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TAX NEWSLETTER

GARRIGUES

Latest developments and legal trends - Legislation of interest

News Roundup - Judgments

CONTENTS

2.7 Transfer and stamp tax.- The tax base in the winding up of a community property system is the amount allocated to each owner

2.8 Tax on increase in urban land value.- The expenses associated with a property purchase increase the cost price

2.9 Tax on large retail establishments.- Tax on large retail establishments in Aragon and Asturias is lawful

2.10 Requests for information.- A general request for information on the legal profession as a whole is precluded by the law

2.11 Cadaster procedure.- The cadaster is not allowed a third chance to value a property

2.12 Review procedure.- The tax authorities must apply the accepted interpretations for one tax to other taxes

3. Decisions and Rulings

3.1 Corporate income tax.- Late-filing of a return prevents the offset of net operating losses

3.2 Personal income tax.- The burden of proof in relation to tax on per diems must lie, generally, with the payer

3.3 Personal income tax.- Income obtained from the sale in installments of a client list after ceasing operations may be recognized as the price is collected

3.4 Personal income tax.- If the local tax on increase in urban land value has not yet been assessed by the local council, it cannot reduce the capital gain

3.5 IRPF.- The capital gain must be estimated if part of the price is uncertain

3.6 VAT.- Clarification of the requirements for the exemption in financial transactions and in ancillary services to insurance mediation companies

3.7 Inheritance and gift tax.- If central government legislation was applied in a filed self-assessment, the application of autonomous community legislation cannot later be requested

3.8 Administrative procedure.- Notices may be served on the person appearing as director of a company at the commercial registry

3.9 Audit procedure.- The assessment in an accepted notice of assessment is not deemed to have occurred and been notified if, within a month from the notice of assessment, an attempt is made to notify the order to complete audit work

3.10 Review procedure.- If new items of proof are produced in the economic-administrative jurisdiction, the court must confine itself to assessing those items

4. Legislation of interest

4.1 Latest amendments to the VAT Directive regarding the reverse charge mechanism and the applicable VAT rates on electronic books

4.2 Lenders will pay stamp tax on mortgages and will not be able to deduct it for corporate income tax purposes

4.3 Approval of the reform of the economic and tax regime of the Canary Islands

4.4 Amendments to forms 303, 322, 390 and 347

4.5 Approval of implementing regulations for various articles of the Regulations on Excise and Other Special Taxes

5. Miscellaneous

5.1 The Tax Agency clarifies the procedure for yachts entering and leaving EU Customs territory

1. Tax auditors are only allowed to review the neutrality regime at the company electing it

A TEAC decision rejected the argument that the tax agency is allowed to audit the shareholders that made a contribution of a line of business to a company because verification of the requirements to elect the special deferral regime must be carried out at the beneficiary company.

This decision examines a case in which individuals had made a non-monetary contribution of a line of business to a company. The beneficiary company of that line of business elected to apply the special deferral regime set out for business reorganizations in the corporate income tax legislation.

The individuals had previously filed a request for a binding ruling request with the Directorate General for Taxes, which confirmed that the special deferral regime could be elected for the described restructuring transaction because, among other elements, the reasons for performing the transaction were valid.

Despite this, the tax auditors adjusted the tax returns of the individuals, arguing that the special deferral regime should not be allowed because (i) there were no valid economic reasons for the restructuring transaction performed and (ii) they had not evidenced the existence of an aim other than obtaining a tax advantage.

In a decision rendered on October 15, 2018, the Central Economic-Administrative Tribunal (TEAC) concluded, however, that verification of the requirements for applying the special deferral regime must be done at the company electing to apply it. In the case of non-monetary contributions, the right to elect this special regime is exercised by the transferee company (i.e. the beneficiary of the contribution).

With this in mind, since there was no evidence that the special deferral regime had not been allowed at the transferee company, TEAC held that the adjustment made to the shareholders had to be reversed.

2. Judgments

2.1 Controlled transactions.- Taxable persons not having a duty to document their controlled transactions may be subject to penalties under the general penalty regime in the General Taxation Law

Supreme Court. Judgment of October 15, 2018

The Corporate Income Tax Law defines a specific penalty regime for controlled transactions applicable to taxable persons legally required to keep and ensure that the tax authorities have access to the documents related to those transactions.

Specifically, if these taxable persons fulfill their duty to document the transactions and the pricing of their transactions is consistent with that included in the documents, no penalties may be imposed on them under that specific regime even if the normal market value of one or more of their transactions is found to be incorrect by the tax authorities.

