GARRIGUES
Commentary

Tax

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Report by the committee of experts on the reform of the Spanish tax system

On March 14, 2014, the Spanish cabinet was presented with the report by the committee of experts on the reform of the Spanish tax system. The report's stated aim is to set out a number of tax reforms that will allow for fiscal consolidation and make for a more competitive economy, bring up savings and raise employment, while keeping the tax system in line with the public debt forecasts at all times. In keeping with these objectives, it sets a general aim to shift the tax burden from direct tax and social security contributions to indirect and environmental taxes, by setting out proposals aimed at rearranging and simplifying the bases of all taxes, currently limited by numerous exemptions, reductions and tax credits.

After an executive summary and an analysis of the general context of the tax system reform, the report is divided into various chapters addressing the reform of personal income tax, nonresident income tax, corporate income tax and taxes on wealth (wealth tax, inheritance and gift tax and transfer and stamp tax), VAT and special environmental taxes. Followed by a chapter on the reform of social security contributions and lastly a description of measures to combat fraud and proposals to foster market unity and tax neutrality.

The main proposals in the field of tax are summarized below:

1. Proposed measures in relation to the various taxes in the tax system

1.1 Personal income tax

Objective: To rearrange personal income tax bases, by reducing tax relief, exemptions and nontaxable cases , while lowering tax rates to achieve an efficient, neutral tax and to promote saving. All alongside the proposed measures to combat tax fraud.

The report proposes the following measures in relation to the above:

(i) Exemptions: elimination of the exemptions established for (i) severance pay, (ii) hedging of interest rate risk on mortgage loans for the acquisition of the principal residence, and (iii) dividends and shares in income.

(ii) Salary income:

(a) Elimination of the nontaxable cases established for (i) health insurance taken out by companies for employees, their spouses and descendants, ii) share awards by the company to its employees, and (iii) loans with an interest rate below the legal rate, taken out before January 1, 1992.

The report proposes that the nontaxable provision of computer equipment to employees should only apply where the equipment is provided for use in work related to the company.

Lastly, the report recommends keeping the nontaxable training and retraining courses that are directly required for the employee's job and for civil liability insurance premiums in connection with the employee's activity or for occupational accidents.

(b) Change in the treatment of multi-year income:

- Lowering of the 40% reduction in multi-year salary income to 30% and making it not apply to the income received in split payments.
- Nonduplication of the maximum reduction in the case of stock options offered on the same conditions to all of the company's employees.
- Extension of the system applicable to stock options to all multi-year compensation treated as stock options.

(c) A single reduction for salary income (applicable to calculate net salary income) for all recipients and lower than the current one (which is between €2,652 and €4,080 annually), retaining the current reduction for unemployed persons who accept a job in another municipality (which is 100% more than that applied ordinarily). This measure is the subject of a dissenting opinion.

(d) Elimination of the special regime established for individual systematic savings plans, although they may be converted into other systems providing protection for dependence and old age.

(iii) Real estate income and imputed income:

(a) Transitional reinstatement of imputed income from the principal residence (such as that currently existing for other dwellings), albeit with limits based on the cadastral value and the tax base of the taxpayer and his or her spouse. This treatment should apply as long as the cadastral values of properties have been revised, bringing them closer to the index or market values, in order to increase real estate tax, on which an important reform is recommended to make it the core of the tax charged on real estate. At the end of the transitional period, only the income from immovable property derived from the transfer to third parties of real estate should be taxed, less deductible expenses (including the new real estate tax). This measure was not the subject of a dissenting opinion.

(b) The finance costs associated with the acquisition or improvement of the real estate should not be deductible from the income from immovable property obtained from the transfer to third parties.

(c) Real estate income and imputed income should be included in the savings component of taxable income albeit without a reduction, and taxed at a fixed rate.

(iv) Savings income: elimination of the reduction for multi-year income in the case of income included in the savings component of net taxable income subject to a single rate.

(v) In relation to income from economic activities:

(a) Eliminate the general reduction applicable to income subject to the direct assessment method, which is currently between €2,652 and €4,080.

(b) Establish a limit of €300,000 for the income qualifying for the reduction for multi-year income (already existing for multi-year salary income).

(c) Eliminate the reduction for maintaining or creating employment.

(d) Eliminate unrestricted depreciation for new property, plant and equipment.

