirement to provide the names of the limited partners.

(iv) On registration of the declaration the Registrar will issue a Certificate of Registration of the Declaration.

(v) On obtaining the consent, approval and Certificate referred to above, the partnership agreement should then be signed by all the partners, which under the Law must include at least one general partner and at least one limited partner, who may be companies incorporated in Jersey or elsewhere or individuals. There is no restriction on the number of partners. On execution of the partnership agreement, the partnership will be constituted as a limited partnership under the Law.

The Certificate of Registration of a Declaration can usually be obtained within two to three days of the above documentation being submitted, although in certain cases it may be possible to shorten this timescale.

The Partnership Agreement

The partnership agreement will set out in detail the respective rights and obligations of the general partners and the limited partners and will deal in particular with the following matters:-

- The name of the limited partnership which must end with the words 'Limited

Partnership' or the abbreviation 'LP' and must not include, subject to certain exceptions, the name of any limited partner;

- The purposes for which the partnership is established;
- The powers and obligations of the general partner in relation to the partnership, including in particular its obligations in respect of the management of the partnership and any limitations on its authority;

- The liability of the general partner to contribute to the debts of the partnership;
- The method and procedure for admission of new partners to the partnership and the retirement of existing partners;
- The extent of liability of each of the partners to make contributions to the partnership;
- The procedure for the transfer of interests in the partnership;
- The maintenance of accounting and other records of the partnership; and
- The allocation and distribution of the capital and profits of the partnership between the partners. This is an aspect which is likely to vary depending upon the particular purpose and nature of the partnership and is likely to entail the most detailed drafting and negotiation.

The Law prescribes that certain powers may be exercisable only if provided for or consented to in the partnership agreement, and that the exercise of certain rights is subject to the terms of the partnership agreement. It is therefore essential that prior to execution a partnership agreement is reviewed against the Law to ensure that the rights, powers and obligations provided for in the partnership agreement are not restricted in any way by the terms of the Law.

Rights and Obligations of a General Partner

The Law provides as a general statement that a general partner of a limited partnership has all the rights and powers and is subject to all the restrictions and liabilities of a partner in a general partnership. The Law also specifically provides that the rules of customary law applicable to partnerships shall, so far as not inconsistent with the Law, apply to limited partnerships. It will therefore be necessary in some circumstances to look at the existing customary law in relation to general partnerships in order to determine the exact scope of the rights and obligations of a general partner, particularly where the partnership agreement does not exhaustively define those powers and obligations.

The general statement set out above as to the rights and powers of a general partner is, however, qualified in three important circumstances. In the absence of a written consent or ratification of all the limited partners, a general partner has no authority to:-

- do anything which makes it impossible to carry on the activities of the limited partnership;
- possess or dispose of the property of the limited partnership other than for a partnership purpose;

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- admit a person as a general or limited partner, unless the right to do so is given in the partnership agreement.

Clearly, restriction (iii) can be and will be removed in most limited partnership agreements. However, restrictions (i) and (ii) will not generally be consented to in the partnership agreement, and in particular in the case of restriction (ii), may be open to different interpretations. For the protection of a general partner, therefore, it may well be desirable to set out the purposes of the partnership in some detail in the partnership agreement and, perhaps, even to include a statement, such as is often seen in the Memorandum of Association of a company, that a purpose of the limited partnership is to do all such things as may be incidental to or conducive to the attainment of the general purposes of the partnership. In the absence of a wide definition of the purposes of the partnership there may be a danger that an act of a general partner involving the property of the partnership could be open to challenge on the basis that it was not done for a partnership purpose. However, there is clearly a balance to be reached on this point between the interests of the general partner and the interests of the limited partners, which are likely to be different in this regard.

The partnership agreement will normally provide that all the property of the partnership is to be held by the general partner, and in any event the Law provides that any property of the partnership which is transferred into or vested in the name of the partnership shall be held or deemed to be held by the general partner in accordance with the partnership agreement. If there is more than one general partner, the property of the partnership is to be held or is deemed to be held by the general partners jointly. The partnership agreement should specifically provide for the property of the partnership to be held by the general partner or partners in accordance with this provision of the Law. The Law does not specifically state that the general partner is to be liable for all the debts and obligations of the partnership. However, this is implicit from the general statement in the Law that a general partner is subject to all the liabilities of a partner of a general partnership.

The Law provides that any debt or obligation incurred by a general partner in the conduct of the activities of the partnership shall be a debt or obligation of the partnership. There may be circumstances where it is unclear whether a general partner is acting on its own behalf or on behalf of the partnership, and in these circumstances, there clearly needs to be appropriate documentation and a clear indication as to the capacity in which a general partner is acting, in order to ensure that a general partner does not incur a debt for which it, rather than the limited partnership, is liable. We would also recommend that, as with trusts, all documents executed by a general partner on behalf of the partnership clearly indicate that the general partner is acting on behalf of the partnership.

For the protection of the property of the partnership, the Law provides that creditors of a general partner (or a limited partner) in that partner's capacity other than as a general partner (or limited partner) of the partnership, shall have no claim against the property of the partnership.

