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Global Tax Alert

Spanish Council of Ministers releases draft anti-tax evasion Bill for public consultation

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Executive summary

On 23 October 2018, the Spanish Ministry of Taxation released a draft Bill proposing measures to prevent and fight tax evasion, including implementation of European Union (EU) Council Directives 2016/1164, dated 12 July and 2017/1852, dated 10 October.

As reported in EY Global Tax Alert, *Spanish Council of Ministers approves anti-tax evasion Bill proposal which includes implementation of ATAD and creation of Digital Services Tax and Financial Transactions Tax*, dated 19 October 2018, this draft Bill includes, among a number of other measures, amendments to the Spanish Controlled Foreign Company (CFC) and exit tax rules to align them with the European Union (EU) Anti-Tax Avoidance Directive (the ATAD).

Stakeholders can provide comments during the public consultation phase until 15 November 2018; after that date the Ministry of Taxation will publish the final Bill to be submitted to the Spanish Parliament for approval.

Note that on 23 October 2018, two more draft Bills establishing the Digital Service Tax and the Financial Transaction Tax, were published. (See EY Global Tax Alerts, *Spain releases draft bill on Digital Services Tax*, dated 25 October 2018 and *Spain releases draft bill on Financial Transaction Tax*, dated 25 October 2018.)

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Detailed discussion

The following is a detailed description of the main measures included in the anti-tax evasion draft Bill that may potentially impact multinational structures and cross-border transactions with Spain.

This draft Bill may undergo changes throughout the public consultation process and its negotiation and approval by the Spanish Congress and Senate.

The draft Bill sets forth that it will enter into force the day after it is published in the *Spanish Official Gazette* and that amendments to the Corporate Income Tax (CIT) and Nonresident Income Tax will apply to fiscal years beginning on, or after, 1 January 2019.

ATAD implementation

The ATAD obliges EU Member States to implement a number of tax measures aimed at preventing tax evasion and base erosion in the EU. Although Spain has already introduced domestic rules covering most of those measures, some adjustments in terms of CFC rules and exit tax were required.

Note that the ATAD also requires that Member States introduce earning-stripping rules to limit interest tax deductibility. Although Spanish rules are not fully aligned with the ATAD, since they allow dividend income to be taken into consideration as EBITDA (earnings before interest, taxes, depreciation and amortization) for the calculation of earning-stripping limitations; Spain has been allowed to maintain this exception until 2024.

Similarly, anti-hybrid rules should be implemented by Spain by 31 December 2019, as required by the ATAD.

CFCs

Amendments to the Spanish CIT included in the draft Bill in terms of the CFC rules are as follows:

- Spanish CFC rules are extended to foreign permanent establishments (PEs); the draft wording expressly discards the application of the Spanish participation exemption regime for PEs if the CFC inclusion applies.
- The existing safe harbor clause for holding companies is abolished. Under this clause, holding companies owning more than 5% in subsidiaries during more than one year were not subject to CFC rules if they had human and material resources to manage the participation and did not qualify as "companies merely holding assets" as per the Spanish CIT rules.

  With the proposed wording, foreign holding companies complying with all the other conditions to fall under the scope of the Spanish CFC rules will be impacted by these rules. The only potential safe harbor foreseen is for EU holding companies which are deemed to perform an economic activity, as explained in more detail below.

  The abolishment of the safe harbor for holding companies, together with the amendments to the Spanish participation exemption regime being considered by the Government[1] may result in CFC rules applying to intermediate holding companies which enjoy a full participation exemption regime on dividends and capital gains.
- The safe harbor clause for EU tax resident companies is also amended such that it is extended to European Economic Area States. The proposed safe harbor applies if "the existence of an economic activity is evidenced," in lieu of the "business reasons for its incorporation and operation" required under the current wording. The change in this safe harbor has to be considered together with the restrictive approach of the Spanish tax authorities who do not generally acknowledge the existence of business activity in pure holding companies. A safe harbor for EU-regulated Collective Investment Vehicles is also proposed.
- The draft Bill includes new sources of CFC income, namely sales and services where the foreign entity does not add significant value, and insurance, leasing and financial activities, even if not performed with Spanish counterparties, where no economic activity is deemed to take place.

