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GARRIGUES

Latest developments and legal trends - Legislation of interest

News Roundup - Judgments

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1. Not electing the special inbound expatriates regime within the time limit implies that the standard personal income tax regime has been chosen

A recent Supreme Court judgment held that if a taxpayer fails to notify on time the decision to elect the special inbound expatriates regime, it is considered that the standard regime has been chosen. This decision recalled the importance of acting with extreme caution when deciding over tax options on tax returns.

The regime for workers sent to Spain allows taxpayers who become Spanish resident to be taxed as nonresidents (subject to a few special rules) in the period in which they acquire their tax residence and in the following five years. Currently this special regime is subject to various requirements and among them the taxpayer has to give notice of election of the regime. This notice must be given within six months from the commencement date of the activity appearing in the notification to the social security authorities in Spain or in the document allowing the taxpayer to stay with the social security legislation of their home country.

This regime has been applicable since January 1, 2004, although the form for electing the regime was approved by ministerial order a few months later. For this reason, it was specified then that anyone who had acquired tax residence in Spain in 2004 or acquires it in 2005 could elect this special regime in the two months following publication of this order (in other words, within two months running from June 11, 2014).

In judgment 1102/2020, delivered on May 18, 2020, the Supreme Court examined the case of a taxpayer who gave notice of his election longer than two months after June 11, 2004; and concluded by denying the right to the special regime. The court found as follows:

a) That two-month time limit was a mandatory requirement for claiming the special regime not simply a procedural requirement.

b) Due to being a requirement defined in the law as an “option”, the taxpayer cannot change it after the end of the time period determined in the law, as specified article 119.3 of the General Taxation Law. This article states that tax options cannot be corrected after the end of the fining period for the return.

c) In short, by not filing the notice on time, it is "as if" the taxpayer had elected to apply the standard personal income tax regime.

The court would predictably reach the same conclusion in relation to the current six-month period mentioned above.

This judgment, together with many others on the tax options rules (which show a very flexible interpretation of the definition of "option"), make it advisable to act great caution when making decisions on tax returns.

2. Judgments

2.1 Personal income tax.- Employers have to evidence that the paid per diems relate to trips for work, even if the recipient is the company's director

Supreme Court. Judgment of May 18, 2020

The Personal Income Tax Law states that certain per diems for traveling, subsistence and accommodation expenses are not taxable. One of the requirements to be eligible for the exemption for certain per diems is to be able to prove the date and place of travel, and reason for traveling. If the per diems are not taxable, the payer does not have to withhold tax.

In this judgment, the Supreme Court confirmed the interpretation settled in its judgments of January 29 and February 6 2020, examined in our Tax Newsletter - February 2020. Under that interpretation, the burden of proving that the per diems are taxable lies with the tax authorities. And if the tax authorities do not have the necessary proof, then they need to contact the employer, who is required to substantiate that the amounts paid in respect of per diems relate to trips made for work reasons.

This judgment also examined for the first time whether the rules on distribution of the burden of proof in this respect have to be altered where the recipient of the per diems is a director of the company paying them. The Supreme Court concluded that the fact of the taxpayer being director of the company does not determine in itself that the employer is responsible for substantiating the trips or the subsistence and accommodation expenses. One of the elements that needs to be verified is whether the requests made to the director mentioned the position in which those requests were made to him, or whether he knew the importance of the legal requirements when making the relevant decisions on the need for the trips.

2.2 VAT/Right to be heard.- Taxpayers’ rights are breached if they are not given access to the complete case file and are denied their rights to deduct VAT due to simple suspicions over the substance of the transaction

Court of Justice of the European Union. Judgment of June 4, 2020. Case C-430/19

An audit on a Romanian company was suspended because of the performance of certain criminal investigations which were ultimately set aside. In the resumed audit, however, the auditors concluded that the business transactions between the company and two of its suppliers were fictitious. The company challenged the auditors’ report and requested access to the complete administrative case file, which was denied.

The CJEU concluded that a private party should be given the opportunity to be provided, if it so requests, with the information and documents included in the administrative case file that the public authority has taken into consideration for adopting its decision, unless the restriction of access to the information is justified by public interest objectives.

In relation to the facts of the case (denial of the right to deduct VAT for the customer on the invoice where it cannot provide any other proof of the substance of the economic transactions performed), the CJEU acknowledged that, in relation to a taxpayer’s right to deduct input VAT, the authorities and the national courts may deny that deduction, if they evidence, using objective elements, that there was fraud or abuse in relying on that right. In view of the absence of European legislation on taking evidence in cases of VAT fraud, the CJEU specified that the national tax authority must evidence these factual elements, and the taxpayer cannot be required to produce additional documents that are not required in the VAT Directive.

The CJEU concluded therefore that, in cases involving simple suspicions (with no proof) over the actual performance of transactions giving entitlement to the right to a deduction, the common system of value added tax precludes the competent tax authority from denying that right where the taxpayer cannot produce more than the invoice evidencing that transaction.

