Main tax issues

Setting up a business in Spain

| Subsidiary, Branch Office and Permanent Establishment | Indirect taxes that apply to setting up a business | Tax formalities |

Business development

Disinvestment
The start-up of business activity in Spain by a foreign company can adopt various forms:

- **Subsidiary**: These companies carry out their activities personally and directly, since they are institutions with their own legal personality (public limited company or private limited liability company, among other forms).

- **Branch Office**: These are secondary establishments with permanent powers of representation and a certain level of autonomy in management with regard to their parent companies. The Branch Office is used to carry out all the parent company's activities fully or partially.

- **Representative office**: This type of office does not have its own legal personality and carries out accessory, auxiliary or instrumental activities.

Corporate income is taxed in Spain when they can be attributed to the subsidiaries and branch offices, but not in the case of representative offices. Said tax differs depending on whether the institution is a subsidiary or a branch office.

There are also differences between these legal forms from the point of view of indirect taxation (VAT). Whereas subsidiaries that carry out transactions are subject to VAT in all cases, branch offices and representative offices will only be liable if they carry out business activities in Spain.
INDIRECT TAXES APPLIED TO THE SETTING UP OF A BUSINESS

The most representative tax costs associated to business set-up in Spain correspond to the concept of Corporate Transactions and vary in accordance to the way in which the business carries out its activities:

- **Subsidiary**: the incorporation of a subsidiary is tax exempt since December 3, 2010. Tax exemption is also granted for successive capital increases.

- **Branch Office**: The incorporation of a branch office of a non-resident institution is subject to tax in accordance with the following conditions:
  - Non-resident institution whose corporate domicile and actual management centre are located in non-EU countries: 1% of the part of the capital used for the activities in Spain.
  - Non-resident institution whose corporate domicile and actual management centre are located in EU countries: **Not subject to tax.**
TAX FORMALITIES

Entities setting up a business in Spain must fulfil the following formal tax obligations:

- Applying for a tax ID number (in Spanish, NIF) during the month after the incorporation of the company and before starting its activities by filing an application for registration on the census (Form 036).

- Before the commencement of the activities, they must file in an application for registration on the Tax Authorities Business Census (Form 036).

- File an application for registration on the Tax on Business Activities (in Spanish, IAE) (Form 840).
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Disinvestment

Taxation of the entry of goods into Spain. Customs duty and VAT on imports

Indirect taxes Applied to the delivery of goods and the provision of services. VAT

Tax on corporate income applicable to subsidiaries and branch offices

Taxation associated with the human capital assigned to the business in Spain

Main issues related to local taxation
TAXATION ON THE ENTRY OF GOODS INTO SPAIN. CUSTOMS DUTY AND VAT ON IMPORTS

Tax costs associated to the entry of goods into Spanish territory consist basically of the following:

- **Customs duties on imports**
  The amount of the customs duty on imports is determined in accordance with the harmonised system for the classification of goods (TARIC code), their origin and customs value.

- **VAT on imports**
  The import of goods is taxed by VAT at the applicable rates (see next page), as well as the general rules for the deductibility of the tax paid.
INDIRECT TAXES ON THE DELIVERY OF GOODS AND THE PROVISION OF SERVICES. VAT

VAT is a harmonised tax within the European Community (Directive 2006/112/CEE) and applicable in the Spanish territory on the Iberian peninsula and on the Balearic Islands. This area excludes the territories of Ceuta and Melilla (where the tax on production, services and imports is applied, the IPSI) and the Canary Islands (where the General Indirect Tax of the Canary Islands, the IGIC, is applied).

VAT tax rates applicable

<table>
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<tr>
<th>General rate</th>
<th>Reduced rate</th>
<th>Extra-low rate</th>
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<tr>
<td>21%</td>
<td>10%</td>
<td>4%</td>
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INDIRECT TAXES ON THE DELIVERY OF GOODS AND THE PROVISION OF SERVICES. VAT

Does VAT represent higher cost?
VAT is a tax applied to final consumption and, in general, unless activities that are exempt from VAT are carried out, it does not represent a higher cost for businesses or professionals. However, the collaboration on collecting the tax may represent administrative costs arising from the fulfilment of formal duties.

How is the VAT paid recovered?
The VAT paid is recovered by deducting the amount from the VAT collected from applying the tax to the recipients of the goods delivered and the services provided.

There is a special procedure for the recovery of VAT by branch offices that do not carry out activities subject to the tax.
TAXATION ON CORPORATE INCOME ATtributable to SUBSIDIARIES AND BRANCH OFFICES

Income obtained in Spain by non-resident entities through subsidiaries or branch offices is subject to taxation in accordance with domestic legislation. It must be taken into account the existence of specialities in the Basque Country and Navarra and the priority of the conventions signed to avoid double taxation.

The taxable amount will generally be the result of correcting the accounting result in accordance with the tax adjustments provided by law.

It shall not be deductible. among others, expenses which represent a return of own funds, donations, fines and administrative penalties, and certain expenses from services to tax havens entities, unless the taxpayer proofs that the operation or service has been effectively carried out.

