



HM Treasury

# **Proposal on using Legislative Reform Order to change partnership legislation for private equity investments**

**Consultation on draft legislation**

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July 2015





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Proposal on using Legislative  
Reform Order to change  
partnership legislation for private  
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# 1 Introduction

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**1.1** The UK is a leading centre for fund management with around 35% of all assets managed in Europe managed out of the UK.

**1.2** The UK investment management industry is an important and successful part of the economy. It contributes 1% of UK GDP and about the same proportion in UK tax revenues and is a significant employer, with over 50,000 people employed in the sector.

**1.3** The private equity and venture capital industry is important to the UK economy as a source of long term capital for innovative companies with high potential for growth.

**1.4** Data from the European Private Equity and Venture Capital Association (EVCA) shows that the UK private equity and venture capital industry continues to be the largest in Europe. Out of the €53.6 billion raised in Europe in 2013, about €34.4 billion (64.2%) was raised by funds managed in the UK.

**1.5** In order to further reinforce the UK's position as a global centre for fund management, at Budget 2013, the government launched the Investment Management Strategy, which included a package of measures to improve the UK's competitiveness. These measures included a commitment to consult on technical changes to the partnerships legislation as it applied to funds with a view to removing unnecessary legal complexity and administrative burdens

**1.6** This consultation sets out proposed amendments to the Limited Partnership Act 1907, which are intended to ensure that the UK limited partnership remains the market standard structure for European private equity and venture capital funds as well as many other types of private fund in an increasingly competitive global market.

**1.7** Comments are invited on the proposals and draft order to help inform the final shape of the proposals and the related legislation.





## 2 Background and scope

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### The need for reform

**2.1** At Budget 2013 the government announced that it would consult on changes to limited partnership legislation to more effectively accommodate the use of limited partnerships for private equity investments.

**2.2** The UK limited partnership is the most commonly used structure for European private equity and venture capital funds, as well as various other types of private fund. The main benefits of the limited partnership structure are its flexibility, its transparency for UK tax purposes and the limited liability protection that it offers to investors.

**2.3** The UK limited partnership structure is governed principally by the Partnership Act 1890, the Limited Partnerships Act 1907 and rules of equity and common law.

**2.4** These two Acts legislate for the establishment and operation of partnerships and have remained largely unchanged for much of the 20<sup>th</sup> century.

**2.5** As a result, existing UK limited partnership legislation has not been able to accommodate fully the needs of private equity and venture capital funds, a relatively modern international industry that developed in the United States in the latter half of the 20<sup>th</sup> century.

**2.6** Further, other jurisdictions in which such funds are typically domiciled either already have, or are in the process of introducing, laws to ensure that private fund sponsors have the flexibility to structure funds in the most efficient way, and to avoid incurring unnecessary costs and administrative burdens. Without such changes, the UK risks becoming a less attractive domicile for funds when compared to other jurisdictions.

**2.7** The proposed amendments are aligned with government objectives to maintain and enhance the UK's competitiveness as a centre for fund domicile and to minimise costs to investors. The proposed amendments expand investor choice while maintaining strong investor protection and the integrity of the regulatory regime.

**2.8** While the government remains committed to exploring the possibility of allowing funds in the UK outside Scotland to elect to have separate legal personality, it is not possible to do so using this Legislative Reform Order. Such a change would be a much more fundamental change to the nature of limited partnerships in England, Wales and Northern Ireland, and further work is needed to explore the implications and legislative changes required.

### History of partnership proposals

**2.9** In November 2003, the Law Commission published a report on partnership law. In 2006 the then government announced that it intended to implement the Law Commission's recommendations specifically relating to limited partnerships.

**2.10** In August 2008, the then Department for Business Enterprise and Regulatory Reform (BERR) published a consultation on a Legislative Reform Order which was largely based on the Law Commission's recommendations for the reform of limited partnership law, and in March 2009 they published their response to the consultation.

