# Take the *bull* by the horns

CLIENTS WITH LINKS TO SPAIN SHOULD IMMEDIATELY ANALYSE THEIR TAX RESIDENCE IN LIGHT OF THE OECD'S COMMON REPORTING STANDARD, WRITES **PATRICIA GARCÍA MEDIERO**

## KEY POINTS

**WHAT IS THE ISSUE?**
The roll-out of the OECD's Common Reporting Standard on 1 January 2016.

**WHAT DOES IT MEAN FOR ME?**
How to determine Spanish tax residence; a review of Spanish voluntary disclosure procedures to allow taxpayers to become fully compliant before information exchanges commence in 2017; and the Spanish tax implications for clients who are settlors and/or beneficiaries of trusts.

**WHAT CAN I TAKE AWAY?**
The practical implications for international private clients with substantial presence, investments or family links to Spain.

**AS OF 1 JANUARY 2016,**[1] Spain has fully adopted the provisions of both the *Council Directive 2011/16/EU* (the EU Directive) 'on administrative cooperation in the field of taxation' and the OECD Common Reporting Standard (CRS) for the automatic exchange of financial account information. For Spain, these two steps undoubtedly represent the most important development in international exchange-of-information practices since the advent of the US *Foreign Account Tax Compliance Act* (FATCA). This development will have a substantial impact on international private clients with a substantial presence or interests in Spain.

## THE SCOPE OF THE CRS

Under the CRS and EU Directive, financial institutions in participating jurisdictions will report the full name and address, jurisdiction of tax residence, tax identification numbers and financial information of individual clients to their local tax authorities, which will then automatically exchange the data with the tax authorities of the participating countries where the individuals are tax-resident. As of 12 May 2016, there are 101 committed jurisdictions, of which 82 are participating jurisdictions (including Barbados, the BVI, the Cayman Islands, Gibraltar, Guernsey, the Isle of Man, Jersey and all EU member states). Spain is one of 54 'early adopters'.

Financial institutions in all participating jurisdictions will be obliged to ascertain and verify the tax-residence status of their individual clients by application of specific due-diligence procedures under the CRS. Individuals who are found to be tax-resident in Spain will have their Spanish tax-residence status and financial

*'Immediate review is key for those who are uncertain about their current tax-residence status'*

information disclosed by financial institutions to their local tax authorities, all of which will be automatically exchanged with the Spanish tax authorities from as early as 2017 onwards, in respect of 2016.

## SPANISH TAX RESIDENCE AND IMPLICATIONS UNDER THE CRS

Under Spanish domestic legislation, 'a tax resident in Spain' generally refers to an individual who remains in Spain for more than 183 days in any given calendar year, or whose business or economic interests are located in Spain. Temporary absences abroad are counted as deemed days of presence in Spain, unless the individual can prove tax residence in another jurisdiction by providing a certificate of tax residence. Spanish law does not contain split-residence provisions, so an individual will qualify as resident or non-resident for the entire calendar year.

The Spanish statutory residence tests also contain a presumption of Spanish tax residence if the individual's spouse and minor children are Spanish tax-resident. An individual may override this presumption by providing a certificate of tax residence in another jurisdiction.

Also, the Spanish legislation contains specific anti-avoidance provisions regarding an individual's transfer or claim to tax residence in tax havens, which in practice means the inability to sustain in most circumstances tax residence in tax havens if the individual's Spanish non-tax residence is challenged by the Spanish tax authorities.

As a result of the above, clients who currently report themselves as non-tax-resident in Spain, but who have a substantial presence, investments or family ties in Spain and are not tax-resident in any other jurisdiction (or claim to be resident in a tax haven), are highly likely to be considered Spanish-tax-resident and reported as such under the CRS. Thus, immediate tax-residence review and planning is of key importance for those who are uncertain about their current tax-residence status.

In addition, clients who have reported themselves as tax-resident in Spain, but who have not fully disclosed their foreign portfolios in their Spanish tax returns will see these fully disclosed and the information automatically exchanged with the Spanish tax authorities under the CRS. Individuals who are identified by the Spanish tax authorities as non-compliant, as a result of the information exchanged under the CRS, are highly likely to be subject to a full Spanish tax audit and possibly face Spanish tax-fraud charges.

Consequently, taxpayers who are likely to be found Spanish-tax-resident under the Spanish statutory residence tests, or those who have reported themselves as Spanish-tax-resident but who have not fully disclosed their foreign assets, income and gains in their Spanish personal tax returns (including settlors and beneficiaries of trusts and foundations), need an immediate evaluation of their situation to ascertain the steps to take towards full compliance.

## VOLUNTARY DISCLOSURES IN SPAIN

### BASIS OF TAX

Voluntary disclosures in Spain are carried out by means of late filings of relevant personal taxes for all years not covered by the Spanish statute of limitations; in practice, from 1 July 2016 onwards, this will generally mean late tax filings for years 2012 to 2015 (and generally 2011 to 2015 in cases of tax fraud).

