Tax Newsletter

Spain

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Contents

1. Tax on increase in urban land value: the tax cannot be collected on transactions performed before November 10, 2021

2. Judgments

2.1 Corporate income tax. – Request for ruling on unconstitutionality submitted by National Appellate Court in relation to Royal Decree-Law 3/2016 not admitted

2.2 Personal income tax. – Analysis of tax on severance pay for removal of chief executive officer

2.3 Transfer and stamp tax. – Charging transfer tax on radio spectrum concessions is precluded by European Union law

2.4 Transfer and stamp tax. – Sale of a supermarket is a transaction subject to stamp tax, even if not registered at the Movable Property Registry

2.5 Administrative procedure. – A jointly and severally liable party may challenge declaration of liability in a chain based on absence of declaration of default by main debtor

2.6 Management procedure / Tax on increase in urban land value. – Tax authorities are required to deliver decision on revocation of final tax assessments in procedure for refund of incorrectly paid tax

2.7 Audit procedure. - Territorial authority of audit bodies cannot be altered without sufficient substantiation of ground

2.8 Review procedure. – Determining amount of claim for lodging ordinary administrative appeal must be done by reference to assessment periods for the tax involved in the observed infringement

2.9 Review and collection procedures. – Tax authorities must refund cost of security requested to stay enforcement of a debt, if assessment is set aside in mutual agreement procedure

3. Decisions

3.1 Corporate income tax. – Tax credit for advertising and promotional expenses can only be used in the period the expenses were incurred

3.2 Personal income tax. – Complete adjustment principle requires tax authorities to refund withholding tax at their own initiative if they conclude that salary income is not taxable

3.3 Personal income tax. – Proof of married status of foreigners who cannot be registered at the Civil Registry can be provided by other means of evidence

3.4 Personal income tax. – Expenses relating to car-derived vans and pick-up type vehicles are deductible for determining net income from economic activity

3.5 Personal income tax. – Tax credit for rental of principal residence can be applied if proof is provided that rented property is renter's principal residence, even if lease agreement is apparently seasonal

3.6 Personal income tax. – Requirements for gain realized on gift of the family business not to be taxable must be fulfilled in year of the gift

3.7 Personal income tax. - Giving an asset in payment to discharge guarantee entered into with third party generates capital gain

3.8 Personal income tax. - Capital gain obtained from portion of deferred price recorded in promissory notes must be recognized in year it is discounted

3.9 Transfer and stamp tax. – Method based on net present value of estimated cash flows can only be used if expressly provided for in the legislation on the tax

3.10 Cadastral values. - The presumed truth of information on the real estate cadaster is rebuttable

3.11 Collection procedure. – Where a notice of attachment is challenged, the proceeding only has to include documents relating to the enforced collection period

4. Resolutions by the Directorate General for Taxes

4.1 Corporate income tax. – An asset is new where it is brought into operating condition for the first time

4.2 Corporate income tax. – Increase in average workforce is measured by reference to workers with equivalent degrees of disability

4.3 Corporate income tax. – Dividends giving entitlement to an exemption are not subject to withholding although a 5% reduction has to be made for management costs

4.4 Personal income tax. – DGT clarifies how to interpret new limits on reduction for contributions to pension and welfare programs

4.5 Wealth tax. – Principles for the valuation of entities that are neither listed nor audited

4.6 Wealth tax. – Taxable amount has to be increased or decreased by refunds or amounts to be paid in respect of personal income tax for the same fiscal year

4.7 Wealth tax. – Unrealized gains cannot give rise to deductible debts

4.8 Transfer and stamp tax. – Clarification of how the winding up of a company is taxed where its primary asset is a property

located in a different autonomous community to where it has its registered office

4.9 Electricity tax and tax on the value of electricity output. – Clarification of how solar self-supply services are taxed

5. Legislation

5.1 Aid for victims of violent crimes and for victims of gender violence declared exempt and amendments made to reserve for investment in the Canary Islands and Canary Islands general indirect tax

5.2 Approval of the trading values in the fourth quarter of 2021 for traded securities

5.3 Financial transactions tax and digital services tax included in the Basque Economic Accord and connecting factors defined for VAT purposes in distance transactions

1. Tax on increase in urban land value: the tax cannot be collected on transactions performed before November 10, 2021

A decision by the Directorate General for Taxes (DGT) examines the situation of real estate sale transactions performed between October 26 and November 10 2021 and concludes that the tax does not have to be paid in these cases.

A constitutional court judgment delivered on October 26, 2021 (published in the Official State Gazette -BOE- on November 25, 2021) held that certain articles of the legislation on the tax on increase in urban land value were unconstitutional and null and void, leaving a legal void in relation to determining the taxable amount which stood in the way of assessment, verification, collection and review of this local tax, and therefore, its enforceability (alert dated November 3, 2021).

That legal void was filled following the approval of Royal Decree-Law 26/2021, of November 8, 2021, adapting the revised Local Finances Law to the Constitutional Court's case law. That decree-law was published in the Official State Gazette (BOE) on November 9, 2021 and came into force on November 10, 2021 (alert dated November 9, 2021).

Since that judgment, high numbers of borderline situations have been emerging which are not being interpreted uniformly by the various local authorities and will have to be decided in the courts. Examples include:

(i) Transactions performed before the Constitutional Court's judgment was delivered (October 26, 2021), whereas their assessment or self-assessment periods fall after that date.

(ii) Transactions before October 26, 2021, assessed before then also, although their payment date occurs on a later date; or their payment date is earlier, but the payment was deferred or split at the taxpayer's request, and the periods for paying the debt end after that date.

(iii) Transactions performed between October 26, 2021 (date when the court's decision became known) and November 10, 2021 (date of the entry into force of the legislative amendment mentioned above).

In relation to this exact same scenario, the Directorate General for Taxes (DGT), in resolution V3074-21, dated December 7, 2021, examined the treatment of transactions performed up until November 10, 2021.

According to the DGT, these transactions have to be reported regardless, because the taxable event has occurred and the tax has become due.

It concluded, however, that in these cases there will be no debt to pay, consistently with the constitutional court judgment.

In line with those findings, a great many courts are now accepting that local authorities should treat as invalid any assessments or self-assessments of the tax on increase in urban land value that had been challenged by taxpayers before October 26, 2021 and which, on that date, had not been the subject of a final decision in a judgment with res judicata effect or a final administrative decision. One such court is the Catalan High Court in a judgment dated December 22, 2021 or Castilla-La Mancha High Court, in a judgment dated November 15, 2021.

