

A B O G A D O S

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THE PROVISION 108 OF THE SPANISH SECURITIES MARKET ACT 24/1988: TECHNICALLY UPGRADED OR EXTREMELY WIDENED?

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We are facing new times. Indirect taxes are gaining ground. Specific anti-avoidance tax rules, too. Yet, tax reforms may sometimes be unbalanced. This might be the case of the Provision 108 of the Spanish Securities Market Act 24/1988. Sometimes, the acquisition of shares in a real estate company (i.e. an entity the assets of which consist of at least 50% of real estate located in Spain and/or a qualifying stake the holding company may have in a real estate company) is taxed.

Traditionally regarded as a new taxable event, the provision is now widened. Technically polished, indeed, but several issues emerge. We below outline some.

First, aside from the assets' valuation (e.g. the values approved by the Tax Authorities, estoppel doctrine) the new rule only refers to goods, but not to rights. They should qualify as assets for sure. The rule says nothing about latent goodwill. Should it be computed for such 50% real estate asset test purposes? To some it shouldn't, it is not feasible to replace -by the fair market value- the net accounting value of an asset that has no accounting value just because it was not booked. ¿And what about those assets, which are totally amortised?

As for 'control', this is legally reached whenever the purchaser acquires directly or indirectly more than 50% of the real estate company's share capital. Control is linked to the 50% threshold (regardless of the voting rights). The analysis is harder when holding companies are involved. Should the control test be carried out vis-à-vis each company? Should the tax be triggered in case the acquisition brings the acquirer the control of the 2nd-tier holding company, which, in turn, controls the 3rd-tier real estate company, eventhough the indirect stake is below 50% in that 3rd-tier company?. Should the indirect stake the acquirer has in the 3rd-tier company be added up to the direct stake, but only whenever the acquirer also controls the 2nd-tier holding company and the latter controls the 3rd-tier real estate company?. Or should the indirect stake in 3rd-tier company be added up to the direct stake in that same company, though the acquirer does not control the 2nd-tier company? Let's wait and see..

But some issues are slowly clearing up. What it is key is that control is gained or increased on a group basis, being taxed the company that acquires the stake even though the control is gained by the top parent company. It is also essential that the company qualifies as a real estate company prior to the transaction that gives rises to control.

Until the new rule came into force, any further share acquisitions were tax-exempt once the investor took control of the real estate company. Now the tax is levied on all further share acquisitions. No transitory period was set. Under the former rule, tax was levied on the basis of 100% of the real estate value, regardless of whether the stake was lower than 100%. But what if, prior to the new rule coming into force, an investor acquired a 51% stake in the company and paid tax on the 100% value of the real estate assets? Will the investor now have to pay an additional tax if it increases further its stake in the company? It doesn't make

any sense from a double taxation approach. We certainly welcome the Spanish Tax Authorities have recently ruled in this way.

Finally, the new wording ensures that the investor is taxed whenever the control of the real estate company is obtained in "any other way". This means that certain transactions may trigger both the transfer tax and the capital duty, though capital duty excludes the transfer tax as a general rule. Think of those transactions subject to capital duty (e.g. capital increase, merger, and spin-off). If the control is gained/increased through a transaction subject to capital duty, but not through newly issued shares, no transfer tax should be triggered (e.g. buy-back shares).

It is better to be safe than sorry. Thus, it is worth to think carefully before making a decision on how an acquisition is going to be structured.
