Tax Newsletter

TAXAND

GARRIGUES

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1. 2020 personal income tax and wealth tax filing season: how to depreciate inherited or gift properties

In the tax information and on the draft return that the finance authority will make available to taxpayers, greater details will be provided of income obtained from rental property, including a calculation of depreciation expense. The Spanish finance authority, calculates the depreciation expense for inherited or gifted properties only on the cost of investments and improvements made on the property and the expenses and taxes associated with its acquisition.

The March 18, 2021 edition of the Official State Gazette (BOE) published **Order HAC/248/2021, of March 16, 2020**, approving the 2020 personal income tax and wealth tax return forms. The standard time period for filing the draft personal income tax return and the returns for the two taxes runs between April 7 and June 30 2021.

However, if the taxpayer elects to pay from their bank account, as a general rule, the time period ends on June 25, 2021. As an exception, the time period ends on June 30, 2021 for personal income tax returns on which it is elected to pay in two installments, if only the second payment will be taken from the taxpayer's bank account.

Starting on April 7, tax information and draft personal income tax returns may be obtained on AEAT's (Spanish Tax Agency) website.

The order states that the finance authority has enhanced the information it provides to taxpayers, among other elements, in relation to income from movable capital, including calculation of the depreciation expense for properties from the information provided on the 2019 return. In relation to this depreciation expense, however, it needs to be taken into account that the method AEAT has been using for inherited or gifted properties is already been questioned by the courts:

(a) The law states that amounts entered for the depreciation of rented properties are deductible, provided they relate to their actual loss in value. Depreciation meets this actual loss in value test for these purposes if it does not exceed a figure obtained by multiplying the higher of the acquisition cost paid or the cadastral value (not including the land value) by 3%.

(b) In relation to the definition of "acquisition cost paid", the tax authorities have been arguing that the acquisition of an asset by gift or inheritance does not entail any cost for the person acquiring them, other than the taxes or expenses associated with the acquisition. For that reason, they consider that the depreciation basis consists only of those taxes and expenses and, if applicable, the cost of any later improvements or investments made on the property. The 2019 personal income tax return filing program was in fact designed for the depreciation of inherited or gifted properties to be calculated in this way and the depreciation calculated in the 2020 information will foreseeably be based on that interpretation.

(c) Some courts and tribunals (including economic-administrative tribunals) have already been construing, however, that the value having to be taken as "acquisition cost paid" is the actual value of the asset, in other words, the value that was taken for inheritance and gift tax purposes, plus the taxes and expenses associated with the acquisition and any relating to subsequent investments. A few of the most recent are the decision by the Valencian Regional Economic-Administrative Tribunal (TEAR), on November 26, 2020 (see here), the decision by Andalusia TEAR on December 11, 2020; or the rulings by Valencia High Court (**judgment of May 30, 2019**) and Andalusia High Court **(judgment of March 12, 2019**).

2. Judgments

2.1 State aid. - Analysis of state aid cannot depend on the financial situation of the beneficiaries when it was subsequently granted

Court of Justice of the European Union. Judgment of March 4, 2021. Case C-362/19 P

A rule in Spanish domestic law required professional sports clubs (CDs) to become publicly traded sports companies (SADs), with an exception for those that had recorded a positive net income figure in the years preceding the adoption of the law. Several Spanish clubs claimed this exception and continued to operate in the form of a sports club.

Unlike the Spanish SAD sports companies, sports clubs are non-profit legal entities and as such benefit from a special rate of income tax, which, until 2016, was below the rate applicable to SADs. For that reason, the European Commission commenced a formal investigation procedure, in relation to the potentially preferential tax treatment granted to sports clubs.

In its decision, the European Commission concluded that Spain had unlawfully implemented aid in the form of a preferential corporate income tax rate for clubs that continued to operate as sports clubs and that this regime was incompatible with the internal market.

One such sports club lodged an appeal with the General Court, which set aside the European Commission's decision by arguing that it had not demonstrated to the requisite legal standard that the measure at issue conferred an advantage on its beneficiaries.

The European Commission lodged a cassation appeal against this judgment with the CJEU. The CJEU held that the question whether that tax regime confers an advantage on its beneficiaries cannot depend on the financial situation of the beneficiaries at the time of the subsequent grant of that aid, but must necessarily be assessed with reference to the time of adoption of the regime in question, by carrying out an *ex ante* analysis.

The CJEU therefore upheld the cassation appeal and entered into examining the other matters originally pleaded against the decision at issue to the General Court which it set aside in their entirely and so confirmed that decision.

2.2 Taxes on advertising and other sectoral taxes. - The implementation of a progressive system does not amount to state aid

Court of Justice of the European Union. Judgment of March 16, 2021. Case C-596 /19

In this ruling, the CJEU confirmed the **judgment rendered on June 27, 2019** by the General Court of the European Union (GCEU) setting aside the European Commission's decision declaring that the Hungarian tax on advertising was state aid.

The European Commission had reached that conclusion because it considered that (i) the progressive tax rates determined a difference between companies with high advertising revenues and companies with low advertising revenues; and that (ii) the mechanism allowing 50% of losses for companies, which did not obtain income in 2013 gave rise to a selective advantage. The General Court concluded to the contrary that tax mechanisms of this type may include a progressive structure, which, in principle, does not make that system discriminatory for other companies in the sector.

In its judgment, the CJEU dismissed all the grounds submitted by the European Commission in its cassation appeal on the basis that none of the provisions at issue give rise to a selective advantage constituting state aid.

2.3 Corporate Income Tax. - Free movement of capital does not preclude restriction on deduction of tax withheld on a dividend to the tax that would have been due on the dividend in the state of residence

Court of Justice of the European Union. Judgment of February 25, 2021. Case C403/19

A French company received dividends from subsidiaries in Italy, the UK and the Netherlands. Tax was withheld on these dividends in those countries. The shareholder company deducted the withholding taxes in France. The French tax authorities reduced the deduction that could be claimed to the amount of tax that would have been charged in France on the same dividends.

The referring court asked whether the free movement of capital precludes the legislation of a member state that restricts the deduction of foreign tax to the tax that would have been paid on the dividends in the member state of residence of the recipient. The CJEU concluded that this legislation is not contrary to the free movement of capital, because it derives from the parallel exercise of tax jurisdiction by the state of source of the dividends and the member state of residence of the recipient company.

