

# THE USE OF JERSEY SPECIAL PURPOSE VEHICLES IN STRUCTURED FINANCE TRANSACTIONS

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## INTRODUCTION

As a politically stable and fiscally advantageous financial centre, Jersey is a prime jurisdiction in which to incorporate a special purpose vehicle ("SPV") as the issuer of debt securities.

Jersey-based SPVs have long been used in connection with a wide variety of international financial arrangements. These have included structures established for the purpose of making investments off-balance sheet, securitising assets, tax driven financing and the repackaging of financial instruments.

A variety of legal vehicles are available:

- a Jersey incorporated company which issues debt instruments ranging from short-term commercial paper through to medium term notes and long-term bonds or redeemable share capital rather than debt;
- a limited partnership issuing partnership interests ("LP"). Two new types of LP, separate and incorporated limited partnerships, are now also available; or
- a trust issuing units or trust interests.

As an SPV normally takes the form of a Jersey incorporated company issuing debt instruments this note focuses upon the establishment of an SPV for that purpose. This is relevant to: (i) a single issue or as a programme (a "**Securities Programme**"); and (ii) SPVs that are consolidated on the sponsor/promoter's balance sheet, orphans or have an off-balance sheet issuer. Other bespoke arrangements for LPs or trusts offer no overriding difficulties in principle but would call for separate analysis of the legal issues.

## CORPORATE SPVs

Jersey companies are constituted pursuant to, and governed by, the provisions of the Companies (Jersey) Law 1991, as amended (the "**Companies Law**"). A Jersey company can normally be incorporated very quickly. The urgent incorporation service allows a company to be incorporated within twenty-four hours, provided that all required information has been supplied.

## CORPORATE GOVERNANCE AND ADMINISTRATION

A Jersey company can be incorporated as a company with shares carrying either limited or unlimited liability. The shares can have a stated par value or the company can be established as a no-par value company. The shares can be denominated in any currency and, if necessary, different classes of shares can be denominated in different currencies. There is no minimum share capital requirement. Companies can also be established with members whose liability is limited by guarantee.

A Jersey company is either a private company or a public company. A company is, or is treated as, a public company if its memorandum of association states it to be a public company, if it has more than thirty shareholders, if it issues a prospectus or if

its securities are admitted to trade on a regulated market - otherwise it is a private company.

A private company must have at least one director and a public company must have at least two directors. The directors need not, as a matter of the Companies Law, be resident in Jersey but it may be desirable for the tax efficiency of a structure that a majority of the directors of the SPV are Jersey resident. The Jersey Financial Services Commission (the "**Commission**") may also require an SPV to have at least two Jersey resident directors as a condition for the issue of regulatory consents required for the issue of securities (as to which see below). Provided that certain conditions are satisfied, the SPV may have corporate directors.

The business of the SPV may, in general, be carried on by its directors, subject to any limitations imposed by its memorandum or articles of association. Directors of an SPV are under a duty to act honestly and in good faith with a view to the best interests of the company.

An SPV must have a company secretary (not necessarily in Jersey) which, in the case of a public company, must be suitably qualified. It must also have a registered office in Jersey, the address of which must be given on all business stationery and notified to the Commission on incorporation.

Every company must keep a register of shareholders, which must be kept at its registered office or at such other place in Jersey as is notified to the registrar of companies. An SPV must also keep a register of its directors and secretary.

There is no requirement that a company should keep a register of mortgages or charges.

Shares in an SPV may be issued as ordinary, deferred, preference or redeemable shares with differing rights as to dividend, voting, participation and winding up etc. and may be issued at par or at a premium of any amount. The Companies Law sets out rules providing for the maintenance of capital governing such things as distributions, reductions of capital and redemptions of shares. The Companies Law now permits greater flexibility in the payment of distributions, which can be paid from any account of the company save for the capital redemption reserve or nominal capital account.

Both private and public companies are required to maintain books of account. A private company is not required to audit or file its accounts but a public company must appoint auditors and must file audited accounts. In certain cases where a private company issues debt securities the Commission may require the SPV to produce audited accounts. Audited accounts of an SPV are not available for public inspection unless the company is a public company.

An SPV must make an annual return (and pay an annual filing fee - currently £150 if paid on time) to the registrar of companies before the end of February in each year. Otherwise, it is only necessary to file any change in the company's registered office together with special resolutions.

With permission of the Commission, it is possible for Jersey companies to migrate to other jurisdictions where such migration is possible and companies incorporated in other jurisdictions may migrate to Jersey.

