Spain

Jose Ramon Vizcaino Fernandez de Casadevante
joseramon.vizcaino@dentons.com

Diego Carrera Dávila
diego.carrera@dentons.com

1.0 OVERVIEW

Spanish taxes can be levied at a national (state), regional (autonomous region) or local (town hall or municipal authorities) level. Additionally, Spanish taxes can be broken down into three groups: taxes, duties and special levies. In any case, and as a general overview, duties and special levies trigger in return of a public service or benefit, such as the parking rate, garbage rate or court fee.

Spain imposes corporate and personal income tax on its residents, including permanent establishments in Spain of non-resident companies, on a worldwide basis for any type of income (e.g., interest, dividends, lease income, capital gains, etc.). Both corporate income tax (CIT) and personal income tax (PIT) are state-level taxes, although Spanish regions can regulate certain aspects of the PIT, such as rates and deductions.

Non-residents not acting through a permanent establishment can also be subject to taxation in Spain under the Non-Residents Income Tax (NRIT) Act. In general terms, a 19% / 24% withholding tax rate would apply to non-residents who obtain Spanish source dividends, interest payments, rents, royalties or management fees (among other kinds of income). The rate of withholding tax depends on the nature of the income (for instance, as a general rule, the 19% applies to interest and dividends regardless of the residence of the non-resident) and on the tax residence of the non-resident (for instance, the 19% applies to residents of the European Union (EU) or the European Economic Area (EEA), while the 24% withholding rate applies to other non-residents of the EU or the EEA). The Spanish payer of such amounts is liable for withholding this tax on behalf of the non-resident recipient before the Spanish tax authorities. However, Spain has one of the most extensive double-taxation treaty networks in the world, which reduces or eliminates the Spanish withholding tax rate on such types of income. Certain payments within the EU, such as interest, dividends and capital gains, are not subject to taxation if certain requirements are met.

From a direct taxation viewpoint there are other applicable taxes, such as local property tax and business activity tax, and others that only apply to individuals, such as the inheritance and gift tax and the wealth tax.

Regarding indirect taxation, value-added tax (VAT) and transfer tax are applicable in Spain. VAT is regulated according to the EU standards under the VAT Directive. VAT is not applicable in the Canary Islands, Ceuta or Melilla, which are not considered Spanish territories from a VAT perspective. Instead, these regions apply their specific sales taxes. Most aspects of transfer tax, including rates, deductions and formalities when filing tax returns, are determined by regional tax laws.

Stamp duties and custom duties on imports are among the other forms of indirect taxation.

Spain has signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI), but the Spanish parliament has not yet completed the ratification process.

2.0 LEGAL SYSTEM

In Spain, the autonomous regions and local territories operate under a civil law legal system established by the Spanish Constitution. Taxes are also governed by international treaties (including double-taxation treaties signed by Spain or the EU), international regulations, the Spanish General Tax Act and other applicable legislation.

3.0 TAXATION AUTHORITIES

The tax system in Spain is administered by the Agencia Estatal de Administración Tributaria (AEAT), which depends on the Spanish Treasury Ministry.

Spanish regions have been entrusted with the administration of certain taxes, along with the regulation of certain aspects (principally, rates and deductions). Municipal bodies administer certain local taxes and have the power to regulate their own municipal taxes, with certain limitations and, normally, within a framework established by state law.

4.0 BUSINESS VEHICLES

A non-resident may either establish a Spanish business vehicle to carry on business in Spain or operate directly, with or without a Spanish permanent establishment. In general, the incorporation of Spanish entities is exempt from taxation.

Additionally, it should be noted that, according to the Corporate Income Tax Act, a company is considered resident in Spain if it has been incorporated under Spanish law, if the corporate address is in Spain or if the place of effective management is in Spain. Special rules apply if the company is established in a tax haven but has assets and/or rights in Spain. Below are the main aspects of Spanish business vehicles, alongside with some introductory tax inputs.

