

Ontario limited partnerships: a globally favoured jurisdiction for private funds

AUTHORS



Lauren Hulme



Ian Lee



Saira Bhojani



Cameron D. Koziskie



Aaron S. Emes



Guillaume Lavoie



Scott Semer



Max Shakin



Andrew J. Beck

We often get asked by both our general partner and limited partner clients as to the merits of using an Ontario limited partnership for private funds—including in comparison to other common jurisdictions worldwide, particularly Delaware and the Cayman Islands (as well as Manitoba and Québec). Ontario is generally viewed as a favourable jurisdiction around the world for fund sponsors and investors, and in this article, we explore the reasons why.

The Ontario advantage

When selecting the jurisdiction to form a private fund, a fund sponsor must consider several criteria, including (i) the tax treatment of any income or gains earned by the fund and (ii) protecting the limited liability of its investors. When weighing these considerations, there is seldom a perfect or risk-free choice.

Ontario is also a very popular jurisdiction for non-Canadian fund sponsors (e.g., Latin American fund sponsors), many of whom, even without any nexus to Canada, determine that Ontario is preferable over other jurisdictions given tax, reputational and other considerations.

For fund sponsors and investors alike, we believe there are several benefits to selecting Ontario over other jurisdictions as the jurisdiction of the fund, including the following:

- It is generally understood that Ontario limited partnerships provide for limited liability of limited partners.
- Canadian tax law generally treats Ontario limited partnerships as transparent entities from an income tax perspective.
- Ontario limited partnerships that do not carry on business in Canada and do not have a Canadian general partner (and are otherwise managed and controlled outside of Canada) are generally not required to report to or provide information to the Canadian tax authorities (except where each investor in the limited partnership is a Canadian resident).
- Ontario has a sophisticated legal infrastructure coupled with limited bureaucratic hurdles for forming and maintaining limited partnership entities.

Formation, ongoing obligations and dissolution

Forming an Ontario limited partnership is a straightforward process, and ongoing filing requirements are limited. The main steps are outlined below:

1. An Ontario limited partnership is formed by filing a declaration under the *Limited Partnerships Act* (Ontario) (the Ontario Act) and can be formed with just one general partner and one limited partner.
2. A declaration is signed by the general partner, which includes the name of the limited partnership and its address, a description of the general nature of its business, a North American Industry Classification System (NAICS) business activity code and the corporate name and address of the general partner.
3. It is not required that any limited partner be resident in Ontario or in Canada, but the general partner must be an Ontario entity or be extra-provincially registered in Ontario (a foreign general partner without a registered address in Ontario needs to engage an agent for service to sign the declaration on its behalf).
4. A declaration may be filed online with the Registrar and an official Declaration of an Ontario Limited Partnership will be issued by the Ontario Ministry of Public and Business Service Delivery typically within 24 hours of filing (though longer turnaround times may apply if the declaration is submitted by mail).

While not a requirement under the Ontario Act, we generally recommend that the partners of an Ontario limited partnership enter into a limited partnership agreement (LPA) that sets out the obligations of the partners and the terms under which the limited partnership will be governed, which can be a very short LPA (i.e., five pages) or a more comprehensive LPA (i.e., 75-150 pages). Some of the detailed terms contemplated may include provisions setting out the limited partnership's investment objective and investment limitations, the term of the limited partnership, reporting obligations to the limited partners, how capital contributions to the limited partnership will be made, how profits will be shared among the partners, how the general partner may be removed, the process for admitting additional limited partners, how amendments to the LPA can be effected, and so on.

The LPA for an Ontario limited partnership is a private document among the partners and is not publicly disclosed or required to be filed.

Ontario limited partnerships are not subject to any periodic filing requirements, other than a requirement to file a declaration of change if there has been a change in any of the information stated in the declaration, including a change in the name of the limited partnership. The general partner must maintain a current record of limited partners at the limited partnership's principal place of business in Ontario, which sets out each limited partner's name, address and the amount of its capital commitment. There is a requirement in the declaration for the fund's "principal place of business" to be in Ontario. However, in our experience, having a registered office in Ontario where books and records of the fund are kept is generally considered to be sufficient for these purposes. A declaration expires five years after the date it is accepted for filing unless it is cancelled or renewed. An Ontario limited partnership is not automatically dissolved if the declaration expires but a nominal additional fee is payable if a renewal is filed late. To effect a dissolution of an Ontario limited partnership, a declaration of dissolution signed by the general partner must be submitted to the Registrar.