2.3 VAT.- Supreme Court examines how the proceeds of a sale of shares and of transactions with derivative hedging instruments carried out by holding companies affect the deductible proportion

Supreme Court. Two judgments delivered on May 19, 2020 (appeal 4855/2018 and appeal 34/2018)

These judgments examine the cases of two holding companies primarily engaged in holding, acquiring and transferring shares. Among other activities, they are responsible for the group's strategic planning, the provision of loans and other corporate services to group companies. The tax authorities made an adjustment to lower the deductible proportions of the two companies, by including in their denominators the capital gains obtained from transferring shares and from entering into financial derivative contracts. According to the tax authorities, these were financial transactions carried out regularly, which entailed a direct and permanent extension of the company's activity, in other words, they were non-ancillary activities.

The Supreme Court concluded as follows:

a) The sale of shares in group companies does not qualify as ancillary in the specific circumstances present in the examined cases because the holding companies provide financial support, accounting, legal, technical and sales services to their subsidiaries, through permanent advisory, consulting and intermediary tasks and providing loans, from which it may be concluded that that sale of shares is indeed a direct, permanent necessary extension of the company's primary activity. The authorities' adjustment is therefore correct regarding inclusion of the proceeds of that sale of shares in the denominator for the distributable proportion.

b) Conversely, the transactions with financial derivative instruments do not entail the performance of taxable transactions and therefore do not have to be included for calculating the deductible proportion. The reason is that besides providing a service when the derivative product is obtained, (with that contract) the holding company simply guarantees that certain risks are hedged which could endanger the success of its own activities. In short, entering into derivative instruments in these cases does not amount to the performance of transactions attributable to the company as part of its business activity and therefore does not have to be included for calculating the distributable proportion.

2.4 Transfer and stamp tax.- The release of co-borrowers from a mortgage recorded in a public deed is subject to stamp tax

Supreme Court. Judgment of May 20, 2020

The court examined a case in which several co-owners of a mortgaged property dissolved the condominium, resulting in both the property and the mortgage loan being assigned to two of the co-owners, and release of the other borrowers.

The Supreme Court concluded that stamp tax is payable on the release of co-borrowers in a mortgage recorded in a public deed because (i) an amendment of the originally arranged mortgage and (ii) a redistribution of the mortgage liability have to be entered at the registry.

2.5 Transfer and stamp tax.- Any transactions that are not unavoidable for compliance with an urban development plan are subject to stamp tax separately

Supreme Court. Judgment of May 19, 2020

A taxpayer joined and redivided a number of properties and dissolved the joint property entity existing in relation to one of them. All these transactions were recorded in a single public deed. The taxpayer filed as many self-assessments as legal transactions it had performed. It later challenged them by arguing that what had taken place was a single overall transaction with a single aim (to enable the transfer of development rights under the urban development plan), and therefore stamp tax only fell due once.

The Supreme Court clarified that, although the transactions were performed for a single aim, the joining and redivision of the properties and the dissolution of the condominium, they were not indispensable transactions to comply with the urban development plan. These are therefore different legal transactions, each subject to stamp tax separately.

2.6 Transfer and stamp tax.- The formation of a company by contributing mortgaged properties is subject to capital duty and transfer tax

Supreme Court. Three judgments dated May 18, 2020 (appeals 3205/2017, 6263/2017 and 5194/2017)

Several mortgage properties were contributed in the formation of a company and the new company assumed the whole of the unpaid debt. The taxpayer self-assessed capital duty on the formation of the company. The tax authorities took the view, however, that it should also have been subject to transfer tax (as a transfer for consideration), because the assignment of properties with the assumption of debts is a taxable event.

The Supreme Court concluded in this judgment that two perfectly separate conventions are present in this case, each indicative of economic capacity: the subscription to capital by contributing mortgaged properties, which is subject to capital duty, and the assumption of the mortgage loan by the newly created company, which is subject to transfer tax.

2.7 Transfer and stamp tax.- Public deeds for mortgage novations involving amendment of the repayment system are exempt from stamp tax

Valencia High Court. Judgment of January 29, 2020

The transfer and stamp tax legislation allows an exemption from stamp tax for the public deeds for any novations amending mortgages covenanted by mutual accord between lender and borrower, if the lender is a financial institution and the amendment relates to the originally covenanted or currently valid interest rate terms, to altering the term of the mortgage, or to both.

In the examined case, the repayment system for a mortgage was amended, by lengthening the grace period and postponing repayment of the loan until the maturity date and allowing it to be paid in a lump sum. The tax authorities took the view that in this case the novation public deed was not exempt because it did not amend either the interest rate or the term, only the repayment method.

Valencia High Court concluded, against this, that it is clear that the covenanted novation impacted the term of the loan and therefore the exemption was fully applicable.

