

Navigating Debt Repurchases in Europe: What You Need to Know

Companies should consider a number of issues and engage in advance planning and structuring to avoid unexpected consequences in launching a debt repurchase program.

Key Points:

- Market shifts often lead companies and their affiliates to consider debt repurchases.
- Important legal considerations to factor into that analysis include:
 - Potential disclosure obligations
 - The impact of tender offer rules
 - Contractual limitations or restrictions
 - Consequences of debt purchase transactions
 - How debt purchase transactions can be structured
 - Potential tax consequences for debt repurchased at a discount
 - Jurisdictional-specific considerations

This Client Alert examines the key issues that typically arise in connection with debt repurchase programs. It also looks at issues applicable to both bond and loan repurchases, as well as jurisdictional issues raised by the UK, France, Germany, Italy, and Spain.

This discussion is intended to provide general answers that may be useful in planning a debt repurchase program. However, companies and their affiliates and financial institutions should consult with counsel about the facts specific to their circumstances before commencing any such program.

Reasons for Conducting Debt Repurchases

The potential benefits of a debt repurchase, whether of bonds or loans, largely depend on the contemplated strategy. Some key benefits from the perspective of issuers/borrowers and their affiliates are as follows:

- A debt repurchase can allow a group to reduce its overall leverage and reduce its future refinancing risk more economically than by making a voluntary prepayment.¹ This de-leveraging can, in turn,

increase capacity for other activities, such as making restricted payments or debt incurrence, and may create headroom under applicable leverage-based financial covenants (which may be particularly relevant if borrowers seek to utilize available capacity under revolving credit facilities to meet any ongoing liquidity/cash flow needs). On the flip side, there can be a potential reduction of cash on the balance sheet for purposes of netting when calculating leveraged-based ratios.

- There may be a reduction in the amount of excess cash that is available for mandatory prepayment of lenders under the group's facility agreement in the relevant financial year.
- A debt repurchase may be an attractive investment to a group's affiliates as they are able to purchase a participation in loans or purchase notes relating to what might actually be a robust credit at a price below par, thereby achieving a greater overall yield for the debt with less of the risk normally associated with the underlying credits of debt trading at below par. The affiliates could further enhance their economic returns by holding the debt and then reselling it at a price above what they paid once the market improves.
- Subject in part to disenfranchisement mechanics, affiliates may see some benefit to holding a significant position in its portfolio group's debt in order to bring creditors to the table in a restructuring or insolvency scenario.

Issues Particular to Repurchases of Bonds

Do Any Contractual Restrictions Apply?

First and foremost, the governing instrument of the bonds in question must allow for the repurchase of such bonds. The indenture or trust deed governing a particular series of bonds being repurchased is unlikely to prohibit or limit repurchases of those bonds by either the issuer or its affiliates. However, if the issuer has other outstanding debt such as revolving or term loans, the facility agreement or other agreement governing such debt may prohibit repurchasing other debt, even *pari passu* unsecured debt, absent pre-negotiated baskets usable for this purpose. In certain instances, facility agreements may limit, or require *pro rata* prepayment upon, prepayment of other equally and ratably secured debt. Additionally, the source of funds for such repurchase may impact an issuer's compliance with its debt agreements, and other debt agreements may also prohibit the use of funds thereunder from being used to repurchase other debt. The relevant covenants must be carefully examined before the repurchase program is commenced.

The intercreditor agreement or subordination deed should be reviewed to determine if the purchased notes would be subordinated to the existing notes and/or facilities (if applicable) by virtue of such notes constituting intra-group liabilities or shareholder liabilities (as applicable). In addition, consideration should be given as to whether such purchased notes would be subject to transaction security in favor of the other secured parties and if there are any local law implications, such as equitable subordination, which could mean, among other things, notes held by shareholders or other affiliates not receiving the benefit of applicable transaction security or voting rights.

Disclosure Issues

Prior to making any debt repurchase, an issuer or affiliate of such issuer contemplating such repurchase must analyze whether it possesses "material non-public information" under US securities laws and must consider the EU and UK onshored Market Abuse Regulation(s) (referred to collectively as MAR), the regulatory protections of other relevant jurisdictions, and the rules of the relevant securities exchange on

which the bonds are listed, if any. Certain specific regulatory requirements are detailed under the Jurisdictional Snapshots that follow, and issuers and their affiliates should consult US securities counsel for advice with respect to US securities laws, in particular the application of Rule 10b-5 under the US Securities Exchange Act of 1934, as amended (the US Exchange Act).

The anti-fraud provisions of the US federal securities laws impose broad restrictions on the purchase or sale of securities while in possession of material non-public information. Purchasers of debt securities need to bear these restrictions in mind, such as Rule 10b-5's requirement under the US Exchange Act to disclose material non-public information or abstain from trading. For example, an issuer that is about to announce a merger that would trigger a change of control put right under a bond indenture or trust deed generally should not be in the market purchasing those bonds at prices below par until the merger is publicly announced. Entities considering purchasing the debt securities of an affiliate face similar issues with respect to material non-public information they possess (or would be deemed to possess) about the issuer. As a result, both issuers and their affiliates should work with counsel to make appropriate materiality judgments regarding undisclosed facts and upcoming events, and to develop repurchase plans that comply with Rule 10b-5 under the US Exchange Act, MAR, and the rules of the relevant securities exchange on which the securities are listed, if any.²

Under MAR, dealings based on inside information are prohibited. "Inside information" is generally non-public information of a "precise nature" relating directly or indirectly to a company or its securities that would, if public, likely have a "significant effect" on the price of the securities. An issuer contemplating a bond repurchase program or open market purchases will need to consider, prior to implementing such a program or making any repurchases, if it is an issuer that is in scope of MAR, and whether it is in possession of inside information. The scope of MAR is very broad, and issuers often fall within some of MAR's provisions even if no application to list has been made, simply because an instrument is tradeable on a market in the EU or the UK. A public register of relevant instruments tradeable on a market in the EU is maintained by the European Securities and Markets Authority (ESMA) and the UK equivalent is maintained by the Financial Conduct Authority (FCA).³

For purposes of US federal securities laws or when a debt instrument is within the scope of MAR, it is important for an issuer to consider unreleased earnings and financial results, any unannounced merger or asset sale, the impact of the bond repurchase on the financial condition of the issuer, and the impact of the bond repurchase on the trading market for those securities. Making judgments over whether such information is or is not public, or price sensitive, or precise, often requires determinations of materiality, so issuers should work with counsel to make and record their own appropriate judgments regarding undisclosed facts and upcoming events.⁴

In addition, in every bond repurchase program, including a determination to make significant open market purchases, the question arises whether the launch of a bond repurchase program is itself material non-public information that should be disclosed to stockholders and/or bondholders in advance of commencement of the program. If the total "float" of a particular series of bonds will not be materially reduced through issuer or affiliate repurchases and retirements, it may be reasonable to conclude that disclosure prior to commencement would not be required.⁵ In some cases, however, a repurchase program's impact on the float or the trading market for the subject bonds or the impact on the issuer's financial condition or results may be independently material, and in those cases an issuer may conclude that additional disclosure may be appropriate. Absent unusual circumstances, market participants generally take the position that the fact that an affiliate of the issuer is preparing to repurchase bonds is less likely in and of itself to be material non-public information. Separately, MAR contains an own trading information defense, meaning that information about a party's intention to repurchase bonds that is price

sensitive does not prevent that party from entering into the repurchase, although it may prevent the party from making other use of that information.

