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Tax Controversy

Spain

Law & Practice
and
Trends & Developments

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practiceguides.chambers.com

2021

SPAIN

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), such as 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 they challenge their own self-assessed tax return (request for the rectification of a self-assessed tax return and refund of undue tax paid). Furthermore, taxpayers are also allowed to challenge withholdings and/or 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).

Corporate Income Tax

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.

Personal Income Tax

With respect to PIT, the STA are focusing their attention on individuals who 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 in CIT/PIT tax rates, but because these entities are commonly used to acquire the personal assets of their partners.

In addition, the STA are increasingly focusing its attention on tax residence issues and their subsequent implications for direct taxes and existing formal obligations. Over the last few years, many high net worth individuals have moved to Spain, or simply visited or acquired properties or assets 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.

Value Added Tax

Regarding VAT, the STA place 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 include the following.

- 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 to the implementation of the measures proposed in the OECD's Base Erosion and Profit Shifting (BEPS) Project. Most of these measures have already been implemented, including EU Tax disclosure rules (DAC 6) and the Anti-Tax Avoidance Directive (ATAD) anti-hybrid legislation.

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

The National Bureau of International Tax Affairs was created in 2013 to manage, plan and coordinate 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 additional tax assessments or against the resolution of the appeal. If such appeals are 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, whether the additional tax assessment comes from a tax settlement or a tax penalty must be determined. 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 cases in which the suspension is made without the granting of a guarantee are less common, taxpayers should grant the guarantee if they want to suspend the debt's 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.

2. TAX AUDITS

2.1 Main Rules Determining Tax Audits

The STA's main purpose is to monitor the proper compliance with their tax obligations of 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. These include:

- 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.

A tax inspection procedure could be initiated within the four years provided by the statute of limitations, to verify compliance with the tax obligation, as stated in Article 66 a) of the GTL. However, Article 68 of the GTL provides some actions or certain rules regarding the suspension of the statute of limitation which was affected due to the COVID-19 pandemic during the state of alarm in the year 2020.

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.

COIVD-19 State of Emergency

The first Spanish state of emergency, declared last year as a consequence of the COVID-19 crisis, temporarily suspended the statute of limitations in tax administrative proceedings such as tax inspections. However, this suspension was

lifted last September although a new state of emergency was declared from October to May 2021. In this sense, it is highly likely that matters derived from the above-mentioned suspension will be argued within procedures in which the tax act is being challenged in the near future.

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.

Effect of COVID-19 on Auditing Procedure

As a consequence of the pandemic, the use of telematic media such as Zoom has become widespread. As a direct consequence of the foregoing, the tax audit procedure has been expedited and, as a result, there is a risk to the taxpayer's rights, because these might be affected or even infringed until this new practice is duly regulated.

2.4 Areas of Special Attention in Tax Audits

In the authors' experience, key areas in a tax audit would be:

- tax residency
- 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 led the legal assistance and defence in more than 30 tax audit procedures in the last five 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 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.

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 that 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 of 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 have a duty/obligation to resolve all claims/appeals. Nevertheless, if the STA have not issued its decision within a six-month 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 less than 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 resolve 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 working 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 for a court to issue 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

In this firm's experience, in judicial tax controversies, the evidence that is usually the most relevant includes the following:

- documentary evidence;
- witness evidence;
- expert reports; and
- the legalisation of signatures and the apostille of the Hague, if certain foreign documents are needed to be filed as evidence in a national procedure.

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 justify 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

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 judgments 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 system (National Courts or High Courts of Justice, 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 Spanish judicial bodies and in claims brought before those courts.

OECD guidelines are deserving of greater scrutiny from, and influence on decisions taken by, Spain's 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.

Contentious-Administrative Courts

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

High Courts of Justice

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.

National Court

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.

Supreme Court

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.