2.4 Corporate Income Tax. - Finance costs on a loan taken out to distribute share premium are not deductible

National Appellate Court. Judgment of February 5, 2021

A company carried out a “concertina” transaction. This involved reducing its capital to zero and immediately afterwards increasing its capital which was subscribed by the shareholders by way of a nonmonetary contribution of shares in another company. This increase was carried out by increasing capital, although a share premium was also created. For the purpose of repaying this share premium, a loan was taken out on the same date.

In an audit, the auditors disallowed the deduction of the finance costs on that loan.

The National Appellate Court confirmed the tax authorities’ method. The court argued that the loan was taken out to benefit the shareholders not the company itself, so the finance costs on the loan did not fulfill the matching revenues and expenses requirement.

At the time of writing two appeals have been admitted by the Supreme Court in which it will analyze a substantially similar issue (admission decisions of February 25, 2021, appeals **5309/2020** and **4762/2020**)

2.5 Personal income tax. - Days of travel must be included for computing exemption for work performed abroad

Supreme Court. Judgment of February 25, 2021. Valencian Regional Economic-Administrative Tribunal. Decision of February 17, 2021

Article 7.p) of the Personal Income Tax Law states that income obtained for work actually performed abroad is exempt subject to certain requirements. At issue was whether days on which the employee travels have to be included for computing the days spent abroad.

Both the Supreme Court and the Valencian TEAR replied that they do. According to both the court and the tribunal, to benefit from the exemption requirements cannot be laid down that are not set out in the legislation and, additionally, the incentive must be interpreted according to its purpose, which is to support international activities by Spanish-resident human capital. For that reason, it is contrary to the logic and purpose of the legislation to exclude from the exemption income received in respect of the days on which the taxpayer travels to or from another country.

2.6 Personal income tax. - Reinvestment in a home under construction is valid for claiming exemption for capital gain on the sale of taxpayer's primary residence

Supreme Court. Judgments of February 11, 2021 and February 17, 2021

A gain on the transfer of a primary residence is exempt if the proceeds are reinvested within two years in another primary residence.

In these judgments, the Supreme Court examined two cases in which the reinvestment was made within the time limit, although in homes under construction, and the building work ended after the end of those two years.

The court concluded that the reinvestment requirement may be considered fulfilled within the time limit because the legislation states that "the amount obtained from the transfer must be reinvested" within two years; but does not state that the taxpayer must obtain ownership of the new home in that period through its physical delivery or that its construction must have been completed.

2.7 Personal income tax. – To reclassify a dismissal as termination by mutual agreement, prima facie evidence must be solid

National Appellate Court. Judgments of December 2, 2020 (appeals 1144/2018 and 2/2018)

The auditors and courts have been reclassifying certain dismissals as terminations by mutual agreement on the basis of prima facie evidence, which entails forfeiture of the right to the exemption under article 7.e) of the Personal Income Tax Law.

In relation to these types of reclassifications, the National Appellate Court concluded that:

(a) For this reclassification to be valid prima facie evidence of the existence of a mutual agreement must be solid.

(b) A solid piece of prima facie evidence would exist if the worker is close to retirement age and has accepted a severance payment below the statutory amount.

(c) By contrast, it is not solid evidence if due to the termination, employer and employee reach an agreement for the employee to keep their pension rights under an insurance policy signed by the employer.

2.8 VAT. - Principal establishment of a company forming part of VAT group and its branch in another member state are separate taxable persons

Court of Justice of the European Union. Judgment of March 11, 2021. Case C-812/19

A company having its principal establishment in Denmark and forming part of a Danish VAT group carries on its activity in Sweden through a branch established in that member state. This branch is not part of any Swedish VAT group. The principal establishment charges to the branch the costs associated with the use of a computer platform for its activities in Sweden.

The question referred to the court concerned whether the Swedish branch must be regarded as a separate taxable person for VAT when it receives the services from its principal establishment.

On the basis of articles 9.1 and 11 of the VAT Directive, the CJEU concluded that the principal establishment of a company situated in a member state, which forms part of a group for VAT purposes formed on the basis of article 11, and its branch (established in another member state) are separate taxable persons for VAT purposes when the principal establishment supplies to the branch services and charges the related costs to it.

2.9 Transfer and stamp tax. - Expiry of statute of limitations for auditing an exemption that is allowed if certain requirements are met is computed from the end of that time period

Supreme Court. Judgment of January 17, 2021

A company bought a few properties to build “government-protected” housing and due to this use reported that the acquisition was exempt for transfer and stamp tax purposes. A condition for claiming the exemption was that in three years the housing units had to obtain a final classification as government protected housing. The company did not obtain that final classification because, before the end of three years, an urban development plan was approved which prevented that classification, despite which it did not file a supplementary return.

At issue was whether the statute of limitations period for assessing the tax started to run, in this case, on the date of approval of the urban development plan that prevented fulfillment of the requirement for the exemption, or after the three-year period had run.

The Supreme Court confirmed that, where “future requirements” cannot be fulfilled (and the legislator grants a specific period for fulfillment), if the person with tax obligations fails to file a supplementary self-assessment, the statute of limitations period starts to run from the end of the time period determined in the legislation for fulfilling the requirements (three years, in this case).

2.10 Tax on customers' deposits at credit institutions in Andalusia. - The deduction for credit institutions having their registered office in Andalusia is contrary to the freedom of movement

Court of Justice of the European Union. Judgment of February 25, 2021. Case C-712/19

The tax on customer deposits at credit institutions in Andalusia (IDECA) was a regional tax, which, from when it was created until 2012 (when it was rendered invalid due to the creation of a national tax) was charged to credit institutions on customer deposits at the head office or local offices situated in Andalusia. The legislation governing the tax contained a deduction system allowing both general deductions (which depended on whether the institution's registered office was in Andalusia and on the number of offices situated in the region) and specific deductions (which depended on the amount used for sustainable economy projects and the amount used for the community projects of savings banks and the fund for education and promotion of credit cooperatives).

In this judgment, the CJEU examined whether the IDECA (in particular, its deduction system) was contrary to the freedom of establishment, the freedom to provide services or the free movement of capital, and whether it must be classified as an indirect tax (instead of a direct tax as determined in the law) contrary to the VAT Directive.

