SPANISH LEGAL FLASH

RECENT LEGISLATIVE AND CASE LAW DEVELOPMENTS | SPAIN | Q3 2020

TAX

(i) COVID-19 implications on tax residence

The present problem was already analyzed in the SLF Q2 (can be found here), however it is extremely relevant to briefly address the question again because the Spanish General Directorate of Taxes through its recent binding ruling to consultation V1983-20 of 17 June 2020, has confirmed a thesis that could already be inferred from the text of the above-mentioned Order (issue addressed in the last publication). It concludes that the days spent in Spain during the State of Alarm/confinement shall be necessarily counted for the purpose of determining tax residence in our country from tax perspective.

Without prejudice to the effects that this criterion may have within future tax audit procedures carried out nearin respect of the "*new*" ones taxable persons, taking into consideration that international mobility is suffering huge constraints, it is important to note that Spanish Tax Authorities ("STA") is assuming OECDE criterion in those scenarios where the issue is about not to lose tax residents; however, is setting aside from that criteria/guidelines (as inferred from the text of the Order) when it is about maintaining or gaining new onesfor tax purposes.

Therefore, the evidence in respect of the voluntary or involuntary stay/residence imposed or not in Spain and the restrictions on movement to third territories or countries because of the concurrent circumstances, becomes particularly important.

(ii) The Spanish Supreme Court confirms that it is possible to initiate the sanctioning preocedure before issuing the liquidation

As it is known, the existence of an anti-legal, typical and guilty conduct is an indispensable requirement to impose a sanction. Therefore, it would be reasonable that the sanctioning procedure could not be initiated until the act of liquidation that terminates the inspection procedure and accredits the performance of the act legally typified as a tax violation has been issued.

However, the Spanish Supreme Court understands that the tax law does not establish any prohibition with respect to the initiation of the penalty procedure before issuing the assessment, since the initiation of the penalty procedure is not equivalent to the penalty

resolution, but rather to the simple instruction of a punitive procedure as a result of the existence of evidence of the commission of an infringement.

In addition, the Spanish Supreme Court declares that the initiation of penalty proceedings before the end of the inspection procedure does not infringe the rights to be informed of the accusation and the defense of the taxpayer.

(iii) It is possible to regularize a liquidation/self-assessment which could not benefit from the rules of the Autonomous Communities as it was prior to the judgment of the European Union Court of Justice

By means of the Judgment of 16 July 2020 (rec. 810/2019), the Supreme Court concluded that it is possible to review, in favour of non-resident taxpayers, those administrative acts for the assessment of inheritance tax which, because of a real obligation to contribute and without having been able to apply the tax benefits in force in the Autonomous Communities laws, have become final, because they were consented to, before the publication of the judgment of the European Union Court of Justice of 3 September 2020 (Case C- 127/12). The mentioned judgement of the European Union Court of Justice declared the law on inheritance tax to be contrary to European Union law because it entailed a situation of discriminatory treatment between residents and non-residents (in breach of Article 14 of the Spanish Constitution) as regards the system of tax benefits provided for tax residents in Spain according to whether their residence was in an Autonomous Community or elsewhere.

In the terms of the Supreme Court, although the doctrine derived from the European Union Court of Justice does not itself constitute sufficient grounds for declaring the invalidity of any act; it does compel, even in the presence of definitive acts, to consider the possibility of declaring a provisional liquidation null and void without one of the grounds for invalidity in Article 217 of the General Tax Law having to be invoked. The opposite would be contrary to the principles of European Union law. In conclusion, all those settlements that may incur in the situation described above shall be declared null and void insofar as they violate the rights and freedoms that are subject to constitutional protection by establishing differences in the tax treatment on inheritances between those taxpayers who are resident and non-resident in Spain.

