

New Spanish Tax Regime for Qualifying Bond Offerings May Boost High-Yield Bond Markets

New rules will facilitate privately held companies' access to bond financing and reassure Spanish investors.

On June 28, 2014, Law 10/2014, on the organization, supervision and solvency of credit institutions (Law 10/2014), entered into force. Additional Provision One of Law 10/2014 provided for a long-awaited reform of the Spanish special tax regime for qualifying bond offerings (previously, set out in Additional Provision Two of Law 13/1985, on ratios of investment, equity and information obligations of financial intermediaries (Law 13/1985)).

Background

Law 13/1985 provided for a special tax regime that allowed, *inter alia*, an interest withholding tax exemption with respect to bonds issued by, among others, Spanish financial institutions and publicly held companies (as well as wholly owned subsidiaries of such entities resident in Spain or in a European Union member state) and bonds held by non-Spanish resident investors who did not maintain a permanent establishment in Spain — subject to the fulfillment of certain requirements.¹

Broadly speaking, such requirements referred to:

- The trading of the instruments (*i.e.* they should be traded on an “organized secondary market”²)
- The supply of certain tax-related information by the paying agent involved in the offering³

Where the offering was carried out by a subsidiary special purpose vehicle (SPV) issuer, the requirements referred to:

- The corporate purpose of the issuing vehicle (*i.e.* its sole corporate purpose should be the offering of qualifying securities)
- The use of the offering proceeds (*i.e.* the net proceeds should be placed at the parent company of the issuer vehicle or at another entity belonging to the same consolidated group of companies)

Welcome Changes

The new tax regime set forth under Additional Provision One of Law 10/2014 provides for the best of all worlds: all bond offerings that could have qualified for the special tax regime set forth under Law 13/1985 will still be covered by Law 10/2014, plus the new law significantly enlarges the pool of eligible issuers. Upon the entry into force of Law 10/2014, *any Spanish-resident company* (not only financial institutions or

publicly held entities, or wholly owned subsidiary SPVs of such entities) will be able to benefit from the special regime.

In addition, offerings carried out by (i) wholly owned subsidiary SPVs of such Spanish-resident companies that are resident within the European Union, and (ii) public entities in corporate form (*entidades públicas empresariales*), will also benefit from such regime.

This is a welcome development in Spanish tax law, since privately held companies had no access to the previous regime set forth under Law 13/1985 and had to deal with a complex (and challenging) tax environment in order to obtain financing in the bond market. After the enactment of the new law, the structuring of such bond offerings will be greatly simplified.

Clarity About the “Organized Secondary Market”

Furthermore, the new tax regime of Law 10/2014 has introduced certain technical improvements with respect to the old regime: one of the big question marks regarding the applicability of the regime set forth under Law 13/1985 referred to the trading venue of the bonds. As noted above, Law 13/1985 required bonds to be traded on an “organized secondary market,” but provided no certainty as to whether such term of art could be deemed to refer both to “regulated exchanges” and “multilateral trading facilities” (within the meaning of the MiFID Directive⁴).

From a market perspective, multilateral trading facilities (such as the Luxembourg Euro MTF and the Irish Global Exchange Market (GEM)) were extremely popular among European issuers. While market participants were relatively comfortable with their use, Spanish issuers generally alerted investors with a “risk factor,” included in the offering documentation, about the risk that the Spanish Tax Authorities took the view that the requirement set forth under Law 13/1985 required the bonds to be traded on a regulated exchange. While a tax ruling issued by the Spanish Tax Authorities in late 2013 seemed to sanction the use of multilateral trading facilities,⁵ the ruling still did not provide full certainty in that regard.

The new tax regime addresses this issue and casts doubts away. Under Law 10/2014, the listing requirement now refers to “regulated exchanges, multilateral trading systems and other organized exchanges.”

