

Fund finance – taking security over a limited partnership interest

Insights - 20/12/2022

While subscription line facilities continue to be the most common type of financing that we see in the fund finance space, the last 12 months have seen a noticeable increase in the number of Cayman fund finance deals involving net asset value (**NAV**) facilities.

One of the key considerations that Cayman counsel must consider for NAV facilities is the form of security required by a lender and how that differs from capital call security in a typical subscription line deal. NAV facilities are secured by the assets of the fund itself which often include equity interests in Cayman vehicles that hold investments of that fund.

In a Cayman context this may involve security over limited partnership interests in a Cayman vehicle and this client briefing seeks to address the issues involved when security is granted over limited partners' interests in a Cayman exempted limited partnership (an **ELP**).

Limited partnership interests

Limited partnership interests in an ELP are recorded in a register of limited partners which is maintained by the general partner of the ELP. The register of limited partners may be inspected by any person, with the consent of the general partner, during all usual business hours. Each limited partnership interest comprises both rights and obligations under the partnership agreement and the Exempted Limited Partnership Act (Revised) (**ELP Act**).

Security

By far the most common way of securing a limited partner's partnership interest is by way of an equitable charge. It is considered an equitable charge because there is a right on the part of the secured party to call for the transfer of the limited partnership interest into the secured party's name, that is, there is a contractual right to a transfer of ownership, which equity will enforce.

An equitable charge (whether in law or in equity) does not involve the transfer of ownership of the secured assets.

Section 32(6) of the ELP Act, requires that, subject to the terms of the limited partnership agreement, the general partner must provide written consent to the grant by a limited partner of any security interest in, or the transfer of, the whole or any part of its limited partnership interest.

Any security interest over a limited partnership interest has priority in accordance with the time that written notice is validly served at the ELP's registered office under section 31(4) of the ELP Act. Section 32(9) of the ELP Act further specifies that such written notice may be given by either the grantor or the secured party. Where the grantor provides such notice to the ELP's registered office, the underlying security agreement should require that the secured party be provided with a signed copy of such notice.

Under section 32(10) of the ELP Act, such notice is not valid unless it specifies:

1. the agreement pursuant to which the security interest is granted
2. the date of the agreement
3. the parties to the agreement
4. the grantor and grantee of the security interest
5. the partnership interest or part thereof that is subject to that security interest.

Section 31(1) of the ELP Act requires the general partner to maintain a register of security interests in respect of all security interests registered and this register may be inspected by any person during all usual business hours. The secured party will typically require an updated copy of the register of security interests post-closing to reflect the security granted in its favour over the limited partnership interest.

It is advisable that the consent of the general partner to the grant of security over a limited partnership interest and to the transfer of that limited partnership interest on enforcement of the security is included as a condition precedent to any financing where such security is required.

Another common closing deliverable to any financing secured by a charge over a limited partnership interest is a signed but undated transfer of limited partnership interest (much in the same way as a signed but undated share transfer form in the case of share security) – this transfer would only be dated upon enforcement. It is always important to check the terms of the limited partnership agreement as it may also require consent from other limited partners before any security interests can be granted over other limited partnership interests or other conditions to transfer interests (which may be applicable on an enforcement).

It is not necessary to have a Cayman law governed security agreement to document security over a limited partnership interest in a Cayman vehicle and in the context of US fund finance transactions we typically see such security being subject to applicable US law, however, such security should include the Cayman specific provisions set out above.

It is also possible to take a legal charge (rather than an equitable charge) over a limited partnership interest, however, such legal charges are rarely granted in practice as secured parties are not typically comfortable taking an absolute transfer of a limited partnership interest and becoming registered as a limited partner in the register of limited partners of the ELP.

If you would like more information, please contact one of our fund finance specialists as detailed on this page.

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