The court affirmed, however, that, in relation to related-party transactions, any taxpayers who by law do not have a duty to keep and ensure that the tax authorities have access to the documents related to those transactions (because, for example, their transactions with one company are not above certain thresholds) penalties could be imposed on them under the general penalty regime in the General Taxation Law, provided the necessary intentional and factual requirements are met to

impose penalties for a certain type of conduct (where, for example, it is verified that they have paid less tax as a result of incorrectly pricing their transactions and fault is held to exist).

2.2 Tax treaties.- The CJEU rules on when it can examine infringements of tax treaties entered into between member states

Court of Justice of the European Union. Judgment of October 24, 2018, case C-602/17

It was raised whether the CJEU could rule on the conformity with EU law of a tax treaty entered into between two member states. The Court held as follows:

(a) The CJEU does not have jurisdiction, in the context of a request for a preliminary ruling, to rule on the potential infringement by a contracting state of the provisions in a tax treaty entered into between two member states.

(b) The CJEU is not allowed either to examine the relationship between a national measure and the provisions of a tax treaty.

(c) However, when a tax regime under a tax treaty forms part of the legal framework applicable to a case that has been presented as such by the national court, the CJEU must take it into account in order to give an interpretation of EU law which will be of use to the national court.

The case examined by the CJEU falls within this scenario, and therefore the court decided to examine the facts of the case. Specifically, it concluded that a provision in the Belgium Luxembourg tax treaty is not precluded by the principle of freedom of movement for workers by stating that the salary income obtained by a resident of one of the contracting states in relation to employment in the other state is exempt from tax in the state of residence of the employee only if the work is physically performed in the other contracting state (and not if it is performed from the state where the employee resides).

2.3 Corporate income tax.- Valid economic reasons exist in the transfer of group financing to the operating subsidiaries where the assets are located

National Appellate Court. Judgment of June 28, 2018

A multinational group set up a company in Spain which acquired the shares of the Spanish operating companies in the group. The acquisition was financed with a loan from the parent company which this company had obtained from third parties. This transaction was followed by a merger between one of the acquired operating companies and the company that acquired them and the creation of a tax group.

The tax auditors found the existence of an artificial arrangement because they considered that the only aim of the reorganization was to place expenditure in Spain that would reduce the group's corporate income tax base. For that reason, they concluded that the transaction had been performed with evasion of the law.

The taxpayer countered that the reorganization was founded on business reasons. This was because, since the financing had been obtained from third parties by the group's parent company, the reasonable course of action was to transfer the debt to the various subsidiaries according to the value of their assets.

In the National Appellate Court's opinion, the reason pleaded by the taxpayer is valid from a business standpoint, because it makes sense for the debt to be placed where the assets are located, regardless of whether tax is saved as a result. It therefore concluded that the finding of evasion of the law by the tax authorities was unfounded.

2.4 Corporate income tax.- The investment impairment allowance is calculated from the subsidiary's individual earnings

Supreme Court. Judgment of October 2, 2018

According to the Supreme Court, the deductible amount of an investment impairment allowance must be calculated by reference to the income or loss of the investee, individually, not the consolidated figure.

The court recalled that the corporate income tax legislation takes precedence over accounting rules and that, specifically, article 12.3 of the law on the tax (which set out the rules on the tax deduction of investment impairment losses) referred to their net asset value per share, which is associated with the entity not the business group.

2.5 Corporate income tax. Banks' input VAT on goods purchased to be delivered as income in kind to customers is not deductible

National Appellate Court. Judgment of May 28, 2018

A financial institution paid certain returns on movable capital to its customers in kind. Because it did not charge VAT on the supply of the goods, its input VAT on the purchase of those goods was not deducted. For that reason, it recognized an expense in respect of the input VAT that had not been deducted, which it deducted from the corporate income tax base.

The National Appellate Court affirmed, however, that the described book expense was not deductible on its corporate income tax return, because it related to voluntary assumption of the VAT cost by the financial institution and therefore must be treated as a gift.

2.6 Transfer and stamp tax.- Deeds for notification of new construction and for establishment of the horizontal property system are subject to stamp tax

Supreme Court. Judgment of October 09, 2018

The Supreme Court confirmed in this judgment that notarized deeds for notification of new construction and for establishment of the horizontal property system in buildings are subject to stamp tax because they relate to a sum of money or a valuable item and contain acts subject to registration at the property registry.