4.1 Public limited companies

In public limited companies (in Spanish, Sociedad Anónima or S.A.), shareholder liability is generally limited to the amount the shareholder contributed to the company's equity. This contribution is represented by the shares that qualify as negotiable securities, which may be listed on the stock exchanges. The minimum capital to set up a Spanish S.A. is €60,000, which must be fully subscribed and at least 25% paid up upon incorporation.

4.2 Private limited companies

Private limited companies (in Spanish, Sociedad Limitada or S.L.) are the most common type of investment vehicle in Spain. Shareholder liability is generally limited to the investment in the company's equity. The minimum capital required to set up an S.L. is €3,000, which must be subscribed and fully paid upon incorporation. The capital is represented by units, an instrument that closely resembles the shares of an S.A, and which can also have a non-voting nature. However, units may not be listed on stock exchanges.

4.3 Partnerships

There are three main types of partnerships in Spain, which are not very common due to the unlimited liability of the members:

- General partnerships are private entities (*sociedad colectiva*) with legal personhood and unlimited joint liability
- Simple limited partnerships (*sociedad comanditaria*) have legal personhood and comprise two types of partners: general partners with unlimited liability, and limited partners whose liability is limited by their contributed amount
- Limited shareholders partnerships (*sociedad comanditaria por acciones*) have legal personhood and comprise two types of partners: general partners with unlimited liability, and limited partners whose liability is limited by their contributed amount

4.4 Foreign entities (with or without a Spanish permanent establishment)

A foreign company that carries on business in Spain, whether it acts through a permanent establishment or not, is subject to tax under the Non-Resident Income Tax (NRIT) Act in respect of such income.

If the foreign entity is resident in an EU country or in a country that has a double-taxation treaty pursuant to which the company may claim treaty benefits, the entity would generally be subject to the rules of EU legislation (for instance, an EU directive or an EU regulation) or the relevant treaty. There are special rules when the profits are earned through a permanent establishment situated in Spain. One of the most important special rules is that a foreign company would not be allowed to claim double-taxation treaty benefits if the activity is performed in Spain through a permanent establishment.

In this regard, a company that operates through a Spanish permanent establishment (such as a branch) will be subject to taxation in a very similar way as a Spanish resident entity. In a nutshell, the rules applicable under the CIT Act would apply in order to determine the NRIT liability of the permanent establishment. However, some particularities should be considered, such as the limitation on certain expenses and valuation of certain transactions.

For non-resident entities not acting through a permanent establishment, the NRIT Act imposes a withholding tax of 19% / 24% (although this rate may vary on certain type of income) on all Spanish sourced incomes paid to non-resident entities. In general terms, these withholding taxes also apply to payments made from a Spanish branch or permanent establishment to its head office. EU legislation or double-taxation treaties will relieve (or even eliminate) this withholding tax obligation.

5.0 FINANCING A COORPORATE SUBSIDIARY

5.1 Equity financing

5.1.1 Contributions for shares

Where an equity investment is made into a Spanish company in exchange for shares, the amount of the investment is added to the entity's "stated capital" account. Incorporation of entities and share capital increases are generally exempt from taxation (exempt from Spanish 1% capital duty and not subject to VAT or stamp duty). However, when assets other than cash are contributed to a Spanish company, it should be considered on a case-by-case basis, because tax could be triggered when contributing mortgaged assets to an entity.

5.1.2 Contributions without taking additional shares

Shareholders can make an equity contribution to an incorporated company without the issuance of additional shares. This is known as "other shareholder contributions," and can for instance be used to offset accounting losses.

In general terms, these contributions are not subject to taxation and do not have CIT implications, as they are not considered accounting income (relevant exceptions could apply in case of debt contribution). Distribution or return from this account should be carefully reviewed as it may have adverse tax consequences.

5.1.3 Distributions of paid-up capital

A 1% capital duty applies on capital reductions or when liquidating the company, to the extent that there is a stake to be distributed to the shareholders.