Approaching existing bondholders to gauge their interest in a potential repurchase program may constitute a market sounding under MAR. MAR provides prescriptive requirements for conducting marketing soundings, including how wall crossing is to be undertaken, and the manner in which recordings of conversations with wall crossed investors are to be preserved. These requirements apply even if the information being discussed in connection with a market sounding is public (or in the public domain), although it is typically easier for issuers to conduct a market sounding if information is already in the public domain, as such information will not be deemed to be inside information and therefore will not put bondholders “off side” with regard to trading the bonds.

With respect to the impact of an issuer repurchase program on financial condition or operating results, it is important to consider whether the potential decline in the amount of outstanding debt and pro forma interest expense, when weighed against the reduction in the issuer’s cash, would permit a bondholder to argue credibly that it would not have sold at the agreed price if it had known that the financial position of the issuer would be so improved by the repurchase program. The materiality of any tax liability triggered by repurchasing the debt at a discount could also impact this analysis.

If the effect of the issuer repurchase program is not material either to the issuer’s financial condition or to the trading market for its bonds, as a general matter, it would be reasonable to conclude that no specific disclosure of the commencement, pendency, or conclusion of the repurchase program would be required. However, each case is unique, and each inquiry is highly fact specific. There will be some cases where a press release or updated disclosure in the issuer’s bondholder reports will be warranted. Issuers should also keep in mind that future financial statements will reveal the retirement of repurchased bonds.

In the event an issuer intends to implement a debt repurchase program that, due to its scope or other characteristics, should be disclosed prior to commencement, there are several ways to make the required disclosure. The most immediate way is to issue a press release announcing the launch of the debt repurchase program. The following text is an example of a pre-commencement press release and included for reference only.

“We are aware that our outstanding debt securities and debt under our credit facility are currently trading at substantial discounts to their respective principal amounts. In order to reduce future cash interest payments, as well as future amounts due at maturity or upon redemption, we may, from time to time, purchase such debt for cash, in exchange for common or preferred stock or debt, or for a combination thereof, in each case, in open-market purchases and/or privately negotiated transactions and upon such terms and at such prices as we may determine. We will evaluate any such transactions in light of then-existing market conditions, taking into account our current liquidity and prospects for future access to capital. The amounts involved in any such transactions, individually or in the aggregate, may be material.”

A common method of more generalized pre-commencement disclosure is to include a similar statement of intention in an annual or interim bondholder report. For example, in the “Liquidity and Capital Resources” section of the MD&A included in the issuer’s annual and interim reports, it may be advisable to insert disclosure along the following lines (tailored, of course, to the issuer’s actual situation):

“We or our affiliates may, at any time and from time to time, seek to retire or purchase our outstanding debt through cash purchases and/or exchanges for equity or debt, in open-market purchases, privately negotiated transactions or otherwise. Such repurchases or exchanges, if

any, will be upon such terms and at such prices as we may determine, and will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. The amounts involved may be material.”

Of course, this option is only available for those who plan ahead. The authors recommend that all issuers with outstanding debt securities consider this or similar disclosure in their annual and interim reports, which may be helpful when evaluating whether pre-commencement disclosure is required.

Under MAR, issuers should consider whether the information regarding a debt repurchase would have a significant effect on the price of the bonds if the information regarding such repurchase was made public at the time of the repurchase or after each subsequent repurchase. If an issuer fails to make an announcement when required, the issuer’s ability to make future repurchases could be restricted.

Notably, the safe harbor available under MAR for the repurchase of shares under a program within certain parameters does not apply to debt repurchases. Those parameters (e.g., the announcement of repurchases and the price and limits on repurchase amounts) are good guidelines, however, for structuring the process for bond repurchases.

For information about specific requirements in certain jurisdictions, see the Jurisdictional Snapshots that follow.

Bond Repurchases and Listing Implications

Bonds issued by European issuers are often listed on an exchange, such as the Euro MTF of the Luxembourg Stock Exchange, the Global Exchange Market of Euronext Dublin, or The International Stock Exchange, headquartered in Guernsey. To the extent an issuer’s bonds are listed on an exchange, the listing rules of the applicable exchange may provide for additional procedures, requirements, and limitations applicable to bond repurchases. Accordingly, issuers should consult with counsel about the facts specific to their circumstances before commencing any such repurchases.

For information about certain requirements with regard to the repurchase of bonds listed on the Euro MTF or Global Exchange Market, see the Listing Snapshots that follow.

Listing Snapshots

Luxembourg

Rule 903 of the Rules and Regulations of the Luxembourg Stock Exchange provides that an issuer must communicate as early as possible to the Luxembourg Stock Exchange any information relating to events affecting the issuer’s bonds admitted to trading that it deems necessary to facilitate the due and proper operation of the market. Such information must be communicated to the Luxembourg Stock Exchange in advance of the securities or corporate event so that it can take appropriate technical measures. Rule 904 of the Rules and Regulations of the Luxembourg Stock Exchange provides that such information includes, but is not limited to, information which, on the date of its publication by an issuer or on an issuer’s behalf, is likely to influence the price of the bonds. Rule 902 of the Rules and Regulations of the Luxembourg Stock Exchange requires an issuer to ensure equal treatment of all holders of bonds issued within the same issue.

As a result, the considerations discussed herein regarding the impact of any repurchases on the price of the bonds, the materiality of the fact that bond repurchases will be made, and whether open market purchases provide for equal treatment of bondholders will apply to all bonds listed on the Luxembourg

Stock Exchange. Latham & Watkins does not practice Luxembourg law. The firm advises issuers to consult with the Luxembourg Stock Exchange to confirm that repurchases are implemented in a manner that does not violate the applicable rules.

Ireland

The considerations discussed herein regarding the impact of any repurchases on the price of bonds, the materiality of the fact that bond repurchases will be made, and whether open market purchases provide for equal treatment of bondholders will apply to all bonds listed on the Irish Stock Exchange. Latham & Watkins does not practice Irish law. The firm advises issuers to consult with the Irish Stock Exchange to confirm that repurchases are implemented in a manner that does not violate the applicable rules.

Guernsey

Pursuant to Rule 3.2 of the Qualified Investor Bond Market listing rules applicable to bonds listed on The International Stock Exchange, an issuer must, as soon as reasonably practicable, notify The International Stock Exchange, via its appointed listing agent, of any full or partial redemption or cancellation of bonds to enable delisting of the repurchased bonds. Generally, such notifications are made within 10 business days after the repurchase.

As The International Stock Exchange is headquartered outside the EU, MAR does apply to issuers as a consequence of listing bonds on The International Stock Exchange. Latham & Watkins does not practice Guernsey law. The firm advises issuers to consult with its appointed listing agent to confirm that repurchases are implemented in a manner that does not violate the applicable rules.

Does a Bond Repurchase Implicate the Tender Offer Rules?

