GARRIGUES
Commentary

TAX REFORM
Preliminary bills to overhaul a range of tax concepts

Index

1. Personal Income Tax **4**

1.1 Severance pay 5

1.2 Tax residence 5

1.3 Itemization of income 5

1.4 Timing of recognition 6

1.5 Salary income 6

1.6 Income from immovable capital 7

1.7 Income from movable capital 8

1.8 Income from economic activities 9

1.9 Capital gains and losses 10

1.10 Inclusion and offset of income 11

1.11 Contributions to pension plans and similar systems 12

1.12 Personal and family allowances 12

1.13 Rates of the tax 12

1.14 Tax credits 13

1.15 International fiscal transparency 14

1.16 Special inbound expatriates regime 14

1.17 Capital gains due to change of residence 15

1.18 Tax return threshold 16

1.19 Withholding taxes 16

1.20 Reporting requirements 17

2. Corporate Income Tax **17**

2.1 The new Corporate Income Tax Law 17

2.2 Measures introduced for the 2014 and 2015 tax periods 24

3. Nonresident Income Tax **28**

3.1 Exemptions 28

3.2 Tax base 28

3.3 Tax rates 29

3.4 Other proposed amendments 29

4. Value Added Tax and Canary Islands General Indirect Tax 30

4.1 Territoriality (VAT) 30

4.2 Cases of non-taxability (VAT and Canary Islands general indirect tax) 30

4.3 Definition of supply of goods (VAT and Canary Islands general indirect tax) 30

4.4 Exit from suspensive areas or arrangements (VAT) 31

4.5 Exemptions in internal transactions (VAT) 31

4.6 Waiver of exemptions in real estate transactions (VAT) 31

4.7 Exemptions in foreign commerce transactions (VAT) 32

4.8 Place of supply of transactions (VAT and Canary Islands general indirect tax) 32

4.9 Chargeability (VAT) 32

4.10 Taxable amount (VAT and Canary Islands general indirect tax) 33

4.11 Modification of the taxable amount (VAT and Canary Islands general indirect tax) 33

4.12 New cases of reversal of the liability (VAT) 33

4.13 Tax rate applicable to medical equipment and medicinal substances (VAT) 33

4.14 Deductions (VAT and Canary Islands general indirect tax) 34

4.15 Refunds to traders not established in the EU (VAT) 34

4.16 Assessment of tax on imports (VAT) 34

4.17 Assessment of Canary Islands general indirect tax 35

4.18 Special simplified schemes and schemes for agriculture, livestock and fisheries (VAT and Canary Islands general indirect tax) 35

4.19 Special scheme for travel agencies (VAT and Canary Islands general indirect tax) 35

4.20 Special VAT grouping scheme (perimeter) (VAT and Canary Islands general indirect tax) 36

4.21 New types of infringements (VAT and Canary Islands general indirect tax) 36

4.22 Liability of the titleholder of a tax warehouse other than a customs warehouse (VAT) 37

5. Excise and special taxes 37

5.1 Electricity tax 37

5.2 Tax on fluorinated greenhouse gases 37

5.3 Other issues 37

6. General Taxation Law and other procedural provisions 38

6.1 General tax legislation 38

6.2 New provisions on the procedures for economic-administrative claims 41

6.3 Amendments resulting from the new provisions on the criminal offense against the public treasury 42

6.4 Other amendments 45

2014
June

TAX REFORM

Measures submitted for public consultation

The ministry clarifies that the new Corporate Income Tax Law will come into force on 2015

On June 20, 2014, the Cabinet of Ministers approved four preliminary bills which propose a root-and-branch reform of several taxes.

Specifically, (i) the Preliminary Bill amending Personal Income Tax Law 35/2006, of November 28, 2006, the revised Nonresident Income Tax Law, approved by Legislative Royal Decree 5/2004, of March 5, 2004, and other tax provisions (**preliminary bill amending personal income tax and nonresident income tax**); (ii) the **Preliminary Bill for the Corporate Income Tax Law**; (iii) the Preliminary Bill amending Value Added Tax Law 37/1992, of December 28, 1992; Law 20/1991, of June 7, 1991, amending the tax aspects of the Canary Islands Economic and Tax Regime; Excise and Special Taxes Law 38/1992, of December 28, 1992; and Law 16/2013, of October 29, 2013, establishing certain measures concerning environmental taxation and adopting other tax and financial measures (**preliminary bill amending VAT, the Canary Islands general indirect tax, and excise and special taxes**); and, lastly, (iv) the Preliminary Bill partially amending General Taxation Law 58/2003 (**preliminary bill amending the General Taxation Law**).

The Preliminary Bill for the Corporate Income Tax Law regulates a new law that would repeal the currently in force Legislative Royal Decree 4/2004 which approved the revised Corporate Income Tax Law; whereas for the other taxes affected by the reform and to which the other three preliminary bills refer, the reform simply incorporates the amendments into the current legal texts that apply in each case.

As noted, these are preliminary bills, so they are subject to public consultation periods and, subsequently, to the relevant passage through parliament, where it is foreseeable that changes will be introduced into the current texts, which will have to be taken with the necessary caveats. However, there are already several proposed amendments that are affected by what is known as the "announcement effect", meaning that, if the reforms in question are finally approved, they will take effect in relation to taxable events that predate their entry into force. In addition, with respect to corporate income tax, although the preliminary bill indicates January 1, 2016 as the date of entry into force of the new law, it also provides for certain measures that are set to already take effect for years commencing on or after January 1, 2014 and 2015.

Following is a summary of the main reforms proposed.

1. Personal Income Tax

The preamble to the preliminary bill amending personal income tax and nonresident income tax states that, in the area of personal income tax, it seeks (i) to generally reduce the tax burden, a reduction which is particularly significant for lower-income recipients of salary income or income from economic activities and for those who bear greater family-related costs, (ii) to expand the threshold for liability to this tax, (iii) to boost long-term savings and (iv) to eliminate tax reliefs for other taxpayers.

The main measures included in the preliminary bill are the following, which, as a general rule, are set to enter into force on January 1, 2015, save for certain exceptions which we will point out in their related sections:

1.1 *Severance pay*

(i) The exemption for severance pay is restricted to €2,000 per year worked, which is computed to determine the amount of the mandatory severance pay.

This restriction will apply (i) to severance for dismissals or terminations that take place on of after June 20, 2014; however, where (ii) terminations arise from a collective layoff procedure, the restriction will apply to those which were not approved or notified to the labor authority before that date.

This change, which is the subject of much discussion in the media, would enter into force if approved on the proposed terms, on the day following that on which the law is published in the Official State Gazette.

(ii) As will be discussed below, the treatment of multi-year salary income is changed so that the reduction (which goes from 40% to 30%) for income that is generated over more than two years and is not periodic or recurring will only apply if the income is received in a single tax period.

As regards this change, and specifically for severance pay, the preliminary bill provides for a transitional regime whereby split severance payments arising from terminations of employment contracts or contracts for services that took place before June 20, 2014 still qualify for this reduction (subject to certain requirements). This transitional regime will also apply to dismissals that take place after that date where they result from an approved collective layoff procedure or a collective dismissal notified to the labor authority before that date.

1.2 *Tax residence*

The article that regulates the requirements for treating a taxpayer as tax resident in Spain is amended to establish that when determining the period of the taxpayer's stay in Spain of 183 days in the calendar year, temporary stays in Spain that result from obligations acquired under cultural or humanitarian cooperation agreements, for no consideration, with the Spanish public authorities should not be computed.

1.3 *Itemization of income*

The preliminary bill establishes that income from capital and capital gains and losses will be considered obtained by the taxpayers who own the assets, property or rights from which they arise according to the rules on legal ownership applicable in each case (and based on the evidence produced by the taxpayers or the evidence discovered by the tax authorities). Where appropriate, the rules on the legal ownership of assets and rights contained in the provisions regulating the matrimonial economic regime and in the provisions of the civil legislation applicable to asset dealings between family members will apply. Currently, the rules on the itemization of income refer to Wealth Tax Law 19/1991.

In cases where the ownership of the assets or rights is not duly evidenced, the tax authorities may consider that the owner is the person who appears as such on a tax or other public register.

1.4 *Timing of recognition*

(i) The timing of recognition of capital gains resulting from the obtainment of any public subsidy is postponed to the moment of collection.

(ii) In addition, certain circumstances are established whereby capital losses arising from past-due and uncollected claims may be recognized in the tax period in which any of these circumstances are present.

Specifically, (i) where a debt reduction established in a court-approved refinancing agreement or an out-of-court settlement becomes effective; or (ii) where, the debtor being technically insolvent, the arrangement establishing a debt reduction in the amount of the claim (in which case the loss will be computed at the amount of the reduction) becomes effective or where, otherwise, the insolvency proceeding concludes without the claim having been paid unless a court orders the conclusion of the insolvency proceeding on certain grounds provided for in the Insolvency Law; or, lastly, (iii) where one year elapses since the start of a court proceeding other than an insolvency proceeding that is aimed at enforcing the claim without it having been paid (this circumstance will only be taken into account where the one-year period ends after January 1, 2015).

Where the claim is collected after the capital loss is computed, a capital gain will be recognized at the amount collected in the tax period in which the collection takes place.

1.5 *Salary income*

(i) Attribution for tax purposes of insurance contracts that cover both retirement and death or disability contingencies

It will be mandatory to attribute for tax purposes the portion of the premiums paid that relate to the sum at risk due to death or disability. For these purposes, "sum at risk" means the difference between the sum insured for death or disability and the mathematical provision.

(ii) Compensation in kind

(a) The case of non-taxability established for awards of shares by a company to its workers is eliminated.

(b) As regards compensation consisting of the right to use vehicles, the valuation is reduced by up to 30% for vehicles considered energy efficient. The specific rules in this regard will be established by regulations.

(c) As regards the valuation of income arising from the use of a dwelling owned by the payer, the preliminary bill specifies that the percentage of 5% will apply in the case of properties located in municipalities where cadastral values have been reviewed and have entered into force in the tax period or in the period of the preceding ten tax periods.

(iii) Multi-year income

(a) The 40% reduction for multi-year income is pushed down to 30%.

(b) This reduction will only apply to income that is recognized in a single tax period. The current legislation only imposes this requirement on income obtained in a notably multi-year manner over time but not on income generated over more than two years and obtained in a manner that is not periodic or recurring.

(c) In addition, the reduction will not apply to income that is generated over more than two years where, in the period of the five tax periods preceding the tax period in which it becomes claimable, the taxpayer obtained other income generated over more than two years to which the reduction was applied.

(d) The preliminary bill eliminates the references to the specific limits applicable to cases where the income arises from stock options exercised by workers but it keeps in place the general limits of €300,000 and the specific limits for severance pay for the termination of employment contracts or contracts for services.

(e) A transitional regime is established for salary income that arises from stock options exercised by workers. Where the stock options were granted before January 1, 2015 and they were exercised more than two years after they were granted, if, in addition, they were not granted annually, the reduction can be applied even if in the period of the five tax periods preceding that in which they are exercised, the taxpayer obtained other income generated over more than two years to which the reduction was applied.

(iv) Deductible expenses

The preliminary bill includes a new case of deductible expenses in respect of "other expenses" in the amount of €2,000 per year, which will be increased in certain cases: e.g., where a change of residence takes place in cases where a job is accepted in another municipality or in the case of serving employees with a disability.

(v) Reduction for salary income

The general reduction for obtaining salary income now only applies to net salary income below €14,450 per year provided that the taxpayer does not obtain income, excluding exempt income, other than the salary income above €6,500. A scale is established whereby the further the income falls below €14,450, the larger the reduction is.