2. Judgments

2.1 Corporate income tax. – Request for ruling on unconstitutionality submitted by National Appellate Court in relation to Royal Decree-Law 3/2016 not admitted

Constitutional Court. **Decision 20/2022 of January 26, 2022**

Royal Decree-Law 3/2016, of December 2, 2016, aimed at the consolidation of public finances and other urgent social measures was published on December 3, 2016. Among other measures, the Corporate Income Tax Law was amended to increase the corporate income tax base in certain cases. These included the following:

(i) New limits were placed on offsetting tax loss carryforwards for entities with net revenues higher than €20 million (50% or 25% of the tax base before the capitalization reserve, by reference to whether those net revenues were between €20 million and €60 million, or equal to or higher than €60 million, respectively).

(ii) An obligation was laid down to revert in 20% portions any impairment losses on securities representing interests in entities which had been deductible in taxable periods that commenced before January 1, 2013, even if actual recovery of the value of the interest had not occurred.

(iii) Article 21 of the Law (relating to the exemption for dividends and gains obtained on the transfer of securities) was amended to state that losses on share transfers would not be deductible where, among other cases, the requirements for the exemption were fulfilled in relation to those shares.

In a direct appeal against the order that approved the corporate income tax self-assessment form for 2016 to adapt it to the royal decree-law mentioned above, the National Appellate Court ruled to submit a request for a ruling on unconstitutionality in relation to those measures, in a decision delivered on March 23, 2021.

In particular, the National Appellate Court considered that Royal Decree-Law 3/2016 was not in accord with the Spanish Constitution due to having been approved by a legislative instrument (a royal decree-law) which is not able to affect the duty to contribute to sustaining the government's public expenditure.

The Constitutional Court ruled not to admit this request for a ruling on unconstitutionality on procedural grounds, without analyzing the doubts raised. Specifically, the court held that:

(i) The procedural requirements relating to adequate formation of the right to be heard period for the parties and for the public prosecutor's office have not been fulfilled.

(ii) In the decision for submission of the request for a ruling on unconstitutionality no reasons were given for the applicability judgment (application to the specific case of the articles believed to be unconstitutional), or the relevance judgment (the importance of the validity of those articles for settling the specific case concerned). Both of these are necessary requirements for admitting a request for a ruling on unconstitutionality.

This decision not to admit the request does not imply that the National Appellate Court cannot submit another request for a ruling on unconstitutionality in relation to Royal Decree-Law 3/2016.

2.2 Personal income tax. – Analysis of tax on severance pay for removal of chief executive officer

National Appellate Court. Judgments of December 23, 2021 (appeal 402/2019) and February 2, 2022 (appeal 401/2019)

Following the removal of a chief executive officer, his previously suspended employment contract was reinstated and later he was dismissed, receiving severance pay calculated by reference to a severance clause signed a few years earlier. The worker argued that he was entitled to the exemption allowed in the Personal Income Tax Law for severance pay and that the non-exempt amount was eligible for the reduction for income generated over more than two years. The tax authorities, however, denied his entitlement to both benefits. Because the chief executive officer had filed a return with his spouse under the joint taxation option, two assessments were issued.

The National Appellate Court shared the tax authorities' conclusions, denied his entitlement to both benefits, and confirmed the two assessments, in a judgment dated December 23, 2021 and another dated February 2, 2022. According to the court:

(i) The only relationship between worker and employer in his period as chief executive officer was a contract for services. The court affirmed that a chief executive officer cannot attempt to argue that his work is confined to advising the board chairman, because, among other reasons, this is not consistent with common practice. As a general rule, a chief executive officer is invested with powers of management and makes strategic decisions.

(ii) When it has been established that his only relationship was a contract for services, he is not entitled to any statutory severance pay in respect of his removal, and is not therefore entitled to the exemption.

It cannot be accepted for these purposes that the previous relationship was suspended, because the agreement stipulating the suspension was signed a long time after he entered the company's managing body.

Nor can it be accepted that the reinstatement of the employment relationship after leaving the board of directors gives entitlement to any severance pay, because it only lasted a few days until his dismissal, and besides, the severance pay was calculated by reference to his last salary as director, instead of the lower salary that he would reasonably have obtained under his last employment contract.

(iii) Nor is he entitled to the reduction for income earned over a period longer than a year because, even though his length of service at the company was longer than two years and there was a severance clause stipulating that, in the event of his removal, he would be paid the severance to which he would have been entitled if had been in an ordinary employment relationship, it cannot be interpreted that the severance is actually linked to the time spent at the company, but rather to a loss of future earnings.

2.3 Transfer and stamp tax. – Charging transfer tax on radio spectrum concessions is precluded by European Union law

Supreme Court. Judgments of January 21, 2022 (rec. 6114/2019) and of January 27, 2022 (rec. 6293/2019)

Under the transfer and stamp tax legislation, administrative concessions are subject to transfer tax (under the transfers for a consideration heading). For that reason, the tax authorities have been charging this tax on concessions granted in relation to the radio spectrum. However, the right to use radio frequencies is subject also to a specific fee for reserving the public radio spectrum.

Directive 2002/20/CEE of 7 March 2002 on the authorisation of electronic communications networks and services (authorization directive), for its part, lays down a number of requirements and limits on fees for rights to use radio frequencies.

In these judgments (among others published recently and containing the same principle), the Supreme Court examined these limits to determine whether it is precluded by European Union law for the fee for reserving the public radio spectrum to coexist with the transfer tax charge.

The Supreme Court's conclusion is that this transfer tax charge is precluded by European Union law. According to the court:

(i) The transfer tax charge is a fee for the purposes of article 13 of the authorization directive, because the chargeable event for that tax is related to the grant of rights to use radio frequencies.

(ii) This tax coincides with the fee for reserving the public radio spectrum and does not fulfill the limits and conditions laid down by the directive. In particular, it does not fulfill the proportionality requirement that article 13 lays down for any fee imposed in respect of the right to use radio frequencies.

These judgments were analyzed in our alert dated February 3, 2022.

2.4 Transfer and stamp tax. – Sale of a supermarket is a transaction subject to stamp tax, even if not registered at the Movable Property Registry

Supreme Court. Judgment of January 20, 2022

For a document to be subject to stamp tax it must (i) be a first copy of a deed or notarial certificate, (ii) have a subject-matter involving an amount or assessable item, (iii) contain transactions or agreements that may be registered at a registry, and (iv) not be subject to inheritance and gift tax, or to transfer tax (under the transfers for a consideration or corporate transactions heading).

At issue in this judgment was whether a public deed recording the sale of a supermarket business is subject to stamp tax if, as the Madrid autonomous community government argued, that deed may be registered at the Movable Property Registry.

