CUATRECASAS

Finance and tax

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Corporate income tax

Central Economic and Administrative Tribunal resolution on capitalization reserve; application of amounts arising from previous tax years together with current year's amount

The Central Economic and Administrative Tribunal ("TEAC") issued a *resolution on September 22, 2021,* ruling on an appeal for nullity to unify the criteria regarding application of the reduction of the CIT taxable base relating to the capitalization reserve.

First, we highlight that, under article 25 of the Company Tax Act ("CIT Act") regarding the capitalization reserve, the reduction effectively applied in the fiscal year cannot be more than 10% of the previous CIT taxable base and must be adjusted in specific line entries. However, in those cases in which the mentioned limit applies, the taxpayer must be able to apply the excess on that limit in future fiscal years; specifically, in the tax periods ending in the two years immediately after the closing of the tax period in which the right to the reduction was generated, respecting the same 10% limit on the taxable base previous to those fiscal years.

However, regarding the application of the capitalization reserve in those two fiscal years, article 25 of the CIT Act does not indicate a criteria for allocating the applied reduction; therefore, it has been put forward whether to consider the reduction applied first to be the reduction generated during the fiscal year (LIFO criteria) or whether the taxpayer could understand that it corresponds to the reduction that was generated in previous fiscal years (FIFO criteria). The second interpretative criteria, of a general nature, is more beneficial for taxpayers.

The TEAC's resolution discusses this matter, ruling that "when applying the reduction corresponding to the capitalization reserve, if there are amounts pending application from previous periods as well as the amount generated in the current period, the taxpayers can apply them in the order they choose, as there is no statement regarding applying some amounts first and others later."

Therefore, the TEAC confirms that there is no specific order of application of the amounts pending from previous years, meaning that the CIT taxpayers could consider that when preparing their CIT self-assessments, that the amounts applied first are those corresponding to those accredited in the previous year(s) (and in order of seniority).

DGT and CNMV binding resolution relating to criteria for special system for dissolving and liquidating SICAV companies

Act 11/2021, of July 9, on measures to prevent and combat tax fraud ("Act 11/2021") approved an optional system for dissolving and liquidating certain investment companies with variable capital ("SICAV companies"). For more information, see *our legal flash* on Act 11/2021.

Since its approval, collective investment institutions ("CIIs") have submitted their interpretative and operational queries to

the Directorate-General for Taxation ("DGT"), the Spanish Securities and Exchange Commission ("CNMV") and to the commercial registry, in relation to the dissolution and liquidation processes for SICAV companies that will be agreed on in 2022.

This led to the DGT and the CNMV issuing documents with criteria for materiality, to which Cuatrecasas has had access recently. The documents are the following:

- DGT response to tax consultation of December 14, 2021 (V3112-21). The DGT confirms our criteria regarding the legal deadlines to be met when applying the SICAV dissolution and liquidation system, approved by Act 11/2021, and also confirms the possibility to arrange CII share transfers after the re-investment of the liquidation amount, with application of the deferral system due to transfers in the case of PIT paying shareholders.

- Letter of December 3, 2021, and response to consultation of December 16, 2021, issued by the CNMV's Directorate-General of Institutions. The CNMV letter establishes certain obligations for collective investment institution management companies ("SGIICs") under the new company tax system for SICAVs applicable from January 1, 2022, and the response to consultation of December 16, 2021, establishes important criteria for the special dissolution and liquidation system for SICAVs.

For more details, see our *legal flash of December 21, 2021.*

Spanish Supreme Court judgment on offsetting tax loss carryforwards

The Supreme Court has issued *judgment of November 30, 2021* on the offsetting of tax loss carryforwards and their consideration as a tax option under article 119.3 of the General Tax Act ("LGT"), criterion that the Central Economic and Administrative Tribunal ("TEAC) has followed since its resolution on April 4, 2017.

In relation to the TEAC's interpretative criteria, the tax authorities have rejected the possibility to offset tax loss carryforwards in certain scenarios.