Taxpayers who would have been entitled to apply the reduction in 2014 because they accepted a job in another municipality, as worded until December 31, 2014, and continue to perform their job in 2015 tax, can apply the reduction in 2015 as worded until December 31, 2014.

1.6 Income from immovable capital

(i) The reduction applicable to leases of properties used as the principal residence falls from 60% to 50%. The increased 100% reduction is also eliminated.

(ii) The reduction for multi-year income goes from 40% to 30% and the income in question must be recognized in a single tax period and the reduction for multi-year income is restricted, as the amount of the net income to which the reduction is applied cannot exceed the amount of €300,000 per year.

The preliminary bill establishes a transitional regime similar to the one described for severance pay in relation to income that was being received in installments before January 1, 2015.

1.7 Income from movable capital

(i) Minimum exemption for dividends

The exemption of €1,500 is eliminated for dividends and shares in income.

(ii) Reduction for multi-year income

The reduction goes from 40% to 30% and the income in question must be recognized in a single tax period. The reduction is restricted, as the amount of the net income to which the reduction is applied cannot exceed the amount of €300,000 per year.

The preliminary bill establishes the same transitional regime for the reduction for multi-year income as the one described for severance pay in relation to income that was being received in installments before January 1, 2015.

(iii) Long-Term Saving Plan

The preliminary bill creates a new instrument whereby an exemption is established for income generated by amounts deposited in an individual long-term savings account or instrumented in a long-term individual life insurance policy. The contributions cannot exceed €5,000 per year during a period of at least 5 years (taxpayers not being able to have more than one long-term saving plan simultaneously) and provided that the taxpayer does not withdraw the capital resulting from the long-term saving plan before 5 years have elapsed since it was opened.

The institution through which these plans are channeled must guarantee to taxpayer that they will receive at least 85% of the amounts contributed to the plan.

(iv) Income from movable capital generated over more than two years

The preliminary bill eliminates the tax offset regime for the receipt of income from movable capital generated over more than two years for taxpayers with financial instruments acquired before January 20, 2006.

(v) Other changes

(a) In cases of the distribution of additional paid-in capital relating to securities not admitted to trading, the proceeds obtained or the normal market value of the assets or rights received will be considered income from movable capital up to the limit of the positive difference between the value of the equity of the shares for the last fiscal year closed before the date of distribution of the additional paid-in capital, and its acquisition cost. The amount by which they exceed this limit reduces the acquisition cost of the shares.

(b) In deferred capital insurance contracts, if the contract combines the contingency of survival with those of death or disability and the capital received relates to the survival contingency, the income will be determined not only by the difference between the capital received and the premiums paid, but also the portion of the premiums paid that relate to the capital at risk due to death or disability that has been used up to date will be deducted, provided that during the entire term of the contract the capital at risk is equal to or less than 4% of the mathematical provision.

(c) The loss from movable capital arising from an inter vivos transfer for no consideration of assets representing the raising and use of external capital will not be computed.

(d) The transitional regime for life insurance contracts that generate capital gains or losses prior to January 1, 1999 is eliminated.

(e) Income arising from the payment for the contingency of disability covered by an insurance policy, where it is received by the mortgagee of the taxpayers as the beneficiary of the insurance policy, with the obligation to repay the taxpayer's mortgage debt in whole or in part, will receive the same tax treatment that would have applied had the taxpayer been the beneficiary. In no case will this income be subject to withholding tax.

1.8 Income from economic activities

(i) The preliminary bill includes within the definition of income from economic activities, that which is obtained by the taxpayer from an entity in whose capital he has a stake and deriving from the pursuit of the activities included in Section Two of the Tariffs of the tax on economic activities (professional activities) where (i) the taxpayer is included, for such purpose, in the special social security regime for self-employed workers or (ii) in a welfare mutual insurance society that acts as an alternative to that special regime.

(ii) For the purposes of considering that property leasing is done as an economic activity, the preliminary bill eliminates the requirement of having premises used exclusively for managing the activity, although it keeps in place the requirement of having a person employed under a full-time employment contract.

(iii) The net revenues figure in the immediately preceding year for the overall activities is reduced from €600,000 to €500,000 for the purposes of applying the simplified form of the direct assessment method.

(iv) The deductibility of amounts paid pursuant to insurance contracts, arranged with welfare mutual insurance societies by professionals not included in the social security regime for self-employed workers is limited to 50% of the maximum contribution for nonoccupational contingencies which is established in each fiscal year.

(v) In relation to the simplified direct assessment method, the preliminary bill limits the amount that is determined for the aggregate of deductible provisions and hard to justify expenses to a ceiling of €2,000 per year.

(vi) Starting in 2016, new requirements are introduced for applying the objective assessment method, both quantitative (by reducing objective limits) and qualitative (by reducing the activities that qualify for the method).

(vii) For the activity of transportation by taxi (code 721.2 of section one of the tax on economic activities) which applies the objective assessment method, the preliminary bill introduces a reduction, according to certain specific rules, in the capital gains that arise on transfers of intangible fixed assets where the transfer is caused by a permanent disability, retirement or cessation of activity due to restructuring of the sector.

It will also apply where, for different reasons, the intangible assets are transferred to relatives up to the second degree.

(viii) As regards the reduction for multi-year income, the preliminary bill sets a ceiling of €300,000 to which the reduction can be applied and pushes percentage of the reduction down from 40% to 30%, in addition to requiring that the income be received in a single tax period.

The preliminary bill establishes the same transitional regime for the reduction for multi-year income as the one described for severance pay in relation to income that was being received in installments before January 1, 2015.

(ix) A reduction of €2,000 is established for net income from economic activities. This reduction is increased if certain circumstances prevail and if certain requirements are met.

If the requirements laid down in the legislation are not met, the taxpayers with non-exempt income below €12,000, including income from the economic activity itself, may reduce their net income from economic activities by certain amounts, determined by reference to the non-exempt income.

1.9 Capital gains and losses

(i) The preliminary bill specifies that where a legal requirement or a court decision triggers monetary compensation or assets are awarded upon the dissolution of the separate property matrimonial economic regime, there will be no capital gain or loss.

The preliminary bill eliminates the reference to the rule that this case cannot trigger the revaluation of the assets and rights awarded and adds the rule that the compensation will not give the right to reduce the payer’s taxable income and will not constitute income for the recipient.

(ii) The preliminary bill declares as exempt the gain obtained, if any, where the taxpayer’s principal residence is given in payment to discharge debts secured by a mortgage incurred with credit institutions or the like and those which arise on the transfer of the residence under a judicial or notarial mortgage foreclosure proceeding, all the foregoing provided that the owner does not have other assets or rights to pay the debt and avoid the disposal of the residence.

In addition, an exemption from the tax on increase in urban land value is included for this case in the Local Finances Law.

(iii) In the case of capital reductions aimed at returning contributions that do not originate from retained earnings relating to securities not admitted to trading, the proceeds obtained or the market value of the assets or rights received will be considered income from movable capital up to the limit of the positive difference between the equity of the shares for the last year-end before the reduction and their acquisition cost (reducing the equity by the income distributed before the reduction originating from reserves

included in that equity). Any excess over and above this limit will reduce the acquisition cost of the shares.

(iv) The application of index-linked adjustment coefficients (which adjust for inflation by updating the acquisition cost) in property transfers is eliminated.

(v) The application of abatement coefficients to assets acquired before December 31, 1994 is also eliminated.

(vi) The proceeds from the transfer of subscription rights originating from securities admitted to trading are classified as a capital gain in the tax period in which the transfer takes place. It thus brings the applicable treatment into line with the case of shares not admitted to trading on any secondary market.

To determine the acquisition cost of these securities, the proceeds obtained from transfers of subscription rights performed before January 1, 2015 will be deducted, with the exception of the proceeds from such rights that would have been taxed as a capital gain.

Where all of the subscription rights have not been transferred, it will be understood that the rights transferred related to the securities acquired first.

1.10 Inclusion and offset of income

(i) As regards income from movable capital that does not form part of the savings income (linked to financing for related entities), the percentage holding to be considered (to calculate the excess of own capital transferred to a related entity over the result of multiplying the equity by 3, in the portion that relates to the taxpayer's holding) will be 25% in cases where relatedness is not defined according to the shareholder-entity or member-entity relationship.

(ii) The differentiation between short- and long-term capital gains/losses (on transfers) is eliminated and, accordingly, all of them will be considered savings income.

(iii) The offset limit on the negative balance that results from offsetting *inter se* gains and losses in the general component of the taxable income (those not derived from transfers) against the positive balance from income and attributions of income is increased from 10% to 25%.

(iv) Taxpayers will be able to offset the negative result of including and offsetting *inter se* losses from movable capital against the positive balance from the inclusion of the capital gains/loss from the savings component of the taxable income, up to 25% of such gains/loss (and vice versa).

The offset percentages will be 10%, 15% and 20% in the 2015, 2016 and 2017 tax periods, respectively.

(v) The preliminary bill sets out the following transitional regime for losses and negative balances originating from prior years which consists of the following:

(a) Capital losses included in the savings income originating from fiscal years 2011, 2012, 2013 and 2014 that are pending offset will continue to be offset against the balance of capital gains and losses that are included in the savings component of

taxable income according to the new wording (those arising on asset transfers, regardless of their generation period).

(b) Capital losses included in the general income originating from fiscal years 2011, 2012, 2013 and 2014 that are pending offset will be offset against the balance of capital gains and losses that are included in the general component of taxable income according to the new wording (those which do not arise from asset transfers) and, if there is any remainder, against the positive balance from the income and attributions that are included in the general component up to the limit of 25% of such positive balance.

(c) Notwithstanding the terms in the preceding letter, capital losses included in the general income originating from fiscal years 2013 and 2014 that are pending offset because they arise from asset transfers whose generation period, therefore, is equal to or less than one year, will be offset against the balance of capital gains and losses that are included in the savings component of taxable income according to the new wording (those arising on asset transfers, regardless of their generation period).

(d) Negative balances resulting from including and offsetting *inter se* the income from movable capital that is included in the savings income originating from fiscal years 2011, 2012, 2013 and 2014 that are pending offset will continue to be offset according to the legislation in force as of December 31, 2014, that is, against the positive balance from the income from movable capital that is included in the savings income.

1.11 Contributions to pension plans and similar systems

The amount of contributions to be made is reduced from €10,000 to €8,000 and the contributions made in favor of a spouse who does not obtain net income from a salary or from economic activities or obtains them in an amount below €8,000 per year is increased from €2,000 to €2,500.

In addition, for the purposes of determining the overall ceiling for applying these reductions, the increased percentage of 50% of net income from a salary and from economic activities and the amount of €12,500 (formerly provided for taxpayers over the age of 50, is eliminated).

1.12 Personal and family allowances

The preliminary bill increases the taxpayer’s allowances and the allowances for descendants and ascendants, as well as the allowance for the disability of the taxpayer and the allowance for the disability of ascendants and descendants and the allowance applicable to those who pay spousal and ascendant/descendant support by court decision (who are not entitled to apply the allowance for descendants).

1.13 Rates of the tax

(i) The portion of the general component of net taxable income that exceeds the personal and family allowance will be taxed according to central government tax scale the marginal rates of which range between 9.50%, for net taxable income up to €12,450, and 22.5% for income from €60,000 and above.

In 2015, however, the scale ranges from 10% to 23.5%.

Although the final taxation will depend on the relevant autonomous community scale, the withholding tax scale included in the preliminary bill carries a marginal rate between 19% and 45% (in 2015, between 20% and 47%).

