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The Legal 500 Country Comparative Guides

Ireland

PRIVATE EQUITY

Contributing firm

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This country-specific Q&A provides an overview of private equity laws and regulations applicable in Ireland.

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IRELAND
PRIVATE EQUITY

1. What proportion of transactions have involved a financial sponsor as a buyer or seller in the jurisdiction over the last 24 months?

There has been a marked increase in the number of transactions involving financial sponsors in the Irish market over the last 24 months, although this is really just an acceleration of a general trend that has been seen in the Irish M&A market over a number of years. In 2020, financial sponsors were involved in 39 of 173 transactions undertaken in Ireland, approximately 23% of the overall market. PE sponsors continued to represent a significant part of Ireland's M&A market in 2021, with the volume of transactions involving financial sponsors increasing to its highest level in seven years – 57 of the total of 169 transactions undertaken, approximately 34% of the overall market.

In addition, in the first half of 2021, the value of M&A transactions involving financial sponsors increased significantly – up almost 500% years on year to a total of €9.8bn. There has also been a noticeable increase in Ireland in the number of bolt-on acquisitions being undertaken by PE backed portfolio companies. We anticipate that financial sponsors, both domestic and international, and their portfolio companies will continue to play a significant part in Irish M&A activity over the course of 2022 and beyond.

2. What are the main differences in M&A transaction terms between acquiring a business from a trade seller and financial sponsor backed company in your jurisdiction?

The two most significant differences are: (i) the pricing mechanism used, with trade sellers typically favouring a completion accounts mechanic whereas financial sponsors tend to have a preference for pricing the transaction on a locked box basis and (ii) the manner in which contractual risk and the related warranty protection is dealt with in the transaction documents, the use of W&I insurance being much more prevalent with financial sponsors than trade sellers.

Financial sponsor sellers will, for the most part, only given fundamental warranties in respect of title and capacity and whilst the target's management team will provide some level of warranty cover in respect of commercial warranties, the cap on liability for such management warranties will typically be significantly lower than the overall purchase price, hence the frequent use of W&I to cover the "gap" risk. On the other hand, trade sellers will typically provide both fundamental and commercial warranties, albeit there has been a noticeable reduction in liability caps for commercial warranties in trade sales as the M&A market has become more competitive.

3. On an acquisition of shares, what is the process for effecting the transfer of the shares and are transfer taxes payable?

The transfer of shares in an Irish company must be (i) evidenced in writing by executing a share transfer form and (ii) signed by the transferor and, in the case of shares which are not fully paid, or an unlimited company, the transferee. It is also important to check the articles of association or the company constitution to ensure there are no restrictions on the transfer or issue of shares. Where the target is an Irish incorporated company, an Irish stamp duty cost will generally arise upon the acquisition of the shares, at a rate of 1% on the consideration paid (or market value, if higher), depending on how the investment is structured. For certain real estate holding companies, a higher stamp duty rate of 7.5% may apply.

4. How do financial sponsors provide comfort to sellers where the purchasing entity is a special purpose vehicle?

On larger transactions, financial sponsors will typically

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issue equity commitment letters, which are supported by legal opinions. Equity commitment letters are usually structured as an irrevocable commitment given by the fund to the acquisition vehicle pursuant to which the financial sponsor commits itself to invest certain funds in the acquisition vehicle for the purpose of either paying the purchase price or, if closing does not occur as a result of the purchaser's breach, a damages claim. The seller can then enforce its right to specific performance of this commitment letter directly against the PE fund if it fails to comply with its terms. A bank or institutional lender may also provide a loan commitment letter which will be conditional on the occurrence of certain events as set out in the sale and purchase agreement. On smaller transactions, financial sponsors may opt to provide comfort to the sellers through certain fund representations made in the share purchase agreement.

5. How prevalent is the use of locked box pricing mechanisms in your jurisdiction and in what circumstances are these ordinarily seen?

Previously, completion accounts were the most commonly used pricing mechanism in Ireland however, locked box mechanisms have been used on the majority of PE exits in recent years. The locked box mechanism provides greater certainty as to the purchase price at signing, greater control over financial information, fixing the date of economic transfer of the target before completion and prompt distribution of sale proceeds to sellers after completion. Despite the growing popularity of locked box mechanisms, given the number of deals involving international (and in particular US) buyers, where no financial sponsor is involved, completion accounts continues to be the most commonly used pricing mechanism, albeit only marginally.

6. What are the typical methods and constructs of how risk is allocated between a buyer and seller?

The allocation of risk between a buyer and seller is very deal specific in Ireland. The current market for sale terms remains, on balance, relatively seller friendly, particularly in those markets which have been less impacted by COVID – Pharmaceuticals, Technology and Media and Telecommunications.