#### OFF-BALANCE SHEET STRUCTURES

Often SPVs are held as an independent or orphan entity with their entire issued share capital held by a charitable or non-charitable purpose trust. This briefing note assumes such trusts are constituted as Jersey trusts, with a Jersey trustee and administered within Jersey.

Generally, such structures use a charitable trust which is constituted with charitable objects. The Securities Programmes are structured to generate a small profit which the SPV can distribute as a dividend to the trust which can be distributed by the charitable trustee to the charitable objects. This assists in fulfilling the objects of the trust and reinforcing the independence of the structure from the promoter/sponsor.

As an alternative to a charitable trust, it is possible to establish a non-charitable purpose trust, i.e. where the share capital of the SPV is held by the trustee on trust to carry out specified purposes which do not qualify as charitable purposes. This means that the trust is established without ascertainable beneficiaries, but with a purpose stated in the trust instrument. A non-charitable purpose trust must have an "enforcer" distinct from the trustee with the ability to enforce the purposes of the trust. It follows that where it is possible to use a non-charitable purpose trust to establish a structure, the requirement to make distributions to charitable beneficiaries does not exist but regard must be had to the purpose for which the trust was established.

Jersey trusts can be established very quickly. There is no Jersey requirement that any licence, consent or other authorisation be obtained prior to the establishment of a trust in Jersey (other than in relation to the issue of units in a unit trust). Additionally, there is no register of trusts maintained in Jersey. The trust is established by the execution of an instrument of trust and the transfer to the trustees of the initial trust assets. The value of such assets is usually nominal.

All Jersey trusts are governed by the Trusts (Jersey) Law 1984, as amended (the "Trust Law"). The Trust Law provides that (subject to certain limitations) the terms of the particular instrument of trust determine the duties and obligations of the trustees. In some cases, the trustees may be required to enter into certain specific transactions. Sometimes the instrument of trust may restrict certain of their powers. The trustees may, for example, be required to form and hold the shares in the SPV, additionally, they may be restricted in their powers to dispose of the shares in the SPV or restricted in their powers to vote such shares in a specific way.

The Trust Law contains express provisions protecting trust assets from the creditors of a Jersey trustee if the trustee becomes bankrupt. The trustee's own assets are distinguished from those held in the trustee's capacity as a trustee. The latter assets are not available to the trustee's creditors.

### SPV AS A BANKRUPTCY-REMOTE VEHICLE

In most structured finance transactions the SPV will be set up as a bankruptcy-remote vehicle. This is achieved by:

- restricting the activities and indebtedness of the SPV through contractual undertakings and the constitutional documents;
- the SPV having no employees;
- the SPV having a known and identifiable group of creditors (i.e. the transaction parties);
- limiting the recourse which those parties have against the SPV;
- including non-petition language in the transaction documents (i.e. an undertaking by the other parties not to take insolvency proceedings against the SPV); and
- regulating the claims of the creditors of the SPV through an agreed order of priorities.

### TAXATION

There are no taxes on capital gains in Jersey and there is no duty upon the issue of either shares or debt securities.

The options for the tax status of an SPV are as follows:

- Zero rate company. There is a general zero rate of tax for most companies. All new SPVs are subject to the zero rate.
- Foreign tax resident. Jersey Law provides that a company which is incorporated in Jersey will not be considered to be resident in Jersey for tax purposes if (i) the Jersey company is centrally managed and controlled in a country or territory where the highest rate at which any company may be charged to tax on any part of its income is 20% or higher and (ii) the Jersey company is resident for tax purposes in that country or territory.

### REGULATORY PROVISIONS

Regulation of Securities Programmes is undertaken by the Commission.

Where a company is to act as an SPV, it will require regulatory consents and permits in order to issue securities. Prior to undertaking the formal application process, it is usual to obtain "in principle" consent for the proposed arrangement from the Commission. This involves providing the Commission with an outline of the scheme and obtaining their confirmation that, on the basis of the information provided, there is no reason "in principle" why the necessary consents and permits will not be forthcoming. "In principle" consent can normally be obtained in good time.

### CONSENTS REQUIRED

Prior to the issue of securities by an SPV, or the circulation of a prospectus or other offer document, the written consent of the Commission is required pursuant to the Control of Borrowing (Jersey) Order 1958, as amended ("COBO"). The provisions

of COBO enable the Commission to issue consents on a conditional basis which is normal practice with the standard conditions usually requiring:

- in the case of a Securities Programme, a stated maximum aggregate principal amount for the entire issue;
- an expiry date for the consent, expressed to be without prejudice to the validity of any notes issued;
- that there shall be no change in any of the principal parties to the Securities Programme or in the ownership of the SPV without the prior consent of the Commission;
- that the approval of the Commission be sought and obtained to any changes associated with the SPV, unless the changes will not materially affect the import of information previously supplied in connection with the relevant consent;
- that the circulation by the SPV of any prospectus, or offering circular, will be subject to the prior consent of the Commission; and
- that a reference (if any) to the consent in any prospectus or any other invitation of subscription will refer to the consent having been granted by the Commission under COBO and shall include a statement that the Commission is protected against liability arising from discharge of its functions.

