Bové Montero y Asociados

DOING BUSINESS IN SPAIN

A practical guide to labour, tax and business laws and regulations

PROFIT editorial

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This book was published in the fourth quarter of 2015. It contains, therefore, all the regulations in force at that date. For more detailed information, readers can contact one of our offices directly.

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Acknowledgements

It is always difficult to summarise in a book of this size the legal, fiscal, accounting and labour rules which govern the creation of a business in Spain. We wanted to produce a work that dealt with all the core issues by using a language accessible by the businessman. If we have succeeded, we will be satisfied.

If in addition to this effort, and thanks to the various translations that are soon to be released in German, French, English, Italian, Portuguese and Russian, we make the process of doing business in Spain more widely known to the community of foreign investors, we will be even more pleased of having made our small contribution to Spanish economic development.

The updated 11th edition of this work, covering the law prevailing in 2016, was written by personnel of our legal and tax department. The person responsible for its undertaking and coordination is Belén Fernández Ulloa.

The whole process of editing, translating and distribution to clients and friends of Bové Montero y Asociados was coordinated by Brigitte Pollinger.

To all of them, my most sincere thanks.

José M. Bové

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1

Spain, the Preferred Destination for Foreign Investment

Few European countries can boast of having attracted as much foreign capital as Spain has. The first to arrive, more invaders than investors, were attracted by the geostrategic position of the Iberian Peninsula and the benefits of the climate and land, ideal for developing the primary sector. That is how it was seen by an endless list of peoples and civilizations from Celts to Arabs and Phoenicians to Romans. Centuries later, during the Industrial Revolution, Spain welcomed British and French investors who contributed decisively to consolidating a modern business fabric. During the course of the twentieth century, capital coming from Germany, the United States and Canada took over and made possible the installation of an unprecedented industrial infrastructure.

With accession to the European Economic Community in 1986, foreign investment underwent growth as never seen before. Spain became the preferred destination for capital originating from other European countries, while investment from the United States maintained steady growth. All economic sectors benefited from entry into the common European area, with the automotive, trade, energy supply and manufacturing industries as the main recipients of investment. The combination of controlled labour costs coupled with a high number of university graduates proved to be irresistible when it came to attracting leading brands in those sectors.

By the beginning of the twenty-first century, when the economy can only be viewed as global, Spain ranked among the top countries in the world in terms of foreign investment. The already traditional European and North American capital has been joined by investors from Russia, China and the Middle East, attracted by the strength of an economy that had already overcome the setbacks of 2009-2012. The renewal of railway and airport infrastructures has further strengthened the geostrategic position of Spain to the point of attracting foreign investment in 2014 of 15,812 million euros, 8.8% higher than the previous year.

In 2015, Spain once again became the preferred destination for foreign investment in Europe, a trend that is expected to be unchanged throughout the decade. In view of the constant arrival of increasingly diversified foreign capital, we feel it appropriate to begin this book with a brief introduction to Spanish reality. The following sections serve as a first contact with a country that has always welcomed foreign investment as part of its own heritage.

1.1. Geographic Distribution of Economic Activity

Spain enjoys a privileged location in the south-west of Europe as a gateway to and from America, Africa and Europe. It occupies a territory of approximately half a million square kilometres, divided between the Iberian Peninsula –which it shares with Portugal– the Balearic Islands in the Mediterranean Sea, the Canary Islands in the Atlantic Ocean and the autonomous cities of Ceuta and Melilla, located on the north coast of Africa and bordering Morocco. Currently, Spain has approximately 46 million inhabitants, who live mostly in urban environments. In this regard, the most important cities are Madrid (the capital), Barcelona, Valencia, Seville, Bilbao and Saragossa.

Madrid is not only the seat of country's political institutions, but also houses the head offices of most companies operating in Spain. A city primarily providing business-oriented services, it still retains an industrial belt of mostly the graphic arts, energy and chemical industries. It is also the hub of the high-speed railway network and of the largest concentration of foreign investment. Barcelona, meanwhile, thanks to the unstoppable growth of its tourism sector, is the busiest airport in Spain in number of passengers and the busiest cruise port in the Mediterranean. Despite the dominance of commercial and administrative services, it maintains an industrial fabric of great importance in the pharmaceutical and automotive industries as well as being one of the world's outstanding cities in organizing conventions and conferences.

