

English High Court Provides Guidance on Scope of Documents Required to be Provided to Private Equity Fund Investors

BY JONATHAN SHENKMAN & MARC MELIA

A series of High Court judgments in London have provided a degree of clarity on the extent to which a limited partner in an English Limited Partnership is entitled to obtain information in relation to a private equity fund and its underlying investments.¹ These judgments are likely to impact contractual discussions between fund managers and limited partners in the key area of investor reporting.

In giving judgment, Norris J considered the extent to which an investor is entitled to obtain such information as a matter of statute (under the Limited Partnerships Act 1907) and as a matter of contract (under the terms of a limited partnership agreement), noting the practical limits to the requests that a limited partner can make. Over the course of two judgments, the judge ultimately decided the case in favour of the general partner by applying a somewhat restrictive interpretation as to what constituted “partnership documentation” and by drawing a distinction between information physically in possession of the partnership (by being held by its general partner and/or manager) and other information which was solely held by underlying investment entities of the partnership.

The judgment is likely to have an effect on the manner by which investors will approach negotiations with general partners on reporting issues in new funds and also provides general partners with some degree of comfort, absent conflicting contractual provisions in their limited partnership agreement, over the means by which limited partners can secure detailed information on the fund’s investments and wider activities.

Background to the Case

The case was brought against a US-based private equity real estate fund manager by a Spanish investor, which had taken certain limited partner positions in a European private equity real estate fund structured as an English Limited Partnership. The fund had a conventional management structure – management of the partnership was vested in the general partner which in turn delegated the performance of certain of its duties to an external manager pursuant to the terms of a management agreement. Under the partnership agreement, the manager was obliged to keep full and accurate books of the partnership to cover all receipts and expenditures, assets and liabilities and profits and losses of the partnership. It appears that the manager produced a conventional level of reporting for the investors in the fund by providing audited accounts of the partnership as well as (amongst other reports) market value and funding package reports for the underlying investment vehicles. The fund made eight investments in all, of which two were particularly in issue as the investors’ capital for those two investments had been eroded by

approximately half. These particular investments were not described in detail in the judgments, but it is apparent that the investments were made via an underlying layer of special purpose vehicles (“SPVs”).

Prior to the losses being recognized on the deals, the investor wrote to the general partner seeking to obtain a better understanding of the investments and their underlying financial structures. Certain information was provided by the general partner, which was deemed insufficient by the investor who then requested further detail. The general partner ultimately refused to provide the further information on the basis that the documents requested went “well beyond what the limited partner was entitled to review”; the proper entitlement being to the partnership documents only. The matter came before Norris J in the High Court who was asked to determine what information a limited partner is entitled to obtain pursuant to its rights under s6(1) the Limited Partnerships Act 1907 “to inspect the books of the firm and examine into the state and prospects of the partnership business.”

In reaching judgment the judge noted that, despite the investor’s arguments, the general partner had in fact identified and collated a substantial body of documentation which it had determined were “partnership documents”, and that therefore the onus had passed to the investor to demonstrate in what respects the available documentation was insufficient to enable it to make a determination as to “the state and prospects of the partnership business” within the meaning of the Act. There can be no doubt that the general partner’s provision of an extensive set of documentation put the investor in a more difficult position in bringing its claim for further information.

The concept of “Partnership Documentation” in relation to the business of “Private Equity”

In giving judgment, the judge noted that the general partner of a partnership was obliged to maintain a record of the partnership’s business and affairs sufficient to enable a partner with access to it to examine into the state and prospects of the partnership business but that the extent of this obligation varies from case to case depending upon the partnership business.

For the purposes of the business of “private equity funds”, it is possible to derive some interesting guidelines from the judgment in relation to key private equity documentation and reporting.

Funding Documentation - the investor sought disclosure of all credit agreements, mezzanine facilities and indeed all correspondence with bank lenders. The judge disagreed that all such information was required to be provided save insofar as the documentation related to credit lines and facilities established in the name of the partnership for which the limited partners could be liable. Most importantly, funding documentation had also been sought by the investors from the investment-level SPVs, but here the judge found that such documentation only needed to be provided to the investor if it was the practice of the partnership to call for and review copies of the transactional or operational documentation of the SPVs. If the information stayed at the SPV level and (subject to the broader principles, sufficient information was still provided for accounts to be drawn up accurately at partnership level), then there was no right for the investor to obtain that information.

