Arthur Cox

Structured Finance Guide

AUGUST 2007

CAPITAL MARKETS GROUP

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Arthur Cox is one of Ireland's leading law firms. It comprises 300 lawyers including 90 partners. The firm's principal office is located in Dublin and we also have offices in Belfast, London and New York. The practice of the firm encompasses all aspects of corporate, business and finance law.

Arthur Cox was the No.1 Irish Legal Adviser, by value, to European Capital Markets in the Thomson Financial European Capital Markets Review 2006.

Arthur Cox Listing Services Limited is the leading Irish listing agent for the listing of debt securities on the Irish Stock Exchange.

ESTABLISHING SPECIAL PURPOSE VEHICLES IN IRELAND

For Russian Loan Participation Note Structures

Introduction

Ireland has firmly established itself as a jurisdiction for the location of special purpose vehicles (SPVs) for structured finance transactions, particularly Russian Loan Participation Note (LPN) and other corporate fundraising structures. Favourable tax laws allow the structures to be, in most cases, tax neutral and a "quoted eurobond" exemption, together with the advantageous Irish-Russian double taxation treaty, allows interest on loans between Irish SPVs and Russian counterparties to be paid gross in most cases. In addition, recent changes in law that allow the use of private companies for most bond transactions will make incorporating an Irish SPV significantly easier and cheaper. Ireland is not a tax haven jurisdiction however, and careful tax planning at an early stage of any transaction is required. Once the optimum tax treatment is achieved however, an SPV located in Ireland benefits from the fact that it is an EU issuer located in an "on shore" jurisdiction.

Legal system

Like the United Kingdom and the U.S.A., Ireland is a common law jurisdiction and its legal concepts will be recognised by most investors, originators and advisers. Ireland recognises the concept of a trust and the laws in this regard are very similar to the laws of England. In addition, the laws relating to personal property and the transfer of assets and the concepts of legal and equitable title are similar to those in England.

Ireland's international status

Ireland is a member of the EU and also of the OECD. For many originators and potential investors, this is one of the more significant advantages of locating an SPV in Ireland. Investors in some jurisdictions may want to purchase debt issued by EU/OECD issuers only, and the inability to access those investors if the SPV is located elsewhere may affect the pricing of a transaction.

In addition, there is a current international trend away from investing in so-called tax havens. Some investors take comfort from the fact that Ireland is not a tax haven and has a developed corporate legal system and tax structure.

Taxation

The predominant reasons for Ireland's popularity as an SPV location are its favourable tax regime, the fact that it is an "on-shore" jurisdiction and the professional and administration services that are available locally.

The following tax points are of particular relevance:

(a) *Entity-level tax - Section 110*

It is essential to ensure that the SPV is tax neutral. While the SPV itself is liable to corporation tax at 25%, the tax is applied on the SPV's net taxable profit, which, with careful structuring, is generally maintained at a negligible level as there is no minimum profit required for tax purposes. This is achieved by having the SPV's tax deductible expenditure equal to its income. The relevant tax legislation, which is contained in Section 110 of the Taxes Consolidation Act, 1997 (Section 110). In short, Section 110 provides that the taxable profits of a company (a "qualifying company") involved in the holding and/or management of "qualifying assets" should be computed on the same basis as a trading company. Consequentially, the cost of funding and other related expenditure is tax deductible. In addition, swap payments, payments to service providers and payments made under certain subordinated loans (see profit extraction below) will in most cases also be tax deductible.

A qualifying asset consists of any financial asset, or any interest in a financial asset. "Financial assets" are defined to include the following:

"shares, bonds, other securities, futures, options, swaps, derivatives and similar instruments, invoices and all types of receivables, 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 instruments."

The range of assets is extensive and, as such, most structured finance vehicles (including vehicles used for Russian LPN Structures) can qualify as Section 110 companies in such a way that the transaction will be tax neutral. As a result, Ireland is an ideal jurisdiction for locating an on-shore, EU/OECD issuer with no tax leakage.

(b) *Withholding tax*

It is obviously crucial to any structure that payments to investors be made gross and not subject to any withholding. If the securities are issued in either bearer or registered form (the law was changed in April 2006 to allow securities in registered form to qualify for the quoted eurobond exemption), carry a right to interest, are listed on a recognised stock exchange and are either held in a recognised clearing system or payments in respect of the securities are made through a paying agent located outside Ireland, then payment on the securities will qualify for the "quoted eurobond" exemption and may be made gross. LPN structures normally satisfy this exemption. Alternatively, investors can rely upon the Irish domestic exemption from withholding tax for SPVs which permits interest payments made to a person resident in an EU member state (other than Ireland), or a country with which Ireland has a double tax treaty (such as Russia), to be made free from withholding tax. This exemption applies automatically without any application being required. Interest payments between Section 110-qualifying companies are also free of withholding tax.