Operations carried out with related persons or entities must be valued at market price, and must also comply with a series of obligations of information in connection with them.

Revenues from the transfer of rights over intangible assets will be reduced by 50% when the stated requirements are met, among which highlights that transferred assets have been created by the transferring entity, some accounting records to determine the income and expenses on the subject, and that the transferee uses those rights to develop a business activity and not resides in a territory considered as a tax haven.

The general tax rate is 30%. However, several special rates could be applicable.
**TAXATION ON CORPORATE INCOME ATTRIBUTABLE TO SUBSIDIARIES AND BRANCH OFFICES**

The applicable legislation provides for both Spanish and foreign source income double taxation relief.

Double taxation relief mechanisms are established in the taxable amount (exemptions) and in the quota (deductions) and, in the scope of the income obtained abroad, they constitute tax incentives for making investments and carrying out activities outside Spain.

Tax incentives are provided for certain activities, with relevance placed on the deduction for the reinvestment of extraordinary profits, which gains access to a fixed rate of 18% for certain types of income. There is also the possibility of applying certain special tax systems, in accordance with the activities carried out or the subjective characteristics of the businesses: Economic Interest Groupings and Temporary Consortia, Foreign Securities Holding Companies, Tax consolidation, reduced-size companies, etc.

Taxation of Branch offices involves certain differences, focused on the deductibility of certain head-office expenses and the existence of a supplementary tax (branch tax).
TAXATION ASSOCIATED WITH THE HUMAN CAPITAL ASSIGNED TO THE BUSINESS IN SPAIN

Individuals with tax residency in Spain are subject to Personal Income Tax (in Spanish, IRPF) on their **worldwide income**.

For earned income, taxes are levied in accordance with the general tax scale (24,75% - 52%). **It can be applied a tax exemption of up to €60,000 on employment income actually carried out abroad by of Personal Income Tax taxpayers.**

Individuals not having their tax residence in Spain are subject to non-resident income tax (in Spanish, IRNR) for their **Spain-source income**.

For the income that comes directly or indirectly from work performed in Spain, a fixed rate of 24% is applied.

Special tax regime for “impatriates”: non resident individuals that are transferred into Spain due to a job rendered in Spain and acquire Spanish tax residence can opt to be tax treated as non residents in Spain, and thus be subject to taxation at a fixed tax rate of 24,75% the tax year during which they acquire tax residence in Spain and the following five years. This special tax regime for “impatriates” is subject to the fulfilment of several requirements, such us a maximum predictable employment income arising from the employment contract of € 600,000.
MAIN ISSUES IN LOCAL TAXATION

The Spanish local tax authorities (Municipalities) will require the following taxes in all cases:

1. Property Tax (in Spanish, IBI): this tax applies to the ownership of rustic or urban property and property of special characteristics owned by individuals or bodies corporate. The amount depends on the cadastral value (normally lower than the purchase price) of the property.

2. IAE (Tax on Business Activities): This tax is applied to the mere exercise of economic activities within the Spanish territory. The tax rates are determined in accordance with the type of activity that is carried out.

3. IVTM (Motor Vehicle Tax): This is applied to the ownership of this type of vehicle in accordance with their power and class.
MAIN ISSUES IN LOCAL TAXATION

Spanish Municipalities may establish and require:

4. ICIO (Tax on Constructions, Installations and Works): This tax is applied to constructions, installations and works in the municipal district for which it is necessary to obtain a municipal licence.

5. IIVTN (Urban-Nature Land Appreciation Tax): It is imposed on the increase of urban-nature land, whether vacant or built upon, at any time it is transferred or when a right in rem over such real property is created or transferred. The tax rate can not exceed 30%.
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Indirect taxation

Direct taxation. Double taxation conventions

Disinvestment
INDIRECT TAXATION

In the cases where there is a reduction of capital and the dissolution of subsidiaries, the real value of the assets and rights awarded to the shareholders will be subject to tax.

In the cases where there is a reduction of the allocation and dissolution of branch offices, the real value of the assets and rights awarded to the non-resident entity will be subject to tax as long as neither its corporate domicile nor actual management centre are located in the European Community or, if they are, they are not subject to any similar tax.

The tax rate will be 1% (or the current rate in the competent Autonomous Region).

The aforementioned transactions will not be subject to taxation if they take place in the framework of business restructuring transactions as defined in the Corporate Income Tax Act.
DIRECT TAXATION. DOUBLE TAXATION CONVENTIONS

Income obtained by a subsidiary or a branch office from its dissolution and liquidation proceedings will be subject to taxation in accordance with the general rules of the profit tax applied to the subsidiary or branch office itself.

The taxation of the income obtained by a resident of the state with which Spain has signed a convention to avoid double taxation (in Spanish, CDI) as a result of the dissolution of companies or branch offices, as well as the transfer of shares in a subsidiary, is governed by the provisions of the said convention.

Most Double Taxation Conventions signed by Spain, attribute the power for taxing the capital gains arising from the liquidation of a subsidiary or branch office and the transfer of shares to the state of residency of the party receiving the gains, except for those arising from property located in Spain.