Tips for Legal Counsel Representing Foreign Investors in Private M&A in Spain

By Rubén Ferrer and David Riopérez

Transactions always vary in one form or another. The singularity of each seller and target requires a personalized approach to ensure a successful closing. There are, however, certain general issues that regularly emerge in Spanish transactions. This article is intended to help legal counsel representing foreign investors navigate M&A deals in Spain.

1. Restrictions to Foreign Investments

Foreign investment in Spain is generally unrestricted. However, a certain control process is in place to gather information concerning foreign transactions and to take measures on grounds of public order and security, where appropriate. Said process may be in the form of a simple notification procedure (either before or after the transaction has taken place), or a review and approval procedure prior to entering into the transaction.

> *"In short, the buyer will not be liable for the payment of any amounts owed by the insolvent company upon transfer of a production unit unless the buyer has expressly undertaken such obligation or unless legally required to do so; for example, in the case of employment and Social Security liabilities."*

With certain exceptions, Spanish legislation requires foreign investments to be notified after the transaction is closed. On the other hand, investments made through a tax haven must generally be notified beforehand. Furthermore, if the acquisition is leveraged and debt is provided from overseas, additional post-deal filings with the Bank of Spain may be required.

Very exceptionally, for foreign investments related to the exercise of public authorities or activities that may affect public order, national security, or public health, the Spanish Government may suspend the liberalization status and restrict or even forbid such investments. Once suspension is declared, foreign investors must request prior administrative approval to carry out any investment. Other industry-specific restrictions exist for foreign investments, although they are limited and generally comparable to other EU member states. In certain scenarios, the Spanish Government must be notified ex post of any investment in a company directly or indirectly carrying out certain regulated activities in the electric, gas or hydrocarbon industries.

With regard to antitrust approvals, investments in Spain are subject to Spanish or EU merger control when certain thresholds are met and control over the target company is acquired.

2. Liabilities in an M&A Transaction

The parties can generally allocate risks and liabilities between them as they deem appropriate, although this will not be enforceable vis-à-vis third parties.[1] Certain limitations apply, such as in the case of willful misconduct, where liability cannot be excluded or limited. Caps, baskets, and deductibles are common in Spanish M&A deals.

In a share deal the buyer acquires all the target's assets and liabilities, except for those that are expressly carved out. The parties may agree that the seller remains liable for certain contingencies and liabilities of the target by agreeing on a specific indemnity or the representations and warranties regime under the acquisition agreement.

In an asset deal, the liabilities are limited to the assets and liabilities being expressly transferred. However, under Spanish law certain tax and employment liabilities are passed over to the buyer if the acquired assets are considered to be a stand-alone business. Such liabilities may be mitigated in some cases by requesting certain certificates of liabilities from the relevant authorities, although sellers tend to resist providing such certificates because oftentimes an audit over them is triggered when such certificates are requested. Transfer of Undertakings (Protection of Employment) regulations (TUPE) may be applicable; hence, the buyer takes over all the employees and related conditions that were employed by the seller and linked to the transferred business.

> *"Employment at will, as such, does not exist under Spanish law."*

The sale of the production units of a company subject to insolvency proceedings has recently become common practice in Spanish commercial courts. These proceedings allow such production units to continue as a going concern, minimizing the destruction of the business landscape. From the buyer's perspective, it will be able to define the acquisition target without all the liabilities outstanding or hidden in the transferor company. In

short, the buyer will not be liable for the payment of any amounts owed by the insolvent company upon transfer of a production unit unless the buyer has expressly undertaken such obligation or unless legally required to do so; for example, in the case of employment and Social Security liabilities.

3. Termination of Employment Agreements

The costs of redundancies in any workforce restructuring post-acquisition must be considered. Employment at will, as such, does not exist under Spanish law. A company's decision to terminate an employment contract is deemed a dismissal, and must be based on disciplinary reasons or objective (economical, technical, organizational, or production) grounds.

> *"In a share deal, careful attention should be paid to the assets of the company because if real estate constitutes more than 50% of such assets, then transfer tax may be levied."*

Objective dismissals require a 15-day prior notice and payment of a compensation equivalent to 20 days of salary per each year worked, up to a maximum of one year of salary. Dismissals without due cause (or dismissals based on disciplinary or objective grounds which, after the affected employee's claim, are subsequently not upheld in court), can normally still be carried out but entail higher compensations.[2] In certain limited cases (i.e., when the dismissal impairs fundamental rights or refers to employees under special protection like pregnant women or employees' legal representatives), a court may find a dismissal to be null and void, which would imply the obligation of reinstating the employee in his or her former post. There is a specific and compulsory process for plant closing or mass layoffs, including a previous round of negotiations with unions for 30 days, with the aim of reaching an agreement on the effects and consequences of the mass layoffs, and with very specific procedure, information and documentation requirements.

