INVESTING in Spain—

Sound Business Appeal

By Robert Zentz and Rubén Ferrer

30-SECOND SUMMARY From an international investment perspective, the fundamental attraction of Spain has grown in recent years. A sophisticated transport infrastructure and an expansive fibre optic network facilitate the ease with which business can be conducted. For companies looking for human capital, significant changes to the country's labour and employment regulations have reduced bureaucracy. Corporate income tax and VAT rates are lower than the European average, and the tax treatment of research and development is the second most favourable among OECD countries. Furthermore, Madrid and Barcelona are ranked among Europe's top 10 business cities for expatriates.

There is no European country that has restructured as deeply as Spain as a result of the global downturn. Having been caught in a perfect storm of a domestic real estate crash and international financial crises, its national and regional governments have embarked upon a rebuilding process to create an economy that is leaner, more agile and increasingly more open to international investment, skills and know-how.

Economic fundamentals

In light of the economic pressures that continue to weigh down Europe, there is no doubt that challenges remain for the Spanish economy. But from an international investment perspective, the fundamental attractions of the country have undoubtedly grown. Spain is a key member of the European Union (EU), and companies domiciled here are able to take advantage of the EU's free flow of capital, goods and people, including the ability to "passport" services across the other 27 EU member states — a market of over 500 million people.

With a population of 47 million, Spain is one of the EU's largest economies. It was one of the founding members of the Eurozone, which has retained its cohesion despite financial bailouts for Portugal, Ireland, Greece and Cyprus since 2010. Indeed, the recent re-election for a third leadership term of German Chancellor Angela Merkel has reaffirmed the evident mood of confidence that is increasingly apparent across Europe.

There seems to be little doubt about the stability of the Eurozone. The belief is that the worst of the economic crisis is over and the Eurozone is actually now expanding. Latvia will formally adopt the euro from January 2014, while the EU's most recent member — Croatia — is likely to follow suit in 2019, bringing the number of euro-denominated countries to 19.

While unemployment levels in Spain may remain stubbornly high, particularly among the young, such a fact has proved to be the catalyst for significant policy, regulatory and legislative changes, to address outdated working and business practices, and to encourage new levels and types of international investment. More government investment is being channeled into education, training and skills development to raise productivity levels, which now well exceed the Eurozone and EU averages.[1]

Spain's receipt of EU and European Central Bank (ECB) stability funds in August 2012 was conditional on significant reform of the country's financial system, heavily impacted by the collapse of the real estate sector in 2008. The cash has helped stabilize the country's banks and prompted the creation of a "bad bank" (SAREB – Sociedad de Gestión de Activos procedentes de la Reestructuración Bancaria) into which the troubled domestic institutions have now placed their most toxic real estate assets, bringing new certainty to institutions' balance sheets to help encourage new inward investment and lending.

Autumn 2013 saw the first takeover of a Spanish bank by a US investor — Apollo's €60m purchase of EVO, a branch of Novacaixagalicia (NCG Banco) — while other recent deals include Blackstone's $166m purchase of Madrid apartment blocks, and TPG's $249m acquisition of 51 percent of La Caixa's real-estate servicing arm — the groups' first investments in Spain's property sector.

World class connectivity

Despite the challenges of the past few years, the Spanish economy nonetheless remains among the most open and diverse in Europe. The Organization for Economic Cooperation and Development (OECD) ranks it fifth for Foreign Investment Openness,[2] and fundamental to the ease of doing business in the country are the domestic and international transport and communication connections.

Spain comprises 17 autonomous regions, to which much decision-making is devolved, albeit overseen by national regulatory and governmental agencies. As such, each region may have a distinct economic character and cultural identity. Nonetheless, the Spanish government is proactively legislating to ensure that the country works as a single market.

Key to integrating these regional identities and economies is the sophistication of Spain's transport infrastructure. As one of the EU's largest countries, Spain has one of the largest networks of high-capacity roads (highways and dual carriageways) and most complete high-speed rail infrastructure. Indeed, Spain's train and construction companies now export their transport expertise around the world.

