

# Voluntary Liquidations and Exempted Limited Partnerships: Are you winding me up?

UPDATE

Update prepared by Simon Dickson (Cayman Islands)

Exempted Limited Partnerships (ELPs) are the favoured vehicle for private equity funds structuring deals through the Cayman Islands. In recent years, the mechanism by which an ELP can be wound up has come under scrutiny. Conflicting decisions in respect of the official liquidation of ELPs has created doubt as to whether an ELP can be wound up or just the General Partner (GP) and whether the provisions of Part V of the Companies Act (2023 Revision) (Part V), which deal with corporate insolvency, applies to ELPs.

With respect to voluntary liquidations (VLs), the position is also confused. Challenges have been made to the power of the Court to appoint a voluntary liquidator and give directions as to the conduct of the liquidation. The recent decision of *In the Matter of One Thousand and One Voices Africa Fund I, L.P.*<sup>1</sup> has gone some way to clarify these issues. However, as this article will show, the extent of the Court's powers remains in doubt.

## The Appointment and Replacement of a Voluntary Liquidator

A VL is commenced in accordance with the provisions of the limited partnership agreement (LPA). In most cases, the GP is nominated in the LPA as the voluntary liquidator. Where an investment has failed or where there is little financial benefit to the GP in conducting the liquidation, tensions tend to arise leading the Limited Partners (LPs) to seek orders replacing the GP with a professional liquidator.

The power of the Court to replace the GP is found at section 36(13) of the Exempted Limited Partnership Act (2021 Revision) (the Act). Section 36(13) provides that the affairs of the partnership shall be wound up by the GP or other person appointed pursuant to the partnership agreement '*unless the court otherwise orders on the application of any partner, creditor or liquidator [of the ELP] pursuant to subsection (3)(g)*'. Section 36(3)(g) is the section which empowers the court to '*make orders and give directions for the winding up and dissolution of an exempted limited partnership as may be just and equitable*'.

## In the Matter of One Thousand and One Voices Africa Fund I, L.P.

Here an application was made pursuant to section 36(13) of the Act to replace the GP with a professional liquidator. The application had the support of 97% of the LPs. The GP opposed the application on two main limbs: first that the Court had no power to interfere with a VL conducted under the LPA and second that the Court's powers under section 36(13) related only to compulsory liquidations and not to VLs.

With respect to the first limb, the argument was simple. Section 36(1) states that an ELP shall be voluntarily wound up in accordance with the provisions of the partnership agreement. That being so, the Court had no power to interfere with the provisions of the LPA and replace the GP. The Court was quick to dismiss this argument. Section 36(1) was not a free-standing provision. The subsections of section 36 explicitly or implicitly applied to VLs commenced under subsection (1) and were superimposed over any regime set out in the LPA. Section 36(13) was no different and applied to VLs commenced under section 36(1).

<sup>1</sup> *In the Matter of One Thousand and One Voices Africa Fund I* (Unreported, 24 April 2024).

As regards the second limb, the argument was more intriguing and afforded moderately more respect. The argument ran that the Court was empowered to appoint someone other than the GP as liquidator pursuant to its powers under section 36(3)(g). Section 36(3)(g) deals with the power of the Court to 'make orders and give directions for the winding up of the ELP as may be just and equitable.' (emphasis added).

Such wording properly construed, it was argued, suggests that section 36(3)(g) is not dealing with the power to make orders and give directions in a VL, but rather orders and directions for the compulsory winding up of the ELP under Part V. If that construction was correct, then section 36(13) is not dealing with the replacement of a voluntary liquidator, but the making of orders in a compulsory liquidation for the appointment of official liquidators in place of the voluntary liquidator.

The Court dismissed this argument partly on the basis that some legislative schemes are drafted with more precision than others, and that section 36 was not at the top of the precision scale. However, the Court acknowledged that this was not sufficient. Instead, the Court looked to see whether any other provision of the Act shed light on section 36(3)(g). The Court applied section 36(9) of the Act. Section 36(9) provides that subject to the LPA, if a GP is not elected within 90 days of the service of a notice of withdrawal, the ELP shall be wound up in accordance with the partnership agreement or the orders or directions the court may make or give in accordance with subsection (3)(g) (emphasis added).

The Court held that this provision expressly contemplates that where a GP is not replaced and there is an automatic winding up, the VL may be administered or managed, not only in accordance with the LPA, but also (presumably where the LPA is silent) in accordance with orders and directions given under section 36(3)(g). If this was the case, then the power to give directions under section 36(3)(g) must expressly apply to VLs.