In its recent judgment, the Supreme Court moves away from the TEAC criterion, considering that the offsetting of tax loss carryforwards cannot be classified as a tax option as established under article 119.3 of LGT, as the following essential requirements are not met:

- the existence of an alternative choice of different and exclusive tax systems, and

- an element of a volitional nature, reflecting the taxpayer's will, unequivocally expressed in a tax return or self-assessment.

Therefore, as these requirements are not met in the offsetting of tax loss carryforwards, the Supreme Court concludes that offsetting tax loss carryforwards is a free-standing right available to taxpayers, who can exercise it or not, but it is not correct to prevent, by way of interpretation, the exercising of this right through a late tax return. For more details, see our *legal flash of December 2021.*

Later, the Supreme Court issued two judgments along the same thinking on *December 2, 2021 and December 3, 2021*.

Personal income tax ("PIT")

Judgment by High Court of Justice of Catalonia on application of exemption under article 7.p) of PIT Act to directors

The High Court of Justice of Catalonia ("Catalonian TSJ") issued a judgment—issued under Cuatrecasas legal supervision—regarding the application of the exemption under article 7.p) of the Personal Income Tax Act ("PIT Act") in cases in which the taxpayer is a director.

The Catalonian TSJ's judgment resolves the appeal filed against the judgment of the Catalonian tax appeal board which, following the traditional criteria upheld by the DGT and the CNMV, rejected application of the mentioned exemption to the remuneration received by a director, understanding that the exemption is only applicable to income earned from an employment relationship.

The Catalonian TSJ moves away from the Catalonian tax appeal board's interpretation, expressly referring to Supreme Court case law, and resolved that the application of the exemption must not be limited to earnings earned under the protection of an employment relationship, and that an analysis must be performed in individual cases of the duties carried out by the taxpayer for the non-resident entity, meaning that if the work carried out by the taxpayer is beneficial to the non-resident entity, the exemption under article 7.p) of the PIT Act would apply.

Lastly, there currently is a cassation appeal with the Supreme Court (number *3468/2020*) pending decision as to whether directors are entitled to apply this exemption.

Judgment of National High Court on application of exemption under 7.e) of PIT Act to compensation received by senior manager in unfair dismissal

The National High Court issued a *judgment on October 21, 2021* on the application of the exemption under article 7e) of the PIT Act to the compensation received by a senior manager in an unfair dismissal.

The National High Court concludes that the reasoning of the Supreme Court in its judgment of *November 5, 2019*, in which it concludes that the exemption does apply to compensation received due to the termination of a senior manager's contract due to the business owner's denial to pay the minimum compensation, under the regulation of senior management staff, of seven days per year worked with a limit of six months pay, is transferable to the compensation paid to senior managers in the case of unfair dismissals.

Therefore, the National High Court admits the application of the exemption to the obligatory minimum amount (if there is no agreement) of 20 days' salary in cash for one year of service and up to a maximum of 12 monthly payments, as established in article 11.Two of Royal Decree 1382/1985, regulating the special employment relationship of senior management.

Wealth tax

DGT's binding resolutions on calculating indirect participation to apply family business exemption

The DGT has issued two binding resolutions with reference numbers *V2945-21* and *V2374-21* in which it rules on the possible calculation of the participation that the taxpayer can own indirectly (through the participation in other interposed entities) for the purposes of applying the exemption under article 4.Eight.Two of the Wealth Tax Act ("IP Act"), commonly known as the family business exemption.

The DGT resolved that, in relation to the requirement of the taxpayer's minimum participation in the entity's capital of 5% (calculated individually) or 20% (calculated collectively), only the taxpayer's direct participation in the entity to which the wealth tax exemption is applied must be considered.

Therefore, the participation percentage that a payer of wealth tax could have in the capital of an entity (X) through the participation in another entity (Y) [as the latter is the holder of a participation in the company (X)] must not be considered when calculating the minimum percentage required to apply the exemption to the shares that the wealth tax payer has in the entity (X).

