Tax Newsletter

Spain

GARRIGUES

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1. Judgments

1.1 Corporate income tax. – Deduction of an expense cannot be questioned due to the fact it was accrued in a statute-barred period

Supreme Court. Judgment of March 22, 2024

The corporate income tax rules require expenses to be recognized for tax purposes in the period in which they were accrued for accounting purposes (article 11 of the Corporate Income Tax Law). However, expenses recognized for accounting purposes in the income statement or in a reserves account in a later period than their accrual period are deductible in that other period, if this does not result in a lower tax liability than would have been the case had the general accrual rules been applied.

In contrast to the interpretation supported by the tax authorities over recent years, the Supreme Court held that the rules do not stipulate as an additional requirement for the right to deduct them (in these cases where the expense is recognized after its accrual) that they must be expenses relating to non-statute barred periods in the year the expense is ultimately recognized.

The Supreme Court recalled that the establishment, amendment, elimination and extension of tax credits must be regulated by law, which precludes the addition of requirements for their deduction which are not set out in the law. Therefore, if accounting rules allow an expense accrued in prior years to be recognized, even if they have become statute-barred, and the tax rules expressly allow deduction of this expense in the year it was recognized for accounting purposes, it cannot be prevented from being deducted causing impairment to the taxpayer's financial capacity by an element falling outside the rules on the tax. If the tax authorities' interpretation was followed, the expense would not be deductible either in the year in which it was accrued, due to being statute-barred, or in the year of its recognition for accounting purposes.

Additionally, the tax authorities retain their right to review (the right to deduct) the expense even if it is accrued in a statute-barred period, under the powers conferred on them by article 115 of the General Taxation Law, which states that the facts, acts, elements, activities and other circumstances determining the tax obligation may be audited.

1.2 Corporate income tax. - The Supreme Court has confirmed its jurisdiction over the right to deduct directors' compensation

Supreme Court. Judgment of March 13, 2024

In recent months, the Supreme Court has delivered various judgments confirming that directors' compensation must generally be deductible, if the expenses are properly recorded for accounting purposes and they relate to services provided (see, among others, our publication dated July 6, 2023, in relation to the first of these judgments in 2023).

In a new judgment, the court recalled this case law and summarized its position on this subject, in a case where the bylaws did not state that directors were compensated for their services. The tax auditors had found that, under the relationship absorption theory, the right

to deduct the compensation of any directors who had a senior management relationship had to be denied. The Supreme Court reached the opposite conclusion, as explained below:

a) **Payments for valuable consideration cannot be gifts,** and that therefore, nor can any directors' compensation that is paid for their services as such, which (insofar as they have not been disputed in the proceedings) must be considered real and actual; all of the above being regardless of whether the relationship absorption theory is applicable. Otherwise, the directors would be being required to provide services without compensation, which is not reasonable.

b) Failure to **comply with the corporate law rules** related to this compensation cannot affect the right to deduct a correctly recorded expense for accounting purposes, and also that, based on the explanations given, it is not a gift. The court recalled that the purpose of those corporate rules is to protect shareholders.

c) The **relationship absorption theory**, is not reflected anywhere in tax law, and therefore, in relation to real services, that theory cannot be used to reject the right to deduct the expense related to the compensation.

d) Lastly, on the issue of whether the expense falls within **expenses in breach of the law** which the Corporate Income Tax Law stipulates cannot be deducted, the court recalled that it has repeatedly held that they relate to very specific cases such as bribes and similar types.

1.3 Corporate income tax. – Sponsorship expenses for events of exceptional public interest are not deductible

Supreme Court. **Judgment of February 27, 2024**

Article 27.3.1 of Law 49/2002 of December 23, 2002 provides a tax credit to be deducted from the gross tax liability for corporate income tax purposes, equal to 15% of advertising and publicity expenses relating to events of exceptional public interest. This tax credit cannot exceed 90% of the donations made to the consortium, publicly owned entities or entities responsible for putting into practice the programs and activities related to the event. None of the incentives provided for in that law are applicable to the donations where this tax credit has been applied.