The Port of Valencia, together with Algeciras in Cadiz, is the largest container and cargo port in the country. Because of the historical importance of its port, Valencia is the hub of a major trade sector which brings together a large number of logistics and transport agencies linked mainly to agricultural

exports. Seville is the main industrial centre in southern Spain, closely allied to derivatives of the primary sector and aerospace technologies, while Bilbao would be its equivalent across the northern third. Besides having one of the most important ports in Spain, economic activity in Bilbao and its province has always been characterized by the marked influence of mining and manufacturing, which is gradually veering towards the services sector. Saragossa, for its part, is noted for containing a major industrial estate in its metropolitan area, where the automotive industry and its auxiliary services play a significant specific role. It also has one of the largest logistics parks in southern Europe.

Beyond the main urban centres, the areas of fruit and vegetable production concentrated around the Levante and Andalusia deserve a special mention, making Spain the leading European exporter in the sector. Moreover, the Mediterranean coast is a prime tourist destination, while the north coast, especially Galicia, is a major focus of foreign trade aligned to maritime transport, having large ports and shipyards supplying ships worldwide. It may be said that the geographic diversity of the country, each territory having very different conditions, has contributed to Spanish productive output being widely diversified, today covering the widest range of industries and specialties.

1.2. Territorial Decentralization in Spanish Political Institutions

The 1978 Constitution provides that the State is a democracy which takes the form of a parliamentary monarchy. King Felipe VI is the Head of State, who arbitrates and moderates the functioning of institutions, assumes the highest

representation in international relations and exercises the functions conferred on him by law, most notably his role as commander-in-chief of the Spanish Armed Forces.

In turn, the *Cortes Generales*, a parliament representing the sovereignty of the Spanish people, are composed of the Congress of Deputies (the lower house) and the Senate (the upper house). MPs and senators are elected by universal suffrage and have the legislative power of the State. Executive power lies with the Government of the nation, which directs domestic and foreign policy, as well as civil and military administration. The government is headed by the President, elected by vote in Congress, who in turn directs the Cabinet.

The territorial organization of the State is committed to decentralization, being divided into three levels, based on the degree of proximity to citizens and powers conferred. At the lowest level is local government, which is run by councils of the various municipalities. At an intermediate level, municipalities are grouped into fifty-two provinces, each with its corresponding provincial deputation. Finally, Autonomous Communities define an area with common historical, cultural and economic characteristics and have their own parliaments which are elected by universal suffrage. Most autonomous communities encompass several provinces, although there are seven (e.g. Rioja and Murcia) which comprise a single province.

Autonomous governments have significant devolved powers, such as those concerning education or health, and some even have their own security forces. In the case of Catalonia and the Basque Country, the autonomous police force is independent from the national police force, whereas in Navarre and the Canary Islands it has a complementary role. Along the same lines of decentralization, it is worth noting

the particular case of the Basque Country and Navarre having, under a set of historic rights, their own treasury, which allows them to regulate and maintain their own tax system. As described in the chapters devoted to tax regulations, exclusive tax powers allow these two territories to apply different tax rates from the rest of the country.

This administrative organization, which is more complex than in other European countries, arises from the need to respond to the cultural and political uniqueness of Spain's various territories, thus ensuring representation of their respective interests in all state institutions. Spain was formed from the union of several independent kingdoms right at the end of the Middle Ages. Today, notable cultural differences between its territories can still be seen. The most obvious cultural difference can be found in the different languages spoken in various autonomous communities, which are co-official with Spanish in their respective areas of influence. These are Catalan in Catalonia and the Balearic Islands, Valencian in the Valencian Community, Basque in the Basque Country and Galician in Galicia. Although Spanish is the common language of the whole territory, co-official languages have a dominant role in autonomous government. Co-official status ensures that all procedures and formalities with the administrations can be carried out indiscriminately in both languages.

1.3. An Integrated European Union Currency Area

During the 1990s, a sweeping majority of countries belonging to the European Union decided to launch a process to harmonize their economic policies in order to introduce a single currency, the euro. On 1 January 2002, twelve countries

went on to share a single currency and a single monetary policy; Spain was among them. Today, there are now nineteen member states of the Economic and Monetary Union, the name by which the area sharing the euro as the single currency is known.