**2.11** Their response explained that in light of stakeholder responses, it was not possible to continue with the comprehensive Legislative Reform Order at the time. The proposed

amendments in the BERR consultation were not focused specifically on investment funds and would have required broad and complex changes to limited partnership legislation.

## About this consultation

**2.12** This consultation seeks to understand the impacts of the proposed amendments to the Limited Partnerships Act 1907 so far as they apply to UK limited partnerships formed as part of a private fund structure.

**2.13** The aim of these amendments is to eliminate many of the uncertainties and inconveniences associated with existing UK limited partnership law so as to ensure that the UK limited partnership remains the market standard structure for European private equity and venture capital funds and other types of private fund.

**2.14** The government is therefore seeking views on how well these amendments meet the aims stated above and evidence supporting your views.

**2.15** The proposed amendments will apply to a UK limited partnership that is a “collective investment scheme” (as defined in section 235 of the Financial Services and Markets Act 2000) but is not a scheme authorised by the Financial Conduct Authority (FCA).

**2.16** These criteria are intended to restrict the UK limited partnerships affected by the proposed amendments to those partnerships formed as part of a private fund structure.

**2.17** These structures may include a number of entities that use limited partnerships including the main fund vehicle, a parallel fund, a feeder fund, a co-investment vehicle and a carried interest vehicle.

**2.18** The changes are proposed to be made through a Legislative Reform Order, under the Legislative and Regulatory Reform Act 2006.

**2.19** More information about the proposed changes can be found in Chapter 3.

## What is a Legislative Reform Order?

**2.20** A Legislative Reform Order (LRO) is a statutory instrument which can amend primary legislation under the powers in the Legislative and Regulatory Reform Act (LRRA) 2006.

**2.21** LROs are deregulatory and are used to remove or reduce burdens resulting from legislation, as well as improve the way regulatory functions are carried out.

**2.22** Under section 1 of the LRRA, a minister of the crown can make a LRO for the purpose of removing or reducing any burden to which any person is subject as a result of any legislation. A burden is defined as:

- a financial cost
- an administrative inconvenience
- an obstacle to efficiency, productivity or profitability; or
- a sanction, criminal or otherwise, which affects the carrying on of any lawful activity

**2.23** Any LRO must meet the preconditions set out in section 3 of the LRRA:

- there are no non-legislative alternatives that will achieve the intended outcome of the provision
- the effect of the provision is proportionate to the policy objective

- the provision strikes a fair balance between the public interest and the interests of any person adversely affected by it
- the provision does not remove any necessary protection
- the provision does not prevent anyone from continuing to exercise any right or freedom which they might reasonably expect to continue or exercise
- the provision is not constitutionally significant
- where a provision will restate an enactment, it makes the law more accessible or more easily understood

**2.24** A LRO cannot be used to:

- remove burdens which fall solely on ministers or government departments, except where the burden affects the minister or department in the exercise of a regulatory function
- confer or transfer any function of legislation on anyone other than a minister; persons or bodies that have statutory functions conferred on or transferred to them by an enactment; or a body or office which has been created by the LRO itself
- impose, abolish or vary taxation
- create a new criminal offence or increase a penalty for an existing offence above certain limits. It can re-state existing penalties over those limits
- provide authorisation for forcible entry, search or seizure or for the compelling of giving of evidence unless the LRO repeals provisions to that effect and the new provision is exercisable for similar purposes; or
- amend or repeal any provision of Part 1 of the LRA or the Human Rights Act 1998

## How to contribute

**2.25** The government is seeking views from the fund management sector as well as other interested parties, in response to the questions set out in this paper.

**2.26** If you wish to contribute or have any questions, please contact: [lp.consultation@HMTreasury.gsi.gov.uk](mailto:lp.consultation@HMTreasury.gsi.gov.uk). Where possible, please provide evidence to support your answer.