And it is a network that continues to expand. The government's Strategic Transport Infrastructure Plan foresees a further 10,000 km of high-speed track connecting major cities, placing 90 percent of the population within 50 km of a network station by 2023. In addition, Spain features prominently in the EU's Trans-European Transport Network Executive Agency's (Ten-T) Top 10 Priority Projects that will see billions of euro committed to expanding Europe's high-speed rail network, connecting the country to a rail corridor that stretches from Scandinavia and Central Europe to North Africa.[4]

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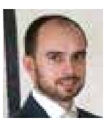

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Case study – Laureate Education, Inc.

INVESTING IN SPAIN: A LEARNING JOURNEY

Spain was the first country outside the United States into which Laureate Education, Inc., expanded. We opportunistically acquired the majority interest in *Universidad Europea de Madrid* (UEM) in 1999, and the country has subsequently proved to be one of our best-performing markets and a stepping-stone to the rest of Europe. We saw the potential to leverage our domestic expertise and offerings and found a strong local demand for what we do. And we continue to feel that way.

Since opening in Madrid, we have expanded the *Universidad Europea* network across the country, capitalising on the excellent infrastructure and distinct character of Spain's autonomous regions. Madrid is now the focus of our business, engineering and architecture, and sports science programmes; in Valencia and the Canary Islands, we have a wider undergraduate and graduate degree offering, while in Marbella, we operate our hospitality-focused *Les Roches International School of Hotel Management*.

Universidad Europea also recently gained approval to offer degrees in medicine. There is no denying that the barriers to entry were high, but we recognised the sense in that. Our experience has shown Spain's regulatory environment to be tough but fair. We have built a constructive relationship with the Ministry of Education and fully understand that the authorities' focus is on ensuring teaching of the highest quality, which is not something we see in all European markets.

And while we may have until recently experienced a leveling off of student numbers as a result of the wider economic pressures, the company is nonetheless constantly asking: What can we do to capitalise on the current situation? We are already attracting more high calibre teaching applicants, as many highly-skilled people have left — or been forced to leave — industry positions, and we are also now assessing the potential for new growth. We see a number of very good Spanish educational institutions that lack the capital or management skills to overcome the current economic challenges.

We are also exploring the potential for greenfield development. We believe in the fundamentals of Spain and of our own sector, and because of our international spread, we now operate 72 institutions in 30 countries. We are content to take a long-term view.

This ability emanates also from the comfort we have in Spain's legal infrastructure; the quality of the local legislation, regulators and lawyers is excellent. From a US perspective, we see more similarities than differences, and firms such as Gomez-Acebo & Pombo, with which we work, operate at the highest levels. That firm's expansion (including into the United States) reflects our own perception of rising inbound investor interest.

We thus see the Spanish Government taking the necessary steps to turn the economy around. Greater focus is being placed on the education sector to develop and raise skill levels, while new legislation applicable to business restructurings means that we — like many others — are better able to reshape our operations to capitalise on changing demand. From a legal and business perspective, Spain has learnt the lessons of the crisis, and our belief is that it will soon again be one of our star-performers. Despite — and in fact, because of — the economic pressures, we see considerable upside in Spain.

Spain boasts 49 airports from which 250 airlines operate,[5] with Madrid Barajas, one of Europe's main hubs for Latin America, and the air shuttle between Madrid and Barcelona among the busiest routes in Europe. In addition, the country operates 46 international ports and the only fixed pipeline to Africa — a strategic connection linking Europe to Algeria's abundant gas fields.

Digital connection in Spain is also among the best in Europe. In April 2013, Vodafone and Orange announced a joint investment of €1bn to expand the country's fibre optic network to an additional six million homes, business premises and offices over the next four and a half years.[6]

Continuing FDI flows

Such connectivity has helped to facilitate continued high levels of foreign direct investment (FDI) throughout the downturn. Within Europe, Spain is the most favoured EU FDI investment destination after the United Kingdom, Germany and France.[7]

The sophistication of Spain's infrastructure has been a direct influence on the decision of a number of major international operators to locate in the country, including a significant number of US technology companies that now utilise Spain as a centre of excellence. Among the most recent arrivals, in 2012, Amazon opened a 30,000m^2 logistics centre on the outskirts of Madrid. The country's logistics sector

Spain's new super-regulatory authority

This past year, Spain created a new regulatory watchdog: (*Act 3/2013, of June 4th*) the National Markets and Competition Commission (CNMC).