2.7 Transfer and stamp tax.- The tax base in the winding-up of a community property system is the amount allocated to each owner

Supreme Court. Judgment of October 9, 2018

A community property system was wound up and the couple's entire home was allocated to one of the spouses.

According to the Supreme Court, the stamp tax base in this case is 50% of the property's value, in other words, the value that relates to the part of the property that the recipient did not have before the community property system was wound up.

2.8 Tax on increase in urban land value.- The expenses associated with a property purchase increase the cost price

Castilla y León High Court. Judgment of July 23, 2018

According to confirmation given by the Supreme Court, the local tax on increase in urban land value only falls due if the land value increases between when the property is purchased and when it is later transferred.

In this judgment the court explained that the calculation of the cost price must include any development, notarization and registration costs and taxes (such as transfer and stamp tax) that fell due in relation to the purchase of the transferred property. This is the only way to calculate the taxable increase correctly for the purposes of the tax on increase in urban land value.

The Castilla y León High Court itself acknowledged that this is not a settled matter at this point and remains to be examined for a final determination by the Supreme Court.

2.9 Tax on large retail establishments.- Tax on large retail establishments in Aragon and Asturias is lawful

Supreme Court. Judgments of October 2, October 11 and October 16 2018

The Supreme Court has rendered new judgments confirming the lawfulness of government regulations related to taxes on large establishments, in this case, the taxes in Aragon and Asturias.

In our Tax Newsletter - October 2018 we discussed earlier judgments by the same court in relation to the taxes in Catalonia and Navarra.

2.10 Requests for information.- A general request for information on the legal profession as a whole is precluded by the law

Supreme Court. Judgment of November 13, 2018

The Supreme Court set aside a decision rendered on July 20, 2017 by the General Council of the Spanish Judiciary which partially approved the request for information made by AEAT on the subject of the participation of lawyers and court procedural representatives (*procuradores*) in all court proceedings in 2014, 2015 and 2016, leaving out any parts related to identification of clients. The information requested by AEAT, for those years, related specifically to identifying each lawyer and court procedural representative that had taken part in legal proceedings at any court or tribunal sitting anywhere in Spain, and providing details such as the starting dates of their participation in the proceeding, the amount involved in the lawsuit, or identification of the client.

The Supreme Court explained that for a request for information of this type to be lawful a few objective guidelines on how they are to be made must be followed, and concluded that, in this

case, the Tax and Customs Control Plans for 2016 and 2017 (which AEAT used to support its request) do not give weight to a request for information addressed generally to the legal profession as a whole.

2.11 Cadaster procedure.- The cadaster is not allowed a third chance to value a property

Valencia High Court. Judgment of April 2, 2018

After two cadaster valuations had been set aside, the cadaster made a third valuation which it intended to have the same effective date as the two earlier ones.

Valencia High Court refused, however, to allow the cadaster to have up to three chances to value a property, and therefore concluded that the third valuation was null and void.

2.12 Review procedure.- The tax authorities must apply the accepted interpretations for one tax to other taxes

Castilla y León High Court. Judgment of May 31, 2018

In a VAT audit, the authorities took the view that certain amounts of input VAT were deductible because the expenses on which the VAT had been charged were incurred for an economic activity.

In a later audit, however, they disallowed deduction of the same expenses for corporate income tax purposes precisely because they had not been incurred for any activity. Castilla y León High Court concluded that this second practice was not correct, because the tax authorities were bound by their own acts.

3. Decisions and Rulings

3.1 Corporate income tax.- Late-filing of a return prevents the offset of net operating losses

Directorate General for Taxes. Ruling V2496-18, of September 17, 2018

In a decision rendered on April 4, 2017, the Central Economic-Administrative Tribunal (TEAC) concluded that if a company has not filed its corporate income tax return, it must be considered that it has not exercised its right to offset net operating losses, and has chosen to defer them in full.

The Directorate General for Taxes adopted this interpretation and concluded that this election cannot be corrected by filing a late return, or in the course of an audit.

3.2 Personal income tax.- The burden of proof in relation to tax on per diems must lie, generally, with the payer

Central Economic-Administrative Tribunal. Decision of November 6, 2018

Payers of salary income subject to personal income tax are required to make withholdings, which subsequently reduce the amount of tax payable by the worker. The tax authorities are allowed to review the correct determination of the amounts to be paid over to the finance authority by both the payer/withholding agent and by the recipients.

