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The Supreme Court has settled a new cassation appeal (in a judgment rendered on May 20, 2016) concerning a leveraged intragroup purchase transaction in which the inspectors had found fraudulent evasion of the law. The importance of this judgment lies in the court's departure from what had been the most common line of reasoning in earlier precedents, by setting aside a finding of fraudulent evasion of the law on the basis that the inspectors did not sufficiently support or evidence that tax reasons had been the only determining factors for performing the transactions at issue.

On this occasion, the acquisition of the subsidiary had taken place in stages (a first portion in a sale and purchase transaction and a second portion, two years later, in a sale and purchase transaction and nonmonetary contribution); the sale and purchase transactions had been financed with loans provided by banking institutions outside the group. The inspectors did not question the economic reasons for the acquisitions but focused on the company's indebtedness; and, as the court underlined, in this case the financing also happened to come from a source outside the group.

The judgment also contains an important determination in relation to goodwill amortization in connection with the acquisitions performed in this reorganization. According to the inspectors, goodwill could not be disclosed on an intragroup transaction.

The Supreme Court rejected this analysis and affirmed, with reference to an earlier judgment on June 24, 2013, that (i) the principles governing consolidation for accounting purposes are not transferable without any adjustments to the tax field; and (ii) article 12.5 of the former corporate income tax law (TRLIS), relating to the deduction of goodwill, prevails, there being no provision restricting its application in intragroup acquisitions, so the inspector's view is tantamount to hollowing out that article.

01 JUDGMENTS

1.1 Corporate income tax.- A transaction cannot be held as a fraudulent evasion of the law where the absence of economic reasons has not been evidenced (Supreme Court. Judgment of May 20, 2016)

As explained briefly in the introduction, the Supreme Court has settled a new cassation appeal concerning a leveraged intragroup purchase transaction in which fraudulent evasion of the law had been found by the inspectors. The primary significance of this judgment is that it sets aside the finding of fraudulent evasion of the law because the authorities did not support or evidence that it was an artificial arrangement. Therefore, the interest on the finance (outside the group in this case) was held to be deductible.

It also concluded that the goodwill that arose on the transaction was deductible. Firstly, it disallowed the argument that its deduction could be questioned on the basis of the finding of fraudulent evasion of the law, because the inspectors had not included the goodwill in that finding. And it also affirmed that separately from the accounting legislation, tax law allows that deduction, without disallowing it cases of in intragroup acquisitions.

1.2 Corporate income tax.- The transfer of tax groups without any interruption does not affect the holding obligation for the target of the reinvestment (Supreme Court. Judgment of April 27, 2016)

Entity A, parent company of a tax group, took a tax credit for reinvestment, in which its reinvestment obligation was performed in shares in another entity, entity B. Following an exchange, that parent company, entity A, came to be owned by a newly created company, entity C, which caused the disbanding of the tax group and the creation of a new one with the same entities as before plus entity C as the new parent company. Later, following the sale of entity A's investment in entity B to entity C, the new parent company, a merger was performed in which entity B (in which the reinvestment obligation had been performed) absorbed entity C.

The tax authorities concluded that this reorganization entailed a breach of the requirement to hold the investment by the disbanded tax group. It underlined that the acquired shares (in entity B) had been transferred to an entity outside the tax group (which had the obligation to reinvest) and, additionally, the acquired entity B itself later absorbed entity C.

The taxpayer asserted, and the Supreme Court accepted, that:

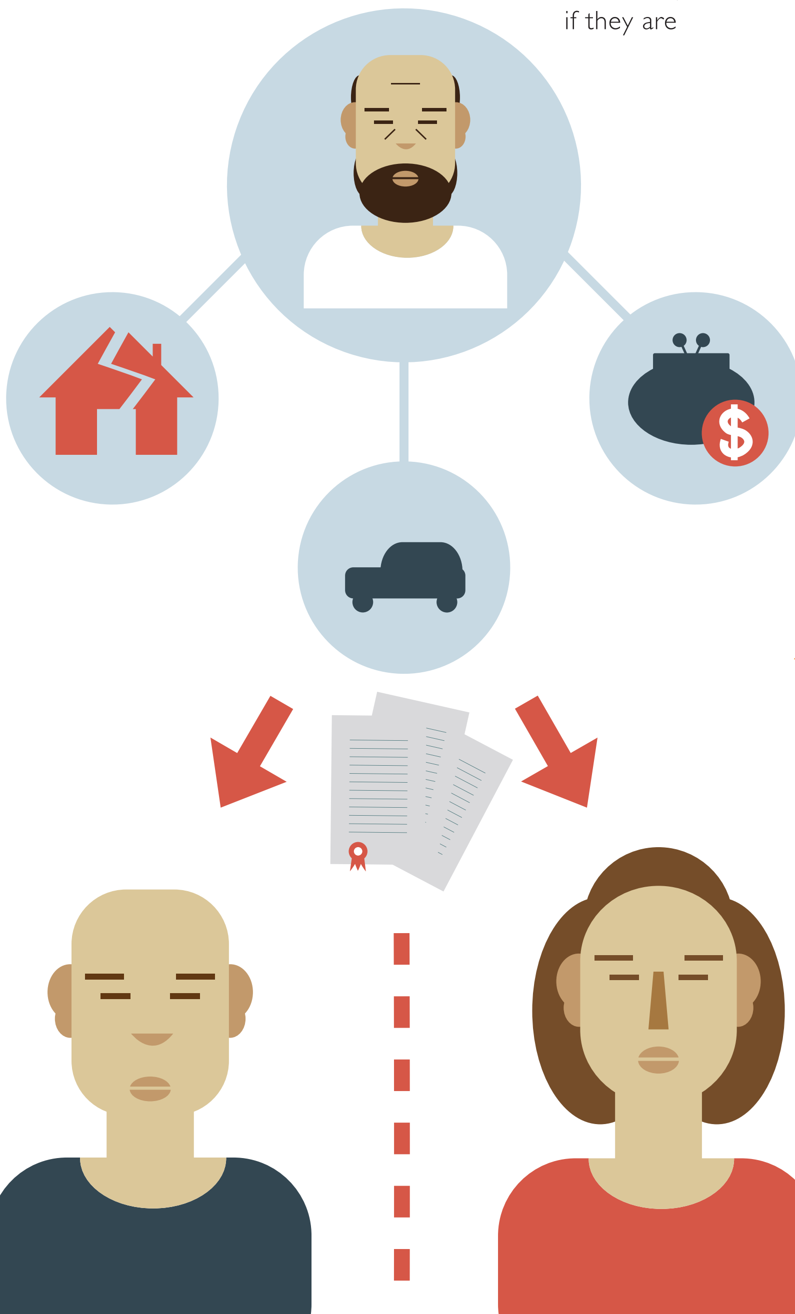
- The exchange gives rise to the disbanding of a tax group and the creation of another without any interruption; this allows what is known as an "intercommunication between groups" to take place. Among other effects, it allows the holding requirement to be considered to be transferred from one group to another.