(ii) The portion of the savings component of net taxable income that exceeds the amount of the personal and family allowance will be taxed according to the following scale (central government and autonomous community):

Savings component of net taxable income - Up to €	Rate in 2015	Rate in 2016
Up to 6,000	20%	19%
From 6,000 to 50,000	22%	21%
50,000 and above	24%	23%

1.14 Tax credits

(i) Tax credit for investments: Taxpayers who engage in economic activities and meet the requirements established to apply the special regime for enterprises of a reduced size may take a credit of 5% of the net income from economic activities of the tax period in which it is invested, in the same tax period or in the following tax period, in property, plant and equipment or investment property used in economic activities pursued by the taxpayer.

(ii) Tax credit for donations: The preliminary bill eliminates the 10% tax credit for amounts donated to foundations and associations declared to be of public benefit that have not availed themselves of Law 49/2002, on the tax regime for nonprofit entities and tax incentives for patronage.

With respect to the tax credits provided for in Law 49/2002, which can be taken by individuals who make donations to entities availing themselves of that Law, (i) the tax credit rate is improved, pushed up to 30% (transitionally for 2015, 27.5%) and (ii) donor loyalty is encouraged by an increase in the tax credits (as explained below in the section on corporate income tax).

(iii) Tax credits for contributions to political parties: The preliminary bill eliminates the reduction for dues and contributions to political parties and replaces it with a new tax credit of 20% of membership dues and contributions to political parties, federations, coalitions or voting groups, up to a maximum base of €600 per year.

(iv) Tax credit for income obtained in Ceuta and Melilla: To be able to take the tax credit for income originating from companies that effectively and physically operate in Ceuta and Melilla, such income must be income to which the tax reduction established in the corporate income tax legislation applies in certain cases.

(v) The business start-up savings account and the tax credit for the obtainment of salary income and income from economic activities are eliminated.

(vi) The amount of the shares acquired with the balance of business start-up savings accounts will not form part of the base of the tax credit for investment in newly or recently created companies where that balance has already been credited.

(vii) The tax credit for the rental of the principal residence is eliminated, although it is kept in place transitionally for taxpayers who have entered into a lease agreement before January 1, 2015, in respect of which they have paid, before this date, amounts for the rental of their principal residence, and provided that the taxpayer was entitled to the tax credit in relation to the amounts paid for the rental of such residence in a tax period accrued before January 1, 2015.

(viii) The preliminary bill creates tax credits for large families or persons with disabilities under the care of the taxpayer for taxpayers who engage in an activity as employees or self-employed workers, for which they are registered with the relevant social security regime or mutual insurance society, subject to certain limits. Taxpayers can apply to the State Tax Agency to be paid the tax credits in advance.

1.15 International fiscal transparency

(i) Taxpayers will attribute any gains on the licensing or transfer of assets or rights, or from the provision of services, where the nonresident company does not have the relevant organization of human and material resources to carry them out. Material and human resources existing at another nonresident entity from the same group will be admitted.

(ii) If the provisions of the above paragraph do not apply, the taxpayer will only attribute gains from the currently envisaged sources (ownership of real estate not used in economic activities, share in equity of entities and transfer of own capital to third parties, financial/credit, insurance and service providing activities). The preliminary bill adds (i) capital redemption and insurance operations that have legal entities as a beneficiary; (ii) intellectual and industrial property, technical assistance, movable property or image rights (unless the special attribution regime for the latter applies); and (iii) financial derivative instruments.

(iii) The possibility of electing to include the attribution in the tax period in which the financial statements are approved is eliminated.

(iv) Included among the information to be submitted together with the return are the place of the tax domicile and the notes to the financial statements of the nonresident entity.

(v) The presumption established for tax havens is extended to no-tax countries or territories.

(vi) The attribution regime will not apply where the entity not resident in Spain is resident in another EU member state provided that the taxpayer evidences that its formation and operations are based on valid economic reasons and that it engages in economic activities.

1.16 Special inbound expatriates regime

(i) Professional sportspersons subject to Royal Decree 1006/1985 are excluded from the regime.

(ii) The regime is extended to relocations to Spain as a result of becoming a director of an entity in whose capital the taxpayer does not have a stake or, otherwise, where the stake does not given rise to related-entity status.

(iii) The requirements that the work actually be performed in Spain, that the work be performed for a company or entity resident in Spain and that the salary income not be exempt from nonresident income tax are eliminated.

(iv) The quantitative requirement that the expected compensation not exceed €600,000 per year is eliminated.

(v) The tax debt will be determined according to the rules laid down in the revised Nonresident Income Tax Law for income obtained other than through a permanent establishment, subject to several special rules:

(a) The exemptions established in the nonresident income tax legislation will not apply.

(b) All of the taxpayer's salary income will be deemed obtained in Spain.

(c) The income obtained during the calendar year will be taxed cumulatively, with no possibility of offset *inter se*.

(d) The dividends, interest and capital gains on asset transfers will be taxed separately from other income, according to the scale already noted for savings income: 19%, 21% and 23%. On a transitional basis in 2015, however, the rates will be 20%, 22% and 24%.

(e) The other income will be taxed according to the following scale:

Net taxable income	Rate in 2015	Rate from 2016
Up to €600,000	24%	24%
€600,000.01 and above	47%	45%

(f) The withholding tax rate for salary income will be 24%. However, where compensation paid by the same payer during the calendar year exceeds €600,000, the withholding rate applicable to any excess will be 45% (47% in 2015).

Taxpayers who have been relocated to Spain before January 1, 2015 may elect to apply the regime in force as of December 31, 2014.

1.17 Capital gains due to change of residence

Where the taxpayer loses his status due to a change of residence, the positive differences between the market value of the shares of any type of entity or of collective investment vehicles that are owned by the taxpayer, and their acquisition cost, will be considered capital gains, provided that the taxpayer has had such status for at least five of the ten tax periods preceding the last tax period for which a personal income tax return must be filed, and a number of requirements are met in relation to (i) the market value of the shares, or (ii) the percentage holding.

Capital gains will form part of the savings income and will be attributed to the last tax period for which a personal income tax return must be filed. If necessary, a supplementary return will be filed, with no penalty, late-payment interest or surcharge whatsoever.

Specific rules are laid down for determining the capital gain.

In any event, where the change of residence occurs as a result of a temporary relocation for work reasons to a country or territory that is not considered a tax haven, following a request from the taxpayer, the payment of the tax debt relating to these capital gains will be deferred by the tax authorities, subject to certain rules regulated in the regime itself.

Where the change of residence is to another member state of the EU or the European Economic Area with which there is an effective exchange of tax information, the taxpayer may elect to apply certain special rules to the capital gains.

This regime will also apply where the change of residence is to a country or territory considered a tax haven and the taxpayer does not forfeit his status as resident in accordance with article 8.2 of the Personal Income Tax Law, also subject to certain special rules.

1.18 Tax return threshold

The threshold below which a tax return need not be filed in certain cases is pushed up from €11,200 to €12,000.

1.19 Withholding taxes

(i) It is clarified that the taxpayer can deduct the amount that should have been withheld where it was not withheld or it was withheld at an amount lower than it should have been for a reason attributable exclusively to the withholding agent.

(ii) In transfers of preemptive subscription rights of shares or units in collective investment vehicles, the custodian entity and, in the absence thereof, the financial intermediary or the public authenticating official who has attested the transfer will be required to withhold the tax.

(iii) The preliminary bill introduces a scale of withholdings for salary income, split into five brackets with rates between 19% and 45%. In the case of delays, the withholding rate is set at 15%.

(iv) The withholding rate for directors and members of the board of directors (35%, 37% in 2015) is lowered to 19% (20% in 2015) where the income originates from entities with net revenues below €100,000.

(v) The withholding rate established for income from professional activities (19%, 20% in 2015) is reduced to 15% where the volume of gross income is less than €12,000 per year.

(vi) The withholding rate for capital gains arising from transfers of preemptive subscription rights is set at 19% (20% in 2015).

1.20 Reporting requirements

Reporting requirements are added or expanded in relation to:

- Entities that market long-term saving plan contracts.
- Autonomous communities, with respect to persons who fulfill the condition of large family and to information on the degree of disability of disabled persons.
- Taxpayers who own protected assets regulated in Law 41/2003, of November 18, 2003.

2. Corporate Income Tax

As indicated, the preliminary bill amending the corporate income tax law regulates a new law that amends many aspects of the corporate income tax law currently in force (Legislative Royal Decree 4/2004). It is expected to enter into force for years commencing after January 1, 2016. Nonetheless, this preliminary bill contains many other provisions which are to take effect in 2015 and certain others which are even to apply as soon as 2014. We describe them separately below.

2.1 The new Corporate Income Tax Law

We list below the main new features of the preliminary bill amending the corporate income tax law, with a reminder that it still has to be processed through parliament prior to its final approval and is not expected to enter into force until 2016.

2.1.1 Tax base

(i) Definition of economic activity:

The law includes a definition of economic activity and requires, specifically for the activity consisting of the lease of real estate, that such activity be pursued by at least one employee working under a full-time employment contract, determined by having regard to all entities belonging to the same group of companies (as group is defined in article 42 of the Commercial Code).

(ii) Time limit for the deduction of intra-group losses:

Losses incurred on intra-group transfers of shares, property, plant and equipment, investment property, intangible assets and debt securities cannot be deducted.

Losses will be deductible in the period in which the foregoing items are transferred to third parties outside the group. In the case of the transfer of shares or of permanent establishments, losses will be reduced by the amount of the gain obtained on the transfer to third parties, unless at least 10% has effectively been taxed.

(iii) Time limit for the deduction of impairment losses on assets

Impairment losses produced by the decline in value of property, plant and equipment, investment property and intangible assets, including goodwill, equity instruments and debt securities (fixed income) will not be deductible. They will be deductible upon the transfer or de-recognition of these assets.

This decline in value is deemed to be covered over time by depreciation/amortization (a table for property, plant and equipment is included in the articles) and systematic depreciation/amortization (the deduction of the price of intangible assets of indefinite useful life and of goodwill is permitted with a maximum annual limit of 5%).

As an exception, allowances for impairment losses on receivables and other assets derived from doubtful debts, as well as those relating to employee welfare systems which have generated deferred tax assets, will be deductible with certain conditions and limits.

Lastly, the deductibility of impairment losses on receivables is maintained, with limits similar to the current limits, as is that of inventory depreciation.

(iv) Deductibility of finance costs

The non-deductibility of the return on equity will apply to all equity treated as such from a commercial standpoint (e.g., non-voting shares or redeemable shares), regardless of its accounting treatment. Included in this category are participating loans granted by entities in the same group of companies (as group is defined in article 42 of the Commercial Code).

The "30% rule" existing in the current legislation in connection with the deductibility of finance costs is maintained on similar terms (requiring, in order for dividends received to be computed as "operating income", a minimum investment of €50 million, rather than the €6 million currently required, where the holding owned is less than 5%).

Nonetheless, a restriction is included in cases of the acquisition of holdings in other entities if, thereafter, the acquired entity is included in the tax group of the acquirer or is submitted to restructuring, with a view to preventing the acquired activity from supporting the finance cost incurred on its acquisition.

(v) Other deductible expenses

(a) A maximum limit is established for the deduction of expenses incurred on customer or supplier entertainment, equal to 1% of the net amount of the net revenues of the tax period in question.

(b) It expressly states that directors' remuneration for the discharge of functions other than those relating to their office as director will be deductible, regardless of whether they are working under an employment contract or a contract for services. This would appear to resolve a matter often questioned under current legislation.

(c) The deductibility of expenses with related companies which, as a result of a *different* tax classification, do not generate income or generate exempt income or income subject to a tax rate of less than 10% (hybrid transactions), is rejected.

(vi) Related-party transactions:

On one hand, the preliminary bill restricts, in general, the rules determining the requirements to be related parties, although it recovers the case of a "de facto" relationship, i.e., a case in which one entity has decision-making power over another, independent of the other rules determining the requirements to be related parties.