(vi) For capital gains and losses:

(a) Eliminate the application of the indexation allowance multipliers (which adjust the acquisition value for inflation) in transfers of real estate.

(b) Eliminate the application of the abatement rates to the assets acquired before December 31, 1994.

(c) Eliminate the differentiation between short and long term changes.

(d) Eliminate the 50% exemption for gains on the transfer of real estate acquired for consideration since Royal Decree-law 8/2012 took effect and up to December 31, 2012.

(e) Permit the offset of the negative balance of gains and losses against the income from movable and immovable capital included in the savings component of taxable income

(vii) In relation to the contributions to pension plans and similar systems:

(a) Require the beneficiaries of the pension plans to receive the benefits from retirement age without any extensions (either in in the form of a lump sum or a regular income).

(b) Bring the deductions for contributions into line with European averages, but without any limits on the financial contribution.

(c) Extend that tax treatment to contributions to special bank accounts that meet the requirements of being restricted, and to assignments of pension plans and funds.

(viii) The personal and family allowances should be reviewed and updated periodically and increased for children under the age of three. Also, for a transitional period, they should continue to be discounted from the tax liability until, in the long term, they begin to be discounted (as they were years ago) from net income.

(ix) In relation to the tax rates:

(a) Reduce the lowest rate on the progressive scale, currently at 24.75%, and the highest rate which should never go above 50% and should be close to the average highest rate for monetary union countries. The number of brackets should also be reduced to four.

(b) Set a single rate for the savings component of taxable income, which rate should coincide with (or come close to) the lowest on the progressive scale.

(x) Concerning tax credits:

(a) Definitively eliminate the tax credit for investment in the taxpayer's principal residence, even if it means a long but well-defined transitional period with annual limits on tax credits depending on the tax liability; on the other hand, for this transitional period, the tax credit would be allowed even if debt is not repaid. In the same vein, the tax credit for renovation work on dwellings to improve energy efficiency, hygiene, health and environmental protection, etc. should also be eliminated.

(b) Review the reduction for fees and contributions to political parties, by making it into a tax credit similar to that for donations.

(c) Change the tax credit for salary income (€400 in general) to make it apply only to taxpayers with a very small amount of income and only in the case of salary income.

(d) Eliminate the tax credit for birth or adoption of children in 2010.

1.2 Taxation of nonresidents

Objective: To bring this tax into line with other European Union countries that have important tax advantages to attract foreign investors and retirees.

The report recommends amending the Personal Income Tax Law to establish a regime for habitually nonresident foreigners (the current inbound expatriates regime, but more flexible) with the following changes to:

(i) Apply it to people who have an employment contract or who carry on economic activities without a permanent establishment, including directors, significant shareholders, retirees and recipients of income from movable and immovable property.

(ii) Eliminate the requirement for income not to exceed €600,000 in a year and for the percentage of income generated outside Spain to be below 15% of the person's salary income (or at least set this percentage at 50% of that income).

(iii) Set a requirement for taxpayers not to have been resident in Spain in the 5 (currently 10) years preceding their relocation to Spain.

(iv) Apply the regime in the year of relocation and the following 10 (currently 5) years.

(v) Not include imputed income from immovable property in the tax base of the inbound expatriate.

(vi) Establish a tax rate equal to the lowest rate for pensions and retired public employee pensions subject to this regime.

(vii) Apply the reduction for mortis causa acquisitions of the principal residence.

1.3 Corporate income tax

Objective: To reduce the nominal rate but eliminate tax credits and other types of incentives, in order to bring the effective tax rates closer to the legal rates, facilitate investment decisions and prevent tax-driven business strategies.

The following measures are recommended:

(i) In relation to the determination of the tax base:

(a) Deduction of finance expenses: limit the deductible net finance expenses to up to €1 million, alongside a new thin capitalization rule for the excess over and above that amount.

(b) Amortization/depreciation:

- Simplification and revision of tax amortization/depreciation rates generally, by adjusting the rates to the average useful lives of the assets and extending (until this revision takes place) the restriction on amortization/depreciation to 70% of the current maximum amortization/depreciation rates.
- Setting of a reduced amortization rate for intangible fixed assets relating to goodwill and for intangible assets with indefinite useful lives, never higher than 2.5%.
- Elimination of unrestricted and accelerated amortization/depreciation, including for enterprises of a reduced size.