2.8 Real estate tax.- If an appraisal has been voided by a final decision, any real estate tax assessments that have used that appraisal must be rendered invalid

Supreme Court. Judgment of May 18, 2020

The Supreme Court concluded that, after the cadastral value has been fully or partially voided by a final decision, the authority responsible for managing real estate tax must render invalid all assessments issued on the basis of the voided cadastral value, even if a new cadastral value has yet to be approved.

This is so even if, after the new cadastral value has been issued, the tax authorities re-issue real estate tax assessments using the new value, as long as their right to assess the tax has not become statute-barred.

2.9 Cadastral values.- The new cadastral value notified by the cadaster as a result of a correction procedure cannot take effect retroactively

Supreme Court. Judgment of May 28, 2020

The legislation governing the cadaster states that, where the cadaster initiates a procedure for correcting discrepancies as a result of a lack of consistency between a property description in the cadaster and the property's actual characteristics, any new appraisal notified for the purposes of the cadaster will be effective from the date following that of the decision to correct it.

In the case examined in this judgment, the appellant argued that the aim behind the cadaster rules determining that the procedure for correcting discrepancies can only be effective in the future is so as not to be detrimental to the owner registered in the cadaster where the new value in the cadaster does not benefit it. In other words, this limit on the timing of its effects does not affect acts in which the correction determines a favorable or less costly effect for the owner registered in the cadaster.

The Supreme Court concluded, however, that, under an interpretation based on the letter and spirit of the law, retroactive effects cannot be allowed under any circumstances for the new cadastral values arising from a procedure for correcting discrepancies.

2.10 Cadastral values.- The tax authorities must commence by their own decision a procedure for correcting discrepancies over the cadastral value if the owner registered in the cadaster provides evidence that those discrepancies exist

Castilla y León High Court. Judgment of April 22, 2020

The cadastral legislation states that the procedure for correcting discrepancies must be initiated by the authorities, by their own decision, if an inconsistency between the description of the properties in the cadaster and their actual characteristics comes to their attention by any means.

Although this procedure is initiated by the tax authorities' own decision, this does not allow them to refuse to initiate the procedure without grounds. As the Castilla y León High Court concluded in this judgment, if the owner of a property informs the tax authorities that there are discrepancies between the description of the property in the cadaster and its actual characteristics and evidence of those discrepancies is provided also, the tax authorities are required to initiate, by their own decision, the relevant procedure to examine and conclude as to whether the correction is justified.

2.11 Collection procedure.- If deferral is requested, but the debt is paid before a decision is issued on the request, the reduction to the surcharge for late returns applies

Supreme Court. Judgment of May 18, 2020

The General Taxation Law states that where a return is filed voluntarily outside the time limit (in other words without a prior request by the tax authorities), a surcharge for late filing may be sought. This surcharge is reduced by 25% if the remaining 75% is paid within the voluntary payment period commenced on its notification, if the whole amount of the debt determined in the late self-assessment is paid when the return is filed; or, if deferred or split payment is requested secured by a guarantee or surety bond certificate, within the time period determined in the deferral decision.

In the case examined in this judgment, a taxpayer had filed his personal income tax self-assessment outside the time limit, requested deferred payment and offered a property as security. Before the tax authorities had issued a decision on the requested deferred payment, the taxpayer paid the full amount determined in his self-assessment. Because the payment had been made outside the voluntary payment period, the surcharge for late payment was sought; and since it had been made before a decision was issued in relation to the deferred payment, the taxpayer took the view that it had to be reduced by 25%.

The tax authorities considered, however, that the 25% reduction was not applicable under an interpretation based on the letter of the law, because (i) no guarantee or security bond certificate had been provided and, additionally, (ii) the deferred payment had not yet been granted when the payment was made.

Against this, the Supreme Court concluded that the authorities' view places taxpayers paying before a decision has been issued on their petitions for deferred payment in a worse position than those not paying the debt until later because they have been granted the right to deferred payment. It concluded therefore that the 25% reduction applies where, after requesting deferred payment of the amount determined in his self-assessment return filed outside the time limit (even if by providing security other than the guarantee or surety bond certificate), the taxpayer pays over the full amount of the tax debt before the tax authorities issue a decision on the requested deferred payment.

2.12 Verification of reported information procedure.- The verification of reported information procedure cannot be used to make complex legal interpretations

Supreme Court. Judgment of May 19, 2020

The Supreme Court examined whether it is allowed in a verification of reported information procedure to audit satisfaction of the requirements to claim the personal income tax exemption for reinvestment in the taxpayer's principal residence.

In its judgment, the court concluded that the verification of reported information procedure may only be initiated in relation to a taxpayer's return or self-assessment and for the purpose of (i) clarifying any information on that return or self-assessment, (ii) clarifying any contradictions with the data on other returns; (iii) correcting formal defects or errors of arithmetic, or (iv) correcting an instance of incorrect application of the law, where the error is patent.

