



Irish Property Funds - An Introduction

The past few years have seen increased interest amongst US and European asset managers in Irish and EU based real estate assets. William Fry has advised numerous managers on the financing and acquisition of these assets, together with the subsequent establishment of an Irish-domiciled investment fund to hold the property.

Property funds domiciled in Ireland are typically established as Qualifying Investor Alternative Investment Fund ("QIAIFs") as QIAIFs confer considerable advantages both from the perspective of liquidity and tax efficiency.

QIAIFs fall under the Central Bank's AIF Rulebook and are subject to the provisions of the EU's Alternative Investment Fund Managers Directive ("AIFMD"). A QIAIF must appoint an Alternative Investment Fund Manager ("AIFM") who will also be regulated under AIFMD.

AIFMD permits AIFMs authorised in the EU to manage and/or market their products on a pan-European basis. This passport regime means that a QIAIF established in Ireland can be marketed right across the EU.

A significant advantage of the QIAIF product in terms of speed to market is that it is subject to a filing only authorisation process (as opposed to a prior full review process) by the Central Bank.

QIAIF Structure

QIAIFs can be established as an investment company, an ICAV, a unit trust, a common contractual fund or an investment limited partnership. A QIAIF can be open-ended, open-ended with limited liquidity or closed-ended.

Choice of Structure

The most popular structure for new QIAIFs is the Irish Collective Asset Management Vehicle or "ICAV", a corporate structure introduced in 2015 that is specifically designed for investment funds. The ICAV has certain advantages when compared against the other product types available in Ireland, such as the investment company. An umbrella ICAV can publish audited financial statements on a sub-fund by sub-fund basis and can dispense with the requirement to hold an annual general meeting of shareholders. The ICAV is not subject to the risk spreading/diversification requirements, which currently apply to investment companies under Irish company law. This is of particular benefit to QIAIFs, which, under the AIFM Directive, are not subject to risk diversification requirements. The ICAV also has the ability to "check the box" to be treated as a transparent entity for U.S. federal income tax purposes. As a result of these advantages, the ICAV has become the corporate vehicle of choice for newly established investment funds.

Umbrella Funds - Segregated Liability

All QIAIFs, irrespective of their legal form, may be structured as an umbrella fund i.e. a structure with more than one sub-fund or portfolio, with segregated liability between the sub-funds. This means that as far as Irish law is concerned, automatic ring fencing of liabilities exists between one sub-fund and the other sub-funds in the umbrella such that there is no cross-contamination or “dipping” into the assets of one sub-fund to discharge the liabilities of another.

Investment in Property and Property Related Assets

A property fund, established as a QIAIF, is exempt from the investment, leverage and borrowing restrictions that apply to retail funds and may thus invest without limitation in:

- Real estate of any kind (commercial, mixed use, residential, etc.)
- Development land
- Debt (loans, loan notes, debentures, etc.)
- Special Purpose Vehicles - to warehouse assets or to enhance tax efficiency
- Mortgage-backed securities and other asset-backed securities

No borrowing or leverage limits apply to a QIAIF. Such borrowing or leverage may be secured by pledging, mortgaging or charging any or all of the investments of a QIAIF. However, a QIAIF can only give security over its assets in respect of the QIAIF's own borrowings; it cannot give security for an investor's borrowings.

Although a QIAIF may not issue debt securities it can issue notes, on a private basis, to a lending institution to facilitate financing arrangements.

There is no restriction on the amount of the QIAIF's net assets that may be invested in any single property. However, a QIAIF structured as an investment company has a statutory obligation to spread investment risk (no such obligation applies in the case of a QIAIF established as an ICAV).

There is also no restriction on the amount of the net assets of a QIAIF which may be invested in properties which are vacant, in the process of development, or requiring development.

Valuation

It is common practice for the AIFM of a property QIAIF to appoint a qualified independent valuer. The criteria for the valuer's appointment must be set out in the QIAIF's prospectus and periodic reports. Typically, the real estate assets of a QIAIF are valued at market value at least twice yearly.

Marketability

Product distribution is a key component to the success and growth of any investment fund. A QIAIF is a highly marketable product as authorisation under the AIFMD Regulations has “single passport” advantages in the EU. This means that regulators of each of the other EU Member States are obliged to permit the sale/marketing of an Irish registered QIAIF in their jurisdiction subject to certain notification procedures and compliance with local marketing laws. The relative ease with which QIAIFs may be sold or passported on a European basis makes them a highly attractive and marketable product.

Qualifying Investors

Investors in a QIAIF are required to be either sophisticated investors or institutional investors. In order to avoid an obligation to produce certain onerous pre-contractual documents, it is recommended that a QIAIF only take subscriptions from an investor who is a professional client within the meaning of Annex II of MiFID

II, which is defined as a client who possesses the experience, knowledge and expertise to make its own investment decisions.

There are a number of entities which are automatically regarded as a professional client such as:

- Entities that are required to be authorised or regulated to operate in financial markets (investment firms, collective investment schemes and management companies of those schemes etc);
- National and regional governments, public bodies that manage debt, central banks and international institutions such as the IMF and the ECB;
- Other institutional investors whose main activity is to invest in financial instruments, including entities dedicated to the securitisation of assets or other financing transactions.