Countries included in the Eurozone not only share a common currency, but also remain committed to coordinating their fiscal and economic policies under the supervision of the European Commission and the European Central Bank. All Member States share a single market allowing for, unless expressly regulated, the free movement of capital, services, goods and people. Spain has been a member of the Economic and Monetary Union since its inception, along with Germany, Austria, Belgium, Finland, France, Greece, Ireland, Italy, Luxembourg, the Netherlands and Portugal. Also in the year 2002, four small European states decided to adopt the euro as their currency: the Vatican, Monaco, San Marino and Andorra. Five years later, in 2007, Slovenia would join the euro area. Cyprus and Malta did so in 2008, Slovakia in 2009, Estonia in 2011, Latvia in 2014 and, finally, Lithuania in 2015.

Today, several member countries of the European Union are on the waiting list to join the Eurozone. When their economies meet the required convergence criteria, they will be able to adopt the euro as their currency and join the Economic and Monetary Union as full members. It is expected that the next countries to adopt the euro as a single currency will be Bulgaria, the Czech Republic, Poland and Romania, between 2019 and 2020 at the earliest.

In this regard, it should be noted that several countries do not participate in the euro, that is they do not share the single currency, including Denmark, UK and Sweden.

1.4. Specialization and Diversification in the Spanish Financial System

Spain enjoys a diversified modern financial system, which is fully integrated into international markets. That financial system is made up of the credit market, the stock market and the money market. Only the latter, the money market, is subject to direct control by public authorities. Even so, it is open as much to banks as investment companies and financial intermediaries. For this reason, the current number of existing financial operators in Spain is frankly high.

When describing the entities that currently make up this rich and diversified financial system, the following list summarizes the various operators by their core business:

- **The central bank.** The Bank of Spain.
- **Lending institutions.** Spanish and foreign banks, the ICO (state-owned bank), savings banks, credit unions and credit institutions.
- **Financial auxiliaries.** Payment and electronic money institutions, mutual guarantee and refinancing companies, and appraisal firms.
- **Collective investment institutions.** Investment companies (securities and real estate), investment funds (securities and real estate).
- **Investment service firms.** Brokerage and securities firms, portfolio management companies and financial advisory firms.
- **Venture capital firms.**
- **Insurance and reinsurance companies and insurance brokers.**
- **Pension plans and funds.**

- **Mortgage securitization funds and asset securitization funds.**

With regard to the credit market and stock market, the role of the administration is almost exclusively limited to three activities. Firstly, the regulation of access conditions, then the task of ensuring the permanent presence of regular operators and, finally, control of operations of financial corporations. All these functions are performed in accordance with the practices commonly used in developed countries and, in particular, in other Member States of the European Union.

2

Investing in Spain from Abroad

As set out in the previous chapter, the Treaty on European Union proclaims full freedom of movement of capital between member countries. However, at the same time, the treaty recognizes that states have the power to establish the administrative requirements they deem appropriate on any operations, including those which a priori are liberalized. For this reason, it is essential to know in detail the specific regulations on foreign investment currently in force, since any foreign organization, investor or entrepreneur wishing to operate in Spain must obviously follow specific legislation from day one.

To this end, the following sections narrow down the definition of what would qualify as foreign investment and set out the administrative formalities to be completed

before (and after) making it effective. In addition, the main existing investment incentives, many of them linked to European Union programmes, are set out along with any restrictions to be noted on monetary transfers made to and from abroad. All of the above aims to present as accurately as possible the current environment governing the undertaking of foreign investment in Spain, and thus preparing the ground for the following chapters in which the legislation relevant to the development of any business activity is set out at length.

2.1. Overview of Current Legislation

Since entry into force of the Treaty on European Union, it can be said that foreign investments in Spain are fully liberalized. It is only necessary to declare such transactions after the event; that is, once the investment has already been made. There are, however, cases where notification is required prior to the operation, such as in the event of investment associated with a territory considered, under applicable law, as a tax haven.

At the same time, there are special rules relating to foreign investments in Spain in certain sectors and in particular in air transport, radio, minerals and raw materials of strategic value and mining rights, television, gambling, telecommunications, private security, the manufacture, distribution or trading in armaments and explosives for civilian use as well as activities concerning national defence.