(c) Elimination of the ability to deduct reversible impairment losses for accounting purposes relating to property, plant and equipment, real estate investments and intangible assets with a finite useful life, until the loss actually takes place (on the disposal of the assets or their retirement due to irreversible losses, provided they are not noncurrent assets held or available for sale).

(d) Elimination of the ability to deduct impairment losses on debt securities relating to investments held until maturity, recognized under measurement bases (except in the case of losses due to retirement, disposal or cancellation of assets).

(e) Introduction of a tax treatment uniform with the personal income tax treatment for the subscription to capital increases out of reserves through which bonus shares are received.

(f) Elimination of the indexation multipliers to make adjustments for inflation in transfers of real estate.

(ii) Double taxation relief mechanisms:

(a) Change to the exemption for the avoidance of international double taxation by establishing a nonexempt minimum (of, for example, 10%) and also eliminate the requirement for the performance of business activities abroad.

(b) Conversion of the tax credit for domestic double taxation into an exemption applicable when the ownership percentage is below 5%.

(iii) Tax rates:

(a) Progressive reduction, in stages, of the standard nominal rate for the tax to 20% (with a transitional rate of 25% being applied).

(b) Reduction in the special rate for enterprises engaged in the exploration, investigation and exploitation of underground oil and gas deposits and stores down to 30% first, and then to 25%, in accordance with the reduction of the standard tax rate.

(c) Progressive increase, from 10% to 20%, in the tax rate applicable to nonexempt activities under the tax regime for not-for-profit entities.

(d) Establishment of solutions for cases where the specified tax rate reductions result in a lowering of the deferred tax assets; or a tax surplus or deficiency arises because of the reversal of deductible or taxable timing differences.

(iv) Tax credits: elimination of almost all the tax credits currently in place to induce certain activities, except for the tax credit for creating jobs for disabled workers. This would include eliminating the tax credits under programs to support events of special public interest, the R&D&i tax credits, the tax credits for investment or reinvestment of extraordinary income, etc.

(v) Special regimes:

(a) Elimination of the special regime for enterprises of a reduced size and the special regime for certain finance lease agreements.

(b) Review of the regime for foreign-securities holding entities, by raising the current threshold of €6 million for the acquisition value of a minimum ownership interest in order to consider that the requirement to apply the exemption to avoid international double taxation has been met.

1.4 Wealth taxes

Objective: To prevent the effects of wealth taxes on savings and the formation of capital in the Spanish economy, in order to achieve a more efficient and neutral tax system that does not hold back growth in production and the creation of employment.

Wealth taxes are currently formed by (i) wealth tax, (ii) inheritance and gift tax, (iii) real estate tax, and (iv) transfer and stamp tax.

The following measures are recommended (in addition to those relating to real estate tax, already mentioned):

(i) Wealth tax: formal and definitive elimination of the tax, and the appropriate statutory provisions should be put in place to prevent the autonomous communities from charging the tax either.

(ii) Inheritance and gift tax:

(a) The inheritance and gift tax should stay and a minimum tax be created for Spain as a whole.

(b) The tax charge (mortis causa or inter vivos) would consist of only three tax rates applicable according to the degree of kinship bearing no relationship to the amount or to the heirs' preexisting wealth. The report recommends that only three groups of kinship should be established, and provides, merely for illustration purposes, an approximate range of tax rates into which they could fall, as follows:

Group A: Spouse, ascendants and descendants by direct line, adopted children and adoptive parents	**Reduced rate** It could be around 4% or 5%.
Group B: Collateral relatives to the second and third degree and relatives by affinity up to the third degree	**Average rate** Between 7% and 8%
Group C: Any other person not included in the above groups	**Highest rate** Between 10% and 11%

(c) In order to keep this a progressive tax, the report proposes a single exempt amount (applicable to the tax base before applying the rate to the net tax base), set by the central government for the whole of Spain subject to the generally applicable regime (excluding Navarra and the Basque Country) and which should be in the range of €20,000 or €25,000.