Financial sponsor sellers will typically assume limited contractual liability under a share purchase agreement in relation to operational matters. Financial sponsor buyers will expect title and capacity warranties and also customary commercial warranties from sellers, save in respect of financial sponsor sellers, where the position outlined in paragraph 2 above is generally accepted.

W&I insurance has become increasingly popular in the Irish M&A marketplace in recent years. Typically, a buyer will want the warranties to be as far-reaching and broad as possible whilst a seller will seek to limit the scope of the warranty to reduce the financial impact arising from a warranty claim. Depending on the level of cover acquired, the policy can be used to reduce the seller's liability to as low as EUR1 for certain assets – in particular property assets, although we are seeing more and more this EUR1 cap applying in other industries. However, the seller typically retains risk for the title and capacity warranties, and full liability will apply if the seller has been found to have acted fraudulently or engaged in willful misconduct or willful deceit.

Financial caps on seller liability for breach of warranty claims of between 25% and 50% of the overall purchase price is common on mid-market and higher value transactions, whereas historically market practice in Ireland would have been for 100% of the overall purchase price to be "on risk" for breaches of warranty. In Ireland, a separate tax deed is typically used to allocate tax risk between a buyer and seller.

7. How prevalent is the use of W&I insurance in your transactions?

The increased use of W&I insurance has been a major development in the structuring of M&A transactions in Ireland in recent years. This has been particularly true over the last two to three years as a greater proportion of businesses which have been acquired by financial sponsors in recent years are now being brought to market, with the use of W&I insurance being a common feature of such exits. W&I insurance bridges the gap between the buyer's need for strong deal protection and a seller's desire for a clean exit free of residual liabilities. W&I insurance benefits both the buyer and seller as any potential liability arising out of a breach of warranty and/or indemnity transfers from the parties to the insurance provider and can provide significant comfort to a buyer and seller in a transaction. We are not aware of any material claims under W&I policies that have issued on Irish transactions in recent years.

8. How active have financial sponsors been in acquiring publicly listed companies and/or buying infrastructure assets?

Public to private transactions by financial sponsors are rarely seen in the Irish market. There were no such

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transactions in 2021 or 2020. A public-to-private transaction is regulated by the provisions of the Irish Takeover Panel Act 1997 (as amended), the Irish Takeover Rules 2013 (Rules) and the European Communities (Takeover Bids (Directive 2004/25/EC)) Regulations 2006. The Rules regulate the conduct of takeovers of Irish companies listed on certain stock exchanges. The Irish Takeover Panel oversees the application of the Rules to specific transactions. Financial sponsors are particularly active in the Irish infrastructure market. By way of illustration, a notable infrastructure transaction in the Irish market in 2021 was Macquarie's acquisition of Ireland's largest waste company, Beauparc Utilities Holdings Limited ("Beauparc") from founder Eamon Waters and Blackstone Tactical Opportunities Fund. Beauparc is a recycling and processing led waste-to-resource business with a market leading position across Ireland, and a significant growing presence in the UK and the Netherlands.

9. Outside of anti-trust and heavily regulated sectors, are there any foreign investment controls or other governmental consents which are typically required to be made by financial sponsors?

The EU Investment Screening Regulation became fully operational across the EU on 11 October 2020. Where foreign direct investments are likely to affect security or public order, Member States are subject to mandatory cooperation and information sharing requirements. In 2020 the Irish Government agreed to draft legislation, the Investment Screening Bill 2020, which will give effect to this regulation. According to an Irish Government press release, the proposed legislation will empower the Department of Enterprise, Trade and Employment to investigate, authorise, condition, prohibit or unwind foreign investments into Ireland by non-EU investors, based on a range of security and public order criteria. However, the draft Irish legislation has not yet been published. It was hoped that the legislation would be ready in the first half of 2021 and it is now anticipated that the legislation will enter into force in 2022. Therefore, the potential impact on the M&A market is not yet clear, in particular, it is not clear what type of transactions are likely to be subject to review (and the extent of that review). It is expected that the Irish approach to implementation will seek to maintain Ireland's attractiveness as a location for inward investment, while reflecting the need to take into account national security and public order considerations in certain strategically important sectors. For now, Ireland is to comply with the cooperation and information sharing requirements under the EU Investment Screening Regulation. Outside of the above and certain mandatory regulatory approvals and governmental consents in specific regulated sectors such as healthcare, financial services and media, no other controls apply to financial sponsors.

10. How is the risk of merger clearance normally dealt with where a financial sponsor is the acquirer?

In Ireland, competition clearances are, where applicable, a condition precedent to completion, leading to a split signing and completion pending approval from the Competition and Consumer Protection Commission. The risks of competition clearance are often passed on to the purchaser by the use of a "strict hell or high water" clause, which may include an obligation on the purchaser to make any required divestments or litigate in the event the transaction is challenged from a competition perspective.