A significant percentage of bond issuances, particularly high yield bonds, have been marketed in the US pursuant to the re-sale exemption found in Rule 144A under the US Securities Act of 1933, so significant amounts of some issuances may be held through US accounts. As a result, and in light of the fact that many jurisdictions have tender offer rules that are or may be applicable to debt securities, issuers planning bond repurchases should take care to design that program such that it does not constitute a tender offer, either in the US or elsewhere. It is beyond the scope of this Client Alert to examine the pitfalls in each significant jurisdiction, however adhering to guidance designed to avoid a tender offer as developed by US case law can provide a good framework for a bond repurchase program.

The US Securities and Exchange Commission's (SEC's) tender offer rules may impose limitations that make bond repurchases less attractive.⁶ Notably, although the SEC Staff has issued no-action guidance to shorten the minimum period for a debt tender offer to five business days in certain cases, tender offers that do not meet the criteria set out in that guidance — for example, third-party tenders and offers for less than all securities in a class — are required to be kept open for a minimum of 20 business days, among other requirements.⁷

So, what is a tender offer? In its clearest form, a debt tender offer is an offer broadly made to all bondholders to tender their bonds for sale at a specified price over a fixed period of time, subject to specified conditions. However, the SEC has never adopted a definition for the term "tender offer." That term instead is defined by case law, from which certain central definitional principles have emerged.

Based on the principles that have developed from case law in the US, market participants typically conclude that accumulations of bonds solely through ordinary open-market transactions generally should not implicate the US tender offer rules.⁸ It is very common for an issuer (or affiliate of an issuer) to simply repurchase debt that is available in the open market through a broker-dealer in an efficient and effective

manner that does not generally constitute a tender offer. However, in other circumstances, including where the repurchase program will include active solicitations or negotiations to purchase bonds, issuers and their affiliates should consider the following prudential factors in designing and implementing their bond repurchase programs in order to avoid characterization as a tender offer:

- **Timing:** Make the repurchases over a reasonable period of time based on the circumstances — avoid set time periods or deadlines in connection with negotiations.
- **Number of Solicited Sellers:** Solicit only a limited number of potential sellers; the fewer the number of holders contacted, the better.
- **Variable Prices and Terms:** Make purchases from multiple sellers at individually negotiated prices and on different terms. The greater the variation in price and terms, the better.
- **Nature of Sellers:** Limit purchases to those from sellers that are sophisticated institutional investors. Market participants generally take the view that the purchase of 80% or less of a series of bonds from a limited number of sophisticated institutional investors does not constitute a tender offer.
- **Character of Offer to Purchase:** Refrain from applying pressure to potential sellers to sell their bonds, such as “take it or leave it” offers, offers conditioned on other purchases, or offers open for very short periods before being rescinded.

Undoubtedly, all facts and circumstances will be relevant in determining what constitutes a tender offer.

Can Bond Repurchase Programs Help an Issuer Win a Consent Solicitation?

Issuers and affiliates should not pursue a debt repurchase program for the purpose of gaining voting control over bonds in anticipation of an upcoming consent solicitation. It is current market practice for indentures and trust deeds to generally provide that bonds held by the issuer or its affiliates are disregarded for purposes of voting, including in the context of consent solicitations.⁹ As a result, a repurchase program by an issuer or affiliate will not typically affect the outcome of a consent solicitation to the issuer’s advantage. In fact, by reducing the number of bonds deemed outstanding for purposes of a consent, a bond repurchase could have the undesired effect of concentrating ownership in the hands of fewer bondholders and providing them with extra leverage in a consent solicitation.

Will Repurchases Impact Credit Ratings?

Issuers should consider whether a bond repurchase, or the announcement thereof, could trigger negative rating actions. Rating agencies may view significant repurchases as a “distressed exchange,” which could result in rating downgrades. Agencies may issue a negative rating if a realistic probability of a default exists and investors receive less value than promised on the original securities as a result of the bond repurchase. Issuers of highly speculative bonds (B-/B3 or lower) are particularly likely to experience a negative rating action as a consequence of a bond repurchase below par.

What Are Some Additional Issues for Affiliates?

In addition to the issues previously described, affiliates of bond issuers (e.g., private equity owners of portfolio companies) face other hurdles when buying or selling those bonds, including:

- An affiliated purchaser will need to comply with the transfer restrictions contained in the indenture, which may require the affiliated purchaser to certify that it is a Qualified Institutional Buyer (QIB) or eligible purchaser under Regulation S in order to purchase the notes. Additionally, absent an effective

resale registration statement or an exemption from the registration requirements of the US Securities Act (such as Regulation S, which permits sales outside the US, and Rule 144A, which permits sales to QIBs), affiliates may be limited in their ability to resell the bonds they have acquired. Regulation S and Rule 144 provide some relief, but still impose certain restrictions on affiliates (e.g., Rule 144 imposes a holding period and volume and manner-of-sale limitations). Fungibility issues may also complicate the resale of bonds by an affiliated purchaser.

- Affiliates with positions on an issuer's board of directors should consider the extent to which contemplated repurchases should first be presented to the issuer's board of directors in order to avoid challenges under local law, corporate opportunity, and similar doctrines.
- Affiliates must consider any other potential impacts of the purchase of debt of one of its affiliates, including restrictions under any fund limited partnership agreements, potential inter-fund conflicts (e.g., when one fund is purchasing the debt of the portfolio company of another fund), or tax implications to the affiliated issuer or other funds.

Issues Particular to Repurchases of Bank Debt

A repurchase of loans involves a borrower or its affiliate (such as another member of the borrower group, an unrestricted subsidiary, or its investors or private equity sponsors) purchasing a portion of the outstanding loans of that borrower. This may be done by way of assignment or transfer of commitments and also by sub-participations and transactions having an economic effect substantially similar to a sub-participation (hereinafter collectively referred to as "debt purchase transactions"). A loan that is purchased may or may not then be extinguished, depending on the documentation, which entity purchases the loan, how the debt purchase transaction is structured, and other technical legal considerations.

The vast majority of facility agreements in the market are based on the Loan Market Association's form of facility agreement or derivatives thereof, which set out precise mechanics for carrying out a debt purchase transaction. However, given that the mechanics are subject to commercial agreement and there are varying degrees of movement away from the Loan Market Association's starting point, each facility agreement should be reviewed individually to understand the precise conditions, mechanics, and restrictions that may apply in that case to such debt purchase transactions. In addition, the borrower group structure should be reviewed to ascertain any adverse local law and tax considerations.

Are Debt Purchase Transactions by Members of the Borrower Group Permitted?

One of the first steps when considering a debt purchase transaction should be to check the relevant facility agreement to determine both whether a specific regime governing debt purchase transactions is included and which entities in the borrower group (including unrestricted subsidiaries) can enter into debt purchase transactions. In some instances, only the borrower of the relevant facility is allowed to purchase debt, in which case the purchase will need to be structured to accommodate this stipulation and also account for any specified consequences of a borrower entering into a debt purchase transaction (e.g., such participations or loans being automatically extinguished). Alternatively, facility agreements may allow for a degree of flexibility by providing that any member of the borrower group (including unrestricted subsidiaries) can enter into debt purchase transactions, and such acquired debt is not extinguished if it may cause a material adverse tax impact on the borrower group. Usually, affiliates of the borrower group are not restricted from entering into debt purchase transactions subject to any limitations set out under the assignment and transfer provisions of a facility agreement and disenfranchisement provisions.