(d) As for the tax reductions currently in place:

- The report proposes to eliminate:
  - The tax base reductions for family members which should be replaced by specific fixed rates on a decreasing scale the closer the relationship to the taxpayer.
  - The reduction for amounts received under life insurance policies.
  - The reduction for acquisition of the principal residence of the deceased, except for the surviving spouse.
  - The reduction for acquisition of assets forming part of the historical artistic heritage.
  - The tax base reductions applied to inter vivos acquisitions, except for those applied to disabled persons.
- The report proposes to keep:
  - The special system of reductions for disabled persons.
  - The reduction for successive asset acquisitions, to avoid excess taxation.
  - The reduction for acquisition of an individual company, of a professional business or of shares or interests in entities classed as a "family business". The value of this reduction, however, should not exceed between 50% and 70% of the net tax base, calculated before discounting the minimum exemption.

- For these purposes, a "family business" will be deemed to mean a business in which more than 50% of the ownership is in hands of family members to the first and second degree with respect to the giver or deceased.

(iii) Transfer and stamp tax

(a) Determination of the taxable events:

The committee found that a first group of problems with these taxes comes from the determination of the taxable events, by taxing legal transactions which, in a large majority of cases, do not represent true economic capacity. For that reason, the main proposals for reform of each of the three taxes forming transfer and stamp tax involve their elimination. The specific recommendations in the report are to eliminate the following:

- Capital duty.
- The ad valorem stamp tax, where the budgetary position so allows.
- The taxable event for transfer tax, consisting of "the creation of loans, security, leases and pensions", while retaining the taxable event for "administrative concessions".
- Tax on the creation of security interests.

The report also proposes phasing in the elimination of transfer tax as the rate of progress in fiscal consolidation so allows, with the aim for it to fully disappear when a structural balance has been achieved.

(b) Delimitation between VAT and transfer tax in the taxation of real estate

The committee has said that although the legislation on both taxes clearly defines which transactions are subject to one tax or the other, in practice double taxation often arises, because as both taxes are managed through self-assessments, only the tax authorities that receive the taxpayer's return have the information on the transaction.

From among the transactions that usually pose the greatest difficulties and which are often incorrectly assessed by the autonomous community tax authorities, the report highlights: (i) the waiver of the VAT exemption between traders, and (ii) cases in which the characteristics of the definition of second and subsequent supplies of buildings may include circumstances not known by the autonomous community tax authorities.

Accordingly, the committee considers that all of these problems would disappear if VAT and transfer tax were managed by the same tax authorities, for which it proposes:

- The establishment of automatic information exchange procedures between the Tax Agency and the autonomous community tax authorities, so that they can have all the available information on transactions in which it is difficult to determine which tax is chargeable. Tax inspectors should use that information automatically before issuing an assessment proposal.

- The assignment to the Arbitration Board, under article 23 of the law on autonomous community government finances (LOFCA), of the resolution of discrepancies in relation to the tax to be levied on a certain transaction. Such discrepancies should be resolved automatically, wherever the tax authorities consider that they must assess a tax already self-assessed or paid to another tax authority.

(c) Valuation of assets and rights

The committee believes that the valuation of assets is a fundamental element of this tax and many others, among other reasons because (i) to assess the tax, the assets must first have been valued, (ii) the legislation on the tax establishes that it must be based on an actual value (an apparently undefined legal concept), and (iii) in many cases, it is a reference for other concepts in the tax system.

For that reason, the committee states that:

- The reiterated principle of the Supreme Court is that "actual value" must be taken to mean the market value of the transaction performed.

- Only in wealth taxes that do not relate to an actual transaction could "actual value" be replaced by an objective aggregate set by law, provided that its uniformity is guaranteed and that the calculated value does not exceed market value.

- The verification of values must be done according to what is stated in article 57.b) and c) of the General Taxation Law relating to "values that appear on the official registers of a tax nature" and to the "average market prices", respectively.

(d) Denial of access to registers

In the tax area, the so-called denial of access to registers entails identifying that the taxes have been paid and, thus, that registration can be made on the register concerned.

The report recommends replacing the denial of access with a real-time information system between official registries, the Tax Agency and equivalent bodies, once that information system has been functioning for a sufficient period of time.

(e) Systematic improvements

Lastly, the report recommends simplifying and improving the organization of the current Revised Transfer and Stamp Tax Law given that, according to the committee's proposals, the only remaining headings will be transfer tax for inter vivos acts and the creation of rights in rem of use and enjoyment.

1.5 Value added tax

Objective: To introduce technical clarifications, increase collection (in keeping with the requirements of international institutions in order to, should the case arise, offset reductions in social security contributions or in direct tax), by reducing the application of the 10% reduced rate or restricting the application of certain exemptions and simplifying the structure of the law.

