INTERNATIONAL TAX REVIEW

Spain: A holding company's paradise: New corporate income tax legislation in the Basque Country

27 May 2014

Share

Daniel Armesto ***Ilazki Otaegi***

The Basque Autonomous Community in Spain, comprising the territories of Alava, Biscay and Gipuzkoa (the Basque Country) has powers to enact its own particular corporate income tax (CIT) legislation and has used those powers to create a very interesting tax scenario for holding companies. Basque regulations compare favourably with the regulations applied in the rest of Spain and in most other European countries.

The new CIT legislation applicable in the Basque Country as of 2014 is very innovative regarding the tax treatment of holding companies, while in many ways it simplifies the previous legislation. This simplification is especially reflected in the unified tax treatment applicable to income deriving from ownership interests in companies, whether the income relates to dividends or capital gains obtained on the disposal of shares, and whether the subsidiary is tax resident in Spain or abroad.

Companies subject to Basque autonomous regulations will generally benefit from an exemption for dividends received and capital gains obtained on transfers of shares, both in Spanish and non-resident companies, while they can still deduct the impairment of these shares or capital losses on their transfer. Logically, there are certain recapture rules to prevent double-dipping. For example, if an impairment loss has been deducted, a subsequent capital gain on the sale of those shares will be taxable up to the amount of the previous deduction. But once you have made up for the previous deduction, any additional gain will be exempt.

Another distinctive feature of the Basque rules is the possibility of taking a tax deduction for the financial goodwill embedded in the acquisition price of the shares in both Spanish and non-resident companies. Financial goodwill is the excess of the acquisition price of the shares over the market value of each of the underlying assets and liabilities. A Basque resident acquirer can depreciate this difference for tax purposes at a 12.5% yearly rate, without needing to record an impairment reserve in the books. This provision is based on different principles than those governing the deduction of financial goodwill under general Spanish rules, so it is not affected by the EU decision on state aid relating to those rules.

Moreover, the deduction of financial expenses is not capped under Basque CIT legislation. Holding companies are able to fully deduct their financial expenses, even those incurred to finance the acquisition of shares benefitting from the participation exemption. They are only subject to thin capitalisation rules, with a 3:1 debt to equity ratio, applying only to net debt with related entities. Furthermore, thin capitalisation rules do not apply if the net debt with related entities does not exceed €10 million ($14 million).

In a nutshell: income is exempt; expenses and losses are deductible. Shouldn't paradise be like this? At least for a holding company!

Daniel Armesto (daniel.armesto@garrigues.com) and Ilazki Otaegi (ilazki.otaegi@garrigues.com)
Garrigues, Bilbao
Tel: +34 944 700 699