Despite this, TEAC held that, under the principle of the availability and ease of access to proof, the tax authorities may not disallow an exemption claimed by a worker because that worker is not in a position to prove the requirements to claim an exemption, without first attempting to obtain the necessary documents from the payer through a request for information.

To arrive at this conclusion, the court made an interesting analysis of the burden of proof in relation to the exemption claimable for per diems in respect of normal traveling, meal and overnight expenses; and underlined that, generally, only the payer is able to prove quickly and conveniently details such as the day or place and the reason for the trip or the relationship between the expenses and the payer company's operations, in other words that the traveling expenses were incurred for reasons related to work and organization of the company's economic activity.

All of the above is regardless of whether (i) some elements will be able to be substantiated by the worker, when the invoice or receipt was issued in the worker's name, for example, as occurs with overnight expenses or toll and parking costs; or whether (ii) the recipient may voluntarily provide support for the exemption if it is available.

3.3 Personal income tax.- Income obtained from the sale in installments of a client list after ceasing operations may be recognized as the price is collected

Directorate General for Taxes. Ruling V2531-18, of September 18, 2018

The requesting party decided to abandon the professional practice (law) he had been operating and sold his client list (proceedings) to a company, in exchange for a price composed of a fixed amount to be received in 2018 and a variable amount by reference to the success of the proceedings in 2019 and 2020.

Insofar as the client list associated with the professional practice is an element used in an economic activity, its transfer gives rise to a capital gain which must be recognized, generally, in the tax period in which the capital gain occurs (2018).

However, the special rule on the timing of recognition of the capital gain may be elected as the payments fall due, even if the client list was sold as a result of ceasing operating.

3.4 Personal income tax.- If the local tax on increase in urban land value has not yet been assessed by the local council, it cannot reduce the capital gain

Directorate General for Taxes. Ruling V2522-18, of September 18, 2018

A property was transferred in 2018, and the local tax on increase in urban land value has not yet been paid. The local council is not expected to assess the tax until the second quarter of 2019, namely after completion of the filing period for the 2018 personal income tax return.

According to the Directorate-General for Taxes, the tax cannot be subtracted from the transfer value when calculating the income to be included in the 2018 return.

Later, when the local council assesses the local tax and it is paid, the tax liability for 2018 may be adjusted by filing the appropriate correction.

3.5 IRPF.- The capital gain must be estimated if part of the price is uncertain

Directorate General for Taxes. Ruling V2517-18, of September 18, 2018

The shares of an unlisted company were transferred in exchange for a price composed of a fixed amount, received on the execution date of the sale deed, and a variable amount, which would be received in successive years if certain parameters were achieved.

Because the transfer value was not a predetermined amount, as a result of depending on unknown variables when the disposal took place, an estimate had to be made of final full price of the transfer, and the capital gain calculated by reference to that estimate. If in later years the amount received in respect of the variable component of the price differed from the estimate amount, then the required adjustment would have to be made, either by filing a supplementary return, with the related late-payment interest, or by correcting the filed self-assessment.

The Directorate General for Taxes acknowledged, however, that because this is actually a transaction with a deferred price, it may be elected to recognize the capital gain as the payments fall due.

3.6 VAT.- Clarification of the requirements for the exemption in financial transactions and in ancillary services to insurance mediation companies

Central Economic-Administrative Tribunal. Decision of October 25, 2018.

These two decisions (numbers 02685/2017 and 01047/2015), both rendered on October 25, examined mediation activities in financial transactions. TEAC concluded in both cases that mediation in financial transactions is exempt only if the mediator is a third party other than the parties it brings into contact, presents itself as such and acts for itself and independently. In other words, the exemption is not claimable if there is no evidence that the mediating entity acts for itself or where it is verified that, in fact, it acts for and on behalf of its principal.

Decision 02685/2017 also examined the exemption in the case of ancillary services provided to insurance mediation companies. TEAC considered that the exemption is claimable in respect of ancillary services provided by the appellant to insurance mediation companies, insofar as it holds an indirect relationship with the insurer and a direct relationship with the policyholder and its activity covers essential components of the activities of insurance agents such as attracting clients.

3.7 Inheritance and gift tax.- If central government legislation was applied in a filed self-assessment, the application of autonomous community legislation cannot later be requested

Central Economic-Administrative Tribunal. Decision of October 16, 2018

The law on autonomous community financing used to establish the connecting factor for inheritance tax in the autonomous community where the deceased resided when the taxable person (heir or legatee) is resident in Spain. This meant that central government legislation had to be applied when the deceased had not been resident in Spain or the taxable person was not resident there.

