



House of Commons  
Regulatory Reform Committee

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**Draft Legislative  
Reform (Private Fund  
Limited Partnerships)  
Order 2017**

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**Second Report of Session 2016–17**

*Report, together with formal minutes  
relating to the report*

*Ordered by the House of Commons to be printed  
6 March 2017*

## Regulatory Reform Committee

The Regulatory Reform Committee (previously the Deregulation and Regulatory Reform Committee) is appointed to consider and report to the House on draft Legislative Reform Orders under the Legislative and Regulatory Reform Act 2006. Its full remit is set out in S.O. No. 141, which was approved on 4 July 2007.

### Current membership

[Andrew Bridgen MP](#) (*Conservative, North West Leicestershire*) (Chair)

[Richard Fuller MP](#) (*Conservative, Bedford*)

[Rebecca Harris MP](#) (*Conservative, Castle Point*)

[Simon Hoare MP](#) (*Conservative, North Dorset*)

[Dr Rupa Huq MP](#) (*Labour, Ealing Central and Acton*)

[Imran Hussain MP](#) (*Labour, Bradford East*)

[Stephen McPartland MP](#) (*Conservative, Stevenage*)

[Rob Marris MP](#) (*Labour, Wolverhampton South West*)

[Mark Menzies MP](#) (*Conservative, Fylde*)

[Wendy Morton MP](#) (*Conservative, Aldridge-Brownhills*)

[Roger Mullin MP](#) (*Scottish National Party, Kirkcaldy and Cowdenbeath*)

[Mr Jeremy Quin MP](#) (*Conservative, Horsham*)

[Andrew Smith MP](#) (*Labour, Oxford East*)

### Criteria against which the Committee considers each draft legislative reform order

Paragraph (3) of Standing Order No.141 requires us to consider any draft legislative reform order against the following criteria: ... whether the draft legislative reform order —

- (a) appears to make an inappropriate use of delegated legislation;
- (b) serves the purpose of removing or reducing a burden, or the overall burdens, resulting directly or indirectly for any person from any legislation (in respect of a draft Order under section 1 of the Act);
- (c) serves the purpose of securing that regulatory functions are exercised so as to comply with the regulatory principles, as set out in section 2(3) of the Act (in respect of a draft Order under section 2 of the Act);
- (d) secures a policy objective which could not be satisfactorily secured by non-legislative means;
- (e) has an effect which is proportionate to the policy objective;
- (f) strikes a fair balance between the public interest and the interests of any person adversely affected by it;
- (g) does not remove any necessary protection;
- (h) does not prevent any person from continuing to exercise any right or freedom which that person might reasonably expect to continue to exercise;
- (i) is not of constitutional significance;

(j) makes the law more accessible or more easily understood (in the case of provisions restating enactments);

(k) has been the subject of, and takes appropriate account of, adequate consultation;

(l) gives rise to an issue under such criteria for consideration of statutory instruments laid down in paragraph (1) of Standing Order No. 151 (Statutory Instruments (Joint Committee)) as are relevant;

(m) appears to be incompatible with any obligation resulting from membership of the European Union.

### **Publication**

Committee reports are published on the Committee's website at [www.parliament.uk/regrefcom](http://www.parliament.uk/regrefcom) and in print by Order of the House.

Evidence relating to this report is published on the [inquiry publications page](#) of the Committee's website.

### **Committee staff**

The current staff of the Committee are Chris Shaw (Committee Clerk), Kevin Candy (Committee Specialist) and Jonathan Olivier-Wright (Senior Committee Assistant).

### **Contacts**

All correspondence should be addressed to the Clerk of the Regulatory Reform Committee, House of Commons, London SW1A 0AA. The telephone number for general enquiries is 020 7219 5777; the Committee's email address is [regrefcom@parliament.uk](mailto:regrefcom@parliament.uk).