5.2 Debt financing

5.2.1 Withholding tax implications

Spanish entities can borrow funds from related or third parties. Interest payments made by a Spanish resident company to a non-resident at arm's length are generally subject to a 19% withholding tax. As previously mentioned, the withholding tax rate can be reduced or eliminated under EU legislation or a double-taxation treaty. It is a general rule that interest payments to an EU resident are exempt from withholding taxation (whether or not the lender is a third party). Particular attention should be given to anti-abuse tax provisions.

5.2.2 Thin capitalization and limitation on deductibility of interest expenses

Thin capitalization rules no longer apply in Spain, although there are some restrictions on the deductibility of interest expenses for Spanish entities. Interest deductibility is subject to compliance with transfer pricing rules and earning stripping rules (i.e., the 30% EBITDA limit).

Under earning stripping rules, net interest expenses (i.e., excess financial expenses accrued over interest income) generally are capped at 30% of EBITDA (as defined in the CIT Act). However, net interest expense is tax-deductible if it does not exceed €1 million per year (known as the minimum allowance). Net financial expenses exceeding this 30% EBITDA limit can be carried forward and deducted in the following years, subject to the same 30% EBITDA limit. Additional restrictions apply for leveraged buyouts and intra-group indebtedness.

Interest accrued on profit-participating loans granted by companies of the same group are non-deductible for CIT purposes, as they are treated as "equity (dividend) contributions," regardless of their consideration as a debt for accounting purposes. However, if the relevant requirements are met, this type of interest can benefit from the participation-exemption regime (explained below in point 6.2).

5.3 Stamp duty

Spanish stamp duty is levied on notarial deeds, certain administrative and commercial documents. For instance, when purchasing a real estate asset or granting a mortgage loan, this tax could be triggered as the transaction would be performed in a notarial deed. If the transaction is subject to capital duty or transfer tax (as opposed to VAT), no stamp duty can be levied.

The applicable tax rate depends on the autonomous regions in which the taxable event occurs. Generally, the rate varies between 0.5% and 1.5%. However, some autonomous regions have included increased rates that vary between 1% and 3% to certain transactions (mainly real estate).

6.0 CORPORATE INCOME TAX

6.1 Income tax rate

The CIT standard rate applicable to resident companies, including Spanish permanent establishments, is 25%. Special tax rates apply to certain entities, most significantly:

- A 15% tax rate applies to newly created companies during their first two fiscal years in which the taxable base is positive
- 1% is the applicable rate for investment funds
- 0% is the applicable rate for Spanish REITs (known in Spain as SOCIMIS)
- 30% is the applicable rate for bank institutions and companies belonging to the hydrocarbons industry
- 0% applicable to charitable entities, nonprofits and pension funds.

As discussed above, non-resident entities not operating in Spain through a permanent establishment would be subject to NRIT (as opposed to CIT), with the applicable rate being 19% / 24% depending on the type of rent and on the tax residence.

6.2 Capital gains

Broadly, capital gains are part of the CIT and NRIT taxable income. Under CIT, the very common "participation-exemption regime" applies to capital gains obtained from the sale of shares. This also applies to the distribution of dividends when both of the following requirements are met:

i. Minimum 5% participation in the subsidiary's (either resident or non-resident) share capital or, alternatively, the stake must have a value higher than €20 million

ii. The participation must have been held for more than one year or, failing this requirement in the distribution of dividend, the stake must be maintained for the time necessary to complete a year.

Particular rules apply when more than 70% of the subsidiary's income comes from dividends or capital gains obtained through the sale of shares in other entities. There are other instances where this participation-exemption regime does not apply, such as when the non-resident subsidiary is not taxed at a minimum nominal tax rate of 10%, or when the payment of dividends generates a deductible expense.

Generally, non-residents without the presence of a permanent establishment in Spain are subject to NRIT at a rate of 19% on capital gains on assets located in Spain, unless otherwise specified in a double-taxation treaty. Additionally, capital gains realized by non-residents as a consequence of the sale of Spanish real estate are subject to a 3% withholding tax that must be withheld by the purchaser of the real estate on the purchase price. Such withholding tax must be paid to Spanish tax authorities by the purchaser as a payment in advance of the final tax due accrued from the sale of the real estate. This withholding tax would offset the final tax due from the seller.