The proposals for reform of VAT legislation are not as ambitious as might be expected or in comparison to those suggested in relation to other taxes, particularly considering that many of its provisions date back to 1986 and were issued in a very different economic and business context from the current one. The proposals do not address the demands for overall reform in relation to deductions, simplification of the payment of VAT in foreign trade transactions or for modernization of the rules applicable to real estate transactions, for example, beyond isolated aspects relating to the application of exemptions.

The specific amendments proposed are as follows:

(i) Exemptions for domestic transactions

(a) Eliminate the exemption relating to public postal services and to the sale of postage stamps due to the distortion of competition that can be generated by applying it, where possible according to EU legislation, and to limit the scope of application of the exemption for games of chance, lotteries and bets.

(b) Eliminate the exemption for the services supplied by professional associations, official chambers, employers' organizations and federations of these types of institutions, and reduce (or introduce restrictions on the application of) the exemption relating to supplies of goods and services to political parties.

(c) Eliminate the requirement that the transferee must be entitled to a full deduction of input VAT in order to be able to waive the exemption on real estate transactions and eliminate the transfer tax on supplies of real estate included in transfers that are not subject to VAT because they qualify as independent economic units, by giving them the same tax treatment as for other transfers of real estate between traders.

(d) Clarify the cases in which the exemption applies to the lease of buildings or portions of buildings to be used exclusively as dwellings, in order to do away with the uncertainties generated by the wording in force at present.

(e) Where compatible with Community legislation, to treat as not subject to VAT the income from the transfer to third parties of any kind of real estate, treating it similarly to the "non subjection to VAT of the interest and dividends obtained on loans or contributions of movable capital."

The committee has not proposed the option of introducing the waiver of the exemption for financial transactions (suggested from various circles, under the authorization given in EU legislation). Due to the complexities this involves, however, the report suggests its introduction in EU legislation (asking the Spanish government to request that change) in relation to insurance transactions.

(ii) Taxable amount: simplify the conditions required to modify the taxable amount in cases of uncollectable debts, making them the same as those required in the corporate income tax legislation to be able to deduct impairment losses in these cases.

(iii) Refund to nonestablished traders: eliminate the reciprocity requirement currently laid down for the refund of input VAT in Spain for traders not established in the Community, Canary Islands, Ceuta and Melilla.

(iv) Tax management: propose the elimination of the cash-basis accounting method as soon as the liquidity and financing position of its beneficiaries has improved, thereby making the regime transitional. That is due to the complexities that have arisen for the recipients by reason of the introduction of that regime.

(v) Tax rates: reduce the goods and services taxed at the 10% reduced rate, restricting its application, for economic policy reasons, exclusively to dwellings, the tourism industry and the transportation of passengers and luggage.

The 4% "super reduced" rate should remain unchanged as regards the list of goods and services that benefit from it, in order not to alter the tax cost of the "shopping cart."

1.6 Excise and special taxes: taxes on alcohol and tobacco

Objective: To achieve the aim behind these excise and special taxes of distributing the social costs caused by the consumption of these substances, making them fall on consumers, while reducing their consumption by being considered unhealthy. Moreover, these taxes are justified under the optimal tax theory, according to which the goods for which demand is less elastic, including alcohol and tobacco because of their addictive qualities, can be taxed to a greater extent.

Thus:

(i) In relation to tax on tobacco products, it is proposed to:

(a) Periodically review the specific tax and the minimum taxation value, so as to maintain the relative weight of excise tax in the price to the consumer.

(b) Continue with the policy of bringing the taxation of tobacco products other than cigarettes into line with the taxation of cigarettes to prevent shifts in consumption.

(ii) With regard to tax on alcoholic beverages, the report suggests the need to progressively increase taxation to reach the Community average, taking into consideration the possible evolution in demand, and to periodically review the specific rates so as to maintain the relative weight of the tax in the final price. They also propose considering a very reduced tax rate on wine, as has recently been done in France.

1.7 Environmental taxation

Objective: For environmental taxes to actually fulfill their aim and, where their aims fall outside the geographical limits of each autonomous community, for them to be managed by the central government. The current landscape is characterized by the existence of a variety of environmental taxes at the different levels of government which form a set of fragmented and limited measures, without an overall tax reform having been carried out in this area that might lead to a "green tax reform."