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# 1 Introduction

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1. The draft Legislative Reform (Private Fund Limited Partnerships) Order 2017 and Explanatory Document were laid before Parliament by HM Treasury under section 14(1) of the Legislative and Regulatory Reform Act 2006 (LRRRA) on 16 January 2017. Under the terms of section 1(2) of the LRRRA, the Government believes that the Order will remove and reduce burdens, namely financial burdens and administrative inconveniences.<sup>1</sup>

2. Through the Order, the Government is proposing to create a new category of limited partnership for collective investment funds. In 2013, the Government committed to a consultation on making changes to partnership legislation and set out measures to improve the UK's competitiveness as a centre for the asset management industry.<sup>2</sup> The Government's objective is to make a series of amendments to the Limited Partnership Act 1907 and Partnership Act 1890 to reduce the administrative and financial burden for investment funds structured as a limited partnership.<sup>3</sup> In doing so, the Government says the intended effect would be to bring the limited partnership structure into line with similar investment vehicles in other jurisdictions. This would minimise costs for investors and increase the attractiveness of the UK as a location for such funds.

3. HM Treasury laid this Order before Parliament on the same day as the Business, Energy and Industrial Strategy Department (BEIS) launched a consultation on Limited Partnership law.<sup>4</sup> BEIS is conducting the review in light of concerns voiced in the media that some limited partnerships registered in Scotland are being used for criminal activity. With this in mind, and given the technical nature of this Order and the potential implications of this deregulatory measure, we held a short inquiry into the Treasury's proposal for creating Private Fund Limited Partnerships and this Legislative Reform Order.

## Background

4. The Partnership Act 1890 sets out the basic structure of partnership law. General partnerships governed by that Act have unlimited liability for the debts and obligations of a partnership. The Limited Partnerships Act 1907 introduced a second form of partnership whereby the liability of one or more of the partners was limited, so long as the partnership also included at least one general partner with unlimited liability.

5. Under a limited partnership, a limited partner contributes an amount of money or property to the business when it is set up but is only liable for debts up to the amount they have contributed. A limited partner cannot take part in the management of the business nor can they remove their original capital contribution. It is the general partner who is liable for any debts that the business cannot pay and they control and manage the business.

6. Limited partnerships are now often used for specialised purposes such as for venture capital and private equity investment funds, but this arrangement confers no special advantage on such enterprises. These partnerships are normally governed by formal

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1 Explanatory Document, para 3.1

2 The UK investment management strategy, HM Treasury, March 2013, para 4.10

3 Impact Assessment, Limited Partnership Reform, July 2016

4 Review of Limited Partnership Law: call for evidence, The Department for Business, Energy and Industrial Strategy, 16 January 2017. Responsibility for the law on partnerships lies with the Secretary of State for Business, Energy and Industrial Strategy.

agreements. There are currently about 250 venture capital and private equity fund managers based in the UK who would be affected by the new regime.<sup>5</sup> It has been estimated that at present approximately 64% of all English partnerships are used as investment fund vehicles.<sup>6</sup>

7. By introducing the proposed Private Fund Limited Partnership structure (PFLP), the Government says it hopes to bring more investment management business to the UK and to have a positive impact on the economy more widely. The Government has indicated any wider ranging proposals to reform the Limited Partnerships Act for other business models would require further consideration and consultation.<sup>7</sup>

8. Unlike partnerships in the rest of the UK, Scottish Limited Partnerships have their own ‘legal personality’ which allows them to hold property, enter into contracts in their own right, borrow money and grant certain types of security. From July last year, media reports have reported that SLPs were being used as vehicles for money laundering and other criminal activity.<sup>8</sup> In light of this, BEIS is currently conducting a review of limited partnership law. Its consultation will close on 17 March 2017. The Government has said that any formal proposals to the limited partnerships, as a result of the consultation, would be subject to full Parliamentary scrutiny.<sup>9</sup>

## What the draft Order proposes

9. The PFLP draft Order enables a limited partnership which is an investment fund to be designated as a PFLP and amends some of the provisions of the 1907 Act as they apply to PFLPs and to partners in PFLPs. A limited partnership can be designated as a PFLP only if it is constituted by an agreement in writing and is a collective investment scheme. The draft Order makes the following changes:

- removes the requirement for limited partners to contribute capital to a PFLP;
- inserts into the 1907 Act a list of actions (described in the Explanatory Document as “the White List”) which limited partners in a PFLP may take without being regarded as taking part in the management of the limited partnership—they include, for example, acting as a guarantor for the firm, approving the accounts, authorising the general partners to make an investment or incur a debt;
- enables limited partners to appoint a person to wind up a PFLP if there is no general partner available to do so, and enables the partners to make an agreement as to winding up of a PFLP; and
- makes consequential amendments to provisions to do with the registry of limited partnerships.

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5 Q13

6 Proposals on using Legislative Reform Order to change partnership legislation for private equity investments: summary of consultation responses, HM Treasury, March 2016, para 1.8.

7 Ibid, para 1.10

8 See for example: ‘Fears grow over Scottish firms used for money-laundering in former Soviet Union’, The Herald, 16 July 2016.

9 Review of Limited Partnership Law: call for evidence, The Department for Business, Energy and Industrial Strategy, 16 January 2017.

## Our inquiry

10. In addition to the draft Order, an Explanatory Document and an Impact Assessment, the Treasury provided the Committee with three responses to written questions from us. As soon as the draft Order was laid, we met informally with Treasury officials, and representatives from the Financial Reporting Council and Insolvency Practitioners Association. We also received a written submission from Elspeth Berry, Reader in Law at Nottingham Law School.<sup>10</sup> The Financial Reporting Council also submitted written evidence. On 21 February 2017, we took formal evidence from Ms Berry and Gwyneth Nurse, Director of Financial Services, HM Treasury. We are grateful for all these contributions to our inquiry within the tight timescale allowed for our scrutiny of this draft Order.

11. The Financial Conduct Authority wrote to the Treasury regarding the Order, following a request by us.<sup>11</sup> They pointed out that the PFLP will be regulated by the FCA capital and conduct rules. PFLP will not be marketed to retail investors more generally, because they are unauthorised collective investment schemes subject to restrictions on their promotion, as set out in the Financial Services and Markets Act 2000. It should be noted that limited partners in these type of structures are either high net worth individuals or professional institutional investors.

12. With respect to transparency and concerns about money laundering, the FCA consider that the proposed changes will have no effect. Operators of these schemes will continue to be subject to the full range of anti-money laundering controls laid out in the FCA rules, Financial Services and Markets Act 2000 and Money Laundering Regulations 2007.

## Parliamentary procedure

13. This current Order is being considered under the affirmative procedure under which the Minister may make the Order if after 40 days of the draft being laid in Parliament, it is approved by a resolution of each House.<sup>12</sup>

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<sup>10</sup> Ms Berry has conducted research into limited partnerships and limited liability partnerships.

<sup>11</sup> Letter from David Geale, Director of Policy, FCA, to Simon Girdlestone, HM Treasury, 6 February 2017.

<sup>12</sup> In the Commons, if our Committee approves the draft Order following a vote, a debate in the House would be required for no more than an hour and a half. If we do not approve the Order a debate in the House would also be required but lasting up to three hours. If we recommend that the Order should not be approved, in the terms of the veto under s17(3), the Minister could not make the Order, unless the recommendation had been overturned by resolution of the House in the same Parliamentary session.

## 2 Preconditions and tests

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14. Section 3(2) of the LRRRA lists certain preconditions which the draft Order is required to meet. House of Commons Standing Order No.141(3), charges us with applying a number of tests to the draft Order, including its appropriateness for delegated legislation, whether it removes a burden, proportionality, whether it removes any protection, whether it is constitutionally significant and whether adequate consultation was undertaken. We consider the substance of the most significant proposals in the Order below.

### Capital contributions

15. The Limited Partnership Act 1907 requires that a limited partner “shall at the time of entering into such partnership contribute there to 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. In the context of private equity and venture capital funds formed as limited partnerships, the Government states 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.