Extraordinary Cassation Appeal

Cassation appeal is not an ordinary appeal but an extraordinary remedy to challenge certain judgments. 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 judgment 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 judgments 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 the term to exercise their rights ends, or the possibility of filing tax assessments and/or self-assessments or the fulfilment of other tax obligations is over, 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 in question should be deemed to be almost identical to the one to which the binding ruling applies 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 rules 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

Tax Penalties and Tax Offences

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 the GTL is not considered as a tax offence. Tax shams (Article 16 of the GTL), however, are considered tax offences; this is the conclusion generally reached by our Supreme Court.

Penalty Reductions for Co-operation

When a taxpayer waives their right to appeal a tax adjustment/ tax settlement, it is entitled to a 30% reduction (in case of conformity) and a 50% reduction (in case of agreement) on any tax penalty arising from the infringement. Furthermore, once the 30% reduction (from conformity) has been applied, where applicable, a further 25% reduction could be applied if the tax penalty is paid within the legal payment period and the taxpayer decides not to challenge it (not applicable when an agreement is finally reached). It is likely that a regulatory modification affecting these reductions will be approved in the near future. If so, the new reductions initially provided for in this modification would be as follows: 65% (in cases of agreement), 30% (in cases of conformity), and in relation to the additional reduction for paying the penalty within the legal payment period for cases of conformity, 40%. However, before such a modification is approved, the Spanish legislature has proposed a final modification of the reduction in cases of conformity from 30% to 45%.

Criminal Tax Offences

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.

Regularisation and Surcharges

To date, if as a result of a tax audit procedure taxpayer want to regularise its tax situation regarding future tax periods to comply with the criteria settled by the STA in that procedure, a complementary tax return must be filed. And if a new tax debt arises due to the regularisation, a surcharge is applied. In this scenario, the STA cannot impose any tax penalty.

However, the Supreme Court, the Spanish National Court and the Central Economic Administrative Court have been concluding – in broad terms – that in that cases the application of said surcharges could not be automatic and must be reviewed case by case. The purpose is to encourage extemporaneous but not spontaneous compliance (due to the taxpayer conduct being promoted by the knowledge of a previous tax action) to comply with the authorities' criteria.

To clarify this situation, it is highly probable that the implications of this untimely compliance in terms of surcharges will be regulated. As a result, taxpayers will have certainty about how and when they have to regularise to avoid not only the penalties, but the surcharges as well.

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 may be initiated, provided that the administrative entities consider there were tax infringements and penalties to be imposed.

When the STA find 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 consider 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 tend to behave as if no clear legal

distinction would exist between administrative tax offences and 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 has accepted the arguments raised by the taxpayer. The "tax penalty agreement" can be appealed.

The criminal procedure is initiated when the STA refer 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**, to date the tax penalty amount may be reduced by 30% (in case of conformity) and 50% (in case of agreement) if the tax assessment is not appealed, and by a further 25% (in case of conformity) 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 their 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 the 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 the 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

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 they can benefit from the DTT as they 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 they are 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 a 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.

We are not aware on any decision related to the MLI or the EU Tax Disputes Directive that have had any consequence in this domain.

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.

In particular, administrative courts have followed the criteria upheld by the ECJ in the Danish Cases not only in the case of dividends but also in the case of interest payments. Spanish courts have not yet ruled on this matter.

The domestic GAAR and SAAR already are considered to include a principal purpose test (PPT). Due to this, we do not expect the new developments introduced by the MLI and the amendment of the DTT preamble to affect the way tax authorities fight BEPS in cross-border situations.

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 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. INTERNATIONAL TAX ARBITRATION OPTIONS AND PROCEDURES

9.1 Application of Part VI of the MLI to Covered Tax Agreements (CTAs)

The option is pending on final ratification (publication) by Spain of the MIL. The approved text includes the option to apply part VI to the CTA.

No DDT signed by Spain contains an arbitration clause.