What Type of Debt Can Be Purchased?

Generally, facility agreements restrict debt purchase transactions by the borrower group to purchases of term debt and do not permit repurchase of revolving lines. Some facility agreements, however, depart from the norm and are unrestricted in this respect, so the facility agreement should be checked to ensure the contemplated repurchase strategy can be achieved. Typically, though, purchasers may not want to repurchase revolving lines as this could result in the debt being extinguished (as explained below), which may reduce available sources for future funding.

What Sources Can Be Used for a Debt Purchase Transaction?

Facility agreements may contain specific restrictions on the source of funds being used for debt purchase transactions and should be checked carefully before embarking on a debt purchase program. There is generally a spectrum of possible restrictions. On one end of the spectrum, some facility agreements require that the consideration for any debt purchase transaction comes solely from excess cash flow or sponsor equity injections and shareholder loans. On the other end, some facility agreements offer the borrower group full flexibility by allowing debt purchase transactions to be undertaken from funds coming from other available sources, including, but not limited to, utilizations under that facility agreement (including undrawn term or revolving facilities) or additional indebtedness — this formulation clearly offers substantial benefits to a borrower if the borrower's objective behind the debt purchase transaction is to reduce overall leverage without expending cash on balance sheet.

Conditions Relating to Debt Purchase Transactions

The facility agreement should be checked if any other conditions to debt purchase transactions apply, which may impact the contemplated repurchase strategy. Two typical conditions are, first, that there is no event of default (or, in some instances, no default) continuing at the time of the debt purchase transaction, and second, that the participations are being acquired at below par.

Consequences of a Debt Purchase Transaction

When entering into a debt purchase transaction, borrowers should consider the potential consequences under the finance documents. Once debt is purchased by a borrower or member of the borrower group (including unrestricted subsidiaries), it should be checked under the relevant facility agreement if the purchase results in the corresponding portion of the debt under the facility agreement being automatically extinguished or if a further step is required to waive or forgive the debt. Borrowers should also check the facility agreement to determine whether any accounting gain arising from the purchase of debt at less than par will be excluded for the purpose of any financial covenants. As discussed below, there can be tax implications with regard to the forgiveness of debt. If a member of the borrower group or an affiliate is acquiring the debt, any intercreditor agreement or subordination deed should be reviewed to determine if the debt would be subordinated to the facilities by virtue of it being intra-group liabilities or shareholder liabilities (as applicable). In addition, borrowers should consider whether such acquired loan (if not extinguished) would be subject to transaction security in favor of the other secured parties and if there are any local law implications, such as equitable subordination, which could mean, among other things, loans held by affiliates not receiving the benefit of applicable transaction security. In some jurisdictions, it is common for intercreditor agreements to exclude equitably subordinated creditors from recoveries and security.

Will Borrowers or Affiliates That Purchase Debt Be Allowed to Vote on Lender Matters?

The facility agreement should be checked to see what rights the purchaser (being a member of the borrower group or certain of their affiliates) might have once it purchases debt. In order to establish a separation between the lender group and such purchasers of debt and avoid potential conflicts of interest,

the relevant facility agreement and intercreditor agreement may provide that such purchaser is disenfranchised (i.e., their commitments would be deemed to be zero for ascertaining lender votes). Additionally, a purchaser may not be allowed to participate in meetings or conference calls which all lenders are invited to attend. Some facility agreements and intercreditor agreements might allow the purchaser to vote on all lender matters only and/or matters that materially adversely impact the rights of such purchaser. It is common for facility agreements to exempt affiliated independent debt funds from such provisions.

How Are Debt Purchase Transactions Structured?

Debt purchase transactions can be structured in a number of formats — borrowers should check the relevant facility agreement to see which formats are provided, and comply with the relevant timelines under the specific format. There might also be obligations to notify the agent under the relevant facility agreement once debt purchase transactions have been completed. Generally, facility agreements include a solicitation process and an open order process, and on occasion a bilateral process, each of which are described in more detail below.

Solicitation Process

This process involves the purchaser, or a financial institution acting on behalf of a purchaser (the Purchase Agent), inviting each of the lenders to offer an amount of its participation for sale.

The lenders that are interested in selling their debt make offers to the purchaser (or the Purchase Agent) and such offers remain irrevocable for a specific amount of time, during which the purchaser can accept the offers.

The facility agreement may provide for flexibility in terms of which offers the purchaser or the Purchase Agent can accept and what needs to be done in case there are multiple offers at the same price (e.g., there may be a requirement that debt be bought pro rata from the lenders that have made the same offer). Additionally, the facility agreement may require the purchaser or the Purchase Agent to accept offers in inverse order of their price (i.e., with the lowest offer being accepted first).

Open Order Process

This process involves the purchaser making an offer to purchase participations up to a set amount at a set price by notifying (including via a Purchase Agent) all lenders under the relevant facility at the same time.

The lenders that wish to sell will communicate this to the purchaser or, if applicable, the Purchase Agent and the lenders' offer to sell will remain irrevocable for a certain amount of time. The facility agreement may include provisions on what should be done in case the offers from the lenders are in excess of the total amount of the open offer (e.g., the purchaser may be required in such instances to accept the lenders' offers on a pro rata basis).

Bilateral Process

The relevant facility agreement may also provide for purchasers to make secondary market purchases of debt or enter into bilateral arrangements for the purchase of debt (including via a Purchase Agent). The process and requirements for such bilateral processes are as provided in the relevant facility agreement. Typically the facility agreement will provide that the purchaser must first undertake a solicitation process or an open order process before it is permitted to make bilateral purchases. There may be further requirements that bilateral purchases are only permitted during a limited window after the solicitation or

open order process expires (e.g., 30-60 days), and there may be limitations on the price paid for any bilateral purchase (e.g., not to exceed the lowest purchase rate tendered by the lenders during the solicitation process).

Other Considerations for Conducting Debt Repurchases

Borrowers should seek tax advice in order to ascertain the implications of any debt purchase transaction, including if there is likely to be a taxable gain on debt being extinguished or any potential stamp or withholding tax issues to consider. For more information on the potential tax implications of a debt repurchase, see the Jurisdictional Snapshots section below.

If the relevant facility and/or the borrower have a specific credit rating, borrowers should consider whether or not a debt purchase transaction could result in adverse consequences vis-à-vis its credit rating and in particular if the debt purchase transaction could result in a default under its credit rating conditions.

Borrowers should also consider the regulatory implications of debt purchase transactions, and seek local law advice in relevant jurisdictions. Relevant aspects may include market abuse or insider-dealing regimes and disclosure of confidential information.