Constitutional Documents and Other Documentation of the SPVs - disclosure was sought in relation to the constitutional and participation agreements relating to the SPVs as well as draft documentation, any notes or records of meetings or conversations where any decision to invest in one of the particular investments was considered, as well as any formal or informal records of the investment strategies of the underlying SPVs. The investor requested the information so that it could determine (over the course of the life of the investment) how and upon the basis of what information, decisions were taken on underlying investments. The general partner argued that this

information had already been provided in its broader reporting schedules. Despite being supportive towards the cause of the investor, the judge found that the general partner was only obliged to provide the constitutional documents in relation to the underlying SPVs and its general reporting package and that there was “no question of the general partner having any obligation to make up partnership books and records which do not at present exist in fact by using whatever shareholder rights the partnership may have to enforce against the underlying SPVs”. The judge also did not see any basis upon which the investor could require the general partner to obtain drafts or notes or conversations between the underlying SPVs and third parties.

Advisory Committee Documentation - the investor also sought disclosure of all documentation in relation to the limited partners' advisory committee (including presentations made to the advisory committee, minutes of meetings and documents referred to in those meetings). The judge found that while the minutes and agenda of the meetings (including any documents annexed to such documents) were “partnership documents”, the documents referred to in such meetings were not “partnership documents” and did not need to be disclosed. However, the judge also found that a reasonable request to supplement the formal record by the provision of readily available and obviously relevant information ought to be met by the general partner.

Underlying Hedging Documentation - due to the nature of the specific transactions in issue, the investor sought disclosure of the hedging documents relating to the partnership's indirect participation in the two investments (note that with the exception of one document, these were all entered into at SPV level only). Again the judge noted that the conventional reporting provided by the manager to the investors would have covered this information (and in particular the pricing of the various hedges) and that this was sufficient in itself.

Primary Transactional Documentation - this was an extensive request by the investor for a complete breakdown of all commitments, including details of when those commitments were made, all investments, amounts invested, all sale and purchase agreements together with a very complete schedule of all investments (including opening balances, additions, disposals, revaluations, gains and losses). The judge was unsympathetic to this request, comparing it to a limited partner in a retail business asking for a copy of all till receipts. The judge referred the limited partner to the audited accounts of the partnership which he had not been persuaded were insufficient to make the necessary determination.

Conclusions

One conclusion to be drawn from the judgment is that sound extensive reporting by a general partner will render it difficult for a limited partner to obtain further documentation from a limited partnership absent specific provision for such further information in the partnership documentation. Another important element of the decision is the extent to which certain documentation retained at the SPV level may be largely insulated from investor requests for disclosure (at least as a matter of statute). As partnership reporting becomes increasingly scrutinized, it will be interesting to see to what extent limited partners will look to negotiate fund limited partnership terms to provide for information flows not just from the partnership itself but also in relation to the underlying SPVs of the partnership. Should this occur, it is likely that this will be resisted by general partners on the basis that they are already spending significant resources on reporting for limited partners and that facilitating the types of detailed investment-level disclosures sought by the investor in the *Inversiones* case would be excessive.

General partners may take away from the case the importance of confidentiality and that requests for disclosure of certain “partnership documents” could be trumped or minimised through an effective confidentiality clause in their relevant limited partnership agreement or management agreement.

While the case concerned an interpretation of English partnership law, it is likely to have implications in other common law jurisdictions and we would expect its interpretation to be relevant to common law offshore fund jurisdictions such as the Cayman Islands and the Channel Islands.



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings lawyers:

LONDON

Jonathan Shenkman
44.20.3023.5131
jonathanshenkman@paulhastings.com

Marc Melia
44.20.3023.5125
marcmelia@paulhastings.com

Christian Parker
44.20.3023.5161
christianparker@paulhastings.com

NEW YORK

Lawrence J. Hass
1.212.318.6401
larryhass@paulhastings.com

Thomas Rao
1.212.318.6838
thomasrao@paulhastings.com

Joshua H. Sternoff
1.212.318.6011
joshsternoff@paulhastings.com

¹ Inversiones Frieira SL and another v Colyzeo Investors II LP and another. Judgments are available at: <http://www.bailii.org/ew/cases/EWHC/Ch/2011/1762.html> (July 2011 Judgement) <http://www.bailii.org/ew/cases/EWHC/Ch/2012/1450.html> (May 2012 Judgement)