
Spanish government approves bills with significant tax implications

Legal flash

November 3, 2020

The Spanish Council of Ministers has approved two bills that contain changes to Spanish tax law that may affect international investors if passed by parliament: the Anti-Tax Evasion Bill and the Budget Bill for 2021. Entry into force of these bills will depend on the parliamentary procedure that has just started.



This legal flash analyzes several measures proposed under these two bills:

- Proposed amendments to the Spanish participation exemption
- Controlled foreign corporation rules
- Exit tax provisions
- Taxation of individuals



After the Spanish parliament approved the Digital Services Tax (see our legal flash [here](#)) and the Financial Transactions Tax (see our legal flash [here](#)), over the last few days, the Spanish government has approved two tax bills that will deserve attention, if passed, as they would have a significant impact on international investors.

The Anti-Tax Evasion Bill aims to transpose the Anti-Tax Avoidance Directive (ATAD) into Spanish law, even though the rules for hybrid mismatches still have not been transposed. The Budget Bill for 2021 includes additional amendments in the context of a general increase of taxation in Spain.

The content and the entry into force of these amendments will depend on the parliamentary process that has just started.

Spanish participation exemption

- Two proposals affect the Spanish participation exemption regime in the Corporate Income Tax (CIT) Act, which would enter into force for tax periods beginning January 1, 2021.
- The first refers to the shareholding requirement. The measure proposes abolishing the possibility of complying with the requirement by having a tax basis in the shares exceeding EUR 20 million. After the approval of this measure, only 5% shareholdings would allow the participation exemption to apply. The proposal is accompanied by a grandfathering rule, so that, until tax year 2025 (inclusive), the shareholding requirement could be fulfilled with a tax basis in the shares exceeding EUR 20 million, if the shares were acquired before tax year 2021.
- The second proposal implies the reduction of the current full participation exemption to a 95% tax exemption, for shares in Spanish and in foreign entities. It would be implemented through a 5% reduction in the amount of the dividend or capital gain that is eligible for the exemption, based on that percentage corresponding to management costs relating to the holding of the shares. The same reduction would be established with respect to the credit system, but not relating to income obtained through a permanent establishment located abroad.
- The proposals do not establish any carve-outs for corporate chains or corporate groups, so the new rule could apply multiple times if a dividend is distributed through a chain of companies. It also rules out the possibility of fiscal consolidation groups avoiding the 5% reduction in the participation exemption through the elimination of the non-exempt dividend as an intra-group transaction.
- Although this amendment would affect the participation exemption applicable to Spanish holding companies (ETVE), it is not expected to change the taxation of



dividends and capital gains derived by its foreign shareholders, which would continue not to be taxable in Spain.

- On a separate note, the proposal would extend the exemption for capital gains obtained in Spain by taxpayers resident in other Member States of the European Union to taxpayers resident in Norway and Iceland (i.e., countries in the European Economic Area that have signed double tax treaties with Spain that include an exchange of information clause).
- The Anti-Tax Evasion Bill also addresses amendments to the rules governing the Spanish blacklist, which has yet to be updated.

Amendments to CFC rules

- Both the Anti-Tax Evasion Bill and the Budget Bill for tax year 2021 include amendments to CFC rules, both for personal income tax (PIT) and CIT purposes. Depending on the development of the parliamentary process, some of these measures may affect tax periods starting on January 1, 2020.
- The proposal aims to update the traditional list of passive income provided for in the Spanish CFC regime. Specifically, the list would add insurance, credit, financial leasing operations and other financial activities carried out as non-economic activities (and regardless of whether they generate deductible expenses in Spain), as well as transactions relating to goods and services carried out by related parties, to which the nonresident entity or establishment adds little or no economic value.
- As the ATAD is a minimum standard, the bill proposes abolishing the current inclusion exceptions for dividends and capital gains arising from qualified shareholdings. The inclusion of all dividends and capital gains as passive income, together with the proposed amendments to the participation exemption regime, would mean the tax implications for international corporate structures would have to be reviewed.
- The substance carve-out clause that applies only to European Union resident CFCs would be amended, to eliminate the reference to the need for sound business reasons, so the clause would only hinge on the CFC's having substance.
- Permanent establishments would be included in the scope of the CFC rules for CIT purposes.



Exit tax provisions

- Spain already provides for a general exit tax regime applicable for CIT purposes, as well as in certain cases for nonresident income tax (NRIT) purposes.
- In both cases, the bill proposes amending the current payment deferral mechanism when the transfer that triggers the exit tax occurs to a Member State of the European Union or the European Economic Area (with which there is an agreement for mutual assistance with collection). By adapting to the ATAD, this deferral mechanism would no longer consist of a postponement until the transfer of the assets to third parties, but rather a fractioning of the payment of five equal yearly installments. However, under certain circumstances, the deferral could be obtained without providing guarantees for the payment of the installments.
- The bill also proposes the update or step-up in the value of the assets (i.e., the tax value of the assets after the transfer will be the market value considered for the purposes of the exit tax in the state of origin).
- For NRIT purposes, a new case is added: in the transfer abroad of a Spanish permanent establishment's activity, the difference between the market value and the tax value of the assets of the permanent establishment. The bill does not include the transfer of assets from a Spanish head office to a permanent establishment in another country, as it considers that such a transfer does not result in Spain losing any taxing rights.
- In line with the ATAD, the exit tax would not apply to transferred assets related to the financing or delivery of guarantees or that meet prudential capital requirements or for the purposes of liquidity management, provided those assets return to Spain within one year.
- The bill does not establish any modification to the exit tax relating to the corporate restructuring regime or the capital gains accrued due to a change of residence for PIT purposes.

Taxation of individuals

- The Budget Bill for 2021 proposes an increase in PIT tax rates. General income rates (including employment income) would increase by two percentage points for taxpayers earning more than EUR 300,000 (in Catalonia, the maximum rate would be 50%, and 48% in Madrid). Tax on savings income (dividends, interest and capital gains) would also be increased to 26% for taxable income exceeding EUR 200,000.
- These increased tax rates would also affect individuals living in Spain and opting for the inpatriates regime. General income exceeding EUR 600,000 would be taxed at 47%, and savings income exceeding EUR 200,000 would be taxed at 26%.



CUATRECASAS

- Increases in tax rates would also affect maximum tax rates for wealth tax (up to 3.5% for tax bases exceeding EUR 10.6 million) in autonomous regions that have not approved their own tax rates. Nonresident taxpayers should carefully analyze how this change may affect them.

For additional information, please contact Cuatrecasas.

©2020 CUATRECASAS

All rights reserved.

This legal flash is a compilation of legal information prepared by Cuatrecasas. The information and comments included in it do not constitute legal advice.

Cuatrecasas owns the intellectual property rights over this document. Any reproduction, distribution, assignment, or any other full or partial use of this document is prohibited, unless with the consent of Cuatrecasas.