On the other hand, it simplifies the documentation rules for entities or groups of entities with net revenues of less than €45 million.

With respect to pricing methods for related-party transactions, a hierarchy of methods is no longer included, but rather any pricing method and technique that is in line with the arm's length principle is admitted on a subsidiary basis.

The estimated income from transactions with permanent establishments located abroad is specifically regulated, although all of this will be subject to the provisions of the applicable tax treaty, if any.

The effects of advance pricing arrangements (APAs) can be extended to transactions from previous tax periods, provided that they have not become statute-barred.

With respect to the secondary adjustment, the preliminary bill does not include the presumed reclassification of the pricing difference in cases in which the relationship is defined in terms of the shareholder-company relationship (share in profits or contribution to equity), but does include the possibility for the adjustment not to be made where the pricing difference is recognized.

Lastly, reference is made to the nontransferable nature of the pricing arrived at according to the transfer pricing rules, i.e., it will be considered only for corporate income tax, personal income tax and nonresident income tax purposes.

(vii) Exemption for the avoidance of double taxation (domestic and international)

One of the most notable of the new features is the unification of the treatment of dividends and capital gains from holdings in companies resident and not resident in Spain.

The general lines of the regime currently applicable to income from holdings owned abroad (exemption regime) will be extended to entities resident in Spain. In order to qualify for the exemption, the holding must be equal to at least 5% or, alternatively, must have a value exceeding €50 million, and the investee must have been charged for a tax identical or analogous to Spanish corporate income tax at a nominal rate of at least 10%.

It should be noted that the preliminary bill does not include the presumption of taxation where there is an applicable tax treaty, as until now, or, as a general rule, require that the investee's income come from a business activity pursued abroad.

In connection with income generated by permanent establishments, the preliminary bill maintains the criteria according to which losses incurred by the permanent establishment are not included in the tax base until its transfer or until the discontinuation of its activity, and expressly regulates the possibility of operating in a single country through differentiated permanent establishments, in which case each permanent establishment will apply the exemption or tax credit regime separately.

(viii) Reduction of income from intangible assets ("Patent Box")

The preliminary bill stipulates a specific treatment for income from the licensing of certain intangible assets, known as the "patent box" on terms similar to those regulated in the current Corporate Income Tax Law.

(ix) Savings banks' community welfare projects

The preliminary bill makes it possible to deduct for tax purposes maintenance expenses of community welfare projects where, pursuant to accounting rules, such expenses are recorded with a charge to the income statement.

(x) Capitalization reserve

As a "replacement" for the traditional reinvestment tax credit, the preliminary bill includes this concept as an incentive for the reinvestment and capitalization of companies.

Taxpayers subject to the standard tax rate or to the 30% rate can reduce their tax base by 10% of the increase in their equity provided that (i) this increase is maintained over a period of 5 years and (ii) a reserve is set up for the amount of the reduction, duly separated and restricted over the 5-year period.

The reduction cannot exceed 10% of the positive tax base prior to the reduction, the inclusion of adjustments for deferred tax assets and the offset of tax losses. If there is insufficient tax base, the outstanding amounts can be applied over the next 2 years, together with that of the year itself, subject to the same limit.

A number of rules are established for determining the increase in equity, mainly excluding shareholders' contributions or variations for deferred assets, which means that as a general rule the equity increase has to come from the year's undistributed income.

(xi) Offset of tax losses

In addition to the absence of a time limit for the offset of tax losses, the most notable new feature is the limitation of the offsettable amount to 60% of the tax base, in all cases admitting offset up to an amount of €1 million.

Rules are also established to limit the use of tax losses in cases in which companies were acquired for the purpose of offsetting their tax losses.

2.1.2 *Tax rate*

(i) The standard tax rate will be 25%.

(ii) Newly formed companies pursuing economic activities will be taxed at 15% for the first two tax periods (unless they qualify for a lower tax rate). This rate will not apply to entities whose main activity is the management of personal and real estate net worth in accordance with the Wealth Tax Law.

(iii) A 20% rate will apply to fiscally protected cooperative entities, except for income not included in the cooperative (standard rate).

(iv) Credit cooperatives and rural cooperative banks will be taxed at the standard rate (25%) except for income not included in the cooperative (30%).

(v) Credit cooperatives and entities engaging in the operation, prospecting and mining of underground oil deposits and gas fields will be taxed at a rate of 30% (credit cooperatives thus continuing to be taxed at the current rate).

2.1.3 *Tax credits*

(i) <u>Tax credits as incentives for certain activities</u>

The preliminary bill only contemplates R&D&I tax credits, tax credits to provide incentives for the cinematographic industry and job creation tax credits.

The rates are maintained for the first type of tax credit, despite the reduction in the standard tax rate, and minor changes are made to the tax credit as currently configured.

The tax credit for investments in cinematographic productions is set at 20% for the first €1 million of tax credit base and at 18% for the remainder, with a view to boosting the development the Spanish industry. A tax credit equal to 15% of expenses incurred in Spain is also established, with a view to bringing the filming of major international productions to Spain.

(ii) <u>International double taxation tax credit</u>

Apart from the changes described above in connection with the exemption for the avoidance of double taxation on dividends and gains on the transfer of securities representing the equity of entities resident and not resident in Spain (and similar rules for income from permanent establishments), the following new features are being proposed.

In connection with <u>foreign-source income which has been taxed outside Spain</u>, the preliminary bill maintains the criteria according to which a tax credit may be taken equal to either i) the tax actually paid abroad, such amount not being able to exceed the tax payable pursuant to the tax treaty signed with the country in question, if any, or ii) the tax which would have been paid in Spain if the income had been obtained in Spain, whichever is lower.

The main new feature with respect to the current treatment is the deductibility of any excess foreign tax unable to be deducted due to exceeding the aforesaid limits, provided that the income taxed was obtained on the pursuit of economic activities abroad.

As regards foreign-source dividends and shares in income, as an alternative regime to the exemption regime described above, it is possible to take a tax credit equal to the tax actually paid by the nonresident entity on the income from which the dividends are paid, including the underlying tax borne by investees at any level.

In order to take this tax credit, taxpayers must meet the same requirements regarding holding percentage and period and/or acquisition cost of the investment in the investee, as those stipulated under the exemption regime: at least 5% direct or indirect holding or, alternatively, an acquisition cost of more than €50 million and, in both cases, a holding period of at least one year, which can be completed following receipt of the dividend.

The amount of this tax credit, together with the tax charged to the taxpayer abroad, cannot exceed the tax which would have been payable in Spain on the same income. Unlike what is stipulated in the case of tax charged to the taxpayer abroad (in connection with the pursuit of economic activities abroad), any excess tax paid by investees will not be treated as a deductible expense for corporate income tax purposes.

2.1.4 Special regimes

The following are the main changes in the special regimes currently regulated under the Corporate Income Tax Law:

(i) Special consolidated tax regime

The main difference with respect to the current regulations is found in the configuration of the consolidated tax group, which is to include, as a general rule, all Spanish companies in which a holding of at least 75% is owned and all permanent establishments in Spain of nonresident group companies, without being subject to conditions based on corporate configuration.

As a special rule, and in order to bring it into line with the different tax rate stipulated for credit institutions, the consolidated tax group can, if all other requirements are met, include entities taxed at the standard tax rate together with credit institutions taxed at a different tax rate, provided that all group companies choose to do so. In such case, the entire group will be taxed at a rate of 30%.

In addition to the above and with a view to perfecting the regime by treating the group as a single entity, minor changes are made to the determination of the group's tax base, which continues to be obtained (as under the current legislation) by adding together the individual tax bases of the entities and permanent establishments forming part of the group.

(ii) Special regime for restructuring transactions

This regime is configured like the standard regime for restructuring transactions and, accordingly, there is no longer a need to choose to apply it, although there is a general obligation to inform the tax authorities when transactions eligible for the regime are carried out.

As a necessary result of applying the exemption system to the transfer of domestic-source holdings, the deductibility for tax purposes of merger goodwill disappears as a mechanism for avoiding double taxation.

(iii) Special regime for enterprises of a reduced size

The preliminary bill does not provide a reduced tax scale for such enterprises like the one currently applied to them. Nonetheless, it does establish a mechanism capable of reducing the tax base by up to 10%, with an annual maximum limit of €1 million, which could therefore result in an effective tax rate of 22.5%.

In this way, the impact of the tax losses which are expected to be incurred over the next 5 years is anticipated in the taxpayer's tax base. This requires recording (with a charge to income for the year in which the reduction is made) a reserve equal to the amount of the reduction in the tax base derived from the "equalization reserve", which reserve will be restricted for the 5-year period.

(iv) International fiscal transparency

This regime, which along general lines continues to have the same treatment as that existing today, includes a new case of obligatory attribution of income obtained by a nonresident subsidiary.

Starting with the requirements regarding minimum holding and maximum taxation (50% holding in conjunction with related persons or entities and taxation of less than 75% of the Spanish tax), under the preliminary bill the taxpayer must be attributed with the income obtained by the subsidiary from the assignment or transfer of goods and rights or from the supply of services, where the subsidiary does not have the required organization of human and material resources for doing so, even if the transactions are recurring.

As an exception, the aforesaid attribution will not take place if the taxpayer proves that the transactions listed above are carried out with material and human resources existing at another entity not resident in Spain and belonging to the same group (as group is defined in article 42 of the Commercial Code), regardless of its residence and of the obligation to prepare consolidated financial statements, or that it was incorporated and is operating on valid economic grounds.

If the material and human resources required for the pursuit of the activities exist, only income from certain sources will be attributed, in line with the current international fiscal transparency mechanism, although minor changes have been made to the current regime under the Corporate Income Tax Law.

Lastly, the preliminary bill eliminates the case of non-attribution where the total income is less than 4% of the total revenues of the nonresident entity, as well as the possibility of measuring the limit which would remain in force (15% of the total income) at group level.

(v) Foreign-security holding companies regime

Two notable changes have been made to this special regime, apart from its necessary adaptation to the new scenario in which dividends and gains on the transfer of resident entities are also exempt if certain requirements are met.

The first is that the minimum amount of the investment required to qualify for the regime has been raised to €50 million if the minimum holding of 5% is not owned. This high threshold (until now €6 million) may prevent entities currently subject to the regime from continuing to apply it.

The second is the correction of the treatment of dividends received from foreign-security holding companies by individuals resident in Spain. Such dividends are now to be reported on the personal income tax return of such individuals as "savings income" (under the current law, dividends are reported on the personal income tax return under general taxable income).

2.1.5 Civil law partnerships

Civil law partnerships with a corporate purpose will be treated as corporate income taxpayers.

The preliminary bill establishes a special tax regime for the dissolution and liquidation of civil law partnerships that present circumstances such as the fact that prior to January 1, 2016 they qualified for the pass-through tax regime or that after January 1, 2016 they met the requirements for becoming corporate income taxpayers.

The tax regime basically entails the exemption or deferral of taxes; in connection with the personal income tax, corporate income tax and nonresident income tax of the partners, the regime established is similar to that formerly regulating the dissolution of asset-holding companies.

Partners of civil law partnerships qualifying for the pass-through tax regime who become corporate income taxpayers may continue to take tax credits for economic activities not yet taken as of January 1, 2016, provided that they meet the conditions and requirements stipulated in the Corporate Income Tax Law.

2.2 Measures introduced for the 2014 and 2015 tax periods

Notwithstanding the fact that, in general, the preliminary bill states that the new corporate income tax legislation will enter into force on January 1, 2016 and will apply to years commencing after January 1, 2016 (and that therefore, in general, the current Corporate Income Tax Law will remain in force until that time), certain measures are included which are to take effect in years commencing in 2014 and in 2015. These are, fundamentally, the following:

(i) Within the scheme for the progressive reduction of the general tax rate from the current 30% to 25% in 2016, a general transitional rate of 28% is established for the 2015 tax period.