Jurisdictional Snapshots

United Kingdom

Issues Particular to Repurchases of Bonds

There is little regulation applicable to bond repurchases under English law. An issuer whose bonds are listed on the regulated market of the London Stock Exchange is subject to Rule 6.1.3. of the Disclosure and Transparency Rules. This rule obliges issuers to give all holders of their debt securities ranking *pari passu* equal treatment in respect of the “rights attaching to those debt securities.” For the avoidance of doubt, most high yield bonds issued by UK issuers in reliance on Rule 144A and Regulation S are typically outside the scope of this principal of equal treatment as such bonds are rarely listed on a regulated market but rather listed on a multilateral trading facility (e.g., the Euro MTF of the Luxembourg Stock Exchange or the Global Exchange Market of Euronext Dublin) or an exchange outside the European Economic Area (e.g., The International Stock Exchange).

The generally accepted position is that rights attaching to those debt securities for the purposes of Rule 6.1.3 refers to rights contained in indentures and trust deeds (i.e., rights enforceable against the issuer (such as the right to payment of principal and interest)). It does not refer to rights that are incidental to ownership, such as the right of a holder to sell its bonds in a tender offer, since a tender offer is a separate contract between issuer and bondholder and separate to the rights given to bondholders by issuers in indentures and trust deeds.

Accordingly, it is not thought that an issuer that employs a strategy to avoid the US tender offer rules and restricts the ability of US holders to participate in the tender offer would fall afoul of Rule 6.1.3. In any event, aside from this limited circumstance, there can be no suggestion that an issuer repurchasing in the open market falls afoul of this rule since all bondholders are understood to have the same opportunity to sell into the open market and any repurchase tender offer would be made available to all bondholders alike.

Notably, a majority of bondholders cannot accept a repurchase offer with binding effect on all bondholders, as the offer to repurchase is conducted between the issuer and each individual bondholder.

Issues Particular to Repurchases of Bank Debt

There are no additional specific considerations to those already set out in the section “Issues Particular to Repurchases of Bank Debt,” above, and the “Corporate Governance” and “Tax Considerations” sections, below, in each case, relating to the UK.

Corporate Governance

Issuers/borrowers (as applicable) should ensure that any debt repurchase complies with general company law requirements, including that the directors act in the best interests of the issuer/borrower, that the repurchase is permitted under the issuer/borrower’s constitutional documents and that the issuer/borrower has sufficient cash liquidity once the repurchase has been completed.

Tax Considerations

A UK company (a UK debtor) acquiring its own debt (whether in the form of a loan or bonds) or a company acquiring the debt of a connected UK debtor (a new creditor) at a discount will generally give rise to taxable income for the UK debtor equal to the difference between the carrying value of the liability in the UK debtor’s accounts and the acquisition price. A cash tax liability will likely be payable if the UK debtor does not otherwise have losses or other deductions that can be used to offset this income. Certain exemptions may apply to exempt such tax charge if debt is acquired by a creditor connected with the UK debtor in limited circumstances. These exemptions include:

- **The corporate rescue exemption:** This exemption applies if (1) the new creditor releases the debt within 60 days of acquiring it, (2) the new creditor acquired the debt in an arm’s-length transaction, and (3) it was reasonable to assume immediately before the new creditor acquired the debt that without the release there was a material risk that the UK debtor would have been unable to pay its debts at some point within the next 12 months.
- **The equity-for-debt exemption:** This exemption applies if the acquisition of the debt is an arm’s-length transaction and the consideration given by the new creditor for acquiring the debt consists only of ordinary shares (or an entitlement to ordinary shares) in the new creditor or a connected company.

For the purposes of the above, there is a connection between two companies if one controls the other or both are controlled by a third person (whether or not a company). The term “control” requires an ability to secure that the affairs of the company are carried out in accordance with the controlling party’s wishes by means of holding shares or possessing voting power, or as a result of any powers conferred by the articles of association or other document regulating the company or any other company. An anti-avoidance provision applies if the parties enter into arrangements that are designed to circumvent a tax charge arising under the rules described above in relation to a company acquiring the debt of a connected UK debtor.

A repurchase of UK plain vanilla debt is likely to be exempt from UK stamp taxes under the UK loan capital exemption, however, the terms of the debt should be reviewed to confirm that there are no features that may prevent this exemption from applying, for example, an interest rate that is dependent on the economic results of the UK debtor.

In the case of a new creditor acquiring the debt of a connected UK debtor, the parties should consider any UK withholding tax implications and any clearances that need to be sought in respect of interest payments made by the UK debtor to the new creditor, if the new creditor is a company resident outside the UK and the debt is not a “quoted Eurobond”.

France

Issues Particular to Repurchases of Bonds

The vast majority of high yield bonds issued by French issuers are governed by New York law and marketed to international and non-French investors, consequently qualifying under article L. 228-90 of the French Commercial Code as “issued outside of France” (*émis à l'étranger*). As a result, most of the French rules applicable to bonds (*obligations*) do not apply to standard New York-law-governed European high yield bonds issued by French issuers. In addition, nearly all high yield bonds issued by French issuers are listed on markets outside of France, in particular in the Channel Islands, Luxembourg, and Ireland, and therefore French listing rules do not apply.

Article L. 228-74 of the French Commercial Code, which provides that all bonds issued by French entities that are bought back by issuers must be cancelled upon repurchase, remains nevertheless mandatorily applicable to all bonds issued by French entities, even when they are considered “issued outside of France” for purposes of article L. 228-90. However, this restriction does not apply to bonds repurchased by a parent, subsidiary, or other affiliate.

In addition, article L. 213-0-1 of the French Monetary and Financial Code provides exemptions to this obligation to cancel repurchased debt securities that apply to non-convertible debt securities that are listed on a regulated market or on a multilateral trading facility that is subject to the laws and regulations on insider trading sanctioned by the French Financial Markets Authority (*Autorité des marchés financiers*). This includes debt securities that are listed on any foreign market subject to MAR. In such instances, a French issuer can hold (i.e., not immediately cancel) its own debt securities, provided that all the following conditions are met:

- The securities are repurchased for purposes of improving liquidity of the instrument
- The aggregate principal amount of the bonds repurchased does not exceed at any point of time 15% of the principal amount of the bonds
- The issuer may only hold the repurchased securities for up to one year after the purchase
- Any right of the issuer as holder of the purchased securities is suspended during the time such securities are held by the issuer

Notably, the provisions of the French Commercial Code providing for the automatic disenfranchisement of any entity that directly holds at least 10% of the share capital of a French bond issuer are not applicable to holders of bonds issued outside of France, such as standard New York-law-governed European high yield bonds.

Finally, repurchases of bonds issued by French issuers that are not issued outside of France within the meaning of article L. 228-90 of the French Commercial Code and/or are listed on French markets (such as most investment grade bonds, convertible bonds, and Euro Private Placement bonds issued by French entities) are subject to a specific regime that may differ from the regime applicable to New York-law-governed European high yield bonds described above.

Issues Particular to Repurchases of Bank Debt

Borrowers organized under the laws of France and willing to acquire their own outstanding bank debt will need to consider whether doing so is compliant with French banking monopoly rules. In particular, if the

transferor is a French entity, the acquisition of a drawn participation may of itself be considered a regulated transaction.

From a contractual perspective, it is common for facility agreements (whether or not they are governed by French law) to include specific provisions that protect the interests of the banks/lenders taken in the context of potential French insolvency or safeguard proceedings, to address the fact that after the commencement of safeguard or judicial reorganization proceedings, creditors' committees must be established to vote on any proposed plan.