Beyond the provisions for those particular sectors, the Government has the power to suspend the general regime of liberalization of foreign investment in uncommon situations. For example, this would happen in cases where the nature, form or requirements of foreign investments could affect the

exercise of power and public order, which includes activities related to the health and safety of the population as a whole.

2.2. Definition and Classification of Foreign Investments

Before addressing more specific issues, it should be made clear who are considered as foreign investors under Spanish law. Firstly, all non-resident individuals, who are domiciled abroad or have their principal residence there, are foreign investors even if they have Spanish nationality. Similarly, for companies domiciled abroad and public entities of foreign states. Change of a legal entity's registered office or the change of an individual's principal residence will also alter the classification of a foreign investment in Spain.

Foreign investments in Spain may be carried out in several ways. These various forms are set out below:

- By holding shares in Spanish companies, whose value is not listed on secondary markets. This includes, by way of example, the formation of a new company, the subscription and total or partial acquisition of their shares or taking over shareholdings. This section includes the purchase of securities, such as rights to subscribe for shares, convertible loan stocks or any other similar type which, by its nature, gives entitlement to a share in the capital. In addition, also included here is any legal transaction under which voting rights are acquired.
- Investing in shares of Spanish companies whose capital is fully or partly listed on Spanish or foreign stock markets. The same goes for subscription rights or similar, whatever the place of issue and acquisition.

- The setting up of branches, and the expansion in the provision of existing ones, of companies with registered offices abroad.
- The subscription to or acquisition of negotiable instruments relating to loans issued by residents.
- Investing in investment funds registered with the National Securities Market Commission (CNMV).
- The acquisition of real estate located in Spain, whose value exceeds 3,005,060.52 euros. If the investment comes from tax havens, the purchase of any real estate regardless of amount.
- Finally, the so-called *other forms of investment*: the setting up, formalizing or sharing in joint ventures, foundations, economic interest groups, cooperatives and partnerships, where the total value of the involvement of foreign investors exceeds 3,005,060.52 euros, or when coming from tax havens irrespective of the amount.

Thus, any investment made in Spain, which fits into one of the above seven forms, and which was carried out by a natural or legal person domiciled abroad, is to be classified as *foreign investment* when declaring its nature.

2.3. Formalities for Notification and Implementation

At the beginning of the chapter it was pointed out that, as a general rule, it is not necessary to declare foreign investments before making them; instead, it is enough to report their nature after they have been made. However, there are some cases where it is required to inform the administration in advance. To overcome any possible doubt, this section sets out when notification is necessary before making an investment

and when it is enough to do it afterwards. It should be noted that any notification of foreign investment, as well as any corresponding liquidations, must be made in the Register of Investments at the Ministry of Economy and Competitiveness.

A. Prior notification:

As already stated, the holder of a foreign investment must make a prior declaration whenever it comes from tax havens. It is important to note that such a declaration does not exclude the one to be made later, once the investment has already been made. However, there are certain exceptions to this general rule. The three cases in which prior notice is not necessary, regardless of the origin of the investment, are:

- Investments in negotiable securities.
- Shares in investment funds registered with the CNMV.
- Investments involving a foreign interest not exceeding a 50% stake in the Spanish company concerned, whether prior to the planned investment or as a result of it.

Whenever prior notification is required, it will be the holder who makes it official in the registry. This notification will be valid for a six-month period from the time it was provided. If the investment does not take place within that six-month period, a new notification will have to be made. Finally, note that when foreign investment from tax havens is to be liquidated, prior notification of such liquidation is not required.

B. Subsequent notification:

Returning to the general rule, most foreign investments are declared after being made. Such subsequent declaration is to be made by the non-resident owner. Additionally, when the transaction has been executed before a notary, it will be the notary who forwards the information to the registry. In special circumstances, other parties may be responsible for notification:

- If involving investments in negotiable securities, notification shall be the responsibility of the investment service companies, credit institutions or the relevant financial institutions.
- In the case of investments in securities not traded on secondary markets, the depository institutions or securities administrators will be responsible for notification of the transaction. In addition, any securities firm, brokerage or credit institution involved must make the declaration.
- In the case of investments in registered shares of a Spanish company, it is the company's duty to notify the authorities.
- Transactions in Spanish investment funds are to be declared by the company managing the fund.

