

## Investment Firms and MiFID

**The transposition of MiFID as led to changes in the organisation of Investment Firms and greater protection for investors. Furthermore, it makes the provision of investment services in Spain by foreign players easier**

The transposition of the Markets in Financial Instruments Directive (MiFID) to our domestic legal system has meant a major modification in respect of the provision of investment services and ancillary services, organisational requirements and the rules of conduct required of those who offer such services.

While Spain has always been characterised by having a system of financial regulation which has provided a high degree of protection to investors, MiFID has meant and has had as its priority objective, the reinforcement of measures aimed at investor protection, as a consequence of a trend towards the greater sophistication and complexity of financial instruments.

Investment Firms are those legal entities whose regular occupation or business is the provision of one or more investment services to third parties and/or the performance of one or more investment activities on a professional basis. Investment Firms must be authorised by the Spanish Securities Market Commission (*Comisión Nacional del Mercado de Valores* or "CNMV"). In addition to the Investment Firms there exist other entities which are empowered to provide investment services and have therefore also been affected by MiFID, such as Credit Institutions and Collective Investment Institutions Management Companies authorised to provide investment services.

### Principal Characteristics of Investment Firms

Investment Firms regulated under Spanish Legislation are:

- ◆ Broker-dealers which operate both on their own account and on behalf of third parties and are authorised to provide all investment and ancillary services.
- ◆ Brokers which only operate on behalf of third parties may provide all investment and ancillary services, except for trading on their own account,

underwriting or placement of financial instruments and extending credit or loans for the performance of operations using financial instrument, where the securities firm itself is participating.

- ◆ Simplified Brokers which may only offer the service of the reception and transmission of orders, without holding funds or financial instruments for their clients.
- ◆ Portfolio Management Firms which may only offer discretionary portfolio management and investment advice, together with the ancillary services relating to advice on capital structure, industrial strategy, mergers and acquisitions and investment research.
- ◆ Investment Advice Firms are one of the innovations of MiFID and are Investment Firms which may only provide investment advice and ancillary services, such as advice on capital structure, industrial strategy, mergers and acquisitions and investment research.

Investment Firms must have a programme of activities submitted to the CNMV in which the services and activities which they offer are listed.

Furthermore, not all Investment Firms offer direct access to the Spanish Stock Exchanges. To become a member of the Stock Exchange Investment Firms must have special authorisation and meet the requirements demanded by the markets. Only Investment Firms which are Stock Exchange members are authorised to purchase and sell directly in the markets concerned. All other Investment Firms may process the orders of their clients through Investment Firms which do have the status of market members and which will be responsible for executing such orders.

## Principal innovations introduced by MiFID

MiFID has had a huge impact upon the provision of investment services by Investment Firms, given that it lays down a series of requirements which they must meet in order to be able to provide such services.

The obligations which Investment Firms must fulfil before providing investment services include:

- ◆ The duty to classify their clients into retail and/or professional categories.
- ◆ The assessment of the appropriateness or suitability of the financial instruments and services, depending on the investment service which the Investment Firm is going to offer to the client.
- ◆ Investment Firms should provide their client with information about the Investment Firm and its services, the financial instruments and their risks, costs and associated charges and the terms and conditions of the contracts.

Investment Firms must send the client a notice in a durable medium confirming execution of orders and periodic statements regarding the investment services provided.

As far as the organisational requirements are concerned, MiFID requires that Investment Firms:

- ◆ Have compliance, risk management and internal audit departments and the final responsibility for compliance with the obligations set out in the Securities Market Law and its regulatory provisions lies with the Senior Management.
- ◆ Investment Firms must keep the records required in the Securities Market Law for at least 5 years; they must comply with the obligations established for the delegation of essential functions for the provision of investment services, they must put in place procedures or policies ensuring the safekeeping and administration of financial instruments, the management of conflicts of interest, the preparation and issue of investment reports, etc.