In relation to whether it is contrary to fundamental freedoms, the CJEU concluded that:

(a) The €200,000 deduction allowed for credit institutions whose registered office is in Andalusia is contrary to the freedom of establishment, in that it gives rise to an unjustified difference in treatment.

That freedom does not, however, preclude the €5,000 deduction for every office situated in the region (which, moreover, rises to €7,500 for every office located in a municipality with fewer than 2,000 inhabitants), unless, in practice, it gives rise to unjustified discrimination by reason of the location of the registered office of the credit institutions concerned, a factor that must be determined by the referring court.

(b) The free movement of capital could preclude the legally allowed deductions for sums used for projects carried out in Andalusia, if the purpose of those deductions is purely economic, which is also a factor that has to be assessed by the Supreme Court as the referring court.

In relation to the nature of the tax, the CJEU concluded that the IDECA is not a turnover or similar tax, and is not therefore precluded by the VAT Directive.

2.11 Tax on construction, installation projects and works. - A provisional assessment of the tax on construction, installation projects and works is allowed based on the indexes or modules provided in the local authority tax rules

Supreme Court. Judgment of February 25, 2021

The legislation on the tax on construction, installation projects and works provides that, for the purposes of the provisional assessment of the tax, the tax authorities may determine the taxable amount (i) either by reference to the cost estimate filed by the interested party,

provided it has been approved by the relevant professional association, (ii) or by reference to any indexes or modules set out in the local authority tax rules.

In this judgment, the Supreme Court clarified that, regardless of whether the taxpayer has filed a cost estimate approved by the relevant professional association, the tax authorities are allowed to determine the taxable amount for the tax (provisionally) by reference to indexes or modules in the applicable local authority tax rules; to the extent that the current wording of the legislation governing the tax on construction, installation projects and works does not determine any preference for either method of calculating the taxable amount.

2.12 Tax on economic activities. - An assessment based on information requests and checks made by individuals who are not public officials is void

Madrid High Court. **Judgment of July 30, 2020**

As part of an audit of the tax on economic activities conducted by a local council, the auditor visited the taxable person's home, accompanied by a person was did not have public official status. This individual made various requests for information and checks, which formed the basis of the report and assessment issued as the outcome of the audit.

Madrid High Court upheld the appeal lodged by the taxpayer and concluded that the legal requirements had not been observed to obtain the evidence on which the assessment for fiscal year 2016 was based. According to the court, it is not lawful for individuals other than public officials to carry out functions of authority in relation to an audit, regardless of whether this is done under the supervision or even by following the instructions of an auditor.

2.13 Cadastral values. - The cost/benefit multiplier must not be used in the cadastral valuation of properties with restrictions regarding their sale

Supreme Court. **Judgment of February 25, 2021**

The cadastral value of urban real estate assets is determined using various modules and multipliers, including the so-called "cost/benefit multiplier", relating to the costs and benefits of the business activity for development of the property.

In this judgment, the case was examined of a local council, which had assigned a plot of land for the construction and subsequent operation of a hospital and of a residential care home for senior citizens. A condition for assignment of the land by the local authority was that the building constructed by the entity could not transferred for a ten-month period.

The Supreme Court concluded that the cost/benefit multiplier does not have to be applied in this case for the cadastral valuation of the property, because it has not been built to carry out a real estate development activity.

2.14 Tax penalties. - When a penalty has been voided, another cannot be imposed with retroactive effect

National Appellate Court. **Judgment of January 8, 2021**

TEAC voided a VAT assessment because it considered that it had not been substantiated sufficiently and ordered reversion of the procedure to allow the substantiation defect to be remedied. Because the assessment had been voided, the penalty was also voided.

The tax authorities carried out new auditing work, and after completing it, gave another assessment and issued a new decision imposing a penalty.

In line with the Supreme Court's case law, the National Appellate Court voided the new penalty under the *non bis in idem* principle which prevents a penalty being imposed if an earlier penalty for the same infringement has been voided.

3. Decisions

3.1 Corporate Income Tax. - A tax liability resulting from accounting errors must occur in the fiscal year when the error was identified

Central Economic-Administrative Tribunal. **Decision of January 26, 2021**

In this decision, TEAC concluded that:

(a) Where accounting errors are found in a period occurring after the financial statements have been prepared, the error must be remedied in that later year.

(b) As a result, the income/loss for accounting purposes for the year when the error occurred does not have to be modified, so the corporate income tax base determined by reference to that figure does not have to be modified either. The subsequent year in which the error is identified is when the higher or lower expense or revenue will have an effect on determining the tax base.

3.2 Corporate Income Tax. - For the purposes of calculating the variation in shareholders' equity for the capitalization reserve, the interim dividend must be excluded

Cantabria Regional Economic-Administrative Tribunal. **Decision of September 30, 2020**

An entity paid an interim dividend out of income for the year concerned. For accounting purposes, this dividend was included in the entity's shareholders' equity with a minus sign. To calculate the reduction in respect of the capitalization reserve, the entity excluded that interim dividend from the computation of shareholders' equity.

According to the Corporate Income Tax Law, the reduction in respect of the capitalization reserve has to be 10% of the increase in shareholders' equity. This increase is calculated by reference to the positive difference between shareholders' equity at year-end (not including earnings for that fiscal year), and the shareholders' equity figure at the beginning of the year (not including earnings for the previous year).

On that basis, Cantabria TEAR confirmed the calculation made by the entity. The tribunal warned that reducing shareholders' equity by the amount of the interim dividend (as the tax authorities intended) would mean subtracting the dividend twice because it is paid on an interim basis against earnings for the fiscal year.

3.3 Corporate income tax. - No limits on amount or time for claiming the credit for reversal of depreciation that was not deducted in 2013 and 2014

Valencian Regional Economic-Administrative Tribunal. **Decision of July 30, 2020**

In fiscal years 2013 and 2014, the depreciation or amortization expense for property, plant and equipment, intangibles and real estate investments was subject, generally, to a limit equal to 70% of the expense for accounting purposes. In or after 2015, the portion that had not been deducted in the preceding two years could start to be recovered. However, because the tax rate in 2013 and 2014 was 30%, but was lowered to 28% in 2015 and to 25% starting in 2016, the legislation allows a tax credit to be claimed equal to 5% (2% in 2015) of the sums reversed each year.