The following conclusions may be drawn from this:

a) This procedure cannot be used to audit any facts other than those reported by the taxpayer; and the accuracy of those facts can only be confirmed from the taxpayer's other returns or self-assessments.

b) Nor can this procedure be used to question the legal characterization of the facts made by the taxpayer, where that characterization may be controversial or may not be clear and evident from the analysis and commentary and case law.

The court therefore set aside that the verification of information procedure may be used to decide (as the tax authorities had done in the case that gave rise to this judgment) whether the taxpayer's marriage and the birth of his first child shortly after the sale of his previous residence qualify for an exception to the obligation to reside in it for three years for the property to be regarded as the principal residence.

2.13 Audit and penalty procedure.- Taxpayers' pleadings have to be considered in assessment and penalty decisions

Supreme Court. Judgment of May 18, 2020

After carrying out an audit, the tax authorities issued the assessment and penalty decisions before receiving the written pleadings filed by the taxpayer against the auditors' report and the proposal to impose a penalty. After the pleadings had been received, they issued new administrative decisions ratifying their earlier decisions, while replying to those pleadings; these second decisions were issued after the maximum auditing period under the General Taxation Law had ended.

The Supreme Court likened the failure to consider the pleadings to omission of the period for submissions, and determined different consequences depending on the procedure:

a) In an audit, failure to consider the taxpayer's pleadings is not a ground for invalidity of the assessment, instead simply for its voidability if it is justified that it caused denial of the taxpayer's due process rights.

   The decision bringing the audit to an end is not the first assessment decision, but the second, in which they replied to the pleadings. Because that decision was issued after the end of the maximum auditing period, the tax authorities' right to assess in relation to several of the audited periods had become statute-barred.

b) In the penalty procedure, omission of the period for submissions (or failure to consider the pleadings) is an invalidating defect in the penalty, which cannot be deemed corrected by the reply given by the tax authorities in the decision issued later. The penalty proceeding is therefore invalid ab initio.

2.14 Enforcement procedure.- Discrepancies over an enforcement decision must be resolved by the reviewing body that issued the decision

Supreme Court. Judgment of May 19, 2020

The tax authorities issued provisional VAT assessments not allowing certain deductible amounts of input VAT. In the decision on the later economic claim the assessments were voided because the tax authorities had made annual assessments and should have issued them in relation to the (monthly or quarterly) assessment periods determined in the law. In the enforcement process for the decision, the tax authorities delivered a decision removing the earlier assessments and confirming new assessments based on the proper assessment periods.

It was examined whether the issues raised in relation to the new assessments issued to enforce the economic-administrative tribunal's decision fall within the scope of enforcement of decisions or within that of economic-administrative claims. The Supreme Court concluded as follows:

a) It recalled, firstly, that after an assessment has been voided on substantive grounds, the tax authorities may issue a lawful assessment in relation to the same issue. It also recalled, however, that this option must be rejected in cases of (i) expiry of the statute of limitations, (ii) the tax authorities repeating or staying stubbornly in their error, (iii) *reformatio in peius*, and (iv) duplicate penalties in which the same subject, facts and grounds are found (*non bis in idem* principle).

b) Following on from this conclusion it added that any discrepancies over the new assessments will have to be handled in an ancillary enforcement proceeding which will have to be resolved by the economic-administrative tribunal that delivered the decision being enforced; and that in that ancillary proceeding it is allowed to examine both procedural arguments relating to the new assessments and substantive arguments that had not been examined or decided in the decision being enforced.

3. Decisions by economic and administrative tribunals

3.1 Nonresident income tax.- If dividends are paid to a holding company resident in a member state, but the beneficial owner is not resident in the EU, they are subject to withholding tax

Central Economic-Administrative Tribunal. Decision of October 8, 2019

A Spanish company withheld nonresident income tax from dividends paid to its parent company (resident in Luxembourg), at the rate provided in the Spain-Luxembourg tax treaty (15%). Later, the parent company filed a Form 210 to request a refund of all the tax that had been withheld. The parent company argued that it was eligible for the exemption allowed for income distributed by subsidiaries resident in Spain to their parent companies resident in other EU member states (article 14.1 h) of the Nonresident Income Tax Law).

In an audit commenced after that request, the exemption was denied and it was also concluded that the withholding rate under Spanish domestic law was applicable (21% in the periods at issue) rather than the rate under the tax treaty.

In a decision delivered on October 8, 2019, published in June 2020, TEAC followed the interpretation determined by the CJEU in a judgment delivered on February 26, 2019 (C-116/16 and C-117/16, T Danmark) and concluded that in the examined case the "antiabuse clause" allowed in the law governing the exemption was applicable.

TEAC underlined the following points in this case:

a) The Luxembourg parent company is wholly owned by a Qatar company and was set up, the auditors' had concluded, to claim the exemption incorrectly.

b) The beneficial owner of the dividends is not the Luxembourg company, instead its Qatar parent.