The Supreme Court acknowledged that it is not mandatory for the acquisition of a supermarket business to be registered at the Movable Property Registry for it to take effect as against third parties. However, it may be registered voluntarily, and therefore, no matter what effectiveness or effects are given to that registration, the requirement that the transaction "may be registered" is met. For that reason, the transaction is subject to and not exempt from stamp tax.

2.5 Administrative procedure. – A jointly and severally liable party may challenge declaration of liability in a chain based on absence of declaration of default by main debtor

Supreme Court. Judgments of January 25, 2022 (appeals 2297/2018 and 8315/2019)

In these judgments the Supreme Court examines two cases of *liability in a chain*. In both instances, a party is declared jointly and severally liable for a debt in respect of which another party has previously been declared secondarily liable.

In the first claim, the party declared jointly and severally liable submitted that default (*fallido)* by the main debtor had not been declared. Because this declaration is necessary to enforce secondary liability in relation to a debt, that enforcement of secondary liability was null and void and therefore the debt could not later be sought from the jointly and severally liable party.

The Supreme Court accepted this argument and concluded that, in cases involving tax liability *in a chain*, the enforcement of secondary liability is a pre-condition for subsequent enforcement of joint and several liability. Therefore, the jointly and severally liable party may challenge the decision to enforce liability against it on the ground that the previous step to enforce secondary liability was not completed correctly, due to the absence of a declaration of default by the main debtor.

In the second judgment, by contrast, the declaration of default by the main debtor had taken place. However, the party declared jointly and severally liable submitted that it was unjustified because the main debtor had attachable assets. The Supreme Court concluded in this case that the enforcement of liability against the jointly and severally liable party is indeed valid because the declaration of default by the main debtor had taken place and was final. In other words, a jointly and severally liable party cannot challenge an enforcement of liability on the ground of an incorrect element in the previous enforcement of liability against the secondary liable party (other than the absence of a declaration of default by the main debtor), where this circumstance was not challenged within the time limit.

2.6 Management procedure / Tax on increase in urban land value. – Tax authorities are required to deliver decision on revocation of final tax assessments in procedure for refund of incorrectly paid tax

Supreme Court. Judgment of February 9, 2022

The General Taxation Law (LGT) states that taxpayers can only apply for a refund of incorrectly paid tax in relation to final tax assessments, and request a review of those assessments, by means of any of the special procedures provided in the law, which include a revocation procedure. A revocation procedure must always be started by the tax authorities at their own initiative where, among other requirements, they consider that their acts clearly infringe the law.

In the case examined in this judgment, the taxpayer applied to a local authority for a revocation procedure in relation to an assessment of the tax on increase in urban land value charged in respect of a sale of plots so that it could then obtain a refund of incorrectly paid tax. This application was based on the constitutional court judgment delivered on May 11, 2017, which held to be unconstitutional the articles governing the taxable amount for the tax on increase in urban land value in cases where no increase in value of the transferred plots occurs. The application was not admitted because, according to the local authority, the decision to initiate a revocation procedure is an option (not an obligation) for the authorities.

Going against the local authority's principle, the Supreme Court concluded that, where taxpayers request revocation of final decisions by the tax authorities in procedures to apply for a refund of incorrectly paid tax, the tax authorities have to decide whether that revocation is justified before acknowledging or denying the right to a refund. Additionally, taxpayers may challenge (presumed or explicit) refusals of their applications by the tax authorities.

In any event, the court concluded in this case that the assessments at issue could not be revoked, because there had not been a clear infringement of the law, a necessary requirement for revocation of a final assessment. According to the court, when the facts under examination occurred, the uncertainty, the opacity of the legislation governing the taxable amount for the tax on increase in urban land value and its possible interpretations plainly existed, because there were different legal and judicial responses which were contradictory even.

2.7 Audit procedure. - Territorial authority of audit bodies cannot be altered without sufficient substantiation of ground

National Appellate Court. **Judgment of November 17, 2021**

Peripheral audit bodies may apply to the director of the Finance and Tax Audit Department for their authority to be extended to include other territories. This extension may be granted where it is "adequate for implementation of the tax control plan".

An entity challenged an assessment issued by the Galicia Tax Office, on the basis that this office did not have the authority to initiate an audit on a company having its tax domicile in Madrid.

The Galicia Tax Office considered that it did have the authority because there was a decision to extend authority substantiated by "the connection with other audits conducted by the Galician Regional Audit Office".

The National Appellate Court concluded, however, that this ground was insufficient, because the decision does not express the reasons why that extension of authority was adequate for correct implementation of the tax control plan. The court recalled that territorial authority cannot be altered without giving reasons or by using reasoning so general as to make it impossible to know the reason for the decision.

Accordingly, it set aside the challenged assessment, because it was issued by an unauthorized body.

2.8 Review procedure. – Determining amount of claim for lodging ordinary administrative appeal must be done by reference to assessment periods for the tax involved in the observed infringement

Supreme Court. Judgment of January 19, 2022

Following a VAT audit, the tax authorities concluded that the taxpayer had committed an infringement under article 201 of the General Taxation Law, consisting of breaching invoicing or documenting obligations. The tax authorities imposed penalties in respect of each of the VAT reporting periods concerned. None of the penalties taken alone exceeded €150,000, although in aggregate they amounted to over €300,000.

To be able to lodge an administrative appeal to the Central Economic-Administrative Tribunal, the amount of the claim must, as a general rule, exceed €150,000. The taxpayer considered that it was entitled to lodge that appeal because the aggregate amount of all the penalties put together was higher than that figure.

TEAC did not admit the appeal, noting that, according to article 35 LGT, where the document containing the challenged administrative decision includes more than one debt, taxable amount, assessment or act of another type, the amount of the lodged claim will be deemed to be equal to whichever is highest, and that amount cannot go above €150,000.

The Supreme Court agreed with TEAC on this point and concluded that, in cases under article 201 LGT, the amount of economic-administrative claims for the purpose of lodging an ordinary administrative appeal must be determined by reference to the various assessment periods for the tax, with respect to which the practice was observed. In the VAT field, the period to be considered is each quarter (or month) affected.

2.9 Review and collection procedures. – Tax authorities must refund cost of security requested to stay enforcement of a debt, if assessment is set aside in mutual agreement procedure

National Appellate Court. Judgment of December 23, 2021

Tax law states that taxpayers are entitled to a refund of the security provided to stay enforcement of a debt, where the assessment decision is set aside fully or partly in a review procedure. If it is partly upheld, costs are to be refunded in proportion to the tax debt held to be incorrect.