All other entities will continue to be subject, throughout 2015 and in general, to the rates in force prior to the reform.

As a result of the new rates applicable in 2015 and in 2016, the tax credits for the avoidance of domestic double taxation relating to years prior to January 1, 2015 may be taken in the following years by recalculating their amount having regard to the tax rate in force in the tax period in which they are taken.

(ii) In general, it should be noted that during the 2015 tax period, the following exceptional measures introduced in previous years due to the economic crisis will continue to apply:

(a) limitations on the application of the rules on unrestricted amortization/depreciation for assets acquired through March 31, 2012;

(b) limitations on the offset of tax losses by large enterprises, according to which:

- large enterprises with net revenues equal to or greater than €20 million but less than €60 million, may only claim tax losses from previous years up to the limit of 50% of their previous tax base;
- large enterprises with net revenues equal to or greater than €60 million may only claim tax losses from previous years up to the limit of 25% of their previous tax base;

(c) special rules for determining the amount of corporate income tax prepayments: minimum prepayment, increased rates, etc.;

(d) the tax deductibility of goodwill acquired from third parties, financial goodwill, merger goodwill and intangible assets with an indefinite useful life, will continue to be subject to a limit of not more than 1% per year for the first three years and not more than 2% per year for year four;

(e) special rules of temporary application under the financial lease contract amortization regime;

(f) the regulation of deferred tax assets, notwithstanding what is stated below.

Please see our previous newsletters for a detailed description of these extraordinary measures introduced in recent years.

(iii) After January 1, 2015 the deduction for tax purposes of financial goodwill will disappear, but a transitional regime is established which permits the deduction in connection with investments made prior to January 1, 2015 pursuant to the legislation currently in force, maintaining the deduction in 2015, as indicated, with a maximum limit of one one-hundredth.

(iv) After January 1, 2014 amounts recorded for impairment losses on receivables or other assets derived from doubtful debts, as well as those relating to employee welfare systems which have generated deferred tax assets are to be recorded in the tax base up to the limit of 60% of the positive tax base prior to their inclusion and to the offset of tax losses, which does not appear to be very consistent with the regulations applicable in 2015 and 2016. For 2015 the preliminary bill establishes, in its place, a limit similar to the current limit on the offset of tax losses for large enterprises.

(v) Additionally, a new article is introduced for the specific regulation of the conversion of deferred tax assets into claimable credit and a similar regime is added, effective from January 1, 2011, for cooperative entities, with certain particular features.

(vi) Despite the fact that the exemption for gains on the transfer of holdings in companies resident in Spain, where the requirements are met, is regulated under the new Corporate Income Tax Law which is to enter into force for years commencing after January 1, 2016, the preliminary bill includes a transitional provision establishing a progressive exemption regime for such income.

Thus, an exemption of 30% in 2015 and of 60% in 2016 is established for the part of the income not related to a net increase in undistributed income generated by the investee during the time the holding is owned.

Pursuant to the preliminary bill, an exemption may be taken on the part related to this net increase in income, on the understanding that the tax credit for the avoidance of double taxation provided for under article 30.5 of the Corporate Income Tax Law, still in force at least for 2015, cannot be taken.

The context of this exemption is the appearance of a new law which, as indicated, provides for a total exemption of gains obtained on the transfer of certain holdings in entities resident in Spain and, accordingly, this new law also provides for the disappearance of the measures currently set forth in the Corporate Income Tax Law to avoid double taxation in the case of distributions of dividends in which the former owners of the holdings were taxed on the transfer.

Accordingly, the introduction of this progressive exemption as from 2015 makes it necessary to include a transitional regime for acquisitions made prior to January 1, 2015 (which will basically comply with the current regime), and for those made in 2015 and in 2016 for which new criteria have been included for the recovery of double taxation.

(vii) Because the resident entities transferring the holding will no longer be taxed, by virtue of the application of the new exemption stipulated in the preliminary bill, merger goodwill will cease to be deductible from the time this provision enters into force. Nonetheless, a transitional regime must be stipulated with a view to avoiding double taxation in cases in which the transferor had already been taxed.

In this connection, the transitional provisions of the preliminary bill only appear to maintain the deductibility of the merger goodwill existing until such time for acquisitions of investees made prior to January 1,2015 and, with some changes to the previous regime, for those made in 2015 and 2016. Nonetheless, it should be noted that in 2015 the provisions of the Corporate Income Tax Law on the special neutrality regime which permits the deductibility of merger goodwill where the requirements for deductibility are met, will still be in force.

(viii) In relation to the consolidated tax regime, the new rules on the configuration of the tax group stipulated in the preliminary bill and discussed above will apply in the first tax period commencing after January 1, 2015. Accordingly, entities which cannot form part of the tax group pursuant to current legislation may join the tax group as from that year.

Also applicable from the first period commencing after January 1, 2015 are the new rules aimed at avoiding the disadvantages caused by the current legislation where one tax group is integrated with another and, accordingly, such transactions will become totally neutral from a tax standpoint.

(ix) A new restriction on the deductibility of finance costs is added to the general "30% rule" restriction and may affect LBO transactions. Thus, restructuring transactions carried out after June 20, 2014 will be subject to an additional limit equal to 30% of the acquirer's operating income in acquisitions of holdings in other entities where, thereafter, the acquired entity is incorporated into the tax group of the acquirer, excluding the income from the acquired entity's activity from the calculation.

The same treatment, i.e., the imposition of the additional limit, will also apply in the area of a restructuring transaction.

(x) As regards the special regime applicable to listed corporations for investments in the real estate *market (Sociedades Anónimas Cotizadas de Inversión en el Mercado Inmobiliario* or SOCIMIs), effective for years commencing after January 1, 2014:

(a) dividends or shares in profits distributed by SOCIMIs are excepted from the general withholding tax regime where the recipient is an entity that is also eligible for the special regime;

(b) the current restriction on the eligibility of nonresident shareholders of SOCIMIs (without a permanent establishment) to take the exemption on their nonresident income tax return for income obtained on transfers of securities or the redemption of shares in investment funds carried out on any of the Spanish official secondary securities markets will only apply where the shareholder's holding is equal to or greater than 5%.

(xi) Effective for the 2015 tax period, significant changes are made to the regime for non-profit entities subject to the provisions of Law 49/2002:

(a) The percentage of the tax credit that may be taken by individuals is increased from 25% to 27.5%. As from 2016 the percentage will be 30%.

(b) Efforts to obtain donor loyalty, whether individuals or legal entities, are encouraged.

In particular, in 2015 individuals may take a 50% tax credit on the first €150 donated and a 32.5% tax credit on the excess, provided that they have made donations to the same entity over the last three years. As from 2016 the percentages will be 75% and 35%, respectively.

After making donations to the same entity for at least 3 years, legal entities will be entitled to a tax credit of 37.5%. As from 2016 the percentage will be 40%.

(xii) Tax incentives applicable to events of exceptional public interest, save those approved prior to June 20, 2014, are repealed in general.

3. Nonresident Income Tax

Various changes are foreseen to nonresident income tax legislation, effective from January 1, 2015, including most notably the following:

3.1 Exemptions

(i) The current anti-abuse clause is amended both for distributions of dividends to parent companies resident in the EU and for payments of royalties to associated enterprises resident in the EU, in order to admit the non-application of the clause exclusively *"where the company (*receiving the dividend or royalty) *was formed and is operated on valid economic grounds and for substantive business reasons other than the management of securities or other assets".*

(ii) A change is made to conditions for the exemption of distributions of dividends to parent companies resident in the member countries of the European Economic Area.

In particular, if to date such parent companies were required to be resident in a state which had "signed with Spain a tax treaty containing an exchange of information clause or an agreement for the exchange of tax information", now the provision is worded so as to require residence in a country with an "effective exchange of tax information", on the new terms introduced in additional provision one of Law 36/2006 on measures to prevent tax fraud, mentioned below.

(iii) The exemption of up to €1,500 for dividends obtained by certain nonresident individuals is eliminated, in line with the amendment proposed for personal income tax.

3.2 Tax base

(i) The Nonresident Income Tax Law now includes the obligation stipulated under the Corporate Income Tax Law to include in the tax base the difference between the normal market value and the book value of items which are used by a permanent establishment that discontinues its activity or which are transferred abroad.

(ii) In the case of capital gains on the transfer of shares obtained by nonresidents who would previously have been subject to the new tax regime due to a change of residence, the preliminary bill expressly stipulates that the capital gain is to be computed by taking as the acquisition cost the market value of the shares used for the purposes of the new regime.

(iii) A change is made to the rules for determining the tax base of taxpayers resident in the EU, which to date permits both individuals and legal entities to deduct the expenses stipulated in the Personal Income Tax Law, provided that they prove that the expenses are directly related to income obtained in Spain and have a direct and inseparable economic link to the activity pursued in Spain.

- On one hand, these rules also extend to residents of a member state of the European Economic Area with which there is an effective exchange of tax information.
- On the other, regard must be had to their effective status as an individual or legal entity since, in the case of legal entities, the provision of reference for the deduction of expenses is the Corporate Income Tax Law, with requirements

regarding proof and relationship with the activity pursued in Spain equivalent to those currently in force.

3.3 Tax rates

(i) The tax rate for permanent establishments will be determined with reference to the Corporate Income Tax Law.

(ii) The supplementary taxation of income obtained and transferred abroad by permanent establishments will take place at a rate of 20% in 2015 and 19% from 2016.

(iii) With respect to income obtained without the intermediation of a permanent establishment, the standard tax rate, which to date was 24.75%, (i) is reduced to 24%, and (ii) to 19% from 2016 (20% during 2015) for residents of the European Union or of a member state of the European Economic Area with which there is an effective exchange of tax information, in line with the reduction of the minimum tax rate on the standard personal income tax scale.

In this way the preliminary bill brings the standard tax treatment of EU residents into line with the treatment given to date to dividends, interest and capital gains on the transfer of assets, which will also be 19% from 2016 (20% during 2015).

(iv) The tax rate of pass-through tax entities with a presence in Spain is set at 25%.

3.4 Other proposed amendments

(i) The preliminary bill establishes a new obligation to withhold tax on transfers of subscription rights by nonresident individuals, in which case the tax base will be the amount of the transfer and the tax rate will be 19%.

(ii) The regime under which taxpayers resident in other EU member states can choose to be taxed for personal income tax is extended to residents of a member state of the European Economic Area with which there is an effective exchange of tax information, extending the eligible cases to a case in which the taxpayer has obtained in Spain income of less than 90% of the personal and family allowance which would have been due to him had he had tax-resident status in Spain, and the income obtained outside Spain was also less than such minimum.

(iii) Capital gains disclosed on transfers of real estate constituting the principal residence of a nonresident in Spain will be tax exempt if the proceeds obtained from the transfer are reinvested in another principal residence, on the same conditions applicable to those with tax-resident status in Spain.

Nonetheless, this exemption does not avoid the application of withholding tax of 3% of the transfer price on transfers of real estate by nonresidents, nor does it release the nonresident from the obligation to file a tax return and pay in the tax debt although, if the reinvestment takes place prior to the transfer, it may be taken into account in order to determine the related tax debt.

(iv) The "definition of tax haven, zero taxation and effective exchange of tax information" is amended (with the resulting impact on various taxes and not only on nonresident income tax) in order to include new criteria updating the list of tax havens and, in particular, the possibility for countries or territories treated as tax havens to sign the

"OECD Convention of Mutual Administrative Assistance in Tax Matters amended by the 2010 Protocol" or the findings of the "peer reviews" performed by the Global Forum on Transparency and Exchange of Information for Tax Purposes.