   Among the reasons enabling it to conclude as to the beneficial owner of the dividends, it underlined the importance of a financial and cash flow analysis, separately from the characterization of the payments made to the parent company as dividends or, for example, as remuneration or a refund of a portion of the funding received.

c) The fact that the Luxembourg company is not the beneficial owner of the dividends precludes both the exemption and the reduced rate under the tax treaty with Luxembourg.

TEAC denied the exemption on the basis that, if it had not interposed a company in an EU member state, the Qatar company would have been subject to withholding tax at source under Spanish domestic law.

3.2 Collection procedure.- New wording of article 150.7 of General Taxation Law (LGT) on calculation of late-payment interest on assessments issued for enforcement is applicable where receipt of the enforcement case file occurs on or after October 12, 2015

Central Economic-Administrative Tribunal. Decision of June 1, 2020

Before the reform of article 150.7 of the General Taxation Law (LGT) made by Law 34/2015 of September 21, 2015, it had been determined in tax commentary and analysis and in the case law that in scenarios involving new assessments issued to enforce others that had been voided for procedural reasons, late-payment interest did not have to be calculated beyond the date that first voided assessment was issued. In other words, when calculating the late-payment interest due in respect of the second assessment the date when the first assessment was issued had to be taken as the end date of the period.

Following that reform, however, late-payment interest in respect of new assessments issued for enforcement has to be calculated between the date that would have been associated with the voided assessment and the point when the new assessment is issued.

In this special appeal for a ruling on a point of law, at issue was determining whether the late-payment interest that is calculated in cases where a new administrative assessment is issued as a result of a judgment or decision ordering a rollback of procedure (to an earlier moment in time) under article 150.7 of the General Taxation Law is subject to the amendment made by Law 34/2015 of September 21, 2015, regardless of the date when the resumed procedure was initiated.

TEAC concluded that the new wording of article 150.7 of the General Taxation Law is applicable, as specified in paragraph 6 of transitional provision one of Law 34/2015, of September 21, 2015, to audit work in which the receipt of the case file by the body responsible for enforcing the decision as a result of the ordered rollback of procedure occurs on or after October 12, 2015, regardless of whether the audit that resumed after the rollback had started before that date.

3.3 Collection procedure.- Late filing surcharges are not applicable to adjustments made in one period as a result of an earlier administrative review

Madrid Regional Economic-Administrative Tribunal. Decision of November 27, 2019

Article 27 of the General Taxation Law contains a surcharge regime for the late filing of self-assessment returns without a prior request from the tax authorities. That article clarifies that a prior request from the tax authorities means any administrative procedure conducted with the taxpayer's formal knowledge which results in the recognition, adjustment, confirmation, audit, or securing of the tax debt.

In the facts examined in this claim, the company filed an additional corporate income tax return for fiscal year 2104 outside the time limit as a result of an earlier audit relating to fiscal year 2011, in which the company had been instructed to make adjustments in respect of later years.

The tax authorities considered that that late filing was voluntary, without a prior request, and therefore issued a late-filing surcharge. Madrid TEAR, however, concluded, on the basis of national appellate court judgment of March 30, 2011, that that late filing arose as a result of an earlier administrative procedure and that, therefore, the spontaneity factor required to assess that surcharge was not present.

4. DGT resolutions

4.1 Corporate income tax.- The DGT reiterates acceptability of non-monetary contributions of shares that allow the "tax fee" on the distribution of dividends to be eliminated

Directorate General for Taxes. Resolutions V1007-20 of April 22, 2020 and V1122-20 of April 28, 2020

In these two resolutions the DGT examined non-monetary contributions of shares by individuals. In both cases the individuals, who shared ownership of shares in company A, contributed those shares in A to two holding companies (B and C) each wholly owned by one of them.

The DGT found that the reasons provided for the contributions were valid and that therefore it was eligible for the neutrality regime. Among the reasons mentioned were:

a) Allowing the equity of the two businesses to be planned and managed separately.

b) Facilitating the handover to the next generation.

c) Enhancing the obtaining of funding for new investments.

d) Funneling through the holding companies the dividends distributed by their investees (in other words, avoiding the "tax fee" arising from distributing those dividends to individuals so as later to make investments).

4.2 Corporate income tax.- Tax losses are not reduced by impairment losses on the investment, if the impairment losses are reverted before the merger

Directorate General for Taxes. Resolution V0853-20 of April 14, 2020

The Corporate Income Tax Law states that, in transactions for which the neutrality regime has been elected, the tax loss carryforwards generated by the transferring company have to be transferred to the transferee. However:

a) If the transferee held an ownership interest in the transferor or both belonged to a group for corporate law purposes, the tax loss carryforwards had to be reduced by an amount equal to the positive difference between the value of shareholder contributions, of any type, related to the ownership interest and their tax value.

b) Additionally, under transitional provision sixteen of the law, any tax loss carryforwards of the transferring company that gave rise to impairment of the ownership interest in the transferee company (or in another company in the group for corporate law purposes) cannot be offset before January 1, 2013.

