

SERIES OF  
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TRANSLATION 15

# Spanish Corporation Tax Legislation



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# **Spanish Corporation Tax Legislation**

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# Preface

The translation of legal text, especially those as complicated as corporation tax legislation, requires more than a sound knowledge of the original language in which they were drafted. A good translation requires expertise in the subject matter, in this case tax and accounting principles of Spain and the US and UK. This work combines the skills of tax lawyers at one of Spain's most prestigious law firms, Uria & Menéndez, with the skills and knowledge of UK and US lawyer linguists, thoroughly familiar with the language and legal concepts of Spanish fiscal theory, practice and policy. We have opted to use UK spelling and terminology where different from the usage in the US.

The principal contributors to the English text of this book are, first and foremost, Bill Harrison M.A.(Oxon), Solicitor (England and Wales), who translated and produced the definitive draft of the English text. Other past and present members of the Legal Language Service Group, including Mariana Crist, Ian Shackleton, Santiago Minguela and Patrick Lee also contributed. On the Spanish side, Rafael Vargas and Guillermo Canalejas of Uria & Menéndez clarified concepts and worked with Bill Harrison on the final draft.

We trust that our combined efforts will serve to make this the definitive book in English on Spanish corporation tax. The book is aimed at foreign investors, companies, governments and their tax and legal advisers who have an interest in the rules and key regulations governing corporate taxation in Spain. It is our belief that the pages that follow will serve as a ready and accurate reference for researching, planning and understanding Spanish tax rules and, most importantly, as a basis for discussing particular issues with Spanish counsel.

*Madrid, March 1999*

*Michael Lindner  
The Legal Language Services Group.*

## Nota

Al cierre de la presente edición han sido publicadas una serie de normas en materia fiscal que modifican parte del articulado, tanto de la Ley 43/1995, de 27 de diciembre, del Impuesto sobre Sociedades, como de su reglamento de desarrollo, contenido en el presente libro. Tales normas son las siguientes:

- (i) Ley 40/1998, de 9 de diciembre, del Impuesto sobre la Renta de las Personas Físicas y otras Normas Tributarias, que modifica los artículos 3, 15, 23, 28, 36.bis, 37, 38, 81, 101, 102 y 109 de la Ley 43/1995 del Impuesto sobre Sociedades.
- (ii) Ley 41/1998, de 9 de diciembre, del Impuesto sobre la Renta de No Residentes, que deroga el Título VII y las disposiciones adicionales sexta y séptima de la Ley 43/1995 del Impuesto sobre Sociedades, normas que recoge en su propio articulado. Cuando corresponda, haremos referencia a los artículos de la Ley 41/1998 que sustituyen a los de la Ley 43/1995.
- (iii) Real Decreto 2717/1998, de 18 de diciembre, por el que regulan los pagos a cuenta del Impuesto sobre la Renta de las Personas Físicas y en el Impuesto sobre la Renta de No Residentes y se modifica el Reglamento del Impuesto sobre Sociedades en materia de retenciones e ingresos a cuenta. Esta norma da nueva redacción al capítulo II del Título IV del Reglamento del Impuesto sobre Sociedades aprobado por el artículo 1 del Real Decreto 537/1997, de 14 de abril.
- (iv) Ley 50/1998, de 30 de diciembre, de Medidas Fiscales, Administrativas y del Orden Social que modifica los artículos 7, 9, 19, 26, 35, 97, 108, 116, 117, 118, 120 y 127 de la Ley 43/1995 del Impuesto sobre Sociedades e introduce un nuevo artículo, el 135.bis, y una nueva disposición adicional, la decimoquinta.

## Note

Since this edition went to print, a series of legislative provisions have been issued in the tax field which amend some of the sections of both the Corporation Tax Act (43/1995, of 27 December) and its subsidiary regulations as contained in this book. The provisions are as follows:

- (i) The Individual Income Tax Act (50/1998, of 9 December) and other Tax Provision 50/1998, of 9 December) and other Tax Provisions which amend Sections 3, 15, 23, 28, 36.bis, 37, 38, 81, 101, 102 and 109 of the Corporation Tax Act (43/1995).
- (ii) The Non-Resident Income Tax Act (41/1998, of 9 December) which repeals Part VII and Additional Provisions six and seven of the Corporation Tax Act (43/1995), provisions which are set out in the new Act. Where appropriate we have referred to the Sections of Act 41/1998 which replace those of Act 43/1995.
- (iii) Royal Decree 2717/1998, of 18 December, governing payments on account of Individual Income Tax and the Tax on Non-Resident's Income and amending the Corporation Tax Regulations in relation to retentions and payments on account. This Decree provides a new drafting of Chapter II of Part IV of the Corporation Tax Regulations promulgated by Section 1 of Royal Decree 537/1997, of 14 April.

- (iv) Act 50/1998, of 30 December, on Fiscal Administrative and Social Measures, amending Sections 7, 9, 19, 26, 35, 97, 108, 116, 117, 118, 120 and 127 of the Corporation Tax Act (43/1995) and introduces a new Section, 135.bis, and a new Additional Provision, 15.