### Clear Legislative Intention

Having disposed of these arguments, the Court made clear that the time for GPs challenging the power of the Court to replace them as voluntary liquidators had come to an end. The Court found it was manifestly clear that the Court had a general power to supervise VLs and an unfettered discretion to replace the GP with an alternative liquidator.

The Court decried the opposition to this application, saying it had an all too familiar ring. In the Court's view, a GP who has lost the confidence of the investors should demonstrate its probity by stepping aside and demonstrating confidence that their impugned management will be vindicated by independent scrutiny. By hanging on at all costs, the Court said, a GP gave the distinct impression that the determination to cling to office is motivated by self-interest at best or the desire to forestall independent investigation into suspect dealings at worst.

### The Extent of the Court's Powers to give Directions

Whilst the Court was adamant that it had a general power to supervise VLs and give directions, the extent of those powers remains at issue.

The powers of a voluntary liquidator in a corporate insolvency are set out in Part V. The key provisions at section 132 and section 133, allow the Court to convert a VL into an Official Liquidation and provide the liquidator with all the associated powers (a **Supervision Order**). However, these provisions do not apply to a VL of an ELP.

*In the Matter of ECM Straits Fund I, LP*,<sup>2</sup> the Court was asked to make directions affording the liquidators powers identical to those under a Supervision Order.

The Court acknowledged, in a short judgment, that the entire scheme for Supervision Orders was disapplied under the Act. Despite this, however, and on the basis of the legislative history and the fact that the Act did not set out a broad mechanism to govern VLs, the Court must have the jurisdiction to grant such powers as are necessary to conduct the VL. Accordingly, the Court made directions creating a de facto Supervision Order, thereby converting the VL into an Official Liquidation. The decision was cited with approval in *One Thousand and One Voices*.<sup>3</sup>

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<sup>2</sup> (Unreported, 20 December 2022, Parker J).

<sup>3</sup> See paras 7 and 23.

This decision must be open to question and any application seeking Part V powers should consider carefully whether this decision is correct. Simply because the Act does not contain a broad mechanism for a VL does not mean that one can be imported.

There may, in fact, be a very good reason why the scheme for Supervision Orders is disapplied. At least one branch of the law suggests that an ELP cannot be wound up by a creditor.<sup>4</sup> Such proceedings may only be brought against the GP. A Supervision Order would have the opposite effect in that it can be brought by a creditor and allows for the liquidation to continue as if the Court had made a winding up order against the ELP. Accordingly, a Supervision Order would be inconsistent with the Act and allow a creditor petition against the ELP by the back door.

Further, it is incorrect to state that the Act does not contain a mechanism for VLs. A liquidator can ask the Court to exercise any of the Court's powers under Part V to assist a liquidation, thereby allowing a liquidator access on a case-by-case basis to many of the relevant powers. Whilst this is different from allowing unfettered access to an official liquidator's powers, it is a mechanism of some utility.

Finally, it is not at all clear why a liquidator should have access to such powers. Where an LP is dissatisfied with the liquidator or believes that the state of affairs in the ELP is such that a VL is inappropriate it may, if the grounds exist, bring a Petition on the just and equitable basis to appoint an official liquidator with all of the requisite powers.<sup>5</sup> That, however, should be a decision for the LP and based on the correct burden of proof, and not a decision made under the disapplied provisions of Part V.

## Conclusion

The Courts are still finding their way with this construct and the Act is a difficult creature in that it is blending issues of partnership and company law which do not sit easily together.

Some welcome clarity has been brought to bear with respect to the power of the Court to appoint voluntary liquidators, but the application of Part V remains a vexed issue. Whilst one can understand the Court's desire to manage VLs with clarity and conformity, the Act does not easily allow for it. As is so often the case, there is no quick fix. For now, practitioners would be wise to consider if contemplating a VL, whether an alternative liquidator is necessary and if so whether the liquidation can be conducted without the powers afforded under Part V. If not, consideration should be given as to what powers the Court can grant and whether the ELP can be compulsorily wound up by the Court.

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For more on this case, please see our update '[Limited Partnerships: Cayman Court confirms jurisdiction to appoint an alternative voluntary liquidator](#)'.

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**Simon Dickson**  
Partner  
Mourant Ozannes (Cayman) LLP  
+1 345 814 9110  
simon.dickson@mourant.com

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<sup>4</sup> See *In re Padma Fund L.P.* [2021 (2) CILR 556] *cf In the Matter of Formation Group (Cayman) Fund I, L.P.* [2022 (1) CILR 594].

<sup>5</sup> The right to present a petition under Part V relies on the other branch of case law *In the Matter of Formation Group (Cayman) Fund I, L.P.* Careful consideration needs to be given as to the conflict between the two.