The issue submitted for resolution concerned a merger by absorption in which a parent company of a group would absorb a wholly owned company, which had tax loss carryforwards. After underlining that the fact of the absorbed company having tax loss carryforwards does not *per se* invalidate the ability to claim the special tax regime, the DGT examined the requirements for the absorbing company to acquire the right to offset the tax losses of the absorbed company and pointed out the following:

- The aim of the limit related to the impairment losses on the investment is to prevent the same loss being used twice; which, if an impairment allowance has been recorded, would occur if the absorbing company has deducted those impairment losses and moreover is allowed to offset the tax losses generated by the absorbed company.

- However, if before the transaction the impairment losses on the ownership interest recorded and deducted by the absorbing company is reverted, the tax loss carryforwards do not have to be reduced in respect of those impairment losses.

4.3 Corporate income tax.- A nonproportional full spinoff following a merger by absorption cannot benefit from the neutrality regime

Directorate General for Taxes. Resolution V0857-20 of April 14, 2020

Two brothers holding different ownership interests in two companies (A and B) engaged in real estate operations, intended to separate gradually the capital owned by each. They planned to carry out a merger in which A would absorb B. The post-merger company would later perform a spinoff resulting in two companies C and D; the brothers would each receive ownership of one of these companies. The assets to be received by C and D did not form lines of business.

The DGT denied eligibility for the neutrality regime because the shareholders of the company performing the spinoff (the post-merger company) would receive shares in the beneficiary companies of the spin-off in different proportions to the interests they held in the post-merger company, which determines that the transaction would qualify as a nonproportional full spinoff; added to which, the transferred assets and liabilities did not amount to lines of business.

4.4 Corporate income tax.- If the merger reserve relates to the capital and additional paid-in capital contributed by the shareholder to the absorbed company, their distribution does not have to be included in the recipient's tax base

Directorate General for Taxes. Resolution V0535-20 of March 5, 2020

Company H set up company P, which in turn acquired the whole of company A. In a downstream merger for which the neutrality regime was elected, company A absorbed company P. As a result of that transaction, a merger reserve emerged at A relating to the capital and additional paid-in capital of P (contributed by H for P to acquire its interest in A). Now company A is going to distribute that merger reserve to company H.

The principle of subrogation in respect of rights and obligations prevails in the tax neutrality regime, and among them the retaining of the tax regime applicable to the capital and additional paid-in capital existing at the absorbed company, regardless of how they are included in the equity of the absorbing company. Therefore, any capital or additional paid-in capital existing at company P (absorbed company) which were later repaid to shareholder H, would retain their tax regime, regardless of whether they had been included in the accounting records of company A (absorbing company) as reserves. In other words, they would treated in the same way as a repayment of capital or additional paid-in capital.

A repayment of capital or additional paid-in capital (article 17.6 of the Corporate Income Tax Law) requires the shareholders to include in their tax bases the amount by which the market value of the received elements exceeds the tax value of their interests.

In the examined case, the tax value of H's interest in A would be determined by reference to the provisions in article 81.2 of the law on the tax (neutrality regime); in other words, the value for tax purposes of that interest would be the tax value that it had at P.

Therefore, if the merger reserve being distributed relates to the capital and additional paid-in capital contributed by H to company P, company H does not have to include any income in its tax base as a result of the distribution.

4.5 Corporate income tax.- The finance cost for distributing additional paid-in capital is deductible within the general limits for finance costs

Directorate General for Taxes. Resolution V1193-20 of April 30, 2020

A company received a loan from a related company and used it in part to repay additional paid-in capital to its sole shareholder. The issue concerned whether the finance cost in respect of that loan would be deductible.

To resolve the issue, the DGT started out from the premise that, since the acquisition or formation of the company by its sole shareholder, it has generated income higher than the additional paid-in capital being distributed, and as a result, under accounting standards, that distribution may be characterized as a distribution of income.

It concluded from that premise that finance costs are deductible if they satisfy the general requirements for the deduction of finance costs under article 16 of the law.

4.6 Personal income tax.- A director may deduct self-employed worker contributions, even if he is not paid for his services

Directorate General for Taxes. Resolution V0718-20 of April 6, 2020

The requesting party is a director of a limited liability company and is not paid for his services. The company has not had any income. The requesting party has not participated as a self-employed worker in the performance of any economic activity, but has paid social security contributions under the self-employed workers program.

The DGT specified that the contributions to the self-employed workers program that the requesting party was required to make for the performance of his functions as director has to be treated as a deductible expense for him when determining his net salary income, which may be a negative amount for this reason.

It is relevant to recall that Madrid High Court, in a judgment delivered on October 14, 2019, adopted the opposite view by arguing that if a director is not paid for his services social security contributions cannot be deducted.