- The fact that the shares in which the reinvestment was made (in entity B) are transferred by the original investor (entity A and parent of the disbanded group) to the new parent company (entity C) cannot be considered, therefore, as a breach of the holding requirement.

- Similarly, the later merger does not entail a breach of that holding requirement if there is a reinvestment replacing it, which is the case. In other words, the performance of a merger which makes the shares of the absorbed company (entity C) disappear from the equity of the absorbing company (entity B) does not entail a breach of the holding requirement in that the obligation must be considered to be performed with the assets of the absorbed company which replace the shares that disappear by reason of the merger.

1.3 Inheritance and gift tax.- An exemption is contrary to the free movement of capital if it entails tax differences according to where the heir is permanently resident (Court of Justice of the European Union. Judgment of May 26, 2016, case C-244/15)

Greek tax law provides an exemption from inheritance tax for the transfer through inheritance of land and buildings to the spouse or children, whether Greek or from another member state, if they are permanently resident in Greece. In view of that legislation and following unproductive discussions in an earlier administrative procedure, the European Commission brought action at the CJEU because it believed that legislation could be contrary to the free movement of capital.



The CJEU confirmed that the Greek legislation was indeed contrary to the free movement of capital on the basis of the following points:

(i) The legislation has the effect of reducing the value of the estate for the heir who is not permanently resident in Greece, by depriving them of the exemption from inheritance tax and thereby resulting in that person having a heavier tax burden than that borne by an heir who is permanently resident in Greece.

(ii) There is no objective difference between them such as to justify a difference in treatment between heirs who are permanently resident in Greece and heirs not satisfying that requirement, even though both types of heirs are in an objectively comparable situation.

(iii) The measure cannot be objectively justified by an overriding reason in the public interest.

1.4 Inheritance and gift tax.- The family business reduction applies even if the person receiving the income in respect of management functions does not hold shares (Supreme Court. Judgment of May 26, 2016)

In the examined case, shares in a company were received by inheritance, and the family business reduction for inheritance tax purposes was taken. To qualify for this reduction, the shares must be exempt from wealth tax. Among the requirements for the exemption, one of the members of the family group must perform management functions at the company, and receive the largest part of their income from the company. In this case, the heir who had been performing those functions did not own shares in the company before the decedent passed away, for which

reason the tax authorities disallowed that heir's right to the reduction. Later, however, Galicia High Court supported the opposite view, namely, that the reduction was applicable.

The Supreme Court confirmed in this judgment that the reduction is applicable in these cases. After first acknowledging that the determinations of the high courts had not been uniform on the subject, it drew that conclusion from the fact that the law does not require the taxable person performing the management functions to own shares when the tax accrues, since the shares can belong to the family group as a whole.

1.5 Inspection procedure.- Official notices of findings issued after the term for the length of proceedings has ended must meet minimum requirements to toll the statute of limitations period (Supreme Court. Judgment of May 23, 2016)

The lower court had held that the tax authorities' right to assess the tax debt had become statute-barred because the inspection work had lasted longer than 12 months.

The tax authorities lodged a cassation appeal arguing that, after the end of that 12 month term, an official notice of findings had been issued which, in the tax authorities' view could validly toll the statute of limitations period. The government lawyer supported this argument by asserting that, pursuant to art. 150.2.a) of the General Taxation Law (LGT), after that term has ended, any later steps, even if not the final assessment, can also toll the statute of limitations period. In particular, the government said that:

a) Article 150.2 states that a failure to comply with the term for the length of the proceeding does not determine that the right to continue has lapsed, and therefore it will continue until it has ended.

b) Among the consequences of that failure, letter a) of the same article 150.2) sets out that the statute of limitations period will not be considered to be tolled as a result of the work carried out until the unjustified tolling of the proceedings; though it adds that in these cases the statute of limitations period will be considered to be tolled if the inspection work is resumed with formal notification to the taxable person or if work is performed after the end of that 12 month term. In these cases, the person with tax obligations has the right to be informed about the items and periods on which the new work will be carried out.

The taxpayer objected to this, using the following arguments:

a) It cannot be presumed that article 150.2 of the General Taxation Law allows any official notice of finding or work by the inspectors that occurs after the end of term for the length of inspection proceedings to have tolling effects.

b) The General Taxation Law (LGT) lays down a number of conditions: the person with tax obligations must be notified that the official notice of findings was issued after the end of the term and of the items and tax periods which may continue to be audited thereafter..

All the taxpayer's arguments were adopted by the Supreme Court.

1.6 Revenue procedure – The amounts reported and paid over in respect of other taxes cannot be taken from the base for calculating the late filing surcharge (National Appellate Court. Judgment of February 10, 2016)

The taxpayer was a professional providing services to a company at which he was the sole director, a company providing services to other entities.

In relation to the receipt of income through professional companies providing services to third parties, the tax authorities published a memo (Memo from the Department of Financial and Tax Inspections, dated March 26, 2009, entitled "Inspection Work in relation to Taxpayers Providing Professional Services") in which it considered that structures such as the one described could be an evasion mechanism.

Taking heed of that memo, the taxpayer decided to make a self-correction. Therefore:

a) he filed additional personal income tax returns, recognizing the revenues directly obtained by the company; and

b) he filed a request for a refund of incorrect payments in respect of the tax the company had paid.

As a result of this self-correction, surcharges were levied for the late filing of personal income tax returns. In the taxpayer's opinion, the amounts that had been reported and paid over by the professional company in its corporate income tax return should not be included in the base used to calculate the surcharges (in other words, it should be in line with the actual economic loss sustained by the public purse).

Secondarily, the taxpayer asserted that there was no justification for claiming the surcharge insofar as the additional personal income tax returns were not filed spontaneously, but rather were induced by the memo published by the tax authorities. In other words, the existence of that memo works as a "prior demand" which makes the surcharge levied by the tax authorities inapplicable.

The National Appellate Court disallowed the taxpayer's claims:

a) Firstly, it disallowed the reduction to the base for the surcharges because there are two separate taxable persons. Therefore, the amounts paid over in respect of corporate income tax cannot be used to reduce the amount of the surcharge for the late filing of a personal income tax return.

b) As for the second petition, although the term "prior demand" must be construed broadly, according to the court, an informative memo cannot be allowed to be considered as such.