Exit taxation

The draft Bill includes some fine-tuning of the Spanish domestic rules on exit tax.

A maximum five-year deferral, with annual installments, is introduced in lieu of the indefinite deferral currently in force, in the case of a migration or transfer of assets/activities to another EU Member State. The draft Bill also sets forth the circumstances which terminate the deferral (namely, the transfer of the relevant assets to a third party, transfer of the tax residence or of the assets to a non-EU Member State, liquidation or bankruptcy proceeding of the entity, or failure to meet payment of the deferral installments).

The draft Bill includes a new exit tax scenario consisting in the transfer of the activity of a PE in the Spanish territory to another State.

Updates to the tax haven concept

The draft Bill introduces amendments to the concept of tax haven territory following the international works by both the OECD[2] and the EU.

The draft Bill expands the concept of tax haven, such that it includes States and territories, as is currently the case, and preferential tax regimes, in line with Action 5 on harmful tax practices of the BEPS[3] Action Plan released by the OECD.

Another proposed measure is the inclusion of the following States, territories and preferential tax regimes as tax havens: (i) where there is tax vagueness and lack of transparency, taking into account the absence of mutual assistance regulations and/or their application in practice; (ii) where the incorporation or utilization of companies or instruments aimed at shifting profits to territories with no actual economic activity is allowed; and (iii) where a nil or low level of taxation applies.

Mutual agreement procedures

The draft Bill foresees amendments to the Spanish rules on Mutual Agreement Procedures (MAP) to align them with the dispute resolution mechanisms within the EU, in particular, the EU Council Directive 2017/1852, dated 10 October 2017.

Under the draft Bill, ongoing Spanish domestic tax and court proceedings will have to be suspended until the relevant MAP procedure is completed, but the suspension would only apply with respect to the technical issues covered by the MAP procedure. The sole exception to this rule would be when the penalties that prevent access to the MAP (see below) are imposed and challenged by the taxpayer, in which case, the MAP will be interrupted until the penalty procedure is concluded.

The draft Bill sets forth that the penalties which prevent the utilization of the MAP include criminal charges against the Spanish Public Treasury, tax infringements consisting in lack of payment, failure to provide information needed for a tax assessment and obtaining undue tax refunds, as well as penalties related to lack of compliance with transfer pricing rules (both in terms of valuation and of documentation).

Finally, delay interest will accrue while MAPs are underway; this rule will apply to MAPs which are initiated once these rules come into force.

Other measures

The draft Bill amends the General Tax Law to require Spanish taxpayers to include the amount of cryptocurrency they own outside the Spanish territory in the tax form where assets held abroad are reported (tax form 720).

The draft Bill includes other amendments to the General Tax Law, among others the prohibition of tax amnesties, certain technical adjustments to the calculation of surcharges and certain delay interest, amendments to the penalty regime, including a new infringement for the manufacturing and commercialization of "dual use software, to Personal Income Tax, to Value Added Tax and Excise Duties, to the Net Wealth Tax rules, to the cadastral regulations, and to the rules governing gambling activities."

Implications

The above tax measures may have a significant impact on multinational groups with a presence in Spain.

All multinational structures that include Spanish holding companies should be carefully reviewed, taking into account the amendments to the CFC and tax haven rules together with the amendments to the participation exemption regime which are being proposed as part of the Budget Law, so as to address any potential adverse tax consequences.

Endnotes

1. See EY Global Tax Alert, *Spanish Council of Ministers approves anti-tax evasion Bill proposal which includes implementation of ATAD and creation of Digital Services Tax and Financial Transactions Tax*, dated 19 October 2018.
2. Organisation for Economic Co-operation and Development.
3. Base Erosion and Profit Shifting.

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