16. The 1907 Act 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.

17. In practice, the Government indicates that 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 unnecessary confusion for those unfamiliar with UK limited partnership law. The Government says it is also not clear what purpose is served by requiring that a limited partner make a capital contribution no matter how small. The Treasury indicated that their consultation showed the usual practice is for £1 of nominal capital contribution from each partner.<sup>13</sup> We have noted, however, that one respondent to the Treasury’s consultation mentioned that there were currently some private funds structured as limited partnerships which have large amounts of capital declared, where the risk is greater. According to the Explanatory Document, capital contributions made under the current regime will not be withdrawable and there will continue to be a requirement to declare the capital contribution of each limited partner.<sup>14</sup>

18. In contrast, Ms Berry argued that removing this capital contribution requirement for the new PFLP structure would reduce the capital available to creditors, and transfers risk from limited partners to creditors, employees and other third parties. She said there was no evidence that capital requirements, as things stand, deter people from becoming

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13 Q20

14 Explanatory Document, para 2.54

limited partners. However, given the usual practice of limited partners making only nominal contributions, the proposed amendment represents no substantial change to the current situation.

19. The majority of correspondents to the Government's consultation agreed that capital contributions created an administrative burden and served no practical purpose for private funds structured as limited partnerships.<sup>15</sup> It was pointed out that as creditors are aware that this is normal practice, they do not rely on declared capital for protection. Instead, creditors seek protection through the assets of the limited partnership and any contractual obligations of limited partners to make advances to the limited partnership.

20. It is also the case that all creditors' positions in the case of insolvency are normally governed by insolvency law. This new PFLP structure does not change any creditor hierarchy and therefore the position of a creditor under the current hierarchy should not change.

## Deregulation and transparency

21. The Government is proposing to simplify the registration process for PFLPs by removing some of the requirements for details that must be specified when a private fund, established as a limited partnership, is registered at Companies House, and when such details change. The details in question are the amount of capital contributed, the setting out of the PFLP's term, and the general nature of the business of the partnership. It has been stated that, given there is currently no procedure for striking off limited partnerships from the register, then requiring PFLPs to register their term serves no real purpose. A strike off process for limited partnerships more generally is an issue that Government expects to cover in future reforms following a further consultation. Similarly, currently recording the domicile of limited partners is not listed as part of the registration process; this may be an issue that is picked up by the BEIS review.<sup>16</sup>

22. Under current legislation, a limited partner is also subject to certain duties which apply to partners generally, but which the Government considers says is 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).

23. The Partnership Act contains substantial leeway to adjust the rights and duties of partners to one another under the Act and the industry has taken advantage of these powers to adapt partnership agreements to better match their use as fund structures. It is now common practice to use section 19 of the 1890 Act to disapply sections 28 and 30.<sup>17</sup>

24. Furthermore, the Treasury explains that changes made to the duties set out in section 28 will not remove necessary safeguards for either limited partners or creditors when assessing the financial health of the PFLP. Given this is current practice for limited partnerships which, in the future, are likely to be PFLPs, then the disapplication of section

15 Proposals on using Legislative Reform Order to change partnership legislation for private equity investments: summary of consultation responses, HM Treasury, March 2016, para 2.43

16 Q36

17 HM Treasury (LRO 02), answer to question 9; Q29.

28 will not change the nature of partners' disclosure to each other.<sup>18</sup> It is, of course, open to limited partners to choose to reapply section 28 if they so wish. In addition, the disapplication of section 28 does not impact upon safeguards for creditors as section 28 applies only to disclosure between partners and not third parties. The Treasury therefore argues that the disapplication of section 28 for all PFLPs would be purely deregulatory, with no harmful impact. We agree.

25. In respect of transparency, the Treasury has also considered the impact of a reduction in Gazette advertisement requirements and has assessed that the planned reduction will not have an impact on the accountability of PFLPs to the public, or on abuse of limited partnerships for criminal activity. We agree.