Capital gains realized on a transfer of shares by non-residents that do not act through a permanent establishment are exempt from NRIT, provided that the taxpayer is tax resident in an EU member state, and that the requirements of the participation-exemption regime under CIT rules apply. However, this exemption may not apply if the asset figure of the Spanish company is formed, directly or indirectly, by real estate assets.

6.3 Computation of taxable income

6.3.1 Taxable base

Taxable income is calculated as worldwide income less deductible expenses. This is obtained from the organization's financial statements, calculated under Spanish GAAP (i.e., the Commercial Code and the Spanish General Accounting Plan). The taxable base is the result of applying certain tax adjustments to the abovementioned taxable income.

Although tax losses resulting from the performance of the company's business activity can be carried forward indefinitely with no time limitation, tax losses from previous years can only be offset against up to 70% of the taxable base. This limitation is more stringent to entities with an operating income exceeding €20 million. A minimum allowance of €1 million would apply in any case.

The CIT Act establishes certain exceptions where the mentioned limitation does not apply, such as when income is recognized on debt waivers or where there are deferrals under an agreement with creditors. Finally, Spanish tax authorities can audit, without limitations, tax losses and tax deductions generated in the past 10 years, regardless of the general statute of limitations, which is normally four years.

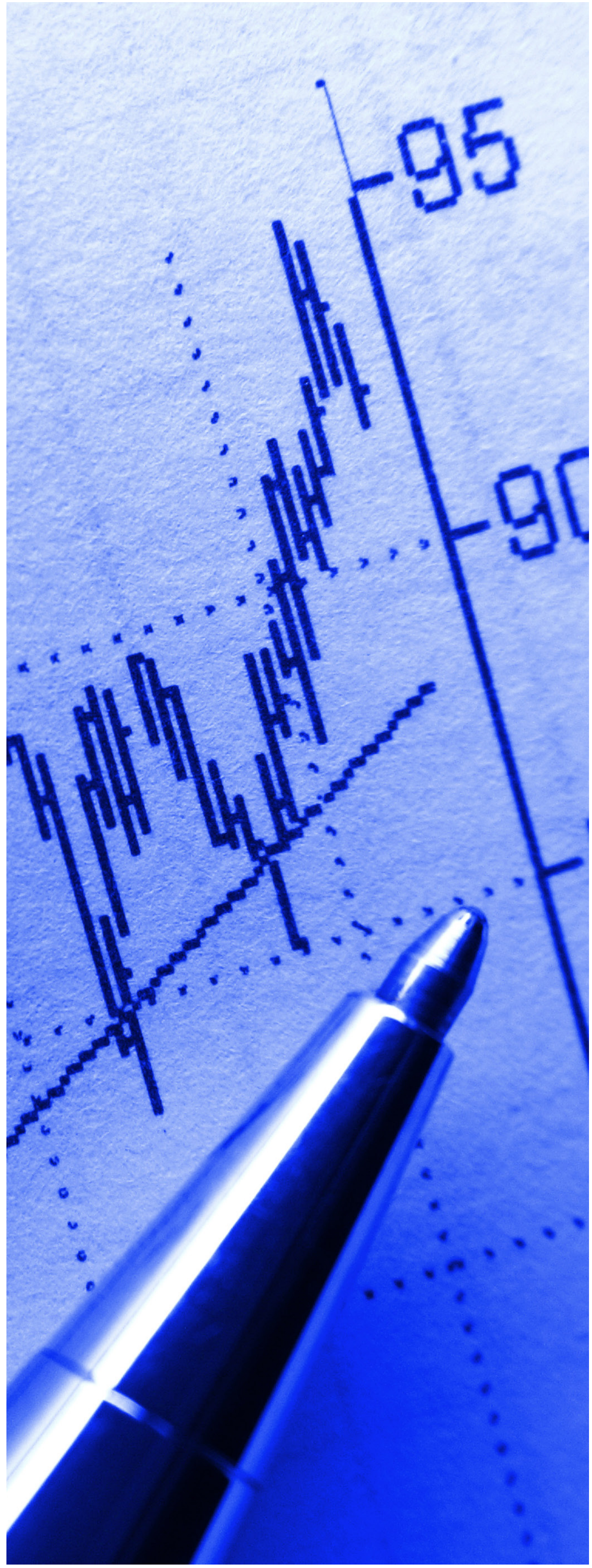
6.3.2 Deductibility of expenses

Special provisions are established for the following expenses:

- Depreciation of assets must be calculated within the limits provided in the CIT Act, unless a higher depreciation can be proven
- Impairment of assets: tangible assets, intangible assets including goodwill, real estate, participations in subsidiaries, debt instruments, etc.
- Exempt income (e.g., dividends distributed by a subsidiary in case the participation-exemption regime applies)
- Net financial expenses
- Accruals
- Non-deductible expenses (e.g., penalties, donations, etc.)
- Non-monetary transactions
- Transactions between related parties
- Change of tax residence
- Temporary allocation.

6.4 Income tax reporting

CIT due must be paid within 25 calendar days following six months after the company's tax period. During the tax year, resident companies and permanent establishments must make tax payments on account, also known as CIT prepayments of the final tax due of the ongoing tax period. Such prepayments are made in three installments with due dates of April 20, October 20 and December 20.



7.0 CROSS-BORDER PAYMENTS

7.1 Transfer pricing

