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SPAIN: An Introduction

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SPANISH INTERNATIONAL PRIVATE WEALTH PLANNING IN 2019/2020: AN OUTLOOK

Following the Spanish regional and general elections during the spring of 2019, some of them yet to occur, some significant personal tax changes have already taken place and continue to be widely expected in Spain, with likely substantial impact for international private wealth clients with Spanish connections.

In the international arena, individuals whom financial or other reporting institutions from participating jurisdictions identify as tax resident in Spain under Common Reporting Standard (CRS) and EU Directive rules are currently having their financial information automatically exchanged to the Spanish tax authorities. This includes individuals who are settlors or vested beneficiaries or have any other reportable connection to a trust or foundation.

Tax residence has been identified by the Spanish tax authorities as one of the key focus areas of Spanish personal tax audits. These tax inspections usually end in substantial tax assessments by application of an increasingly aggressive interpretation of the Spanish statutory tax residence and Double Tax Treaty provisions, leading to lengthy court procedures and, in certain cases, criminal prosecutions under tax fraud charges.

The likelihood of a Spanish tax audit on individuals (including settlors and beneficiaries of trusts and foundations) who declare themselves as non-tax resident but are in practice spending a substantial amount of time in Spain, or have a substantial Spanish asset base or activities, or have been reported as resident under CRS, or have failed to make a full disclosure of their foreign interests in their Spanish returns, is currently very high. A full analysis of their Spanish tax situation is therefore of critical importance.

Individuals who are not tax compliant or have applied questionable technical criteria in their Spanish tax returns should consider entering into a voluntary disclosure procedure.

Taxes concerned on voluntary disclosures include income tax (with marginal rates under general rules ranging from 45% to 46% on regular income and 23% to 23.5% on investment income and gains), wealth tax (with rates generally ranging from 0.2% to 2.5%, with tax exemption for Madrid

residents), inheritance and gift tax where applicable, and Foreign Asset Information returns (Form 720).

Full voluntary disclosures enable uncompliant taxpayers to avoid potential Spanish tax fraud charges. They also entail a substantial reduction in penalties.

In terms of the basics of Spanish personal tax for 2019, resident individuals remain taxed on worldwide income and gains. The general marginal income tax rate for regular and investment income for 2019 is set at 45% and 23% respectively.

Spanish tax resident individuals with passive investments abroad remain affected by Spanish CFC provisions. This may have a special impact on individuals with Dutch, Luxembourg, Belgian, Irish or similar holding structures.

The Spanish exit tax continues to be of application in 2019. This charge takes the form of a deemed taxable gain arising on 31 December of the last year of tax residence. This may, however, be postponed in a number of situations and there are special provisions for intra-EU transfers of residence.

Individuals holding financial interests in non-Spanish assets must continue to file Form 720 Information Returns. Although the EU Commission is claiming potential discriminatory elements in the legislation governing 720 returns, the case has not yet reached the EU Court of Justice and therefore no EU resolution is expected in the short to medium term.

In terms of corporation tax, the general tax rate is set at 25% for 2019. The legislation excludes from the tax, under participation exemption rules, most dividends and capital gains derived by any Spanish tax resident corporation. This regime is extremely advantageous from a tax perspective and opens up major tax planning opportunities.

In terms of impatriation planning alternatives, the Special Impatriation regime continues to be a popular alternative for individual impatriations in 2019. Qualifying individuals (employees or company directors/Members of the Board of a Spanish company with no or less than a 25% shareholding) limit their Spanish personal income tax liability to Spanish source income and gains, plus employment income worldwide. Spanish wealth tax is limited to net Spanish situs assets and there is no obligation to file 720 Information Returns. It should, however, be noted that no protection is provided

against Spanish inheritance and gift tax. The regime applies for the first six years of tax residence.

However, a growing number of individuals applying this Special Impatriation regime are being subject to Spanish tax audits leading to substantial tax assessments and in some cases prosecutions under Spanish tax fraud charges.

Consequently, international private wealth clients currently applying the Special Impatriation regime are strongly advised to perform an urgent analysis of their eligibility to the regime with a view to determining their potential exposure to Spanish personal tax assessments and even potential Spanish tax fraud charges under current inspection practices.

Wealth tax continues to apply in 2019. Under general rules, the marginal rate remains at 2.5% for individuals with a net asset value in excess of EUR10.7 million (with a EUR700,000 tax-free allowance). This tax is fully transferred to the Spanish regions, so situations vary significantly.

As for inheritance and gift tax, regional benefits on close family free transfers (including Madrid, Canary Islands, Valencia, Balearics and Catalonia, as in prior years) may be applied to cross-border estates and gifts, both EU and non-EU, by application of a complex set of rules. Clients should obtain advice on inheritance and gift tax planning alternatives, to ensure applicability of regional benefits if available, and also in cases where the taxpayer is linked to a region with no benefits on close family transfers.

As a recent development on Spanish inheritance and gift tax, following the regional election in Andalusia in early 2019, the new conservative regional government has introduced a

99% tax exemption on all close family free transfers to individuals subject to regional Andalusia rules. Any future change towards a left-leaning regional government (which has historically long been the case) is likely to result in the abolition of this tax benefit and the reintroduction of the full tax.

Consequently, taxpayers with interests or ties to Andalusia (including Marbella, Sotogrande, Cadiz and Malaga) are strongly advised to perform a specific full inheritance and gift tax review, including planning for a full implementation within the current regional parliamentary season.

Finally, following the Spanish general election in late April 2019, a new Spanish government led by the Socialist Party is expected to be formed. As a result, as publicly announced, it is strongly likely that personal taxes will be raised, including an increase in income tax rates on investment income and gains. Other potential changes might include the curtailment of certain corporation tax benefits (particularly as regards the current participation exemption regime) and the introduction of minimum and maximum limits for regions in respect of both wealth tax and inheritance and gift tax rates, therefore potentially eliminating the wealth tax exemption in Madrid and substantially minimising current regional inheritance and gift tax benefits.

International private wealth clients are therefore also recommended to keep a close eye on developments, with a view to ascertaining the best way forward in terms of their Spanish personal tax planning, once the new government announces its specific tax policies and new regional parliaments are formed.