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Tax Controversy

Spain: Law & Practice
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and

Spain: Trends & Developments
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Law and Practice

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1. Tax Controversies

1.1 Tax Controversies in this Jurisdiction

As a general rule, tax controversies arise as a result of tax assessments derived from an administrative procedure initiated by the Spanish Tax Authorities (STA), like those addressed to tax data verification, tax restricted checking or tax inspection (with either a general or partial scope).

However, they can also be initiated by the taxpayer in the event that he or she challenges his or her own self-tax return (request for the rectification of a self-tax return and refund of undue tax paid). Besides, taxpayers are also allowed to challenge the withholdings and/or the output VAT by lodging a claim against them before the STA.

1.2 Causes of Tax Controversies

The taxes that give rise to the most tax controversies are corporate income tax (CIT), personal income tax (PIT) and value added tax (VAT).

With regard to CIT, the most common controversial matters/issues are:

- the application of tax losses and deductions carried forward, which are open to amendment for a special ten-year period;
- the use of what are known as "brass plate companies" and/or "offshore companies";
- the assessment of existence of sound business reasons to carry out restructuring operations upon which the tax neutrality regime depends;
- transfer pricing issues in related-party transactions;
- deducibility for tax purposes of expenses linked to partners and board members' remuneration;
- the "real residence" of foreign companies; and
- the application of tax transparency rules.

With respect to PIT, the STA are focusing their attention on individuals that render professional services through their own companies when benefits from the professional activity are left and used at the company level; and not distributed to the individual. This is because this may lead to a lack of payment in terms of total tax due. Not only due to the difference CIT/PIT tax rates, but because these entities are commonly used to acquire the personal assets of their partners.

In addition, the STA is increasingly focusing its attention on tax residence issues. In our experience in tax litigation, over the last few years many high net worth individuals have moved to Spain, or simply visited or acquired properties in the country, without being aware of the conditions under which an individual may become a Spanish tax resident and without having previously analysed the tax implications that arise from the condition.

Among other consequences derived from being considered a Spanish tax resident, the STA are applying the tax penalties related to Form 720 (those derived from the lack of declaring this arrangement) to those individuals who, being Spanish tax residents (for whatever reason), have not declared all their assets deposited abroad. This is despite the arrangement and its consequences/penalties being challenged by the European Commission. One of the more burdensome consequences is the consideration of an unjustified increase in equity as entirely allocated to the oldest tax period for which the statute of limitations has not expired. In addition, a tax penalty of 150% shall be imposed. It must be highlighted that the European Commission started an infraction procedure against Spain in 2015 due to this penalty regime, considering it discriminatory and in conflict with the fundamental freedoms of the EU.

Regarding VAT, the STA places special emphasis on:

- the tax regime on real estate transactions;
- VAT status of holding companies and deductibility of input VAT borne; and
- pro-rata deduction of companies performing limited exempt transactions (ie, financial and insurance companies or companies belonging to the healthcare and education sectors).

1.3 Avoidance of Tax Controversies

Some recommended guidelines in order to mitigate potential tax controversies may be:

- The management of tax compliance risks through the implementation of structured processes aimed at the systematic identification, assessment, ranking, and treatment of those risks (eg, failure to register or to properly report tax liabilities).
- Asking for tax and legal advice on the envisaged transactions in advance, in order to be aware of their tax and legal status before the STA and to avoid the execution of projected operations/transactions in any way that may give rise to a tax controversy.
- Preparing and obtaining any documentary evidence through which the taxpayers could prove, within the tax audit procedure, the existence of, or the business reasons for, said business or a specific legal operation/transaction.
- Formulating, if deemed necessary by counsel, binding consultations to the General Directorate of Taxes (GDT) when no clear interpretative criterion exists about the transactions/operations that are intended to be carried out; this binding consultation is recommended to be prepared if a taxpayer does not want to assume any risk.

- Being aware of the STA's position on a tax issue and of the previous jurisprudence and pending litigation with respect to relevant transactions/operations or any other issues that may give rise to tax controversies.

1.4 Efforts to Combat Tax Avoidance

The STA have consistently shown a high level of commitment in the implementation of the measures proposed in the Base Erosion and Profit Shifting (BEPS) Project. Many of these measures have already been implemented.

Additionally, further developments are currently being discussed in the Spanish parliament to implement measures contained in Directive 2016/1164 as amended by Directive 2017/952 (ATAD I and ATAD II).

Spain was one of the signatories of the OECD multilateral convention to implement tax treaty related measures to prevent BEPS (MLI), signed on 7 June 2017. The definitive MLI position of Spain is still to be approved by the Spanish Parliament.

The National Bureau of International Tax Affairs was created in 2013 to manage, plan and co-ordinate international tax affairs; in particular, certain risk areas directly connected with BEPS. This has led to increased attention from the STA that will certainly result in increased tax controversies in the following areas:

- transactions carried out by Spanish tax residents using hybrid mismatch or other aggressive tax planning arrangements;
- leveraged acquisition of participation in a company with the main aim of generating tax-deductible expenses;
- transactions carried out with low-tax countries (especially with those qualified as tax havens) and by persons or entities that change their residence with the aim of avoiding the payment of taxes;
- payments and complex transactions to which model provisions to prevent treaty abuse, including through treaty shopping, may be applicable – special attention will be paid to dividends and royalties paid through "conduit companies" set up in countries with favourable tax treaties to channel investments and obtain reduced rates of taxation;
- permanent establishments of non-resident entities that are currently being taxed as if they were not established in Spain for tax purposes, especially in the cases of multinational enterprises; and
- effectiveness of information exchange and co-operation between tax administrations.

1.5 Additional Tax Assessments

Firstly, according to tax regulations the taxpayer will be entitled to file either an internal administrative appeal (*recurso de reposición*) or an economic-administrative claim against the above-mentioned additional tax assessments or against the resolution of the appeal. If such appeals were totally or partially rejected by the administrative authorities, taxpayers may challenge/appeal those resolutions before the judicial courts.

The appeal of the tax assessment before an administrative court does not prevent its execution (payment of tax appealed), as an assessment is enforceable since it is issued by the STA. However, the taxpayer may choose to pay the appealed tax due or suspend its execution; bearing in mind that the payment choice does not determine the waiver of any right in the appeal or claim filed against them.

If the taxpayer decides to suspend the mentioned tax debt, it must be distinguished whether the additional tax assessment comes from a tax settlement or a tax penalty. When deriving from a tax penalty, the file of an appeal determines the automatic suspension of its execution in administrative proceedings, without a need to provide any further guarantee. However, the suspension is not automatic when the appeal is filed before a judicial court once the economic procedure is finished.

When deriving from a tax assessment, however, the submission of an appeal does not determine the automatic suspension of the tax debt execution in administrative proceedings. Because the cases in which the suspension without granting a guarantee are less common, taxpayers should grant it if they want to suspend its execution. Thus, if they decide not to pay the tax due or not to apply for its suspension, the STA may initiate an enforcement procedure for the collection of the corresponding amount; which is absolutely independent of the appeal or claim filed.

1.6 Possible Impact of COVID-19 on Tax Controversies

Spain, through Royal Decree 463/2020, March 14th (RD 463/2020) declared a "state of alarm" for the management of the health crisis arising from COVID-19, which involved, for tax purposes, certain specific measures regarding the suspension of actions as well as procedural and administrative deadlines, and prescription and expiration periods too.