The amendment also enables the government to update the list of countries and territories treated as tax havens.

4. Value Added Tax and Canary Islands General Indirect Tax

The preamble to the preliminary bill amending VAT, Canary Islands general indirect tax and excise and special taxes, which contains the amendments in the area of VAT, divides them into three large groups: those adapting its provisions to bring them into line with Community legislation, with their interpretation by the Court of Justice or with the criteria of the Commission; some technical adjustments made for the sake of the principle of legal certainty; and lastly, a raft of fraud prevention measures.

With respect to the amendments made in relation to Canary Islands indirect general tax, although the Canary Islands are outside the scope of application of the common VAT system and therefore are not subject to Community legislation or case law, some of the changes made in VAT have been included in the Canary Islands general indirect tax legislation to achieve greater harmonization of both taxes.

The main changes envisaged for January 1, 2015 are:

4.1 Territoriality (VAT)

The references to the different territories are brought into line with the provisions of the Treaty on the Functioning of the European Union, and the classification of some territories in particular is introduced.

4.2 Cases of non-taxability (VAT and Canary Islands general indirect tax)

In relation to the transfer of an autonomous economic unit, besides some minor changes, the preliminary bill makes non-taxability of that transfer conditional on the economic unit being considered an autonomous economic unit at the transferor.

The non-taxability of public bodies is also modified to legally establish that the tax will not apply to transactions carried out in the context of the management functions entrusted to public bodies, organizations or entities that have the status of in-house and technical service providers of the public authorities that engage them, and those provided to the public authorities by public sector entities where those authorities have control over their management or the right to appoint more than half the members of their managing body.

4.3 Definition of supply of goods (VAT and Canary Islands general indirect tax)

In order to bring national provisions into line with the Court of Justice's criteria, transfers of securities attributing the ownership, use or enjoyment of a building are classified as supplies of goods, so that they are not exempt from those taxes.

Additionally, in the specific area of Canary Islands general indirect tax, the definition of supply of goods is amended as follows:

(i) In works of construction the purpose of which is to build or restore a building, the cost of the materials provided by the builder must exceed 40% of the taxable amount (up to now, that percentage has been 33%).

(ii) Transfers of goods pursuant to installment sales contracts with a condition precedent and transactions treated as leases-sale are deemed supplies of goods.

Through those changes, Canary Islands general indirect tax is brought into line with VAT legislation.

4.4 Exit from suspensive areas or arrangements (VAT)

The preliminary bill gives the status of law to the administrative view that the taxable event consisting of a transaction treated as an import will not arise upon exit of the goods from the areas or arrangements established in articles 23 and 24, where that exit is the result of an intra-Community supply, export or similar exempt transaction.

4.5 Exemptions in internal transactions (VAT)

On October 24, 2012, the European Commission issued a reasoned opinion prior to filing a complaint with the Court of Justice contending that the Spanish exemption applicable to notary services relating to financial transactions did not comply with the provisions of the directive.

The amendment proposed now removes these services from the list of exemptions, in keeping with the Commission's criteria.

Besides this adaptation, the following exemptions are modified:

(i) Elimination of the exemption for the supply of land in initial contributions to Development Apportionment Entities by landowners and the apportionments which those entities make to them in proportion to their contributions.

(ii) Elimination of the reference to the "exclusive" aim of the not-for-profit entities engaged in political, union, etc., activities.

(iii) Elimination of the restriction whereby the works must be carried out by the developer in order for land in process of urban development to be non-exempt.

(iv) Revision of the references in the technical exemptions of article 20.1.24 to the elimination of the exemption on the contributions to Development Apportionment Entities.

4.6 Waiver of exemptions in real estate transactions (VAT)

The preliminary bill extends the possibility of waiving the exemption in real estate transactions, which will no longer be conditional on the acquirer having the right to the full deduction of the VAT borne on the acquisition. A partial deduction, whether effective or according to the envisaged use of the transferred goods, will now suffice.

4.7 Exemptions in foreign commerce transactions (VAT)

Some technical adjustments are made in respect of services related to exports and to imports with placement under warehousing arrangements other than customs arrangements, the objective scope of which is confined to certain cases and goods.

4.8 Place of supply of transactions (VAT and Canary Islands general indirect tax)

(i) Place-of-supply rules for supplies of telecommunications services, radio and television broadcasting services and services supplied electronically

This change results from the compulsory transposition of the provisions of Directive 2008/8, effective starting on January 1, 2015, to establish the new place-of-supply rules applicable to telecommunications services, radio and television broadcasting services and services supplied electronically and which have been discussed extensively in past Bulletins.

By way of a summary, up to December 31, 2014, these services supplied by entities established in the territory where VAT or Canary Islands general indirect tax applies, to end customers domiciled in the Community or the Canary Islands, are subject to Spanish VAT or Canary Islands general indirect tax.

Starting on January 1, 2015, however, they will be taxed in the member state where the customer is established, meaning that, if the customer is the final consumer, the supplier will be obliged to charge and pay over the VAT (or, as the case may be, Canary Islands general indirect tax) of the state where the customer is established.

In the VAT area, in order to simplify the management of the obligations to be met in each of the member states where services are supplied, the possibility is established of electing to use the single point of electronic contact, referred to as "Mini One-Stop Shop", according to which the tax return to be filed in each jurisdiction will be managed exclusively through the tax authorities of the supplier's place of establishment (Spain, in this case).

In addition, with regard to Canary Islands general indirect tax, the catch-all clause of place of effective use or operation is modified to adapt it to the modifications made in the correlative clause of the VAT Law with effects from January 1, 2014, by eliminating the same reference that was made to "Canary Islands, Ceuta and Melilla," thus preventing situations of double taxation.

(ii) Place of supply of assembled goods

The preliminary bill eliminates the quantitative limit on the installation cost in order for supplies of goods with installation or assembly to be deemed located in the territory where the installation is completed, although the immobilization requirement is maintained.

4.9 Chargeability (VAT)

The legal reference to article 235 of the Revised Public Sector Contracts Law, established in relation to the chargeability of VAT on certifications of public works, is revised without altering its contents.

4.10 Taxable amount (VAT and Canary Islands general indirect tax)

Regarding VAT, also pursuant to Community case law, the market value of transactions the consideration of which is not wholly or partially in cash is replaced by the value agreed by the parties, applying, by default, the rules on self-supplies and clarifying that the exclusion from the taxable amount of grants not linked to the price does not apply to "amounts paid by a third party in consideration for the transactions."

In the area of Canary Islands general indirect tax, the same changes are made, expressly including the above-mentioned rules for determining the taxable amount.

4.11 Modification of the taxable amount (VAT and Canary Islands general indirect tax)

In cases where the taxable person is adjudged insolvent, the period for modifying the taxable amount is increased by two months.

In cases of bad debt, the preliminary bill establishes the possibility for traders with the status of SME (Small to Medium Enterprise) for tax purposes to reduce the taxable amount in the six months following the taxable event or in the general period of one year, and sets forth the conditions for computing the periods in transactions to which the cash-basis accounting scheme applies.

In the VAT area, a technical correction is also included regarding the reference to the provision regulating the correction of deductions by the recipient of the transaction.

4.12 New cases of reversal of the liability (VAT)

Along the lines established by the latest legislative amendments, new cases of reversal of the liability are established as a fraud prevention measure. The new cases are applicable to supplies of:

(i) Silver, platinum and palladium;

(ii) Mobile phones;

(iii) Videogame consoles, laptop computers and digital tablets.

4.13 Tax rate applicable to medical equipment and medicinal substances (VAT)

In 2010, the European Commission initiated an EU law infringement proceeding against Spain, in its preliminary administrative phase, on the ground that the application of reduced rates to the following infringed the VAT Directive:

(i) Medicinal substances capable of being used habitually and suitably to obtain medicines;

(ii) Medical devices, material, equipment or appliances which, viewed objectively, can only be used to prevent, diagnose, treat, alleviate or cure illnesses or ailments in humans or animals, but which are not "normally used to alleviate or treat disability, for personal and exclusive use by disabled persons";

(iii) Aids and equipment which may be used essentially or primarily to treat physical disabilities in animals; and

(iv) Aids and equipment essentially or primarily used to treat human disabilities, but which are not intended for the exclusive personal use of the disabled.

As Spain did not adopt the Commission's position, the Commission brought an action before the Court of Justice on July 8, 2011, which was resolved by means of a judgment against Spain dated January 17, 2013.

In order to adapt the legislation to what is established in the Court of Justice judgment, the list of goods subject to the reduced rate of 10% has been modified and that rate is now confined to, among other products, medicine for animal use, certain pharmaceutical products that can be used by the consumer, and the medical equipment and devices listed in a new Schedule 8 to the Law (which include, among others, prescription glasses and contact lenses) while the 4% rate is for medicine for human use. This rate is also maintained for vehicles for persons with reduced mobility and for the supply of prostheses, orthoses, and internal implants for disabled persons.

In general terms, the reduced rates only apply to goods serving to alleviate or treat physical, mental, intellectual or sensorial disabilities in persons.

4.14 Deductions (VAT and Canary Islands general indirect tax)

The preliminary bill establishes the obligation to determine the amounts of deductible tax by allocation to business and non-business activities in the case of public entities that pursue both types of transactions (the so-called "dual enterprises") using reasonable criteria that take into account the proportion of income obtained from each type.

Moreover, the computation of the general deductible proportion applicable to common inputs, in the deduction rules for different sectors of business, excludes the turnover derived from the special VAT grouping scheme.

Lastly, in VAT, the preliminary bill extends the possibility of applying the obligatory special deductible proportion to cases where the sum of deductions in the general deductible proportion exceeds by 10% the result of applying the special deductible proportion.

With regard to Canary Islands general indirect tax, this possibility is introduced for the first time in the law, replacing the cases that up to now required applying the special deductible proportion.

4.15 Refunds to traders not established in the EU (VAT)

The reciprocity requirement is eliminated for the tax borne on hotel, restaurant and transport services linked to the attendance of trade fairs, conferences and exhibitions, and in relation to the acquisition or import of molds, templates or equipment used to manufacture goods that are exported for delivery to the non-established trader, where that equipment is also exported when its use has ended.

4.16 Assessment of tax on imports (VAT)

Although the system for assessing import VAT on imports is maintained, the preliminary bill establishes that the tax can be collected and paid in the tax return of the period in which that assessment is received, which will avoid the financial effect of paying the tax to the Public Treasury and subsequently recovering it through its deduction in the periodic returns.

However, the procedure and requirements for taxable persons that use this procedure have been left to be implemented in regulations.

Until that implementation by regulations, a specific procedure is established for inspecting import VAT that will be regulated by the General Taxation Law, with the particularity that the purpose of the procedure will be limited to verifying the fulfillment of the tax obligation in relation to this taxable event, and therefore the scope of the procedure will be confined to that aim and cannot be extended.

Moreover, the preliminary bill repeals single additional provision of Law 9/1998, which regulated the reimbursement of VAT on imports of goods to customs agents and to the entities acting in their own name and for the account of the importers.

4.17 Assessment of Canary Islands general indirect tax

The preliminary bill establishes the new possibility for the tax authorities to initiate a procedure for issuing the provisional assessment where thirty days elapse since the taxable person has been requested to file the self-assessment that it did not file on time, unless the breach is remedied or the absence of obligation is proven.

These provisional assessment would be enforceable immediately upon their notification, notwithstanding the possibility of filing the relevant claims.

4.18 Special simplified schemes and schemes for agriculture, livestock and fisheries (VAT and Canary Islands general indirect tax)

The quantitative limits permitting the application of the simplified regime and the subjective and quantitative requirements for applying the special scheme for agricultural, livestock and fishery activities are reduced (the latter taking effect on January 1, 2016), and some technical corrections are made in the VAT legislation in relation to real estate transfers in the compensatory charge scheme.

