

## PARTNERSHIP ASSET OR NOT? EXEMPTED LIMITED PARTNERSHIPS AND DERIVATIVE CLAIMS

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Section 33 of the Exempted Limited Partnership Act (2021 Revision) (the "ELP Act")¹ sets out the general rule to the effect that, "ordinarily, actions for and on behalf of an ELP [exempted limited partnership] must by statute be brought by the general partner of that ELP" and "a claim belonging to a limited partnership must be brought by the GP [general partner] acting for and on behalf of the ELP".² Exceptionally, however, a derivative action may be brought in respect of an ELP if a GP has,

"without cause, failed or refused to institute proceedings".3

The test of "without cause" is not to be equated with the "special circumstances" test that applies –

for example – in the trusts context (although, "consideration of whether there are special circumstances is likely in most cases to be of considerable assistance in determining whether the decision is 'without cause'").4

Section 33 is, as a matter of statutory interpretation, strictly concerned with when, and in what circumstances, a limited partner ("LP") may sue or be sued in its capacity as a partner in an ELP.<sup>5</sup> That said, the section has no application to direct claims that may be brought by an LP in respect of its own cause of action such as it may have as against (and for example) a GP.<sup>6</sup> As such, before an LP may bring a claim derivatively for and on behalf of an ELP in which it is a partner, the ELP must itself have a claim in respect of which it may be said to have suffered loss.<sup>7</sup>



It is in this context that the significance of an ELP's lack of corporate legal personality recently arose for consideration. In the Kuwait Ports case, 8 the issue was whether the ELP, as "an entity [that] does not exist at

- Unless otherwise stated, all references to sections of legislation are to sections of the ELP Act.
- 2 Both submissions were accepted by the Cayman Islands Court of Appeal ("CICA") in Kuwait Ports Authority v Port Link GP Ltd (Unreported, 20 January 2023) ("Kuwait Ports (CA)") at [21].
- 3 Section 33(3).
- 4 Kuwait Ports (CA) at [98].
- The section does not operate as a rule prohibiting an ELP from suing or being sued in its own name: Country Garden (Hong Kong) Development Company Ltd and Five Others v Formation Group (Cayman) Fund I L.P. [2022] 1 CILR 594.
- 6 Kuwait Ports (CA) at [21].
- 7 Kuwait Ports (CA) at [141].
- In Kuwait Ports Authority v Port Link GP Ltd [2022] 1 CILR 12 ("Kuwait Ports"), upheld in Kuwait Ports (CA).

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law",9 could incur loss.10

The judge at first instance thought not, holding that,

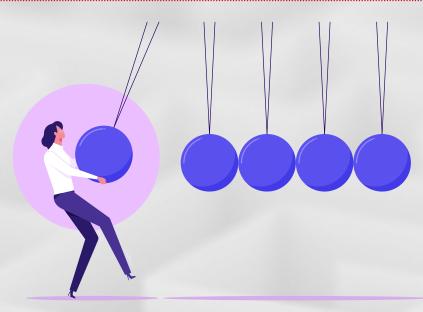
"where an ELP is alleged to have suffered loss, as in this case, that is the loss of each of the limited partners".11

This finding was not appealed but the CICA stressed that it was, "not to be taken as agreeing that this is correct".12 The CICA referred first to the statutory trust arising pursuant to s.16(1), under which the "GP of an ELP holds its [i.e., the ELP's] assets on trust for all the limited partners". 13 In the case of a trust, a trustee's breach of trust may cause a loss to the trust fund,14 and a beneficiary of a subsisting trust may bring a claim to recover that loss.15 The remedy is for an order to "restore to the trust what ought to have been there".16 The CICA said the same approach and remedy was equally applicable in the case of the statutory trust created pursuant to s.16(1), concluding that "in proceedings against the GP, a limited partner can recover for loss suffered by the breach of the statutory trust but that the remedy would be the restoration of the ELP's fund thus compensating the direct losses suffered by all the constituent limited partners".17



Secondly, the CICA referred to the principle that a successor trustee may bring a claim against a former trustee

- 9 Kuwait Ports at [63].
- 10 Kuwait Ports (CA) at [142].
- 11 Kuwait Ports at [63].
- 12 Kuwait Ports (CA) at [145].
- 13 Kuwait Ports (CA) at [56].
- 14 Lewin on Trusts (20th Ed., 2023) ("Lewin"), at [41-002].
- 15 Lewin, at [41-010] and [41-071].
- 16 Kuwait Ports (CA) at [57] citing Target Holdings Limited v Redferns [1996] AC 421. And see Lewin, at [41-010].
- 17 Kuwait Ports (CA) at [59].
- 18 Lewin, at [41-080].
- 19 Kuwait Ports (CA) at [145].
- 20 Lewin, at [47-007] referring to claims against third party advisers to the trustee. See also Bayley v SG Associates [2014] EWHC 782 (Ch) at [47]. This article assumes the position is the same when the putative claim is against a defaulting trustee.
- 21 Bradstock Trustee Services Ltd v Nabarro Nathanson [1995] 1 W.L.R. 1405 at page 1411F
- 22 HR v. JAPT [1997] Pens. L.R. 99 at [78].
- 23 Young v Murphy [1996] 1 VR 279 at page 317.
- 24 Importantly, not all contracts made by trustees, are necessarily made by them in the course of the administration. A contract may be made for private purposes as opposed to being made in the management of the trust estate: Young v Murphy at page 291.
- 25 Young v Murphy at page 317. Bayley v SG Associates [2014] EWHC 782 (Ch); [2014] W.T.L.R. 1315 at [51]. See also Royal Brunei Airlines v Tan [1995] 2 AC 378, at page 391F.



for breach of trust and for restoration of the trust fund. 18 "Thus", the CICA concluded, "even though like an ELP, a trust is not a separate legal entity, it can properly be said that the trust as well as a beneficiary has a claim against a trustee for breach of trust"

(emphasis added).<sup>19</sup> By analogy, the CICA appeared to consider that an ELP could have a claim against a GP.

