ADVISORY | IRELAND INFORMATION

Locating SPVs in Ireland

Introduction - Why is Ireland a leading jurisdiction for SPVs?

Ireland is a firmly established centre of excellence for the establishment of special purpose vehicles ("SPVs") for financial investment transactions including warehousing, ABS, CLOs, CMBS, CRT / SRT, securitisations, repacks, receivables financing and distressed asset investment.

There are a number of reasons for Ireland's popularity: Ireland is an onshore jurisdiction and a long standing member of the European Union and the Organisation for Economic Co-operation and Development. Ireland's favourable securitisation tax regime allows structures to be established which can effectively be tax neutral. In addition, Ireland has an extensive network of double tax treaties which may allow for the return generated by underlying assets to be paid to an SPV with zero or reduced foreign withholding tax.

Ireland has a respected legal system, which has adapted over the years to facilitate structured finance transactions. It has the appropriate infrastructure with an excellent choice of experienced legal and accounting professionals and corporate service providers. Efficient listing of securities can also be undertaken on The Irish Stock Exchange plc, trading as Euronext Dublin.

Legal and regulatory framework

Ireland is a common law jurisdiction. Its legal concepts will therefore be familiar to most investors and promoters. Establishing an SPV in Ireland is a straightforward and inexpensive process. Typically, there are no regulatory or other approvals required, though this will depend on the nature of the activities of the SPV. For example, an SPV established as a reinsurance vehicle (known as a Solvency II SPV or SII SPV) and certain loan owners must be authorised by the Central Bank of Ireland. There are also certain other local regulatory considerations for entities involved in lending, swaps, securities financing or securitisations which need to be considered on a case-by-case basis.

Chart 1: Total Active Irish SPVs and Assets

Source: Atlantic Star Analytics, Q3 2024 Report.

Taxation

Qualifying companies

An important reason for Ireland's popularity as an SPV location is its favourable tax regime. A specific tax treatment applies to a "qualifying company" (often referred to as a Section 110 company as it is governed by section 110 of the Irish Taxes Consolidation Act, 1997 as amended ("Section 110")). No advance ruling or clearance is required to avail of the tax treatment under Section 110.

Section 110 provides that the taxable profits of a qualifying company involved in the holding and/or managing of "qualifying assets" should be computed on the same basis as a trading company. This allows for the cost of funding and other related expenditure (including, for example, interest and currency swap payments and payments to service providers) to be tax deductible. The ability to claim a tax deduction also extends to profit participating interest (subject to conditions). While the qualifying company is subject to corporation tax at the rate of 25%, tax neutrality can be achieved by matching deductible expenditure with income through the sweep out mechanism of a profit participating note or loan ("PPN"). Interest can be paid (or accrued) on the PPN in each accounting period.

Subject to some exceptions, the taxable profits of a qualifying company will follow the accounting treatment. As a general rule, a qualifying company may prepare its tax computation in accordance with Irish GAAP accounting rules as they existed at 31 December 2004, or by election in accordance with current Irish GAAP accounting rules ("IAS"). The use of historic GAAP can allow for less volatility and create more certainty in modelling expected returns. A qualifying company is not required to make any minimum profit for Irish tax purposes. However, it will normally retain a spread for corporate benefit purposes in each accounting period.

Requirements of Section 110

A qualifying company is a company which is resident in Ireland for tax purposes and which, among other things, carries on in Ireland a business of holding, managing, or both the holding and managing of qualifying assets, including in the case of plant and machinery acquired by the company, a business of leasing that plant and machinery, and, apart from activities ancillary to that business, carries on no other activities.