The partnership agreement will normally provide for the retirement of a general partner on the giving of a certain period of notice, although retirement may be conditional upon a suitable replacement general partner being appointed. Otherwise, if the retiring general partner is the sole general partner and the limited partners are unable to find a replacement within 90 days of the general partner's withdrawal, the partnership will be dissolved.

RIGHTS AND OBLIGATIONS OF A LIMITED PARTNER

Contributions

A limited partner is liable under the Law to contribute to the partnership the amount agreed to be contributed by the limited partner, which will normally be set out in the partnership agreement.

The Law specifically permits contributions to be made by a limited partner in money, property or services.

Share of Profits and Return of Contributions

The Law gives a limited partner the right to share in the profits of the partnership, subject to the terms of the partnership agreement and the Law. The Law similarly gives a limited partner an entitlement to the return of all or part of the limited partner's contribution to the partnership at the following times:-

- at the time specified in the partnership agreement;
- on a dissolution of the partnership; or
- on the expiry of six month's notice to all other partners, if the partnership agreement does not specify a time for the return of the contribution or for the dissolution of the partnership.

Although the Law permits partnership contributions to be made in the form of money, property or services, unless the partnership agreement provides otherwise, or the consent of the partners is obtained, a limited partner has no right to demand return of his contribution except in the form of money. The method of payment in respect of return of contributions may include the release of a further obligation to make capital contributions.

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The partnership agreement will normally provide for the respective entitlements of each of the limited partners to share in the profits of the partnership and to a return of contributions. In the absence of any such provisions, the Law provides that limited partners shall, in respect of profits, rank pro rata to contributions, and in respect of return of contributions, rank *pari passu*.

The Law imposes an important limitation on the rights of a limited partner to receive payments in respect of profits or return of contributions. A limited partner is only entitled to receive a payment in respect of profits or return of contributions if at the time the payment is made and immediately thereafter the partnership is solvent. For these purposes solvent means that the general partner is able to discharge the debts and obligations of the partnership as they fall due without recourse to any assets of the general partner which have not been contributed to the partnership. If this solvency requirement is not met, a limited partner will be liable for a period of six months thereafter to return such payments with interest if they are required in order to meet a debt or obligation of the partnership incurred during the period such profits or contributions (as the case may be) represented an asset of the partnership. Where payments have been made in respect of return of contributions, a limited partner will also be liable to repay the payment in the case of fraud.

Dealings with the Partnership

The Law envisages that limited partners may lend to, borrow from or enter into other transactions with a partnership, and it is common for money or assets to be provided by a limited partner to a partnership in the form of both contributions and loans. The Law provides that in any claim by a limited partner against the partnership in respect of any such loan or other obligation owed to a limited partner (other than in respect of return of contributions) the limited partner shall rank as a creditor of the partnership.

Rights to Information

A limited partner has the right under the Law to inspect and take copies of the books and records of the partnership. More importantly, he is entitled to demand full information of all things affecting the limited partnership and may require a formal account of partnership affairs when 'circumstances render it just and reasonable'. These rights are not subject to limitation by the partnership agreement and therefore represent an important protection for limited partners to be kept fully informed of all matters affecting the partnership.

Limitation of Liability

A limited partner will not be liable for any of the debts or obligations of the partnership unless he participates in the management of the partnership, in which case he will be liable as a general partner. However, this potential liability

is restricted under the Law in a number of important respects:-

- liability will only arise on an insolvency of the partnership;
- a limited partner will only be liable for the debts and obligations of the partnership incurred during the period that the limited partner participated in the management of the partnership;
- a limited partner will only be liable if he participates in the management of the partnership "in its dealings with persons who are not partners". Hence, participation merely in the internal management of the partnership which does not relate to dealings with third parties will not incur liability;
- a limited partner will only be liable to a person who transacts with the limited partnership "with actual knowledge of the participation of the limited partner in the management of the partnership and who then reasonably believed the limited partner to be a general partner";
- the Law also provides that doing any one or more of the following will not amount to participation in the management of the partnership:-
 - being a contractor for, agent or employee of the partnership, or of a general partner, or acting as a director, officer or shareholder of a corporate general partner;
 - consulting with and advising a general partner with respect to the activities of the partnership;
 - investigating, reviewing, approving or being advised as to the accounts or affairs of the partnership or exercising any right conferred by the Law;
 - acting as surety or guarantor for the partnership either generally or in respect of specific obligations;
 - voting, or otherwise signifying approval or disapproval of a number of specific matters set out in the Law;
 - bringing an action on behalf of the limited partnership if the general partner has refused to institute such proceedings.
- The Law goes on to say that the existence of the exemptions set out in paragraph (v) above shall not give rise to any implication that the possession or exercise of any other power by a limited partner will necessarily constitute the participation by such limited partner in the management of the limited partnership.