4.7 Personal income tax.- Inbound expatriates can benefit from the rules allowing exempt or non-taxable salary income (flexible compensation)

Directorate General for Taxes. Resolution V0589-20 of March 16, 2020

The DGT examined the case of a company hiring employees electing the special regime for workers sent from other countries (inbound expatriates). These workers receive various types of income in kind. Under the special regime for inbound expatriates, the tax debt has to be determined under the rules provided in the revised Nonresident Income Tax Law, with certain specific provisions. This reference to the Nonresident Income Tax Law contains an embedded reference to the rules in the Personal Income Tax Law, made in article 13.3 of the Nonresident Income Tax Law. Among the mentioned specific provisions, it is determined that inbound expatriates cannot claim exemptions.

The issue submitted for resolution concerned whether inbound expatriates can benefit from the exemptions that the Personal Income Tax Law allows for certain types of income in kind.

The DGT recalled that the distinction between cases of exempt and nontaxable income that has existed since January 1, 2015 in the Personal Income Tax Law is for clarification and cannot imply that the exemptions under article 42 of the Personal Income Tax Law give rise to salary income that is taxable for inbound expatriates. In short, anyone who has elected the inbound expatriates regime may benefit from the exemptions allowed in the Personal Income Tax Law for income in kind.

4.8 Personal income tax.- The indemnity received by a false self-employed worker, as agreed in a judicial conciliation hearing, is not tax-exempt if unjustified dismissal is not suitably acknowledged

Directorate General for Taxes. Resolution V0777-20 of April 7, 2020

The requesting party was dismissed by the company where she worked as a false self-employed worker, so she decided to sue the company. A judicial conciliation agreement was reached between both parties in which, without entering into considering the legal characterization of the dismissal, the claimant was granted an amount of indemnity.

The DGT provided the following interpretation:

a) Because the proceeding conducted by the labor court starts out from the premise that the requesting party had an employer/employee relationship, the indemnity has to be characterized as salary income.

b) It is only exempt, however, if unjustified dismissal is acknowledged, either before the conciliation service, or through a court decision.

c) In this case the exemption is not applicable because unjustified dismissal was not expressly acknowledged (although the 30% reduction may be applicable if the generation period is longer than two years).

4.9 Personal income tax.- Fees in respect of proceedings that took several years are multi-year income

Directorate General for Taxes. Resolution V0609-20 of March 30, 2020

The requesting party is a lawyer and occasionally receives fees in relation to court proceedings that lasted over a year, and charges a single amount at the end of those proceedings.

The DGT recalled that the reduction for multi-year income is not applicable to income obtained from carrying on an economic activity which regularly or ordinarily generates this type of income. It mentioned, however, that the Supreme Court clarified, in a judgment delivered on March 19, 2018, that to determine whether income is obtained regularly or ordinarily the starting point is an analysis of the specific activity carried on by each taxpayer. In that judgment, the court concluded (and this was taken on board by the DGT) as follows:

a) The regularity or ordinary receipt of the income which prevents the reduction from being claimed has to do with the professional whose tax position is involved and to the revenues obtained individually on his personal income tax return, not to the practice of the legal profession or the characteristics of that profession, considered as a whole or in abstract terms.

b) The revenues obtained by a lawyer for acting as defense counsel in a proceeding that lasted longer than two years, where they are received in one or more payments in the same period, are considered generated in a period longer than two years and may benefit from the treatment allowed for multi-year income.

c) The burden of proving that the factual requirements to claim the reduction are met lies with the tax authorities, who will have to face the unfavorable consequences of failing to provide evidence of them. That burden obviously involves justifying and supporting the reasons why the reduction is not applicable.

4.10 Personal income tax.- Within the scope of economic activities, the depreciation basis for premises received as a gift is their salable value, increased by the costs and taxes associated with the acquisition

Directorate General for Taxes. Resolution V0728-20 of April 6, 2020

The requesting party carries on a professional activity. The premises where it carries on its activity were received as a gift. The request concerned the acquisition value of the premises for the purposes of their depreciation.

The acquisition value (which has to match the carrying amount that must be taken to include the asset in the record book of capital goods) is the salable value of the premises when they were acquired, increased by the expenses and taxes associated with their acquisition. The salable value is the price that it is presumed a potential buyer would be prepared to pay by reference to the specific characteristics of the asset.

The value calculated as described above, excluding the value of the land, is the basis for depreciating the premises.

4.11 Personal income tax.- The two-year period for reinvestment in a new residence stopped running between March 14, 2020 and May 30, 2020

Directorate General for Taxes. Resolution V1115-20 of April 28, 2020

The gain on the sale of a taxpayer's principal residence is exempt if the price obtained is invested in two years.

As we summarized in our alert dated June 5, 2020 (view here), the DGT took the view that the two-year period stopped running between March 14, 2020 and May 30, 2020.

4.12 Nonresident income tax.- An activity lasting under six months, which has recurred over several years, may give rise to the existence of a permanent establishment in Spain

Directorate General for Taxes. Resolution V1008-20 of April 22, 2020

The requesting party, a German national, is a lawyer tax resident in Germany. He owns premises in Lanzarote that have been fitted out for a café bar business and he intends to carry on that business personally (without employing any workers) during the vacation periods in Spain, which are not longer than two or three months in a year and are not continuous.