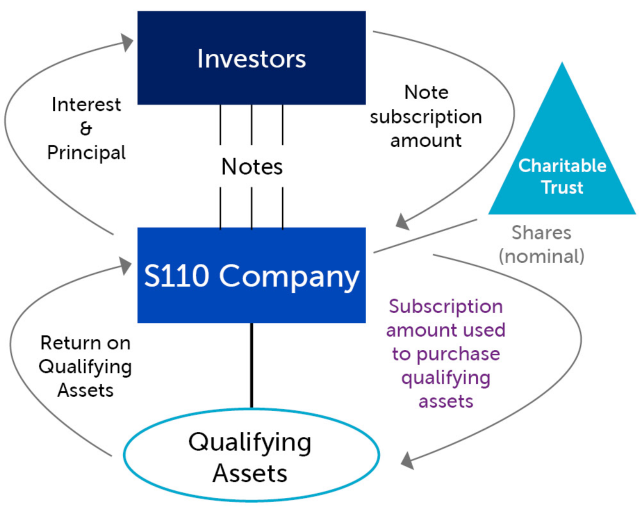
A qualifying asset consists of any financial asset, certain commodities, plant and machinery or any interest (including a partnership interest) in such assets. Financial assets are further defined to include the following:

1. shares, bonds and other securities;
2. futures, options, swaps, derivatives and similar instruments;
3. invoices and all types of receivables;
4. obligations evidencing debt (including loans and deposits);
5. leases and loan and lease portfolios;
6. hire purchase contracts;
7. acceptance credits and all other documents of title relating to the movement of goods;
8. bills of exchange, commercial paper, promissory
9. notes and all other kinds of negotiable or
10. transferrable instruments;
11. carbon offsets; and
12. contracts for insurance and contracts for reinsurance.

Commodities are broadly defined as tangible assets (other than currency, securities, debts or other assets of a financial nature) which are dealt in on a recognised commodity exchange.

Plant and machinery includes aircraft, ships, rolling stock and other equipment. Section 110 companies have frequently been used as a financing mechanism for the aviation industry and enhance the infrastructure available for Ireland's world renowned aircraft financing and leasing industry.

Simple structure diagram



An SPV will not be a qualifying company if any transaction is entered into by it otherwise than by way of a bargain made at arm's length. However, there is an exception to this requirement in certain circumstances in relation to the payment of profit participating interest under a PPN. The payment of profit participating interest by a Section 110 company under a PPN is similarly excluded from Ireland's extended transfer pricing rules which apply since 1 January 2020. Arrangements entered into by a Section 110 company (other than a PPN) were already subject to the general arm's length requirement in Section 110, therefore the extension of the transfer pricing rules to transactions between a Section 110 company and its "associated persons" (as defined) should for the most part only involve additional transfer pricing documentation requirements (if any) rather than giving rise to any transfer pricing adjustment.

It is also a requirement of Section 110 that the first assets held or managed by the qualifying company have an aggregate value of not less than €10,000,000. This requirement is a day-one test only applicable to the first transaction(s) entered into by the qualifying company and the value of subsequent transactions is irrelevant for this purpose.

Financing of the SPV

The SPV is generally funded by way of medium-term or long-term notes. Loan funding or swap arrangements are also possible. The notes may be issued with a stated interest rate or may be profit participating in nature through the issuance of PPNs. The return on PPNs can vary with the profitability of the SPV, while still retaining interest deductibility for tax purposes. Transactions are commonly funded through the issuance of senior notes with a fixed interest rate and a subordinated note which is profit participating in nature.

If the investors are known at the outset (and it is not anticipated that new investors will come on board other than through transfers of notes by existing noteholders), a single issuance note structure may be put in place. Alternatively, a note issuance programme may be put in place where the SPV will issue notes in separate ring-fenced series whose return is segregated from the return of all other series. In each case a series will be linked to a particular pool of assets and a default with respect to one series will not impact any other series – in this way the same result can be achieved as provided for in protected cell company arrangements.

Financing and withholding tax

A qualifying company is financed by way of debt (including profit participating debt). The debt may take the form of a loan, notes or bonds. There are currently no restrictions on the ratio of debt to equity for a Section 110 company for Irish tax purposes. The return to investors is taken by way of interest payments. Withholding tax at the rate of 20% applies to interest payments made by an Irish resident company. However, there are a wide range of exemptions available to a qualifying company such as the quoted

Eurobond exemption for notes which are quoted on a recognised stock exchange. There is also no obligation to withhold tax in respect of interest paid by a Section 110 company to a person who is tax resident in an EU Member State (other than Ireland), or in a country with which Ireland has signed a double tax treaty.