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Admission of New Partners and Transfer Interests

The partnership agreement will normally provide a procedure for admitting additional or replacement limited partners, which will usually involve the new limited partner executing a deed of adherence under which the limited partner agrees to be bound by the terms of the partnership agreement. The partnership agreement may also provide for the level of contributions to be made by any new limited partner, which in some cases may be calculated by reference to a formula. Unless specifically permitted by the partnership agreement, the Law prohibits the admission of new limited partners without the consent of the existing partners.

Depending upon the nature of the partnership, the partnership agreement may permit the assignment of partnership interests by limited partners without the consent of the other partners being required. However, if assignment is not expressly permitted by the partnership agreement, a limited partner will only be entitled to assign his interest with the consent of all the other limited partners and the general partners.

An assignee of a limited partnership interest will become a limited partner on the assignee's name being entered in the register of interests required to be maintained under the Law. On becoming a limited partner, the assignee will acquire all the rights and be subject to all the obligations of the assignor of the interest, other than certain liabilities incurred by the assignor under the Law prior to assignment, such as the liability to repay profit/ capital distributions, or liabilities incurred by reason of taking part in the management of the partnership. These types of liabilities will remain with the assignor notwithstanding anything to the contrary in the partnership agreement or any other agreement.

Third Party Dealing with a Limited Partnership

There are a number of provisions in the Law which are relevant to the position of a third party dealing with a partnership. In particular, the Law provides as follows:-

- Where a general partner executes a document on behalf of a limited partnership it is conclusively presumed in favour of a third party that the general partner has the authority under which he purports to act and that the document has been validly executed. In order to be able to rely on this provision it is important that third parties ensure that documents are expressed to be executed by a general partner "on behalf of the partnership". This is also important in order to ensure that the third party will have recourse to the assets of the limited partnership itself, and will not be adjudged to be a creditor only of the general partner in its personal capacity, which would mean that the third party would have no claim against the property of the limited partnership.

- Legal proceedings against a limited partnership must be instituted against any one or more of the general partners only and not against any of the limited partners. Service can be effected either by delivery to the general partner or by post or delivery to the registered office of the limited partnership. No judgment may be enforced against the property of a limited partnership unless such judgment has been granted against a general partner in his capacity as a general partner of the partnership.
- As referred to above, a limited partner will not be liable to a third party for the debts of the partnership unless the third party had actual knowledge that the limited partner was participating in the management of the limited partnership, and the third party reasonably believed the limited partner to be a general partner.

Maintenance of records and Accounts

The Law requires that certain records be kept at the registered office of the limited partnership and provides that the records are prima facie evidence of the particulars required to be contained therein. These records must be updated within 21 days of any change of particulars. The records required to be kept include the following:-

- a register of each limited partner showing his full name and address and the percentage interest or number and class of units held in the partnership;
- a copy of the partnership declaration and agreement;
- statements of the amount and dates of contributions made, and agreed to be made, by each limited partner;
- a statement of the amounts and dates of contributions returned to limited partners.

Any change in the particulars of the partnership declaration filed with the Registrar of Limited Partnerships must be notified to the Registrar within 21 days and the Registrar will then issue a certificate of registration of the change on payment of the prescribed fee. This would include any change in the general partner, registered office or the name of the partnership. In the case of a change of registered office, and we assume also the name (although the latter is not clear), the change will only be effective on registration of the notice.

Limited partnerships are required under the Law to maintain accounting records which are sufficient to show and explain its transactions and are such as to disclose with reasonable accuracy at any time the financial position of the partnership. There is no requirement to produce or file accounts or to appoint auditors unless the partnership agreement provides for this.

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Dissolution of a Limited Partnership

The partnership agreement will normally set out the conditions and procedure for dissolution of the partnership, and it is the responsibility of the general partner under the Law to wind-up the affairs of the partnership. Dissolution will not be effective until a statement of dissolution together with the prescribed fee has been delivered to the Registrar of Limited Partnerships who will then cancel the declaration. A limited partnership will automatically be dissolved on the death, dissolution, bankruptcy or withdrawal of the last remaining general partner, unless the general partner is replaced within ninety days of the dissolution of the partnership, in which case the dissolution will not be effective and the partnership will continue.

If the general partner is not replaced within the ninety day period the partnership will be dissolved in accordance with the partnership agreement, or in accordance with the directions of the Court if an application to the Court is made by a limited partner or a creditor. On such a dissolution a statement of dissolution must be signed by a limited partner and filed with the Registrar of Limited Partnerships who will then cancel the declaration.

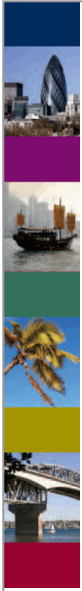
Notwithstanding the terms of the partnership agreement, it is open to a partner to apply to the Court to dissolve a limited partnership on the grounds that it is being conducted in a manner prejudicial to the activities of the limited partnership or oppressive to one or more limited partners or alternatively that it would otherwise be just and equitable to dissolve the partnership.

On dissolution of a limited partnership, the assets of the partnership will be distributed first to satisfy creditors, and then in accordance with the partnership agreement or any other subsequent agreement between the partners. In the absence of any agreement regulating distributions on dissolution, the Law provides a specific order and priority for distributions amongst general and limited partners.

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