The CNMC, which is structured as an independent body, is the result of the merger of six former regulators: the National Competition Commission, the National Energy Commission, the Telecommunications Market Commission, the Rail Regulation Committee, the Airport Economic Regulation Commission and the National Postal Industry Commission.

The creation of the CNMC is intended to enhance the effectiveness, coordination and transparency among the merged regulatory bodies and their functions, preventing redundancies and even divergent opinions, as has happened in the past.

Only three existing regulators are left outside its scope: the Securities Exchange Commission, the Bank of Spain and the Nuclear Security Council, which will maintain their own separate powers and remits.

is now the fifth largest in Europe in terms of volume and employment.

In particular, US investment flows have continued to rise since a low in 2009, with over 1,500 US company subsidiaries alone estimated to operate across all economic sectors. France and Germany may dominate Spain's international imports and exports, but it is the United States that is Spain's largest foreign investor (followed by Italy, France and the United Kingdom).

As noted above, a key characteristic of Spain's economy is its geographic diversification. Madrid may be the administrative capital and increasingly the country's finance centre, but Barcelona is a cluster for pharmaceuticals and biotechnology expertise and a centre of EU manufacturing. The city has emerged over the past decade as a leading R&D hub for agro-biotech and for the advanced diagnosis and treatment of oncology and personalized medicine.

Barcelona is also home to SEAT, the country's largest carmaker and the first non-German subsidiary of the Volkswagen Group. Indeed, the automotive sector is one of Spain's most significant industries, representing 10 percent of GDP.[8]

One of the most evident responses to Spain's labour reforms has been a significant increase in investment by automotive manufacturers and the transfer of production to the country. Ford, the first foreign manufacturer to establish production capacity in Spain in the mid-1970s, announced last year the €582m expansion of its Almussafes plant in Valencia to offset closures in Belgium and the United Kingdom. With 17 plants, Spain is Europe's second-largest car manufacturer and the leading producer of industrial vehicles in the world. Around 90 percent of the vehicles manufactured are exported.

No discussion of the Spanish economy can ignore tourism — an industry valued at US$56bn. In 2012, the country attracted 57.9m tourists, making it fourth in the world by number of arrivals and second only to the United States in terms of tourism revenues.[9] Last year saw 159m passengers pass through Spanish airports[10] — 45m through Madrid Barajas and 35m through Barcelona El Prat.[11]

Investor incentives and vehicles

It is not only Spain's visitors that receive a warm welcome. The government's desire to encourage economic growth sees that international investors enjoy increasingly attractive incentives and benefits.

As with most other EU countries, the main direct taxes applicable are Corporate Income Tax, Personal Income Tax and Non-Resident Income Tax; the main indirect taxes being Value Added Tax (VAT) and Transfer and Stamp Tax.

Spain is among the EU countries with the largest number of double taxation and investment protection treaties. Around 13,000 foreign enterprises already operate in the country and are subject to corporate income tax and VAT rates that are lower than the European average, while the tax treatment of research and development (R&D) is the second most favourable among the OECD countries — both for big companies and SMEs.[12]

The Spanish government is keen also to offer defined investment and tax benefits for activities carried out in priority industry sectors in view of their growth potential (e.g., aerospace, automotive, biotechnology and life sciences, renewable energy, environmental, information and communication technologies). Each of Spain's autonomous regional governments also offers specific investment incentives.

Such benefits extend to the tax treatment of company profits, which is below the OECD and US average. In addition, deductions and allowances applicable to new foreign investments

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can bring this down further to an effective rate of less than 20 percent. Tax incentives also apply to foreign workers' earnings.

Recent years have seen the introduction of special purpose investment vehicles in addition to the holding company tax regime — ETVE (Entitad de Tenencia de Valores Extranjeros). In light of the collapse of the country's real estate market — with prices having fallen on average 20 percent — investors are also making increased use of dedicated real estate investment vehicles (REITS), which, in Spain, benefit from a very favourable tax treatment.