In addition, qualifying companies can avail of the "wholesale debt" exemption from withholding tax. In order for the wholesale debt exemption to apply, notes issued by a qualifying company must mature within two years, be held in a recognised clearing system and must be issued in minimum denominations of US$500,000, EUR500,000 or the foreign currency equivalent of EUR500,000. It is not necessary for the notes to be held in a clearing system and issued in the above denominations provided the noteholders are resident in Ireland and have provided a tax reference number or, where they are resident outside of Ireland, they provide a prescribed form of declaration confirming their name, address and country of tax residence.

Existing domestic withholding tax exemptions such as the above may not apply to payments of interest where the interest payment is made to an associated entity (for the purposes of outbound payments defensive measures) that is resident in a territory that is on Annex I of the EU list of non-cooperative jurisdictions or in a zero-tax or no-tax territory. There is an exclusion from outbound payments defensive measures for payments of interest on quoted Eurobonds and wholesale debt instruments where it is reasonable to consider that the company making the interest payments is not, and should not be, aware that the interest is payable to an associated entity.

Tax treatment of profit participating interest

Section 110 contains provisions which deny a tax deduction for profit participating interest for certain transactions commonly referred to as "double no tax structures". This seeks to discourage a qualifying company from entering into "hybrid" arrangements where profit participating interest payments made by a qualifying company are not subject to tax in the hands of the recipient, due to some form of participation or similar exemption.

There are a number of exemptions from these anti-avoidance provisions (such that profit participating interest will continue to be tax deductible), including where the interest is paid to:

1. an Irish tax resident person; or
2. a person who is, under the laws of an EU Member State (other than Ireland) or a country with which Ireland has entered into a double tax treaty (a "relevant territory"), subject, without any reduction computed by reference to the amount of the interest, to a tax which generally applies to foreign source interest received in that territory (the "subject to tax" test), or where Irish withholding tax has been deducted at the standard rate in force at the time of payment; or
3. a pension fund, government body or other person resident in a relevant territory who under the laws of that territory is exempted from tax which generally applies to profits, income or gains in that territory, provided such person is not a specified person (the meaning of "specified person" is discussed below).

Where these particular exemptions are relied upon, the PPN may contain a representation as to the taxable status of the noteholder. In addition, profit participating interest paid in respect of quoted Eurobonds and wholesale debt instruments should be tax deductible provided that:

1. the person holding the quoted Eurobond or wholesale debt instrument is not a "specified person" in relation to the qualifying company; or
2. if the person holding the quoted Eurobond or wholesale debt is a "specified person" in relation to the qualifying company, the qualifying company was not aware at the time the PPN was issued that interest payable in respect of the instrument would not be "subject to tax" in a relevant territory as outlined above.

A "specified person" is a company which directly or indirectly "controls" the qualifying company, is "controlled" by the qualifying company or is, with the qualifying company, under the common "control" of a third company. A person has "control" of a company where either through the holding of shares, voting power, or other powers conferred on it, the person can ensure that the affairs of the company are conducted in accordance with its wishes. A person can also have "control" of a company for the purposes of Section 110 where it has significant influence over the company, being the ability to participate in the financial and operating decisions of the qualifying company, together with holding, directly or indirectly, more than 20% of the company's shares or PPNs. A person (or a group of related persons) will also be a "specified person" in relation to a qualifying company where the qualifying company has acquired assets from that person, has made loans to that person, holds loans made to that person or has entered into swap arrangements with that person, where the aggregate value of such assets, loans, or swap arrangements represents not less than 75% of the aggregate value of the qualifying company's assets.

Irish real estate related investments

Certain targeted measures apply to tax gains arising to Section 110 companies investing in Irish real estate backed loans. Section 110 companies that have no exposure to Irish real estate are unaffected by these measures.

