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Global Tax Alert

Spain releases 2021 State Budget Bill

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Executive summary

On 28 October 2020, the Spanish Government released the Budget Bill for Fiscal Year (FY) 2021 (the Budget Bill). The Budget Bill, which was approved by the Spanish Council of Ministers on 27 October 2019, will now follow the parliamentary discussion and approval process.

The Budget Bill includes some of the tax measures which were originally considered in the Budget Bill for FY 2019 which failed to obtain Parliament's approval (see EY Global Tax Alerts, *Spain releases 2019 State Budget Bill*, dated 17 January 2019 and *Spanish Parliament rejects 2019 State Budget Bill; Government calls for elections*, dated 15 February 2019).

Detailed discussion

Background

On 27 October 2020, the Spanish Council of Ministers approved the Budget Bill which has been submitted to the Spanish Parliament for approval.

The current wording of the Budget Bill may change as a result of the parliamentary discussions and has to be approved by both the Congress and the Senate.

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Proposed tax measures

The Budget Bill includes a number of tax measures, mainly aimed at increasing the tax revenues for FY 2021.

The following is a description of the tax measures included in the current wording of the Budget Bill which, if finally approved, could have a significant impact on multinational groups with Spanish operations.

Amendments to the participation exemption regime for dividends and capital gains

The exemption for dividends and capital gains from domestic and foreign subsidiaries would be limited to 95% of the income. This 5% reduction is achieved by treating 5% of the income as non-deductible expenses.

Given that the standard Corporate Income Tax (CIT) rate in Spain is set at 25%, the effective tax rate on dividends and capital gains derived by Spanish companies would be 1.25% (1.50% for financial entities). The tax cost of this proposed tax measure would not be eliminated within a Spanish tax unity.

As a result of this amendment, all other provisions dealing with the avoidance of double taxation (or making reference thereto) foreseen in the CIT Law are amended accordingly. For example, among others, the tax credit to avoid double taxation for dividends and capital gains received by Spanish entities.

The Budget Bill also amends the minimum participation requirement such that the participation exemption will continue to apply only where the Spanish holding company owns more than 5% in the relevant subsidiaries but it will no longer be available for subsidiaries with an investment cost of at least €20 million as is the case until now. This specific amendment will come into force in financial years starting on or after 1 January 2026 after a five-year transitory regime, applicable if the subsidiary is already held before 1 January 2021.

Unlike in the 2019 Budget Bill, the exemption for income derived through a foreign permanent establishment is not limited to 95% in the Budget Bill.

Finally, it should be noted that the Budget Bill does not amend the Spanish holding company (ETVE) regime with respect to the taxation of the income derived by the non-Spanish tax resident shareholders.

Amendments to the Collective Investment Vehicles regime (SICAV)

In addition to the measures included in the Budget Bill, the Government has announced the intention to use the Anti-Tax Avoidance Bill (see EY Global Tax Alert, *Spain sends anti-tax evasion Bill to Parliament for approval*, dated 28 October 2020) to introduce rules impacting certain Collective Investment Vehicles (SICAV) and the Spanish Real Estate Investment Trust (SOCIMI).

In line with the 2019 Budget Bill, SOCIMIs would be taxed at 15% on undistributed profits.

As for SICAVs, the new rules would grant the Spanish tax authorities the ability to review them to ensure the relevant requirements are complied with for this special tax regime to be applicable.

Nonresident Income Tax amendments

The Spanish domestic exemptions on interest payments and capital gains which currently apply to European Union (EU) taxpayers are extended to residents in the European Economic Area.

The Spanish domestic exemption for EU shareholders obtaining dividends from Spanish companies or deriving a capital gain upon the transfer of shares in Spanish tax resident companies (which do not qualify as land-rich) is amended to limit the scope of application only to those shareholders owning at least 5% in the Spanish companies (and not those holding an investment of, at least, €20 million, in line with the amendment to the participation exemption regime as summarized above).

The amount of exempt dividend income under the Spanish domestic implementation of the EU Parent-Subsidiary Directive continues to be 100%. Similarly, the amount of exempt capital gain is not limited and continues to cover 100% of the qualifying capital gain.

Personal Income Tax

The Budget Bill introduces an increase in the applicable rates, as follows:

- The State tax rate applicable to income, other than savings, exceeding €300,000 is increased by 2%, up to 24.50%.
- The State tax rate applicable to savings income (dividends, interest and certain capital gains) exceeding €200,000 is increased to 13%.

Note that, to the State tax rates noted above, the tax rate applicable in the Autonomous Region would have to be added.

Other tax amendments

The Budget Bill also proposes amendments to other taxes such as Value Added Tax (VAT), Net Wealth Tax, Special Taxes and Local Taxes, and increases the tax rate applicable on insurance premiums.

The Government has also announced its intention to finally pass the tax on non-reusable plastic (see EY Global Tax Alert, *Spain: proposal for an indirect tax on non-reusable plastic packaging*, dated 10 June 2020) and to create a new "green tax" applicable on certain waste treatment activities.

Next steps and implications

The Budget Bill is expected to enter into force as of the day following its publication in the Spanish *Official Gazette* (once approved by the Parliament); however, for CIT, the amendments, if finally approved, will be applicable to tax years beginning on or after 1 January 2021, if not concluded before the date of entry into force.

As anticipated, the Budget Bill will now go through the legislative procedure for approval before both the Spanish Congress and the Senate. It is uncertain whether the Government has sufficient support to approve the Budget Bill or whether, in the course of negotiation of the Budget Bill, some or all of the specific tax measures discussed above may be fully or partially redrafted.

Given the potential impact that some of the proposed measures could have on structures with a Spanish holding company, multinational groups should review their structures and ongoing transactions to determine, not only the potential practical implications, but also the alternatives and timing potentially available to mitigate them.

EY will closely monitor the parliamentary procedure and issue new tax alerts if and when any developments on these tax measures are known.

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