Similar restrictions may also apply to a French entity that has issued private / non-listed bonds subject to French law (e.g., in a unitranche financing).

In addition to the above, the French Commercial Code provides that any company that directly holds at least 10% of the share capital of a French issuer may not vote in any general meetings of holders of a category of bonds held by such shareholder. This rule is generally considered mandatory and may not be waived through contractual or other arrangements.

Tax Considerations

A repurchase by a French borrower of its own debt (whether in the form of a loan or bonds) for consideration below the nominal value or issue price of such debt gives rise to taxable income equal to the difference between the outstanding principal amount of such debt and its repurchase price. Such income is subject to French corporate income tax at the ordinary rate (i.e., at a current maximum actual rate of 25.83%) with respect to the fiscal year during which the debt is cancelled on the balance sheet of the borrower. In the case of bonds that are to be later resold in the market (if such bonds would not have to be cancelled by the borrower further to their repurchase), the borrower realizes an ordinary profit or loss equal to the difference between the resale price of the bonds and their acquisition price on the market.

The repurchase of debt through an affiliated entity does not *per se* trigger any particular consequences at the level of a French borrower or issuer. However, such repurchase by an affiliated entity may trigger, at the level of the borrower or issuer, the application of the interest deductibility limitations that apply in respect of debts contracted from so-called "related" or "associated" parties (i.e., primarily the application of French thin capitalization rules and the anti-hybrid provisions implemented into French tax law pursuant to the European Union ATAD 2 provisions). If such affiliated entity is a French tax resident, such repurchase may generate taxable profit at the level of such affiliated entity if the debt is repaid in full at its nominal value or issue price by the French borrower/issuer or subsequently resold on the market at a price above the price at which the affiliated entity repurchased it, or a loss at the level of such affiliated entity if the debt is subsequently resold on the market at a price below the price at which the affiliated entity repurchased it. In the case of a waiver of debt that is motivated by financial reasons, the deduction of the corresponding loss at the level of the affiliated entity is subject to very stringent conditions. In the event the loss is not deductible, a specific tax regime may allow the borrower to be exempt from corporate income tax on the corresponding profit, but here again subject to strict conditions (i.e., the waiver of debt must be granted by a parent company of the borrower/issuer in the sense referred to under the French parent-subsidiary regime, and the borrower must undertake to proceed with a share capital increase paid in cash (or by means of an offset against an existing receivable) to be subscribed by such parent company in an amount at least equal to the amount of the waiver of debt before the close of the second subsequent fiscal year).

Germany

Issues Particular to Repurchases of Bonds

Equal Treatment of Bondholders

Bond repurchases are sparsely regulated under German law. However, an issuer that has chosen Germany as its home EU Member State and whose bonds are listed on a regulated market may, under certain circumstances, be subject to an obligation to treat all holders of a class of securities equally. For the avoidance of doubt, high yield bonds issued by German issuers in reliance on Rule 144A and Regulation S are typically outside the scope of this principle of equal treatment as such bonds are rarely listed on a regulated market but rather listed on a multilateral trading facility (e.g., the Euro MTF of the Luxembourg Stock Exchange or the Global Exchange Market of Euronext Dublin) or an exchange outside the European Economic Area (e.g., The International Stock Exchange).

For issuers who choose Germany as their home EU Member State and whose bonds are listed on a regulated market, the principle of equal treatment applies irrespective of the law governing the securities. The principle of equal treatment will generally be satisfied in the case of bond repurchases via a stock exchange.

In the context of a bond repurchase, there are two primary ways of complying with this rule. If the issuer repurchases in the open market, all bondholders are understood to have the same opportunity to sell into that market. Alternatively, the issuer can conduct a repurchase offer that is open to all bondholders. It is important to note that certain strategies described under the title “Does a Bond Repurchase Implicate the Tender Offer Rules?” above that are used to avoid a tender offer under the US rules may be at odds with the German requirement to treat all bondholders equally. The current understanding and interpretation of the German equal treatment rule would also prohibit incentivizing certain, but not all, bondholders to tender into the offer by adding additional consideration. However, such “sweetening the deal” is permissible in the context of an early tender premium so long as such early tender premium is available to all bondholders. For bonds governed by German law, it is not possible for a majority of bondholders to accept a repurchase offer of an issuer with binding effect on all bondholders.

Issues Particular to Repurchases of Bank Debt

Under German law, a borrower (or any affiliate of a debtor) may acquire liabilities owed by it unless the parties have agreed otherwise. However, if a borrower becomes the creditor of a receivable or other claim against itself, such receivable or other claim will generally be automatically extinguished. Hence, if a borrower purchases a participation in a loan owed to it, the relevant loan and underlying commitment would cease to exist. This concept is, however, limited to repurchases by the debtor of a receivable, and any receivables and claims acquired by an affiliate of the debtor will continue to exist.

In addition, many bond and loan transactions are governed by laws other than German law (in particular, English or New York law). In this case, under German conflict of law rules, the law governing the relevant debt instrument also governs the question of whether such an instrument will continue to exist following its acquisition by the issuer, borrower, or an affiliate thereof.

Equitable Subordination

Under German insolvency law, claims under loans granted by (direct or indirect) shareholders or transactions with a similar economic effect are subordinated if insolvency proceedings are opened in respect of the debtor thereof. According to the prevailing view in German legal literature, bonds should be treated as transactions with a similar economic effect and therefore can be subject to the same

subordination as loans granted by shareholders. In the context of a syndicated loan or widely placed bonds, the rights of the other lenders or bondholders should not be “tainted” if a shareholder holds a participation in the loan or bonds. However, this has not been confirmed with a final ruling by German courts.

In addition, any repayment of a shareholder loan or a transaction with similar effect can be clawed back by an insolvency administrator if it occurred within the last year prior to the filing for the opening of insolvency proceedings. Similarly, the granting of any security or guarantee for such obligations can be clawed back for a period of up to 10 years prior to the filing for the opening of insolvency proceedings. Typically, intercreditor agreements with German borrowers, issuers, or guarantors tend to include provisions excluding shareholders of the relevant German entity from the distribution of any proceeds from the enforcement of credit support to mitigate the risk that the claims of other creditors are tainted and therefore subject to the same subordination and clawback risks.

Tax Considerations

If a German borrower or issuer repurchases its own debt at less than nominal value, German tax law assumes a profit of the borrower/issuer in the amount of the difference between the book value and the amount paid (including transaction costs). The repurchase of the debt through an affiliated German or foreign entity may avoid this tax burden. However, if such affiliate is a German tax resident, it may generate a taxable profit if the debt is subsequently paid back by the German borrower/issuer in total at its nominal value or issue price. This may differ in other jurisdictions. A subsequent waiver by the acquiring affiliate, on the other hand, may result in a tax burden at the level of the borrower/issuer. Under certain circumstances, a tax exemption for the taxes triggered by the waiver may be available. However, such tax exemption typically requires a financial crisis of the borrower/issuer (i.e., the borrower/issuer could not, on the basis of its balance sheet structure and financial forecast, service its existing debt in full) and in practice usually is supported by a binding ruling with the competent tax office to be sought in advance of the repurchase.