## Market overview

Currently there are 100 Investment Firms registered in Spain with the CNMV. The majority are Brokers and

Broker-dealers. The number of Portfolio Management Firms is decreasing (only 10 Portfolio Management Firms are currently registered with the CNMV). The new category of Investment Advice Firms has rapidly increased (currently there are 22 Investment Advice Firms registered with the CNMV).

On average over the last few years, there have been between 6 and 8 de-registrations in the Investment Firms' Register and the same number of registrations.

With respect of foreign Investment Firms, in recent years the creation of branches in Spain has highly increased over the last 4 years from 18 to 64.

With respect to freedom of services, the number of foreign Investment Firms which offer investment services in Spain by taking advantage of the EU passport has increased significantly. This increase is due to the fact that following the transposition of MiFID, the activity of investment advice has become a reserved activity just like any other investment service and therefore can only be offered by duly authorised companies. Currently there are 1,600 Investment Firms with a passport to offer investment services under freedom of services, but nevertheless, only about 10% actually offer such provision.

There are today over 7,000 tied agents of Investment Firms registered with the CNMV.

Furthermore, there are in Spain 200 Credit Institutions which have the capacity to offer investment services, 342 foreign Credit Institutions which have the EU passport to offer investment services in Spain, 56 branches of Credit Institutions from Member States of the European Union (EU) and 8 branches from States which are not members of the EU.

Finally, there are 42 Collective Investment Institutions Management Companies which are authorised to carry out investment services.

## Setting up an Investment Firm in Madrid

The number of foreign Investment Firms which are authorised to offer investment services in Spain has grown rapidly over recent years. Madrid is the centre chosen to set up the majority of foreign Investment Firms.

Furthermore, the transposition to our legislation of MiFID has simplified the possibility of offering investment services in Spain enormously.

Investment Firms of Member States of the EU are able to provide investment services in Spain by:

- ◆ Taking advantage of the EU passport for freedom of services. In order to obtain the EU passport, Investment Firms should send an application to their Home State Regulator, describing the services and activities which they wish to perform in Spain. The Home State Regulator of the Investment Firm will forward notification to the CNMV that an EU passport has been processed. Following the notification the Investment Firm will be able to provide investment services in Spain.
- ◆ By opening a branch in Spain. The Investment Firms should notify the Home State Regulator of their intention to carry out investment services and activities in Spain. The Investment Firm will be able to start operating in Spain from the moment in which the CNMV proceeds to enter them in the appropriate Register.

Furthermore, foreign Investment Firms may choose to set up a subsidiary in Spain. To create a local Investment Firm it is essential to comply with a series of requirements that cover all aspects of the organisation: minimum capital, shareholders, board of directors, administrative structure, procedures for control, feasibility of the project, etc. Once an Investment Firm has been incorporated in Spain it may take advantage of the passport to offer investment services in other countries within the EU.

- ◆ Finally, the Investment Firm may opt to carry out cross-border operations by means of tied agents. To appoint tied agents the Investment Firm should notify the Home State Regulator, adding the basic details of the agent, with their address, contact information, etc. to their notification of cross-border activities under freedom of services.

With respect to Investment Firms from non-member States who wish to offer investment services in Spain, they may opt to open a branch in Spain or to set up a local Investment Firm. For both cases the prior official authorisation of the Ministry of the Economy and Finance is required. In order to obtain such authorisation compliance with an extensive series of requirements is essential and must be demonstrated to the CNMV. Once the authorisation has been obtained,

the Investment Firm may enjoy the benefits of the EU passport system in order to offer their services in the other Member States of the EU, either through a branch or under freedom of services.

## Tax regime for Investment Firms

### Direct taxation of Investment Firms

- ◆ Investment Firms which are tax resident in Spain are subject to Corporate Income Tax, which is a direct personal tax which is applicable to the earnings of companies and other corporate entities.
- ◆ The tax rate applicable will be 30 %.
- ◆ The taxable base for the tax is calculated with corrections by applying the provision of the Law on Corporate Income Tax to the book earnings determined according to the standards provided for in the Commercial Code and other laws relating to determining the earnings and in such provisions as are issued as regulations to these laws.
- ◆ A number of requirements have been established for tax credits for the impairment of certain asset items.