1.7 Penalty procedure.- The penalties imposed in the reassessment of a nonmonetary contribution that benefitted from the neutrality rules (Supreme Court. Judgment of May 23, 2016)

The entity made a nonmonetary contribution of assets. The inspectors considered that the neutrality regime was not applicable for two reasons: (i) because the contribution included debts which had not been expressly acquired to finance the contributed assets; and (ii) because the entity did not evidence the valid economic reasons for the contribution, and the examined documents substantiated that the entity's position after the contribution was no different from the position it was in before (in other words, there was no restructuring or rationalization of the business).

Besides issuing the assessment decision concerned, the inspectors initiated a penalty proceeding, justified by the existence of a view adopted repeatedly by the DGT (which the entity must have been aware of) that the contribution of assets together with debts not expressly acquired to finance the acquisition of those assets determines that the special regime cannot be taken for the transaction.

The National Appellate Court confirmed the assessment decision but set aside the penalty for the reason that the neutrality regime is a complex system in relation to which interpretation work is especially important, and additionally, because information had not been concealed from the tax authorities.

The Supreme Court, however, concluded that the penalty was justified. In particular, it affirmed that:

- The penalty was levied for a minor infringement, and therefore the aggravating factor of concealment had not been applied. Therefore, the penalty cannot be set aside on the ground that the concealment did not take place.

- Moreover, the tax authorities had provided extensive and thorough justification for considering that the neutrality regime could not be allowed on the basis of a reasonable interpretation of the applicable law and that there were no valid economic reasons. And, according to the court, all of the above reasons justify the penalty because it is sufficiently founded and the asserted ground is valid for levying the penalty (basically, the view repeatedly adopted by the DGT in relation to similar transactions).

1.8 Judicial review procedure.- The judgment may be rendered by a judge other than the one that initiated the proceeding and heard the evidence stage where there is no trial (Supreme Court. Judgment of April 27, 2016)

In the judgment of April 27, 2016 summarized above, the Supreme Court raised an important procedural issue: The rapporteur at the start of the proceeding, with whom the evidence period started, who admitted the evidence and was present at the replies and explanations given by the expert, did not later take part in the deliberation and vote on the lower court's judgment.

The appellant pleaded a number of articles requiring the judgment to be rendered by the judges attending the trial, and therefore, if that is not possible, a new trial must be held presided by the substitute judge. Otherwise, the proceedings must be held null and void as a matter of law. Against this, the government lawyer pleaded that those articles referred to cases in which there is a trial, which has not occurred in this proceeding, in which the conclusions were submitted in writing.

The Supreme Court confirmed this latter view.

The court added, in relation to the procedural duty of the court "*to notify the parties of the members of the Panel or of the Chamber that is to decide on the lawsuit or case*", that in this case the parties were notified of the designation of a new rapporteur for the judgment, against which no appeal was lodged, which is further justification for setting aside the pleaded ground.

1.9 Judicial review procedure.- The person who acquired the obligation to pay a tax may have standing to contest (Madrid High Court. Judgment of December 22, 2015)

The Company had become bound by contract to pay the tax on the increase in urban land value (IIVTNU) in a sale and purchase transaction for buildings in which it acted as the purchaser. It must be remembered that, under Spanish tax law, the taxable person for this tax is the transferor of the urban building, not the purchaser.

Following discrepancies between the tax authorities and the Company after an assessment had been issued for that tax, the Company initiated a proceeding, in which its standing to contest the assessment was denied because it was not the taxable person for the tax.

Against this decision, Madrid High Court concluded that the person ultimately responsible for the payment of the tax (even if under a contract with

the taxable person) has standing to contest the administrative decision, if the setting aside of that decision would have a positive effect on it or avoid an identified loss to it (from which it may be surmised that it has a legitimate and direct interest in the subject-matter of the appeal).

02 DECISIONS AND RULING

2.1 Corporate income tax.- Recovery of the depreciation or amortization expense not deducted in 2013 and 2014 where assets are transferred or retired in 2015 or after (Directorate-General for Taxes. Ruling V1864-16, of April 27, 2016)

Article 7 of Law 16/2012 placed a limit on the depreciation or amortization expense in respect of property plant and equipment, intangibles and real estate investments that were deductible for corporate income tax purposes in the tax periods commenced in 2013 and 2014.

Any such depreciation or amortization expense for accounting purposes that is prevented from being deducted by that limit may be deducted on straight-line basis over ten years or, as an alternative option, over the useful life of the asset, starting in the first tax period that begins in 2015.

According to the DGT, where assets are transferred or retired, the way the nondeductible depreciation or amortization expense can be recovered will differ according to the chosen option:

a) If straight-line deduction over a 10-year period has been elected and in that period the item leaves the company's assets (by being transferred or retired from the inventory), any book depreciation or amortization expense that was determined not to be deductible and remains to be deducted may continue to be deducted on a straight-line basis over that 10-year period.

b) If deduction over the asset's useful life has been chosen and in that period the asset leaves the company's assets by being transferred or retired from the inventory, any book depreciation or amortization expense that was determined not to be deductible and remains to be deducted may be deducted in full in the period in which the asset is transferred or retired.

2.2 Corporate income tax.- Any excess withholding borne over and above the amount provided in the tax treaty may not be treated as a tax-deductible expense (Directorate-General for Taxes. Ruling V1637-16, of April 14, 2016)

A Spanish company, which carries on its business in Costa Rica, receives income from royalties from which the payer withholds 15%, which is higher than the 10% rate under the Spain-Costa Rica tax treaty.

The DGT concluded that neither Spanish domestic law nor the tax treaty allow more than 10% to be deducted, given that the excess up to 15% is an imposition not in accord with the provisions in the treaty.

This excess cannot be treated as a tax-deductible expense either, for the same reason.

2.3 Corporate income tax.- There may be valid economic reasons in the nonmonetary contribution of a portfolio by individuals followed by the sale of the interest in the beneficiary entity of the contribution (Directorate-General for Taxes. Rulings V1468-16, of April 7, 2016, and V1506-16, of April 12, 2016)

The DGT has issued two rulings on similar scenarios. In ruling V1506-16, the request concerned two individuals who, to restructure their assets, are going to make a nonmonetary contribution of their shares in a number of entities to a newly created company. In ruling V1468-16, the DGT examined the nonmonetary contribution of shares by an individual to an entity which already has real estate assets and which operates an agricultural/livestock property.

