Pillar 2 in Spain: Global Minimum Tax for large groups approved

December 2024

We review its main characteristics and remind you of the aspects to which you should pay special attention.

On 21 December 2024, Law 7/2024 of 20 December was published in the Official State Gazette (BOE), which, among others, transposes Council Directive (EU) 2022/2523 in Spain, which aims to ensure an overall minimum level of taxation for multinational groups and large-scale domestic groups (Pillar 2). Specifically, the law incorporates a complementary tax (so called “Top-up-Tax, "**TUT**"), applicable to large groups with an annual **consolidated** revenue of **EUR 750 million** or more in at least two of the four fiscal years prior to the reference year, so that a **minimum taxation threshold of 15%** is reached in all cases. This tax will apply to large groups **with a presence in Spain**.

In general, the new tax will be **effective** for tax periods beginning on **or after 1 January 2024**, although certain deferred application rules are provided for and will be summarised below.

In addition, **in this publication** we analyse other tax measures included in Law 7/2024, and **here** the novelties related to the Economic and Fiscal Regime of the Canary Islands.

As anticipated in previous publications (post of 2 July 2024 of the Garrigues Tax Blog), the main characteristics of Pillar 2 are as follows:

1. Calculation rules

The calculations of the new tax should be performed on a jurisdiction-by-jurisdiction basis, considering the aggregate figures of the constituent entities of the group that are based in the jurisdiction under analysis. The accounting measures used shall be those prepared in accordance with the financial accounting standard used in the preparation of the consolidated financial statements of the ultimate parent.

Two calculation methods are envisaged:

a. **Initially, the possibility of applying the system of transitional "safe harbours" is foreseen (4th Transitional Provision of the Law)**:

   The simplified transitional "safe harbour" system can be applied by taxpayers belonging to a multinational group that prepares and submits Country-by-Country Reports. This system will be in force for **the tax periods from 2024 to 2026**. Specifically, during this period **no tax will be due if any of the** following **three tests are met**:

   - *De minimis* test: met if (i) the amount of the group's revenue in a jurisdiction is less than or equal to €10 million; and if (ii) the profit before tax in that jurisdiction is less than or equal to €1 million. Both magnitudes will be obtained from the Country-by-Country Report prepared in accordance with the standards and guidelines published by the OECD (Qualified Country-by-Country Report).

   - Simplified effective tax rate test: met if the simplified effective tax rate in the jurisdiction is equal to or higher than the transitional rates of 15% for 2024, 16% for 2025 and 17% for 2026. The simplified effective tax rate is obtained by dividing the Simplified Covered Taxes

(i.e., mainly, Corporate Income Tax) recorded in the entities' financial statements by the profit before tax obtained from the Qualifying Country-by-Country Report.

- Routine profits test: will be met if the profit (or loss) before income tax in a jurisdiction is less than or equal to the amount of the substance- based income exclusion. In simplified form, SBIE will be calculated by multiplying the salary expenses and the net value of tangible assets in a jurisdiction by the coefficients provided for each of these items in 2024, 2025 and 2026 (in accordance with the provisions of the Second Transitional Provision of the Law)

  By application of this test, where the group makes a net loss in a jurisdiction, it will not have to pay tax in that jurisdiction.

If in any tax period none of the above tests are met, the "safe harbour" system cannot be applied in that jurisdiction in any subsequent tax period, and the second set of calculations set out below will need to be used.

b. **For financial years starting from 2026 (or in cases where conditions to apply the transitional "safe harbours" 2024 and 2026 are not met)**:

The TUT arises when the effective tax rate ("**ETR**") of the constituent entities of a group in a jurisdiction is lower than the minimum rate of 15%.