Spain's transfer pricing regime generally follows the principles of the Organisation for Economic Co-operation and Development (OECD) transfer pricing guidelines. Spain provides the following possible methods to comply with the transfer pricing requirements: cost plus, resale price, profits split, transactional net margin and comparable uncontrolled price.

Spanish tax authorities can impose a transfer pricing adjustment in respect of a transaction that has not been made on arm's length terms or conditions, as required by OECD principles. If a difference arises, Spanish tax authorities will apply the tax treatment that corresponds to the real nature of such income. Spanish taxpayers are also required by law to prepare specific documentation such as local files, master files or country-by-country reports for related party transactions.

7.2 Withholding tax on passive income

Payments made by a resident of Spain to a non-resident in respect of certain types of interest payments, rents, royalties, dividends, management or administration fees are subject to tax at the rate of 19% / 24%.

However, this withholding rate may be eliminated or mitigated under applicable EU legislation and/or a double-taxation treaty signed by Spain. It would require that the recipient be the beneficial owner, the "substantial and economic business reasons" are met and that proof of tax residence from the non-resident entity is provided (through the issuance of a tax residence certificate by the relevant authorities).

7.3 Withholding tax on services fees

When a payment is made to a Spanish non-resident with reference to services performed in Spain, the payer must withhold a 24% tax rate of the payment. This rate will be 19% when the recipient of the services is resident in the EU or the EEA. However, rates may vary or services may be exempt of withholding taxation due to the application of a double-taxation treaty.

8.0 PAYROLL TAXES

8.1 Introduction to the Spanish social security system

Companies that develop activities in Spain must be registered with the General System of Social Security and must also register their employees. Social Security allowances mainly cover medical services, temporary illness, permanent and total disabilities, maternity situations, unemployment situations, retirement and death.

Employers and employees must pay a monthly contribution to Social Security, but the employer must do it on behalf of the employee. For an employee whose employment contract is for an indefinite term, the employer contributes 29.9% of the employee's wages and the employee contributes 6.35%. The employer also is required to make a contribution for professional contingencies at a rate between 0.9% and 7.15%, depending upon the nature of the employer's activities.

The maximum contribution base is capped at €3,803.70 per month. The minimum varies from €858.60 to €1,199.10, depending on the employee's job position, which would determine their contribution group.