In relation to these operations, it was asked (i) whether the tax neutrality regime could be applied and (ii) whether any potential income generated in the event of a subsequent transfer of the shares received by the beneficiary company of the contribution may benefit from the corporate income tax exemption regime.

The DGT confirmed that:

a) The restructuring transaction satisfies, in principle, the requirements to apply the regime.

b) If, however, that restructuring is performed with the aim to sell the shares contributed by the recipient entity, it could alter the above conclusions if that later transfer took place under a more beneficial tax regime than for the direct transfer of the shares by the current shareholders.

c) Otherwise, that is, if that aim does not take place, the potential later transfer of the shares by the beneficiary of the contribution will be eligible for the exemption under the corporate income tax legislation (the tax regime applicable at the time of the transfer must be observed in all cases).

2.4 Corporate income tax.- The finance costs derived from debt for the distribution of dividends are deductible (Directorate-General for Taxes. Ruling V1486-16, of April 8, 2016)

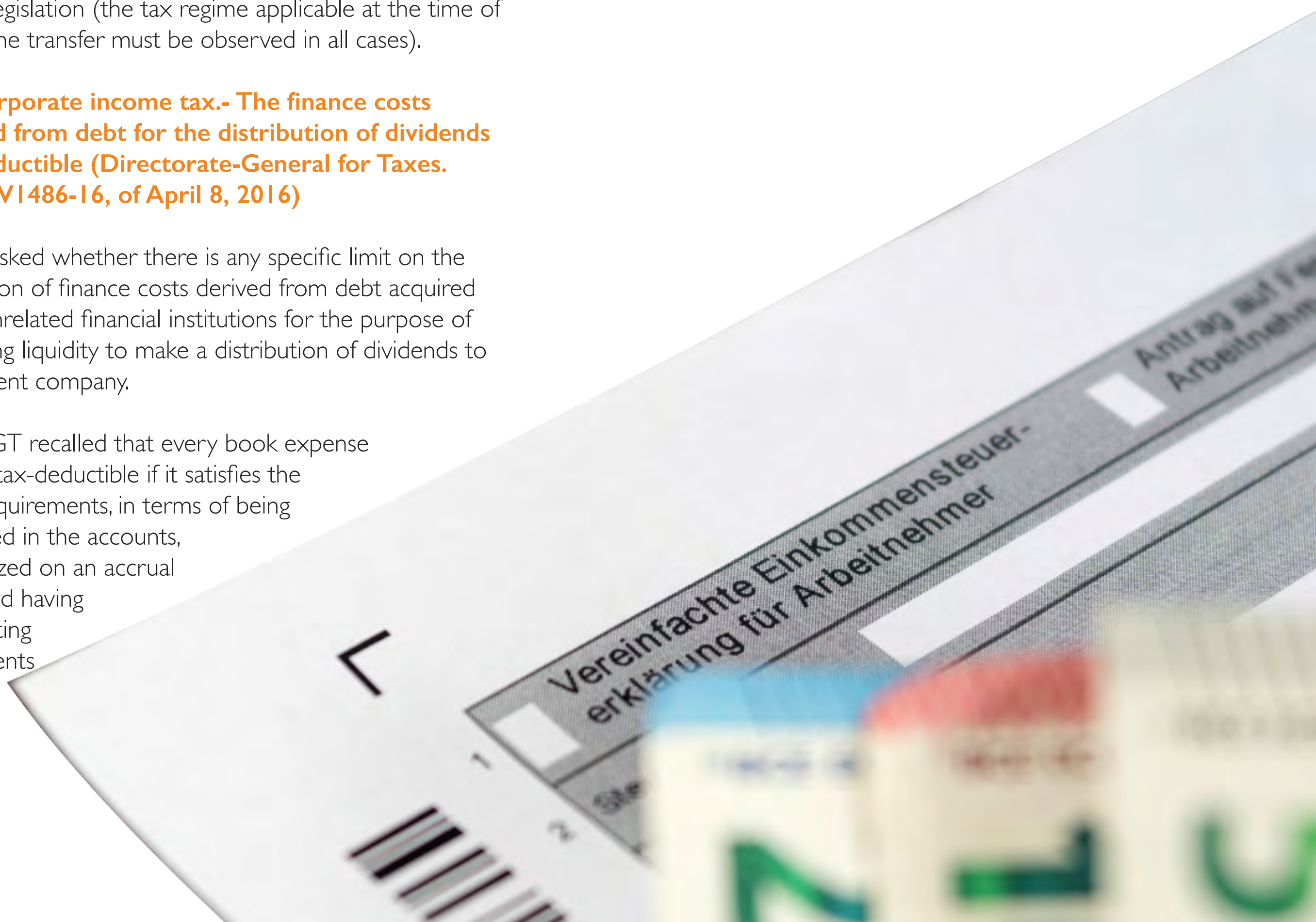
It was asked whether there is any specific limit on the deduction of finance costs derived from debt acquired from unrelated financial institutions for the purpose of obtaining liquidity to make a distribution of dividends to the parent company.

The DGT recalled that every book expense will be tax-deductible if it satisfies the legal requirements, in terms of being recorded in the accounts, recognized on an accrual basis and having supporting documents and provided it does not qualify as a non-tax deductible expense under any specific rule provided in the law.

Therefore, finance costs will be tax-deductible if they satisfy the general requirements for their deduction referred to above, but are also subject to the limit contained in article 16 of the Corporate Income Tax Law (LIS) for the deduction of expenses of this type (30% of operating income). In the cases of entities taxed under the consolidated tax group rules, the limit on the deduction of finance costs refers to the tax group.

2.5 Corporate income tax.- Various questions concerning the deduction of gift and entertainment expenses in tax groups (Directorate-General for Taxes. Ruling V1474-16, of April 7, 2016).

The current Corporate Income Tax Law contains a new rule on the deduction of gift and entertainment expenses related to customers and suppliers, under which these types of expenses will be deductible up to a limit amounting to 1% of the net revenues in the tax period. The DGT replied to various questions about the application of this rule:



a) Whether, for tax groups, that limit must be calculated by reference to the individual net revenues figure or the figure for the group as a whole. The DGT concluded that the consolidated figure must be used.

b) Whether, in the transfer of an item used for public relations or customer entertainment purposes which gives rise to a loss, that limit applies. According to the DGT, that limit refers only to gift and entertainment expenses in relation to customers or suppliers and not to assets used for public relations or customer entertainment purposes, and therefore that limit is not applicable in these cases.