A restriction on the deductibility of profit participating interest can apply to the extent that the qualifying company carries on a "specified property business" (as defined), which includes, inter alia, holding and / or managing a loan which is secured on, and which derives its value from, or the greater part of its value from, directly or indirectly, Irish land. However, the interest restriction does not apply to interest paid to certain categories of excluded persons, including persons within the charge to Irish corporation tax or Irish resident individuals, certain types of Irish and EU pension arrangements, certain Irish regulated funds, and EU/EEA nationals or EU/EEA companies where certain conditions apply.

In addition, in recognition of the importance of the securitisation industry to the Irish economy, activities such as CLO transactions, CMBS/ RMBS transactions, loan origination business and sub-participation transactions (in each case, as defined) are specifically excluded from the scope of the provisions.

The interest restriction also extends to profit participating or excessive interest paid by a Section 110 company which holds and/or manages shares that derive their value, or the greater part of their value, directly or indirectly from Irish land. However, the exclusions outlined above continue to apply.

VAT and stamp duty

The activities of an SPV are often outside the scope or exempt activities for the purposes of VAT. The SPV will therefore generally have only a limited ability to recover any VAT charged to it. There is also a specific exemption from Irish VAT in relation to investment management and administration services provided to a qualifying company. From 1 March 2023 this management exemption will not be available to a qualifying company which holds plant and machinery.

Assuming the SPV remains a qualifying company for the purposes of Section 110, stamp duty will not apply on the issue or transfer of notes issued by the SPV. Stamp duty is also not payable on any instruments creating security over Irish assets.

Double tax treaties

Ireland is party to an extensive range of double tax treaties which often ensure that an Irish resident SPV can receive income on its underlying assets with zero or reduced foreign withholding tax. Ireland has signed comprehensive double tax treaties with 76 countries. In addition, a number of new tax treaties are at various stages of negotiation. A full list of Ireland's tax treaties is available on www.revenue.ie or alternatively can be requested from your usual Walkers contact.

EU developments - ATAD tax treaties

Similar to all EU member states, Ireland was required to implement a number of corporation tax measures as a result of the EU Anti-Tax Avoidance Directives ("ATAD") – the EU's response to the OECD's Base Erosion and Profit Shifting ("BEPS") project of corporation tax reform.

Hybrid mismatch provisions are designed to neutralise arrangements where amounts are deductible from the income of one entity but are not taxable for another, or the same amounts are deductible for two entities. The rules are complex and accounting considerations are relevant. However, a noteholder should not in general be treated as an associated enterprise of a qualifying company merely as a result of holding notes, meaning that in many cases payments of interest by a qualifying company should not come within the scope of hybrid mismatch provisions. Reverse hybrid mismatch provisions should not impact a qualifying company as it is not considered tax transparent for Irish tax purposes.

The interest limitation rule ("ILR") seeks to link a taxpayer's allowable net interest deductions directly to its level of earnings, by limiting the net deduction to 30% of tax-adjusted EBITDA, subject to certain exemptions / exclusions. A restriction only applies if the borrowing costs of a relevant entity (deductible interest equivalent) exceed interest equivalent taxable revenues by more than 30% of EBITDA or (if greater) the de minimis amount. The de minimis amount is, in respect of an accounting period of 12 months, €3,000,000, and in respect of an accounting period of less than 12 months, €3,000,000 reduced pro rata.

The 'group ratio' and 'equity ratio' provisions of the ATAD ILR have also been introduced and the legislation makes, inter alia, the equity ratio provisions available to an entity which qualifies as a "single company worldwide group". A company that is neither a standalone entity (e.g. because it has a single shareholder such as a share trustee company) nor a member of a consolidated group for accounting or Irish tax purposes may qualify as a "single company worldwide group". In practice, these provisions may enable certain non-consolidated securitisation SPVs to apply the equity ratio and thereby disapply the ILR in certain circumstances, irrespective of whether the SPV has exceeding borrowing costs in excess of the higher of 30% of its tax-adjusted EBITDA or €3,000,000. The provisions are complex and require analysis on a case by case basis to assess the impact, if any.