### White list activities for limited partners

26. Under the Limited Partnerships Act 1907 a limited partner may not “take part in the management of the partnership business” or they will be liable for the debts and obligations of the limited partnership incurred while they take part in the management, as though they were a general partner.

27. New section 6A(2) sets out a list of actions that a PFLP limited partner would be permitted to carry out without being regarded as taking part in management. The Treasury believes that introducing a non-exhaustive list of permitted activities should give clarity to limited partners and avoid firms having to take costly legal advice on what is permissible when setting up and running a PFLP. Such lists have already been introduced in other jurisdictions, where funds are domiciled.<sup>19</sup> Ms Berry argues that while introduction of a list would be welcome in principle in providing legal certainty, many activities on the list in her opinion were core management activities. However, it was the Treasury's view that the duties on the list merely formulised activities that limited partners were already undertaking.

28. Following its consultation, the Treasury made some changes to the drafting of the “white list” to clarify that the role of the limited partner is to advise and consent to actions taken by the general partner, but not to act on behalf of the partnership. We believe that this appears to be in accordance with the role an investor would perform, as a limited partner, where they would be consulted and would advise on investments but where the general partner would execute decisions and operate and manage a fund. Nonetheless, we consider that a white list could be of benefit to limited partnerships more widely and this should be considered as part of a future consultation.

### Impact assessment and savings

29. The Government expects that between half and two-thirds of the cost savings associated with the PFLP proposal are attributable to the introduction of the white list and the clarification of the permissible activities by limited partners, as this is the area where limited partners require the most legal advice at present. Similarly, there will be cost savings associated with not having to dis-apply sections 28 and 30 of the Partnership Act 1890, as this will also reduce the need for legal advice.

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18 LRO0005

19 The proposed White List would align UK limited partnership law with the State of Delaware, Luxembourg, Guernsey and Jersey.

30. Overall, the Government anticipates that an individual fund will make cost savings of between £14,800 and £27,600 over the course of its lifetime.<sup>20</sup> It is expected that £10,000 to £20,000 of this will be as a result of legal savings associated with the introduction of the white list and avoiding the current practice of dis-applying sections 28 and 30 using Section 19 of the 1890 Act.

31. With respect to registration processes, the estimated cost saving accrued from the simplification of the registration process, reducing the number of publications in the Gazette and removing the requirement for a capital contribution would total around £4,000 to £6,000 savings per fund.

## Consultation

32. In July 2015, the Government published a consultation setting out its proposed amendments to the 1907 Act.<sup>21</sup> The consultation ran from 23 July to 5 October 2015 and principally asked whether the 1907 Act should be amended to include a regime for limited partnerships designated as PFLPs. A total of 22 responses were received. Most of these were from legal firms and bodies representing the legal community. Several trade bodies representing the private equity industry and the unauthorised investment fund industry also responded.

33. With hindsight we believe the Government should have been more proactive in seeking responses from the relevant financial regulatory bodies and, particularly in this case, the position of the Financial Conduct Authority should have been published early on so that its views were openly available. Similarly, we would have expected bodies such as the Financial Reporting Council to have been involved from an early stage rather than contact between them and the Treasury being in the very latter stages of the policy's formation.

34. The timing of the Treasury laying this Order was unfortunate, to say the least, given that it clashed directly with the launch of the BEIS Department's wider review. This does not appear to be a good case of joined-up Government, given one Department is seeking to make deregulatory measures in a specific area, whilst the other is consulting on whether there may potentially be a requirement to tighten regulation in another related area.

35. The Treasury pointed out to us that its current policy measures for the introduction of PFLP have been in gestation since 2013 and that in its view they were not necessarily controversial. Arguably, the Treasury has been slow and measured in taking these proposals forward. The Government has indicated that if the BEIS review were to uncover concerns and that further actions were necessary, all partnerships, including PFLPs, would be affected and the Government would consider what additional safeguards should be placed on these vehicles as well as other limited partnerships.