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Introduction

Introducción



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# Introduction to the New Corporation Tax

## General Considerations. Special Reference to New Features Introduced by the Corporation Tax Act (43/1995)

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Enactment of the Corporation Tax Act (Act 43 of 27 December 1995; hereinafter 'CTA') and its subsidiary Regulations (Royal Decree 537/1997 of 14 April, hereinafter 'CTR') introduced a new legal framework intended to adapt corporate taxation to the increasingly complex and sophisticated world of economic relations. The incessant development of the tax code seen in recent years (an almost complete overhaul) requires continuous adaptation not just by Spanish taxpayers but also by foreign investors and, above all, by tax professionals in general. Our aim in these brief lines is thus to provide an introductory study and analysis of the CTA and those aspects developed by the CTR to help the reader acquire an overall view of the Act and its Regulations together with a summary of the main new features introduced.

The most important types of company in Spain are the 'Sociedad Anónima' (S.A.) or Joint Stock Company and the 'Sociedad de Responsabilidad Limitada' (S.R.L.) or Limited Liability Company. In this regard, and similarly to other jurisdictions, Corporation Tax is levied on a corporate entity's net taxable income from all sources. In principle, taxable income will as a rule be determined using a direct method of computation based on the taxpayer's accounting records in accordance with the accounting rules. The standard corporation tax rate for resident companies is 35%, similar to other EU member states.

According to the stated purpose of the Corporation Tax Act, the principles that have been fleshed out are:

1. *Neutrality* – taxpayers' business decisions should not be influenced by corporation tax.
2. *Transparency* – corporation tax provisions must be easy to interpret in order to reduce uncertainty amongst taxpayers.
3. *Systematisation* – individual and corporate income tax must be coordinated, especially with respect to issues such as dividend distributions in which double taxation might arise.
4. *International coordination* – Spanish corporate taxation must be in line with other corporate taxes levied in countries with a similar international framework.
5. *Competitiveness* – in line with other economic policies, corporate taxation must promote a more competitive environment for Spanish business.

The first and last of these principles are to a certain extent contradictory. In fact, the first drafts of the CTA focused more on the neutrality principle than the final draft which

## INTRODUCTION

drifted during political discussions in Parliament more towards competitiveness objectives. As a result, the law is a compromise between the two principles.

Before taking up a more detailed examination of the CTA, we should mention that its enactment resulted in repeal of a broad collection of tax legislation previously dispersed amongst a variety of regulatory provisions. Whilst some of the repealed provisions were incorporated into the new Act, albeit with important modifications, a large part have been included (with a large degree of consistency) in the Regulation. As a result of the delayed enactment of the CTR there were major inconsistencies in application of the new rules with continuous references to provisions which had been repealed in part yet still in effect in regard to certain essential aspects of the system as a whole (e.g., *deduction at source*). This perhaps explains why the legislature, aware of the difficulties in applying the new system, included a large number of important transitional provisions to allow a smoother transition from the previous to the new systems (e.g., *financial leases, tax transparency, etc*).

Enactment of the CTR solved a large proportion of these problems, stating in its Final Provision that the Regulations will apply to fiscal periods to which the CTA itself is applicable (those commencing after January 1, 1997). Nevertheless, the new rules on the obligation to deduct at source will only be applicable to deduction obligations arising after the Regulations come into force (April 25, 1997).

Lastly, it should be emphasised that we cannot rule out the possibility of the Government introducing new tax measures to modify the present CTA as a means of alleviating and reducing the public deficit with a view to Spain's full membership in the European Monetary Union such as the package of emergency tax measures implemented by Royal Decree-Acts 7 and 8 of 1996 which, given their special importance, will be mentioned throughout this brief summary of the CTA.

We will begin this analysis of the CTA with a few observations on the scope of application of the new tax, the taxable events involved and taxpayers subject to the tax (*Part 1*). We will then discuss the axis around which most of the modifications introduced in the CTA have revolved: assimilation of taxable income to accounting profit, in all cases assuming the latter has been determined in accordance with applicable accounting standards and principles. In this respect, the new Act introduced major changes as regards adjustments of a tax nature which must be made to accounting profit for the purpose of determining taxable income (*Part 2*).

On the other hand, and although they have important consequences, there have been few changes in relation to the tax period, tax rates and the system of applicable tax credits, which had been sufficiently modified by special tax legislation passed in recent years (*Part 3*).

Nevertheless, for the sake of greater clarity it would have been helpful to have compiled the abundant and still dispersed legal rules applicable to non-residents, individuals or legal entities who obtain income in Spain into a single legal text. Such legislative consolidation has not been carried out, however, and there are still a not insignificant number of contradictions with respect to the rules covering individuals (*Part 4*).