**2.27** The consultation closes on Monday 5 October 2015

## Non-disclosure of responses

**2.28** Section 14(3) of the LRA provides what should happen when someone responding to the consultation exercise on a proposed LRO requests that their response should not be disclosed.

**2.29** The name of the person who has made representations will always be disclosed to Parliament. If you ask for your representation not to be disclosed, the minister must not disclose any confidential information in that representation. Alternatively, the minister may disclose the content of the representation in such a way as to preserve the confidentiality of such information.

**2.30** If you give information about a third party which the minister believes may be damaging to the interests of that third party, the minister does not have to pass on such information to

Parliament if they are unable to obtain the consent of the third party to disclose. This applies whether or not you ask for your representation not to be disclosed.

**2.31** The Scrutiny Committees may, however, be given access on request to all representations as originally submitted, as a safeguard against improper influence being brought to bear on ministers in their formulation of legislative reform orders.

# 3 Specific amendments to UK limited partnership law

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**3.1** This chapter sets out the amendments to UK limited partnership law proposed to be made through a legislative reform order. The changes cover registration issues and on-going filing and notification requirements; the role, function and rights of limited partners; and obligations of, and restrictions on, limited partners in respect of capital.

## Designation as a private fund limited partnership

**3.2** It is intended that the changes proposed in this chapter should only apply to those limited partnerships which are private fund vehicles. The draft order therefore includes a process for the designation on the register of limited partnerships (the “register”) of those limited partnerships which are private fund vehicles at the point of registration. This will make it possible to identify from the register (and from the certificate issued to the partnership by the registrar) those limited partnerships to which the amended regime applies. This is dealt with at article 2(6), (7)(a) and (8) of the draft order.

**3.3** The draft order also proposes, at article 3, an option for existing limited partnerships to become designated as private fund limited partnerships within the first year of the changes coming into effect.

Q1. What are your views on the proposed process for designating private fund limited partnerships?

## Amendments to the register

**3.4** There is currently no procedure for removing a limited partnership from the register. Private equity and venture capital funds often have a fixed life cycle and are wound down at the end of this period. However, even after it has been wound down, a partnership would remain on the register in perpetuity, meaning that the register becomes progressively out of date and the names of dissolved limited partnerships are not able to be used again.

**3.5** The proposed changes in article 2(11) of the draft order would grant the Registrar of Companies a power to remove such entries on application by the partnership or where the partnership is no longer operating. This is similar to the power with respect to companies under the Companies Act 2006.

Q2. What are your views on the measures to allow the registrar to remove from the register entries for inactive private fund limited partnerships?

## White list activities for limited partners

**3.6** Under the Limited Partnerships Act 1907 a limited partner may not “take part in the management of the partnership business” or it will be liable for all the debts and obligations of the limited partnership incurred while it takes part in the management as though it were a

general partner. However the Act does not state expressly what actions are, or are not, to be considered to amount to taking part in the management of the partnership business.

**3.7** Although investors in private equity and venture capital are generally passive, they may be actively involved in monitoring and assessing the performance of the fund itself and its investments.

**3.8** The exact nature of involvement varies from fund to fund but it will commonly include consultation rights, both direct and indirect through representatives appointed or nominated by limited partners to some sort of advisory body, although not in respect of day to day management issues.

**3.9** It may also extend to more substantive protection rights, for example to approve investments that would otherwise breach the limited partnership's investment restrictions set out in its partnership agreement.

**3.10** The proposed changes in article 2(4)(a) and (5) of the draft order introduce a new section 6A of the Limited Partnerships Act, setting out a non-exhaustive list of activities that a limited partner in a private fund limited partnership may undertake without being considered to take part in the management of the business, and therefore without losing their limited liability.

**3.11** This list is intended to provide greater certainty and allow an investor to monitor their investments without risking losing their limited liability.

Q3. Is there uncertainty around what actions constitute "taking part in the management of the partnership business"?

Q4. Does the proposed list in the draft order cover the type of activities a limited partner is likely to undertake in monitoring and assessing the performance of a private fund? Are there any activities that should not be on the list?