8.2 Payroll taxes

Spanish companies and permanent establishments of foreign entities are obliged to withhold a portion of an employee's wages and pay it to Spanish tax authorities, as a payment in advance of the employee's personal income tax.

9.0 INDIRECT TAXES

9.1 Goods and service tax

Spain's VAT is a European-harmonized value-added tax imposed on the final domestic consumption of most goods, services supplied, self-supplies, intra-EU transactions and importation of goods in Spanish VAT territory (which does not include the Canary Islands, Ceuta or Melilla). Specific rules with respect to the place of supply exist to determine whether a supply is deemed to be made in Spain. For example, a special localization rule applies to real estate properties and services related to these assets.

The current standard VAT rate is 21%. A reduced rate of 10% applies to goods such as food or services as transport. Essential products or services have a special reduced rate of 4%. Some goods or services are exempt from VAT.

VAT tax reporting is generally made quarterly, although in some cases monthly tax files are required. In the latter case, the taxpayer must register in the real-time reporting VAT system (in Spanish, *Suministro Inmediato de Información* or SII System). Spanish entities that carry business in Spain are required to register, keep accounting records, issue invoices, and collect and remit VAT on such supplies.

Each taxpayer is generally entitled to a VAT refund for the expenses made with direct relation to the business operative. Conversely, no refund is allowed for VAT incurred on expenditure that is unnecessary for business purposes or related to the acquisition of goods or services used for a VAT-exempt activity. However, there are certain exemptions where VAT incurred relating to the export of goods is normally fully recoverable.

9.2 Sales tax in the Canary Islands, Ceuta and Melilla

Canary Islands sales tax has five types of rates: reduced (3%), general (7%), incremented (9.5%), special incremented (13.5%) and other special rates that vary between 20% and 35%.

Ceuta and Melilla each levy an independent tax on the sale or import of goods or services. The rate varies depending on the place of import and the type of good or service.

9.3 Transfer tax

Transfer tax is triggered on the transfer of assets or rights performed by individuals or entities but, in this case, only on those transactions out of the scope of their business. Additionally, transfer tax could also trigger in transactions subject but exempt from VAT, such as certain real estate transactions.

Where the taxpayer is the acquirer of the asset or right, the applicable tax rate varies in each autonomous region, but the general rates are:

- 6% to 11% for transfers of real estate property
- 1% to 10% for transfers of movable assets and administrative concessions
- 1% on some real estate rights.

10.0 MAIN LOCAL TAXES

10.1 Business activity tax

Business activity tax is a municipal tax levied annually on any business activity conducted within Spanish territory. The tax base will be determined on the basis of several factors, such as the type of activity, the area in which it is conducted and the cadastral value of the real estate asset. Taxpayers that begin their activity in Spain may apply for a two-year exemption on this tax if certain requirements are met.

10.2 Property tax

Property tax is a local tax levied annually on January 1. It applies to the ownership of certain rights over real estate, including the ownership of real property. The owner or the beneficiary of the right over the real estate asset is subject to property tax, which will range between 0.4% and 1.1%, depending on the municipality.

10.3 TIVUL

Transfer of urban real estate assets will be subject to a municipal tax on the increase in value of urban land (TIVUL in its Spanish acronym, also known as the *plusvalía municipal*), provided that the sale of the asset has not reported a loss. TIVUL will be payable by the seller of a urban real estate asset, based on the deemed increase in the value of the land which forms part of the property. The increase in value is calculated as a percentage applicable to the cadastral value of the land, which is an official value given to the land, and the final amount to be paid takes into account other elements such as years of ownership or the location of the property. The applicable tax rate will vary depending on the municipality where the real estate assets are located, to a maximum of 30%.

10.4 Works, constructions and installations tax (WCIT)

Refurbishment works that require a building license would trigger WCIT, the taxable base being the cost of the works, excluding certain expenses (e.g., VAT, public rates, professional fees, business profit). The applicable rate varies by municipality but it cannot exceed 4%.