On the other hand, a change of control in an M&A transaction may trigger certain resignation and compensation rights in favor of top executives. Contractors who have the risk of being reclassified as employees is an usual issue to come across in M&A deals. If new employment contracts with top executives are signed at closing, it should be verified whether they are aligned with any earn-out provisions under the acquisition agreement and whether the relevant contract responds to the reality of the duties to be performed.

4. Tax Issues

Tax implications in a share deal are generally different from those in an asset deal. Also, if the acquisition is implemented by means of a merger or a demerger, then certain tax breaks may apply.

Asset deals normally involve that the acquirer inherits any tax liabilities attached to the acquired assets, although such liabilities can be materially limited if certain certificates are obtained from the seller as mentioned above. In a share deal, careful attention should be paid to the assets of the company because if real estate constitutes more than 50% of such assets, then transfer tax may be levied.

> *"If personal data is expected to be transferred outside of Spain, additional restrictions may apply, including the need to obtain specific authorization from the Spanish Data Protection Agency."*

Normally, no value added tax (VAT) or transfer tax is levied in a share deal. VAT may be levied in an asset deal if the relevant assets do not constitute a stand-alone business or other conditions are met. In a share deal, if a post-acquisition merger between the special purpose vehicle and the target is envisaged, careful attention should be paid to such merger to ascertain whether any goodwill would be tax deductible as well as whether the beneficial tax regime for mergers in Spain can be applied.

5. Data Protection and Privacy Issues

Strict rules exist in Spain regarding the collection, use, processing, and transfer of personal data and potential fines are substantial. It should be ensured that all personal data files have been properly managed and notified to the Spanish Authorities and that the target has in place all security measures and paperwork required under Spanish law. If personal data is expected to be transferred outside of Spain, additional restrictions may apply, including the need to obtain specific authorization from the Spanish Data Protection Agency. The EU Regulation on Data Protection that has recently been published (applicable from May 25th, 2018)[3] sets forth new requirements and fines.

> *"Software subject to a patent right is difficult to obtain in Spain."*

6. Information Technology (IT) and Intellectual Property (IP) Matters

Careful consideration should be given to IT/IP matters to make sure that title to all assets stays with the target, and that no other group company, employees, in-

dependent contractor or third parties can claim any economic rights over such assets. Patents, trademarks, and other IP rights tend to have an expiry date, but oftentimes subject to possible (limited or unlimited) extensions. Software tends to be considered a type of IP right, which is similar to copyright, for which registration in a public register is not mandatory. Software subject to a patent right is difficult to obtain in Spain.

7. Conclusion

Matters described above are some of the issues foreign investors and their legal counsel must consider when approaching a potential deal in Spain. Experienced Spanish legal counsel is imperative to know how to best approach them.

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Endnotes

1. For instance, Spanish tax authorities will seek payment of any tax debts from the legally established taxpayer and not from the liable person pursuant to the acquisition agreement, irrespective of subsequent claims between the parties.
2. In accordance with Spanish Employment Law, a combination of up to 45 days of salary per each year worked capped at 42 monthly payments until February 11th, 2012, and up to 33 days of salary per each year worked capped at 24 monthly payments from February 12th, 2012.
3. http://ec.europa.eu/justice/data-protection/.

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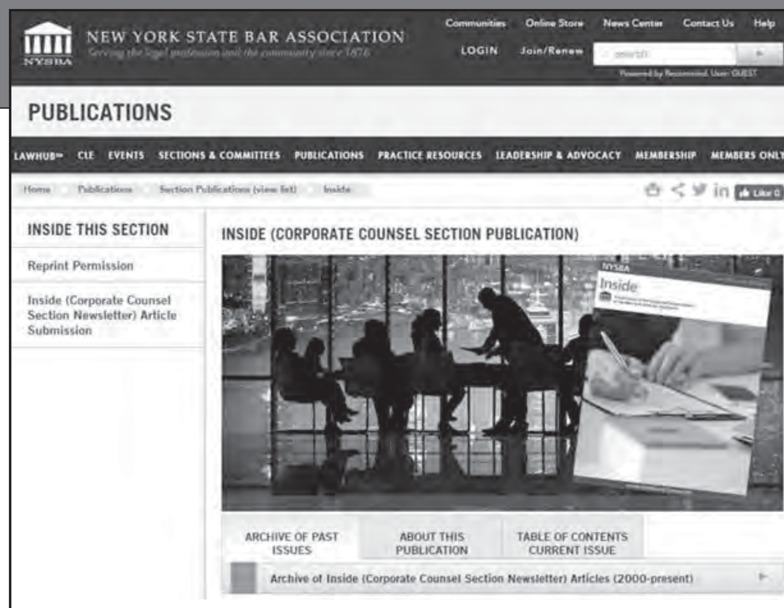

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