Other new developments

Constitutional Court judgment declaring unconstitutionality of articles determining method for calculating tax on increase in value of urban property

The Constitutional Court has declared, in its *judgment of October 26*, the unconstitutionality and nullity of the articles of the consolidated text of the Spanish Act on Local Tax Authorities ("TRLHL") establishing the method for calculating the tax on the increase in the value of urban property ("IIVTNU"), resolving question of unconstitutionality number 4433-2020, submitted by the High Court of Justice of Andalusia (Málaga seat).

The judgment declares the second paragraph of article 107.1, and articles 107.2.a) and 107.4 of the TRLHL to be unconstitutional and void because it considers that the current objective and compulsory method for determining the taxable base is far removed from the reality of the real estate market and the economic crisis. Therefore, as it is outside the economic capacity imposed by the tax and proved by the taxpayer, it is contrary to the principle of economic capacity.

The judgment, issued on October 26, 2021, limits the effects to cases appealed from the date it was issued. However, we highlight that the judgment was not published in the Official Gazette of the Spanish State until November 25, 2021.

The Constitutional Court states that *"any tax obligations accruing as a result of this tax that, on the date this judgment is issued, have*

been finally resolved through a judgment which has the force of res judicata or through a final administrative decision will not be considered situations that can be reviewed on the basis of this judgment. For these purposes alone, the following will also be considered consolidated situations: (i) provisional and definitive settlements that have not been challenged before the date of the judgment, and (ii) self-assessments the adjustment of which have not been requested under article 120.3 of the General Tax Act before that date."

Therefore, despite declaring that the method to calculate this tax is unconstitutional and void, the court clarifies that the effects of the judgment will only apply to cases appealed from the date it was issued. The limitation of the judgment's temporary effects is controversial; however, we must highlight that this limitation on bringing a challenge only affects the grounds for opposing tax returns based on this new judgment.

For further details, see our *Finance and Tax Legal Flash of November 2021*.

Royal Decree-Law 26/2021, introducing amendments regarding regulation of tax on increase in value of urban property

The Council of Ministers has approved *Royal Decree-Law 26/2021*, of November 8, adapting the consolidated text of the Spanish Local Revenue Service Regulation Act, approved by Spanish Royal Legislative Decree 2/2004, of March 5, to the recent case law of the Constitutional Court in relation to the tax on the increase in the value of urban property ("RDL 26/2021").

RDL 26/2021 introduces amendments in the regulation of IIVTNU to find a way to fill the legal vacuum arising from the recent Constitutional Court judgment of October 26, 2021, mentioned earlier, and through which the unconstitutionality of the previous regulation regarding calculating the taxable base is declared.

Firstly, RDL 26/2021 establishes a new case of non subjection to cases in which there is no increase in the value of urban property. Immediately after, it regulates a kind of optional system for calculating the taxable base (incorporating a direct calculation system of the taxable base, which is applied at the request of the taxpayer instead of the traditional objective method for determining the taxable base) with the purpose of meeting the Constitutional Court's mandates in its last sentence. RDL 26/2021 also approves the maximum coefficients that city councils can approve, applicable depending on the period generating the increase in value, to determine the taxable base by the objective method. While the corresponding tax ordinances are not adapted by the municipalities, approving the corresponding coefficients, the maximum coefficients under RDL 26/2021 would apply directly.

We also highlight that the amendments approved under RDL 26/2021 will come into force on November 10, 2021.

For further details, see our *Finance and Tax Legal Flash of November 2021.*

Tax measures approved for 2022

The *General State Budget Act for 2022* introduces significant tax measures

affecting corporate income tax and personal income tax in Spain.

Regarding corporate income tax, the budget act approves the establishing of a minimum tax liability net of all credits and allowances applicable to all taxpayers, for the tax years started from January 1, 2022. Specifically, the budget act states that the minimum tax liability net of all credits and allowances cannot be lower than the result of applying 15% to the taxable base, increased or reduced, as applicable, by the adjustments to the equalization reserve.