Tax considerations

Tax transparency

An Ontario limited partnership is generally treated as a transparent entity for Canadian tax purposes. We also understand that many jurisdictions generally treat Ontario limited partnerships as transparent for their respective domestic tax purposes, which makes an Ontario limited partnership an attractive vehicle for not just Canadian sponsors but non-Canadian sponsors as well.

Tax havens

In our experience, there is sometimes a perception among some investors that the Cayman Islands are a tax haven, which can be met with increased scrutiny from tax authorities in many countries, limiting the usefulness of those jurisdictions to form private funds from a tax-efficiency perspective. Furthermore, some reputation-conscious investors may be deterred from investing in funds established in such jurisdictions. Ontario, however, does not suffer from that perception.

Limited liability

In accordance with the Ontario Act, a limited partner of an Ontario limited partnership is generally only liable for the debts and obligations of the limited partnership up to the amount that the limited partner has committed to invest in the limited partnership, subject to the provisions of the relevant LPA. For instance, many LPAs will include a giveback provision, requiring limited partners to return a portion of the distributions they received from the fund to cover the fund's liabilities and obligations (which could be on top of the limited partners' commitment amounts).

Exceptions and rights to limited liability

However, a limited partner may become liable for the debts and obligations of an Ontario limited partnership where the limited partner takes part in the control of the business of the limited partnership. As there are very few Ontario and Canadian judicial decisions that consider in which circumstances a limited partner may be viewed as having taken part in the control of the business of the limited partnership, distinguishing between acts that may or may not compromise the limited liability of the limited partners is a fact-based exercise that is challenging to determine with a high degree of certainty.

Notwithstanding the foregoing, the Ontario Act sets out certain permitted limited partner rights and powers in the context of an Ontario limited partnership which, if put in place and exercised, will not result in the limited partners being seen as taking part in the control of the business of the limited partnership. This includes the right to inspect the limited partnership's books and request information about matters concerning the limited partnership, obtain a court order to dissolve the limited partnership, examine the state and progress of the limited partnership and advise as to its management, act as a contractor for or an agent or employee of the limited partnership or of the general partner, and provide loans to, and transact business with, the limited partnership (provided that limited partners cannot provide loans that are secured by the property of the limited partnership, and the loans granted by limited partners must be subordinate to those of non-limited partner creditors).

In addition, the Ontario Act specifies that a limited partner will not be *presumed* to have taken part in the control of the business of the limited partnership by reason only that the limited partner exercised rights and powers in addition to the rights and powers specifically conferred upon limited partners by the Ontario Act.

Legal considerations for liability

Ontario legal counsel can typically provide an opinion confirming that the liability of a limited partner is limited to the amount that it has agreed to contribute to the limited partnership (subject to the terms of the relevant LPA) and that a limited partner should not be found to have taken part in the control of the business of the limited partnership solely by reason of exercising those rights and powers granted to the limited partner in the relevant LPA. In the context of a typical private fund, this may include the ability to extend or terminate the fund's term or investment period, as well as certain other excuse rights and remedies, such as the right to remove the general partner under select scenarios.

However, because of the lack of jurisprudence on this topic, legal counsel's opinion is not determinative on the matter of limited liability. When deciding whether a limited partner has taken part in the control of the business of the limited partnership, a court is likely to consider not just the terms of the relevant LPA but also the actual conduct of the limited partner. Due to this fact-based analysis, it is difficult to predict with certainty, based solely upon a review of the provisions of the relevant LPA without knowing all of the facts, whether there is a material risk that a limited partner could be found by a court to have participated in the control of the business of the limited partnership.