In a judgment rendered on September 3, 2014, the CJEU concluded that this law was precluded by the principle of freedom of movement of capital. It must be taken into account that a few autonomous communities provide very large reductions that do not exist in the central government legislation.

In the wake of this judgment, the law on the tax was amended. In additional provision two it provides that the legislation of an autonomous community legislation may be applied in cases where the deceased was resident, or the taxable person, is resident, in the European Union or in the European Economic Area (or both of them are) if any of the parties or property involved has any connection with an autonomous community.

This judgment examined the case of a taxable person whose wife resided in the United Kingdom. The death occurred in 2014, before the CJEU judgment and the subsequent entry into force of additional provision two. As a result of the filing periods for the tax, however, the self-assessment was filed afterwards. To be safe, the taxable person applied the central government legislation, but later applied for a refund of the excess amounts paid, by arguing that the principle in the judgment applied to him.

TEAC denied the right to a refund in this questionable decision. The tribunal held that when the return was filed, the taxpayer had a choice and elected to apply the central government instead of the autonomous community legislation, and therefore, in accordance with article 119.3 of the General Taxation Law, that election cannot later be changed. The tribunal recalled that it is a right that additional provision two establishes, a right for the taxpayer to apply the autonomous community legislation, and, since it is a right, it has to be elected.

3.8 Administrative procedure.- Notices may be served on the person appearing as director of a company at the commercial registry

Central Economic-Administrative Tribunal. Decision of October 15, 2018

According to TEAC, the notice to communicate mandatory inclusion on the enabled electronic address system of a company to the person appearing as its director at the commercial registry is correct, and therefore takes effect in relation to the company.

In other words, that notice does not have any liability effect for the director, instead it is the company itself which, under the principle of trust by the third party (in this case the authority that notifies the person appearing at the registry as representative) cannot refuse to assume the consequences of that notice served in good faith.

3.9 Audit procedure.- The assessment in an accepted notice of assessment is not deemed to have occurred and been notified if, within a month from the notice of assessment, an attempt is made to notify the order to complete audit work

Central Economic-Administrative Tribunal. Decision of October 15, 2018

The General Taxation Law provides that a tax assessment in a notice of assessment is deemed to have occurred and been notified if in a period of one month, running from the day following the date of the notice, a decision by the competent authority ordering, among other options, completion of the procedure or the performance of additional audit work has not been notified.

This decision concerned a case in which the authorities had attempted to notify the taxpayer of a decision ordering completion of the audit work before the end of the one-month period running from the signing of the accepted notice of assessment. However, that decision was ultimately notified to the taxpayer after the end of that period.

In this context, TEAC concluded that it is sufficient if the first attempt at notifying the order to complete audit work was made within the one month period for the assessment in the notice not to be deemed to have occurred and been notified, even if the actual notification of the order takes place after the end of the one month period.

3.10 Review procedure.- If new items of proof are produced in the economic-administrative jurisdiction, the court must confine itself to assessing those items

Central Economic-Administrative Tribunal. Decision of October 15, 2018

In the purchase of a property various expenses were paid which the taxable person considered should be added to the purchase price. To substantiate this, in the economic-administrative claim it produced the invoices supporting those expenses. These invoices had not been produced earlier in the audit.

In its decision TEAC accepted that new items of proof could be produced in an economic-administrative claim proceeding. By doing so it reiterated its own interpretation (stated in a decision rendered on November 2, 2017 -Tax Newsletter - September 2017-), based on the Supreme Court's case law (in judgments rendered on April 20, 2017 -Tax Newsletter - May 2017- and September 10, 2018 -Tax Newsletter - September 2018-).

The court did however significantly limit the usefulness of producing these items of proof because it underlined that, in view of these new items of proof, its activity must be confined to assessing them, not carrying out any new review activities (which it is prohibited from doing). In the examined case, the taxpayer's view was not accepted because, in its opinion, the simple fact of being in possession of an invoice does not allow *per se* the recognition of an expense.

4. Legislation of interest

4.1 Latest amendments to the VAT Directive regarding the reverse charge mechanism and the applicable VAT rates on electronic books

Directive 2018/1695 and Directive 2018/1713, both dated November 6, 2018, were published in the Official Journal on November 12 and November 14.

The first directive amends Directive 2006/112/EC concerning the period of application of the optional reverse charge mechanism in relation to supplies of certain goods and services susceptible to fraud and of the quick reaction mechanism against VAT fraud.