In a few cases (such as that examined in this judgment), the laws approving the program state that the 90% limit must be determined by reference to amounts paid in respect of sponsorship to the consortium or organization responsible for putting the program into practice. At issue in this judgment is the right to deduct from the corporate income tax base the sponsorship expenses that must be taken into account to determine that limit.

The Supreme Court concluded that those expenses are not deductible, because (i) the legal benefit is provided in the form of a reduction to the gross tax liability not as a reduction to the tax base; and because (ii) the law treats sponsorship expenses in the same way as donations (not deductible as an expense) for the purposes of that limit. This conclusion is not altered by the fact of the law not expressly stipulating that the sponsorship expenses included to calculate the 90% limit have to be nondeductible. According to the court, accepting that 15% of the sponsorship expenses may be deducted from the gross tax liability while also being deductible from the tax base would involve a double deduction which is not justifiable.

1.4 Personal income tax / Reserve for investments in the Canary Islands. - The assignment of properties to a community property system amounts to an economic activity for the purposes of the reserve for investment in the Canary Islands, if the co-owner participates in management

Supreme Court. Judgment of February 26, 2024

A taxpayer engaging in an economic activity as an oral medicine doctor had recorded the reserve for investment in the Canary Islands (RIC) and fulfilled the related investment obligations by purchasing properties which he assigned to a community property system to use them for business purposes. It was examined whether a personal income taxpayer may be considered to carry on a property leasing economic activity for the purposes of the reserve for investments in the Canary Islands, where that taxpayer carries on the property leasing activity through a community property system in which the taxpayer is a co-owner not performing any management tasks, and to which he contributed properties that he had purchased using the reserve.

The Supreme Court concluded that the rules do not state that the income attributed to co-owners in respect of the performance of an economic activity by their community property system is treated as income from the economic activity, whether or not they participate regularly, personally and directly in the organization for their own account of the means of production and human resources used for the activity.

However, even if the leasing is carried on as an economic activity, it is necessary, for the purposes of the reserve for investment in the Canary Islands, to fulfill the requirements laid down in relation to this activity. Namely, (i) the community property system must be a tourism company, (ii) the properties must be used to carry out the industrial activities included in parts 1 to 4 of section one of the tax on economic activities classifications, (iii) they must be located in commercial zones situated in areas where the supply of tourism services is in decline, or (iv) the leased properties must residential properties protected by the developer company.

1.5 Nonresident income tax. – The transfer of federative rights by a foreign football club amounts to a capital gain subject to nonresident income tax

Supreme Court. Judgment of March 4, 2024

At issue was whether the transfer of a player's federative rights by a non-Spanish resident club to a Spanish resident entity creates a capital gain subject to nonresident income tax.

The Supreme Court concluded that this is a transfer of rights (so-called "federative rights") which have economic content and may be exercised in Spain. Consequently, there is a capital gain subject to nonresident income tax.

1.6 VAT. - The sale of shares is not included in calculation of the proportional distribution where it is an ancillary and one-off transaction unrelated to the holding company's main economic activity

National Appellate Court. Judgment of December 26, 2023

It was examined whether, under article 104.3.4 of the VAT Law, the denominator used to calculate a holding company's proportional distribution can include the amount obtained from

the sale of shares in group companies, where, besides providing management services to its subsidiaries, it also provides financing to them.

The National Appellate Court affirmed that in this case it may be interpreted that the sale of shares amounts to an isolated transaction, unrelated to the activity involving providing management or financing services, insofar as it cannot be considered a direct, permanent and necessary extension of that main activity. Furthermore, this sale of shares does not involve a significant use of goods and services. Therefore, the amount obtained from the sale of shares must be excluded from calculation of the proportional distribution.

1.7 Inheritance and gift tax. – Liability for inheritance tax arises on the death of the decedent even if parentage is recognized after death

Supreme Court. **Judgment of February 19, 2024**

A taxpayer obtained judicial recognition as son of the decedent, who died in 2006, by a judgment confirmed in an appeal proceeding in 2009. After his parentage had been determined, the tax authorities issued an inheritance tax assessment denying the right to apply a reduction that came into force in 2008, in other words, after the decedent's death, but before his parentage had been confirmed.