(iv) New Supreme Court ruling on the criterion for the allocation of income and expenses

The Supreme Court, through its ruling of 17 June 2020 (rec. 3687/2017), has set a new criterion in relation to the principle of correlation of income and expenses. In the case at issue, STA found that the taxpayer accounted for the income from its development activity as customers made prepayments to it, so that income was brought forward in time. Although this is not in accordance with the accrual principle, it is expressly permitted by Article 11.3 of the Corporate Income Tax Law. This is as long as it does not result in lower taxation than would have been the case had the accrual principle been applied.

In addition to the above, the taxpayer allocated in each period the part of the expenses that belonged to the income recorded according to the principle of correlation of income and expenses. However, according to the opinion of STA, these expenses had to be activated, with all that this entails, in such a way that the taxpayer advanced expenses.

The taxpayer argued with the STA that if any the expenses or the income were regularised in accordance with the accrual principle, the same should be done for the other, which meant that it was not permissible an asymmetrical application of Article 11.3 of the Corporate Income Tax Law as it generated a higher tax liability than that which the taxpayer had to pay in the end. In other words, any adjustment to the criteria for allocating income and expenses would have to affect both economic flows bilaterally.

And this is the thesis that has been defended by the Supreme Court in its judgement. The Supreme Court states that STA may not temporarily allocate expenses recorded in accordance with the accrual principle and, however, may not do the same with income accounted for in advance of its accrual. In this way, the Supreme Court upholds the prevalence of correlation of income and expenses principle laid down in Article 11.1 of Corporate Income Tax Law over the special rule stated in Article 11.3.

(v) Estate tax implications on in life signed successors agreements

Two recent binding resolutions issued by the Spanish General Directorate of Taxation (reference V1780-20 and V1790-20) date both June 5th, 2020 holds that the tax benefits applicable to post mortem transfers of a family owned business (consisting on a 95% reduction of the tax base) shall no longer apply.

The line of reasoning held by the aforementioned General Directorate is that said tax benefits are conditioned to the owner of the family owned business having previously passed away, leaving this way in life signed successors agreements out of the scope of application of the foregoing tax benefit.

Having said that, it must be stressed the fact that estate tax in Spain is a tax managed by the different Spanish regions (17 in total) and it happens to occur that those two binding resolutions refer to an in life signed successors agreement in the region of the Balearic Islands. On the contrary, an opposite criteria was been held by the tax authorities in the region of Catalonia (resolution reference 286/19 of October 14th, 2019) resulting thus in a different tax treatment depending on the Spanish region competent and entitled to collect the taxes.

CORPORATE

During the last quarter and within the framework of the alarm state enacted, several regulatory texts have been published aiming at mitigating the effect of the economic and social impact generated by the outbreak of COVID-19.

In this sense, despite the preliminary measures adopted by Royal Decree-Law 8/2020, March 17 on the first quarter regarding to, among others, the possibility to hold corporate meetings by telematic means, the extension of the legal periods to draft, approve or audit of annual accounts, and the impossibility for the shareholdersto execute their separation right or to dissolvea company, there have been additional measures adopted within this last quarter which must be highlighted.

(i) Corporate apects

Royal Decree-Law 11/2020, March 31, introduces certain adjustments to Royal Decree-Law 8/2020 such as the following:

- Regarding the application of the economic result stated in the annual accounts, despite these annual accounts were already drawn up and the general shareholders meeting had already been called, this royal decree allows companies to replace the application of the result stated in the Financial Statements if justified by the company's directors.

- Regarding the possibility of holding telematic meetings by the corporate bodies of the companies, this royal decree establishes the possibility of holding them by multiple telephone conference and always provided that the secretary is able to recognize and identify to all the assisting members.

In this regard, the Royal Decree-Law 21/2020, June 9, extends the possibility of holding meetings of the corporate bodies by telematic means until 31 December 2020, provided that all the requirements are met. The board of directors may also adopt resolutions in writing in lieu of a meeting if the chairman so decides or if two of its members request it, until such date.