## Capital contributions

**3.12** The Limited Partnership Act 1907 requires that a limited partner "shall at the time of entering into such partnership contribute thereto a sum or sums of money as capital or property valued at a stated amount." There is no stipulated amount of capital that a partner must contribute.

**3.13** In the context of private equity and venture capital funds formed as limited partnerships, it is typical for an investor to have its total funding commitment split between a nominal capital contribution (to meet the legislative requirement) and a contractual undertaking to fund the balance of its commitment by way of interest free loans or advances.

**3.14** The Limited Partnership Act 1907 also states that a limited partner may not "during the continuance of the partnership, either directly or indirectly, draw out or receive back any part of his contribution" and that if a limited partner does withdraw their capital during the life of the partnership they "shall be liable for the debts and obligations of the [limited partnership] up to the amount so drawn out or received back." But these restrictions only apply to capital contributions. In practice, investors who might want to withdraw part of their contribution prior to the end of the life of the fund, without being liable for any debts and obligations of the fund, simply make the majority of their commitment through loans rather than a capital investment. This results in considerable complications and, moreover, unnecessary confusion for those unfamiliar with UK limited partnership law. It is also not clear what purpose is served by requiring that a limited partner make a capital contribution no matter how small.

**3.15** It is proposed to remove the requirement for limited partners in private funds to make a capital contribution. We also propose to remove the liability of limited partners in private funds for capital contributions that have been withdrawn. This is dealt with at article 2(3) of the draft order.

Q5. Is any purpose served by the requirement that a limited partner make a capital contribution, no matter how nominal?

Q6. Should a limited partner be allowed to withdraw their capital during the life of partnership? If so, should they remain liable for the amount withdrawn?

Q7. If limited partners are allowed to withdraw their capital, should any other conditions be put in place?

## Winding up a limited partnership

**3.16** It is common practice for private equity and venture capital funds formed as partnerships to be granted the right to remove the sole general partner and dissolve the partnership in certain situations.

**3.17** Where the sole general partner of a limited partnership is removed and the partnership is to be dissolved, the remaining limited partners must apply for a court order confirming that the affairs of the partnership be wound up under the supervision of the court. This imposes significant delays and administrative burdens on the limited partners, many of whom may operate from outside of the UK.

**3.18** We propose to allow the partners (and where there is no general partner, just the limited partners) in a private fund to agree among themselves who should wind up the limited partnership without having to obtain a court order. This is dealt with at article 2(4)(c) of the draft order.

Q8. Should the limited partners in a private fund be allowed to agree among themselves who should wind up the partnership without having to obtain a court order?

## Registration of a limited partnership

**3.19** A limited partner only benefits from limited liability following the establishment of a limited partnership and the certificate of registration is proof that the limited partnership came into existence on the date of registration. In an application for registration as a limited partnership, the following details must be specified:

- 1 The general nature of the partnership business.
- 2 The name of each general partner and of each limited partner.
- 3 The amount of each limited partner's capital contribution (and whether paid in cash or in another form).
- 4 The address of the proposed principal place of business of the limited partnership.
- 5 The term for which the limited partnership is to be entered into.

**3.20** Any change in the particulars listed above must be registered within 7 days of the change.

**3.21** A limited partner is prohibited from taking part in the management of the partnership business and should any unsatisfied liabilities arise, any counterparties would not have recourse to the limited partners, making the need to include the capital contribution of each limited partner unnecessary.

**3.22** Further, disclosure of each limited partner's capital contribution may enable tracking by any person of investment decisions which may be market sensitive.

**3.23** In order to reduce the administrative burden of registering a private fund as a limited partnership and to protect investors' privacy, we propose to simplify the process by removing some of the requirements for the details that must be specified when a private fund established as a limited partnership is registered, and when such details change. These details include the amount of capital contributed. The proposals are set out at article 2(7)(c) and (9) of the draft order.