When determining the cash available for a repurchase, borrowers/issuers should take into account the potential tax liability that might be triggered by such profits (depending, of course, on the overall earnings of the borrower).

Italy

Issues Particular to Repurchases of Bonds

Repurchases of debt securities may be governed by tender offer rules pursuant to Italian laws and regulations of general application. However, selective or private repurchases of debt securities as well as cash tender offers involving debt securities that (1) are extended exclusively to qualified investors or (2) have a minimum denomination of at least €100,000 launched by the issuer of such securities or its parent, or an affiliate or by an intermediary engaged by one of the latter, are, in each case, exempt from the Italian tender offer rules. From a general perspective, all offers to repurchase debt securities undertaken by an Italian issuer are exempt from Italian tender offer rules, provided that the debt securities repurchased are not (1) financial instruments with voting rights in an ordinary or extraordinary shareholders’ meetings of a listed issuer (voting instruments); (2) saving shares; (3) units issued by investment funds and SICAVs; or (4) convertible into or rights to subscribe or purchase for Voting Instruments (see Article 35-bis, paragraph 4, of the Consob Regulation no. 11971). This exemption extends to (1) offers undertaken by affiliates of the issuer (such as companies or entities controlling the issuer, or companies controlled by or under common control of the issuer); (2) offers undertaken by an intermediary on behalf of the issuer or affiliates of the issuer, provided that there is an obligation by the

intermediary to transfer the purchased securities to the issuer or its affiliates, and (3) offers undertaken by a guarantor of the securities that are subject to the offer (see Article 35-bis, paragraph 7, of the Consob Regulation no. 11971).

In addition, consent solicitations and amendment and waiver requests are not subject to the Italian tender offer rules. Note that debt securities held by the issuer cannot be voted in connection with any amendment or waiver request and, as a general rule of Italian law, debt securities held by the issuer cannot be counted for quorum purposes in the resolutions adopted by bondholders' meetings.

Public Disclosure Requirements

Due to Italian tax requirements, debt securities issued by Italian entities that do not have listed shares are nearly always listed on a regulated market or a multilateral trading facility (MTF) within the EU. Therefore, issuers will nearly always need to take into account considerations relating to MAR when purchasing debt of an Italian issuer.

Issues Particular to Repurchases of Bank Debt

Borrowers incorporated under the laws of Italy and willing to acquire their own outstanding bank debt will need to consider whether doing so is compliant with Italian laws on lending restrictions. In particular, the acquisition of a drawn participation may itself be considered as a transaction subject to such restrictions, therefore, only authorized institutions such as Italian financial institutions, EU financial institutions controlled by EU banks, Italian/EU banks, non-EU banks subject to authorization by the Bank of Italy, SACE S.p.A., Italian insurance companies, Italian securitization vehicles, and Italian and EU AIFs could be authorized to conduct such transactions. Note that these Italian lending restrictions are a primary reason that many typical Term Loan B structures are unavailable in Italy. Therefore, under typical circumstances, an Italian company will most likely not be able to repurchase its own bank debt.

In addition, from a contractual perspective, it is common for facility agreements (whether or not they are governed by Italian law) to include specific provisions that protect the interests of the banks/lenders (such as in the context of voting under the finance documents), which would be expected to apply in the case of repurchased bank debt.

Equitable Subordination

Italian corporate law contains subordination provisions to protect creditors against "undercapitalized companies". Specifically, in the case of a loan to a company made by (1) a person that, directly or indirectly, directs the company or exercises management and coordination powers over that borrowing company, (2) any entity subject to the management and coordination powers of the same person, or (3) a quota holder in the case of a company incorporated in Italy as a limited liability company (*società a responsabilità limitata* or *S.r.l.*), such loan will be subordinated to all other creditors of that borrower and rank senior only to the equity in that borrower if the loan is made when, taking into account the kind of business of the borrower, there was an excessive imbalance of the borrower's indebtedness compared to its net assets or the borrower was already in a financial situation requiring an injection of equity and not a loan ("undercapitalization"). Any payment made by the borrower with respect to any such loan within one year prior to a bankruptcy declaration is required to be returned to the borrower. The above rules apply to shareholders' loans "made in any form", and scholars generally conclude that such provisions should be interpreted broadly and apply to any form of financial support provided to a company by its shareholders, either directly or indirectly.

There are several court precedents interpreting the provisions summarized above. Some of these precedents have held that such provisions also apply to companies incorporated as joint stock companies (*società per azioni* or *S.p.A.*).

Tax Considerations

Any repurchase or decision to cancel debt securities or loans should be discussed in advance with Italian tax counsel, as such decision could have tax implications, depending on the facts and circumstances associated with the transaction, particularly in the case of any debt cancellation.

Spain

Issues Particular to Repurchases of Bonds

Most of the high yield bonds issued by Spanish issuers are governed by New York law and marketed to international and non-Spanish investors, consequently qualifying under article 405 of the Spanish Companies Act (*Real Decreto Legislativo 1/2010, de 2 de julio, por el que se aprueba el texto refundido de la Ley de Sociedades de Capital*) as “issued abroad” (i.e., outside of Spain). As a result, most of the Spanish rules applicable to bonds, in particular, the rights of the bondholders vis-à-vis the issuer, their forms of collective organization, and the regime for the repayment and redemption of the securities do not apply to standard New York-law-governed European high yield bonds issued by Spanish issuers. Additionally, most of the high yield bonds issued by Spanish issuers are listed on markets outside of Spain, in particular in Luxembourg and Ireland, and therefore Spanish listing rules do not apply.

Consequently, the repurchase of bonds by Spanish issuers and/or its affiliates will depend on the law to which the issuance is subject to and the terms agreed in the governing instrument of the bonds in question.

For Spanish local bonds where the issuer is Spanish and the bonds are subject to Spanish law, article 430(c) of the Spanish Companies Act requires that all bonds issued by Spanish entities and that are repurchased by such Spanish entities must be cancelled upon repurchase. In addition, this restriction also applies to entities that belong to the group of companies of the Spanish issuer.

Issues Particular to Repurchases of Bank Debt

According to Spanish law, a borrower is entitled to acquire its own outstanding bank debt unless expressly agreed otherwise under the underlying finance documents. If the finance documents are subject to Spanish law and as a consequence of such repurchase a person is, at the same time, a borrower and creditor of the same debt, such debt is automatically extinguished.

Notably, a significant portion of the loans provided to Spanish corporations are governed by English or New York law, and under such circumstances the law applicable to the loan regulates any potential issue in connection with the extinguishment of such debt if a borrower becomes the creditor at the same time.

Equitable Subordination

According to Spanish insolvency law, in an insolvency proceeding, the rights of the creditor/bondholder are subordinated to the unsecured and secured creditors if the creditor/bondholder is deemed to be a “closely related party” to the insolvent debtor/issuer when the loans/bonds were made.¹⁰ Hence, if the bank debt/bond has been acquired by a shareholder or a member of the borrower’s group, it will be subordinated in the event insolvency proceedings are opened in respect of the debtor/issuer thereof.

Equitable subordination will also prevent the relevant creditor from voting in the insolvency proceeding.