Since the declaration of the state of alarm, some other regulatory acts have been approved in order to specify and/or clarify the scope of the above-mentioned measures just adopted (particularly in the tax and procedural field) and to adopt other new ones with the main purpose of protecting the taxpayer/actor from being legally impaired as a consequence of COVID-19 and the limits to the acts arising from it. Regulatory acts that have been adopted are as follows: Royal Decree-Law 8/2020, March 17th; Royal Decree 465/2020, March 17th; Royal Decree-Law 11/2020, March 31st; Royal Decree-Law 15/2020, April 21st;

and Royal Decree-Law 16/2020, April 28th. The most relevant new measures, which directly impact on the procedural tax field/tax litigation, are discussed below.

Measures Adopted in the Administrative and Economic-Administrative Field

RD 463/2020, by which the state of alarm was declared, provided, in essence, the interim suspension of the terms and deadlines for the processing of judicial and administrative processes during the state of alarm period.

Just a few days later, the first Royal Decree Law (8/2020) was passed with the aim of regulating certain specific measures in tax matters. This Royal Decree Law established specific regulations regarding tax deadlines for administrative procedures which were initiated before the state of alarm was declared. Among other measures, the legislature provided the extension of unfinished tax deadlines, the new deadlines being April 30th and May 20th, depending on the content of the procedural step which had to be carried out by the taxpayer before the STA.

The regulation resulting from this act was complex and generated some doubts and uncertainty, as taxpayers were obliged to "guess" the applicable rule in each case and the new maximum available term within which they would have to comply with their procedural step.

Because of this, and without entering into a detailed explanation about the regulatory evolution since the RDL in question, May 30th is the new date that has to be taken into consideration in the following fields.

- Unfinished deadlines for certain procedural actions have been postponed until May 30th; in this regard, it is important to mention, among others, (i) the fulfilment of STA requirements, (ii) the formulation of allegations, and (iii) hearing procedures.
- The initial month-long period for lodging an appeal or economic-administrative claim against administrative acts notified before or/and during the state of alarm start to run on May 30th.
- Limitation periods, and the expiration of those actions and rights provided for in the tax regulations, are suspended for the period between March 14th and May 30th 2020.

Depending on the development of the COVID-19 pandemic and any other extension of the state of alarm that may me approved, it is possible that the above-mentioned periods may be extended again and new measures may be taken in this regard.

Whether or not taxpayer's deadlines are further extended in such terms, those procedures which are being handled need not be totally paralysed. Therefore, the STA may start new procedures and issue any new administrative acts in relation to existing procedures and the taxpayer may choose to comply with the deadline without waiting for the end of it (May 30th, provisionally).

Additionally, despite of what has been provided for in the regulations of certain autonomous regions, there have been no relevant deferrals in the payment or self-assessment of tax debts.

However, with regards to Value Added Tax (VAT), it is important to mention that if the landlord and the tenant of a business property agree on the suspension of the rental contract or a moratorium, suspension or lack of payment of the rent – as may be the case due to the temporary closure of a business because of the state of alarm legal measures – VAT will not be accrued during that suspension, moratorium or lack of payment.

Measures Adopted in the Contentious-Administrative Jurisdiction Field

The days from August 11th to 31st have been declared to be open for legal proceedings purposes. It is important to bear in mind that Spanish legislation establishes that August is not normally available for legal proceedings. As a consequence, this implies a change in the general rule for this year.

Procedural periods that had been suspended under RD 463/2020 will be resumed from the day following which the state of alarm ceases to be in force. However, a special rule has been provided for those deadlines for the announcement, preparation, formalisation and filing of appeals against court decisions as well any other final resolutions that were notified prior to the declaration of the state of alarm. In the new legal scenario, the remaining period initially suspended will not be resumed, but a new one will be granted, whose counting will start after the date on which the state of alarm ends.

Deadlines for the announcement, preparation, formalisation and filing of appeals against court decisions and any other final resolutions are extended for a new and additional period equal to the one provided for such actions in its specific regulatory law. For this extension to apply, the above-mentioned court decisions and other final resolutions must have been notified (i) during the suspension period initially established by RD 463/2020 or, (ii) within twenty working days following the date on which the state of alarm ends.

As a result of the COVID-19 crisis public spending been substantially increased; this is in order to deal with the various and urgent economic needs that have arisen. However, the public authorities' independence principle and duty implies that, a priori, such a situation, and the urgent need of tax revenues,

should not produce undue pressure on judges and/or magistrates presiding over tax disputes to decide pro-fiscum. Constitutional and legal constraints should apply otherwise and the Spanish Constitution and laws should provide a proper remedy on appeal.

This being said, it is true that, traditionally, in times of economic crisis, the number of tax audit actions in Spain have increased. In fact, this is precisely what happened after the real estate and financial crisis of 2008.

Moreover, the approval of some specific taxes is already under discussion in the Spanish Parliament and these are expected to come into force shortly (Tobin tax, Google tax, etc).

The Spanish government is already working on increasing tax revenues by raising tax rates, amending tax exemptions, harmonising taxes, etc.

2. Tax Audits

2.1 Main Rules Determining Tax Audits

The STA's main purpose is to monitor the proper compliance with tax obligations by taxpayers and fight against conduct that may give rise to tax fraud and/or tax evasion. As a consequence, because of their possibly "fraudulent" nature (under the scope of the STA), these are some actions or circumstances that may make a tax inspection or verification more likely:

- the existence of tax losses to be offset and deductions from the tax quota pending application;
- the use of companies to allocate the personal costs of their partners;
- the use of companies known as "brass plate companies" or "offshore companies" which, in fact, do not carry out any economic activity from a Spanish law perspective;
- the presence of high financial expenses in relation to operating profits;
- the performance of business restructuring operations benefiting from tax deferral conditioned on sound economic reasons;
- the elimination of double taxation (either by the way of exemption or deduction); and
- tax residence issues, both for individuals and companies.

Regarding high net worth individuals, their tax residence and the applicable special tax regimes (such as those that apply to impatriates) are relevant topics on which the STA are focusing their attention.

Likewise, the STA will check the amounts declared by taxpayers on their tax returns in order to determine whether they differ significantly from those declared in the business sector to which they belong.

Finally, it is important to note that very large companies, as well as those which operate in regulated sectors, and those ultra-high net worth individuals who are considered "major taxpayers" (*grandes contribuyentes*), are regularly subject to tax audit procedures.

2.2 Initiation and Duration of a Tax Audit

The regulation of tax verification and inspection proceedings is set out in the General Tax Law (GTL) and in its implementing regulations.

The tax inspection procedure could be initiated within the four years provided by the statute of limitations, to verify the correct compliance with the tax obligation, as stated in Article 66 a) of GTL. However, Article 68 of GTL provides for some actions or circumstances that may interrupt the mentioned statute of limitations.

Generally, the tax inspection procedure cannot last for more than 18 months. Nevertheless, under certain specific circumstances it may last up to 27 months. If the STA fail to comply with the above-mentioned maximum periods for tax inspection proceedings, the statute of limitations shall not be deemed to be interrupted. Nevertheless, the tax inspection procedure must continue and end, even after the deadlines have elapsed. However, if this happens, any action performed by the STA during the inspection proceedings will be understood as not having interrupted the statute of limitations.

In 2015, the GTL was reformed and Article 66 bis was added to it In accordance with this Article, the STA are empowered to audit and consider legal operations/transactions concluded in tax periods whose statutes of limitations have expired and have or may have an impact on the tax period which is under tax inspection. However, this does not mean that the STA are empowered to request tax debts or penalties related to the time-barred periods, but rather to assess any additional tax adjustments arising in the tax period under tax verification as a consequence of those statutorily barred periods.