***36. Given that the BEIS consultation closes on 17 March 2017, we recommend that Government refrain from putting this draft Order before the House. It should at least allow time to assess responses to the BEIS consultation to check for any significant or urgent concerns which would cast doubt on making the changes in this Order. We***

20 Limited Partnership Reform, Impact Assessment, Table 5

21 Proposal on using Legislative Reform Order to change partnership legislation for private equity investments, Consultation on draft legislation, July 2015

*consider this is the prudent way to proceed on this occasion, especially given the time that has already passed since the Treasury's own public consultation on PFLPs. Once the Government has received convincing assurances from the current consultation that there are no wider issues to consider it should proceed with this Order in the House.*

37. Notwithstanding the unfortunate timing of the laying of this Order, overlapping with the BEIS review, we conclude that the responsibilities relating to the consultation procedures laid out in section 13 of the LRRRA have been properly fulfilled.

### 3 Conclusion

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38. While the creation of Private Fund Limited Partnerships creates a new category of limited partnership with some features that could benefit limited partnerships more widely, we conclude that the proposals seem sensible and are essential to ensure that the UK remains an attractive environment and domicile for these types of investment funds. Even though the estimated cost benefits for transfer of existing funds to this new structure appear relatively modest, it is vitally important that the UK regime remains competitive with other jurisdictions given the benefits to the economy provided that it does not jeopardise the UK's financial reputation in any way.

39. The proposed Order will amend the 1907 Act which applies to the whole of the UK. Given a wider review of limited partnerships law is currently underway, we recommend that the Government adhere to its commitment to review the arrangement for Private Fund Limited Partnerships as soon as the BEIS review is completed. As part of a future consultation, we believe the Government should consider the benefits of introducing a white list more widely for all limited partnerships.

40. Having considered these proposals against the essential tests, we agree that this Order serves the purpose of removing or reducing a burden as set out in section 1(2) of the LRRRA and that the conditions in section 3(2) are satisfied in relation to the draft Order. **We therefore conclude that all the relevant preconditions and tests have been met. We recommend that the draft Order be approved.**

41. The Government recommended that the affirmative resolution procedure should apply. **We agree that this is appropriate.**

# Formal Minutes

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**Monday 6 March 2017**

Members present:

Andrew Bridgen, in the Chair

Rebecca Harris	Jeremy Quin
Rob Marris	Andrew Smith
Roger Mullin	

Draft Report (*Draft Legislative Reform (Private Fund Limited Partnerships) Order 2017*), proposed by the Chair, brought up and read.

*Ordered*, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 41 read and agreed to.

*Resolved*, That the Report be the Second Report of the Committee to the House.

*Ordered*, That the Chair make the Report to the House.

[Adjourned till a date and time to be fixed by the Chair

## Witnesses

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The following witnesses gave evidence. Transcripts can be viewed on the [inquiry publications page](#) of the Committee's website.

**Tuesday 21 February 2017**

*Question number*

**Elsbeth Berry**, Reader in Law, Nottingham Law School, and **Gwyneth Nurse**,  
Director of Financial Services, HM Treasury

[Q1–59](#)

## Published written evidence

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The following written evidence was received and can be viewed on the [inquiry publications page](#) of the Committee's website.

LRO numbers are generated by the evidence processing system and so may not be complete.

- 1 Elspeth Berry ([LRO0001](#))
- 2 Financial Reporting Council ([LRO0004](#))
- 3 HM Treasury ([LRO0002](#))
- 4 HM Treasury ([LRO0003](#))
- 5 HM Treasury ([LRO0005](#))

## List of Reports from the Committee during the current Parliament

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All publications from the Committee are available on the [publications page](#) of the Committee's website.

### Session 2015–16

First Report	Draft Legislative Reform (Further Renewal of Radio Licences) Order 2015	HC 632
Second Report	Draft Legislative Reform (Exempt Lotteries) Order 2016	HC 718

### Session 2016–17

First Report	Harrogate Stray Act 1985 (Tour de Yorkshire) Order 2016 (Draft)	HC 876
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