There is also a procedure whereby investors other than those mentioned above can elect to be treated as a professional client. This involves waiving some of the protections afforded by the MiFID II conduct of business rules.

Conditions applicable to Subscription

The minimum initial subscription for an investor in a QIAIF must normally be the equivalent of €100,000. A QIAIF may not accept subscriptions from persons that group amounts of less than €100,000 for individual investors. The QIAIF may grant an exception to these requirements for certain investors such as the AIFM or the investment manager.

The initial offer period of a real estate QIAIF may extend up to two years and six months provided that the terms of the initial offer ensure that early shareholders are not prejudiced by the arrangements.

As QIAIFs do not have to be actively marketed to the public, most QIAIFs have a very small number of investors. However, QIAIFs must be open to subscription by the public.

Prospectus Requirements

The Prospectus must:

- describe the investment objectives and investment and borrowing policies of the QIAIF. These descriptions must be comprehensive and accurate, readily comprehensible to investors and be sufficient to enable investors to make an informed judgement of the investment proposed to them;
- contain quantitative parameters on the extent of leverage which is engaged in by the QIAIF (there is no limit on the level of leverage which may be employed by a QIAIF);
- contain a prominent risk warning which will make specific reference to the potential for the above average risk involved and the suitability of this type of investment only for people who are in a position to take such risks; and
- indicate in a prominent position that the QIAIF has been authorised for marketing solely to qualifying investors and specify that while the fund is authorised by the Central Bank, the Central Bank has not set any limits or other restrictions on the investment objectives, the investment policies or on the degree of leverage which may be employed by the QIAIF.

Authorisation Process

A key advantage of establishing a QIAIF in Ireland is the speed of the authorisation process, with the Central Bank providing regulatory approval within 24 hours of the receipt by it of a complete application for authorisation. In practice, the authorisation process for a QIAIF generally takes eight weeks, to allow for the various service provider contracts to be negotiated and the prospectus and other QIAIF documentation (such as the constitutional document) to be agreed.

Taxation

A QIAIF is not subject to any tax in Ireland on rental income or capital gains derived from real estate or real estate related assets (foreign taxes may apply however). In addition, no Irish withholding tax applies to income distributions or redemption payments made to non-Irish resident investors regardless of where they are resident with the exception of distributions from QIAIFS that invest in Irish real estate or assets deriving their value from Irish real estate (described as “IREFs”).

Ireland introduced a new tax regime for Irish real estate funds in Finance Act 2016. Under the new regime, IREFs continue to be exempt from corporation or income tax on their profits. However, 20% withholding tax will apply to certain payments made by IREFs and withholding tax requirements will apply to certain purchasers of IREF units in the secondary market. Irish withholding tax must be withheld at 20% on distributions and other payments (including payments on redemption) made by IREFs to their investors. The 20% withholding tax on distributions, redemptions and other payments is imposed on the amount of the payment that is derived from the profits of the IREF arising from Irish real estate assets (eg, rental income, gains on disposal and development profits). Certain categories of investor are exempt from the withholding tax charge including other regulated investment funds, pension funds and insurance companies, in each case resident in either Ireland or another EU Member State. It is also possible for foreign investors not falling within the exempted categories to claim a reduction or exemption from the withholding tax under Ireland’s double tax treaties. The new regime for IREFs does not affect the existing tax treatment of QIAIFs that do not hold Irish real estate assets.

QIAIFs are exempt from Irish income tax and Irish corporation tax and are not subject to tax on their net asset value. Additionally there is no stamp duty payable on the transfer of shares in a QIAIF. An “exit tax” may arise for investors who are resident in Ireland for tax purposes (or ordinarily resident) on a “chargeable event” (distributions, redemptions, repurchases, transfers and cancellation of units or on every 8 year anniversary). Funds set up as common contractual funds, however, are treated as tax transparent by the authorities and the income and gains of such funds are treated as though they accrue to the investors directly.

Funds in Ireland are not required to charge VAT as financial services are exempt, however, funds may be required to register and self-account for VAT if they receive certain taxable services from suppliers outside of Ireland including legal advisory services, tax advisory services or advertising services.

It is also of note that Ireland has a wide Double Taxation Treaty network available to it with approximately 80 agreements. However, each jurisdiction should be considered on a case by case basis to determine whether an agreement can be availed of by a QIAIF and its shareholders.

Joint Ventures

Given the regulated nature of a QIAIF, it can be difficult to enshrine common joint venture terms (ROFR, pre-emption, veto, etc.) into fund documentation. There are various solutions to this in circumstances where joint venture partners wish to operate a QIAIF in a more conventional JV partnership manner. These include inserting a partnership below the QIAIF where the QIAIF holds only a limited partnership interest and the limited partnership, through its general partner, holds the asset. Tax advice is a key factor in this and we are happy to engage on this in relation to the JV partners both individually and jointly in terms of agreeing the best structure.

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