At issue was how this provision applies to cases where the administrative decision is set aside as a result of a mutual agreement procedure.

The tax authorities argued that, for this provision to apply, a final judgment or administrative decision was needed, which precluded agreements adopted in a mutual agreement procedure.

The National Appellate Court recalled, however, that the act that sets aside the assessment is not the agreement adopted in the mutual agreement procedure, but rather the administrative decision enforcing it, so the article is fully applicable.

3. Decisions

3.1 Corporate income tax. – Tax credit for advertising and promotional expenses can only be used in the period the expenses were incurred

Central Economic-Administrative Tribunal. Decision of January 25, 2022

The Patronage Law allows a tax credit for advertising and promotional expenses relating to programs supporting events of exceptional public interest. Namely, persons liable to corporate income tax may deduct from their gross tax liability 15% of the expenses they incur, under plans and programs for activities established by the consortium, on multiyear advertising and publicity for promotion of the event concerned. The tax credit cannot exceed 90% of gifts to the consortium, public entities or entities under article 2 of the same law, responsible for implementing the programs and activities.

It is specified in the regulations that an application for entitlement to the tax credit must be filed more than 45 days before the start of the filing period for the tax return relating to the taxable period in which the tax credit is to take effect.

In the case examined in this decision, an entity had applied to the authorities for recognition of entitlement to the tax credit for 2020. The tax authorities rejected the application because the expenses had been incurred in 2019, and therefore, that year was when entitlement to the tax credit should have been reported, if applicable, and the statutory and regulatory requirements should have been fulfilled.

Against this, the company argued that:

(a) The Corporate Income Tax Law lays down a statute of limitations for exercising the right to a tax credit generated in one year and not used in that year, which runs for 15 or 18 years, depending on the case, and this time period applies to that tax credit for advertising and promotional expenses.

(b) Additionally, it fulfilled the requirement set out in the regulations implementing the law on tax incentives for patronage, because it applied for the prior recognition by the tax authorities more than 45 days before the start of the period for filing the 2020 return, which is when it intended to use the tax credit.

(c) There is no provision, in either the Corporate Income Law or the patronage legislation, that requires a tax credit to be used in the period when the expense giving entitlement to the tax credit is incurred.

TEAC concluded, however, that the tax credit may only take effect in the year the expenses are incurred, which in this case was 2019 (regardless of whether later, due to insufficient tax liability, the unused tax credit is transferred to subsequent years).

Therefore, since the expenses concerned were incurred in 2019, the application for prior recognition by the tax authorities of entitlement to the tax credit should have been made, at the latest, 45 days before the start of the statutory filing period for the tax return relating to that year. Because the company filed the application outside the time limit, its right to the tax credit has to be denied.

3.2 Personal income tax. – Complete adjustment principle requires tax authorities to refund withholding tax at their own initiative if they conclude that salary income is not taxable

Cantabria Regional Economic-Administrative Tribunal. Decision of October 29, 2021

The tax authorities concluded that certain amounts of salary income should not have been reported by the taxpayer, and therefore reduced taxable income by the amount of the relevant administrative assessment. They failed, however, to subtract from net tax liability the withholding tax that the payer had deducted from those amounts of income.

The Cantabria TEAR concluded that, under the complete adjustment principle, the tax authorities should, in addition to decreasing taxable income by the incorrectly reported amount of salary income, have refunded to the taxpayer the withholding tax deducted by the payer.

By failing to do so, the tax authorities are forcing the taxpayer to apply for a refund of withheld tax in a later refund procedure for incorrectly paid tax, which runs counter to the complete adjustment principle.

3.3 Personal income tax. – Proof of married status of foreigners who cannot be registered at the Civil Registry can be provided by other means of evidence

Valencian Regional Economic-Administrative Tribunal. Decision of October 28, 2021

Two non-Spanish national taxpayers, who married abroad but were tax resident in Spain, filed a personal income tax self-assessment under a joint taxation arrangement. The tax authorities rejected that arrangement because they had not provided proof of their married status in the form of a certificate of its registration at the Civil Registry.

However, the circumstances of their marriage (between foreign nationals, celebrated in their country of origin and under the legislation of that country) do not match any of the cases that can be registered at the Civil Registry.

The Valencian TEAR therefore rejected the authorities' interpretation, which it classed as overly bureaucratic, and recognized that marriage is a provable fact that may be evidenced by means other than the certificate of registration at the Civil Registry.

In this case, the taxpayers had produced (i) a historical individual certificate from the municipal register, and (ii) a marriage certificate from their country of origin, with an official translation and bearing the Hague apostille. According to the tribunal, these documents are sufficient proof of the existence of the marriage for the purposes of recognizing their right to apply the reduction for joint taxation.

3.4 Personal income tax. – Expenses relating to car-derived vans and pick-up type vehicles are deductible for determining net income from economic activity

Valencian Regional Economic-Administrative Tribunal. Decision of October 15, 2021.
Catalan Regional Economic-Administrative Tribunal. Decision of October 29, 2021

The deduction of expenses inherent in ownership of a vehicle (including its potential impairment) to determine net income from an economic activity on a personal income tax return requires fulfillment of the general requirements for the deduction of any expense, in addition to the requirement that the vehicle must be used exclusively for the activity. In other words, a combination of personal and professional use is not allowed.

Article 22.4 of the personal income tax regulations, however, contains a presumption of total use for the economic activity for certain motor vehicles, such as "mixed" vehicles (designed to transport both passengers and goods) used for transporting goods.

In these decisions, the Valencian TEAR and the Catalan TEAR examined the ability to deduct expenses generated in relation to a car-derived van and a pick-up vehicle:

(i) Car-derived van: a vehicle with the same characteristics as a passenger vehicle, although it is used to transport goods, and therefore only has one row of seats, and contains a loading compartment that is not separate from the rest of the habitacle, plus a back door for loading goods.

The Valencian TEAR examined the ability to deduct the expenses generated in respect of a car-derived van that the taxpayer uses for its harmful animal extermination and disinfection services.

The tribunal concluded that, while the vehicle does not transport goods, it is nevertheless used exclusively for the taxpayer's business, and therefore, in this case, the burden of proof is reversed and it lies with the tax authorities to provide proof that the vehicle is not used exclusively for the business.

(ii) Pick-up vehicle: according to the Traffic Authority, these vehicles are treated as passenger vehicles if their maximum weight is below 3,500 kg, their total height is below 2 meters and the seating and loading areas are not in a single compartment. Otherwise they are to be treated as trucks.