Where a prospectus is issued (and where, therefore, the SPV will be, or be treated as, a public company for the purpose of the Companies Law), it is, in addition, necessary that the prospectus complies with the provisions of the Companies (General Provisions) (Jersey) Order 2002, as amended. A copy of the prospectus signed by the directors of the SPV must be filed with the registrar of companies.

### CELL COMPANIES

It is also possible to incorporate cell companies in Jersey. A cell company is a company which can create cells within which assets and liabilities can be segregated. Assets of a cell are only available to creditors and shareholders of that cell.

The administrative benefits of a cell company are significant. Once a cell company structure is in place, repeat transactions can be established in a much reduced time scale. This is particularly attractive in repackagings and other structured finance products where there are repeat transactions using the same core documents and the same key participants.

A framework can be established which includes all of the participants in the structure and master agreements entered into governing the contractual roles of those participants. Regulatory consents can be obtained in advance for the structure, and then, as new cells are added, the level of regulatory scrutiny that will be required is much reduced.

When particular transactions are planned - for example, adding a new vehicle to acquire receivables in a securitisation - a cell can be created specifically to act in that defined role. As the agreements and regulatory consents have already been agreed, a

new cell can be added at a fraction of the cost and time that would be required were the structure to be established from scratch.

Two types of cell company can be incorporated in Jersey:

- the protected cell company ("PCC"), which creates protected cells which do not have separate legal personality. A PCC has the advantages of flexibility and cost-effectiveness; and
- the incorporated cell company, which creates cells which are separate companies with their own legal identity, leaving no doubt as to the effectiveness of the ring-fencing within the cells.

#### USE OF THE CHANNEL ISLANDS SECURITIES EXCHANGE

Securities issued by SPVs can be listed on any relevant stock exchange in order to meet investor requirements. The Channel Islands Securities Exchange Authority Limited ("CISE") has received a number of recognitions which make it an attractive and increasingly popular option for listing debt securities.

The CISE is designated by the UK Inland Revenue (now "HM Revenue & Customs") as a "Recognised Stock Exchange" under section 841 of the Income and Corporation Taxes Act 1988. Accordingly securities listed on the CISE may qualify as quoted Eurobonds for UK tax purposes. The CISE is also officially recognised by the Australian Securities Exchange.

The CISE offers the issuer an efficient listing service (initial application papers are usually considered within 48 hours and the Listing and Membership Committee meets daily to approve listings). The CISE currently charges £3,300 as a one-off listing fee by a private issuer (and an additional £1,000 per issue in a debt programme or £750 per issue by an SPV debt issuer) with no annual fees.

The CISE requires certain general criteria to be met before the listing of debt securities may occur. These criteria include for an SPV debt issuer:

- the securities intended to be listed must be eligible for deposit in a clearing and settlement system approved by the CISE, or cash settlement via the issuer;
- an approved listing document which complies with the CISE Listing Rules must be produced - the content requirements for specialist debt securities are straightforward;
- the securities must be freely transferable and tradeable (with limited exceptions); and
- the issuer must be validly established in its relevant jurisdiction and be operating in conformity with its constitutional documents. In many respects, the CISE listing requirements afford flexibility to the issue. In particular:
  - the issuer can be public or private;
  - audited accounts are not required for an SPV debt issuer; and
  - a paying agent need not be located in the Channel Islands.

The procedure for listing is simple. The initial application comprises the submission of

documents in draft form followed by the final submission of the executed documents. A fast track "equivalence approach" may apply which permits the use of a listing document for the securities prepared under the relevant guidelines of a jurisdiction or stock exchange recognised by the CISE where no material change has occurred to the information contained in such listing document.

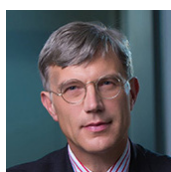
Please note that this briefing is only intended to provide a very general overview of the matters to which it relates. It is not intended as legal advice and should not be relied on as such.  
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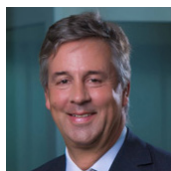
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