2.6 Corporate income tax.- Deduction of the costs derived from foreclosure on a mortgage for buildings delivered as security for a debt of a related company (Directorate-General for Taxes. Ruling V1464-16, of April 7, 2016)

In the case on which a ruling was requested, as security for a loan provided to an entity, a company related to that entity offered a building. An insolvency order was issued on the borrower and it entered into liquidation. Later, a notice of directions for foreclosure on a mortgage was served on the guarantor entity concerning the asset provided as security. It was asked in the ruling request whether the amount the guarantor company paid to the bank as a result of that court foreclosure is deductible for corporate income tax purposes (due to the inability to collect the loan from the borrower, a related company).

The DGT stated that:

a) The legislation in force in 2014 (when the foreclosure on the mortgage occurred) does not contain any specific rules on mortgage foreclosures, and therefore any expenses or revenues that this transaction might generate for accounting purposes will have full effects for tax purposes, without limitation to the treatment available for the debt between two related parties.

b) The ruling of March 1, 2013, by the Accounting and Audit Institute, issuing the rules on the recognition and measurement of property plant and equipment and of real estate investments provides that the retirement of an asset gives rise to the recognition of a gain or loss in respect of the difference between the fair value of the asset and its carrying amount.

c) It may be concluded from applying this method to the case under examination that the mortgage foreclosure will mean that the requesting entity must record the retirement of the building and recognize a gain or loss in respect of the difference between the fair value of the consideration received (in principle, equal to the amount of the receivable from the related party) and the carrying amount that is retired. After recording the receivable from the related party, the

requesting entity will determine the potential impairment or loss in respect of a confirmed bad debt according to the order for payment to creditors determined in the insolvency proceeding and, if required, record an expense in the income statement. An impairment loss on the receivable from the related company will be tax-deductible if that company is under an insolvency proceeding determined in an insolvency order by a court. That has happened in the case described, because the company is in liquidation.

2.7 Corporate income tax.- The timing of recognition for installment transactions cannot be applied to the income generated on a debt acquired at a discounted value (Directorate-General for Taxes. Ruling V1402-16, of April 5, 2016)

The requesting entity acquires promissory notes at a discount between 2015 and 2017. It was asked whether the method for installment transactions (set out in article 11.4 LIS, the current Corporate Income Tax Law), may be applied to a gain arising on the collection of the promissory notes. The DGT concluded, with a very questionable view, that:

a) The cash basis method cannot be applied to the described transaction, because the requesting entity is seen as the transferee of an asset (the promissory notes), not the transferor.

b) In this respect, installment or deferred payment transactions, as defined by article 11.4 of the Corporate Income Tax Law (LIS), are those in which all or part of the consideration is payable in successive payments or in a single payment, if the period that has run between when the last or single installment accrued and matured is longer than a year. The reference to "a consideration" necessarily implies a previous transfer, provision of a service or even an indemnification, which in turn entails or determines a "creditor" or "seller" position for the party receiving that consideration.

c) In the case described, the requesting entity acquires some promissory notes, in other words, it makes an acquisition, not a transfer.

2.8 Personal income tax.- Treatment of the amounts paid to the mortgage borrower in respect of the reversal of the collar clause (Directorate-General for Taxes. Rulings V2430-16 and 2431-16, of June 3, 2016)

An individual received in 2015 the excess interest collected by a financial institution as a result of applying a collar clause (*cláusula suelo*) in a mortgage. The amount was collected by enforcing the supreme court judgment of May 9, 2013, which rendered clauses of this type null and void. According to the DGT:

a) The decision rendering collar clauses null and void, effective for economic purposes on the publication date of the supreme court judgment, means that the clause will be considered not to exist from that date.

b) This means that the repayment to the requesting entity of the excess amounts paid as a result of applying that clause does not qualify as taxable income for personal income tax purposes.

c) If, however, those amounts had been included in the base for the tax credit for investment in a principal residence made by the taxpayer, the taxpayer will forfeit the right to take the credit in relation to those amounts, which will require the taxable person to self-correct its tax returns (in respect of the amounts incorrectly deducted for that reason from their net tax payable in fiscal year 2015, plus the related amount of late-payment interest).

2.9 Wealth tax.- For the family business exemption the income requirement must be met at the investee with respect to all the income that may be received from other entities which are not directly owned (Directorate-General for Taxes. Ruling V1406-16, of April 6, 2016)

The individual is sole shareholder at a holding company which in turn has two subsidiaries. At all three companies the individual performs management functions (at the holding company, as sole director, and at the subsidiaries as employee) and receives income for doing so.

The law determines that for the exemption from wealth tax for family businesses to apply the taxable person's income in respect of management functions at the company concerned must account for at least 50% of the sum total of their business income, professional fee income, and salary income. It was asked how that percentage must be calculated. The DGT:

a) recalled that the calculation must be made separately for each of the companies in which an investment is held, which are those that must be reported in the tax return;

b) affirmed therefore that to determine the percentage that the compensation in respect of the management functions performed at each company bears to the sum total of the salary and business income of the taxable person, the income derived from the management functions at the other companies at which the requirements for the exemption are satisfied must not be included (in the denominator);

c) concluded that, in this case, the income from the subsidiaries cannot be excluded from the denominator because the taxable person does not have investments in those companies (which could give rise to failure to satisfy the test to apply the exemption).

2.10 Inheritance and gift tax.- The obligation to be taxed as a nonresident taxpayer applies in relation to foreign securities held at financial institutions located in Spain (Directorate-General for Taxes. Ruling V1405-16, of April 6, 2016)

A U.S. resident inherited from her father, a Spanish national resident in Madrid, financial investments in company bonds and shares and investments in mutual funds held at a Madrid office of a financial institution. The financial investments are instruments issued by (nonresident) foreign companies listed on organized markets in countries outside Spain.

Considering that the inherited securities were not issued in Spain, in other words, that they can only be exercised in other countries (even though, circumstantially they are held at a bank's office located in Madrid), it was asked whether the heir is subject to inheritance tax in Spain (as a nonresident taxpayer).

The DGT:

a) recalled that taxpayers not having their principal residence in Spain are taxed as nonresident taxpayers, in other words, they are not taxed on the acquisition of all types of property, just on the property falling within any of the following scenarios:

- Acquisition of assets and rights which are located, may be exercised or have to be performed in Spain.

- Receipt of amounts derived from life insurance contracts where the contract was concluded with Spanish insurance companies.

- Receipt of amounts derived from life insurances contracts where the contract was concluded in Spain with foreign companies operating in Spain.

b) affirmed that, in the case described, what we have is financial investments held at the office in Spain of a bank. Therefore, according to the DGT, there is an obligation to be taxed in Spain in respect of those investments, because they are located in Spain. The DGT underlined in this respect that the fact of the financial investments being instruments issued by (nonresident) foreign companies listed on organized markets in countries outside Spain is irrelevant for the purposes of their being taxable; the important factor is that they are located in Spain, which is sufficient for them to be taxed as a nonresident taxpayer.