In this decision, the case was examined of an entity that applied for correction of its 2015 self-assessment, because it forgot to claim the described tax credit. After the correction, the tax credit could be carried forward to future years. In its 2016 self-assessment, the entity claimed both the unused tax credit for reversal relating to 2015 and the tax credit for that fiscal year 2016.

In a management procedure, the tax authorities concluded that the tax credit for a specific year could not exceed 2% (2015) or 5% (from 2016 onwards) of the amounts included in the tax base for the year concerned, in respect of reversal of those timing measures. In other words, in any year tax credits for previous years cannot be claimed on top of the tax credit for that year.

Taking the opposite view, the Valencian TEAR accepted the company's arguments on the basis of transitional provision 37.3 of the law, according to which "any amounts not deducted due to insufficient gross tax payable may be deducted in subsequent taxable periods". The tribunal added that otherwise taxpayers would never have the chance to deduct unused amounts from prior years.

3.4 VAT. - The time period for applying for a refund to non-established entities begins with the issuance of the invoice entitling to exercise the right to a deduction

Central Economic-Administrative Tribunal. **Decision of November 19, 2020**

The tax authorities denied the right to a VAT refund requested in the procedure for non-established entities under article 119 bis of the VAT law. The tax authorities argued that the entity had corrected the invoices to bypass the statutory time period for requesting a refund.

TEAC made the following statements in this decision:

(a) The time period for requesting a refund for non-established entities is a nontollable time bar period that starts to run when the tax is actually incurred, in other words, when the relevant invoice is received.

(b) If the original invoice has defects preventing the right to a refund from being exercised, the VAT is not deemed to be incurred and therefore that nontollable time bar period for requesting a refund does not start running, until the correction invoice is received that will allow the right to a refund to be exercised.

(c) If, however, the original invoices do allow the right to a refund to be exercised, the VAT is deemed to be incurred on receipt of that invoice. In that case, any subsequent correction of the invoice is irrelevant.

In the examined case, the tribunal held that the correction invoices submitted by the claimant (in which it had only broadened the description of the services) were irrelevant for the purposes of computing that nontollable time bar period, because the original invoices did allow the right to the refund to be exercised.

3.5 VAT. - Modification of the taxable amount in the event of insolvency proceedings on the customer is allowed if the parties are not related

Central Economic-Administrative Tribunal. Decision of January 25, 2021

An entity modified its taxable amount as allowed by article 80.Three of the VAT Law in cases where an insolvency order has been issued on the customers for the transactions. Both entities (the one that performed the transaction and the customer) were more than 25% owned by the same shareholder, although before performing the transaction, the sole shareholder had shed its interest in the customer entity. At the time the transaction was performed, however, the transaction had yet to be registered at the Commercial Registry.

In a limited review procedure, the tax authorities found that the modification of the taxable amount was not allowed because, in their opinion, the entities were related to each other.

TEAC concluded that they were not related because when the transaction was performed, the shares that gave the claimant's sole shareholder a 25% ownership interest in the customer for the transactions had been transferred. According to the tribunal, a failure to register the share transfer at the Commercial Registry is not an obstacle to that conclusion.

3.6 VAT. - It lies with the taxable person to report that its intra-Community acquisitions were taxed in the member state of arrival to prevent application of the anti-fraud rule

Central Economic-Administrative Tribunal. Decision of January 25, 2021

A Spanish entity purchased used vehicles in another EU member state, and notified its suppliers of its VAT ID number supplied by the Spanish tax authorities. However, those vehicles were taken to a third EU member state where the purchased vehicles were delivered to individuals. In an audit, the tax authorities found that those acquisitions should have been subject to VAT in Spain under article 71.Two of the VAT Law, and the self-charged VAT was not deductible because the vehicles had not been used for the performance, in the VAT area, of any transactions giving the right to a deduction.

TEAC confirmed this conclusion. According to the tribunal, intra-Community acquisitions are made in the Spanish VAT area if the purchaser in the transactions has notified the seller of a Spanish VAT ID number, and VAT has not been charged on them in the member

state of arrival of the goods or of the transport, and it is up to the entity to prove that the acquisitions were taxed in the member state of arrival to prevent application of this anti-fraud rule.

The tribunal recalled that the taxable person is not entitled to deduct the input VAT incurred on these acquisitions, because the goods are not entered into Spain and therefore are not used for the needs of the taxed transactions.

Moreover, it transpires from EU case law it that if it were allowed to deduct this VAT in the member state of identification, any incentive would be lost to report the intra-Community acquisition in the member state of arrival, in other words, in the member state of final use.

3.7 VAT. - Discounts granted to dealerships in the sale of financed vehicles with the financing entity defraying the cost do not reduce the taxable amount for that sale

Central Economic-Administrative Tribunal. Decision of October 21, 2020

The claimant, a company engaging in the sale of vehicles to a dealership network, carried out marketing initiatives to boost sales. In one of these initiatives, discounts on the final price of the vehicle were offered if the customer financed the vehicle purchase with the group's finance provider. The cost of the discounts was assumed partly by the claimant and partly by the finance provider.

The discounts were recorded as follows:

(a) The entity issued correction invoices to customers on which it included all the discounts, in other words those defrayed by the entity itself and those defrayed by the finance provider.

(b) The entity also issued another invoice to the finance provider, in respect of intermediation services in the financing transactions, for an amount equal to the discount defrayed by that finance provider.

The tax authorities concluded that the discounts granted by the finance provider are part of the price for the sale of vehicles. In other words, the amount of these discounts does not have to be subtracted from the taxable amount.

TEAC confirmed that those discounts do not have to reduce the taxable amount for the sale of the vehicles, because a third party covers them. It stated that the amount obtained by the claimant (the seller of the vehicles) is the same no matter whether the financing transaction is signed or not.

3.8 Principle of legitimate expectations. - A change of method making taxpayers worse off cannot be applied retroactively

Central Economic-Administrative Tribunal. Decision of June 11, 2020

An entity elected the tax neutrality regime for a partial spin-off. That election was made in view of the DGT's reply to an issue submitted by the entity itself for resolution, in which the definition of line of business had been construed under the method employed by the tax

authorities at that time. The auditors, however, rejected the ability to claim the special regime based on subsequent TEAC decisions and Supreme Court judgments that had drawn different conclusions in relation to that definition of line of business.