Finally, the Royal Decree-Law 18/2020, May 12 (as amended by Royal Decree-Law 24/2020, June 26) establishes a relevant issue regarding the dividend distribution. In this sense, the companies which take advantage of the temporary layoff proceedings (due to force majeure and due to economic, technical and organizational reasons) may not distribute dividends corresponding to the corporate year in which these temporary layoff proceedings are applied, unless they previously pay the amount corresponding to the exemption applied to the social security contributions and renounce it. This limitation on the distribution of dividends shall not apply to those entities which, on 29 February 2020, had less than fifty employees.

(ii) Foreign Investments

Royal Decree-Law 11/2020, March 31, together with Royal Decree 8/2020, suspends their liberalization regime regarding certain foreign investments, in order to protect Spanish companies within strategic sectors of activity (e.g. infrastructures, technology, and media) whose market value has decreased due to the current health crisis.

In this respect, the suspension implies that those investments (i) from residents outside the EU and the European Free Trade Association (EFTA) or residents of EU/EFTA countries whose real ownership corresponds to residents of countries outside the EU or EFTA; which (ii) exceed the amount of EUR 1 million and, (iii) grant the foreign investor a stake equal to or greater than 10 per cent of the share capital of the Spanish company, or which, as a consequence of any legal transaction or business, the foreign investor achieves effective control or management of the company, they will be subject to a previous authorization by the Spanish Authorities.

(iii) Bankruptcy

Additionally, Royal Decree Law 16/2020, April 28, establishes several new amendments regarding bankruptcy matters such as the following:

- The obligation of the insolvent debtor to apply for bankruptcy will be suspended until 31 December 2020, with voluntary bankruptcy taking precedence over necessary court proceedings.

- Provided certain conditions are met, the possibility of modifying Court approved refinancing agreements is allowed even if a year has not elapsed since the refinance agreements approval.

- The obligation of the insolvent debtor to seek liquidation if the Court approved agreement cannot be fulfilled will be suspended until 14 March 2021.

- More advantageous treatment of financing by especially related persons is enacted affecting bankruptcy proceedings declared within two years from the declaration of the alarm state.

- Losses for the current financial year 2020 shall not be taken into consideration for the sole purpose of determining mandatory dissolution provided for in article 363.1 e) of the Spanish Companies Act.

(iv) Recast text of the Bankruptcy Law

The Legislative Royal Decree 1/2020, of May 5, approving the revised text of the Bankruptcy Law, came into force on September 1, 2020. This regulatory text introduces some relevant modifications regarding insolvency matters, which are, among others, the following:

- It is expressly determined that the communication of the beginning of negotiations with the company's creditors will not by itself produce the early maturity of the deferred credits.

- It is established that the suspension of the foreclosure will apply to holders of rights in rem regardless of whether they are bankruptcy creditors or not.

- It is established that the amount obtained from the execution of a seizure will not be mandatorily used to pay the credit that would have given rise to it.

- It is determined that the default interest, unlike the remuneration interest, is not covered by the security right and, therefore, will be suspended after the declaration of bankruptcy.

- It is established that, once the bankruptcy has been declared, it will not be possible to offset the credits and debts of the bankrupt party except for those coming from the same legal relationship, whose offsetting will be permitted.

- It is established that the limit of the special privilege of the value of the guarantee is only applicable to the agreement, the refinancing agreements and the extrajudicial payment agreements.

- Participative loans are classified as subordinated.

- The elimination of security rights for loans from specially related persons is extended to all subordinated credits.

- The productive unit is defined and it is established that it will be the judge who will determine if the requirements to consider that there is a succession of a company (*sucesión de empresa*) are met or not, as well as its scope.

- In the area of credit capitalization agreements, the reference to the application of reinforced statutory majorities is eliminated, being only the legal ones applicable.

- The homologation of agreements with creditors representing at least 51% of the financial liabilities is allowed.

- The fact of being in a situation of insolvency is determined as a requirement to obtain a valid refinancing agreement.

- It is determined that the prohibition to request a refinancing agreement until one year after, is activated either requested by the debtor himself or by his creditors.