4.19 Special scheme for travel agencies (VAT and Canary Islands general indirect tax)

In order to adapt the legislation to the Court of Justice judgment of December 26, 2013, the preliminary bill introduces various changes in the special scheme for travel agencies:

(i) It expressly includes the application of the scheme to transactions carried out by any trader that entail acting in its own name in the contracting of accommodation or transport services for the benefit of a third party.

(ii) It eliminates the possibility of stating in the invoice the reference to “VAT/Canary Islands general indirect tax included in the price”, the amount resulting from multiplying by 6 (by 2 in the case of Canary Islands general indirect tax) and dividing by 100 the price of the transaction and that this amount be deemed borne by the recipient for purposes of making its deductions.

(iii) However, where the recipient is a trader, it may elect to apply the general tax scheme.

(iv) It eliminates the possibility of determining the taxable amount on a global basis for each tax period.

4.20 Special VAT grouping scheme (perimeter) (VAT and Canary Islands general indirect tax)

Spanish legislation permits applying this scheme to a parent company and its subsidiaries where the former's holding in the latter is at least 50% of the capital stock.

In 2009, the Commission published a Communication to the Council and to the European Parliament with its interpretation of the provisions of the Directive in respect of what Spain has transposed as the Special Grouping Scheme.

In that Communication, in relation to the entities that can be treated as a "single taxable person", the Commission advocates, based on the literal wording of the Directive, for the simultaneous existence of ties of a financial, economic and organizational nature which, in the Spanish law, had been transposed by a mere reference to the aforementioned minimum holding of 50%.

In order to adapt the Spanish law to the interpretation set forth in the Commission Communication, Spain has modified the subjective requirements for applying the scheme, so that, starting on January 1, 2015, there must be ties of a financial, economic and organizational nature. The parent entity must have effective control of the investees, holding more than 50% in the capital stock or in the voting rights.

Moreover, the law is also amended to establish the application of the scheme to parent entities that do not have the status of taxable persons of the tax because they are mere holding entities of shares or units, which possibility the Court of Justice had considered permitted by the Directive (contrary to the criteria of the Commission in its Communication) in various judgments handed down in April 2013.

4.21 New types of infringements (VAT and Canary Islands general indirect tax)

The following tax infringements are established:

(a) The failure to communicate in time or the incorrect communication of the performance as traders in cases of reversal of the taxable person applicable to supplies of buildings in execution of guarantees which is penalized with a proportional fine of 10% of the tax relating to the transactions in which the breach takes place.

(b) The failure to communicate in time or the incorrect communication of the performance as traders and of the nature of the works in cases of reversal of the taxable person applicable to works of construction which is penalized with a proportional fine of 10% of the tax relating to the transactions in which the breach takes place.

(c) Exclusively in the VAT area, the failure to report or the incorrect or incomplete reporting of the VAT assessed on imports in the VAT self-assessment where so required also constitutes an infringement, which could be penalized with a fine of 10% of the amount of the output VAT relating to the assessment made.

(d) In the Canary Islands general indirect tax, the failure to report in the relevant self-assessment the amounts of the tax of which the recipient of supplies of investment gold, in which the exemption has been waived, is the taxable person constitutes a tax infringement.

All of the above penalties will be subject to the reductions established in the General Taxation Law.

4.22 Liability of the titleholder of a tax warehouse other than a customs warehouse (VAT)

The preliminary law establishes the secondary liability of the titleholder of a tax warehouse other than a customs warehouse for the tax debt payable upon exit of the goods.

5. Excise and special taxes

In the area of excise and special taxes, the three large groups of measures of the proposed reform in the preliminary bill amending VAT and Canary Islands general indirect tax and special and excise taxes are as follows:

5.1 Electricity tax

Electricity tax is revised in depth, going from being a special tax on manufacturing to a tax on the supply of electricity for consumption or self-consumption by producers of electricity.

This revision entails the comprehensive regulation of all the elements of this tax as a separate chapter, eliminating the references to the articles on special manufacturing taxes.

Of the main changes proposed, the most noteworthy is the 85% reduction in the tax base for industrial activities for which the consumed electricity represents more than 50% of the cost of a product, analogously to what is already established in the law for other cases.

Moreover, from a registry standpoint, the registration obligations are confined to the operators that perform electricity supplies and to the beneficiaries of certain exemptions and reductions in the tax base, thus reducing the administrative costs, notwithstanding the obligations for taxpayers not established in Spain. The registrations already made in the context of the former electricity tax will be valid for purposes of the new tax.

5.2 Tax on fluorinated greenhouse gases

The preliminary bill introduces technical adjustments in relation to the tax on fluorinated greenhouse gases, expanding the applicability of the tax to the intra-Community import and acquisition of gases in certain cases, while excluding losses relating to imprecisions in measurement instruments from the tax.

It also includes new exemptions related to recharging in equipment, devices or installations to replace other gases under certain conditions, to supplies to vessels or aircraft that engage in international maritime or air navigation, to supplies to officially recognized centers and to supplies made to the armed forces in fire extinguishment equipment.

Lastly, it defines the concepts of “final consumer” and “reseller.”

5.3 Other issues

Amendments are proposed to certain provisions to give greater legal certainty to taxpayers and, in particular:

(i) In the area of excise tax on oil and gas, a clarification is included regarding the tax charge on natural gas, establishing that the special rule on the chargeability for supply contracts for a consideration does not apply where the supply to the final consumer is

done other than through fixed piping, thereby giving the status of law to the administrative interpretation made in ruling number V0196-14.

(ii) The penalty regime established in the special and excise taxes legislation is brought into line with that established in the General Taxation Law, establishing greater detail in the legal definition of infringements.

The legislative amendments include new minimums for serious infringements and increase the amount of penalties, in relation to the possession for commercial purposes of alcoholic beverages or tobacco products that do not bear the fiscal markings established by regulations, but reducing the scale of the penalty for repeated commission of this type of infringement.

Although the date of **entry into force** of the law is envisaged as **January 1, 2015**, the changes relating to tax on fluorinated greenhouse gases, save for new exemptions, will apply starting on **January 1, 2014**.

6. General Taxation Law and other procedural provisions

The stated goals in the Preliminary Bill amending the General Taxation Law are to increase the legal certainty, of both taxpayers and the authorities, to prevent tax evasion, heighten the efficiency of the authorities' work on the application of taxes and reduce the amount of litigation in this area.

The main amendments proposed for these purposes in the General Taxation Law are the following:

6.1 General tax legislation

(i) In relation to conflict in the application of tax law, it is established that penalties can be imposed in cases of regularization based on the application of this anti-abuse instrument.

For these purposes, the reports of the consultative committee issued in declaration of conflict proceedings will be made public (after eliminating any references that may identify the person concerned), with the result that for returns filed by other tax payers in which the authorities' preexisting and public administrative criterion was breached this may serve as justification for the imposition of penalties where the cases are substantially the same.

It has also been established that the consultative committee can determine the existence of conflict in the application of the law, not just in relation to inspection proceedings, but also in relation to acts or transactions not attributable to specific taxpayers.

(ii) Various amendments have been made concerning the statute of limitations, notably:

(a) It has been expressly included, in relation to taxes that are collected periodically through tax statements, that, where it is not necessary to file a return or self-assessment to determine the tax debt, the statute of limitations will start to run on the date the tax fell due.

(b) The statute of limitations regime for connected tax obligations is defined, establishing that where the statute of limitations for a tax is tolled the statutes of limitations for any other taxes that are conditional on the regularization of the main tax will also be tolled;

(c) It is expressly established that there is no statute of limitations for the tax authorities' right to perform reviews and investigations in relation to elements or circumstances that determine the tax obligation and originate in statute-barred years, provided they take effect with respect to years open for review.

(iii) In relation to the indirect assessment method, the sources are provided from which to take the data to be used in this method for determining the tax base (from the signs, indexes and modules if the taxpayer might have applied the objective assessment method, from the enterprise itself, from statistical surveys or from a sample created by the inspectors). It is clarified also that the method may be used partially (only to determine sales/revenues but not purchases/expenses, for example) and, lastly, it allows the deduction of input VAT that has been assessed indirectly, even if the invoices or documents generally required by VAT legislation are not available.

(iv) A measure has been included consisting of the publication of a list of debtors, which in essence means that the tax authorities can decide to publish periodically lists of "defaulting taxpayers" to the public treasury in respect of tax debts or penalties amounting to more than €1,000,000, which are involved in enforcement proceedings and where with respect to at least 25% of their amount, more than one year has run since the end of the time limit for payment in an enforcement period.

Any tax debts and penalties that have been deferred or stayed will not be computed for these purposes.

(v) On the subject of evidence, it is established that the invoice is not a preferred form of evidence with respect to the existence of the transactions, and therefore once the authorities question their effectiveness on a founded basis, the taxpayer must produce evidence of the authenticity of the transactions.

It is also established that, after the period in which the case file is made available for examination or after the submissions period, if any, no further documents may be included in the case file or taken into account as evidence of the facts in the proceeding on application of taxes or in the resolution of appeals or claims, unless the taxpayer proves that the document could not have been produced before the end of that period.

(vi) An option has been proposed to be included in the articles of the General Taxation Law for any tax identified by the authorities in the computation for the year to be distributed on a straight-line basis over the monthly or quarterly assessment periods, where the taxpayer does not substantiate that they relate to another period in accordance with the legislation on the tax.

(vii) Some amendments have been envisaged to the rules on the value review proceeding with the aim to safeguard the option to impose and adapt the penalties imposed in cases where a contrasting expert's appraisal is requested.

(viii) In the context of a limited review proceeding, the taxpayer is allowed to produce his commercial accounting records, voluntarily, without a prior request, simply to determine the validity of certain data that the authorities have available, and the voluntary production of those records cannot prevent a subsequent review in the context of an inspection proceeding.

(ix) On the length of inspection proceedings, the law has been amended substantially, by establishing, in essence, an increase in the maximum length of the period for those proceedings from 12 to 18 months, generally, and to 27 months in the case of enterprises required to audit their financial statements or enterprises which are part of a consolidated tax group.

Alongside this amendment, the computation of cases of "justified tolling" and "delays not attributable to the authorities" (concepts that were excluded from the inspection proceeding) are replaced with a number of scenarios for tolling the period for computing the length of proceedings, either on certain objective grounds (where the case file on conflict in application of the law is sent to the consultative committee, for example), or at the request of the taxpayer, who may request that the period be tolled for up to 60 days over the whole of the inspection period. In both cases, the scenarios for tolling the period will entail an extension in the maximum length of the period for the inspection proceeding.

(x) In relation to any potential delays in the complete production of documents by the taxpayer, it is established that such delays will only affect the length of the proceeding where the requested documents are produced after the period granted in the third request made by the inspectors, in which case the maximum period for the proceedings will be extended by 3 months (provided the production of documents occurs after the end of at least 9 months from the commencement of the proceedings). The extension will be 6 months where the documents are produced after the notice of assessment has been executed, in which case the extension will also affect the length of the period for any penalty proceeding that might be in progress.

Moreover, the effects of a breach of the maximum length of period for the proceeding by the authorities have been maintained, although the reference to formal notification of the taxpayer in relation to proceedings entailing the resumption of the inspection proceeding has been eliminated, and the case of unjustified tolling for longer than 6 months has also been eliminated.

Lastly, although the preliminary bill maintains the provision determining that where a court or economic-administrative decision orders the reversion of proceedings they will have to end in the period remaining from the date to which the proceedings are reverted until the end of the general period, or within six months if this latter period is longer, it adds a provision determining that this period must be computed from the notification to the taxpayer of the resumption of the inspection proceeding.

