

FUND FINANCE FRIDAY

‘NAV’igating Cayman LP Interest Security – Lender FAQs

March 18, 2022 | Issue No. 167

**By Michael O'Connor**
Partner | Conyers**By Brian Foster**
Partner | Fund Finance

As noted in our previous update, “[‘NAV’igating Cayman Share Security – Lender FAQs.](#)” fund finance lenders are increasingly encountering pledges of shares in SPVs incorporated in the Cayman Islands as part of the collateral package in NAV-based transactions. Another commonly seen aspect of such deals is a pledge of limited partnership interests (“LP Interests”) held by a borrower or other credit party (“Credit Party”) in one or more exempted limited partnerships formed in the Cayman Islands (“Cayman ELPs”). Such Cayman ELPs may be downstream holding or operating vehicles held by the Credit Party or interests it holds in funds managed by other sponsors. While security over LP Interests in Cayman ELPs is similar in some ways to taking security over shares of a Cayman company, there are some notable differences in legal requirements. This note aims to answer some of the most frequent questions that lenders ask in respect of security over LP Interests in Cayman ELPs.

Do we need a separate security agreement for the Cayman LP Interests?

There is no requirement from a Cayman perspective that security over LP Interests must be granted by an agreement governed by Cayman Islands law. In our experience, security over Cayman LP Interests which is granted as part of a fund finance transaction is most commonly documented under a New York law-governed security agreement that has been “Caymanized” to incorporate appropriate charging and security language and to otherwise address certain Cayman law issues (as further detailed below).

Are there any specific Cayman legal requirements in respect of taking security over LP Interests?

The Cayman Islands Exempted Limited Partnership Act (the “ELP Act”) has a number of specific requirements in respect of security over LP Interests. Most notably:

- The Cayman ELP must maintain a register of security interests detailing any security that has been granted over LP Interests;
- Unless otherwise specified in the LPA, a general partner must consent either prior to or simultaneously with the granting of security over LP Interests;
- Priority of a secured party’s security is obtained by either the holder of the LP Interest or the secured party serving valid notice on the registered office of the Cayman ELP of the existence of the security. The notice must contain certain statutorily prescribed information to be valid (as set out in further detail below).

What type of diligence needs to be completed ahead of the grant of security?

As the core of the security will be the ability for the secured party to effectively have the LP Interests transferred to it or its nominee in an event of default, the LPA of the Cayman ELP will need to be carefully reviewed to establish what restrictions exist on the grant of security over LP Interests and the transfer of LP Interests – in particular, what consents are required from the general partner or other limited partners. Unlike security over shares in a Cayman company where the articles of association are commonly amended to incorporate lender-friendly language, it is in many cases more difficult to undertake this for Cayman ELPs. As such, consideration of any LPA issues that, though undesirable from a lender perspective, cannot be revised in that instance is an important issue in the diligence process.

In addition, the register of limited partnership interests and register of security interests of the Cayman ELP should be checked to verify the holdings of the Credit Party and that there are no presently existing security interests reflected over the LP Interests in question.

Is the security interest registered in the Cayman Islands or are any notices required?

The Cayman Islands does not have a central forum or legal framework for the granting or registration of security over LP Interests in a Cayman ELP. The ELP Act does, however, specifically provide that security granted over LP Interests shall have priority in accordance with the time when notice of such security is validly served on the registered office of the Cayman ELP in the Cayman Islands. In order for the notice to be validly served it must: (i) be in writing; (ii) be given by the grantor or grantee of the security; and (iii) specify the agreement pursuant to which the security is granted including the date, parties thereto (including the grantor and grantee) and the details of the part or whole of LP Interest secured. As a result of the ELP Act being specific as to these requirements, it is common for the credit agreement to incorporate an undertaking requiring the Credit Party to deliver the notice concurrently with closing and to evidence the delivery of the notice as soon as possible thereafter.

Are additional documents needed beyond the security agreement?

Irrespective of whether the security agreement in question is governed by U.S. or Cayman Islands law, certain ancillary documents are generally required to be delivered at closing to ensure the lender is in the best position to enforce its security upon default, most notably: (i) consent by the general partner of the Cayman ELP to the grant of security and an undertaking

by the general partner that it will process a transfer of the LP Interest in an enforcement scenario; and (ii) a signed but undated LP Interest transfer form (together the “Cayman Security Deliverables”). It is also generally a requirement that the Credit Party deliver to the lender, post-closing, a copy of the register of security interests of the Cayman ELP updated to reflect the grant of security and, as discussed above, a copy of the notice to the registered office of the Cayman ELP.

How would we enforce the security in an event of default?

The security agreement will commonly provide the specifics of enforcement but, assuming the Cayman Security Deliverables have been obtained on closing, then enforcement of the security is usually a simple matter of executing the LP Interest transfer form provided on closing and delivering it to the registered office of the Cayman ELP, which will then update the register of limited partners and specify any other documents that the secured party may need to execute (such as a deed of adherence to the LPA).

Is stamp duty payable and at what rate?

Unless the security document is executed in or brought within the Cayman Islands, no stamp duty (or other Cayman Islands tax) is payable on the creation of the security interest.

If the Cayman ELP is registered as a Cayman Islands Mutual Fund or Private Fund, are any regulatory approvals required?

No prior regulatory approval (or post-closing notification) is required in respect of the granting of security over LP Interests of a Cayman ELP that is registered with the Cayman Islands Monetary Authority (“CIMA”) as a mutual fund or private fund. CIMA approval is not required for enforcement of the security over an LP Interest or any resulting change of control of the entity.