In addition, the Finance Act, 2003 also extended exemptions from withholding tax for notes with denominations of €500,000 or more issued by an SPV with a maturity of less than two years in various circumstances, including where the notes are held in a recognised clearing system or a paying agent located outside Ireland is used or where a foreign noteholder provides a declaration of non-Irish residence.

(c) *International Accounting Standards (IAS)*

The taxation issues surrounding the introduction of IAS were resolved in Ireland by continuing to allow SPVs to be taxed on the basis of accounts prepared in accordance with Irish GAAP as it existed in December 2004, unless they elect otherwise. This applies to existing and new SPVs.

(d) *Stamp duty*

On the assumption that the SPV remains a qualifying company for the purposes of Section 110 mentioned above, stamp duty will not apply on the issue or transfer of notes. Stamp duty can apply on the transfer of Irish assets, but should not be payable on the transfer of non-Irish assets. Stamp duty (which was minimal) is no longer payable on any instrument creating security over Irish assets.

(e) *VAT*

SPVs are engaged in exempt activities, and so will generally have limited ability to recover any VAT charged to them. Management services (which includes portfolio management services for CDOs) supplied to an SPV, whether by an originator or otherwise, can be supplied exempt from Irish VAT.

(f) *Revenue notification and opinions*

An SPV is merely required to notify the Revenue and give the appropriate confirmations that the SPV satisfies the conditions in Section 110. This is simply a notification and self-certification process and no return approval or Revenue Ruling is required, unlike some other jurisdictions.

(h) *Double tax treaties*

Ireland is also party to an extensive range of double taxation treaties that, depending on the particular treaty, can ensure that the SPV receives income on its underlying assets free from withholding tax. Avoiding tax leakage in this manner is very important to a transaction. The Irish-Russian double taxation treaty is very favourable in this regard, with no withholding on interest payments. We have established streamlined procedures for obtaining the required treaty protection between Ireland and Russia. A list of other countries with which Ireland has treaties is available upon request.

(i) *No minimum profit*

An Irish company is not required to make an annual statutory minimum profit for Irish tax purposes. Instead, the SPV need only receive a nominal fee at the start of the transaction. Interest on the loan to the Russian entity can then exactly match interest on the LPNs.

Listing

The Irish Stock Exchange (ISE) has, in the last few years, become the largest European exchange for the listing of asset backed debt securities such as those issued by SPVs. The ISE provides an efficient and comparatively speedy response time to draft offering circulars. Currently, the ISE guarantees comments within three days of receipt of the first draft of an offering circular. In addition, the ISE played a significant role in the drafting of the disclosure standards under the Prospectus Directive and has taken a very proactive role to ensure the Prospectus Directive is implemented smoothly in Ireland.

Arthur Cox advises on the listing of a wide variety of asset-backed transactions and has established a listing company, Arthur Cox Listing Services Limited for this purpose. Details of our experience and services are available on request.

Procedure for establishing an SPV in Ireland

(a) *Private limited liability company or plc*

Following a change of law in December 2006, an Irish private company can now issue bonds to the public if the issue falls within certain offer exemptions. The most likely applicable exemption is where the bonds issued by the Irish private company have a minimum denomination of at least €50,000 (which is usually the case to avoid the provisions of the Transparency Directive). If this is not the case, another exemption may be available.

Using a private company rather than a public limited company (plc) has the following advantages:

1. the minimum number of shareholders is 1 (for a plc it is 7); and
2. the minimum issued share capital is €1 (for a plc it is €40,000) and no trading certificate is required for a private company, meaning an Irish SPV can be fully incorporated and ready to start trading in five working days.

If a plc is required, it normally takes approximately three weeks to fully incorporate the company. This allows sufficient time for the company to be formed and a trading certificate to be obtained. Excluding legal fees, it costs approximately €400 to incorporate a plc and €100 to incorporate a private company.

In addition, it is worth noting that there are no "thin capitalisation" rules for SPVs in Ireland and therefore no limit to the value of assets that can be securitised, subject to a minimum amount of €10 million or its equivalent.