To achieve this objective, the report proposes a sweeping amendment of the tax treatment of energy and, in particular, of the tax on oil and gas products and of the tax on coal:

(i) Tax on oil and gas products is fundamentally designed as a collection instrument, with very little environmental purpose attached to it. For that reason, the report proposes that Spain should prepare for the approval of the proposed EU energy tax reform, to make the tax a suitable instrument to encourage energy efficiency and reduce CO2 emissions, allowing the increased amount of tax revenues to be used to finance a reduction in tax on the work factor. Thus, the proposals consist of:

  (a) Dividing the tax into a levy on energy and another on CO2, according to the criteria of the EU's proposal for tax reform.

  (b) Making the rate on diesel oil equal to the rate on unleaded gas in the period deemed appropriate by the government (measure which it considers less ambitious).

  (c) Using the additional amounts of tax revenues to reduce the central government charges on the work factor.

(ii) The report highlights that the effective tax on coal is almost zero, for which reason it proposes eliminating the exemptions that prevent a more extensive application of the tax, and bringing its structure closer to that proposed for the tax on oil and gas products.

(iii) The report points to the absence of any environmental content in the electricity tax, because its tax base is determined according to the price paid for electricity consumption. For that reason, it proposes:

  (a) Replacing the current electricity tax base with the number of kilowatts/hour consumed, to encourage energy efficiency and energy saving and adapt it to the EU's proposal for energy tax reform.

  (b) Drastically limiting exemptions, which should be confined to minimal values and justified in each specific case in an explicit, transparent and exhaustive manner.

(iv) The committee considers that the tax on the value of electricity production, does not have any underlying environmental aims, but rather is designed simply as a collection instrument that ends up impacting the consumer, for which reason it proposes eliminating it, and making up for the loss in revenues (which are used to finance the electricity tariff deficit) with an increase in the electricity tax which would be collected by the central government and not by the autonomous communities.

(v) The charge on the use of inland water for electricity production is a third tax levied on electricity production and which, in the committee's opinion, bears no relation to the damage caused to public waters. Its design reveals rather that it is a tax on the revenues of hydroelectricity plants, established to finance the tariff deficit. For that reason, the committee believes it more consistent to eliminate this tax, and make up for the loss in revenue with an increase in electricity tax.

(vi) With respect to the taxes on nuclear waste, the report analyzes the tax on the production of spent nuclear fuel and radioactive waste resulting from the generation of nuclear power and the tax on the storage of spent nuclear fuel and radioactive waste at centralized facilities. Although the committee considers that the structure of these taxes may seem correct at first sight, it advises that they are in fact levied twice on the same

actual circumstances and that they do not act as a disincentive (because there are no alternatives) and therefore the report proposes a joint reform of both taxes according to the following principles:

(a) Combination of both central government taxes on nuclear waste.

(b) Express coordination of the new Andalucía tax on nuclear waste, beyond the current reference in the law on autonomous community government finances (LOFCA).

(c) Conversion of the new tax into a levy to be used to defray the cost of managing and storing waste after the tariff deficit has been covered.

(vii) In the area of transportation, the report proposes replacing the tax on motor vehicles and the special tax on certain means of transportation with a new tax on the use of motor vehicles with the following features:

(a) The tax liability will depend on the theoretical emission of carbon, and the rate of the tax may be lowered if changes are made to the vehicle that reduce emissions and vehicles for the exclusive use of disabled persons can be exempted provided that certain income thresholds are not exceeded.

(b) Given that carbon dioxide emissions are a global problem, the new tax would be regulated by the central government and its rules would be uniform throughout Spain.

(c) The tax would be managed by the local authorities, which would transfer to their respective autonomous community governments the portion of the revenues that will be established to apply generally.

(viii) Also in the area of transportation, the committee proposes establishing new charges for:

(a) The use of transportation infrastructure, so that it does not overlap with the new environmental tax on the use of motor vehicles and the increase in the tax of diesel fuel.

(b) The entry of vehicles into city centers ("congestion charges"), particularly in Madrid and Barcelona and in other cities of considerable historical/monumental value, a measure which should be accompanied by the existence of parking lots for vehicles along the access roads to the city.