Regarding personal income tax, the budget act approves amendments in the tax and financial system governing individual and company contributions to social welfare systems, which will enter into force in 2022.

For further details, see our *Finance and Tax Legal Flash of December 2021.*

Amendments introduced under Royal Decree-Law 29/2021

Royal Decree-Law 29/2021 ("RDL 29/2021"), which was published on December 21 adopts urgent measures in the *energy sector to promote electric mobility,* self-consumption and the deployment of renewable energies.

In relation to the tax measures, and with the aim of promoting and increasing the number of charging stations for electric vehicles, the possibility for municipal ordinances to approve the following tax incentives has been introduced:

- an allowance of up to 50% on property tax for properties where charging stations have been installed for electric vehicles;
- an allowance of up to 50% on business activity tax for those paying the municipal rate and where charging stations have been installed in the establishments used for the activity, and lastly;
- an allowance of up to 90% on tax on construction, installations and works, for the works required to install charging points for electric vehicles.

Various tax measures are also introduced to combat the upward trend of electricity costs, extending the temporary validity of certain tax measures already approved, including the reduction of the tax rate from 5.11269632% to 0.5% of special electricity tax and the temporary suspension of tax on the production value of electricity.

For further details, see our *Finance and Tax Legal Flash of December 2021.*

Lastly, RDL 29/2021 has extended the validity until June 30, 2022, of various temporary measures introduced to incentivize the supply of certain health care material. In particular, RDL 29/2021 has extended the validity of 0% VAT to intra-Community supplies, imports and acquisitions and the 4% VAT rate applicable to surgical masks.

For further details, see our *Finance and Tax Legal Flash of December 2021.*

Amendments introduced under Royal Decree-Law 27/2021

Royal Decree-Law 27/2021, of November 23, extends certain economic measures to support business recovery ("RDL 27/2021"). It amends article 13 of Spanish Act 3/2020 of September 18, on procedural and organizational measures to tackle the impact of COVID19 in the area of administration of justice.

Article 13 of Spanish Act 3/2020, specified that, for the purposes of the grounds for dissolution due to qualifying losses, established in 363.1. e of the consolidated text of the Spanish Companies Act, losses from 2020 could not be considered. Through the amendment approved by RDL 27/2021, this exclusion is extended to losses from 2021, with the following wording:

"Article 13. *Suspension of the grounds for dissolution due to qualifying losses.*
1. For the sole purpose of determining the concurrence of the grounds for dissolution due to qualifying losses established in article 363.1. e of the consolidated text of the Spanish Companies Act, approved by Royal Legislative Decree 1/2010 of July 2, losses from 2020 and 2021 will not be considered. If, in the results of the 2022 fiscal year, the losses reduce the equity to an amount lower than half of the share capital, the directors or any shareholder must, within two months from the closing date of the fiscal year in line with article 365 of the mentioned act, call a general meeting to dissolve the company, unless the company's capital is sufficiently reduced or increased.

2. The text in the previous section is understood without prejudice to the requirement to apply for an insolvency declaration in line with Act."

We highlight that, under article 58.4.d) of the CIT Act, entities that, at the close of the fiscal year are, according to their annual financial statements, in the equity imbalance situation described in article 363.1.e) of the consolidated text of the Spanish Capital Companies Act, cannot form part of the tax groups, unless, at the close of the fiscal year in which the annual financial statements are approved, they have overcome the equity imbalance situation.

After the amendment introduced by RDL 27/2021, the losses from 2020 and 2021 must not be considered to determine whether the company has grounds for dissolution as established in article 363.1.e) of the consolidated text of the Spanish Companies Act, in the 2020 and 2021 fiscal years, and this also affects the analysis of the companies that must be excluded from/included in the tax group.

Bill to promote startup ecosystem

The bill to promote startups (the "Bill") introduces significant changes affecting the venture capital industry, entrepreneurs and impatriates.