Based on the protection given to the taxable person by the principles of legal certainty and of legitimate expectations and in line with earlier rulings by both the National Appellate Court and the Supreme Court, TEAC concluded that the taxable person's decisions had to be observed if they were supported by the interpretation employed by the DGT or AEAT when it took those decisions.

This means that, if the Supreme Court or TEAC change an earlier method, their change of view binds all the tax authorities only from when that change of method occurs, and they cannot adjust earlier positions in which taxpayers applied a method employed by the tax authorities.

A **Supreme Court decision rendered on December 17, 2020** admitted a cassation appeal in which this issue will be re-examined.

3.9 Electronic notices. - Since Law 39/2015 came into force, AEAT is not obliged to notify the inclusion in the electronic address system for entities required to deal with the public authorities by electronic means

Central Economic-Administrative Tribunal. Decision of January 25, 2021

The tax authorities left a notice of the commencement of a limited review procedure at the electronic address allocated to a legal entity. Since the entity did not access it contents in ten calendar days, the notice was deemed to be given. The same occurred with the decision to commence a penalty proceeding and later with the decision to impose a penalty.

The Aragonese TEAR held, as the company had argued, that unopened notices were defective, because AEAT had not proven that it had given prior notification of the taxpayer's inclusion in the allocated electronic address system.

TEAC, however, concluded that, following the entry into force of Law 39/2015, of October 1, 2015, AEAT is no longer required to give prior notification of inclusion in the allocated electronic address system for legal entities and entities without a separate legal personality, which have to deal with the public authorities, by electronic means. TEAC clarified, however, that the notification obligation remains in force, following the entry into force of Law 39/2015, with respect to individuals fulfilling certain requirements.

3.10 Management procedure. - In a limited review procedure the deduction of an impairment loss for accounting purposes could not be adjusted because the accounting records could not be examined

Galician Regional Economic-Administrative Tribunal. Decision of September 16, 2020

An entity recognized financial assets for accounting purposes as "held for sale" and recorded an impairment loss, which was deducted on its corporate income tax return. In a limited review procedure, the authorities found that the loss was not deductible. To reach this conclusion, the authorities examined the financial statements filed at the commercial registry.

The taxpayer argued against this that the assets had been recorded for accounting purposes as held for sale by mistake; and that they were, it pleaded, financial assets held for trading.

The Galician TEAR held that the burden of proof as to the correct recording in accounting records lies with the taxpayer. It recalled, however, (based on previous TEAC decisions) that where it is necessary to review the accounting records, the tax authorities must end the limited review procedure and commence an audit procedure. Because this had not been done, the tribunal voided the appealed assessment.

3.11 Management procedure. – Scope of the procedure given in the notice of commencement must specify items, taxes and years to be reviewed

Valencian Regional Economic-Administrative Tribunal. Decision of July 30, 2020

The tax authorities commenced a limited review procedure. The scope of the procedure, as it appeared in the notice of commencement, consisted of "reviewing the incidents detailed in the reasons for this notice".

The Valencian TEAR held that determining the scope of work in these terms was the same as not determining it at all or omitting items from it. According to the tribunal, the vagueness or generality with which that scope was defined prevents the taxpayer from knowing from the start the items on which the review will be made and its extent or breadth in relation to each of the potential items to be reviewed, which impairs the taxpayer's right to defend itself.

It therefore voided the challenged act by the authorities without needing to hear the facts of the case.

3.12 Audit procedure. – An assessment is not void by operation of the law, even if items falling outside the scope of the procedure were examined

Central Economic-Administrative Tribunal. Decision of February 18, 2021

A company underwent a partial audit relating to corporate income tax and VAT. In the assessments, items were adjusted that fell outside the scope of the procedure.

TEAC concluded that:

(a) The assessment was incorrect because it was issued without observing the scope included in the notice of commencement of audit work.

(b) However, the assessment was not issued by completely and absolutely ignoring the legally established procedure, but rather within the most suitable procedure (an audit). Therefore, the committed error does not render the assessment void by operation of the law and can therefore be corrected.

Consistently with this conclusion, TEAC ordered the procedure to be reverted so that, on a reasoned basis, the scope of the audit work could be extended and if necessary a new assessment could be issued based on this broader scope.

This principle has been reiterated by the TEAC because it reached the same conclusion in its **decision in July 2020**.

3.13 Extension of liability. - Failure to give reasons in a penalty decision prevents extension of liability to the main debtor's director

Madrid Regional Economic-Administrative Tribunal. Decision of December 22, 2020

Following an adjustment by the authorities to an entity, various penalties were imposed on it for serious infringements under article 191 of the General Taxation Law, due to arguing that there had been concealment, as a result of failure to provide the required standard of care for correctly calculating its tax liability. In the reasons given for the penalties, the tax authorities stated that they had not found the existence of an involuntary error or reasonable discrepancy between methods, and therefore it had to be concluded that the requirement for the existence of fault was fulfilled, at least in the degree of ordinary negligence.

As a result of the decision determining fault on the part of the entity, a decision to extend liability to its directors was notified.

Madrid TEAR recalled that the procedure for extending secondary liability under article 43.1.a) of the General Taxation Law requires the fulfillment of two requirements:

(a) A requirement relating to the facts involved, consisting of the existence of tax infringements committed by the main debtor.

(b) A requirement relating to the person involved, consisting of the existence of conduct that is at least negligent by the liable person, determining the commission of tax infringements by the company.

Reasons must be given for determining the fulfillment of both requirements.

The TEAR found that, in this case, sufficient reasons had not been given to support the requirement relating to the person involved because the penalty decisions had been supported by generic and stereotype reasons, in that no mention had been made of specific negligence or fault on the part the main debtor entity.

This failure to give reasons for the penalties from the start makes it unnecessary to assess the degree of negligence attributable to the director in relation to the infringements committed by the main debtor; and it is sufficient in and of itself to void the decision declaring liability.

3.14 Collection procedure. - Attachment of community property for payment of separate debt of one of the spouses may be stayed while community property arrangement is dissolved and liquidated

Madrid Regional Economic-Administrative Tribunal. **Decision of December 22, 2020**

The tax authorities sought to attach community property to collect payment of a debt owed individually by one of the spouses.