The second amends Directive 2006/112/EC concerning the rates of value added tax applied to books, newspapers and periodicals, and allows member states to apply reduced rates of value added tax to certain electronic books.

Our VAT Alert 3-2018 takes a look at the new legislation in this Directive.

4.2 Lenders will pay stamp tax on mortgages and will not be able to deduct it for corporate income tax purposes

As we reported in our Tax Alert 16-2018, Royal Decree Law 17/2018, of November 8, 2018, amending the Revised Transfer and Stamp Tax Law, was published in the Official State Gazette on November 9, 2018

This royal decree-law has introduced the following measures:

(a) In mortgage loan deeds executed on or after November the party liable for stamp tax will be the lender. The related tax debt will not be deductible for corporate income tax purposes by the lender for fiscal years beginning on or after November 10, 2018.

(b) Mortgage collateral loans will be exempt, however, if the borrower is any of the organizations eligible for stamp tax exemptions listed in article 45.I.A) of the Revised Transfer and Stamp Tax Law (central government and regional authorities, not-for-profit organizations, savings banks and banking foundations, the Catholic church and other religious communities with arrangements with the Spanish state, political parties, etc.).

4.3 Approval of the reform of the economic and tax regime of the Canary Islands

Law 8/2018, amending Law 19/1994 which amends the economic and tax regime of the Canary Islands, was published in the Official State Gazette on November 6, 2018 and came into force the day after. This Law was discussed in our Tax Commentary 8-2018.

4.4 Amendments to forms 303, 322, 390 and 347

Order HAC/1148/2018, of October 18, 2018, was published in the Official State Gazette on October 31, 2018 and amends the orders approving the following forms:

(a) Form 322 (monthly self-assessment, individual form), form 353 (monthly self-assessment, aggregate form), form 039 (notification of information) relating to the special VAT regime for groups of entities.

(b) Form 347 (annual return for transactions with third parties).

(c) Form 303 (VAT, self-assessment) and form 390 (annual value added tax recapitulative statement).

(d) Form 036 (census notification for registration, amendment, and deregistration relating to the register of traders, professionals and withholding agents) and form 037 (simplified register notification for registration, amendment, and deregistration relating to the register of traders, professionals and withholding agents).

In addition to making various technical amendments to some of these forms, it has notably changed the filing period for form 347 to February each year in relation to transactions performed in the previous calendar year.

Lastly, it establishes that the new management system for information returns envisaged for 2018 (Transmission of Large Information Volumes with on line validation) will be applicable:

(a) For forms 156, 181, 182, 187, 188, 190, 192, 193, 194, 196, 198, 291, 345, 346 and 347 relating to 2018 that are filed from 2019 onwards.

(b) For all other information returns relating to 2019 that are filed from 2020 onwards.

The Order entered into force on November 1, 2018 and will be applicable, for the first time, to the filing of VAT self-assessments (forms 303 and 322) relating to the last assessment period of 2018 and information returns (forms 390 and 347) relating to 2018.

4.5 Approval of implementing regulations for various articles of the Regulations on Excise and Other Special Taxes

Order HAC/1147/2018, of October 9, 2018, approving the implementing rules for articles 27, 101, 102 and 110 of the Regulations on Excise and Other Special Taxes was published in the Official State Gazette on October 31, 2018. Specifically:

(a) In relation to the **sales en route procedure**, the necessary instructions have been approved for completing and sending the accompanying document to AEAT, the delivery note forms to be issued for each supply associated with the accompanying document, and the instructions for completing the delivery notes and the disclosing electronically to AEAT the information contained in them.

(b) In relation to the exemption envisaged for **aircraft fueling operations**, the delivery receipt form has been approved along with the implementation of the procedure for reporting to AEAT the information contained in the delivery receipts.

(c) As regards the refund application procedure for excise tax on hydrocarbons in **gasoil refueling operations**, the applicable media and procedure for the application have been established and the delivery receipt form applicable to these supplies has been approved.

The Order entered into force on November 1, 2018 and will be applicable to deliveries and refueling operations made on or after July 1, 2019.

5. Miscellaneous

5.1 The Tax Agency clarifies the procedure for yachts entering and leaving EU Customs territory

The Department of Customs and Excise and Special Taxes has published an information notice to facilitate compliance with the tax and customs obligations in the procedure for yachts entering and leaving EU customs territory, as discussed in our **Tax Commentary 7-2018**.

For further information:

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