9.2 Types of Matters That Can Be Submitted to Arbitration

The option adopted under the MLI is the one mentioned in **9.1 Application of Part VI of the MLI to Covered Tax Agreements (CTAs)**.

According to it (Article 19.12) Spain reserves the right for the following rules to apply with respect to its covered tax agreements notwithstanding the other provisions of the Article:

- any unresolved issue arising from a mutual agreement procedure case otherwise within the scope of the arbitration process provided for by this Convention shall not be submitted to arbitration, if a decision on this issue has already been rendered by a court or administrative tribunal of either contracting jurisdiction; and
- if, at any time after a request for arbitration has been made and before the arbitration panel has delivered its decision to the competent authorities of the contracting jurisdictions, a decision concerning the issue is rendered by a court or administrative tribunal of one of the contracting jurisdictions, the arbitration process shall terminate.

The approved text pending ratification (publication) also contains specific reserves excluding from Part VI, according to Article 28.2.a) of the MLI, the following issues:

- application of internal GAAR and SAAR rules; and
- cases in which the party has been finally sanctioned according to criminal or administrative tax rules

9.3 Application of the Baseball Arbitration or the Independent Opinion Procedure

The approved text does not contain any specific option and/or provision on this subject.

9.4 Implementation of the EU Directive on Arbitration

This issue does not arise in relation to tax controversy in Spain.

9.5 Existing Use of Recent International and EU Legal Instruments

The authors are not aware of any use publicly revealed.

9.6 Publication of Decisions

Decisions should be made public according to general rules.

9.7 Most Common Legal Instruments to Settle Tax Disputes

The authors expect DTT after the MLI and EU Directive and Convention as those possibilities are the most effective. This is due to the guarantees they provide to settle the disputes.

9.8 Involvements of Lawyers, Barristers and Practitioners in International Tax Arbitration to Settle Tax Disputes

The authors are not yet aware of actual or projected involvements of Spanish professionals in the international tax arbitration field

10. COSTS/FEES

10.1 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 they may theoretically be required to pay the costs of the procedure. The authors are, however, not yet aware of this possibility being used.

10.2 Judicial Court Fees

There are the legal costs arising from parties' lawyers and representatives. At first or single instance, legal costs will be imposed 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 some claims but not others, each party should pay its own legal costs, unless the 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, 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 based 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.

10.3 Indemnities

In the event that the judicial court recognises the appellant/claimant's (taxpayer's) right and also grants it the refund of its legal costs, according to the rules mentioned in **10.2 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 resulted directly from the STA's actions.

10.4 Costs of Alternative Dispute Resolution

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

11. STATISTICS

11.1 Pending Tax Court Cases

There are no publicly available statistics on pending cases.

11.2 Cases Relating to Different Taxes

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

11.3 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.

12. STRATEGIES

12.1 Strategic Guidelines in Tax Controversies

In recent years the use of electronic technology by the STA have 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.

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ABOGADOS

Trends and Developments

Contributed by:
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The purpose of this article is none other than to inform individuals and/or legal entities who are resident for tax purposes in Spain (or in the process of becoming so) about the most controversial tax aspects in the Spanish legal system and on which the Spanish Tax Authorities (STA) and the courts place special emphasis.

As in previous years, the STA have published a set of directives/guidelines (the General Tax Control Plan 2021) whose main purpose is to inform taxpayers about its principal lines of action in the areas of tax inspection, collection and management.

It is necessary to recall the fact that those matters and taxes that can be subject to verification and investigation by the STA are not limited by the contents of the General Tax Control Plan 2021, in such a way that any operation or circumstance that may evidence non-compliance with tax regulations may be tracked by the STA.

It should be noted in this respect that, while the tax inspection plans are prepared for the year 2021, 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 above-mentioned Plan, both tax professionals and, of course, taxpayers themselves (current and potential) in Spain, 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 proposed STA actions that we consider to be most relevant.