Liability determination in other jurisdictions

In an Ontario limited partnership, limited partners who are found to have participated in the control of the business of the limited partnership will be liable as a general partner and face unlimited liability for the debts and obligations of the limited partnership. In both Delaware and the Cayman Islands, it is our understanding that whether a limited partner loses limited liability is similarly determined by assessing whether such limited partner participated in the control or conduct of the business of the limited partnership. We further understand that both jurisdictions, however, employ an additional “detrimental reliance” test: (i) in Delaware, for instance, a limited partner who is found to have participated in the control or conduct of the business of the limited partnership will only be liable to persons who transacted with the limited partnership with a reasonable belief, based on the limited partner’s conduct, that the limited partner is a general partner, and (ii) in the Cayman Islands, such a limited partner will only be liable to persons who had actual knowledge of that limited partner’s participation in the business of the limited partnership and who then reasonably believed the limited partner to be a general partner. We understand that Manitoba has a similar rule, which provides that a limited partner who takes an active part in the business of the limited partnership is only liable as a general partner if parties dealing with such limited partner do not know that such limited partner is a limited partner.

While these considerations may be important to understand from a legal perspective, from a practical point of view, limited partners of Ontario limited partnerships are generally able to get comfortable with Ontario’s limited liability construct given that investors generally participate as passive investors who do not take part in the day-to-day business decisions, administration or operations of the limited partnership (which obligations are conferred on and exercised by the general partner only). Further, we are unaware of any claim brought by a third party against a limited partner in a private fund formed in Ontario.

Considerations for limited partner advisory committees

In respect of a private fund, certain limited partners may receive a seat on the fund’s limited partner advisory committee (LPAC) and, as a result, be vested with certain additional duties and authorities that are not available to other limited partners. For instance, a fund’s LPAC is often charged with reviewing and approving various conflict of interest matters and permitting exceptions to certain of the fund’s investment and other limitations. The LPAC will also commonly receive additional reporting about the fund’s activities that is not made available to other limited partners. These additional functions and responsibilities need to be considered in the limited liability analysis in respect of advisory committee members. LPAs will often expressly indemnify LPAC members from losses incurred in connection with their actions or omissions related to the fund as a result of the representative of the limited partner serving on the advisory committee, subject to certain customary carve-outs. Ontario legal counsel will generally still be able to deliver “should” level limited liability opinions in respect of LPAC members notwithstanding their heightened level of involvement with the fund.

What about Manitoba?

In addition to the merits of Ontario limited partnerships, Manitoba is another Canadian provincial jurisdiction in which Canadian and non-Canadian fund sponsors have demonstrated a particular interest. Manitoba is generally viewed as offering very strong limited liability protection (as described above); however, Manitoba also requires public identification of the limited partners and their capital contributions, which entails ongoing filings for sponsors and puts pressure on restrictions around the disclosure of information. From a Canadian tax perspective, Manitoba limited partnerships are treated the same as Ontario limited partnerships (all else being equal). While about 10 years ago, there was a lot of discussion and consideration among sponsors to move their funds to Manitoba, we generally find that discussion has subsided, and Ontario remains the jurisdiction of choice for Canadian partnerships.

And Québec?

Québec limited partnerships bring about their own set of considerations and can offer certain advantages, although some believe these advantages are offset by certain additional requirements imposed by Québec legislation. As in Ontario and Manitoba, Québec limited partnerships offer very strong limited liability protection and are also treated as a transparent entity for Canadian tax purposes, but they also require public disclosure—notably of the three largest limited partners and of certain indirect ultimate beneficial owners of their general partners and limited partners. They also require the limited partnership to adopt a French name (in addition to any name ascribed in another language). For these reasons, Québec limited partnerships are often avoided when there is no Québec connection to the entity being structured. That said, Québec limited partnerships are particularly attractive where limited liability is a major concern given the strong limited liability protection offered by the Québec civil law regime.

Request our comparison chart

We have prepared a comparison chart that covers some of the key characteristics of Ontario, Delaware and Cayman Islands limited partnerships. This chart may be requested by emailing any of our authors. Click on an author name to go to their bio page with their contact info.

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