In addition, the Spanish state of emergency, declared as a consequence of the COVID-19 crisis, has temporarily suspended the statute of limitations in tax administrative proceedings, such as tax inspections.

2.3 Location and Procedure of Tax Audits

Article 151 of the GTL provides that tax inspections may be carried out, at the STA's discretion, in any of the following places:

- at the tax domicile of the taxpayer, or where a representative of the tax payer is domiciled or has an office;
- the place where the taxable activities are carried out;
- the place where there is at least partial proof of the taxable event or of the de facto assessment of the tax liability; or
- at the STA office's, when those matters to be inspected could be examined there.

Notwithstanding the above, the examination of the legal documents of the taxpayer by the STA must be carried out at the domicile, premises, or office of the taxpayer, before him or her, or a person designated to such effect. However, as a matter of fact, the tax procedure is mainly processed in the STA's offices.

During the tax proceedings, companies must communicate with the STA through electronic means and the STA online platforms. Individuals are not obliged to use such electronic means and platforms.

2.4 Areas of Special Attention in Tax Audits

In our experience, key areas in a tax audit would be:

- partners/board members tax status and remuneration;
- real ownership for tax purposes of company assets;
- tax residence of taxpayers;
- tax deferral special tax regime (restructuring companies);
- tax-deductible expenses;
- temporary allocation of financial expenses;
- tax-loss carry forwards;
- related-party operations/transactions;
- deductions/exemptions on operations/transactions which have been subject to double taxation;
- real estate operations/transactions;
- holding, foreign and offshore companies; and/or
- the nature of operations/transactions carried out according to GAAR.

2.5 Impact of Rules Concerning Cross-Border Exchanges of Information and Mutual Assistance Between Tax Authorities on Tax Audits

Information exchanges and tax verification procedures have increased. This is due to the fact that the STA have more resources at their disposal in order to obtain information/documentation from taxpayers.

Despite the fact that our law firm has carried out more than 25 tax audit procedures in the last four years, we are not aware of tax authorities from different jurisdictions having jointly initiated tax procedures against the same tax payer in their own jurisdictions. However, our law firm is aware that tax authorities from different countries are closely co-operating and sharing relevant information/documentation. The tax authorities from the USA (IRS), the UK (HMRC), Italy (AE) and Switzerland (ESTV) should be expressly mentioned in this respect.

Both Spain and Italy are working together to obtain information regarding cross border taxpayers. However, despite the fact that the existence of tax audit procedures initiated jointly by different states is not the general rule, in the collection procedures inside the EU the rule is the other way round. Thus, both tax dues and tax penalties imposed and not paid in Spain would be prosecuted and executed by the tax authorities where the taxpayer is located or residing.

2.6 Strategic Points for Consideration During Tax Audits

The key strategic steps to take during a tax audit are, among others:

- to make a preliminary analysis of the controversial tax issues followed by a rigorous analysis of the request made by the STA;
- to provide the documentary support at the appropriate procedural moment; and
- to have a deep knowledge of the applicable tax legislation and accountancy, together with a wide experience in tax litigation.

3. Administrative Litigation

3.1 Administrative Claim Phase

In general, the administrative procedure for appeals/claims in Spain, once a tax assessment or penalty has been notified by the STA, consists of two stages: an administrative phase and an economic-administrative phase.

The administrative phase is optional and is initiated through the appeal lodged before the same administrative body which issued the tax settlement or penalty (appeal for reversal). As it is optional, the taxpayer may instead submit an economic-administrative claim directly before the Tax Administrative Court without the need to first file an appeal for reversal.

The economic-administrative phase is mandatory. This phase begins with the lodging of the claim/appeal before a Tax Administrative Court – at first or single instance – (economic-administrative appeal). The economic-administrative appeal is thus the mandatory way to first challenge a tax assessment.

It is submitted before the same tax administrative body that issued the tax settlement; and, depending on the amount of tax debt or tax penalty and/or its subject matter, it will be processed, whether within an ordinary proceeding or through a summary/ fast track procedure, before the Tax Administrative Court.

In terms of deadlines, the economic-administrative appeal must be filed within one month as of the date of notice of tax assessment or tax penalty, or, otherwise, when a tacit negative decision takes place (this arises from the failure by the STA to raise the final resolution).

In the case of periodically accruing debts and collective notification, the period to file an appeal begins from the date following the end of the voluntary payment period.

Once all the administrative stages of appeal have been exhausted, taxpayers may file an appeal before the judicial courts.

In addition to the ordinary administrative review procedures mentioned above, there are several special review proceedings that could be used in exceptional cases.

It is important to note that none of the administrative appeal proceedings before Tax Administrative Courts require the taxpayer's representation by an attorney (legal representative) or lawyer.

3.2 Deadline for Administrative Claims

The deadline for the appeal for reversal is one month from the day following the filing of this kind of appeal. The STA has a duty/obligation to solve all claims/appeals. Nevertheless, if the STA has not issued its decision within a six months period, the appellants may consider the claim/appeal dismissed (tacit negative administrative decision) and file an economic-administrative appeal before the Tax Administrative Court.

The deadline for an economic-administrative appeal/claim is one year, or six months in certain cases, such as appeals whose amount would be inferior to EUR600, from the day following the filing of this kind of appeal. Nevertheless, if the Tax Administrative Court has not issued a resolution in the course of one year, the appellants would be able to consider the claim/ appeal dismissed (tacit negative administrative decision) and file a further appeal before the judicial court. Likewise, the Tax Administrative Court also has the duty to solve the appeals.

The deadlines to issue a decision/resolution can be interrupted under certain circumstances, for example if the Tax Administrative Court makes a request to the appellant.

4. Judicial Litigation: First Instance

4.1 Initiation of Judicial Tax Litigation

Once all tax administrative proceedings are finished, taxpayers-claimants should lodge an appeal before the competent judicial court in order to initiate the contentious-administrative procedure. Normally, in such judicial procedures, appellants must first file the appeal showing their disagreement with the resolution raised by the Tax Authority/ Tax Administrative Court and, subsequently, once it has been admitted, they should file the proper lawsuit containing the merits.

The Jurisdiction Act governing the procedure contains the rules assigning competence for review to the different judicial courts, these are:

- the Contentious-Administrative Courts;
- the High Courts of Justice;
- the National Court; and
- the Supreme Court.

4.2 Procedure of Judicial Tax Litigation

Ordinary Procedure

The appeal must be filed within a non-extendable period of two months from the notification of the administrative resolution. Once the appeal is admitted by the judicial body, the claimant is granted 20 labour days to present its lawsuit, in which the legal merits and the evidence to support the claim have to be included/filed. Subsequently, a written summary with the conclusions could be granted. In this document both the plaintiff and the State Attorney should briefly argue on the respective legal merits of their cases and the evidence gathered. The average term in which a court issues its sentence ranges from two to three years.

Once the first instance judgment has been handed down, the possibility of a further appeal is subject to special rules. When there is no second instance procedure, the judgment may be appealed before the Supreme Court, through the cassation appeal, provided that certain requirements are met, and solely on legal grounds.

In any procedure, the plaintiff may request that the judicial body submit a preliminary ruling request to the ECJ. However, with the sole exception of the Supreme Court, the decision to request such a ruling from the ECJ is exclusively at the discretion of the Spanish judicial body. However, the Supreme Court (because it is the court of final instance) is compelled to file this preliminary ruling unless it considers that there is no doubt about the tax controversy.