Labour flexibility and skills development

Fundamentally, Spain wants to attract investment that will make best use of its human capital. Key to the efforts being made to turn the economy around are significant changes to the country's labour and employment regulations and efforts to reduce bureaucracy.

Unemployment currently stands at around 26 percent, the second highest in the Eurozone after Greece, but down from a high of 27.2 at the start of 2013. And with unemployment among those under the age of 25 at over 50 percent, many of the most dramatic measures introduced are aimed at encouraging employers to take on younger workers, including absorbing social security costs. Labour costs in Spain are now below the EU average, and the list of incentives available is growing for those employers and institutions able to offer new training and skills development opportunities. The labour force in Spain is considered among the most highly skilled and educated in Europe.

The country's private universities and business schools rank among the best in the world. Madrid was the location of Laureate International's first private university outside the United States, albeit it now operates nine institutions across Spain and 19 in total across Europe.

A focus on skills and efforts to increase productivity are already beginning to show results. Spain ranks fourth in Europe for levels of post-secondary education in scientific/technical subjects. But the 2012 amendments to Spain's labour and employment regulations, previously among the most protective in Europe, have also proved significant. The historical differences in employment protection enjoyed by full-time and contract employees have been reduced, and greater flexibility is available to employers to redeploy workers and relocate business operations.

One of the drivers behind Ford's expansion of its Almussafes plant was increased labour flexibility that will see it add up to 2,000 new jobs by 2014; the labour reforms having implied a significant shift in bargaining power away from the unions to the employers.

Likewise, collective dismissal and redundancy rules have been diluted, removing the need for administrative authorizations for dismissals — increasingly difficult from a political perspective — and an objective test has been introduced replacing the previous requirement for companies' to justify the reasonableness of their redundancy plans.

Such structural changes are complemented by new incentives to attract foreign investors, executives and managers. In line with such goals, the government has enacted a new International Investors and Entrepreneurs Law (Act 14/2013), which, among other measures, introduces permanent residence visas for foreigners who, among other situations, acquire real estate with a net investment value of at least €500,000 per applicant.

And Spain is a very nice place to live. Life expectancy is among the highest in Europe, and it has one of EU's most far-reaching health systems. Madrid and Barcelona are ranked among Europe's top 10 business cities for expatriates, while the country was ranked fourth by the OECD for Work-Life Balance in its Better Life Index — including second for time devoted to leisure.[13] With 8,000 km (4,970 miles) of coastline, its beaches are among the best in Europe — regardless of the economic outlook, the sun continues to shine, and the Mediterranean continues to sparkle. **ACC**

ACC EXTRAS ON… Conducting business in Spain and other European countries

ACC Docket
Tips & Insights—As Europe's Economy Struggles, Companies Expand Into Emerging Markets (June 2013). *www.acc.com/docket/t&i_jun13*

Quick Reference
Overview of Employment and Labor Law in Spain (Jan. 2013). *www.acc.com/quickref/law-spain_jan13*

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CMS Guide to Anti-Bribery and Corruption Laws (July 2013). *www.acc.com/corrup-law_jul13*

The Company Administrator as the Liable Party in Spanish Law (Jan. 2013). *www.acc.com/liability-spain_jan13*

New Legal Rules Under Spanish Insolvency Law (Apr. 2012). *www.acc.com/span-insolvency_apr12*

Primers
The Meritas Guide to Employee Non-Compete Agreements in Europe, the Middle East and Africa (July 2013). *www.acc.com/primer/non-com_jul13*

A Quick Guide to Venture Capital Law in Europe (July 2013). *www.acc.com/vent-cap_jul13*

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NOTES

1 *http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=tec00116.*
2 *www.oecd.org/daf/inv/ColumnChart-FDI_RR_Index_2012.pdf.*
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4 *http://ec.europa.eu/transport/themes/infrastructure/ten-t-implementation/priority-projects/index_en.htm.*
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6 *www.vodafone.com/content/index/media/group_press_releases/2013/fibre_spain.html.*
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9 UNWTO Tourism Highlights 2013 Edition.
10 *http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&language=en&pcode=ttr00012&plugin=1.*
11 *www.aena.es.*
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