After receiving the notice of attachment, the debtor spouse asked for the attached property (forming part of the community property arrangement) to be replaced by the debtor spouse in the community property arrangement, as determined in article 1373 of the Civil Code. According to this article “each spouse is liable with their personal assets for their own debts and, if their own separate property is not sufficient to pay those debts, the creditor may request the attachment of community property, which shall be notified immediately to the other spouse, and that other spouse may require that in placing the attachment the common property is replaced with the portion owned by the debtor spouse in the marital property system, in which case the attachment will entail dissolution of that system”.

Madrid TEAR concluded that the tax authorities should have stayed enforcement of attachment of the property. This stay does not mean that the attachment is lifted, it only stops

collection activities for the length of time needed to secure orderly dissolution and liquidation of the community property arrangement. The attachment of community property may be lifted, according to the tribunal, where it has been replaced with the separate property allocated to the debtor spouse in a final court decision.

3.15 Penalty procedure. - The 25% reduction applies even if payment of the penalty is deferred or split with a dispensation from having to provide security

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

In the examined case, a deferral was granted with a dispensation from having to provide security in relation to certain penalties, because the taxpayer did not have sufficient assets to secure the debt.

In this scenario, the TEAC was asked whether the 25% reduction applicable for penalties paid in cash is compatible with the granting of deferred or split payment.

TEAC concluded that the taxpayer's right to deferred payment cannot prevent it being entitled to a reduction to the penalty, even if security has not been provided, in cases legally exempt from providing security; regardless of whether this dispensation derives from exemption from the obligation to provide security because the penalty does not exceed the amount required in the regulations (currently, €30,000), or if it is decided because the party required to pay it does not have sufficient assets to secure the penalty in cases where the enforcement of payment against its assets could materially affect its ability to retain its production capacity and the level of employment of the economic activity, or serious breaches against the finance authority's interests could occur.

3.16 Review procedure. - Pleadings submitted in the abbreviated proceeding after filing the claim must be examined by the tribunal, unless a decision has already been rendered

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

The abbreviated proceeding for economic-administrative claims requires pleadings to be submitted in the claim instrument.

TEAC concluded however that the tribunal must consider pleadings submitted after the claim has been filed, unless a decision ending the proceeding has been rendered.

TEAC also examined whether notice of an administrative decision has been given if the interested party became aware of it after entering AEAT's website voluntarily, even though it was not required to receive notices by electronic means; to which the reply was yes. According to the tribunal, notices may be served either by electronic means consented to

by the taxpayer, or on the website of the competent tax authorities if the interested party visits the website voluntarily, even though it is not required to receive notices by electronic means.

4. Resolutions

4.1 Corporate income tax. - Tax neutrality regime applies to reverse partial spinoffs of stock

Directorate General for Taxes. Resolution V3550-20 of December 14, 2021

The issue concerned a transaction in which a company (A) will spin off its majority interest in another company (B), for the benefit of this latter company. In other words:

(a) Company A will reduce its equity with a charge to unrestricted reserves in an amount equal to the value of the spun-off assets (majority interest in company B).

(b) The beneficiary of the spinoff will be company B itself and A's shareholders will receive shares in B in proportion to their ownership interests in A.

From a corporate law standpoint, this transaction has been admitted by the Directorate-General for Registries and the Notarial Profession, which confirms its viability and validity.

The DGT concluded that the tax neutrality regime could be elected for this reverse spinoff of stock if (i) it is classified as a spinoff and not as a distribution of reserves for corporate law purposes; and (ii) the spinor (A), after hiving off its interest in B, keeps in its assets a line of business or a majority interest in another entity or other entities.

The DGT added that in principle it must be considered that this transaction is performed for valid economic reasons, unless its primary aim is the distribution of reserves in kind (avoiding the tax consequences associated with this distribution).

4.2 Personal income tax. - A benefit for a dependent child paid by a foreign social security regime may be tax exempt

Directorate General for Taxes. Resolution V0100-21 of January 28, 2021

The requesting individual, who is tax resident in Spain, works from home in Spain (where they live with their partner and 2-year-old daughter) for a company resident in Switzerland. They contribute to the Swiss social security system from which they receive a benefit for a dependent child.

The DGT concluded in this resolution that insofar as this is a benefit for a dependent child coming from a foreign public social security regime it is protected by the exemption allowed in article 7 h) of the Personal Income Tax Law for public benefits for births, multiple births or adoptions, adoptions, dependent children or orphanhood.

4.3 Personal income tax. - Clarification given as to how a property lease is taxed in various rent reduction or deferral scenarios

Directorate General for Taxes. Resolution V0081-21 of January 22, 2021

Various property-leasing scenarios are examined in which the received rent is lower than the originally agreed amount or the payment of rent is deferred:

(a) Case 1: Lessor and lessee agree on a reduction to the amount originally determined as the rental price (whatever the amount of the reduction). In this case:

(i) The whole amount of income from immovable capital relating to the periods falling within the reduction agreement will be the amount relating to new sums agreed by the parties.

(ii) The expenses incurred in the period included in the modification may be deducted.

(iii) The reduction may be claimed for any leased real estate assets used as homes.

(iv) Although if in any of the periods the lessee does not have to pay rent, no real estate income can be attributed.

(b) Case 2: Lessor and lessee agree on a deferral of rental payments:

(i) In the months in which no rent has to be paid, revenues do not have to be included to calculate the relevant income from immovable capital. The expenses incurred in those periods can be deducted however.

(ii) Nor will any income be generated in those periods under the mechanism for imputing real estate income.

(iii) The reduction for leasing residential properties may be claimed if applicable.

(c) Case 3: No agreement is reached to modify or reduce the amount determined as the rental price or to defer its payment, but all or part of the rent is not paid on its due date. In this case:

(i) The unpaid rent must be attributed as gross revenues.

(ii) Uncollectible rent may be deducted as expenses after six months or where the debtor is in an insolvency proceeding.

In 2020 and 2021, the six-month time period was lowered to three months under article 15 of Royal Decree-Law 35/2020, of December 22, 2020, on urgent tax measures to support the tourism, hospitality and retail industries.

If and when the debt that gave rise to a deductible expense is collected, an amount of revenue must be computed.