OECD Model GloBE Rules and the EU Minimum Tax Directive / Pillar Two

The OECD's Global Anti-Base Erosion Model Rules ("GloBE Rules") published in December 2021 are aimed at ensuring that large Multinational Enterprises ("MNEs") will be subject to a global minimum 15% tax rate. In December 2022 the Council of the EU unanimously adopted the agreed compromise text of a directive to implement the GloBE Rules in the EU (the "Minimum Tax Directive"). Ireland subsequently implemented the Minimum Tax Directive into Irish law with the provisions applying to in scope entities for accounting periods commencing on or after 31 December 2023 (the "Irish Pillar Two rules"). The Irish Pillar Two rules introduce a minimum effective tax rate of 15 per cent. for MNE groups, large-scale domestic groups and some standalone entities of a certain size.

The rules are complex and require detailed consideration on a case-by-case basis as to whether an entity is in scope, and the impact, if any, of the provisions.

If an Irish SPV is regarded as part of an MNE group (or large-scale domestic group) which has consolidated revenues of more than EUR 750 million a year in at least two out of the previous four years, or if the SPV has such revenues on a standalone basis, it may be within the scope of the Irish Pillar Two rules. The revenue threshold is adjusted on a pro-rata basis if the relevant accounting period is less than or exceeds 12 months.

An SPV will be part of a "group" for Pillar Two purposes if it is included in consolidated financial statements on a line by line basis, or if it is excluded from consolidation solely based on its small size, on materiality grounds or on the grounds that it is held for sale. In addition, in circumstances where a parent entity is not required to prepare consolidated financial statements, a deemed consolidation test must be applied.

In practice, many SPVs that are legally established as orphan vehicles (such as in the case of bankruptcy remote securitisation vehicles) are unlikely to be consolidated into any other entity. However, there are circumstances where consolidation could be required and an analysis must be undertaken in each case.

A number of entities are also excluded altogether from the application of the Irish Pillar Two provisions (such as pension funds, certain investment funds (as defined) and their 95% or more subsidiaries), and in-scope entities where the jurisdictional effective tax rate is not less than 15% should not be affected although certain compliance obligations may apply.

Where an entity is in scope, complex rules apply to calculate the entity's profits for Pillar Two purposes and the effective tax rate, particularly in the context of consolidated groups, and Irish domestic top-up tax may apply if the jurisdictional effective tax rate is below 15%. An entity which is part of a consolidated group may also be assessed on a standalone basis if the ultimate parent entity of the group has an ownership interest of less than 30% (minority owned constituent entity). Where the minority owned constituent entity provisions apply, the entity's effective tax rate is calculated on an entity basis rather than a jurisdictional basis. In the case of an Irish Section 110 SPV, this may result in the effective tax rate being above 15% since a qualifying company is subject to corporation tax at the rate of 25%. However, the effective tax rate must be assessed based on the computational rules for Pillar Two purposes.

In recognition of some of the potential challenges which may be faced by securitisation entities as a result of the GloBE Rules, the OECD released administrative guidance with respect to securitisation entities and addressed the treatment of securitisation entities which are part of an MNE group under a jurisdiction's domestic minimum top-up tax regime. The guidance was implemented into Irish law in Finance Act 2024 and applies to an Irish SPV that is a securitisation entity (as defined) and which is part of an in-scope consolidated group for Pillar Two purposes. Where applicable, the legislation provides for the domestic top-up tax liability (if any) of the Irish securitisation entity to be imposed on other non-securitisation entity group members in Ireland and not on the securitisation entity itself. As a result, the securitisation entity should remain broadly tax neutral and not subject to additional tax under Pillar Two. If, however, there are no group members in Ireland, or all other group members are themselves securitisation entities, the exemption from the charge to domestic top-tax for the securitisation entity does not apply. While not relevant to all securitisation transactions, the exemption is a welcome development.

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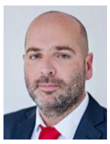

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