Taxes that can be voluntarily disclosed include income tax (with marginal rates ranging from 45 to 56 per cent on regular income, and 21 to 27 per cent on investment income and gains, depending on the region of residence and the relevant year), wealth tax (with rates generally ranging from 0.2 to 2.5 per cent, with tax exemption for Madrid residents), and inheritance and gift tax (in cases of taxable events in years not covered by the Spanish statute of

## EXCHANGE-OF-INFORMATION RESOURCES

STEP has added further material to its automatic-exchange-of-information (AEOI) resources page:

- a webcast by George Hodgson on some differences between FATCA and the CRS which may trap the unwary;
- an article by John Riches on beneficial ownership registers and automatic exchange of beneficial ownership information;
- guidance on the CRS implementation handbook that the OECD released in August 2015; and
- briefing notes on the uncertainty over whether cash is a 'financial asset' for CRS purposes, and on the treatment of discretionary beneficiaries when the trust is a passive non-financial entity.

To access the AEOI resources, head to **www.step.org/policies/aeoi-resources**

limitations). Foreign asset information returns (Form 720) can be voluntarily disclosed for 2012 onwards.

Spain taxes its tax residents on a worldwide basis. Consequently, an individual is generally liable to Spanish income tax on all worldwide income and gains earned throughout the calendar year. Wealth tax is also levied on an individual's worldwide net worth at 31 December each calendar year, generally with a EUR700,000 *de minimis* exempted amount (with a current full tax exemption for Madrid residents). Worldwide inheritances and gifts are subject to Spanish inheritance tax if the heir or donee is tax-resident in Spain. Domicile, citizenship and/or nationality do not have any effect in determining liability to Spanish tax, which only looks to tax residence as a determining factor.

## DISCLOSING INTERESTS IN TRUSTS

In the case of undisclosed interests in trusts by Spanish-tax-resident settlors and/or beneficiaries, although trusts are arrangements alien to Spanish law, a growing number of tax rulings regarding trusts have been issued by the Spanish tax authorities, as well as relevant statements of practice and certain provisions in the Spanish anti-money laundering legislation. According to these, trusts are arrangements that must be disregarded for Spanish tax purposes. Assets, income and gains are attributed to the settlor or the beneficiaries for Spanish tax purposes depending on the actual facts of the case, the trust deeds and other relevant documents.

Spanish-tax-resident individuals with a taxable interest in a trust (whether deemed full ownership, usufruct, bare ownership or otherwise) must report this for Spanish income-tax, wealth-tax and inheritance-tax purposes; Spanish-tax-resident beneficiaries with a taxable interest in a trust must also report this in Form 720. Spanish-tax-resident settlors must fully report their trust arrangements in Form 720 even if the trust is irrevocable and they are not named beneficiaries.

## INTEREST, PENALTIES AND SURCHARGES

Voluntary disclosures also entail, in most cases, interest on overdue tax and surcharges of up to 15 per cent (given full and prompt settlement). In addition, in the case of Form 720, foreign assets reported late are generally subject to formal penalties, as well as a 45 to 56 per cent income-tax charge on the value of assets that the taxpayer cannot prove were either acquired out of income declared for Spanish tax purposes or acquired in years of non-tax residence in Spain.

*'Full voluntary disclosure enables non-compliant taxpayers to avoid potential Spanish tax-fraud charges'*

## ADVANTAGES OF DISCLOSURE

Full voluntary disclosure by means of late filings enables non-compliant taxpayers to avoid potential Spanish tax-fraud charges, applicable where the individual taxpayer has wilfully not paid more than EUR120,000 in any given tax in any given year not covered by the Spanish statute of limitations – a figure easily reached considering the taxing provisions for assets reported late, as described above.

Voluntary disclosure also entails a substantial reduction in penalties; the overall cost of a voluntary disclosure is generally significantly lower than the cost of tax assessments by the Spanish tax authorities during the course of an audit.

## CONCLUSION

The likelihood of a full Spanish tax audit of individuals who either declare themselves non-tax-resident but are reported as resident under the CRS, or who have failed to make a full disclosure of their foreign interests in their Spanish returns (including settlors and beneficiaries of trusts and foundations), will be very high once information begins to flow under the CRS. These audits could potentially result in tax-fraud charges against the taxpayer, a criminal offence under Spanish law.

Consequently, clients with substantial links to Spain (including presence, investments and family ties) are strongly advised to perform an immediate analysis of their tax-residence situation, in view of the new international framework on multilateral automatic information exchange. Clients who report themselves as tax-resident in Spain, but who have not fully disclosed their foreign assets, income and gains, are equally strongly advised to assess their Spanish tax situation under the provisions of the Spanish tax laws.

All individuals deemed Spanish-tax-resident with interests abroad, including settlors and beneficiaries of trusts, will need to achieve full and complete compliance in terms of Spanish tax during the course of this year if they wish to avoid the adverse consequences of being found non-compliant, including potential tax-fraud charges, once the CRS becomes operational in 2017.

### CRS DUE DILIGENCE

All financial institutions are required to follow a standard list of indicia to determine if an account is reportable to a specific jurisdiction. Find out more on page 31 of the OECD's *Standard for Automatic Exchange of Financial Account Information in Tax Matters*, available at **bit.ly/1k8wISL**

1 Following Royal Decree 1021/2015

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