2.11 VAT. Provision of pro bono services (Directorate-General for Taxes. Ruling V0920-16 of March 10, 2016)

The company, engaged in providing fee-based legal services, set up a pro bono work program for advisory services to nonprofit institutions or organizations, providing free legal training services to underprivileged people with the intention to promote at institutional level the participation of its lawyers in outreach initiatives in the community in which it carries on its activity.

The DGT highlighted that, for VAT purposes, those services must be regarded as being aimed at promoting the firm (in that by providing them the firm is enhancing how it is perceived by public opinion generally) and as being addressed at the firm's professionals (allowing it to attract talented professionals with social awareness) which ultimately results in better achievement of the enterprise's own purposes. In other words, these pro bono services do not satisfy private needs, given that their aim, ultimately, is primarily to serve the enterprise's purposes.

As a result, it is within the bounds of the self-supply scenario contemplated in article 12.3 of Law 37/1992.

03 LEGISLATION

3.1 The voluntary payment period for the national and provincial tax charges on economic activities for fiscal year 2016

The Official State Gazette (BOE) for June 15, 2016 published the Decision of June 10, 2016, of the Revenue Department of AEAT (Spanish tax agency), amending the voluntary payment period for the tax on economic activities (IAE) bills for fiscal year 2016 in respect of the national and provincial charges and providing the place for payment of those charges.

The new period (for the national and provincial charges collected through the approved credit institutions) will fall between September 15 and November 21 2016, inclusive.

3.2 Changes in the management of appointments of representatives and in the registration and management of successions and of the legal representatives of minors and incapacitated persons for the performance online of formalities and steps at the tax agency

The Official State Gazette (BOE) of June 13, 2016 published the Decision of June 8, 2016, of the Directorate-General of AEAT, amending the decision of May 18, 2010, in relation to the registration and management of appointments of representatives and the registration and management of successions and of the legal representatives of minors and incapacitated persons for the performance online of formalities and steps at the tax agency.

3.3 Se aprueban los modelos del Impuesto sobre Sociedades y del Impuesto sobre la Renta de No Residentes del ejercicio 2015

The Official State Gazette (BOE) of June 7, 2016 published Order HAP/871/2016, of June 6, 2016 approving the corporate income tax and

nonresident income tax return forms for permanent establishments and for pass-through entities formed in other countries but with presence in Spain, for the tax periods commenced between January 1, 2015 and December 31, 2015. The order also approves the standard document for the specific reporting on controlled transactions of the entities satisfying the requirements in article 101 of Corporate Income Tax Law 27/2014, of November 27, 2014.

The order, which entered into force on July 1, 2016, carries out a general overhaul of the self-assessment forms to adapt them to the new corporate income tax law in force for fiscal years that commenced on or after January 1, 2015.

Despite that general overhaul of the forms, no significant changes were made to the following elements:

a) The customary forms for additional information and the requirements for filing them have been retained (for example, where book income or loss has fallen by €50,000 or more under the heading for "other adjustments to income or loss" or where the amount of certain credits is €50,000 or more).

b) The media on which the return can be filed and the filing and payment payments remain unchanged. Thus, the period will end, generally, on July 25 but will end on July 20 if the payment by direct deposit option is elected.

3.4 Aprobación y rectificación de diversos modelos de IVA

Article 5 of the Regulations implementing the tax exemptions relating to NATO, to that organization's international military bases and to the NATO member countries and setting out the procedure for applying them (approved by Royal Decree 160/2008, of February 8, 2008) defines the procedure for claiming those VAT exemptions for domestic and intra-Community transactions.

Order HAP/841/2016, of May 30, 2016:

a) Approved **form 364**, "VAT. Application for refund of input VAT relating to NATO, to the

organization's international military bases and to the NATO member countries".

b) Approved also **form 365**, "VAT. Application for prior acknowledgement of the exemptions relating to NATO, to the organization's international military bases and to the NATO member countries".

That order also amends Order EHA/789/2010, of March 16, 2010 approving **form 360**, input VAT refund application for traders and professionals established in Spanish VAT territory, the content of the refund application for traders or professionals not established in Spanish VAT territory, but established in the Canary Islands, Ceuta or Melilla communities, and **form 361**, VAT refund application for certain traders or professionals not established in Spanish VAT territory, or in the Canary Islands, Ceuta or Melilla communities, and setting out also the general conditions and the procedure for its remote filing.

Lastly, final provision two amends Order HAP/2194/2013, of November 22, 2013, on the procedures and general conditions for the filing of certain self-assessments, informative returns, business taxation status notification forms, communications and refund applications.

This is done for the purpose of extending generally the requirement for large enterprises to file electronically the documents, applications or notices of election which do not appear in the return or self-assessment forms and the tax relevant documents relating to tax proceedings handled by the tax agency through the agency's electronic register; and of enabling, through the appointment of a representative, the electronic filing of a single business taxation status notification form to be included on the register of parties with tax obligations, change of address and/or changes to personal data, form 030, prepared by both spouses.

3.5 Council Directive (EU) 2016/856 of 25 May 2016 on the common system of VAT, as regards the duration of the obligation to respect a minimum standard rate

Article 97 of Council Directive 2006/112/EC provided that from January 1, 2011 until December 31, 2015 the standard VAT rate could not be lower than 15%.

Following the entry into force of Council Directive 2016/856, effective on January 1, 2016, the term for the obligation to observe a 15% minimum standard rate has been extended until December 31, 2017.