According to the Catalan TEAR, if they are classed as passenger vehicles, the ability to deduct the expenses will require proof to be provided of their exclusive use for the business.

In any event, the tribunal upheld the appellant's claim because the tax authorities had not verified whether the requirements for classifying the vehicle as a passenger car were fulfilled. Without that verification, according to the tribunal, adjustment of the expenses cannot be accepted.

3.5 Personal income tax. – Tax credit for rental of principal residence can be applied if proof is provided that rented property is renter's principal residence, even if lease agreement is apparently seasonal

Central Economic-Administrative Tribunal. **Decision of October 25, 2021**

On July 1, 2014, a taxpayer signed a lease agreement which was characterized as seasonal by the parties, even though it was covenanted for a complete year. At the end of a year, a new agreement was entered into for a five-year term and with the same terms and conditions, which was really a renewal of the previous agreement.

On the renter's personal income tax return, the tax credit for rental of the permanent residence was used. This tax credit is applicable for agreements signed before January 1, 2015.

The tax authorities rejected the ability to apply that tax credit due to considering that the agreement was seasonal, according to the name given to it by the parties in the agreement.

TEAC found in the taxpayer's favor. According to the tribunal, even though the parties refer to the agreement as a "seasonal lease", it cannot be ignored that it was signed for a complete year and that it has been extended by another agreement for a further five years with the same terms and conditions. Therefore, under the substance over form principle, it must be concluded that this is a lease agreement for a principal residence and therefore gives entitlement to the tax credit.

3.6 Personal income tax. – Requirements for gain realized on gift of the family business not to be taxable must be fulfilled in year of the gift

Central Economic-Administrative Tribunal. **Decision of October 25, 2021**

The Personal Income Tax Law determines that capital gains are not taxable if they are realized on gifts of family businesses triggering entitlement to the reduction of taxable income allowed in the inheritance and gift tax legislation.

A taxpayer gifted his pharmacy business to a family member and did not report the capital gain on his personal income tax self-assessment. The tax authorities denied his right to the non-taxable treatment because they considered that the giver had not substantiated fulfillment of the requirements laid down in the inheritance and gift tax legislation, namely, that, before the gift, the giver must have been carrying on the activities in the pharmacy business habitually, personally and directly, and that these activities must be the giver's main source of income in the year immediately preceding the year of the gift. The giver had, by contrast, substantiated that he fulfilled these requirements in the year the gift was made.

Moreover, the tax authorities attributed to him an amount of income from the economic activity in respect of the gift of the pharmacy's inventories.

The TEAC concluded as follows:

(i) Under the principle determined by the Supreme Court in various judgments and in an earlier TEAC decision on June 18, 2019, the examination of fulfillment of the requirements for the capital gain realized on the gift not to be subject to personal income tax (which are those laid down in the inheritance and gift tax legislation) must relate to the year in which the gift took place (not the immediately preceding year, which runs counter to the arguments raised by the auditors).

(ii) Additionally, TEAC concluded that the non-taxable treatment allowed in the Personal Income Tax Law applies to a transfer of the business as a whole not to individual elements, and therefore the non-taxable gain must be calculated by including all the assets used in that business, including its inventories.

Therefore, TEAC set aside the issued assessment.

The tribunal noted that its method runs counter to that determined by the DGT, in resolutions V2440-10, V0554-19, V1479-20 and V3467-20, among others.

3.7 Personal income tax. - Giving an asset in payment to discharge guarantee entered into with third party generates capital gain

Central Economic-Administrative Tribunal. Decision of September 22, 2021

A married couple entered into a guarantee obligation in relation to the sums owed by a company in respect of loans provided by another entity. When the time came, the guarantors delivered a number of properties to pay off the guaranteed debt, at which point a right to payment against the guaranteed company arose.

The taxpayers did not include the transfer on their personal income tax self-assessments. The auditors' view, however, was that they should have reported a gain in respect of the difference between the market value of the properties (equal to the right to payment against the guaranteed entity) and their cost price, against which the taxpayers argued that, at the most, a loss had occurred because they had ceased to own one of their assets.

TEAC confirmed the tax authorities' conclusions:

(i) It first noted that the existence of a capital gain is unquestionable and that it must be calculated as the difference between the right to payment that is added to the guarantor's assets (equal to the value of the delivered properties) and the cost price of the assets that were transferred.

(ii) And concluded, secondly, that there will only be a capital loss if the right to payment ultimately becomes uncollectible. To be able to use that loss, the guarantors will be required to have pursued all legal avenues for collection against the main debtor.

3.8 Personal income tax. - Capital gain obtained from portion of deferred price recorded in promissory notes must be recognized in year it is discounted

Central Economic-Administrative Tribunal. Decision of April 22, 2021 (Principle 1 and Principle 2)

A taxpayer transferred shares in an entity in 2007. Payment was deferred using promissory notes maturing in 2009 and 2010. For this reason, the taxpayer recognized the gain as and when the promissory notes matured.

The auditors recognized the whole gain in 2007 because the promissory notes were discounted in that year. Additionally, they disallowed finance costs related to the discount from being deducted when determining the gain.

Against the adjustment, the taxpayer submitted that the gain relating to the discounted promissory notes had to be recognized in 2009 and 2010, because the discount included a "subject to clearance" clause.

In a recently published decision, TEAC took the view that the finality of transfers of discounts is not affected by a "subject to clearance" clause. The gain therefore had to be recognized in 2007.

Additionally, it confirmed that the costs relating to discounting the promissory notes cannot be deducted when calculating the capital gain, because they are not inherent in the sale, and instead relate to the seller's intention to collect the deferred payment in advance.

3.9 Transfer and stamp tax. – Method based on net present value of estimated cash flows can only be used if expressly provided for in the legislation on the tax

Central Economic-Administrative Tribunal. Decision of December 16, 2021

The tax authorities commenced an audit of reported values and engaged an expert to draw up a report. To value the property, the expert used the method based on the net present value of estimated cash flows as set out in article 57.1.a) LGT. In view of the result of that report, the tax authorities issued a transfer and stamp tax assessment, in which they stated that the method used was that allowed in article 57.1.e) LGT (valuation based on a report by tax authority experts).

In the economic-administrative claim proceeding brought with TEAC, the taxpayer argued that the valuation method actually used by the tax authorities was the income value method (not the method based on an expert report) and that method was not consistent with the law because it was not expressly provided for in the transfer and stamp tax legislation.

TEAC upheld the claim and concluded that this income value method cannot be used if it is not provided for in the law on the tax. The tribunal held that application of the capitalization system is a matter for the law, and its application cannot be left to an expert's arbitrary opinion.