(ix) With regard to central government taxes on water, the committee, following proposals made by the OECD, proposes reforming the regulation charge, the water use rate, as well as the charge for the use of public water assets and the effluents monitoring charge, with a view to ensuring that the costs of performing and maintaining works on water infrastructure are borne by the users of the infrastructure.

(x) Unlike the above-mentioned environmental taxes, the committee considers that the recent tax on fluorinated greenhouse gases is properly configured and that it could serve as a model for the design of other environmental taxes. Accordingly, it does not consider it necessary to make any proposals regarding this tax until enough experience has been gained on how it functions.

(xi) Regarding other apparently environmental taxes:

(a) The report highlights the proliferation of taxes that are supposedly environmental in nature, including most notably taxes essentially aimed at boosting revenues and with distorting effects for renewable energy sources, given that they can be inconsistent with the central governments environmental policy and may be entirely or partly lacking in environmental incentives. This is the case of wind charges and of taxes on water in reservoirs. Consequently, the committee proposes abolishing them, given that they lack any environmental purpose and reasons, notwithstanding their replacement with other taxes that have a suitable environmental purpose.

(b) There are other taxes with an apparent or secondary environmental aim, such as taxes on large retail outlets and taxes on carbon dioxide emissions. With regard to taxes on large retail outlets, they are deemed to distort, from an economic perspective, market unity and they unjustifiably protect certain distribution channels, so the report proposes eliminating them. The same proposal is made in relation to autonomous community taxes on carbon dioxide emissions, since they are not a suitable tool for efficiently resolving global environmental problems and they pose difficult problems for coordinating with emission permit systems.

(c) The report analyzes a third group of taxes which are considered authentically environmental but which are unsuitable because of the patchwork of legislation governing them. Among these are the taxes on air emissions other than CO2, the effluents charges and the taxes on waste. These taxes should be extended to the entire national territory, with minimally harmonized regulations which respect the particularities of each autonomous community, by creating central government environmental taxes that are completely devolved to the autonomous communities. Conversely, the report does not consider it appropriate to extend taxes on single-use plastic bags to the entire country due to their doubtful environmental benefit.

1.8 Taxes on financial activities and insurance

Objective: To encourage saving and promote tax neutrality, so as to keep the financial system from weakening, savings from being offshored, credit from being reduced and the economic recovery from slowing down.

(i) With regard to the tax on financial institution deposits, it is proposed:

(a) To definitively and generally abolish these taxes and the equivalent autonomous community taxes.

(b) Alternatively, to avoid pernicious economic effects that would adversely affect the Spanish economy as a whole, convert it into a central government controlled tax that cannot be delegated to the autonomous communities.

(c) Lastly, if the government were of the opinion that the financial system bears a disproportionately low tax burden, to convey this opinion to the European Commission and use the tax coordination mechanisms existing in the euro area to move toward a common tax on financial activity.

(ii) As for the tax on insurance premiums:

(a) To make the proper references to other laws as far as the exemption for life insurance and the chargeable event of the tax are concerned, specifying that, in the case of payments made through insurance brokers, the chargeable event will occur at the moment that the insurer becomes aware that the payment has taken place.

(b) To specify:

- The taxability of transactions performed by agents and brokers, since the performance of these transactions gives rise to the receipt of amounts by the insurer as prepayments of the premiums for future insurance contracts.
- The legal definition of the tax base, supplementing it with a list of various cases which, according to the courts and the administrative rulings, form part of that base.
- The interpretation adopted by the Directorate-General of Taxes regarding the rectification of the tax charged.

2. Reform of social security contributions

The report proposes a root-and-branch reform of social security contributions to integrate them into the general tax system. To this end, it proposes a conversion of the current system of contributions based on rates according to occupational category into an authentic payroll tax, with a reduction in the level of the tax rates, so that overall revenue is equivalent to the current revenue. It also proposes:

(i) Establishing a new distribution of the resulting burden between employers and workers.

(ii) Entrusting the management of the new system to an authority functioning in tandem with the tax authorities and with common returns and procedures.

(iii) Improving the "contributive nature" of the social security benefits system, by directly linking the amount of the contributions over employees' working lives with pensions and other benefits.

(iv) Restricting exemptions from or reductions in social security contributions.

Once this conversion of social security contributions has been carried out, it is also proposed to reduce social security contributions and funding the reduction with VAT increases on top of those described above for this tax in order to eliminate the currently existing bias regarding the relative weight of social security contributions compared with the European average.