11. Have you seen an increase in the number of minority investments undertaken by financial sponsors and are they typically structured as equity investments with certain minority protections or as debt-like investments with rights to participate in the equity upside?

Minority investments undertaken by financial sponsors have increased in Ireland in recent years and this is something we expect to see continue as dedicated minority funds enter the market, both local and international.

There are a variety of capital structures used, ranging from ordinary equity investments with certain control rights, preferred equity or debt-like structures with limited governance rights but with the ability to participate in equity returns. While not a major feature of the Irish market in recent years, mezzanine debt and convertibles have also become more common. Typically, a financial sponsor who is taking a minority position will seek certain rights and protections including tag along and drag along rights, the ability to appoint a director, a right to information about the company, rights of first refusal in respect of new equity or debt issuances and board representation. It is important that a well negotiated shareholders agreement is put in place to ensure a minority investor obtains adequate protection, but in a way which does not unduly stifle the development of the relevant business.

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12. How are management incentive schemes typically structured?

A common management incentive scheme in Ireland is granting the managers of the selling entity direct equity interests in the purchaser's acquisition group structure. The positive aspects of this structure are that the equity can result in gains being subject to capital gains tax treatment when the managers roll-over into the purchaser structure upon their disposal of shares in the target company. This can be contrasted with the tax treatment that applies to share option, exit bonus or phantom share schemes which attract higher rates of tax for the individuals and social security contributions for the portfolio company which employs them.

13. Are there any specific tax rules which commonly feature in the structuring of management's incentive schemes?

In general, whilst share incentivisation is common in Ireland, the tax treatment of most forms of share incentivisation is not particularly advantageous for employees/directors based in Ireland, with marginal rates of income tax, universal social charge and social security generally applying on any benefits obtained (subject to the comments below). However, if the shares that the employees receive qualify as "restricted shares" (under Irish tax rules), there could be a material abatement of up to 60% of the taxable value of the shares for Irish tax purposes (subject to certain qualifying conditions being met). This is, potentially, very favourable for employees/directors. Ireland also introduced a "Key Employee Engagement Programme" ("KEEP") which provides for an exemption from income tax, universal social charge and social security arising on the exercise of a qualifying share option to acquire shares in a qualifying company in the SME sector, provided certain conditions are satisfied. To date, we have seen a limited take up of the KEEP scheme in private equity backed businesses.

14. Are senior managers subject to non-competes and if so what is the general duration?

Senior managers in Ireland are typically subject to non-compete clauses. While the standard duration of non-compete clauses in an employment contract for senior executives is typically between 6 and 12 months in duration, in a share purchase agreement, the non-compete period for sellers (which may include senior managers) can be up to three years in duration when the transfer of the undertaking includes the transfer of customer loyalty in the form of both goodwill and know-how. Like in many other jurisdictions, the balance between restraint of trade and protection of legitimate business interests makes enforceability fact specific. In equity documents involving a financial sponsor, the typical time period for key managers is between 12 and 24 months.

15. How does a financial sponsor typically ensure it has control over material business decisions made by the portfolio company and what are the typical documents used to regulate the governance of the portfolio company?

Including specific covenants in a shareholders' agreement (or investment agreement) is how a financial sponsor will typically ensure it has control over material business decisions made by the portfolio company. The main investment agreement will typically allow the financial sponsor to control the composition of the group's board of directors, include veto rights over material business decisions and oblige the management team to submit regular financial and event driven reporting to the sponsor for the purpose of monitoring its investment. Alternatively, or in parallel with a shareholders' agreement, a financial sponsor will hold the majority of voting rights in the target entity to ensure control over material business decisions.

16. Is it common to use management pooling vehicles where there are a large number of employee shareholders?

Typically, the management team of between four and six senior executives will individually invest for ordinary shares ("sweet equity") in their own names. Occasionally, where there is a larger pool of management investing in the sweet equity pot, this will be structured through a NomineeCo. Any arrangements put in place with the management team will be subject to a thorough tax analysis to ensure the most beneficial outcome for the participants on any exit.

17. What are the most commonly used debt finance capital structures across small, medium and large financings?

Capital financings in Ireland typically take the form of either long-term (i.e. four to five years plus one (or one plus one) year options to extend) or short-term loan facilities akin to a bridge that may be refinanced by a

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bond on larger financings. Revolving facilities are commonly made available for working capital purposes. It is not uncommon for medium to large financings to have a mezzanine element. With multiple alternative credit providers having entered the Irish market in recent years, venture capital financing has increased, particularly in the fintech and pharmaceutical industries. The increase in activity in the Irish property sector has also resulted in the use of alternative financing structures, such as note issuance programmes, which enable investors who might not otherwise be permitted to lend into Ireland to build up market share. We are also seeing continued growth in alternative credit providers, as well as more traditional lenders, offering finance through investment funds. This often involves the provision of secured or unsecured subscription (or capital call) facilities to bridge capital calls to investors, thereby improving the availability of working capital and/or investment finance.

