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Ireland as a location for structured finance SPVs

Turlough Galvin
Matheson Ormsby Prentice

In recent years Ireland has become an increasingly popular jurisdiction for the establishment of special purpose vehicles (SPVs) for securitisation, repackaging, collateralised debt obligation (CDO), collateralised loan obligation (CLO), warehousing and other structured finance transactions. As the market has become more sophisticated, Ireland as a jurisdiction has constantly responded, in terms of its legal and tax framework, in order to continue to position itself as the location of choice for SPVs. The benefits of using an Irish SPV are set out below.

Onshore status

Ireland is a member of the European Union and also of the Organisation for Economic Cooperation and Development (OECD). In the current environment many originators and arrangers prefer not to use offshore entities in their transaction structure. In fact, many investors in structured finance transactions will invest only in notes issued by SPVs located in EU or OECD member countries.

Taxation

Ireland is not a tax haven. It is an onshore EU tax jurisdiction and in coming to Ireland arrangers and originators must deal with the Irish tax position and must ensure, through careful planning and advice, that the tax analysis required is achieved. It is critical in any structured finance transaction to minimise any liability to taxation arising to either the SPV or the noteholders.

SPV taxation

Irish tax legislation provides for special treatment in relation to qualifying SPVs. A qualifying SPV must be resident in Ireland for tax purposes. It must acquire financial assets or enter into swaps or other legally enforceable financial arrangements with a market value of at least €10 million, although this financial requirement applies only to the first transaction entered into by the SPV.

The SPV may acquire, hold, manage or enter into any of the following financial arrangements (either directly or indirectly, for example through a partnership):

- shares, bonds and other securities;
- futures, options, swaps, derivatives and similar instruments;
- invoices and all types of receivable;
- obligations evidencing debt (including loans and deposits);
- leases and loan and lease portfolios;
- hire purchase contracts;
- acceptance credits and all other documents of title relating to the movement of goods;
- bills of exchange, commercial paper, promissory notes and all other kinds of negotiable or transferable instrument;
- greenhouse gas emissions allowances; and
- contracts for insurance and contracts for reinsurance.

Profits arising from the activities of a qualifying SPV are chargeable to corporation tax as if the SPV were a trading company. This is important as it ensures that a tax deduction is available in respect of any interest expense incurred by the SPV. Through proper and careful planning the position can be achieved such that the SPV earns a minimal profit (there is no specified minimum amount required by law) subject to the corporation tax rate of 25 per cent.

A combination of the treatment of the SPVs as similar to trading companies for the purpose of calculating their tax liability and the availability of an interest deduction for payments of interest on notes (including profit participating notes) ensures that the SPV is both profit neutral and tax neutral. Although the SPV must notify the Revenue commissioners of its existence, no special rulings or authorisations are required in Ireland in order for the SPV to achieve this tax-neutral status.

Taxation of noteholders

Income tax

Where interest is paid by a qualifying SPV to any person resident in an EU member state (other than Ireland) or in a jurisdiction with which Ireland has a double tax treaty there is a domestic exemption from Irish income tax on the receipt of such interest. Ireland is currently a party to 44 double tax treaties and the Irish authorities are very active in increasing the number of treaties to which Ireland is a party. Ireland has currently ratified double tax treaties with Australia, Austria, Belgium, Bulgaria, Canada, China, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, India, Israel, Italy, Japan, Korea, Latvia, Lithuania, Luxembourg, Malaysia, Mexico, the Netherlands, New Zealand, Norway, Pakistan, Poland, Portugal, Romania, Russia, the Slovak Republic, Slovenia, South Africa, Spain, Sweden, Switzerland, the United Kingdom, the United States and Zambia.

However, if this domestic exemption does not apply due to the residence of the noteholder, there is a longstanding unpublished practice in Ireland whereby no action will be taken to pursue any liability to such Irish tax in respect of persons who are regarded as not being resident in Ireland provided such persons are not otherwise subject to tax in Ireland or do not seek to obtain repayment of tax in respect of other taxed income from Irish sources.

Withholding tax

In general, withholding tax at the rate of 20 per cent must be deducted from interest payments made by an Irish company. However, two major exemptions from the charge to Irish interest withholding tax are provided under domestic legislation: the quoted Eurobond exemption and the EU/double tax treaty exemption.

A 'quoted Eurobond' is defined as a security which is issued by a company, is quoted on a recognised stock exchange and carries a right to interest. There is no obligation to withhold tax on payments of interest on quoted Eurobonds where the person by or through which the payment is made is not in Ireland or, if the payment is made by or through a person in Ireland, the quoted Eurobond is held in a recognised clearing system or the beneficial owner of the quoted Eurobond provides a declaration that it is not resident in Ireland.

In addition, there is no obligation to withhold tax in respect of interest payments made by a qualifying SPV to any person who is resident in an EU member state (other than Ireland) or in a double tax treaty jurisdiction. In order to rely on this second exemption from withholding tax it is necessary to be able to identify the holders of the notes issued by the SPV. Such identification can be managed by issuing definitive registered notes with certain transfer restrictions.

Other exemptions from withholding tax are also available, including an exemption for specific types of note with a maturity of less than two years. In general, withholding tax does not apply to swap payments.

Other taxes – VAT and stamp duty

Other taxes of relevance to structured finance transactions in Ireland include value added tax and stamp duty.