The OECD's commentaries state that a permanent establishment exists where the activity in the place of business is not purely temporary, which is generally interpreted to require that the activity is carried on for longer than six months.

According to the DGT, however, even where the period in which the activity is carried on is shorter than six months, a permanent establishment may also exist if the activity is of a recurring nature over more than one year, which appears to take place in the case submitted for resolution, together with the fact that the activity is always carried on at the same premises. Additionally the café bar business will be carried on by the requesting party only in Spain (he will not carry on a similar business in his country of residence).

It has to be concluded therefore that a permanent establishment in Spain does indeed exist. In particular, the rules for determining the tax base provided for seasonal business activities must be applied.

4.13 Nonresident income tax.- Legal costs received by a UK resident are characterized as a capital gain which, under the tax treaty, is only taxable in the state of residence

Directorate General for Taxes. Resolution V1010-20 of April 22, 2020

The Nonresident Income Tax Law states that income must be characterized under the personal income tax rules with a few specific provisions. For this reason, broadly speaking, legal costs obtained by a nonresident (other than through a permanent establishment) have to be characterized as a taxable capital gain.

The DGT concluded, however, that, if the Spain-UK tax treaty is applicable, this gain is exempt in Spain (and only taxable, if applicable, in the UK).

It must be remembered that TEAC concluded that the capital gain must be determined by reducing the costs by the expenses incurred in the process, subject to the limit of their amount (view our alert here).

4.14 VAT.- Output VAT on advance payments for hotel bookings must be corrected if the customer fails to show

Directorate General for Taxes. Resolution V0839-20 of April 14, 2020

In this resolution the DGT examined whether amounts received by hotel establishments are subject to VAT if the booking is canceled or the customer fails to show, in a case where the hotel offers two alternatives:

a) Alternative 1: Pay a reduced price for the room and make an advance payment, which will is not refundable if the booking is canceled or the customer fails to show.

b) Alternative 2: Pay a price without a reduction for the room, and with no advance payment; if the customer fails to show or cancels the booking outside the time limit, the price of one night’s stay is charged to their credit card.

The DGT based its resolution of this issue on the criteria determined by the Court of Justice of the European Union in Case C-277/05, Société thermale d’Eugénie-les-Bains, and concluded as follows:

a) Alternative 1:

- The nonrefundable amounts that are paid in advance are prepayments towards the final service and therefore subject to VAT.
- If a cancellation occurs or the customer fails to show, the withheld amounts (the advance payment) are not consideration for an act of consumption, instead a type of indemnification not subject to VAT. Therefore, the VAT originally charged has to be refunded to the customer due to termination of the contract, by issuing a correcting invoice.

b) Alternative 2: The amounts charged for cancellation of the booking or because the customer failed to show do not relate to an act of consumption, instead to a payment whose aim is to remedy the consequences of failure to perform the contract (an item of indemnification). Therefore no transaction subject to VAT exists.

4.15 Tax on the value of electricity output.- Not chargeable on electricity generated for own use with the receipt of remuneration for surplus electricity

Directorate General for Taxes. Resolution V1187-20 of April 30, 2020

The requesting party was finalizing an investment agreement to acquire the status of owner and associated consumer at a plant generating electricity from renewable energy sources and will elect the option of generating electricity for own use receiving remuneration for surplus electricity.

Since under article 14.4 of Royal Decree 244/2019, consumers' time-based surplus energy under the simplified remuneration system will not be treated as energy fed into the electricity system, the taxable event triggering the tax on the value of electricity output will not occur.

5. Legislation

5.1 Approval of voluntary tax-debt adjustment forms in cases involving a tax offense

Law 34/2015, of September 21, 2015, partially amending the General Taxation Law, introduced a new article 252 defining the voluntary adjustment regime preventing the tax authorities from passing on an official copy of the case record to the court with jurisdiction and sending the case to the public prosecutor's office.

You are reminded that this voluntary adjustment must involve acknowledgment and payment in full of the tax debt before notice of the commencement of audit and investigation work to determine the debt; or, if those procedures had not occurred, (i) before the public prosecutor's office, the government lawyer, or the procedural representative of the autonomous community, provincial or local government concerned, files a criminal complaint or report of a criminal offense against the party with tax obligations, or (ii) before the public prosecutor's office or the examining judge carry out procedures formally informing the party with tax obligations of the commencement of investigations.

Now, Order HAC/530/2020, of June 3, 2020, published by the Official State Gazette (BOE) of June 16, 2020 contains approval of the following forms and determines the terms and conditions and procedure for filing:

a) Form 770 for self-assessment of late-payment interest and surcharges for the voluntary adjustment under article 252 of the General Taxation Law.

b) Form 771 for self-assessment of tax liability in respect of items and periods where no form is available on AEAT's website for the voluntary adjustment under article 252 of the General Taxation Law.

The order entered into force on June 26, 2020.

More information:

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