In a trust context, whether a derivative action is possible appears to depend on whether the cause of action can be considered trust property.<sup>20</sup> If it cannot, a beneficiary has no ability to bring a claim derivatively on behalf of the trust.<sup>21</sup> If, as the CICA said in the Kuwait Ports case, it is, "strongly arguable that the position is the same in relation to an ELP".

then it is submitted that precisely the same question must be posed under s.33(3), namely: is the claim which the LP seeks to bring properly to be considered as being partnership property? Only if that question is answered in the affirmative will it become necessary to consider the "without cause" test. Whether a,

"particular chose in action is or is not a trust asset involves no contest involving high principles and great authorities but rather an examination of the particular facts of the particular case",<sup>22</sup>

including examination of what, if any, is the connection between the cause of action and the administration of the trust and the nature and extent of any such connection.<sup>23</sup> In this context, it may be necessary to differentiate between claims against third parties and claims against the incumbent (defaulting) trustee.

Claims of the former type can quite clearly constitute trust property. For example, when a contract is made by the trustee in the course of the administration of the trust, and for the purpose of the trust, <sup>24</sup> the benefit of the contract will itself be trust property with the result that any right of action thereunder will also constitute trust property. <sup>25</sup> By parity of reasoning, an

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ELP's claim against a manager under a management agreement entered into by the GP on behalf of the ELP under s.14(2),<sup>26</sup> appears clearly to be partnership property (in the English case of Henderson PFI Secondary Fund II LLP v. Henderson Equity Partners (GP) Ltd. [2013] QB 93 there was no dispute that the claim against the manager under the management deed was a partnership asset, "owned jointly by the partners" [26]).

The position as regards claims in the latter category (i.e., against a trustee), is less clear. In the Henderson case, the judge held that the partnership had no claim against the GP.27 It was that finding which the CICA gave emphasis to in the Kuwait Ports case.28 Drawing an analogy with a trust, the CICA thought that the trust's claim for breach of trust could, "be considered as an asset of the trust",29 emphasising the fact that any sums recovered would be held upon the terms of the trust.30 Arguably, however, that conflates the recoveries made from a cause of action, with the cause of action itself, which distinction was drawn in Bradstock Trustee Services Ltd v Nabarro Nathanson [1995] 1 W.L.R. 1405 at page 1411F-G as follows:

"Where the action sounds in tort there can be no question of the trustees constituting themselves as trustees of a chose in action right from the moment that they first consulted the solicitors.

As I see it the claim cannot be regarded as part of the trust property, though doubtless any damages which may be recovered would be".

Trustees no doubt have the right to commence an action against cotrustees or former trustees (as well as strangers) for loss caused by a breach of trust,<sup>31</sup> but it is not clear that that cause of action constitutes trust property or that an analogous cause of action by a GP against a defaulting GP would constitute partnership property. If such a cause of action is not partnership property, that would explain why any attempt to bring such a claim derivatively would fail, not just as a matter of discretion (on the basis that any breach of duty by the GP is enforceable by the LPs, as was the case in the Kuwait Ports case)<sup>32</sup> but in limine, as a matter of jurisdiction.

Thankfully, what seems clearer is that the bringing of a derivative claim by an LP will not result in the loss of limited liability, assuming the reference to subsection (2) of s.33 in s.20(2)(h) is the drafting legacy it appears to be.<sup>33</sup>





Which section provides that, "[a]Il letters, contracts, deeds, instruments or documents whatsoever shall be entered into by or on behalf of the general partner (or any agent or delegate of the general partner) on behalf of the exempted limited partnership" (emphasis added).

<sup>27</sup> Henderson at [28]

<sup>28</sup> Kuwait Ports (CA) at [144].

<sup>29</sup> Kuwait Ports (CA) at [145].

<sup>30</sup> Kuwait Ports (CA) at [145].

<sup>31</sup> Young v Murphy at page 282. Lewin, at [41-071].

<sup>32</sup> Kuwait Ports (CA) at [149]-[151].

As originally enacted, the statutory test for a derivative action was found in s.13(2). By the Exempted Limited Partnership (Amendment) Law, 2009 s.7(3) of the Law (which section provided that a limited partner would not take part in the "conduct of the business" of the ELP within the meaning of s.7 by the conduct stipulated in s.7(3)(a)-(f)) was expanded to expressly include the taking of any action required or permitted by the partnership agreement or by law to bring, pursue, settle or terminate any action or proceedings brought pursuant to s.13(2) of the statute. That right is now enshrined in s.33(3) of the ELP Act.