3. Specific measures to combat tax fraud

In addition to the measures proposed generally for each of the taxes indicated, the report suggests specific measures to combat tax fraud, some of which are related to taxes already discussed. Thus, the report suggests:

3.1 General measures

(i) Establishment of policies aimed at raising social awareness of the need to pay taxes to the public treasury.

(ii) Reduction in tax rates and the highly progressive nature of the taxes to reduce the marginal utility of the evaded taxes.

(iii) Reduction in the indirect costs of taxes and simplification of the tax system (e.g., by facilitating and simplifying the return filing process).

(iv) Increase and improvement in human and material resources of the tax authorities and establishment of instruments that will make it possible to process information in a mass and coordinated manner (e.g., information from different taxes).

(v) Change in tax monitoring techniques (to make monitoring more dynamic, to target it at discovering tax evasion and bring it closer to the date of the return or the occurrence of the taxable event).

(vi) Establishment of an appropriate table of penalties with deterrent effects, more flexible in its application, which does not only absorb the benefit derived from the tax fraud but also makes it more costly.

(vii) Establishment of a system of "tax rewards" to encourage taxpayers to demand an invoice for transactions (in the areas of personal domestic services, the performance of construction work and the provision of services in the sphere of the home and family).

3.2 Specific measures in the area of personal income tax

(i) Monitoring of a taxpayer's assets by using mass databases on real estate, vehicles, movable capital and financial transactions and annual notification to the taxpayer of the data appearing in these databases in the taxpayer's draft personal income tax return.

(ii) Elimination of the objective assessment regime and significant reduction in the direct simplified assessment method (establishing highly simplified accounting procedures in it).

(iii) Reduction of limits below which there is no obligation to report where salary income is obtained and elimination of these limits in the case of other sources of income.

3.3 Specific measures concerning VAT

(i) Introduction of restrictions on the parties that can apply the simplified scheme by reducing the quantitative limits that allow it to be applied.

(ii) Elimination of the special compensatory charge scheme in retail trade.

(iii) Enhancement of cross-checking of transactions using the taxpayer identification number of suppliers and customers (in particular in the case of repairs or payments to professionals).

(iv) More effective supervision by the tax authorities of intra-Community transactions.

(v) Request to the European Commission to introduce such changes as it sees fit to replace the transitional scheme currently applicable to intra-Community transactions and to establish a definitive scheme based on taxation at destination.

4. Decentralized taxation, market unity and tax neutrality

Lastly, from the standpoint of market unity and tax neutrality, the committee proposes a raft of measures, some of which have already been mentioned but which are repeated to contribute to these objectives (in the opinion of the committee):

(i) The grant of greater legislative powers to the autonomous communities to establish copayment systems for public services, within certain minimum limits established by the central government.

(ii) The establishment of measures to safeguard the principles of tax neutrality and market unity, including the following:

(a) In the case of personal income tax:

- To keep in place the power of the autonomous communities to establish autonomous community rates, although setting maximum marginal rates that cannot be exceeded in any autonomous communities (considering the central government and autonomous community rates as a whole).

- To keep in place the central government powers with respect to rules on determining the taxable amount, the rates and the tax liability for the savings component, which should be standard throughout Spain.

(b) To avoid the devolution of powers to the autonomous communities regarding harmonized indirect taxation –centralizing the legislative powers for these taxes, however, within the Tax and Financial Policy Council.

(c) To regionalize the taxes on spirits, tobacco and insurance premiums –considering, however, the possibility of the existence of tax arbitration between the autonomous communities.

(d) To perform an in-depth review of the environmental taxes and their elimination in certain cases.

(e) To eliminate the wealth tax.

(f) To establish certain maximum and minimum levels of taxation under the inheritance and gift tax applicable in all autonomous communities.

(g) To generally encourage taxes that are levied on real estate ownership to grant legislative powers to the territorial authorities.

(h) To keep in place a significant degree of centralized tax management, closely evaluating the functions hitherto performed by the High Council for Tax Management and Coordination.

(i) To broaden prior coordination with respect to the autonomous communities to establish their own taxes, establishing a system for evaluating in advance – within the Tax and Financial Policy Council – whether the new taxes proposed are already levied by the central government, whether they affect the free movement of persons, goods, services or capital and whether they hinder transactions.

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