The chart below highlights the main differences between the new tax regime under Law 10/2014 and the previous one with regard to bond offerings:

	<i>Old regime (Additional Provision Two of Law 13/1985)</i>	<i>New regime (Additional Provision One of Law 10/2014)</i>
Main eligible issuers	Spanish financial institution or publicly traded entity, or wholly owned subsidiary of such persons resident in Spain or in the EU. ⁶	There is no longer a reference to “financial institutions” or “publicly traded entities,” since any offering carried out by a Spanish-resident entity (publicly held or not) or its wholly owned subsidiaries resident in Spain or in the EU may qualify. Public entities in corporate form are expressly included within the scope of the special regime.

Requirements as to issuer vehicle	If the issuer vehicle was a wholly owned SPV, its corporate purpose should be limited to the issuance of securities.	No longer applicable.
Requirements as to notes	Listing of the notes on an “organized secondary market.”	Listing of the notes on a regulated exchange, multilateral trading facility or any organized exchange. The bonds must not grant voting rights or preferred subscription rights with respect to future bond offerings.
Requirements as to offering proceeds (in case the offering is carried out by a subsidiary SPV issuer)	The net proceeds should be placed within an entity belonging to the same consolidated group or subgroup of companies.	Similar to old regime.
Tax certification procedures	Payment statement to be supplied by the paying agent (contents will depend on the clearing systems involved).	Similar to old regime.

Remaining Ambiguities

Market participants should note that even though the regime enacted by Law 10/2004 is great news for Spanish enterprises, the new tax regime still does not fully address certain relevant aspects. On the one hand, Law 10/2004 does not provide for a “grandfathering” provision, meaning that bond offerings launched before its entry into force (on June 28, 2014) are not able to benefit from its provisions. The new law may also fail to dispell doubts as to whether a “tap” offering could benefit from the new tax regime too. In addition, Spanish issuers may need to iron out structuring issues if they intend to carry out an offering through a subsidiary SPV issuer resident for tax purposes in Spain. If such an issuer vehicle on-lends the offering proceeds to a Spanish-resident parent company, there may be withholding tax leakages with respect to such a proceeds loan if both entities do not belong to the same fiscal unity for Spanish tax purposes.

Conclusion

Notwithstanding the above, the developments introduced by Law 10/2014 are in line with the Spanish Government’s intention to allow Spanish enterprises to access the international bond markets and may facilitate their access to bond financing (and, in particular, to the high-yield bond market).

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Endnotes

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- ¹ Such special tax regime also applies with respect to qualifying offerings of preferred shares. This Client Alert references only the aspects relevant for bond offerings, and does not address the particular requirements applicable to offerings of preferred shares.
 - ² This is a term of art that was not defined under Spanish law, and which has given rise to controversies in the past, as explained in our Client Alert dated February 12, 2014 ("*Tax Ruling Offers Welcome Clarification on Spanish Regime for Qualifying Bond Offerings*"), available at www.lw.com/thoughtLeadership/lw-spain-tax-ruling-bonds.
 - ³ Under the applicable Spanish regulations (article 44 of Royal Decree 1065/2007, dated July 27, 2007), the applicability of the withholding tax exemption requires that the paying agent involved in the offering supplies the issuer, prior to the interest payment date, with a payment statement providing for certain information relating to the payment that is relevant for Spanish tax purposes. Where the bonds are registered at a clearing system operated by a regulated clearing entity not based in Spain (such as e.g. Euroclear or Clearstream), then the payment statement to be supplied by the paying agent involved should include details on the identification of the bonds, the payment date, the amount of income to be paid on the relevant payment date, and the total amount of income corresponding to Notes held through such non-Spanish clearing systems.
 - ⁴ Markets in Financial Instruments Directive (Directive 2004/39/EC).
 - ⁵ The contents of such tax ruling are explained in detail in our Client Alert dated February 12, 2014 ("*Tax Ruling Offers Welcome Clarification on Spanish Regime for Qualifying Bond Offerings*"), available at www.lw.com/thoughtLeadership/lw-spain-tax-ruling-bonds.
 - ⁶ Offerings carried out by Spanish issuer SPVs of a non-Spanish financial institution or publicly traded company could also qualify for this regime.