The Supreme Court concluded that parentage has retroactive effects due to amounting to a natural obligation that arises from birth. Therefore, the tax falls due on the date of death of the decedent not the date on which the judgment declaring parentage became final, and therefore in the examined case that reduction cannot be applied.

1.8 Real estate tax. – The cadastral value of a property can be questioned when challenging the decision to enforce secondary liability if there are exceptional and unforeseen circumstances

Supreme Court. **Judgment of March 1, 2024**

An entity purchased a property in 2013, after the due date for real estate tax in that fiscal year (January 1). The tax authorities enforced secondary liability on the purchaser in relation to the 2013 real estate tax debt. In the purchaser's challenge of the enforcement of secondary liability, the cadastral value of the property was also challenged.

The Supreme Court concluded that the new owner can question the cadastral value (in the procedure for challenging the decision to enforce secondary liability), if exceptional and unforeseen circumstances exist that were not present when that value was notified to the previous owner. It added, however, that the fact of the cadastral value not having been notified to the new owner cannot be treated as an exceptional and unforeseen circumstance, because the tax authorities are not required to make that notification, which is why, in this specific case, the court dismissed the appeal by the person that was held liable. In any event, it recalled, this person had the necessary legal tools available to request correction of the cadastral value from the authorities (the cadaster authorities). If that request for correction is upheld, a refund application may be made for incorrectly paid amounts of the tax.

1.9 Local authority charges. – The volume of generated waste is a basic element of the charge for the waste collection, disposal or treatment service

Supreme Court. Judgment of January 19, 2024

In this judgment, relating to the local authority charge for the waste collection, disposal or treatment service (waste charge), the Supreme Court concluded that the volume of generated waste and the cost of its disposal or treatment are basic elements of the charge, and therefore the technical and economic report used as support by local councils to approve the fiscal rules governing this charge must contain those elements. This ensures that the ability-to-pay, equivalence and proportionality principles are observed in determining the cost of the administrative service and in applying the rules for charging and distributing the cost among taxpayers.

In the case examined in this judgment, the court concluded that, under the applicable legislation on the due date for the tax (fiscal year 2017), it was not required to determine the exact volume of generated waste for each activity to calculate the tax liability, it being valid for the local council to use (as it did) other principles to obtain an indirect assessment of the volume of waste.

We will have to wait for the court's interpretation in relation to future rules on the waste charge to be approved by local councils, by reference to the new requirements introduced in Law 7/2022 of April 8, 2022 on waste and contaminated land for a circular economy.

1.10 Cadastral values. – The impact value applied in determining the cadastral value of land must be determined by reference to the actual use made of the property

National Appellate Court. Judgment of February 5, 2024

Under the cadaster rules, developed or undeveloped land must be appraised using the impact value in the related official schedule of values by reference to the applicable use, defined in euros per square meter of construction. The National Appellate Court confirmed in this judgment that this impact value must be determined by reference to the actual use of the property rather than its possible use under the planning rules.

1.11 Tax on construction, installation projects and works - Enforcement procedure. – The tax authorities' right to assess the tax became statute-barred after proceedings at the economic-administrative tribunal were held up for over four years

Murcia High Court. Judgment of January 23, 2024

Following a challenge of enforcement of a judgment confirming an assessment of the tax on construction, installation projects and works, proceedings at the municipal economic-administrative tribunal were held up for over four years. For this reason, Murcia High Court confirmed that the local authority's right to assess that tax debt had become statute-barred.

1.12 Audit procedure / Entry and search. – Obtained items of proof are lawful even if the entry and search was authorized before the audit had commenced

Supreme Court. Judgment of March 1, 2024

In the case examined in this judgment, the domicile of a company had been entered and searched a few minutes ahead of notification of the commencement of an audit. The judgment challenged in a cassation appeal upheld the company's appeal, and denied the validity of items of proof obtained in that procedure, by applying the supreme court's interpretation in a judgment dated October 1, 2020 (October 2020 Newsletter). In that judgment it was concluded that an entry and search cannot be ordered before or simultaneously with commencement of the audit process.