3.10 Cadastral values. - The presumed truth of information on the real estate cadaster is rebuttable

Central Economic-Administrative Tribunal. Decision of January 26, 2022

The revised real estate Cadaster Law provides that the cadastral values of real estate assets cannot be higher than their market values. Furthermore, all the information contained on the cadaster is presumed to be true, unless proven otherwise by interested parties seeking to evidence their inaccuracy.

In this decision, the tribunal reviewed a case involving an entity which challenged the decision to alter the cadastral value of a real estate asset owned by it, based, among other grounds, on that value being higher than the market value of the property.

To achieve its aim, the entity produced as proof an appraisal report issued by a third party. That report had not been admitted by the Madrid TEAR, on the basis that, in that court's judgment, calculations and valuations made by companies or private parties, or any made by interested parties themselves, cannot be presumed to have the objectivity that is a characteristic of those made by the cadaster's technical services.

After posing the debate in these terms, TEAC concluded in its decision that, under the provisions in the cadastral legislation, the presumed truth of the information contained on the cadaster is rebuttable by proof provided by the interested parties, who may produce any reports they believe to be necessary for these purposes.

The tribunal recalled, however, that this cannot, under any circumstances, mean that the reports produced as proof by the interested parties allow it to be affirmed without any further steps that the cadastral values of the real estate assets are higher than their market values. In fact, TEAC ultimately rejected the value provided as evidence in the appraisal report produced by the entity, due to its inconsistencies and because it departed from the valuation method laid down in Order ECO/805/2003.

3.11 Collection procedure. – Where a notice of attachment is challenged, the proceeding only has to include documents relating to the enforced collection period

Central Economic-Administrative Tribunal. Decision of January 18, 2022

After verifying that a taxable person had not paid over a tax debt in the voluntary period, and the relevant order initiating enforced collection proceedings had been issued, the tax authorities served notice of an attachment order. In a later claim, the taxable person submitted (i) that there were errors and omissions making it impossible to identify the debtor or the enforced debt and (ii) that the right to seek payment had become statute-barred.

The Valencian TEAR upheld the claim because, as the taxpayer had contended, in addition to the documents in the enforced collection proceeding, the attachment proceeding should have included also records relating to the assessments that were the source of the attachment.

TEAC concluded, however, that documents relating to earlier assessments are not among those having to be included in a proceeding relating to an attachment, although the body hearing the case may ask for them to be produced at any time.

Lastly, TEAC clarified that because the right to seek payment of the debt had become statute-barred (which is a ground for challenging a notice of attachment), only any that arose after the order initiating enforced collection proceedings could be examined.

4. Resolutions by the Directorate General for Taxes

4.1 Corporate income tax. – An asset is new where it is brought into operating condition for the first time

Directorate General for Taxes. Resolution V3224-21 of December 28, 2021

The corporate income tax legislation contains various incentives for investment in new assets, such as unrestricted depreciation for small-sized entities.

The DGT clarified that an asset is new where it is used or is brought into working condition for the first time. In other words, where an industrial building is purchased, for example, it cannot have been used earlier and it must enter into operation for the first time under the ownership of the purchasing entity.

This is nevertheless a question of fact which must be proven by any legally valid means of proof and which will be evaluated by the competent bodies of the tax authorities.

4.2 Corporate income tax. – Increase in average workforce is measured by reference to workers with equivalent degrees of disability

Directorate General for Taxes. Resolution V3223-21 of December 28, 2021

The Corporate Income Tax Law allows a job creation tax credit for disabled workers, which varies in amount by reference to the degree of disability. The tax credit is calculated as follows:

(i) €9,000 for each person/year with regard to increases in the average workforce with degrees of disability between 33% and 65%, compared with the average number of workers of the same type in the immediately preceding period.

(ii) €12,000, where the increase in the average workforce relates to workers with degrees of disability equal to 65% or higher.

The DGT underlined that these are really two different tax credits, which depend on the degrees of disability of the hired workers.

Therefore, to apply, for example, the tax credit for an increase in the average workforce with degrees of disabilities between 33% and 65%, it is not necessary for the number of workers with degrees of disabilities equal to or higher than 65%, or the total workforce with disabilities, to have increased. The increase in the average workforce must be measured within each category of workers, by reference to their degrees of disability.

4.3 Corporate income tax. – Dividends giving entitlement to an exemption are not subject to withholding although a 5% reduction has to be made for management costs

Directorate General for Taxes. Resolution V3204-21 of December 23, 2021

Starting in years commencing on or after January 1, 2021, the exemption for dividends and gains obtained from transferring shares has to be reduced by 5% in respect of management costs.

In relation to this reduction, the DGT set the following guidelines:

(i) As with finance costs, any management costs that the entity actually incurs are tax deductible under the general rules, although with the described reduction.

(ii) This reduction also applies to dividends and gains obtained by entities under the special tax regime for foreign-securities holding entities (ETVE).

(iii) The dividends are not subject to withholding, despite not benefiting from a full exemption as a result of the described reduction.

4.4 Personal income tax. – DGT clarifies how to interpret new limits on reduction for contributions to pension and welfare programs

The General State Budget Law for 2022 (see our commentary dated December 29, 2021) has reduced the amounts entitling taxpayers to reduce their taxable income for personal income tax purposes as a result of contributions to pension and welfare systems.

The law provides in particular that the maximum annual amount for contributions to pension and welfare systems giving entitlement to a reduction is €1,500 and that this limit must be increased by €8,500, where the increase comes from employer contributions or employee contributions to the same pension and welfare instrument, if the employee's contributions match or are lower than the employer's contributions.

The DGT interprets this rule as follows:

(i) **Overall limit.** The law places an overall annual limit amounting to €1,500 which comprises both individual contributions to individual or occupational programs and employer contributions to occupational programs.

Therefore, that overall limit may only include workers' contributions to their occupational welfare and pension programs, and they are not conditional on contributions made by the employer.

In other words, the worker could contribute up to €1,500 in a year and stay within this overall limit.

(ii) **Additional limit.** The increase to that limit by €8,500 per year is an additional limit that relates to both employer contributions to an occupational program and employee contributions to the same occupational program in an amount matching or lower than those employer contributions.

Therefore, that additional limit includes workers' contributions to their welfare and pension programs, which are conditional on the employer making contributions in, at least, the same amount. Additionally, amounts contributed by the employer cannot result from a decision by the worker (otherwise, they will be treated as contributions by the worker and not able to be included in this limit).

In short, the worker could contribute up to €4,250 a year to be included in this limit, if the employer company makes employer contributions amounting to a further €4,250, to take full advantage of this increase of up to €8,500.