(iii) The expenses incurred cannot be deducted.

(iv) Real estate income cannot be imputed.

(v) The reduction for leasing residential properties may be claimed if applicable.

4.4 Personal income tax. - The reduction for multi-year income cannot be claimed for an indemnity payment due to termination of the contract of a professional service provider

Directorate General for Taxes. Resolution V0074-21 of January 22, 2021

An architect who had a contract for services with a sports association submitted the issue. In view of the potential termination of the contract by the association, it was asked whether the 30% reduction could be claimed in respect of the indemnity.

The DGT replied that this was not allowed based on the following arguments:

(a) The indemnity is not received by reference to the length of the contract for professional services, but rather in respect of termination of the contract itself, from which the right to receive the indemnity arises. Therefore, it is not generated over a period of more than 2 years. The DGT recalled that the legislation governing the reduction for income from economic activities does not allow the number of years that the worker has provided services to the company to be included in the period in which the income was generated (unlike for multiyear salary income).

(b) Nor is it an amount of income from an activity that may be classed as income obtained clearly on a multi-year basis over time. On the list of income obtained clearly on a multiyear basis, the legislation mentions indemnity and aid in respect of the termination of economic activities, but in this case the indemnity does not result from termination of an activity, instead only from termination of a contract.

4.5 Personal income tax. - DGT clarifies how property lease with call option is taxed

Directorate General for Taxes. Resolution V0049-21 of January 18, 2021

The owner of business premises who intended to lease them with a call option submitted the issue. The lease agreement is for a 2-year term. In that time period, the owner will receive rental income. If at the end of that period the option is exercised all amounts paid earlier in respect of rent will be subtracted from the price payable.

Because the lease is not managed with the minimum organizational structure required for the existence of an economic activity, the lessor/seller will obtain the following amounts of income:

(a) Rental income, which will be classified as income from immovable capital and included in the general component of taxable income.

(b) Income from the grant of the call option on the property, which will be classified as a capital gain and will also be included in the general component of taxable income because it is not obtained from a transfer. Its amount will be determined by reference to the value actually obtained, unless it is below market value, in which case market value will prevail. All expenses and taxes associated with the transaction that have been paid by the option or will be deducted from this value. The gain must be attributed in the taxable period in which the call option right is created on the property.

(c) Income obtained from the transfer of the property, if the call option is ultimately exercised. The amount of the gain or loss must be determined under the general rules, although the transfer price must be reduced by:

(i) The amount already received in respect of the call option.

(ii) The rent received over the lease term.

The capital gain or loss must be attributed in the taxable period in which the call option is exercised and included in the savings component of taxable income.

4.6 Personal income tax. - Special valuation rules for salary income in kind do not apply to income from economic activities

Directorate General for Taxes. Resolution V0032-21 of January 15, 2021

The issue was submitted by an individual, who provided services as independent contractor to a company and obtaining income from economic activities. The company pays for those services by giving the individual use of a vehicle for professional use. It was asked whether the value of that use may be determined under the rules in the Personal Income Tax Law for salary income in kind (20% of the acquisition cost or market value as new, depending on whether or not the vehicle is owned by the company).

The DGT concluded that, where the use of vehicles generates income from the activity, the special valuation rule in the Personal Income Tax Law for salary income in kind is not applicable. Therefore, in the submitted case the income must be valued at its normal market value.

5. Legislation

5.1 The new double taxation agreement between Spain and China has been published

The March 30, 2021 edition of the Official State Gazette published the new **Agreement between China and Spain for the elimination of double taxation**, done at Madrid on November 28, 2018.

The main elements of this agreement are described below:

(a) The agreement contains a specific clause for income received by persons who are wholly or partly transparent for tax purposes.

(b) **Dividends** may be taxed, in general, at a rate not exceeding 10%. The rate is lowered to 5% if the beneficial owner is a company (other than a partnership) which holds directly at least 25% of the capital of the company paying the dividends throughout a 365 day period that includes the day of the payment of the dividend. There are also exemptions for dividends paid to beneficial owners, which are public, or government-owned entities.

(c) **Interest** may be taxed at a rate not exceeding 10% if the beneficial owner of the interest is a resident of the other state. There are exemptions however for interest paid to beneficial owners, which are public entities or government-owned entities, or for the sale on credit of commercial or scientific equipment.

(d) **Royalties** may be taxed at a rate not exceeding 10% if the beneficial owner is a resident of the other state.

(e) In relation to **capital gains**, the treaty contains a clause on real estate companies, meaning companies deriving more than 50% of their value directly or indirectly from real estate assets situated in the other state, not including any real estate assets that are used for conducting the company's business.

There is also a clause on the taxation of gains obtained by holders of a significant interest (holding directly or indirectly at least 25% of the capital of a company) with a few exceptions for shares transferred on stock exchanges.

(f) **Double taxation tax credits:** Both states allow the tax credit method of eliminating double taxation.

(g) It is specified in the **Protocol** that the limit on the tax rates for dividends, interest and royalties must be directly applied rather than through a levy-then-refund procedure, where the rates are lower than those stipulated in the domestic law of the state in which the income arises.

(h) A **clarifying provision** has been included to specify that nothing in the agreement may prejudice the right of each state to apply its domestic laws and measures concerning the prevention of tax avoidance, whether or not described as such, insofar as they do not give rise to taxation contrary to the agreement.

The date given for its entry into force is May 2, 2021 and it will have effect, for taxes not withheld at source, in the years beginning on or after that date.

The previous 1990 treaty will largely cease to have effect from the date the provisions of the new agreement become applicable. However, the provisions of article 23 ("Capital") of the 1990 agreement will cease to have effect from December 31, 2021.

5.2 Publication of the annual equivalent rate for second quarter of 2021, for the purpose of characterizing certain financial assets for tax purposes

The March 29, 2021 edition of the Official State Gazette (BOE) published **the decision of March 24, 2021, by the Office of the General Secretary for the Treasury and International Finance**, which, as is now the custom, sets out the reference rates that will apply for the calculation of the annual effective interest rate for characterizing certain financial assets for tax purposes, this time for the second calendar quarter of 2021. The rates are as follows:

(a) Financial assets with terms equal to or shorter than four years: -0.317 percent.