However, further specifications were later added to this judgment by the Supreme Court itself in judgments delivered on June 9 and June 12 2023 (July - August - September 2023 Newsletter), in which the court concluded that, even if the entry and search at the domicile is authorized when the audit work has not yet commenced, the obtained items of proof may be considered lawful.

In view of this, the Supreme Court ordered in this new case a reversion of procedure, with the setting aside of the appealed judgment, to allow a judgment to be delivered again after assessing in conformity with the law the produced items of proof and evidence, without excluding those obtained in the entry and search.

1.13 Tax procedure. - Partial audits do not stop the clock on the statute of limitations for the right to apply for a refund of incorrectly paid taxes if the requested refund does not fall within the scope of the audit

Madrid High Court. Judgment of December 13, 2023

A taxpayer forgot to apply some tax credits in corporate income tax self-assessments, and therefore applied for their correction and the relevant refund of incorrectly paid taxes. The application was filed after the end of the statute of limitations. The taxpayer argued, however, that the clock had stopped ticking on the statute of limitations as a result of various partial audits made by the tax authorities.

Madrid High Court confirmed the tax authorities' interpretation after verifying that the audit processes related to a different matter from the reason for the application for a refund of incorrectly paid taxes.

2. DECISIONS

2.1 Personal income tax / Transfer and stamp tax. – The transferor of a property must be allowed to question the value audited at the purchaser

Galician Regional Economic-Administrative Tribunal. Decision of March 16, 2023

A taxpayer transferred a number of properties. The tax authorities considered that, to determine the transferor's capital gain for personal income tax purposes, the values audited

by Xunta de Galicia (the Galician autonomous community government), for the purposes of the transfer and stamp tax payable by the purchaser, should be taken as the transfer prices.

In this decision, the Galician TEAR set aside the personal income tax assessment issued on the transferor, because the transferor was not notified of the documents arising from the audit of reported values carried out on the purchaser, nor was the transferor given the opportunity to challenge the result of that audit or, if applicable, to request an expert appraisal made at the taxpayer's instance. According to the tribunal, these procedural errors reduced the transferor's defense options, and therefore, in addition to setting aside the assessment, it ordered reversion of procedure to allow those errors to be corrected. The Galician TEAR based its view on the supreme court's case law and on the indivisibility of government principle.

2.2 VAT. – Application of the effective use rule analyzed in relation to advertising services

Central Economic-Administrative Tribunal. Decision of January 25, 2024

Article 70.2 of the VAT Law provided, until January 1, 2023, that certain services, (advertising services included) were subject to VAT in the VAT area where they were supplied to traders not established in the European Community, as long as those services were used in that area ("effective use rule"). In the case examined by TEAC, the entity provided advertising services to its parent company (resident outside the European Union) and considered that those services were not subject to VAT in Spain under the general place-of-supply rules ("customer rule"). However, the tax authorities considered that they should have been subject to VAT in Spain under the effective use rule.

TEAC confirmed the tax authorities' adjustment. The tribunal recalled that, according to the Court of Justice of the European Union in a judgment delivered on February 19, 2009 in case C-1/08, supplies of advertising services must be considered to be used in the country where the advertising material is disseminated from and, in the examined case, the purpose of the advertising services was to increase product sales in the territory of application of the tax.

Lastly, TEAC added that the amendment of article 70.2 of the VAT Law introduced by General State Budget Law 31/2022, (effective from 2023) was not made to change an article in breach of the directive, but rather results from exercising the power that article 59 of the VAT Directive grants to the States.

2.3 Tax on economic activities. – A cadastral review of a property stops the clock on the statute of limitations for the right to apply for a refund of incorrectly paid tax

Catalan Regional Economic-Administrative Tribunal. Decision of January 11, 2024

Under the tax on economic activities rules, the tax liability on a property leasing activity is calculated as 0.10% of its cadastral value (which must be notified to the tax authorities by the taxable person by filing a notification of registration status).