General Tax Control Plan 2021

Tax residence

The main focus on individuals' tax residence issues is expected to be the implementation of tools based on "Big Data" information processing for the purpose of verifying the tax residence of an individual.

Through this the STA are expected to obtain relevant evidence to be able to determine both the physical presence of a taxpayer in Spanish territory over a period of more than 183 days, as well as the existence of a centre of economic and vital interests in Spain.

Controversies over tax residency have been ongoing for the last few years. A circumstance that is likely to increase as a result of the pandemic and restrictions on the movement of people.

In this regard, this firm's vast experience in tax controversies/litigation, due to the legal assistance provided to ultra-high net worth individuals/clients during tax audit procedures and judicial proceedings, has shown that one of the aspects on which tax inspection has focused its attention is the verification of the tax residence of individuals who are moving to Spain (for social, economic and/or political reasons) from third countries. In particular, we are referring to those people (ultra-high net worth individuals) who have been residing in Latin American countries or in the USA and have decided to move to Spain, or simply come to the country in order to make certain investments in real state, services or retail. In these cases, problems may arise if Spanish tax residence is acquired involuntarily,

and if it is declared within a tax audit procedure without having been previously foreseen.

For this reason, we duly recommend contacting a local tax lawyer, in order to clarify in advance the conditions on which Spanish tax residence would be acquired and, if so, the consequences that this will have in terms of direct taxation (from the perspective of personal income tax, wealth tax, as well as inheritance and/or gift tax) and in terms of obligations to provide information to the STA.

Secondly, the Tax Inspectorate is focusing its attention on changes of residence for tax purposes to other – more tax friendly in the eyes of the STA – jurisdictions, such as Portugal or Andorra. Tax issues may arise when these changes are not real; the appearance of a new residence is created, but the individual is still residing in Spain in accordance with domestic legislation.

Evidence of the new residence becomes essential. If special tax regimes (similar to the Spanish impatriate tax regime for individuals or the UK non-domiciled tax regime), which do not tax worldwide income, apply in the new jurisdiction, obtaining the tax residence certificate in accordance with the double tax treaty will not be easy or simply impossible.

Finally, from the domestic law perspective, controversies between regional tax authorities in which individuals are involved are arising due to changes in tax residence within the Spanish territory. This is due not only to professional or economic reasons, but also political ones or even to obtain a lower rate of taxation from the perspective of personal income tax, wealth tax, inheritance and gift tax.

The criteria for determining residence in a certain autonomous communities are not the same as those established by the national legislature to determine whether an individual is a tax resident in Spain.

Again, the change of residence to other autonomous communities or that the new residence is real, becomes essential, as well as proof of this reality.

These kinds of conflict within a tax audit procedure are frequent and very relevant in those cases in which a death-related succession takes place and the tax residence of the deceased is a litigious matter.

Tax on certain digital services

With regard to the tax on certain digital services, recently implemented in the Spanish legal system, it is established that the census, as well as verification management will be carried out in order to ensure the correct determination of who is going to have the taxpayer status.

Multinational groups, large companies and tax groups

In relation to this section of the Plan the STA will endeavour to focus, in particular, on the following issues:

- tax deductibility of financial expenses, in particular where such expenses derive from financing granted within the scope of the group to which they belong;
- verification of the correct fulfilment of reporting obligations for related-party transactions;
- multilateral controls carried out in the European Union in order to check intra-group payments for the transfer of intangibles; and
- the requirements for the incorporation of entities into tax groups.

Offset of negative tax bases

Continuing with those actions derived from the implementation of the 2020 Tax Control Plan, the

verification of many corporate entities who accumulate in their balances negative tax bases from previous years will also be carried out.

This is to the extent that these tax losses, which are being offset by the company that generated them, but may also be offset by others that continue their activity, substantially affect corporate income tax (CIT) collection.

In such a way that the STA will pay special attention to those files in which the aforementioned negative tax bases exist in order to verify the existence of the balance, its accuracy and its origin.