Any potential future acquired debt tainted for being owned by a “closely related party” will also be subordinated, despite the fact that the new holder of such debt may not be a closely related party.

If there is no insolvency proceeding, no equitable subordination risk applies.

Tax Considerations

If a Spanish company (a Spanish debtor) repurchases its own debt (either in the form of a loan or bonds) at less than its nominal value, income will generally arise in an amount equal to the difference between the book value and the amount paid (including transaction costs). In this regard, no book-to-tax adjustment is foreseen in the Spanish Corporate Income Tax (CIT) law for these debt transactions, and therefore the income derived from the repurchase of debt will be fully taxable at the general CIT rate (currently 25%) in the fiscal year during which the debt cancellation is recorded on the balance sheet of the Spanish debtor. A cash tax liability will likely be payable if the Spanish debtor does not otherwise have carried forward losses (which exceptionally can be offset without limitation in the case of repurchases of debts, as is the case with other debt transactions such as write-offs), or other deductions that can be used to offset this income.

If the repurchase of the debt is executed by an affiliated entity (either a Spanish or a non-resident company), this taxation can initially be avoided, although taxable income will be generated when the debt is repaid at the level of the Spanish debtor (i.e., if the debt is not totally repaid, subject to the discussion included below in respect of waivers or capitalizations) or at the level of the affiliated company (i.e., if such affiliate is a Spanish company and the debt is repaid above the debt repurchase value, subject also to the discussion included below in respect of waivers or capitalizations).

In the case of a waiver of debt, the Spanish debtor will generally record income equal to the debt book value, and this income will be fully taxable at the general CIT rate, unless the waiver is granted by a creditor that holds a 100% interest in the Spanish debtor's share capital, in which case the waiver will be treated as an increase of the creditor's participation in the Spanish debtor's equity. If the creditor does not hold a 100% interest in the Spanish debtor's share capital, taxable income will be recorded by the Spanish debtor for the proportion of debt that does not correspond to the shareholding of the creditor. In any case, even if the creditor holds a 100% interest in the Spanish debtor's share capital, the Spanish debtor is likely to be taxed on the difference between the fair market value of the debt repurchased (i.e., the repurchase price) and the book value (i.e., the principal amount) of the debt.

In a capitalization of the debt, a special tax rule (article 17.2 of the CIT law) applies according to which, irrespective of the accounting implications, no income is realized by the Spanish debtor for tax purposes, provided that the share capital or equity increase is equivalent to the principal amount of the debt. However, according to this special valuation rule, such income will be captured at the creditor level and will be fully taxable at the general CIT rate provided that the creditor is a Spanish resident company. If the creditor is a non-resident entity, according to certain binding rulings issued by the Spanish tax authorities, such non-resident creditor may obtain income that will be deemed a capital gain. Such capital gain will be equivalent to the difference between the tax basis (acquisition cost) of the loan rights surrendered and the higher of (1) the market value of the rights surrendered and (2) the nominal value of the shares received in exchange (plus any share premium). In practical terms, though, if the non-resident entity is entitled to the benefits of a double tax treaty in force between its jurisdiction of residence and Spain, such gain is not likely to be taxable in Spain.

The repurchase of plain vanilla debt should not give rise to any Spanish stamp duty. Stamp duty is levied on transactions documented in a public deed (*escritura notarial*) reflecting “valuable acts” that may be

recorded in a Spanish public registry (such as the property or the moveable property registry). To the extent that the repurchased debt is not guaranteed by any in rem security (such as a real estate mortgage), such transaction should not include any act capable of being recorded before a public registry, and hence no stamp duty should be triggered.

Conclusion

Companies should carefully consider the issues discussed in this Client Alert before launching a debt repurchase program. Whether a company is considering repurchasing its own bonds or loans or those of an affiliate, there are a number of important issues to take into account, and advance planning and proper structuring will help to avoid unexpected consequences and enhance the execution of a repurchase.

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Endnotes

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- ¹ Facility agreements typically require prepayments to be made at par and may also include the payment of certain prepayment fees.
 - ² For example, Rule 10b5-1 trading plans may provide additional protection for open-market purchases taking place over an extended period of time, although in the authors' experience entrance into such plans for purchases of debt securities is not common practice.
 - ³ For access to the public register of relevant instruments tradeable on a market in the EU maintained by the European Securities and Markets Authority as of the date of this Client Alert, see: https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_firds#. For the UK equivalent, see: <https://data.fca.org.uk#/viewdata>.
 - ⁴ A special sub-class of the pre-commencement disclosure issues may arise depending on what the issuer's plans may be with respect to the balance of the bonds that remain outstanding. This Client Alert assumes that the opportunistic acquisition of bonds at favorable prices is the only objective being pursued. However, some companies may consider implementing an open market bond repurchase program as a first stage in an integrated plan to retire the entire issue — for example, by launching a tender offer (presumably at a higher price) for the bonds not purchased on the open market or in privately negotiated transactions. Similarly, a company may contemplate repurchasing bonds more cheaply immediately prior to exercising optional redemption rights at a fixed but higher price. In either case, disclosure questions about the issuer's plans will need to be addressed.
 - ⁵ The percentage reduction in the float of any given bond issue that is material will need to be considered in light of all prevailing facts and circumstances. An issuer who purchases bonds "at the market" in small amounts over time may never be telegraphing its intention to substantially reduce the overall float to any individual seller and therefore avoid triggering any Regulation FD obligation. In general, a bondholder who sells its bonds will not be concerned about the size of the float after the sale and will therefore not have a claim under Rule 10b-5 of the US Exchange Act that it would not have sold at the agreed price had it known of the pending float reduction.
 - ⁶ Section 14(e) of the US Exchange Act and Rule 14e-1 promulgated thereunder are the primary laws governing non-convertible debt tender offers.
 - ⁷ See SEC No-Action Letter, *Abbreviated Tender on Exchange Offers for Non-Convertible Debt Securities* (Jan. 23, 2015), <https://www.sec.gov/divisions/corpin/cf-noaction/2015/abbreviated-offers-debt-securities012315-sec14.pdf>.
 - ⁸ A hiatus should be taken between bond repurchases on the open market and the launch of a conventional tender offer to avoid integrating the debt repurchase program and the subsequent tender offer as well as to avoid potential claims that the open-market repurchases were part of a "creeping" tender offer.

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- ⁹ A consent obtained in connection with a tender offer, or an “exit consent,” is distinguished on the grounds that it is given by the tendering holder prior to the consummation of the tender, and is not a consent given by the issuer (or its affiliate) as the holder of the bonds. Therefore, properly structured exit consents generally are effective to achieve a desired consent.
- ¹⁰ Closely related party includes, among others: (i) holders, directly or indirectly, of at least 5% of the insolvent debtor's share capital, if the debtor company had securities listed on a securities exchange or, otherwise, 10% or more of the insolvent debtor's share capital, provided that such shares are held on or prior to the date their respective credit right arises, companies of the insolvent company's group as well as their common partners or shareholders; and (ii) creditors that are directors or deemed as *de facto* directors (*administradores de hecho*) within the two (2) years prior to the declaration of bankruptcy of the debtor.