Following a change to the cadastral value of a number of properties (in response to an application for review by an entity), an application for correction of its notifications of registration status was filed, as a means of requesting a refund of incorrectly paid tax. The tax authorities denied that application due to considering that, when it was filed, the

taxpayer's right to apply for a refund of the excess tax on economic activities paid through a correction of notifications of registration status had become statute-barred.

The tribunal upheld the claim. In its opinion, under the *actio nata* principle, the steps taken at the cadaster tolled the taxpayer's right to apply ultimately for a refund of incorrectly paid tax on economic activities. As the tribunal underlined, the taxpayer could not apply for correction of its notifications of registration status until a decision had been delivered on the cadastral value by the Cadaster, which it did.

2.4 Tax collection procedure. - The existence of prior mortgages on a property does not prevent it from securing a stay of the debt

Central Economic-Administrative Tribunal. Decision of March 14, 2024

A taxpayer provided a property with mortgage charges to secure a stay of enforcement of a tax debt. The tax authorities considered that the asset was not eligible for this purpose, because, if the mortgages were enforced the security interest provided for the public purse would disappear.

TEAC, however, used the doctrine determined in earlier decisions to conclude that the authorities' reasoning would mean voiding of content any security interests consisting of second or further mortgages on assets. In other words, the existence of prior mortgage charges does not, in and of itself, preclude the eligibility of the asset provided as security, although those charges must be taken into consideration to assess the sufficiency of the value of the property concerned.

3. LEGISLATION

3.1 Approval of the 2023 personal income tax and wealth tax return forms

Published in the Official State Gazette on March 22, 2024, Order HAC/265/2024 of March 18, 2024 approves the 2023 personal income tax and wealth tax return forms, notably adding the following elements:

a) The tax particulars and draft personal income tax return may be obtained on or after April 3, 2024.

b) The filing periods for the returns for both taxes (including confirmation of the draft personal income tax return) start on April 3 and end on July 1, 2024, inclusive.

   Payment of the debt by direct debit may only be specified until June 26, 2023 (inclusive). If only the second installment is to be paid by direct debit, this form of payment may be specified until July 1, 2024.

c) The notable new features of the personal income tax return are (i) the new format of the section relating to the "Special rules on mergers, spinoffs, share exchanges and non-monetary contributions" (information on these transactions must be provided in annex C.2 to the return, including among items the amount of the deferred gain where the neutrality regime is applied); and (ii) the new additional information section to cover the new special recognition rule applicable in relation to awards of shares granted to workers at startup companies.

3.2 Approval of information form 239 and amendment of form 234

Order HAC/266/2024 of March 18, 2024, published in the Official State Gazette on March 22, 2024, approves form 239 for “Reporting certain tax planning arrangements in the context of the Multilateral Competent Authority Agreement on the automatic exchange regarding CRS avoidance arrangements and opaque offshore structures" and determines its filing terms, conditions and procedures.

The same order also amends Order HAC/342/2021 of April 12, 2021, approving (i) form 234 for "Reporting certain cross-border tax planning arrangements", (ii) form 235 for "Reporting updates of certain marketable tax planning arrangements"; and (iii) form 236 for "Reporting the use of certain cross-border tax planning arrangements".

The main specifications for these forms are as follows:

a) **Form 239** must be used to fulfill the new obligation to submit information on certain tax planning arrangements in the context of the Multilateral Competent Authority Agreement on the automatic exchange regarding CRS avoidance arrangements and opaque offshore structures.

   The parties with reporting obligations are intermediaries or taxpayers (as defined in DAC-6) who are directly related to the design, marketing, organization, making available, implementation or use of a cross-border tax planning arrangement presenting certain hallmarks.

   This return must be filed electronically within thirty calendar days following the creation of the obligation (as defined in article 46.3 of the General Regulations on the Application of Taxes).

b) **Form 234** contains a change to Annex I to Order HAC/342/2021 to exclude the information on the identity of the intermediaries exempt from the reporting obligation due to a legal professional privilege. Additionally, the summary of the cross-border arrangement includes the duty to report any information that may help the tax authorities assess the tax risk associated with the arrangement.

This order came into force on March 23, 2024. Form 239 must be filed in relation to cross-border arrangements for which the reporting obligations arises on or after that date.

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