In general, the activities of a qualifying SPV are exempt activities for VAT purposes and therefore there is no obligation on the SPV to charge VAT in respect of its activities. The SPV is typically not in a position to obtain a repayment of any VAT incurred by it in respect of services received. No charge to Irish VAT arises in respect of corporate administration services supplied to a qualifying SPV. Further, it is notable in relation to CDO or CLO transactions that no charge to Irish VAT arises in respect of collateral management services supplied to a qualifying SPV.

In relation to stamp duty, as long as the SPV remains a qualifying company within the meaning of the relevant legislation, no Irish stamp duty will be payable on either the issue or transfer of the notes, provided that the finance raised by the issue of the notes is used in the course of the business of the SPV. There is no capital duty in Ireland.

Double tax treaties

As discussed above, Ireland is a party to 44 double tax treaties and the terms of the appropriate treaty can ensure that the income in respect of the underlying assets acquired by the SPV can be paid to it without any withholding or other taxes. This can provide a significant advantage for Ireland over the use of tax haven jurisdictions where withholding tax can otherwise result in significant tax leakage in the transaction. The number of tax treaties to which Ireland is a party is increasing every year. New agreements with Argentina, Chile, Egypt, Georgia, Kuwait, Macedonia, Malta, Moldova, Morocco, Serbia, Singapore, Thailand, Tunisia, Turkey, Ukraine and Vietnam are in the course of negotiation or approval.

Offering of securities

Ireland implemented the EU Prospectus Directive (2003/71/EC) on July 1 2005 pursuant to the Prospectus (Directive 2003/71/EC) Regulations 2005. Pursuant to the regulations, an Irish SPV will be obliged to publish a prospectus if it wishes to offer its securities to the public in Ireland, subject to certain exceptions including for:

- offers made to qualified investors (as defined in the directive);
- private placements made to fewer than 100 persons (other than qualified investors); and
- offers with a minimum of total consideration per investor or specified denomination per unit of at least €50,000.

No matter whether the securities are publicly offered, the regulations also require a prospectus to be published if the securities are listed on the Irish Stock Exchange.

Prior to publication of a prospectus, the Irish SPV must apply to the Irish Financial Services Regulatory Authority for approval of the prospectus. The regulator has delegated certain tasks relating to the scrutiny of prospectuses to the Irish Stock Exchange. Following the approval of the prospectus by the regulator, it must be published by the Irish SPV and this can be achieved by publication of the prospectus on the regulator's website. Once the prospectus has been approved by the regulator it can avail of the 'passport' provided to issuers by the directive, which means that it must be accepted throughout the European Union for public offers and/or admission to trading on regulated markets.

Private limited company or PLC?

Historically a public limited company (PLC) had to be incorporated for the majority of structured finance transactions where an Irish SPV issued securities, particularly where such securities were offered to anyone other than a select number of sophisticated investors. Following the enactment of the Investment Funds, Companies and Miscellaneous Provisions Act 2006 which, among other things, amended the Companies Acts, a private limited company can now be used for most transactions.

The use of a private limited company rather than a PLC has two principal advantages:

- A private company can be incorporated with a minimum share capital of €1, whereas a PLC must have a minimum share capital of €38,100. However, the share capital of a PLC may be used to defray costs incurred by the SPV in entering into the transaction; and
- A private company can be incorporated in five working days, while it usually takes two weeks to have a PLC fully operational, as prior to entering into any documentation or transacting any business a PLC must also hold a certificate of a public company entitled to do business.

A private limited company can now be used where:

- the offering of securities is made only to 'qualified investors';
- the offer is made to fewer than 100 persons (not including qualified investors); or
- the minimum subscription amounts or the minimum denomination of the securities is not less than €50,000.

If the offering of securities does not fall within one of these three categories it will be necessary to incorporate a PLC, particularly for transactions that involve large-scale retail offers with low minimum denominations.

A qualified investor, for the purposes of determining whether the first or second category above would apply to an offering of securities, includes:

- legal entities authorised or regulated to operate in financial markets (eg, credit institutions, investment firms, insurance companies, collective investment schemes, pension funds and commodity dealers);
- entities not authorised or regulated but whose corporate purpose is solely to invest in securities;
- national and regional governments, central banks and other international institutions (eg, the International Monetary Fund, the European Central Bank and the European Investment Bank);
- legal entities which meet two of the following three criteria:
  - at least 250 employees;
  - a total balance sheet in excess of €43 million; and
  - an annual turnover in excess of €50 million; and
- certain natural persons and other small and medium-sized enterprises that are entered on a register of experts maintained by the Irish Financial Services Regulatory Authority.

Listing

The Irish Stock Exchange has extensive experience in the listing of specialist debt securities such as those issued by SPVs and provides an efficient, effective and timely listing service. It is now recognised as having a leading position in this market. Debt securities listed on a 'recognised stock exchange' (eg, the Irish Stock Exchange) can avail of the quoted Eurobond exemption from withholding tax (see above for more details).

Conclusion

Ireland has a highly regarded regulatory regime and has consistently introduced and refined its legislation dealing with structured finance transactions. Ireland is also an onshore jurisdiction that is an EU member state, a member of the OECD and within the eurozone. Ireland, like the United Kingdom, is a common law jurisdiction. Ireland has a large double tax treaty network and has a domestic infrastructure capable of implementing the most difficult structured finance deals (eg, experienced corporate administrators, lawyers, auditors) in a cost-effective manner. All of these factors now combine to make Ireland a very attractive jurisdiction in which to locate structured finance SPVs.