### Indirect taxation of Investment Firms

- ◆ Investment Firms, just as all other entities, are subject to the tax obligations set forth in the regulations on Value Added Tax, since they are taxable under this law.
- ◆ Nevertheless, we should point out that financial operations in general, with certain exceptions, are exempt from this tax.
- ◆ With respect to the possible operations which Investment Firms may carry out, operations with shares and brokering services for such operations are, among others, exempt from this tax. On the other hand, the services of the management and deposit of securities and portfolio advice and management and financial advisory services, among others, are not exempt from Value Added Tax.
- ◆ With regard to Transfer Tax and Stamp Duty (ITP y AJD) upon incorporation, Investment Firms are subject to Capital Duty and this tax amounts to 1 % of the nominal value of the capital including share premium.
- ◆ **Taxation of a branch of Investment Firms**

Foreign Investment Firms have the option to offer their services in Spain by opening a Branch. Since the Branch is considered to constitute a permanent establishment for tax purposes, it will be subject to Non-Resident Income Tax.

Nevertheless, under the provisions of the regulations on Non-Resident Income Tax, permanent establishments are taxable under the provisions of Corporate Income Tax, except where specific exceptions are applicable.

In this respect, payments which the Branch makes to its parent company and other permanent establishments in foreign countries as interest (except banks), canons, commissions for technical assistance services or for the use or transfer of goods and fees are not deductible. Furthermore, a reasonable part of the management and general administration expenses corresponding to the permanent establishment are deductible, subject to the fulfilment of certain requirements.

On the other hand, the setting up of the Branch will not be subject to taxation in Spain under the regime of Capital Duty if any of this requirements are met: (i) the holding company's Register domicile and its business management are both located in an EU Member State or (ii) at least the holding company's Register domicile is located in an EU Member State. In case that none of the mentioned requirements are met, the Branch will have to pay 1 % of the capital assigned by the holding company under the regime of Capital Duty under Transfer Tax and Stamp Duty.

◆ **Taxation of Investment Firms under regime of free rendering of services**

Foreign Investment Firms which operate in Spanish territory under the freedom of services system are taxable in the following manner:

- ✓ If they are resident in a country with which Spain has a Double Taxation Treaty in order to avoid international double taxation, as a general rule earnings obtained by Investment Firms which arise from the performance of their business are not subject to tax in Spain.
- ✓ If they are not resident in a country with which Spain has a Treaty in order to avoid international double taxation, as a general rule earnings obtained by Investment Firms which

arise from the performance of their business will be subject to Non-Resident Income Tax at a rate of 24 %.

## Useful Contacts:

Bank of Spain (Banco de España): [www.bde.es](http://www.bde.es)

CNMV: [www.cnmv.es](http://www.cnmv.es)

Tax Authority (Agencia Tributaria):

[www.agenciatributaria.es](http://www.agenciatributaria.es)

## Principal relevant legislation:

- ◆ Law 24/1988 of 28 July, on the Securities Market
- ◆ Royal Decree 217/2008, of 15 February, on the legal system applicable to Investment Firms.
- ◆ Royal Legislative Decree 4/2004, of 5 March, Approving the Consolidated Text of the Law on Corporate Income Tax.
- ◆ Royal Decree 1777/2004, of 30 July, Approving the Corporate Income Tax Regulations.
- ◆ Law 37/1992, of 28 December, on Value Added Tax.
- ◆ Royal Legislative Decree 1/1993, of 24 September, Approving the Consolidated Text of the Law on Transfer Tax and Stamp Duty.
- ◆ Royal Legislative Decree 5/2004, of 5 March approving the Consolidated Text of the Law on Non-Resident Income Tax.