The ETR of a jurisdiction will be the result of dividing the adjusted covered taxes by the net income or loss (“**GloBE Income or loss**”) of the constituent entities located in that jurisdiction (as a percentage and rounded to 4 decimal places):

$$\textbf{ETR} = \frac{\text{Adjusted Covered Taxes}}{\text{GloBE Income or loss}}$$

For the purpose of determining the **GloBE Income or loss**, the accounting result of the constituent entities shall be taken as the starting point, to which certain adjustments shall be made for the following items:

- Net tax expense.
- Excluded dividends (for holdings of 10% or more or held for more than one year).
- Excluded equity gains or losses.
- Included revaluation method gains or losses.
- Gains or losses arising from the disposal of certain excluded assets and liabilities (Article 37 of the Law).
- Asymmetric foreign currency gains or losses.
- Policy disallowed expenses.
- Prior years errors and changes in accounting principles.
- Accrued pension expense.

The **adjusted covered taxes** are determined on the basis of the Corporate Income Tax expense (or similar tax) recognised in the profit and loss account, to which certain adjustments must be made, including the following:

- The recalculation of deferred tax income and expenses associated with temporary differences and tax loss carryforwards, the generation and application of which must be calculated at 15%.
- Qualified refundable tax credits (i.e. certain tax credits that must be paid as cash or cash equivalents) are not considered as a decrease in covered taxes, but as an increase in the GloBE income.
- The deferred expense or income corresponding to the generation and use of tax credits is not included in the calculation, unless the 1st Transitional Provision of the Law is applicable to tax credits generated in years prior to its entry into force.

Once this calculation has been made, if the ETR is higher than the overall minimum rate of 15%, no TUT will arise. On the other hand, if the ETR is lower than the minimum rate, **a TUT rate will arise**, amounting to the difference between 15% and the ETR.

This TUT rate will have to be applied to the amount of GloBE net income adjusted by the substance-based income exclusion, in accordance with the coefficients applicable to eligible salary expenses and the net value of tangible assets for each financial year (as provided for by Article 14 and the 2nd Transitional Provision of the Law). From this operation, the **TUT** payable for each jurisdiction will be obtained.

2. Modalities, declaration and payment of the tax

The configuration of the TUT is based on three modalities, in the following order:

a. First, the Domestic Minimum Top-up-Tax (“**DMTT**”), which is the result of applying the above rules to all Spanish constituent entities of groups subject to Pillar 2.

b. Secondly, the primary TUT, which derives from the application of the so-called "income inclusion rule" ("**IIR**"). This is applied by ultimate or intermediate parent companies of groups resident in Spain in respect of income obtained by the constituent entities in which they participate, which are based in a jurisdiction other than Spain. The tax, if any, calculated in this way will represent the percentage share of such parent companies in the eligible profits of the constituent entities in which they have an interest.

   This modality provides for rules for the elimination of double taxation where such constituent entities have been subject to a DMTT.

c. Third, the **secondary TUT**, which derives from the application of the under-taxed profits rule ("**UTPR**") by Spanish resident constituent entities belonging to a multinational group whose income is not taxed by a DMTT or by a primary TUT in another jurisdiction.

   This closing rule, which is highly controversial and difficult to control in practice, means that Spanish-based subsidiaries of multinational groups may have to collect a TUT from their parent companies or other constituent entities of the group on income obtained outside Spain.

   This problem explains why the UTPR rule will not enter into force in Spain until 1 January 2025, and even until 1 January 2026, when the ultimate parent company in question was subject to a corporate income tax at a nominal rate of at least 20%.

The Law establishes the obligation to file an **information return** for all constituent entities based in Spain that are part of a group subject to the TUT. However, they will be released from this obligation when the ultimate parent of the group resides in Spain or when the multinational group complies with the obligation to file the information return in another jurisdiction that has an admissible information exchange agreement with Spain (in this case, it will be sufficient to identify the entity that has complied with the information).

Pending on the regulatory development, the minimum content of the information return will be the following: (i) the identification and jurisdiction of the constituent entities, (ii) the structure of the group, the entities excluded and any changes in the composition of the group, (iii) the ETR calculation method and, finally, (iv) the options exercised by the group.