18. Is financial assistance legislation applicable to debt financing arrangements? If so, how is that normally dealt with?

Yes, it is unlawful for an Irish company to directly or indirectly give financial assistance for the purpose of an acquisition of its own shares or, where the company is a subsidiary, in its holding company. There are however a number of exemptions, with the most common exemption being the carrying out of a whitewash procedure (known as a summary approval procedure), which approves and permits the form of assistance rendering it lawful. The Companies Act 2014 introduced an additional carve out against financial assistance where the company's principal purpose in giving the assistance is not to give it for the purpose of any such acquisition (the so-called "principal purpose test") or the giving of the assistance for that purpose is only an incidental part of some larger purpose of the company (the so-called "incidental part test"), and, in each case, the assistance is given in good faith in the interests of the company.

The summary approval procedure involves a number of steps, including the swearing of a declaration by all or a majority of the directors of the relevant company that, among other things, the directors have (following full inquiry) formed the opinion that the company will be able to pay or discharge its debts and liabilities in full as they fall due for a period of twelve (12) months following the giving of the financial assistance. Shareholder and board approvals are also required. Public companies and their private subsidiaries are not able to avail of the summary approval process and thus, unless the relevant financial assistance falls within one of the other more limited categories of exemption, it will not be permitted. Failure to comply with the prohibition on financial assistance is a criminal offence and any financial assistance (eg. guarantees, charges, etc.) granted in breach of the legislation is voidable.

19. For a typical financing, is there a standard form of credit agreement used which is then negotiated and typically how material is the level of negotiation?

The Loan Market Association's standard form leveraged facility agreement is used for most medium to large corporate loan financings in Ireland. The level of negotiation on the terms of the LMA facility agreement will vary on a deal by deal basis but, as drafting often follows a pre-agreed term sheet and commercial issues are usually agreed at an early stage of a transaction. The LMA form requires a number of Irish law related changes (particularly in relation to insolvency and tax matters), however, these amendments do not tend to be heavily negotiated. Unlike the UK or US, the Irish market is more traditional in its approach to drafting and the lenders' counsel will usually draft the loan agreement, although the strength of the sponsor can very occasionally dictate the ability of a borrower to present a "first draft" of the loan agreement.

20. What have been the key areas of negotiation between borrowers and lenders in the last two years?

Since March 2020, and throughout 2020 and 2021, a significant proportion of loans, particularly those exposed to the retail, hospitality, tourism, aviation and student accommodation sectors, have undergone a mix of payment breaks, financial covenant waivers, covenant deferral periods and longer-term covenant re-sets. In our experience, lenders are working closely with their borrowers in a constructive manner to find longer term solutions for both sides. We expect this trend to continue, although at a reducing level, with the level of longer term waivers and amendments being very much dependent on market trends in the relevant sectors. Prior to the onset of COVID-19 related issued for borrowers, financial covenants (and cures to any covenant breaches), were also a key area of negotiation, along with assignment and transfer provisions (and, in particular, the scope of white / black lists). Accordion facilities, options to extend the term and the mechanics around exercising these options also tend to be closely scrutinised. In contrast to the UK, the local Irish market has not embraced cov-lite transactions, although in some pre-March 2020 deals we were starting to see a

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relaxation of permissions around the use of cash. Other areas where we have seen increased focus recently are the inclusion of green and sustainability-related provisions and an increased concentration on benchmark and interest rate fallback related provisions as the phasing out of LIBOR becomes closer.

21. Have you seen an increase or use of private equity credit funds as sources of debt capital?

There has been a sharp increase in the number of alternative credit funds and private equity investors active in the Irish market in recent years. In the real estate sector in particular, the relatively conservative lending practices of the traditional Irish banks has resulted in many Irish real estate developers and investors seeking capital from alternative sources. In the SME sector, the Irish government has developed a number of initiatives to ensure that the supply of credit in the market (from bank and non-bank sources) is sufficient to meet the existing and future funding needs of SMEs. The Irish government has invested, via the Ireland Strategic Investment Fund, in a number of private equity credit funds who provide debt capital to Irish SMEs. Although we have seen private equity credit funds lend through a variety of financing structures, typically funds are advanced via a secured loan or from the proceeds of a note issuance programme.

In addition, Ireland’s partnership laws have been updated to modernise Ireland’s Investment Limited Partnership (ILP). The ILP is a regulated fund and is an alternative to vehicles such as the Luxembourg SCSp or the Cayman Islands Exempted Limited Partnership. Although we have seen private equity credit funds lend through a variety of financing structures, typically funds are advanced via a secured loan, from the proceeds of a note issuance programme or, more recently, through ILPs.

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