(b) Financial assets with terms longer than four years, but equal to or shorter than seven, and for assets with longer terms: -0.200 percent.

(c) Assets with ten-year terms: 0.281 percent.

(d) Assets with fifteen-year terms: 0.530 percent.

(e) Assets with thirty-year terms: 1.038 percent.

In all other cases, the reference rate for the period closest to the period when the issuance is made will be applicable.

5.3 International agreement on tax between Spain and the UK in relation to Gibraltar published

The March 13, 2021 edition of the Official State Gazette (BOE) published the **International Agreement** on tax and the protection of financial interests between Spain and the United Kingdom, signed "*ad referendum*" in Madrid and London on March 4, 2019. The key measures in this agreement were discussed in advance in our **Abril 2019 Newsletter**, and relate mainly to determination of the tax residence of individuals and legal entities and administrative cooperation in the tax field. In relation to this element:

(a) It specifies enhanced administrative cooperation with a view to exchanging information that is relevant to the administration, enforcement and collection of taxes.

(b) From the date on which EU law ceases to apply in Gibraltar, the parties will apply measures that have equivalent effect to the principles and modalities of EU legislation regarding mutual assistance.

(c) The exchange of information between Spain and Gibraltar will consist mainly of: (i) annual information on cross-border workers, (ii) six-monthly information on vessels, aircraft and motor vehicles, (iii) direct and free access to the records of the Registrar of Companies in Gibraltar and to the Gibraltar Land Registry, (iv) direct access to beneficial ownership information as is public or, on request to the Commissioner of Income Tax in Gibraltar, on companies, any body corporate, partnerships and foundations; and (v) direct access to information as is public or otherwise available to the Commissioner of Income Tax in Gibraltar on the settlors, trustees, beneficiaries, assets of all types of trusts, etc.

The first exchange of information relating to cross-border workers and information on vessels, aircraft and motor vehicles will be in respect of periods commencing on or after January 1, 2014 until the date of entry into force of the Agreement, on March 4, 2021. Any other exchange of information will be in respect of periods commencing on or after January 1, 2011.

This agreement entered into force on March 4, 2021 and started to have effect from that date. However:

(a) The rules relating to the residence of individuals and legal entities will have effect in taxable periods commencing on or after March 4, 2021. Where there are no taxable periods, they will have effect in respect of tax obligations arising on or after March 4, 2021.

(b) The rules relating to administrative cooperation in tax matters have effects:

(i) For taxable periods that commenced on or after January 1, 2014, in respect of the exchange of information on cross-border workers and information on vessels, aircraft and motor vehicles.

(ii) For taxable periods that commenced on or after January 1, 2011 and, where no such period exists, for tax obligations arising on January 1, 2011, in all other cases.

5.4 COVID-19.- Transactions carried out and charged to companies' Recapitalization Fund will be exempt from any national, regional or local taxes

Royal Decree-Law 5/2021 of March 12, 2021 approving new extraordinary measures supporting the solvency of businesses to mitigate the effects of the pandemic was published in the Official State Gazette on March 13, 2021.

In our **alert on March 15, 2021**, we analyzed the key measures in the tax field.

5.5 ATAD 2 Directive. - Spanish anti-hybrid legislation approved

On March 10, 2021, **Royal Decree-Law 4/2021, of March 9, 2021** was published, which transposes Council Directive (EU) 2016/1164 of 12 July 2016, amended by Council Directive (EU) 2017/952 of 28 May 2017 (ATAD II Directive), as regards "hybrid mismatches", and amends the corporate income tax and nonresident income tax laws.

We discussed this royal decree in our alert **on March 10, 2021**.

5.6 Belarus-Spain tax treaty published

The **Agreement between Belarus and Spain** for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital, done at Madrid on June 14, 2017 was published in the Official State Gazette (BOE) on March 2, 2021..

The main elements of this treaty are described below:

(a) **Dividends** may be taxed at up to:

(i) 0%, if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividends and this interest amounts to at least €1,000,000.

(ii) 5%, if the beneficial owner is a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividends.

(iii) 10%, in all other cases.

(b) **Interest** may be taxed at up to:

(i) 5%, if the beneficial owner is resident in the other state.

(ii) 0%, if the interest is paid to public agencies in the other contracting state or to financial institutions or pension funds.

(c) **Royalties** may be taxed at up to 5%, if the beneficial owner is resident in the other state.

(d) **Capital gains** obtained from the alienation of shares or similar rights deriving more than 50 per cent of their value directly or indirectly from immovable property situated in a contracting state may be taxed in that state.

(e) **Elimination of double taxation:** Both states allow the credit method for taxes on income paid in the other state.

The treaty states that it will enter into force on May 9, 2021 and will be applicable (i) in respect of taxes withheld at source, on the amounts paid or owed to nonresidents on or after that date; and (ii) in respect of other taxes, in fiscal years commencing on or after that date.

When the new agreement has effect, the agreement between Spain and the Union of Soviet Social Republics for the avoidance of double taxation on income and wealth, signed on March 1, 1985, will cease to be applicable in respect of relationships between Spain and Belarus. However, articles 24 (on the mutual agreement procedure) and 25 (on the exchange of information) of the new treaty will apply in relation to every tax, mutual agreement procedure or information covered by those articles, even where the matters related to them existed before the entry into force of the new treaty or the date on which it has effect.

6. Miscellaneous

6.1 AEAT publishes information notice on claiming the international juridical double taxation tax credit

The Central Office for Large Taxpayers has published on AEAT's website a **Notice on claiming the international juridical double taxation tax credit** under article 31 of the Revised Corporate Income Tax Law and of the currently in force Corporate Income Tax Law.

AEAT recalled that:

(a) Proof must be provided of actual payment of the tax in the other state.

(b) If a double taxation agreement exists (DTA), withholding taxes may only be deducted consistently with the DTA. For these purposes, the taxpayer must provide proof of the income received.

(c) The limit on the gross tax payable that would have to be paid in Spain is calculated on the net income obtained in the other state.

AEAT adds that, since 2015 (in other words, since the current Corporate Income Tax Law has been applicable), any foreign tax that has not been deducted due to exceeding that limit will be deductible for determining the tax base provided it relates to the performance of activities abroad, but that, for these purposes, any withholding that was made without observing the provisions of a double taxation agreement cannot be deducted from the tax base.

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