A different reporting period is foreseen for the transitional period (i.e. the period of first application of the TUT for the group) and for subsequent years:

a. **For the transitional period**: the return must be filed by the last day of the 18th month following the end of the first tax period in which the TUT is applicable. Therefore, for large groups subject from the outset to this tax whose fiscal year is the calendar year, the first filing deadline will be 30 June 2026.

b. **For subsequent years**: the return must be filed before the last day of the 15th month following the end of the fiscal year.

A specific issue in Spain is that there will be only one entity acting as a substitute for the other Spanish entities of the group, which will have to pay all the group's tax liability in Spain. Apart from that, this entity will have the burden to maintain the relationship with the tax authorities in the name of all the Spanish constituent entities. This substitute entity will be the ultimate parent of the group if it is resident in Spain or, if not, any other Spanish constituent entity that has the highest net asset value among all the Spanish entities. The rest of the Spanish constituent entities are jointly and severally liable for the tax debt.

An **exemption** from TUT for the first 5 tax periods is provided for both **domestic groups** and **groups that are in the initial phase of their international activity** (i.e. those whose constituent entities are located in no more than six different jurisdictions and where the sum of the net book value of the tangible assets of all the constituent entities of the multinational group located in jurisdictions other than the most relevant jurisdiction does not exceed EUR 50 million).

3. Points of special attention

The new tax will have a significant impact on all affected groups and it is therefore advisable to start assessing this impact and preparing estimates as soon as possible. In addition to the above, there are some areas of interest to which special attention should be paid:

a. **The accounting and reporting systems** of the groups should be **reviewed** so that they can perform the calculations efficiently and without errors. In view of the fact that the information returns contain a large amount of data, the **severe sanctioning regime** established by the Law deserves special attention.

b. In the case of **Spanish subsidiaries** of multinational groups **whose parent companies reside in jurisdictions that have not implemented Pillar 2 rules** (e.g. the United States, China or Mexico), the progress of negotiations with these countries and their legislative processes will have to be monitored in order to be prepared for the application of the secondary TUT in 2026.

c. **Spanish ultimate or intermediate parents** should multiply their efforts to apply the primary TUT in respect of their subsidiaries located in jurisdictions that have not implemented Pillar 2 rules.

d. With regard to **joint ventures and entities with minority shareholdings** (**"MOCEs"**), the Law provides for certain special rules that may have an impact on minority shareholders. It will therefore be advisable to pay attention to share purchase and partnership agreements entered into after the entry into force of the Law.

e. The integration of Pillar 2 into our legal system will probably have a tax impact for **the Canary Islands Special Zone, foral regimes of Basque Country and Navarre and for tax credits** (e.g. deductions for R&D&I or film productions).

f. In relation to **investment funds and SOCIMIs**, a review of their structures will be necessary to determine their possible exclusion from the TUT or, where appropriate, alternative calculations.

g. Finally, it will be advisable to analyze and anticipate the impacts of Pillar 2 in relation to **impairments of shareholdings and tax losses on liquidation of subsidiaries**.

4. Other amendments

The law includes amendments to Royal Decree 1514/2007, of 16 November, approving the General Accounting Plan and Royal Decree 1159/2010, of 17 September, approving the Rules for the Preparation of Consolidated Annual Accounts and amending the General Accounting Plan approved by Royal Decree 1514/2007, of 16 November, and the General Accounting Plan for Small and Medium-sized Companies approved by Royal Decree 1515/2007, of 16 November.

These amendments provide for a **mandatory temporary exemption from the recognition and disclosure in the notes to the financial statements of deferred tax assets and liabilities** arising from the implementation of the new TUT. This exemption had already been recognised by the ICAC in its resolution published in BOICAC 136 of December 2023.

Finally, an amendment is introduced to Law 58/2003 of 17 December 2003 on the **duration of tax audits**. Specifically, it stipulates that the term of the inspection proceedings when the purpose of the procedure is the verification or investigation of the TUT will, in any case, be 27 months.

More information:

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