Abbreviated Procedure
This judicial procedure is very similar to the one outlined above; the main difference is that the notice of appeal must also include the facts and legal grounds against the contested administrative action and be accompanied by the relevant evidence.

Likewise, when the first instance judgment has been handed down, the possibility of a further appeal before the High Spanish Judicial Courts may be filed if, for example, the amount of the claim is EUR30,000 or more.

4.3 Relevance of Evidence in Judicial Tax Litigation

Based on our experience, in judicial tax controversies, the evidence that is usually the most relevant includes the following:

- documentary evidence;
- witness evidence; and
- expert reports.

Any evidence on which the claim is based must be proposed and provided at the time of filing the lawsuit. Additionally, the plaintiff must provide at that time the reasons why the evidence is relevant to the appeal.

However, it is also possible to provide evidence after the lawsuit is filed, provided that such evidence was not available or known at the time of the filing and that it is relevant to the claim.

Expert evidence could also be provided after the lawsuit filing. But its issues and content should be detailed in advance within the lawsuit.

Witnesses and experts may be summoned to appear and be questioned before the judicial body.

Finally, note that for evidentiary rules, the civil jurisdiction regulations are supplementary to those applicable within the Contentious-Administrative System.

4.4 Burden of Proof in Judicial Tax Litigation

The GTL establishes the obligation of the STA to fully motivate its tax assessments/settlements.

During the tax administrative procedure, the general rule regarding the burden of proof is that the party asserting its right must prove the relevant supporting facts. The burden of proof related to tax benefits or credits falls, therefore, on the taxpayer.

In judicial proceedings (contentious-administrative claims) the burden of proof follows the general principles of the law. Thus, whoever alleges a fact or invokes a right must prove its existence.

In the criminal jurisdiction the Prosecutor's Office must discharge the burden and prove the commission of a criminal act during the trial. The presumption of innocence fully applies otherwise. This principle is also applicable to tax penalties.

4.5 Strategic Options in Judicial Tax Litigation

In general, there is hardly any possibility of strategically scheduling the submission of evidence and/or arguments, since they must be submitted at the required times mentioned in **4.3 Relevance of Evidence in Judicial Tax Litigation**.

The possibility of reaching transactional settlements or agreements on tax disputes is strictly forbidden by the law.

If and when a taxpayer notifies the STA of the submission/lodging of a judicial appeal with a request for suspension of the execution of the tax debt or penalty, the suspension will be automatically granted or maintained until the judicial court issues its judgment on the stay for execution. Suspension of tax debts execution usually require the guarantees laid down by the GTL.

4.6 Relevance of Jurisprudence and Guidelines to Judicial Tax Litigation

In essence, the case law in the Spanish legal system is key to guaranteeing the certainty and equality of citizens before the law with the unity of judicial decisions, as well as completing and integrating the legal system.

The judgements handed down by the Spanish Supreme Court constitute binding case law in tax matters, which all administrative and judicial bodies are obliged to apply and follow. Judgments issued by the rest of the judicial bodies (National Court or High Court of Justices, mainly) are not binding on different judicial bodies.

At the international level, the case law of the ECJ (in any issue related to EU tax law) is binding both on the Spanish courts (including the Spanish Supreme Court) and on the STA.

In tax appeals raising constitutional and fundamental rights issues, the case law of the Spanish Constitutional Court, the ECJ and the ECHR could be relevant before the Spanish judicial bodies and in claims brought before those courts.

OECD guidelines are deserving of greater scrutiny from, and influence on decisions taken by, our jurisdictional and economic-administrative courts.

5. Judicial Litigation: Appeals

5.1 System for Appealing Judicial Tax Litigation

In Spain, Tax Litigation issues are judicially reviewed in the Contentious-Administrative System.

It is composed of the following judicial bodies:

- the Contentious-Administrative Courts;
- the Central Contentious-Administrative Courts;
- the Contentious-Administrative Chambers of the High Courts of Justice;
- the Contentious-Administrative Chamber of the National Court; and
- the Contentious-Administrative Chamber of the Supreme Court.

In tax matters, the competence of the specific judicial body entitled to know and decide the appeal depends on the type of tax matter, the public body that issued the disputed administrative/tax act and on the amount appealed.

The Contentious-Administrative Courts will hear, at sole or first instance according to the applicable law, the appeals against the tax assessments of local entities.

The Contentious-Administrative Chambers of the High Courts of Justice will hear, as courts of sole instance, the appeals arising from:

- the acts and resolutions issued by the Regional and Local Economic-Administrative Courts that put an end to the economic-administrative procedure; or
- the resolutions issued by the Central Economic-Administrative Court regarding transferred taxes to the corresponding Autonomous Community.

Also, they will hear, as courts of second instance, appeals (for taxes amounting to more than EUR30,000) against judgments and orders issued by the Contentious-Administrative Courts.

The Chamber of the National Court shall hear, as court of sole instance, the appeals against acts of an economic-administrative nature issued by the Minister of Economy and Finance and by the Central Economic-Administrative Court regarding any taxes, with the exception of transferred taxes.

The Contentious-Administrative Chamber of the Supreme Court will hear cassation appeals of any kind, in the terms discussed in **5.2 Stages in the Tax Appeal Procedure**.

5.2 Stages in the Tax Appeal Procedure

In general, there is no second judicial instance in tax matters, except in the case of local taxes (and in the event that the amount appealed exceeds EUR30,000.)

The second instance appeal shall be submitted to the court which issued the judgment under appeal within 15 days of its notification, by means of a reasoned document containing the merits on which the appeal is based. The appeal shall be heard by the competent High Court of Justice, which shall decide within ten days from its resolution that the lawsuit was concluded for judgment. In practice, the ten-day term to issue the judgment is seldom respected.

Cassation appeal is not an ordinary appeal but an extraordinary remedy to challenge certain judgements. Since the last modification of the applicable jurisdiction law, the cassation appeal may only be admitted if all the following requirements are declared fulfilled by the Supreme Court:

- the judgment from the first or second instance court infringed either the law and/or Supreme Court precedents;
- there is an interest in passing judgment on the appeal related to precise binding precedents or issuing new ones; and
- the appellant's have provided evidence before the Supreme Court that the infringement committed by the instance court determined that court's dismissal resolution.

The extraordinary appeal of cassation must be filed within 30 working days before the same instance court which raised the judgement that is challenged on cassation appeal. In this respect, this appeal could be filed against National Court and High Court of Justice judgments. Residually, certain judgements raised by the Contentious-Administrative Courts could also be challenged through this appeal.

Once it is presented before the same instance court which solved the case at hand and that court has granted initial leave for appeal, the appellant should lodge the appeal before the Supreme Court within 30 days. In this second procedural stage, the appellant may not introduce new arguments or legal grounds different from those filed in the first stage.

5.3 Judges and Decisions in Tax Appeals

The Contentious-Administrative Courts and Central Contentious-Administrative Courts are single judge bodies while the Contentious-Administrative Chambers of the High Courts of Justice, Contentious-Administrative Chamber of the National Court and Contentious-Administrative Chamber of the Supreme Court are collegiate bodies (composed of two or more judges).

Judges are designated to serve in each judicial body on the basis of their experience and merits. They are all career judges (civil servants) and their independence from any authority is legally protected.