04 MISCELLANEOUS

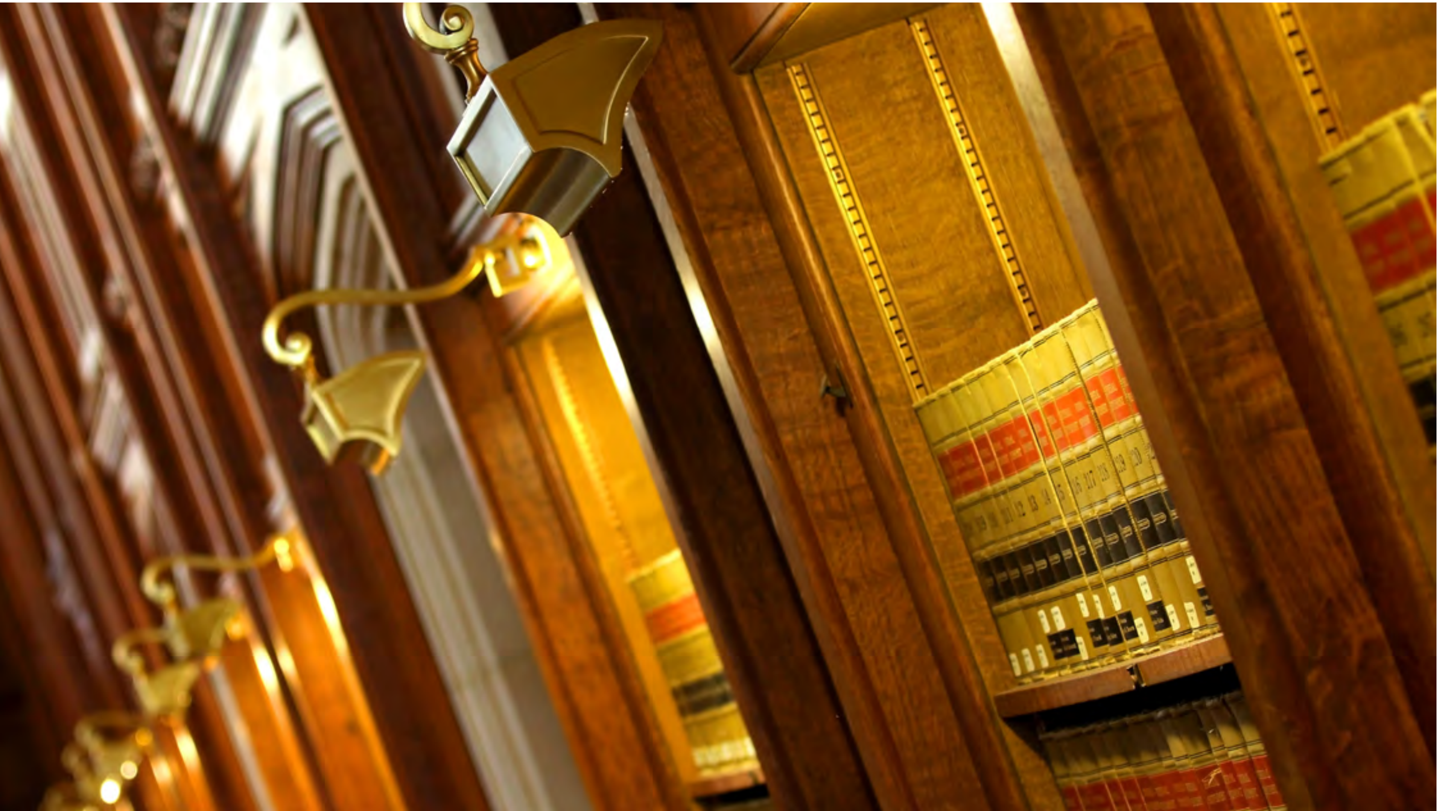
4.1 Proposal for a Council Directive against tax avoidance practices

On June 21 the EU's Economic and Financial Affairs Council (ECOFIN) made public the adoption of a political agreement on the proposal for a Council Directive laying down rules against tax avoidance practices that directly affect the functioning of the internal market (Anti-Tax Avoidance Directive or ATAD). Formal approval will take place at a forthcoming meeting of ECOFIN.

The primary objective of this Directive is to facilitate a more coherent EU approach to a number of anti-abuse measures recommended by the OECD (BEPS), and to add others (rules on exit taxation, for example) not specifically covered by the BEPS reports.

The directive provides other minimum standards (i.e. the member states may lay down stricter, but not more relaxed, rules) concerning the limit on the deduction of interest, exit taxes, the rules on international tax transparency and the provisions (simplified, in comparison with the BEPS project) on hybrid instruments and entities. It also lays down a general anti-abuse rule similar to the existing rule in the parent-subsidiary directive.

In Spain, the directive might require the amendment of some elements of the Corporate Income Tax Law which has already set a limit on the deduction



of finance costs and the tax on assets or companies relocated abroad. It could also have an impact on the rules on international tax transparency and on the need to limit the effect (double deduction or detaxation) linked to hybrid entities.

The directive will apply to all EU-resident companies, and to the permanent establishments in the EU of entities resident in third countries. Generally, its measures will come into force on January 1, 2019, although there are transitional provisions on exit taxation (January 1, 2020) or on the limits on the deduction of finance costs (any countries which, like Spain, already have rules in this respect, could defer adapting them to the directive until there is consensus over Action 4 of OECD BEPS Action Plan, for which the time limit ends on January 1, 2024).

4.2 Service tax on water and drainage services

The DGT issued a report on May 20, 2016 in relation to the taxes on the provision of water and drainage services, in particular, on the impact of the elimination (which came into force on March 6, 2011) of paragraph 2 of article 2.2.a) of the General Taxation Law, according to which, on defining the service or activity tax, it was considered that the services or activities were provided or carried on under the public law system where they were carried out in any of the forms provided in the administrative legislation for the management of the public service and they were owned by a public entity.

The DGT indicated that the view it had been adopting in this respect is that the elimination implied a return to the preexisting arrangement laid down by the Supreme Court (in judgments of July 2, 1999 and October 2, 2005) which determined a test to differentiate between a service or activity tax and a tariff in relation to the provision of local public services on the basis of the status of their management entity.

Under that test, if a local entity manages the public service directly it must charge a service tax and, conversely, if the entity managing the service is a municipal private company, or a private company

under an administrative management contract, the charges must be classed as revenues under private law.

4.3 The compensation received by directors in respect of non-management activities does not have to appear in the bylaws

The Official State Gazette (BOE) of June 6, 2016 published the Decision of May 10, 2016, of the Directorate General for Registries and the Notarial Profession (DGRN), on the appeal lodged against the refusal by the commercial and movable property registrar for Toledo to enter a deed of amendment to a company's bylaws.

It was stated in the deed, in relation to directors' compensation, that directors were not compensated for their services except in respect of "any work as an employee" carried out by the director. The commercial registrar refused to enter that description on the argument that the fact of a director being compensated for work as an employee to be performed at the company is contradictory with directors' services not being compensated, given that this work results, in any event, from her status as director.

The DGRN found in its decision on this issue that there is a distinction to be made between (i) compensation in respect of the functions attached to the office of director and (ii) compensation for functions not associated with that office.