On most transactions, it is not necessary for the SPV to obtain any licences or government approvals. In addition, the same SVP can be used to do multiple LPN transactions without any government approvals etc.

(b) *Ownership / Directors / Auditors*

SPVs are usually set up as orphan companies with their shares being held on charitable trust. SPVs are required to have at least two individuals acting as directors and the annual financial statements of the SPV are required to be audited. The first set of accounts must be prepared within 18 months of incorporation.

There are a number of institutions operating in Dublin which provide corporate services to SPVs (such as administration, directors and share trustee and company secretarial services). Arthur Cox can obtain quotes from corporate service providers and auditors if required. Most international banks have a presence in Dublin, and so complicated cashflow models can usually be managed by an Irish administrator.

Auditors Consents no longer required

A further change in Irish law in December 2006 has reduced the circumstances in which it is necessary to obtain the consent of an expert to the inclusion in a Prospectus of a report prepared by such expert. In particular, in most transactions it will no longer be necessary under Irish law to obtain the consent of an auditor to the inclusion of historical financial information in a Prospectus where such information was not prepared for the purpose of inclusion in the Prospectus. This will be particularly relevant for LPN structures that use an Irish SPV.

Conclusion

By virtue of its favourable tax and corporate laws and its status as an EU/OECD member, Ireland is the ideal location for the establishment of an issuance vehicle for a wide range of structured finance transactions.

If you are considering such a transaction or would like to discuss any of the issues discussed above, please do not hesitate to contact any of the Arthur Cox people listed on the back page.

Recent Transactions

Arthur Cox has advised on substantially all of the LPN and Russian corporate fund-raising structures to use an Irish SPV. In particular, we have incorporated and advised Irish SPVs for the following Russian borrowers:

Stand-Alone Transactions	**LPN Programmes**
Alfa-Bank	Bank St. Petersburg
Bank Soyuz	Bank VTB-24
Bank Zenit	MDM Bank
Credit Bank of Moscow	Renaissance Capital
EuroChem Mineral and Chemical Company	URSA Bank
Gazprombank	
Locko-Bank	
MDM Bank	
National Bank Trust	
Nizhenkamskeftekhim Inc. (NKNK)	
NOMOS-Bank	
OJSC Coal Company Kuzbassrazrezugol	**ECP Programmes**
Promsvyazbank	Gazprombank
Raspadskaya	Russian Standard
Tatfondbank	
TransCapitalBank	
TransCreditBank	
Transneft	
Trust Investment Bank	
Vostochny Express Bank	

In many cases, these Irish SPVs have entered into a number of repeat transactions. All of these transactions are listed on either the Irish Stock Exchange (mostly) or the London Stock Exchange.

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This memorandum is a general summary and is not a complete statement of the law. It is not intended to give specific legal advice. If you require advice please contact your usual Arthur Cox contact or any of the persons listed.

Contacts

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Glenn is a partner in our Capital Markets Group. Formerly a capital markets partner at Allen & Overy, Glenn specialises in all forms of capital markets transactions, particularly repackagings, CDOs, CLOs, bond issues, debt issuance programmes, LPN structures, derivatives and equity linked products such as convertibles and exchangeables. He also advises on a range of banking and security issues and on the capital markets aspects of restructurings. Glenn has led the Arthur Cox team on all Russian LPN transactions upon which the firm has advised.
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Caroline Devlin
Caroline is a partner in our Tax Group. She advises domestic and international companies on tax planning, and has extensive experience in advising on tax planning and structuring aspects of securitisations, tier 1 instruments and other structured products. Caroline also advises on tax aspects of mergers and acquisitions, and other tax planning areas. She is the Law Society's representative on the Irish Revenue's IFRS Consultation Group. Caroline leads the Arthur Cox tax team on LPN transactions.
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Helen Berrill
Helen is Director of Listings of *Arthur Cox Listing Services Limited*, having joined the firm from the Irish Stock Exchange. She has extensive specialist debt securities experience and has been involved in the financial services industry since 1995. As Head of Specialist Debt Securities listings at the Irish Stock Exchange from 1999 to March 2004, Helen was responsible, amongst other things, for drafting the Exchange's current listing rules for asset backed debt securities, specialist bonds and specialist warrants. Helen oversaw the listings of all transactions during this five year period of substantial growth at the Irish Stock Exchange and carried out senior reviews to ensure understanding of transaction amongst her colleagues and to ensure an efficient, smooth, stream lined approach at all times. As such, she has an unrivalled knowledge of the Exchange's rules and procedures.
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