6. Alternative Dispute Resolution (ADR) Mechanisms

6.1 Mechanisms for Tax-Related ADR in this Jurisdiction

In Spain there are no ADR mechanisms regarding a pending judicial/administrative procedure. In accordance with the provisions of the law, the rights of the Spanish Treasury may not be subject to the result of any agreed transaction either judicially or extra-judicially, nor may any disputes arising in connection with such pending procedures be submitted to arbitration, except by means of a royal decree agreed upon by the Council of Ministers. We are not aware of any case in which such arbitration had been approved.

Notwithstanding the foregoing, in tax audit procedures and before any litigation is initiated, the GTL regulates a special agreement between the Tax Authorities and the taxpayer (*Actas con acuerdo*) for cases of special difficulty, whether in applying a specific rule or for the assessment or evaluation of elements of the tax obligation subject to uncertainties in their quantification.

6.2 Settlement of Tax Disputes by Means of ADR

See **6.1 Mechanisms for Tax-Related ADR in this Jurisdiction**.

6.3 Agreements to Reduce Tax Assessments, Interest or Penalties

See **6.1 Mechanisms for Tax-Related ADR in this Jurisdiction**.

6.4 Avoiding Disputes by Means of Binding Advance Information and Ruling Requests

Before ending the term to exercise its rights, or the possibility of filing tax assessments and/or self-assessments or the fulfilment of other tax obligations, taxpayers may contact the GDT regarding the tax regime, classification or qualification that corresponds to them in each case. The GDT has six months to issue a ruling and answer the request. However, in practice it takes longer to obtain a ruling and quite often the answer is delayed or unclear. Moreover, failure to respond within the required term does not imply acceptance by the GDT of the proposed content for the requested ruling.

The ruling shall be binding for the STA in charge of applying taxes in their relationship with the consultant. Also, the STA shall apply the criteria contained in the binding rulings to any taxpayer, provided that the facts and circumstances are identical to those included in such binding rulings.

It is very important that the case at hand could be deemed to be almost identical to the one of the binding ruling to avoid any kind of risk. However, if it arises from a close or similar situation, it could provide some legal certainty in order to show that a reasonable interpretation of the rule was followed and, therefore, that there was a lack of the subjective element (mens rea or negligence) required in the area of tax penalties.

6.5 Further Particulars Concerning Tax ADR Mechanisms

See **6.1 Mechanisms for Tax-Related ADR in this Jurisdiction**.

6.6 Use of ADR in Transfer Pricing and Cases of Indirect Determination of Tax

See **6.1 Mechanisms for Tax-Related ADR in this Jurisdiction**.

7. Administrative and Criminal Tax Offences

7.1 Interaction of Tax Assessments with Tax Infringements

Not every tax adjustment/tax assessment automatically leads to the imposition of a tax penalty. A tax infringement will only be considered as a tax offence if and when the following requirements are met:

- the infringement results from a taxpayer action or omission regarded as an offence by the law;
- the offensive action or omission is attributable to the taxpayer as a consequence of its intention or negligence (the subjective element of the offence).

Both the forbidden actions or omissions and the intention or negligence of the agent in causing them, must be proved by the administrative entities in the tax penalty procedure.

An action or omission subject to the GAAR contained in Article 15 of GTL is not considered as a tax offence. Tax shams (Article 16 of GTL), however, are considered tax offences.

When a taxpayer waives its right to appeal a tax adjustment/tax settlement, it is entitled to 30% reduction on any tax penalty arising from the offence. An additional 25% reduction would apply if the tax penalty is paid and the taxpayer decides not to challenge it.

A criminal tax offence may be applied as long as the debt from a tax infringement exceeds EUR120,000 and it is proven that the

taxpayer's conduct was intentional (mens rea). The existence of criminal tax offences can be appraised during the tax verification procedure. In such a case the administrative proceeding must be suspended, and the prosecution referred to the Public Prosecutor's office. If the Public Prosecutor or the judicial court or judge consider that there is no crime, the proceedings are returned to the STA.

7.2 Relationship Between Administrative and Criminal Processes

The tax verification proceedings are initiated first. Once they conclude with any tax assessment, the tax penalty procedure could be initiated, provided that the administrative entities consider there were tax infringements and penalties to be imposed.

When the STA finds evidence of a criminal offence against the State Treasury/the public finances and the tax due is expected to exceed EUR120,000 (Article 305 of the Criminal Code), the procedure will be referred to the Public Prosecutor's Office or the judge. With only some exceptions established by the law, the STA should issue two different tax assessments: one containing the tax due as a consequence of actions or omissions deemed to be the criminal offence; and the other containing the tax due as a consequence of actions or omissions different from those constituting the criminal offence.

The amount due as a consequence of a tax criminal offence is thus initially assessed by the STA and confirmed, amended or rejected afterwards by the courts. It must be paid at the time of the assessment and credited according to the result from the final sentence of the competent court on the tax due (if any).

7.3 Initiation of Administrative Processes and Criminal Cases

The tax penalty procedures may be initiated by the tax administrative entities following a tax audit procedure when they consider that a tax infringement has taken place. There are different tax infringements codified by the GTL that involve different tax penalties.

The criminal proceedings against a taxpayer must be initiated – and any tax infringement procedure on the same subject discontinued – when the STA considers that there is evidence of a tax criminal offence contained in the Criminal Code (Article 305) and the amount of the tax fraud exceeds EUR120,000.

Therefore, the difference between the offences and the procedures followed arise from the action or omission performed and the applicable law (GTL or Criminal Code). However, sometimes the STA tends to behave as if no clear legal distinction would exist between the administrative tax offences and the criminal tax offences.

"Non bis in idem" issues and limitations may be raised according to the jurisprudence of the Spanish Constitutional Court, the ECJ and the ECHR when an action or omission was considered not to be a criminal tax offence or tax administrative offence and different proceedings are subsequently initiated or followed.

7.4 Stages of Administrative Processes and Criminal Cases

In the tax penalty procedure the taxpayer is first notified of a "proposal of tax penalty" in order to file the allegations considered appropriate. Once the allegations have been reviewed, the "tax penalty agreement" is notified if those allegations were dismissed. This agreement imposes the respective tax penalty according to the "tax penalty proposal" unless the administrative body had accepted the arguments raised by the taxpayer. The "tax penalty agreement" could be appealed.

The criminal procedure is initiated when the STA refers the proceedings to the Public Prosecutor's Office or directly to the criminal jurisdiction. The criminal procedure is composed of a set of procedural stages culminating in the trial before a general criminal court deciding on all kinds of criminal offences.

The criminal judicial courts are therefore different from the courts reviewing the legality of the settlement and the tax penalty.

The payment of the settlement issued in advance by the STA regarding the prosecuted criminal offence should afterwards be credited to the tax debt finally determined in the criminal procedure.

7.5 Possibility of Fine Reductions

As mentioned in **7.1 Interaction of Tax Assessments with Tax Infringements**, the tax penalty amount may be reduced by 30% if the tax settlement is not appealed, and by an additional 25% if the tax penalty is not appealed and paid.

7.6 Possibility of Agreements to Prevent Trial

There is no such possibility regarding tax assessments and tax penalties either before their appeal or once appealed.

In the area of criminal offences, the STA will not forward the file to the Public Prosecutor's Office if the taxpayer has fully accepted and paid its tax debt before being notified of the commencement of any proceedings aimed at determining the tax debt. In other words, the full recognition and payment of the debt in these terms prevents potential criminal prosecution and conviction.