As for the form and term of the investment, the declaration must be made within one month when affecting unlisted companies, branches, those known as *other forms of investment* and real estate. Investments concerning negotiable securities follow a declaration procedure which must be carried out by all the depository institutions and securities administrators, or else by those entities which, without acting as depository, settle transactions for the

purchase or sale of securities on the instructions of non-resident persons.

Finally, it should be noted that, under certain circumstances or simply because they are required to do so, Spanish companies with foreign shareholders and branches in Spain of non-residents must submit to the Directorate General of Trade and Investments of the Ministry of Economy and Competitiveness, an annual report on the development of investment within the maximum period of nine months from the end of the fiscal year.

It is worth remembering here that any breach of the obligations relating to the notification of foreign investment can be a punishable offence.

2.4. Aid and Incentives for Foreign Investment

In Spain, those natural or legal persons interested in investing from abroad can benefit from certain aid, which takes the form of grants or highly concessional loans. Such aid may come from the Spanish authorities, both state and regional, or directly from the European Union (EU).

Regional incentives (those of Spanish origin) are determined in certain respects by EU directives. They usually apply to companies intending to set up in less developed geographical areas with high unemployment rates or in industrial sectors in crisis. The central government, through various ministries, provides specific aid. In parallel, the autonomous communities also develop their own action programmes. Among the existing incentives, it is worth highlighting the granting of loans intended to finance fixed assets or the creation of companies, which are always in substantially more favourable terms than those offered by

the market. It should also be noted that grants are provided for investments in research and development as well as the internationalization of companies.

Furthermore, the incentives of the European Union appearing in EU budgets are known as structural resources, that is, European Structural Funds and the Cohesion Fund. Both are the main instruments available to the EU to strengthen economic and social cohesion. They aim to reduce disparities between the various territories by financing regional development plans in cooperation with member states.

2.5. Transfers Abroad and Exchange Control

Naturally, holders of foreign investments have the right to transfer the proceeds of their liquidation and the resulting economic returns abroad. It should be clarified that the existence of this right is not incompatible with the system of administrative procedure already discussed in previous sections or with the specific regulation of exchange control.

Following the guidelines set by the European Union, Spanish legislation regarding exchange control has been progressively liberalized, the basis for which is EU Directive 88/361/EEC. In effect, today it can be said that exchange controls pose no obstacle for any kind of business activity in Spain. The Spanish Government went beyond what was set out in the EU directive by liberalizing transactions with all countries, whether or not members of the European Union.

Thus, the basic principle on which Spanish legislation is based is that of complete freedom of capital movements and economic transactions abroad. Any acts, business,

transactions and operations between residents and non-residents involving (or which may be derived from) foreign receipts and payments are completely unrestricted. Similarly, so are transfers to or from abroad, as well as variations in accounts or financial debtor or creditor positions abroad. The only restrictions that may exist are those laid down up by law.

Therefore, we can say in general that there is no requirement to declare in advance any transfer abroad. However, there are always certain exceptions to the rule. Specifically, the following two cases are subject to compulsory prior notification:

a) The movement into or out of Spain of coins, banknotes or bearer cheques in euros or any other currency or physical medium, which would also include electronic media designed to be used as a means of payment, in excess of 10,000 euros per person per journey.

b) The movement within Spain of coins, banknotes or bearer cheques in euros or any other currency or physical medium, which would also include electronic media designed to be used as a means of payment, in excess of 100,000 euros.

It should be made clear that in both cases where *electronic means* of payment are mentioned, this does not refer to personal credit or debit cards.

Leaving the exceptions to the rule aside, receipts and payments between residents and non-residents are totally and absolutely unrestricted, as well as transfers to or from abroad, as long as they are handled through banks. The registered entity must only declare information concerning the transaction to the relevant bodies of the

state administration and the Bank of Spain. Even that declaration is not necessary when receipts, payments or transfers are less than 50,000 euros. Nor should it be forgotten that making payments and transfers abroad is not subject to the prior verification that any tax obligations have been fulfilled.

Additionally, and for purely statistical and informational purposes, any natural or legal persons resident in Spain who carry out transactions with non-residents, or have foreign assets or liabilities, must declare them to the Bank of Spain. The frequency of communications will depend on the volume of transactions carried out in the preceding year as well as the balances of assets and liabilities at 31 December. Specifically, the frequency of such communications will be as set out in the following table.