For example, if the employer makes employer contributions amounting to €4,250 over a year, the worker could make contributions to the same welfare and pension program amounting to €5,750 over a year, of which €1,500 would be included in the overall limit and €4,250 in the additional limit.

4.5 Wealth tax. – Principles for the valuation of entities that are neither listed nor audited

Directorate General for Taxes. Resolution V3167-21 of December 22, 2021

The issue submitted for resolution concerned how to value an unlisted company with negative shareholders' equity and which had not recorded income in the previous three years. The company had not been audited nor had it entered an insolvency proceeding.

Under the wealth tax legislation, to determine the value of shares in the share capital of legal entities not traded on organized markets, where the company's balance sheet has not been audited or the auditor's report does not contain a favorable opinion, they must be valued at the highest of the following three figures: their par value, their carrying amount on the latest approved balance sheet or the value arrived at by capitalizing at a rate of 20% the average income figure for the three fiscal years immediately preceding the date the tax becomes due.

The DGT recalled that, according to the findings in supreme court judgment 873/2013, of February 14, 2013, the reference point for "the latest approved balance sheet" must be that approved within the statutory time period for filing the appropriate self-assessment, even if the approval took place after the tax became due.

Moreover, for shares in an entity under an insolvency proceeding (which was not the case in this instance) the method described in resolution V3614-16 would have to be applied. According to that resolution, the valuation method provided in the wealth tax legislation must be combined with the "fair value" concept referred to in the insolvency legislation, determined according to the report issued by an independent expert under generally accepted valuation principles and rules.

Lastly, the DGT noted that the powers to set or determine values in relation to this field are held by the offices managing wealth tax.

4.6 Wealth tax. – Taxable amount has to be increased or decreased by refunds or amounts to be paid in respect of personal income tax for the same fiscal year

Directorate General for Taxes. Resolution V3002-21 of December 3, 2021

The taxable amount for wealth tax purposes consists of the value of the taxable person's net worth, determined by reference to the difference between the value of assets and rights owned by that person and the value of debts or obligations for which they are liable.

From the standpoint that the tax becomes due as of December 31 each year, the DGT's view is that the final personal income tax liability for the same fiscal year (if it is a positive figure) may appear among the taxable person's debts. According to the DGT, the fact that the personal income tax debt is not payable as of that date does not mean that it does not exist.

Similarly, any amount to be obtained in a refund must be computed as a right able to be included in the taxable amount for wealth tax purposes.

4.7 Wealth tax. – Unrealized gains cannot give rise to deductible debts

Directorate General for Taxes. Resolution V3168-21 of December 22, 2021

As mentioned above, the taxable amount for wealth tax purposes is calculated by reference to the difference between the value of assets owned by the taxable person and the charges or encumbrances that decrease their value. The submitted issue concerned whether any tax obligations that would arise on the realization of unrealized gains on the assets could be included as encumbrances.

The reply was that they could not. The tax obligations relating to the various assets and rights forming part of the taxable person's net worth are deductible if they are properly substantiated, are nontransferable (i.e., only the taxable person is liable for them) and have been determined before the wealth tax becomes due.

Therefore, any potential tax obligations that may arise from the future realization of gains on the assets are not deductible, because they are neither properly substantiated, nor are they debts for which the taxable person is liable when the tax becomes due.

4.8 Transfer and stamp tax. – Clarification of how the winding up of a company is taxed where its primary asset is a property located in a different autonomous community to where it has its registered office

Directorate General for Taxes. Resolution V3001-21 of December 3, 2021

The submitted issue concerned the dissolution of a company whose primary asset is a property located in another autonomous community to where it has its registered office. In relation to this case, the DGT concluded as follows:

(i) The winding up and liquidation of a company with distribution of its real estate assets to shareholders is a transaction subject to transfer tax (under the corporate transactions heading), and the taxable persons are the shareholders in respect of their received assets and rights.

(ii) The taxable amount for each shareholder is the value of the assets and rights distributed to them, which may be verified by the tax authorities.

(iii) The tax rate is 1%.

(iv) And the tax must be assessed in the autonomous community where the company has its registered office.

(v) If a distribution in excess is received, that excess amount will additionally be subject to transfer tax (under the transfers for a consideration heading).

4.9 Electricity tax and tax on the value of electricity output. – Clarification of how solar self-supply services are taxed

Directorate General for Taxes. Resolutions V3003-21 and V3006-21 of December 3, 2021

In these resolutions, the DGT clarifies how solar self-supply services offered by an energy company to its customers are taxed in respect of the electricity tax and the tax on the value of electricity output.

According to the DGT:

(i) The treatment for a supply with self-supply and no surpluses arrangement is as follows:

(a) Self-supply by "small electricity producers" at their plants (capacity of their generator or all their generators in aggregate equal to or lower than 100 kilowatts), of the electricity they generate themselves.

(b) The taxable event for electricity tax will occur, although with exemption, where that self-supply takes place at an electricity generation plant that has an installed capacity equal to or higher than 100 kilowatts (kW) without going above 50 megawatts (MW), if the plant uses renewable, cogeneration or waste technology.

(c) Outside the two described cases, a producer's consumption of electricity it has generated itself is subject to and not exempt from the electricity tax.

(d) However, under this type of self-supply arrangement, the consumer or consumers (in cases of collective self-supplies), owning the electricity generation plant might need to purchase electricity. If so, the supplier must charge the electricity tax on any electricity supplied to them.

(e) In these cases, because the electricity is not fed into the grid, the taxable event for the tax on the value of electricity output does not take place.

(ii) Under a supply with self-supply and surpluses arrangement, according to the DGT, this arrangement may be divided into two types:

(a) An arrangement with surpluses and election of the offsetting option, and

(b) An arrangement with surpluses and without election of the offsetting option.

Self-supply may be further classified as individual or collective depending on whether the generation plant has one or more associated consumers.

Lastly, in these two self-supply arrangements with surpluses there are two types of taxable persons: the consumer and the producer, who may be individuals or legal entities and the same or different persons.

For the **self-supply with surpluses and election of the offsetting option**:

(a) Where consumer and producer are the same person, normally a portion of the generated electricity is consumed by the producer, and the remaining electricity is fed into the grid.

- Regarding electricity consumed by the producer and the electricity tax, the scenario is the same as that analyzed for a self-supply without surpluses arrangement.

- On the portion of electricity fed into the grid, no circumstances occur which would give rise to the taxable events contained in the legislation on the electricity tax.