The Bill, aimed at fostering startups driving innovation, adopts measures to attract talent and investment in startups (tax benefits, simplification of procedures and flexibility in the application of certain rules), it promotes public support instruments and public-private partnership (e.g., innovation at universities) and it regulates regulatory sandboxes so that, during one year, startups in regulated sectors can carry out tests in an environment controlled by the

corresponding regulator.

The Bill regulates the tax treatment of the additional remuneration paid to managers of private equity and venture capital funds in compensation for their successful management (known as carried interest).

To foster startups driving innovation, it introduces tax benefits and flexibility by applying certain rules to attract talent and investment in startups (taxation of stock options, investment tax deductions and the reduced taxation of startups).

It also modifies the impatriate tax regime to attract entrepreneurs and workers residing abroad, including so-called "digital nomads."

According to the Bill, it is expected to enter into force on the day following its publication in the Official Gazette of the Spanish State, although the main tax developments would not apply until January 1, 2023.

For further details, see our *Finance and Tax Legal Flash of December 2021.*

New developments regarding tax notifications by electronic means

The tax authorities have published a *communication* informing of the migration of its notifications from the authorized electronic address to the single authorized electronic address.

As a temporary measure, and until April 4, 2022, notifications will be sent to both the authorized electronic address and the single authorized electronic address, and after that, the tax authorities will no longer send notifications to the authorized electronic address.

We highlight that in the single authorized electronic address, it is possible to see the list of public bodies registered in this notification system. To access the notifications of bodies not registered in this system, it will be necessary to access the website where those bodies publish their notifications.

For more details, see our *Finance and Tax Legal Flash of December 2021*.

Multilateral amendment of tax agreements

After the deposit with the Organisation for Economic Co-operation and Development ("OECD") at the end of September, on December 22, 2021, the instrument that will amend double tax treaties was published in the Official Gazette of the Spanish State ("BOE"). The internal procedures for its official approval were pending until this publication in the BOE.

The Multilateral Instrument is an international treaty aimed at amending double tax treaties, to introduce some of the main measures under the OECD's BEPS Plan.

The Multilateral Instrument will come into force in Spain on January 1, 2022. However, it will be necessary to analyze each double tax treat individually and exhaustively to assess the impact of these amendments, as the Multilateral Instrument could affect each one differently.

For more details, see our *Finance and Tax Legal Flash of December 2021.*

Proposals for directives on direct taxation

In October, the OECD published blueprints with details of its proposals for taxation of the digital economy (*Pillar One*) and the global minimum taxation (*Pillar Two*).

One year later, the OECD published the agreement that confirmed that these two elements would be basic elements in guiding the amendment of the tax regulations, with the aim of adapting them to the digitalization of the economy.

The developments made since then have been more noteworthy in relation to the objective of global minimum taxation and, on December 20, 2021, the OECD published a new *report* providing the details of the proposal. One rule that stands out is that the taxation of large multinational groups (annual revenue of at least €750 million) must be a minimum of 15% in each jurisdiction where they operate.

On this basis, two days later, the European Commission published its *proposal for a directive* to ensure the global minimum taxation of the groups. The highly ambitious schedule includes introduction of the directive in 2023, meaning that during 2022, we can expect intense legislative work at national and EU level.

Also on the same date, the European Commission published its *proposal for a directive* to prevent the misuse of shell entities for tax purposes.

New infringement proceedings against Spain over possible breach of EU law

In recent weeks, the European Commission sent Spain two communications expressing its queries about the compatibility of the Non-resident Income Tax Act ("NRIT Act") with the fundamental freedoms of the Treaty on the Functioning of the European Union.

The *first infringement proceedings* refer to the withholding taxes charged on gross royalty payments, without the possibility to deduct directly related expenses. The *second proceedings* refer to the impossibility for non-resident taxpayers to pay NRIT on capital gains where they are paid in instalments.

For additional information, please contact Cuatrecasas.