Once criminal proceedings have been initiated against the taxpayer, it is possible to reach an agreement with the Public

Prosecutor's Office. In order to do this, it is necessary to accept all the terms indicated by the respective public prosecutor (such as paying the entire tax debt and accepting a large economic sanction). In the case of an agreement, the public prosecutor will reduce the length of the term of imprisonment that it is requesting from the court (when the proposed prison sentence is two years or less, its execution can be suspended and the taxpayer will not be imprisoned at all).

7.7 Appeals Against Criminal Tax Decisions

An appellate procedure (*recurso de apelación*) may be lodged against the conviction that ends the first instance. The judicial bodies competent to hear the appellate procedure are:

- the Provincial Courts (*Audiencias Provinciales* for sentences handed down by the *Juzgados de lo Penal*; and.
- the Appellate Chamber of the National Court with respect to sentences issued by the National Court.

In addition to the appellate procedure, a cassation appeal (*recurso de casación* could be lodged before the Supreme Court against the judgments handed down by the Provincial Courts and the Appellate Chamber of the National Court.

A constitutional appeal (*recurso de amparo*) could also be filed before the Spanish Constitutional Court against the final sentences handed down by the Provincial Courts or the Supreme Court.

Article 954 of the Criminal Procedure Act (*recurso de revisión de sentencias firmes*), allows the review of a final judicial decision when the ECHR has declared that the decision in question violates any of the rights recognised in the European Convention for the Protection of Human Rights and Fundamental Freedoms, provided that the violation entails effects that persist and could not cease except by means of revision. The Criminal Chamber of the Supreme Court is the competent body to hear and decide on the case.

7.8 Rules Challenging Transactions and Operations in this Jurisdiction

The Spanish Constitutional Court has ruled out tax transactions challenged under the GAAR (Article 15 of GTL) being prosecuted as criminal tax offences.

Although it has not been specifically addressed and decided, a similar conclusion should apply in the case of tax transactions challenged under the SAAR contemplated in Council Directive 2009/133/EC applicable to mergers, divisions, partial divisions, transfer of assets and exchanges of shares. We do not know of any transaction of this kind being prosecuted as a criminal offence.

Tax shams (Article 16 of GTL) have been prosecuted and sentenced as criminal offences.

There are also many rulings issued by the Supreme Court that refer to the GAAR and tax shams in administrative tax cases.

8. Cross-Border Tax Disputes

8.1 Mechanisms to Deal with Double Taxation

In this law firm's experience, the STA will, as a general rule, make use of double taxation treaties (DTTs) to solve double taxation situations as long as the taxpayer has evidenced that he or she can benefit from the DTT as he or she is resident for tax purposes in one of the contracting countries.

However, eventually it may happen that either the taxpayer does not agree with the way in which the DTT has been applied or the DTT has not been applied to the taxpayer even though it should have been.

In both cases, the taxpayer may urge the tax authorities of the country in which he is resident to initiate a mutual agreement procedure (MAP) – regulated by a DTT or in an arbitration convention – with the tax authorities of another contracting state. The outcome of the MAP depends exclusively on the tax authorities of the contracting states.

Even though recourse to MAP has increased in recent years, it is not a widespread way of resolving double taxation disputes because of the limited chances of success. Therefore, domestic litigation is still the most common solution to double taxation issues.

8.2 Application of GAAR/SAAR to Cross-Border Situations

As a general rule, the STA apply the domestic GAAR and SAAR in cross-border situations covered by bilateral tax treaties (without further analysis of potential conflicts between domestic and conventional rules). However, most of the past challenges raised have been so far rejected by the Supreme Court.

Nonetheless, there are certain GAAR and SAAR matters on which the Spanish Supreme Court has already ruled, such as the "Brazilian juros case" or the "Austrian bonds case"; "double-dip" situations in which jurisdictions from different countries granted different tax treatment to the same income resulting in non-taxation of a specific cross-border arrangement.

8.3 Challenges to International Transfer Pricing Adjustments

Transfer pricing adjustments are usually challenged in the domestic tax courts, as this is the only way to impose tax penalties. However, EU arbitration convention or DTT MAPs have been increasingly used to challenge major international transfer pricing adjustments in recent years.

8.4 Unilateral/Bilateral Advance Pricing Agreements

Even though their use is still not widespread, advance pricing agreements (APAs) are becoming increasingly common in Spain. Requests for APAs have risen significantly in the last few years.

Spanish law provides taxpayers with a statutory right to seek APAs, whose filing procedure is set out below.

Pre-filing Actions

The company may file a preliminary request, with the following contents:

- identification of the parties;
- brief description of the transactions; and
- basic elements of the intended pricing proposal.

Filing

The actual filing must be accompanied by a proposal that is consistent with the arm's length principle and contain a description of the method and the analysis followed to determine the market value.

Evaluation

The tax inspection department of the Spanish national tax agency (the STA) will examine the proposal together with the documentation submitted. In addition, it may request additional information related to the proposal from the taxpayer, as well as explanations or clarifications.

Final Resolution

The APA filing procedure will be finalised when the tax inspection department approves or rejects the proposal filed by the taxpayer.

8.5 Litigation Relating to Cross-Border Situations

The cross-border matters which have traditionally generated the most litigation are transfer pricing issues and the deductibility of intragroup financial expenses.

There are certain actions that could eventually help to mitigate the above-mentioned controversies. These include:

- requests for APAs, as explained in **8.4 Unilateral/Bilateral Advance Pricing Agreements**;
- formulation of binding consultations to the GDT in relation to those operations/transactions whose tax treatment may not be clear or straightforward;
- carrying out non-aggressive but conservative and prudent tax planning; and
- due justification and sound economic reasons underlying the operations/transactions carried out.

9. Costs/Fees

9.1 Costs/Fees Relating to Administrative Litigation

There are no costs involved in the appeal for reversal (which is the first possible appeal that could be filed before the STA). Likewise, the economic-administrative procedure will also be free of economic charge. However, if the economic-administrative appeal is dismissed or considered inadmissible, and the Tax Administrative Court finds that the claimant/appellant displayed recklessness or bad faith, then he or she may theoretically be required to pay the costs of the procedure. We are, however, not yet aware of this possibility being used.

9.2 Judicial Court Fees

There are the legal costs arising from parties' lawyers and representatives. At first or single instance, when the judicial Court is rising the judgment or deciding about the actions or incidents brought before him, shall impose the legal costs on the party whose claim has been dismissed, unless the Court finds serious doubts about the facts or the applicable law.

Where the sentence recognised partially some claims, each party should pay its own legal costs, unless the judicial court, after giving due reasons, orders one of the parties to bear all of them because it has sustained its action or brought the action in bad faith or in a reckless manner.

At second instance, the legal costs should be imposed on the appellant if the appeal is dismissed in its entirety. Legal costs may be awarded in whole or in part, or up to a maximum amount.

In cassation appeals, the legal costs corresponding to the previous instance should be decided upon the above rules. The legal costs corresponding to the cassation appeal should be paid by each party unless the judicial court orders one of the parties to bear all of them because it has sustained its action or brought the action in bad faith or in a reckless manner. Cassation legal costs may be awarded in whole or in part, or up to a maximum amount.

Legal costs should be paid as requested by the court regarding each instance decision. Refunds are entitled in case of reversal. No interest is granted on these refunds.