FREQUENCY OF NOTIFICATION ON TRANSACTIONS	
When the amounts of the transactions in the preceding year, or the balances of assets and liabilities at 31 December of the preceding year...	are equal to or greater than 300 million euros ONCE A MONTH
	are equal to or greater than 100 million euros ONCE EVERY QUARTER
	are less than 100 million euros ONCE A YEAR
	do not exceed the amount of 1 million euros: Only when requested by the Bank of Spain; within two months of the request

Bank accounts may be opened by residents at the overseas offices of both registered entities and any foreign banking or credit entity. For non-residents, the opening and maintenance of accounts in euros or other currencies is unrestricted at offices in Spain of registered entities.

3

Labour Market and Legislation

Any entrepreneur wanting to create a new company in Spain must have a thorough knowledge of the rules governing relations with its workers. For foreign investors, the obligation is even more urgent since current Spanish legislation emanates from a comprehensive set of laws that recast and correct each other, and go back as far as the second half of the 1970s.

The main source of labour law is the "*Estatuto de los Trabajadores*" (Statute of Workers). It is the basic law regulating employment contracts and sets out the rights and duties of the various parties involved. Because of its general nature, it does not include each and every particularity of the world of labour, so over the years a number of collective agreements have been elaborating the working conditions of the various productive sectors. Such collective agreements, negotiated

between companies and workers' representatives, are binding on both parties and are reviewed periodically.

Before making an investment in any given productive sector, the collective agreement must be reviewed in order to understand the rules regulating it and which may contain such specific aspects as the distribution of working hours or pay scales. This chapter summarizes the contents of general labour legislation in Spain from the Statute of Workers to the various reforms and specific laws, and therefore also includes sections on the recruitment and social status of foreigners.

3.1. Employee Wage Payment

The law in Spain sets minimum limits on the wage received by workers. Any remuneration below these limits is outside the law and can result in legal action. Specifically, the minimum wage set by the government, which is reviewed annually, is 655.20 euros per month. This is one of the lowest limits in Western Europe, only exceeding the minimum wage in Portugal.

However, such a minimum wage does not apply in those sectors where a collective agreement exists specifying general regulations. It should be noted that all collective agreements between employers and employees improve the wage set by the government. Their annexes include a pay scale specifying the minimum remuneration to be received by workers depending on their position within the company.

In most cases, workers are entitled to at least two extra monthly payments. This means that the annual gross salary is paid in fourteen instalments. However, many collective agreements contain the possibility of apportioning the extra pay over the whole year. In practice, this means that many

companies pay in twelve annual instalments, where each month includes a portion of the extra pay.

3.2. Distribution of Working Hours

Due to the different needs of each productive sector, the length and hours of the working day are set out in the various collective agreements and employment contracts. However, the law specifies that the maximum length of the normal working week is an average of 40 hours actually worked, calculated over the year.

Similarly, the working day may not exceed 9 hours, unless by collective agreement or an agreement between the employer and the workers, some other time distribution is established. In either case, workers have the right to a rest period of 12 hours between the end of one working day and the beginning of the next. Regarding the possibility of paid overtime, the law specifies that it may not exceed 80 hours per year.

As to holidays, legislation sets out that they are to be 30 calendar days per year of service. This means that those 30 days include both weekdays and weekends. In addition, throughout the year, there are 14 paid public holidays on weekdays, which cannot be carried over to the next year. The 14 public holidays are divided into those which are national (holiday in the whole of Spain), those which only affect a particular autonomous community and those which are local (two per year in total).

3.3. Social Rights of Workers

Since the Spanish transition to democracy, Spanish workers have enjoyed rights comparable to those of other European

countries. The Statute of Workers and the Spanish Constitution of 1978 guarantee freedom of association, including the right to form unions and to belong to whichever one the worker chooses. Meanwhile, unions are free to establish confederations and join international workers' organizations. In turn, nobody can be forced to join a union.

With regard to union representation of workers, it varies depending on the size of the company. When a company has less than 50 and more than 10 employees, staff representatives are responsible for representing the entire workforce. In companies with between 6 and 10 workers, there may also be a staff representative if so decided by a staff majority. Furthermore, where there are more than 50 workers, representation will be carried out by works councils. In all cases, it is the workers who freely choose and vote for their representatives.