Non-plan Issues

Hybrid asymmetries and other anti-tax evasion measures

As a consequence of the transposition of the ATAD 2 directive, a new rule has been added to the CIT law with the purpose of regulating the "hybrid asymmetries" which were an unsolved problem in the Spanish tax system. The aim of this provision is to regulate situations in which a tax deregistration or a double deduction of expenses takes place as a result of the existence of different legal qualifications in different countries or territories.

As a general rule, in all hybrid asymmetries, the "primary rule", defined as the solution considered appropriate to remove the tax effects of the hybrid mismatch, involves the elimination of the referred effects of the hybrid mismatch, which consists in denying the deductibility of an expense when no income is generated.

In some of the modalities the "secondary rule" is also introduced, which is determined by the inclusion of income, provided that the country of origin has allowed the deductibility of the expense.

A draft law that also provides for the transposition of the ATAD 2 directive, which lays down rules against tax avoidance practices, is currently being discussed.

In this law, measures to fully align international tax transparency and exit tax rules with BEPS/ATAD 2 principles are expected to be implemented.

Professional entities

In recent years, professional entities have been under the focus of the STA. The reason: taxpayers shall not benefit from those tax consequences derived from the interposition of entities for the development of professional activities.

The first aspect that is subject to analysis by the STA in relation to this issue is whether the above-mentioned entity has material and human resources and whether those resources used to provide the service really belong to the company or to the professional themselves.

Secondly, whether the intervention in the provision of the service by the entity is real or not needs to be determined.

Once a tax inspection has been carried out, the STA will consider whether the issue is a tax sham or a conflict in the application of the tax law.

A tax sham can be defined as the apparent alteration of the cause, legal business, or the true object of an act or contract (ie, the mere interposition of the company to reduce the tax burden of the partner). In this regard, the STA tend to confuse the aforementioned tax sham with an incorrect valuation of related-party transactions (ie, the company's involvement in the provision of the service is real, but the professional is not adequately remunerated according to market conditions).

As opposed to a tax sham, there is another legal institution which is known as the conflict in the application of the tax law. Under this denomination there is a measure or an anti-abuse general clause of the tax rule that claims to be an effective instrument against tax shams that, with the formal application of a tax rule, avoids the application of another tax rule that may tax a determinate act or contract. The difficulty that the STA have when implementing this measure is that it is necessary to request a previous positive decision from the Advisory Commission.

The most recent court rulings, with regard to the application of the institutions of tax sham or the conflict in the application of tax law, offer little clarification. It remains necessary to examine each specific situation in order to determine whether the facts fall into one category or the other.

Currently, there are many proceedings before the courts where the legal/tax status of this kind of entity is subject of discussion.

Procedure for the derivation of tax liability

It is becoming increasingly common for the STA to start these types of proceedings in order to collect those tax debts that, somehow, have not been paid by the taxpayer.

Spanish tax law foresees two kinds of tax liabilities; on the one hand there is subsidiary liability and, on the other hand there is solidary liability.

While subsidiary liability is more stringent (demanding a series of requirements for it to be initiated; for example, that the taxpayer must be declared "insolvent" and have no assets to satisfy the tax debt), solidary liability can be initiated when the taxpayer has not paid the referred debt in the voluntary payment period.

In practice, this means that it is becoming increasingly common for the STA to initiate a procedure for the derivation of solidary liability as opposed to subsidiary liability. The reason: solidary liability is more convenient when demanding payment from the responsible parties.

Many responsible parties, through this firm's assistance, have disputed such derivations before the courts on the grounds that they were not carried out in accordance with Spanish tax law. This is due to the fact that the STA, on many occasions, apply the procedure that is the easiest for it (solidary liability), when it should have initiated the subsidiary liability procedure (or neither).

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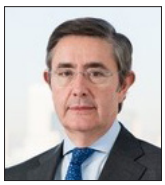

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