9.3 Indemnities

In the event that the judicial court recognises the appellant/claimant (taxpayer) right and also grants it the refund of its legal costs, according to the rules mentioned in **9.2 Judicial Court Fees**, it should order the STA to pay legal costs. Therefore, the STA will compensate the taxpayer in this respect.

In addition, the STA will have to pay interest on the corresponding late payment since the taxpayer paid the tax debt now revoked by the judge. In the event that the debt was suspended, the STA must also pay the taxpayer the cost of the guarantees provided.

No further indemnities may, in principle, be claimed. In exceptional cases, however, some damages arising from the tax assessments – and different from the tax debts – interest on them and legal costs could be claimed when they directly resulted from the Tax Authorities' action.

9.4 Costs of Alternative Dispute Resolution

See **6.1 Mechanisms for Tax-Related ADR in this Jurisdiction**.

10. Statistics

10.1 Pending Tax Court Cases

There are no publicly available statistics on pending cases.

10.2 Cases Relating to Different Taxes

There are no publicly available statistics on the number of cases relating to different forms of tax.

10.3 Parties Succeeding in Litigation

There are no publicly available statistics on the proportion of tax cases that end in total or partial success for either the STA or the taxpayer.

11. Strategies

11.1 Strategic Guidelines in Tax Controversies

In recent years the use of electronic technology by the STA has increased and improved both the exchange of information between administrative entities at national and international level and the power to process and verify proper tax compliance from taxpayers.

In this scenario, our experience shows that, in order to manage the associated risks of tax disputes/controversies, it is important to follow these recommendations:

- A comprehensive and updated prior tax evaluation, as well as planning of transactions, should be performed, considering the approach of the STA to the transactions in question and the precedents from courts regarding issues previously raised by the STA.
- Produce and retain comprehensive evidence and documentary justification of any operation/transaction performed that may give rise to a tax controversy in a tax verification proceeding.
- Perform comprehensive and accurate tax compliance procedures and submit to the STA the evidence and documentary justification mentioned above.
- The burden of proof should be taken into appropriate consideration in order to discharge it through any of the allowed means of proof.
- All the disputed issues, from the very beginning of the appeal, should be covered, properly addressing the questions of fact and law with sufficient evidence and legal arguments that are up to date with the latest binding precedents from the courts.

GTA Villamagna was founded by professionals of recognised standing, with over thirty years of experience in the civil service and private legal practice. The firm's tax controversies team is formed by highly qualified former members of international law firms and tax administrations. It enjoys a reputation as a handler of complex, sophisticated and highly demanding tax procedures and its team is recognised by clients and peers as one of the leading tax litigation departments in the Spanish market. Significantly smaller than all its major competitors, its senior qualified lawyers are actively involved in rendering all of its services and offer personal attention. The firm has acted as legal counsel for major clients on some of the leading recent tax controversies in Spain and collaborates with leading law firms in many jurisdictions.

Authors

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GTA VILLAMAGNA
ABOGADOS

Trends and Developments

Contributed by:
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GTA Villamagna** **see p.21

Readers of this chapter, individuals and/or legal entities that are considering investing in Spain and therefore becoming taxpayers of some sort, will be informed of the tax controversies that currently arise and those that, in view of what we are presently experiencing and our own legal experience, could arise in the coming months.

In this regard, it is necessary to bear in mind the general tax inspection/control plan (the Plan) that the Spanish Tax Authorities (STA), in charge of carrying out tax verification and investigation procedures, make available to all citizens through their website.

It details the so-called tax inspection plans: all the matters or areas, the types of legal transactions concluded and the economic activities carried out during the year 2020, which will be checked and investigated as a matter of priority by the STA until a new tax inspection plan is approved for the following year.

It should be noted in this respect that, while the tax inspection plans are prepared for the year 2020, the tax verification and investigation is carried out in order to check compliance with the liabilities incurred for the tax periods for which the statute of limitations period had not expired.

By analysing the plan, both tax professionals and, of course, taxpayers themselves (current and potential) in our jurisdiction, can get some idea of Spanish tax procedures and priorities and, therefore, can make an informed guess of the risk that a tax inspection procedure would be initiated. To this end, we provide below a brief summary of the actions that we consider to be the most relevant of those to be carried out by the STA.

The General Tax Control Plan 2020
The STA publishes some general guidelines every year which, in sum, indicate the most relevant lines of action in the areas of inspection, collection and management of taxes to be carried out by the said Authorities.

Specifically, in the tax inspection area, the following general measures/guidelines proposed by the STA, in order to prevent and control tax fraud, should be noted:

With regard to international groups, big companies and tax groups, special emphasis will be placed on transfer pricing risks, using available information on related-party transactions as a basis.

By way of example, the Plan focuses on certain operations that will be subject to special attention by Tax Inspection Authorities in verification procedures; which are:

- business restructuring;
- valuation of intra-group assets transfers; and
- deduction of certain items that may significantly erode the tax base (accounting profit), such as:
  (a) royalty payments for the transfer of intangibles or for intra-group services; or
  (b) the existence of repeated losses.

Additionally, the STA is planning to carry out a special verification plan with respect to payers of corporate income tax (CIT) who have repeatedly included in their tax returns tax losses to be offset and deductions in the tax quota pending application.

The STA will also place special emphasis on the inspection of specific forms of tax fraud deriving from the simulation of tax residence outside the Spanish territory; as well as the verification/investigation of all those fraud schemes carried out to subtract from taxation the income from assets in Spain or due by possession of those assets.

Likewise, another focus of the STA's fight to prevent tax fraud will be the avoidance of the interposition of legal entities/corporate bodies whose main economic purpose, under the scope of the STA, is to serve as an instrument to avoid/delay the payment of personal income tax (PIT) by individual taxpayers whose taxation is irregularly reduced by the current difference in tax rates.

Finally, the control of any income obtained by non-tax resident artists and sportsmen and women who carry out activities in the Spanish territory will be intensified, given that such activities may be subject, depending on the case, to income tax for non-residents (NRIT).

This document, drawn up by the STA itself, in no way limits its power to carry out other tax verification activities in the field of other taxes or matters different from those described in this document. The fact is that the STA not only can, but must, check/investigate whether tax obligations have been correctly

settled wherever there are any doubts on this question, and may act outside of its tax inspection plans.

Non-Plan Issues

Notwithstanding the unquestionable relevance of the tax inspection plans, we have noticed that there are some other topics of great importance, which, without any doubt, constitute an essential focus of attention for the STA that will certainly raise controversies in the short to medium term. Our experience in providing legal and tax advice to ultra-high net worth individuals – both resident and non-resident in Spain or with interests in Spain – and of the legal assistance and defence services we provide to them before administrative entities and judicial courts (sometimes as a result of a lack of prior advice with regard to carrying out certain actions), makes us highlight the following:

Tax residence conflicts/disputes

Tax residence disputes may arise between the STA and the tax authorities of any other state; a circumstance that occurs when the tax residence conflict arises as a result of two countries being considered competent to levy a tax. This conflict may even occur between the different administrative entities of the STA, which happens when the conflict of tax residence arises between two Autonomous Communities (with regard to taxation involving CIT, PIT, wealth tax, inheritance and donation tax (IDT)).

The criteria for determining the residence in both cases, whether internationally or within Spain – between Autonomous Communities – are not the same. In the first case it is important to consider/comply with the provisions of any double taxation treaties (DTT), if they exist, and/or the internal regulations of each jurisdiction. In the second case, the criteria established in the Law 22/2009 should be followed. However, there is a common denominator that must be observed in all cases: the relevance of the evidence/proof available regarding tax residence in a given jurisdiction or territory for subsequent submission to an administrative procedure or judicial process in which a dispute arises in this regard.

