

SPAIN: An Introduction

SPANISH TAX PLANNING FOR INTERNATIONAL PRIVATE WEALTH CLIENTS: A 2023/24 OUTLOOK

In the context of the current regional and national election cycle, personal taxes have become one of the defining issues in terms of domestic political agenda. The coalition of the left running the national government advocates the present high tax approach, particularly among the affluent. The opposing conservative parties, with significant wins at the recent regional elections, uphold significant reductions and exemptions of wealth and inheritance taxes. The outcome of the next general election on 23 July 2023 will shape the path of Spanish personal tax policies for the next parliamentary term.

In terms of the basics of Spanish personal tax for 2023, Spanish tax resident individuals remain taxed on a worldwide basis. The marginal income tax rate for regular and investment income and gains are set around 50% (depending on the region of residence) and 28% respectively.

An individual's exposure to Spanish personal taxes depends on their tax residence status, as determined by the Spanish domestic law and the provisions of any relevant Double Tax Treaty. Tax residence tests under Spanish law consider (i) presence in Spain, (ii) direct or indirect economic ties to Spain and/or (iii) close family ties to Spain. Tie break tests under Double Tax Treaties largely adopt the OECD model.

Individuals who are tax resident in Spain in any given calendar year will generally be taxed on a worldwide basis for income, wealth and inheritance and gift tax purposes. Individuals who are non tax resident in Spain in any given calendar year will only be taxable on a Spanish situs/source basis.

Given the large number of foreign individuals with second homes in Spain and a stable presence in this country, **tax residence has been specifically highlighted as one of the target areas of review by the Spanish Tax Compliance Control Plan for 2023**; to this effect, the Spanish tax inspection is now actively using Big Data and Automatic Exchange of Information resources to pinpoint specific individuals and situations. These investigations often result in large tax assessment under aggressive technical criteria and subsequent lengthy court cases – sometimes under tax fraud charges.

Individuals, including settlors, grantors or beneficiaries of trusts or foundations, who declare themselves as non-tax resident in Spain but spend time in this country, even below 183 days, or have a substantial Spanish asset base or activities (directly or indirectly), are “tax nomads”, declare themselves as tax resident in certain favourable jurisdictions (e.g. Portugal, the UK, Switzerland or Italy) or have been reported as Spanish tax resident under CRS, FATCA or other, are strongly recommended to examine their tax residence status.

In this context, **uncompliant taxpayers or those applying untenable technical positions** (either as regards their tax residence status or in other situations e.g. vested beneficiaries of trusts who fail to disclose their interests in their Spanish returns) are **strongly encouraged to consider filing remedial returns to avoid potential Spanish tax fraud charges**.

Qualifying individuals relocating to Spain may now benefit from the **improvements in the Spanish Special Impatriation Regime in 2023**. This is a six-year regime available to employees or directors of a Spanish company. Qualifying individuals limit their Spanish personal income tax liability to Spanish source income and gains, plus employment income worldwide. Spanish wealth tax and solidarity tax is limited to net Spanish situs assets and there is no obligation to file 720 Information returns.

Under the new provisions, availability of the regime is extended to remote workers, certain entrepreneurs and high skilled professionals. Individuals appointed as directors of Spanish companies carrying on a trade or business may now qualify for the regime even if they are full owners of these companies in certain cases. Spouses and children under 25 may now also benefit from the regime as part of a family group, subject to a number of requirements and limits.

Wealth tax continues to apply in 2023. Under general rules, the marginal rate continues to stay at 3.5% 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, with Madrid and Andalucia applying a full exemption. Exposure to this tax may be reduced significantly with efficient tax planning.

On 29 December 2022, a **new Temporary Solidarity Tax** was enacted into law. This is a new federal tax which the Spanish regions cannot reduce or abate and applies to both Spanish tax resident and non-tax resident individuals. The tax has an initial duration of two years (2022 and 2023), but has been technically designed to allow for future extensions and applies to Spanish tax resident individuals with taxable net worth in excess of € 4 million. This tax **coexists with the existing Wealth Tax** - any Wealth Tax paid in the region of tax residence is fully creditable against the Solidarity Tax. Therefore the new tax is particularly relevant to taxpayers who reside in regions currently operating a Wealth Tax exemption (Madrid and Andalucia) or reduction (Galicia).

Potential tax planning mechanisms as regards this new tax include income limitation strategies in order to maximise the application of existing capping rules, the application of Business Property relief as well as shifting wealth via intergenerational gifts.

As regards **developments on taxation of real estate**, with effect from 2022 onwards, **foreign wrappers of Spanish situs properties have been brought into the scope of Spanish Wealth Tax/Solidarity Tax**. As a result, shares in private foreign entities with Spanish real estate with a direct or indirect value amounting to 50% or more of its total asset base are deemed Spanish situs. According to the Spanish tax authorities, tax must be levied on the whole of the taxable value of the shares in the foreign entity (therefore including any non-Spanish asset in the structure).

Potential tax planning strategies in these cases include broadening the asset base of the foreign entity to dilute the overall value of Spanish assets in the structure or certain debt restructuring actions.

As for **inheritance and gift tax**, regional benefits on spousal and close family free transfers continue to be of application to cross-border estates and gifts, both EU and non-EU. Mid-term, particularly depending on the outcome of the imminent general election, these may be substantially curtailed, reintroducing a full inheritance and gift tax, potentially with rates which might be in the region of 28% to 32%.

In this scenario, taxpayers with interests or ties to Spain are strongly advised to perform an Inheritance and Gift tax review to make use of current exemptions which may potentially be phased out or curtailed in the next Parliamentary term. Tax planning possibilities include free transfers of bare ownership of assets, retaining a legal right of use, shifting a significant portion of the family's wealth to the next generation. Planning for the best legal way to allocate and manage rights post-transfer is of critical importance.

International Private Clients should therefore undertake a review of their Spanish personal tax situation in view of the uncertainties ahead and consider shifting wealth over to the next generation in an orderly, flexible and overall tax effective manner.

Javier Estella Lana
Patricia García Mediero
Gabriel Pérez de Cárdenas

Partners
Avantia Asesoramiento Fiscal y Legal