(b) Where there are other associated consumers besides the producer, normally a portion of the electricity is consumed by the producer, another portion is delivered to the other consumers, and the remaining portion is fed into the grid. In these cases:

- Regarding the portion of electricity consumed by the producer, the scenario is the same as that analyzed for a self-supply without surpluses arrangement.

- In relation to electricity fed into the grid, no circumstances occur which would give rise to the taxable events contained in the legislation on the electricity tax.

- With respect to the electricity delivered to the other consumers, the producer is making a supply of electricity to an individual or entity that acquires the electricity for their own consumption, which amounts to a taxable event for the electricity tax.

  The taxable amount will be the amount that would have been determined for VAT purposes for supplies made for consideration between unrelated parties (regardless of whether the supplies to other consumers are made with or without consideration).

- In respect of the electricity supplied by a retailer to a producer under a self-supply with surpluses and election of the offsetting option arrangement, the person making that supply must charge to the purchaser of that supplied electricity the amount relating to the electricity tax. The supplied electricity is exempt, however, if it is offset against the price of the surplus electricity at time-of-use rates.

- Lastly, the surplus electricity at time-of-use rates is not treated as electricity fed into the grid, and therefore the taxable event for the tax on electricity output never takes place.

Under the **self-supply without election of the offsetting option** arrangement:

(a) If consumer and producer are the same person, normally a portion of the generated electricity is consumed by the producer, and the remaining portion is fed into the grid. In these cases:

- Regarding electricity consumed by the producer, the scenario is the same as that analyzed for a self-supply without surpluses arrangement.

- In relation to the portion of electricity fed into the grid, no circumstances occur which would give rise to the taxable events contained in the legislation on the electricity tax.

(b) Where there are other associated consumers besides the producer, normally a portion of the electricity is consumed by the producer, another portion is delivered to the other consumers and the remaining portion is fed into the grid. In these cases:

- Regarding the portion of electricity consumed by the generator, the scenario is the same as that analyzed for a self-supply without surpluses arrangement.

- In relation to the electricity fed into the grid, no circumstances occur which would give rise to the taxable events contained in the legislation on the electricity tax.

- With respect to the electricity delivered to the other consumers, the producer is making a supply of electricity to an individual or entity that acquires the electricity for their own consumption, which amounts to a taxable event for the electricity tax.

The taxable amount is the amount that would have been determined for VAT purposes for supplies made for consideration between unrelated parties (regardless of whether the supply is made without consideration).

(c) For supplies of electricity made by a retailer to a producer or to a consumer under an arrangement for self-supply with surpluses and without election of the offsetting option, the person making that supply has to charge the relevant amount to the person receiving that supplied electricity.

(d) For electricity generated and fed into the grid the taxable event for the tax on electricity output occurs. The taxpayer for the tax is the producer.

The taxable amount consists of the total amount receivable by the taxpayer in respect of the electricity output produced and measured in power plant busbars on the electricity production market, for each plant in the taxable period.

The taxable period matches the calendar year, unless the taxpayer has stopped using the plant to generate electricity, in which case the tax period will end on the date on which generation stopped.

The tax must be charged at 7% percent.

5. Legislation

5.1 Aid for victims of violent crimes and for victims of gender violence declared exempt and amendments made to reserve for investment in the Canary Islands and Canary Islands general indirect tax

On December 30, 2020, the Official State Gazette (BOE) published Royal Decree-Law 39/2020, of December 29, 2020, amending letter (y) of article 7 of Law 35/2006, of November 28, 2006, on personal income tax, to include guaranteed minimum income in the exemption under that letter with effect from June 1, 2020 (see our alert dated December 30, 2020).

Now, that measure has again been included in Law 2/2022, of February 24, 2022, on financial measures for social and economic support and on compliance with the enforcement of judgments (Official State Gazette -BOE- on February 25, 2022).

Additionally, the exemption in the same letter of article 7 has been extended to include certain types of aid granted to victims of violent crimes and of gender violence.

Moreover, Law 2/2022 introduces various amendments in relation to the reserve for investment in the Canary Islands and to the Canary Islands general indirect tax:

(a) **In relation to the reserve for investment in the Canary Islands**:

The contents of final provision two of Royal Decree-Law 39/2020, of December 29, 2020 have been validated. That provision extended by a year the time periods for investing the portion of the reserve for investment in the Canary Islands allocated out of income obtained in 2016, and the allocation to that reserve relating to advance investments made in 2017 (see our alert dated December 29, 2020).

The time period for investing the reserve from 2017 and later years has not been extended.

(b) **In relation to the Canary Islands general indirect tax:**

To avoid cases of double taxation and coordinate the rules on these cases with the rules established in the VAT legislation, the catch-all use and enjoyment rule for determining the place of supply for services has been adapted, with effect from January 1, 2021.

The exact rule is that the services listed below must be regarded as supplied in the Canary Islands general indirect tax area, where (under the place-of-supply rules applicable to these services) they are not deemed to be performed in the European Union, but their effective use and enjoyment takes place in the Canary Islands general indirect tax area:

- Those mentioned in point one.3 of article 17 of Law 20/1991, of June 7, 1991, where the customer is a trader or professional acting in their capacity as such.
- Mediation services for and on behalf of another where the customer is a trader or professional acting in their capacity as such.
- Services consisting of hiring means of transportation
- Electronically supplied services and telecommunications, radiobroadcasting and television services.

5.2 Approval of the trading values in the fourth quarter of 2021 for traded securities

The February 25, 2022 edition of the Official State Gazette (BOE) published Order HFP/115/2022 of February 23, 2022, approving the list of securities traded at traded venues, with their average trading values for the fourth quarter of 2021, for the purposes of:

(i) The 2021 wealth tax return.

(ii) The annual information return on securities, insurance and income.

Additionally, a few technical amendments are added to the designs for recording information on form 189 for the information return on securities, insurance and income.

5.3 Financial transactions tax and digital services tax included in the Basque Economic Accord and connecting factors defined for VAT purposes in distance transactions

Law 1/2022 of February 8, 2022, amending Law 12/2002, of May 23, 2002, approving the Economic Accord with the Basque Country autonomous community was published in the Official State Gazette -BOE- on February 9, 2022. Among other new legislation, the tax on financial transactions and the tax on certain digital services have been included and the connecting factors have been determined for charging VAT and reviewing special VAT schemes such as that for distance transactions. In our alert dated February 9, 2022 we summarized the main new provisions introduced in this law.

Tax Department

Follow us:

GARRIGUES

Hermosilla, 3

28001 Madrid, Spain.

T +34 91 514 52 00 **F** +34 91 399 24 08