The different special systems provided for in the new Act constitute an important novelty. These special systems constitute a complex framework very different to the previous rules. This is the case, for example, with categories such as *Economic Interest Groups*,

'UTE's (joint ventures), *Venture Capital Funds and Companies*, *Collective Investment Entities*, the *Tax Transparency system* (both domestic and international), *Consolidated Groups*, the special system for *Mergers, Demergers, Asset Contributions and Share Exchanges*, certain types of *financial leases*, *Small and Medium Sized Entities (SMEs)*, and, lastly, the new system for *Foreign Security Holding Companies*. A detailed analysis of each and every change introduced in these systems is of course beyond the scope of this analysis but we have covered the broader features of these special systems (*Part 5*).

## Part I. Scope of Application, Taxable Events and Taxpayers

### A. Scope of Application

Part I (Sections 1 through 3) lays down the nature of the tax and its territorial scope. In theory, the CTA will apply throughout Spain, without prejudice to local tax and economic administration arrangements in effect in the historic territories of the Basque Country and the Navarre Region, where specific regulation have introduced particularly significant modifications and features compared with the general system. These special features are aimed at attracting outside capital and investments to these areas.

Section 3 of the Act, with no substantial modifications, proclaims the primacy of international Treaties and Conventions which have been incorporated into domestic law in relation to corporate taxes.

### B. Taxable Events

Part II of the new Act (Sections 4 through 6) addresses the relevant taxable events which in the case of Corporation Tax is the generation of income. The principal innovation in the new wording is the replacement of the traditional classification of income in the Spanish system (trading income, investment income, and capital gains) with a single global concept of 'income' as net revenue after deducting expenses. The previous classification remains in effect exceptionally, however, in certain areas such as the obligation to deduct at source (on a transitional basis) and the special system applicable to non-residents.

Section 5 lays down a presumption of valuation at normal market value for all transfers of assets and rights. Insofar as this is a *juris tantum* presumption (i.e., a *prima facie* presumption which can be rebutted), the main difficulty consists in establishing what type of evidence can override the presumption (and, moreover, the inclusion of this question in the Chapter covering Taxable Events is highly questionable).

Lastly, Section 6 continues to provide that the income of certain entities, even where they have a distinct legal personality such as some types of partnership regulated by the Civil Code, shall be attributed to their members under Individual Income Tax (IIT) rules, since such entities are transparent for Corporation Tax purposes. Furthermore, as we will see later, there are several entities which are subject to Corporation Tax even though they have no separate legal personality.



## INTRODUCTION

### C. Taxpayers

Part III (Sections 7 through 9) regulates aspects regarding taxpayers and introduces some changes with respect to previous rules. Firstly, it replaces the former general definition of taxpayer for the purposes of CTA with an exhaustive list of the entities concerned. The previous general definition of taxpayer led to considerable vagueness and legislative amendments as a result of the subsequent need to include certain entities without legal personality as taxpayers under the tax and exclude others such as 'civil partnerships' which, notwithstanding their legal personality, were deemed transparent and their income fell within the scope of IIT.

In particular, under the new Act, legal entities (except for 'civil partnerships'), including co-operatives, associations, foundations and, also naturally, commercial companies, are considered subject to Corporation Tax. Commercial companies are the most numerous and include joint stock companies, limited liability companies, general and limited partnerships, mutual guarantee companies and employee-owned companies.

In addition the CTA lists further entities which are liable for Corporation Tax. These include Investment Funds regulated by Act 47/1984 on Collective Investment Undertakings, Temporary Joint Ventures regulated by Act 18/1982, Venture Capital Funds regulated by Royal Decree Law 1/1986, Pension Funds regulated by Act 8/1987, Mortgage Market Buffer Funds regulated by Act 2/1981, Mortgage Market Securitisation Funds regulated by Act 19/1992 and Real Estate Investment Funds.

These entities are subject to CTA and depending on whether they are Spanish residents will be liable for corporation tax on either all income, irrespective of where it is obtained (world wide income), or only on income obtained in this country (income arising in Spain).

The concept of residence is therefore essential in assessing the tax. In theory, entities fulfilling any of the following requirements are deemed to be resident in Spain:

- (i) entities incorporated under Spanish law,
- (ii) those with their registered office located in Spain,
- (iii) those whose place of effective management is located in Spain; for these purposes, an entity will be deemed to have its place of effective management in Spain if the management and control of its activities as a whole are carried out in Spain.

In addition, the address for tax purposes of resident taxpayers is deemed to be their registered office provided that their administration and management is carried out there. Otherwise, the address for tax purposes will be where the said administration and management is located. Where it is not possible to establish the location of the address for tax purposes however, the place where the greater part of their fixed assets value is located will be used.

Finally, Section 9 lists entities and bodies exempt from this tax, removing the distinction between wholly and partially exempt entities. Under the new system, wholly exempt entities and bodies are listed in Section 9, while Sections 133 to 135 provide a new system applicable to partially exempt entities.

The State, autonomous regions and local authorities, autonomous government controlled state administrative bodies, autonomous government bodies of a commercial, in-