Investment Limited Partnerships: A Banking & Finance Perspective

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There have been a series of reforms in Bahrain over the last couple of years in an attempt by the government to re-establish Bahrain's position as a regional financial hub in the Middle East. One such change has been the introduction of investment limited partnerships and protected cell companies (which we discussed in the December/January 2017 edition of Law Update). This article focuses on investment limited partnerships and its commercial advantages from a banking and finance perspective.

Investment Limited Partnerships ('ILP')

An investment fund is a pooled investment vehicle which acquires, holds and disposes of equity and equity related investments in unlisted companies. The investment strategy of a private equity fund will specify its target sectors (for example pharmaceutical companies) and its geographical target area (for example Europe). There are many legal structures available for such an investment fund such as a company (in Bahrain this is generally a joint stock company); an investment limited partnership or trusts and contractual arrangements. The limited partnership is the vehicle of choice worldwide for closed-ended investment funds.

The Law on Investment Limited Partnerships (Law No. 18 of 2016) was implemented on 4 August 2016 ('ILP Law'). An ILP can only undertake the Permitted Activities (which are exactly the same activities a PCC can undertake). An ILP is similar to a limited partnership company in that a general (defined as an 'Active Partner' in the ILP Law) partner's liability is unlimited and a sleeping (defined as a 'Dormant Partner' in the ILP Law) partner's liability is unlimited. ILPs are regulated by the CBB. Bahrain is now a challenger to offshore fund jurisdictions as it has a state of the art ILP Law; it is a tax advantaged regime and it has a sophisticated regulatory regime.

Management and decision making in an ILP

The general partners manage the fund or contract with the manager. The general partners sign on behalf of the fund. The limited partners cannot take part in management. There are safe harbour provisions for limited partners including:

1. holding office or interest in general partner;
2. contracting with the fund;
3. consulting with or advising the general partner;
4. reviewing and approving partnership accounts and business affairs;
5. participating in partner meetings;
6. sitting on investment boards or other committees;
7. voting on specified decisions;
8. taking certain legal actions;
9. approving changes to the partnership agreement.

Duties of the general partner

The general partners have a duty:

1. not to conduct affairs in a way prejudicial to partners;
2. to render true accounts and full information about partnership to other partners;
3. to exercise powers to meet the fund’s objectives;
4. not to compete unless specified consent is provided;
5. to disclose personal interests in accordance with partnership agreement; and
6. to compensate for any breach of duty or law.

Limited partner rights

The limited partners have the following rights:

1. limited liability;
2. access to partnership information;
3. to take certain action on behalf of the partnership;
4. compliance by the general partner with partnership agreement and the law;
5. protection from prejudicial actions; and
6. preference over general partner on distribution/dissolution.

Requirements for registration of an ILP

Registration of an ILP requires a:

1. no objection letter from the Central Bank of Bahrain (“CBB”);
2. notarised statement from general partner including:
    1. name of investment fund partnership;
    2. particulars of business;
    3. address of registered office;
    4. statement of duration;
    5. identification of general partners;
    6. statement of partners’ capital and manner of payment;
3. formal identification documents for general partnership;
4. limited partnership agreement; and
5. fee for registration and the no objection letter.

Investment Fund Partnership Agreement

An investment fund partnership agreement (“ILP Agreement”) is a written binding contract between all the partners. The ILP Agreement is filed with the CBB. The ILP Agreement must contain the following minimum information, namely:

1. the manner and timing of contributions;
2. the restrictions of transfer of interests (if any);
3. the business of the ILP;
4. any profit entitlements of the partners;

5. any restrictions on the general partner;
6. when partner meetings are to be held;
7. when the fund terminates; and
8. conflict of interest policy.

Advantages of an ILP

Limited partnerships are the most popular structure for closed ended funds internationally and its structure is understood by international fund investors. ILPs allows clear legislative backing to popular fund structure choice internationally. It also provides an additional option to fund promoters. ILPs catches up with neighbouring Gulf Cooperation Council ("GCC") jurisdictions namely Dubai, Abu Dhabi and Qatar. ILPs also permit clear options to be given on investors' rights and permits flexibility of constitutional documents.

ILPs clearly designates responsible entity for fund management and control. It allows flexibility for division of profits from a fund. It avoids corporate requirements for capital maintenance. Further, it places clear fiduciary responsibilities on the general partner. ILPs provides investors access and transparency. ILPs are the first GCC 'onshore' limited partnership.

With partnership laws being well established in common law jurisdictions, such as London, New York, and Singapore, the ILP Law allows firms in and/or from such jurisdictions to operate in Bahrain within a legal framework with which they are familiar. The ILP Law also supports investment companies in establishing financial investment funds, and enables them to access new funding mechanisms.

Conclusion

Bahrain is now a challenger to offshore fund jurisdictions as it has a state of the art limited partnership law, a tax advantaged regime and a sophisticated regulatory regime. It is hoped that the ILP Law will provide a strong boost to the financial sector in Bahrain and support growth in real estate funds, private equity funds, venture capital and technology funds, start-ups, and Shariah-compliant funds, as well as captive insurance. However, as the ILP Law and ILPs have only recently been implemented in Bahrain, it may take some time before ILPs are widely adopted and are the structure of choice for investment funds in Bahrain. Nevertheless, it is expected that ILPs will enhance Bahrain's competitiveness in the financial services sector by making it easier to structure investment activities.