It should be noted that in the event that the same company has several workplaces in the same province or neighbouring provinces, and that their separate totals do not reach 50 workers, but do reach that number in total, a joint works council between the various sites will be set up. Additionally, in the case of those multinationals which are required to have representatives in the European Works Council, they will be chosen from among existing works council members.

3.4. Recognition of the Right to Strike

That same 1978 Constitution protects the right to strike by workers to defend their interests and is called upon to specify the rules of that right in the drafting of a future law. However, the drafting of that law is still pending, so the right to strike remains regulated by the provisions of Law 17/1977, which

has subsequently been modified by a number of rulings of the Constitutional Court.

Specifically, the law includes the right to strike by express agreement of the workers, which can be adopted directly in assembly, through their legal representatives or by the various unions. When workers adopt the decision directly in assembly, a simple majority of those present is enough to approve the strike; the votes of a certain overall percentage of staff are not required.

Moreover, mandatory minimum services can only be stipulated when the company's business directly affects maintaining basic services such as healthcare and public transport.

3.5. Current Standard Contracts

Current legislation provides for the possibility of a number of ways to recruit personnel, which can be summarized into four main groups: permanent contracts, temporary contracts, training contracts and, finally, placement contracts. Within each of those four major types of contracts, there are different forms and types that respond to the various circumstances and needs of any one industry. All the above contracts must be put in writing and registered with the "*Servicio Público de Empleo Estatal*" (Spanish Public Employment Service).

The **permanent contract** states that the worker shall provide services without there being a date to mark its end. It is, therefore, a contract where the term of the relationship between employer and employee is not fixed. Permanent contracts can be full-time, part-time and for providing permanent seasonal services; the latter form being used to meet the needs of a particular business activity that takes

place during specific dates over the year. If an employer wants to dismiss an employee with a permanent contract without having to pay the compensation required by law, it may only be done on the grounds set out in the Statute of Workers or collective agreements. In section 3.6 below, the various circumstances that can lead to termination of the employment relationship are summarized.

For their part, **part-time permanent contracts** allow the provision of services for a number of hours a day, a week, a month or a year whenever this is less than full working hours. If production requires an increase in working hours, workers with a part-time contract can do overtime. There is always a maximum limit on the overtime that a worker can do, which will be as stipulated by law in proportion to the agreed working hours.

The permanent contract also has an additional variant: the **employment contract for support to entrepreneurs**. It is a new type of permanent full-time contract which can be used by those companies with fewer than 50 workers. Companies using this form of contract enjoy certain tax incentives and reductions in Social Security contributions as long as certain requirements and conditions are met. One of the main requirements is that workers must keep their jobs for at least three years from the date of the contract. Should any of the specified conditions not be fulfilled, the employer must return any incentives received upon signing this form of contract.

Fixed-term contracts, by contrast, explicitly state the completion date of the relationship between worker and company. Such contracts have four main variants: work and service contracts to perform a specific task, temporary contracts to meet production needs, replacement contracts to substitute for a semi-retired worker and interim contracts to

substitute for an employee who cannot occupy the post for a certain time. If the employer wants to end the relationship with the employee before the due date, or if the circumstances that led to the temporary contract are still valid, dismissal may be declared inadmissible.

Those who have just completed their studies may benefit from a **work placement contract**. To enter into this type of contract, workers must have completed their studies in the last five years (seven in the case of a disabled worker). Similarly, those studies must be for a university degree, vocational training qualification or be officially recognized as equivalent, and must qualify the employee to hold the position offered. In any case, if the worker is under 30 years old, the date of completion of the studies is not taken into account.

Finally, the purpose of a **training contract** is for workers to obtain a specific professional qualification, alternating on-the-job paid work with some theory-based learning. It is important to note that the worker must be seeking work and have no formal training related to the activity to be undertaken. With this type of contract, companies benefit from a 100% reduction in Social Security contributions, for both the worker and the company, and a 100% refund of the costs of associated training courses.

3.6. Compensation for Termination of Contract

Employment contracts, as discussed above, can be arranged for a fixed or indefinite period of time. If indefinite, the employer cannot terminate them unilaterally unless one of the situations provided for in the Statute of Workers arises, that is, by disciplinary dismissal based on serious and wilful breach by the worker.