In relation to the compensation system for functions attached to the office of director, which, in all cases, have to appear in the bylaws, it must be taken into account that these functions are not always identical, and a distinction must be made between four types of organizational structures for the management a company:

- A complex structure (collective body/board), in which case the functions attached to the office of director are reduced to the deliberative function, for which the compensation system must be set out in the bylaws. By contrast, their executive functions are not functions attached to the office of director as such, and therefore the associated compensation is not required to appear in the bylaws, but rather in the executive director agreement that must be signed between board meeting and director.

- Three simple structures (sole director, more than one director acting jointly or more than one director acting severally), in which case the functions attached to their office include all of their functions and especially their executive functions, and therefore the fact that they are compensated for their services and their compensation system must appear in the bylaws.

  Within the three types of simple structures, however, there may also be functions not associated with their office (which have nothing to do with the management and administration of the companies) which need not appear in the bylaws but rather simply in the relevant agreements. What must be included in all cases is their compensation under senior management employment contracts to the extent that the functions attached to that contract overlap with the functions attached to the office of director in managing bodies adopting any of these forms).

The DGRN therefore upheld the entity's appeal, by holding that the bylaw clause must be upheld (although its wording could have been clearer) which, while setting out that the office of director is not compensated (with the result that they will not receive compensation for their services as such) adds that compensation will be paid for other services.

4.4 Automatic exchange of country-by-country reports

Council Directive (EU) 2016/881 of 25 May 2016 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation was published in the Official Journal on June 3, 2016.

This directive implements the mandatory requirement for multinational groups to prepare country-by-country reports in relation to the transactions performed within those groups. This report must be communicated in an automatic exchange of information using the standard form on the CCN network.

Each member state must therefore adopt the necessary measures to require the ultimate parent entity of a multinational enterprise group (with consolidated group revenue equal to or higher than €750 million), having its residence for tax purposes in its territory, to file a country-by-country report for every fiscal year within twelve months from the last day of the fiscal year.

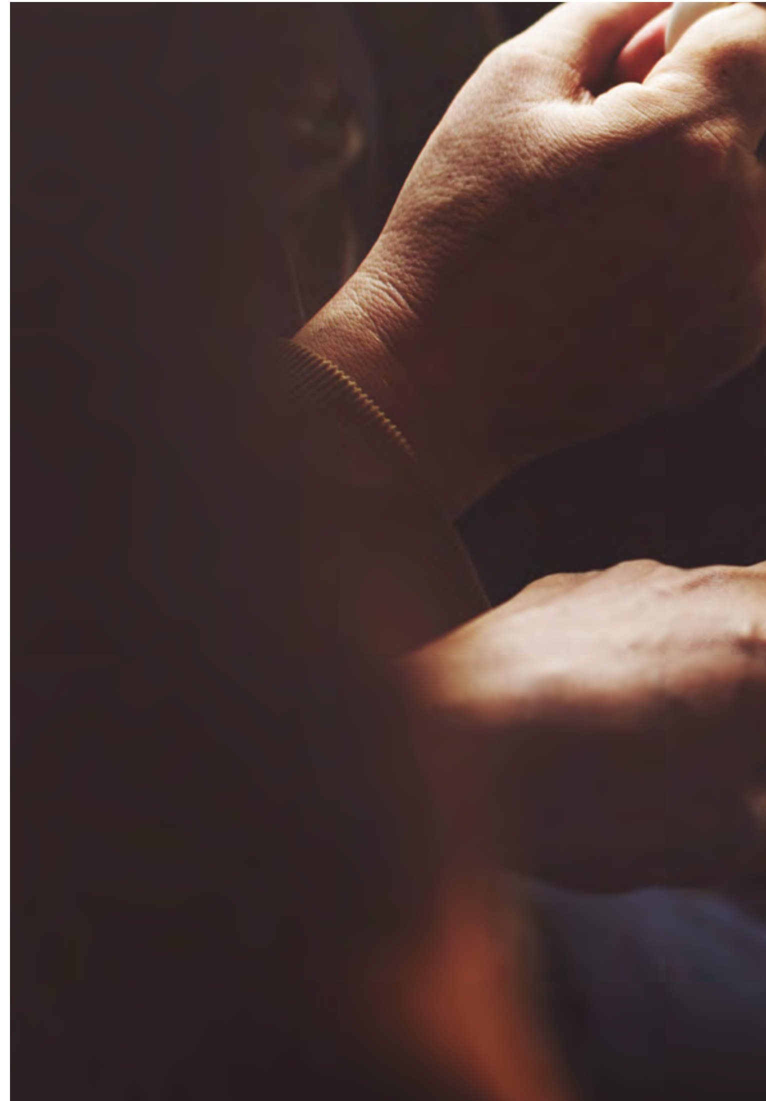
Groups may, however, designate any other entity in the group as their surrogate parent entities, and that entity will be the only substitute for the ultimate parent entity to file the country-by-country report in that entity's jurisdiction of tax residence, on behalf of the multinational enterprise group.

Additionally, where more than one entity in the multinational enterprise group are resident for tax purposes in a member state and one of the following conditions applies: (i) the ultimate parent entity is not required to file a country-by-country report in its jurisdiction of tax residence; (ii) the jurisdiction in which the ultimate parent entity is resident for tax purposes does not have a qualifying competent authority agreement in effect allowing the communication of the country-by-country report; or (iii) there has been a systematic failure of the jurisdiction of tax residence of the ultimate parent entity that has been notified by the member state to the group entities resident for tax purposes in that member state, the multinational enterprise group may designate one of those resident entities to file the country-by-country report.

Within fifteen months from the last day of the fiscal year of the multinational enterprise group to which the report relates, the competent authority of the member state where the country-by-country report was received must communicate the report to any other member state in which, on the basis of the information in the country-by-country report, one or more entities in the multinational enterprise group of the reporting entity are either resident for tax purposes or subject to tax with respect to the business carried out through a permanent establishment. The first country-by-country report to be communicated will be the report for the fiscal years that commence on or after January 1, 2016, which will be communicated within 18 months from the last day of the fiscal year.

The country-by-country report must contain the following information with respect to the multinational enterprise group:

a) Aggregate information relating to the amount of revenue, income (loss) before income tax, income tax paid, income tax accrued, stated capital, accumulated earnings, number of employees, and tangible assets (premises, plant and equipment) other than cash and cash equivalents with regard to each jurisdiction in which the multinational enterprise group operates.



b) An identification of each entity in the group, setting out the jurisdiction of tax residence of that entity and (where different from that jurisdiction of tax residence) the jurisdiction under the laws of which that entity is organized, and the nature of the main business activity of activities of that entity.

It determines that member states should lay down rules on penalties applicable to infringements of national provisions adopted pursuant to the directive, the terms of which came into force on June 4, 2016.

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