(xi) In the event of the commencement of a mutual agreement procedure, any administrative and judicial examination procedures that may have been commenced will be stayed, until the mutual agreement procedure is conducted.

(xii) It is expressly added that any taxpayers who, when the review and investigation proceeding started, had used or offset any unused amounts by filing supplementary returns, cannot render invalid any amounts offset or used in another year and apply to offset or use those sums in the year under review, and by doing so, alter the classification of the infringement potentially committed.

(xiii) In procedural matters under EU law, a new Title VII is added to the General Taxation law in which specific provisions have been provided on the proceedings to follow for the enforcement of decisions on the recovery of State aid, expressly mentioning the specific statute of limitation rules applicable in this respect under Community legislation.

It is established that deferred or split payment cannot be requested for debts resulting from the enforcement of decisions on the recovery of such aid.

Lastly, as a mechanism for adapting the General Taxation Law to EU law, a new special procedure is established for the "revocation of acts ordered under tax laws which have been declared unconstitutional, illegal or against EU law", which may only be commenced where the statute of limitations period has not elapsed since the last decision with a tolling effect that might have been ordered before the judgment that declared that the act was unconstitutional, illegal or inconsistent with EU Law.

(xiv) The preliminary bill provides that from the date of its publication, the financial liability of the legislator State in connection with tax which may result from any judgment declaring that tax law is unconstitutional, illegal or not consistent with EU law can only be made effective through the revocation procedure described above or, if applicable, through rectification of the self-assessment.

(xv) Lastly, the authority of the economic-administrative bodies to refer economic-administrative matters for a preliminary ruling by the Court of Justice of the European Union, has been expressly recognized, just as the Court of Justice has accepted.

All these amendments will, of course, only take effect if the law is ultimately approved on these terms.

6.2 New provisions on the procedures for economic-administrative claims

The preliminary bill contains a number of amendments concerning economic-administrative claims, designed to speed up the courts' procedures and reduce litigation. The most notable measures proposed are:

(i) On the role of the examining economic-administrative bodies, art. 229 of the General Taxation Law has been amended to broaden the system for providing definitive rulings on a point of law by conferring on the Central Economic-Administrative Tribunal the authority to hand down rulings on a definitive point of law and on the Regional Economic-Administrative Tribunals the authority to hand down rulings (on their own initiative) to set the criterion with respect to the chambers with jurisdiction for specific provinces.

(ii) It has been made obligatory to bring economic-administrative claims electronically (on the website of the body that rendered the decision to which the claim relates) where the claimants are required to receive communications and notifications electronically.

In these cases, any acts and decisions affecting the interested parties or ending an economic-administrative claim in any instance will be notified to them electronically.

(iii) An attempt has been made to improve the system for joining economic-administrative claims, by simplifying the rules on compulsory joinder of claims and adding the optional joinder system for cases in which the court considers that a single decision is needed because it affects the same tax or various taxes but there is sufficient connection between all of them.

(iv) In relation to the order for costs, it is clarified that where an ordinary administrative appeal to a higher administrative body has been lodged the enforceability of the order for costs handed down in the first instance will be conditional on confirmation of the order in the decision that may be rendered on that appeal.

Furthermore, it is included that an order for costs may be made where the claim is not admitted, and express mention is required, in all cases, of the grounds on which the economic-administrative body observed the existence of bad faith or frivolousness, and the quantification thereof.

(v) The special rule on the computation of the period for appealing against decisions presumed by administrative silence is eliminated (the legislator has reproduced the case law of the Supreme Court on this point) and the rules are set out on automatic notification and challenging of the express decision rendered after the presumed dismissal by administrative silence where it is challenged.

(vi) In the context of an ordinary administrative appeal to a higher administrative body and for cases where the appeal is lodged by director-generals at the ministry or by department heads at the Spanish Tax Agency (AEAT), and by the equivalent bodies of the autonomous communities and cities with a charter of autonomy, it gives the option to request a stay of execution of the challenged decision, where there is reasonable *prima facie* evidence that collection of the debt that might ultimately become due, might be prevented or seriously hindered.

(vii) Some technical improvements and clarifications are added to the provisions on action for annulment.

(viii) An appeal against enforcement is created, to set aside decisions handed down as a result of the enforcement of an economic-administrative decision.

This appeal will undergo an “abbreviated” proceeding (*procedimiento abreviado*), except in the specific case where the economic-administrative decision had ordered the reversion of the proceeding, in which case it will undergo an “abbreviated” or a general proceeding depending on the quantum of the initial claim.

It is also established that the appealed decision cannot be stayed where no new rulings are applied for in relation to the economic-administrative decision being enforced and that an appeal for reconsideration is not allowed to be lodged before the appeal against the enforcement.

(ix) Lastly, some improvements are made to the provisions on the so-called “abbreviated” proceeding conducted by single-member bodies.

6.3 Amendments resulting from the new provisions on the criminal offense against the public treasury

Possibly the most trenchant amendments added to the General Taxation Law are those resulting from the reform of the provisions on the criminal offense against the pubic treasury made through Organic Law 7/2012. The preamble states that a number of amendments are needed to establish an administrative proceeding in which tax assessments can be made and their amounts collected and secured even in cases where a criminal proceeding is started.

A Title is introduced for this purpose devoted to the proceedings to carry out in these cases. At the same time, substantial amendments are made to the regime on injunctive remedies and new wording is given for an article with such capital importance as article 180 had.

The main new provisions introduced in this area are:

(i) Assessments made in the case of indicia of a criminal offense against the public treasury and exceptions to the general regime.

Unlike the previous legal regime, in the preliminary bill it is provided that where the tax authorities observe indicia of a criminal offense, the general rule must be to continue with the proceeding according to the general rules, even if the official copy of the case record containing indicia of criminal liability is forwarded or the case file is referred to the public prosecutor's office. The related assessment will thus be handed down by separating the elements that are associated with the potential criminal offense against the public treasury and those that are not into two separate assessments. The proceedings in relation to the elements not associated with the potential offense will take place under the ordinary assessment regime.

As may be expected, the restriction is kept on commencing or continuing with a penalty proceeding in relation to the same facts where a potential criminal offense has been observed.

Conversely, only in cases where (i) conducting the administrative assessment procedure may cause the criminal offense to become statute-barred according to the time limits set out in the Penal Code, (ii) the amount of the assessment could not be determined accurately or could not be attributed to a specific taxpayer or (iii) the tax assessment may be detrimental to the investigation or review of the evasion, an official copy of the case record containing indicia of criminal liability will be forwarded or the case file will be sent to the public prosecutor's office and no assessment will be made.

(ii) The concept of tax regularization is passed into positive tax law by being defined as the complete recognition and payment of the tax debt before notification has been served of the commencement of review or investigation proceedings.

It is specified that the tax debt for these purposes is deemed to be composed of all the elements mentioned in article 58 of the General Taxation Law, and the taxpayer must carry out a self-assessment and simultaneous payment of the tax liability plus the late-payment interest and surcharges legally due on the date of payment. It is also expressly provided that the taxpayer may carry out a voluntary regularization after the tax authorities' right to determine the tax debt has become statute-barred.

In this area, it confirms the tax authorities' powers to carry out the necessary reviews to determine, if applicable, the existence of a voluntary regularization on the terms described above and, only where they cannot achieve certainty in relation to that regularization, will the official copy of the case record containing indicia of criminal liability be referred to the competent jurisdiction or to the public prosecutor's office.

(iii) An express definition is provided of the proceeding to be followed where a tax assessment is made with some very new provisions such as:

(a) Any procedural defects that may be incurred cannot ever have the effect of extinguishing all or part of the tax debt associated with the criminal offense.

(b) The voluntary payment period for the tax debt resulting from the administrative assessment, after the official copy of the case record containing indicia of criminal liability has been forwarded or the case file referred to the public prosecutor's office, will only start to be computed from when the admission of the relevant report of an offense or criminal complaint has been served.

(c) Failure to admit the criminal complaint or report of a criminal offense will cause the inspection proceedings to revert to before the assessment associated with the criminal offense was issued, and then the relevant notice of assessment will be executed.

(d) If wilful misconduct determining a potential criminal offense is observed alongside other elements or amounts to be regularized in which no willful misconduct can be observed, two assessments will be made:

- One related to the criminal offense to which will be added all the elements in relation to which willful misconduct is observed and from which all the adjustments to which the taxpayer is entitled will be subtracted, along with the items to be deducted or offset in the tax base or tax liability and the liability originally deposited.

- A proposed assessment comprising all the reviewed elements (whether related to the criminal offense or not) from which the sum resulting from the proposed assessment related to the criminal offense will be deducted.

(e) No administrative appeal or claim is allowed against the administrative assessment related to a potential criminal offense, notwithstanding any adjustment allowed in the rules on the criminal process. Conversely, the general administrative appeals and claims may be lodged against an assessment resulting from elements and amounts not related to the potential criminal offense.

(iv) On the collection of these tax debts, it is expressly provided that the existence of a criminal process will not halt the collection proceedings for the debt. Only certain defined grounds can be raised against the steps in the collection proceeding.

(v) Moreover, it defines as persons liable for the assessed tax debt anyone who had caused or actively participated in the performance of any acts giving rise to that assessment and have been accused in the criminal process for the reported criminal offense or convicted as a result of it.

(vi) An additional provision ten is added to Law 29/1998, of July 13, 1998, on the Judicial Review Jurisdiction which removes the right of the bodies in the judicial review jurisdiction to entertain any claims that are filed in relation to tax proceedings that are ordered under these rules and with respect to the injunctive remedies adopted after the criminal process for a criminal offense against the public treasury has commenced.

(vii) Additional provision ten of the General Taxation Law (Requiring civil liability and a penalty for a criminal offense against the public treasury) is amended with the aim to include within the civil liability the tax debt that the tax authorities have not assessed because it is statute-barred or on any other legal ground, including late-payment interest, together with the fine at the stipulated daily rate. It is also provided that this liability will be required under the enforced collection administrative proceeding.

(viii) These provisions may be seen to be completed on customs matters with the addition of a specific article setting out the particular provisions on the assessment of the customs debt in cases of criminal offenses against the public treasury.

And these copious novel provisions are rounded off with the amendments added in relation to injunctive remedies, to adapt the previous wording to the appearance of these dual assessments that did not previously exist. Also adapted is the wording of article 180 on the principle of no concurrent tax penalties to adapt it to the new regime established in Title VI.

6.4 Other amendments

Lastly, the preliminary bill amends the Criminal Procedure Law with the stated aim to clarify and dispel any doubt that criminal proceedings take precedence in scenarios of criminal offenses against the public treasury, and confer jurisdiction on the criminal courts to entertain tax assessments resulting from a criminal offense against the public treasury, including the injunctive remedies. It establishes that the mere filing of a request for a stay of execution of the assessment with the criminal court will not produce any effects unless there is an express court decision with the execution of guarantees.

Amendments are also introduced to the Criminal Procedure Law to adapt the regime on enforcement of criminal judgments to that established in tax law.

Moreover, articles are amended and added in Organic Law 12/1995, on the Suppression of Smuggling with the aim to secure the assessment and collection of tax and customs debts resulting from smuggling.

Follow us:

GARRIGUES www.garrigues.com

This publication contains information of a general nature and does not constitute a professional opinion or legal advice.

© **J&A Garrigues, S.L.P.**, all rights reserved. This work may not be used, reproduced, distributed, publicly communicated or altered, in whole or in part, without the written permission of J&A Garrigues, S.L.P.

Hermosilla, 3 - 28001 Madrid (Spain)
T +34 91 514 52 00 - **F** +34 91 399 24 08