- The concept of "*disproportionate sacrifice*" is specified as a reason for contesting an approval.

(v) Bill amending the consolidated text of the Spanish Companies Act

On September 7, a bill which transposes the Directive on the promotion of long-term shareholder involvement was published. The main new implications of this bill are the following:

- As for the definition of listed company, it is detailed that they will be the ones whose shares are admitted to a regulated market that is domiciled or operates in a member state.

- Additionally, the right of companies to know the identity of their shareholders and to identify the ultimate beneficiaries is reinforced.

- It is established the right of shareholders to vote at least every 3 years on the policy of remuneration of directors. Likewise, more requirements are introduced in relation to the report on remuneration, increasing the required content.

- The bylaws are allowed to establish additional voting rights in order to reward loyalty to the company by the shareholders.

- Regarding to related-party transactions, the concept is modified to the extent that the percentage of significant participation is raised to 10%, in addition to the inclusion of certain rules for publicity and approval of this type of transactions.

- Finally, it establishes that the directors of the listed companies must be individuals and not legal entities.

(vi) Amendment of the Good Governance Code for Listed Companies

On June 26, 2020, the CNMV published the amendment of the Code of Good Governance for listed companies regarding:

- Intra-group relationship and potential conflicts of interest.
- Voting and assistance to the meetings by telematic means.
- Gender and age diversity in the administrative bodies.
- Increased transparency, communication and information measures.
- Remuneration of directors.

(vii) Court order of the Local Court No. 60 of Madrid on the adoption of precautionary measures based on the principle of "Rebus Sic Stantibus"

The Local Court No. 60 of Madrid issued a court order accepting the request for precautionary measures by a company that is unable to meet its obligations under a financing contract, as a result of the situation caused by the sanitary crisis related to COVID-19. This company asserts the principle of "*Rebus Sic Stantibus*" as a result of this sanitary and social crisis. The Court determined in the aforementioned court order that the requirements for the application of this principle were met: (i) unpredictability of the situation, (ii) intense economic affliction, (iii) accreditation of the impact on the particular situation], as well as the requirements in order to grant the precautionary measures requested [(i) fumus bonis iuris, (ii) periculum in mora].

(viii) Termination of Bilateral Investment Treaties between EU Member States

On September 30, 2020, the provisional application of the Agreement for the termination of bilateral investment treaties between member states of the European Union was published.

Thus, those bilateral investment agreements will cease to have effect, once that such state has joined the EU.

CRIMINAL LAW

(i) Alteration of certificates verifying the holding of the meetings of the General shareholders and the Board of Directors may constitute a forgery of documents crime

On June 3rd, 2020, the Spanish Supreme Court found the director of a company guilty for the commission of a forgery crime within article 390 of the Spanish Criminal Code. The defendant had issued false certificates regarding the holding of the General shareholders' meetings of the company. The High Court concluded that a certificate could be considered a commercial document and therefore issuing a forged certificate could be constitutive of a forgery of documents crime considering the seriousness of the alteration and its significance consequences on legal transactions.

(ii) Spanish National High Court acquits three Spanish residents from money laundering and tax crimes after being charged as a result of failing to report to the Spanish Tax Agency the information return on assets and rights held abroad

On September 21st,2020, the Spanish National High Court issued a resolution which acquitted three Spanish residents who opened bank accounts in Andorra and made deposits between 2009 and May 2012 without reporting them to the Spanish Tax Agency. These three individuals, as a result of a tax inspection, were accused by the public prosecutor for the commission of two crimes: tax crime and money laundering crime. The rationale behind the acquittal was that the statute of limitations of the tax crime (4 years in tax law and 5 as general rule -although occasionally 10- in criminal law) was ignored. Also, a worse treatment was applied breaching article 9.3 of the Spanish Constitution which guarantees the principle of non-retroactivity of punitive measures that are unfavorable. Furthermore, no evidence was found that confirms any intention of committing the crimes and that confirms the illicit origin of the money, essential requirement of the money laundering crime.

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