Q9. Should the requirement to register the amount of capital be removed for private funds?

Q10. Should the requirement to register the general nature of the limited partnership's business and the term of the limited partnership be removed for private funds?

## Gazette notices

**3.24** Under section 10 of the Limited Partnerships Act 1907, if a general partner becomes a limited partner or a limited partner assigns its interest in a limited partnership to another person, it will only have effect on being advertised in the London, Edinburgh or Belfast Gazette (as appropriate).

**3.25** Article 2(10) of the draft order proposes to remove the requirement for the advertisement of such changes in respect of private funds to be advertised in the Gazette.

Q11. What are your views on the on the requirement to advertise a notice in the Gazette? Does is present any specific problems? Is it appropriate to remove the requirement for private funds?

## Exemption from statutory duties

**3.26** Under current legislation, a limited partner is subject to certain duties which apply to partners generally, but which appear inconsistent with the position of a largely passive investor who may have investments in a number of funds, some of which may fund competing businesses. This is particularly the case for the duties in section 28 of the Partnership Act 1890 (duty to render accounts and information to other partners) and section 30 of that Act (duty to account for profits made in competing businesses).

**3.27** The draft order therefore includes a provision at article 2(4)(d) exempting limited partners in private funds from these duties.

Q12. Should the duties to render accounts and information, and to account for profits made in competing businesses, be removed for limited partners in private funds?



## Interaction with authorised fund limited partnerships

**3.28** The Collective Investment in Transferable Securities (Contractual Scheme) Regulations 2013 enable limited partnerships to be used as vehicles for funds authorised by the Financial Conduct Authority. Regulation 16 of those Regulations made modifications to the Limited Partnerships Act 1907 as it applies to such authorised schemes. The amendments proposed to the 1907 Act for private fund limited partnerships amend some of the provisions in the 1907 Act which are modified by the 2013 Regulations, but take a different approach in some respects.

**3.29** In order to preserve the effect of the 2013 Regulations after amendments have been made to the Limited Partnership Act 1907 by the draft order, article 5 of the draft order makes consequential amendments to regulation 16 of the 2013 Regulations.

Q13. Do you have any comment on the interaction of the legislation for authorised fund limited partnerships and the proposed legislation for private fund limited partnerships?



## 4 Summary of questions

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- Q1. What are your views on the proposed process for designating private fund limited partnerships?
- Q2. What are your views on the measures to allow the registrar to remove from the register entries for inactive private fund limited partnerships?
- Q3. Is there uncertainty around what actions constitute “taking part in the management of the partnership business”?
- Q4. Does the proposed list in the draft order cover the type of activities a limited partner is likely to undertake in monitoring and assessing the performance of a private fund? Are there any activities that should not be on the list?
- Q5. Is any purpose served by the requirement that a limited partner make a capital contribution, no matter how nominal?
- Q6. Should a limited partner be allowed to withdraw their capital during the life of the partnership? If so, should they remain liable for the amount withdrawn?
- Q7. If limited partners are allowed to withdraw their capital, should any other conditions be put in place?
- Q8. Should the limited partners in a private fund be allowed to agree among themselves who should wind up the partnership without having to obtain a court order?
- Q9. Should the requirement to register the amount of capital be removed for private funds?
- Q10. Should the requirement to register the general nature of the limited partnership’s business and the term of the limited partnership be removed for private funds?
- Q11. What are your views on the on the requirement to advertise a notice in the Gazette? Does it present any specific problems? Is it appropriate to remove the requirement for private funds?
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## **HM Treasury contacts**

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If you require this information in an alternative  
format or have general enquiries about  
HM Treasury and its work, contact:

Correspondence Team  
HM Treasury  
1 Horse Guards Road  
London  
SW1A 2HQ

Tel: 020 7270 5000

Email: [public.enquiries@hmtreasury.gsi.gov.uk](mailto:public.enquiries@hmtreasury.gsi.gov.uk)