The implications that could arise in the event of conflicts of tax residence (from the perspective of taxation in Spain), both in terms of tax debt – for PIT and for wealth tax, insofar as they could be subject to tax in Spain on worldwide income and property – and of obligations to provide periodic information, are of great importance.

In such situations, real problems of double taxation, understood as those resulting from the demand for tax debts in both jurisdictions, are common because the tax authorities of each territory consider the same taxpayer to be a resident in their respective territories. This may occur in accordance with the parameters of the DTT in force and/or their internal regulations, and even despite the DTT. Without prejudice to the fact that there may be specific clauses in the DTTs signed to resolve these conflicts of tax residence, in practice it is not infrequent that taxpayers are immersed in an unfortunate situation in which they may be considered to be simultaneously resident in two states, at least for a certain period of time.

In this respect, there is a circumstance which is both impossible to accurately predict and extraordinarily relevant, since it will undoubtedly be decisive for the tax residence of many individuals. We refer to the pandemic we are experiencing at world level due to COVID-19 and the impact it has had, and will surely continue to have, in terms of restrictions on the movement of people between different territories/countries and border closures, even within the EU.

Given this new situation, and that it is very possible that it will extend over time, there will be people whose tax residence will be questioned mainly on the basis of the criterion of staying in a certain territory (determined by reference to the number of days of physical presence). This is the case even if the reason for this "new obligation" to stay in a country or territory is completely beyond their control and has been imposed on them by the authorities. This scenario will likely force a review of the legal positions of many high net worth individuals before the STA, as well as between those authorities which may come into conflict over that position.

Spain has not yet issued express instructions on how these exceptional circumstances to determine the tax residence of individuals should be considered. However, the OECD understands that situations like this demand a special level of coordination between contracting states to prevent and mitigate the effects of excessive formalities necessary to re-establish the situation of taxpayers.

Likewise, circumstances relating to the pandemic will undoubtedly be a key factor in the short and medium term for those assessing a possible change of tax residence.

Misapplication of the special tax regime applicable to workers relocated to Spanish territory

It is not impossible that in the near future the STA will initiate tax verification procedures in relation to taxpayers who have improperly applied the "Special tax regime applicable to workers relocated to Spanish territory", the so-called "Impatriates" tax regime, regulated by the PIT law. This tax regime essentially allows certain taxpayers, who are subject to this tax, to pay tax during the period in which they changed their residence to Spain, and the five subsequent tax periods, as if they were taxpayers under the NRIT (which provides for tax rates ranging from 19 to 24%) and only for actual obligations. However,

certain requirements must be met in order to apply this rule. The most relevant are that: (i) the taxpayer must not have been resident in Spain in the ten tax periods prior to that in which the posting takes place; and (ii) the relocation should be as a result of an employment contract (with the nuances provided for in the regulations) or as a result of the status as a company board member (in which there is no participation in its share capital or, if there is such participation, this does not determine the tax status to be that of a person affiliated to the company).

The problem that has arisen to date – and we presume that it will continue in the future – regarding the application of this regime is that it is being abusively applied. The reason is that the STA have noticed in recent months the tax planning of large non-resident fortunes that, in order to avoid the application of PIT (and its taxation in Spain on a worldwide basis at marginal rates), have "forced" the application of the benefit's requirements to the extent that the STA have disregarded, for tax purposes, the creation of such structures or businesses. All this entails not only the demand of the tax debt for the PIT in Spain – that is applicable to the income obtained in this country – but also the demand of the tax debt for the PIT for all the income/yield/profit obtained worldwide; in addition to the non-fulfilment of the formal tax obligations in which they would have incurred.

Holding of shares in companies in low or no-tax countries

It has sometimes been the case that the holders of foreign fortunes that have subsequently been established in Spain, or where there has been an intention to do so, have not carried out a previous analysis of the legal and tax implications from the perspective of Spanish law. It is particularly important to do this where corporate structures/ownership interests are in companies incorporated in certain jurisdictions with low or no taxation and/or that do not carry out an economic activity under the terms of the Spanish PIT regulations; and/or where contracts/businesses take forms that are not recognised in the Spanish legal system (such as Anglo-Saxon trusts).

We refer to the potential risks for such situations, whether on the income tax (eg, possible application of the tax transparency regime, among others) of the holder of the shares or interest; on the PT (in the event that the holder establishes him or herself in an Autonomous Community where he or she is not entitled to tax relief and must submit his or her assets to taxation); or on the IDT, as a result of the transfer (inter vivos and/or mortis causa) that may eventually take place of the aforementioned assets and be subject to taxation in Spain. These situations should have been foreseen, in order to modify the structure and/or to anticipate the risks.

Anomalous legal business entities

Another relevant matter should be noted: the STA is still focusing their attention on certain business carried out by high net worth individuals and/or entities which could be deemed to not be real (tax sham), in the view of the STA, with the sole purpose of obtaining certain tax benefits in Spain or applying certain special tax regimes. The same is happening in the case of entities or individuals that applied certain tax regimes under the scope of an existing tax rule which should not be applicable as a consequence of the GAAR applicable to such situation.

Other Key Areas

Lastly, it is important to keep in mind the growing importance of taxation, both personal income tax and non-resident income tax (IRNR), of European and/or non-European clients who become tax residents in Spain. Additionally, as a result of these situations, relevant issues have arisen regarding the IDT (due to the problems caused by the legislation in force in the different Spanish regions that distinguish between the status of residents in Spain and non-residents) and in the wealth tax (for the same reasons). Litigation in this field is likely to increase in the coming months and/or years.

Additionally, as a result of the above-described situations, important new controversies have arisen regarding the IDT and the wealth tax, as a result of the different legislation in force in the Spanish regions. Tax benefits set forth in these pieces of legislation are strictly linked to the Spanish tax residence, without having in mind the new family arrangements that may occur; especially in the situation that COVID-19 is forcing on us.

For that reason, litigation in this field is likely to increase in the coming months and/or years.

To conclude, we believe that succession planning (through, among other mechanisms, Law 650/2012) will be more relevant than ever.

GTA Villamagna was founded by professionals of recognised standing, with over thirty years of experience in the civil service and private legal practice. The firm's tax controversies team is formed by highly qualified former members of international law firms and tax administrations. It enjoys a reputation as a handler of complex, sophisticated and highly demanding tax procedures and its team is recognised by clients and peers as one of the leading tax litigation departments in the Spanish market. Significantly smaller than all its major competitors, its senior qualified lawyers are actively involved in rendering all of its services and offer personal attention. The firm has acted as legal counsel for major clients on some of the leading recent tax controversies in Spain and collaborates with leading law firms in many jurisdictions.

Authors

Felipe Alonso co-founded GTA Villamagna in 2012 and specialises in general taxation, corporate tax law, indirect taxation and tax litigation. Before that he was head of the tax departments of both CMS Albiñana & Suárez de Lezo and the Madrid office of Baker & McKenzie, where he was a managing partner. Prior to going into private practice, Felipe was General Deputy Director of Legal Regulation and Legal Assistance for the Spanish Tax Agency and he has been a state tax inspector since 1982. He lectures at the Universities of Valencia and Madrid and the Tax Agency Institute as well as international tax forums. Felipe is a member of the Madrid Bar Association and the Spanish Association of Tax Advisors, AEDAF.

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