If such disciplinary grounds do not exist and the dismissal is declared unfair, the employer is required to compensate the employee in an amount equivalent to 33 days' pay for each year of service up to a maximum of 24 months' salary. However, compensation for unfair dismissal in contracts signed before the 12th of February 2012 will be equivalent to 45 days' pay, per year of service, for the time worked before that date, and equivalent to 33 days' pay, per year of service, for the time worked after that date. The compensation package shall not be in excess of 720 days' pay unless the sum of days accumulated before the 12th of February 2012 is higher than 720 days, in which case that sum shall apply to the amount of compensation up to a maximum of 42 months' salary.

In addition, the Law permits the termination of an employment contract in the objective circumstances expressly provided, it being also necessary to meet the following requirements:

- Dismissal must be communicated to the employee in writing, stating the cause leading to termination.
- Compensation equivalent to 20 days' pay per year of service, with a maximum of 12 months' wages, must be made available to the employee upon receiving the written notice.
- A period of 15 days' notice must be granted from the time the worker personally receives the communication up to the termination of the employment contract.

Once termination of contract has been carried out, a court may rule that the dismissal be declared unfair if it was produced under a variety of circumstances. In such a situation, the employer is required to reinstate the employee in his previous job. Essentially, there are two situations that can lead

to unfair dismissal: first, that the reason for dismissal is one of discrimination as laid down in the Constitution or any other law in force and, second, that the fundamental rights and civil liberties of the worker have been violated.

Similarly, there is one other case that can lead to unfair dismissal. Such a case would occur if the termination is carried out while the worker is enjoying any kind of leave or situation regulated by law to support the reconciliation of work and family life. Such leave includes, for example, reduction of the workday to care for family members or suspension of the contract due to pregnancy. Should dismissal arise in such circumstances, the power of a court is to rule on whether it should be regarded as so arising or not.

3.7. Special Employment Relationships

Everything described in this chapter applies in most employment relationships when a company pays a salary to an employee in return for their services. However, the diversity and complexity of the labour market has led to working relationships arising to which the general law cannot respond. For this reason, certain industries and jobs have specific regulations that go beyond what is described here. This is the case, to cite a few examples, of senior management, professional sportsmen and women and domestic workers.

In the field of foreign investment, provisions on commercial agents may be of special interest. This would involve personnel engaged in sales transactions as a mediator. When this special employment relationship takes place, the "*Ley de Contrato de Agencia*" (Law on Agency Agreement) may apply, which determines the establishment of a business

relationship and which is harmonized with the EU Directive on Commercial Agents.

3.8. Social Security Contribution Base

The cornerstone of the welfare state in Spain is the Social Security system, which aims to provide citizens with a range of benefits in the most varied situations of need, from retirement to sick leave. Specifically, the main services offered by Social Security fall into two broad areas: first would be everything related to medical and pharmaceutical services, universally; and then cash benefits intended to cover temporary disability, unemployment, pregnancy leave, maternity, permanent disability, retirement, widowhood, orphanhood and other aspects of family need.

The Social Security system is financed by contributions that employers and employees pay monthly. Personnel are classified into a series of contribution groups for the purpose of determining their Social Security contributions. Each group has a maximum and a minimum contribution rate, which are usually revised every year.

It could occur, for example, that after making the appropriate calculations, a worker with a very high salary has a higher contribution base than the one set by the State. In that case, the contribution base would not be the one derived from his salary, but the maximum set by law. Similarly, a worker with a very low salary, which does not amount to the minimum contribution base, would calculate what he has to pay to Social Security from what is set by law rather than from his actual wage.

At present, the minimum and maximum bases on which contributions to Social Security are calculated according to each professional and job category are set out in the following table.

CATEGORY	MINIMUM BASE EUROS/ MONTH	MAXIMUM BASE EUROS/ MONTH
1. Engineers, graduates and senior management	1.067,47	3.642,00
2. Qualified technicians and assistants	885,37	3.642,00
3. Clerical and workshop supervisors	770,23	3.642,00
4. Unqualified assistants	764,17	3.642,00
5. Clerical officers	764,17	3.642,00
6. Subordinates	764,17	3.642,00
7. Clerical assistants	764,17	3.642,00
	EUROS/DAY	EUROS/DAY
8. Skilled workers grade 1 and 2	25,47	121,40
9. Skilled workers grade 3 and specialists	25,47	121,40
10. Unskilled workers	25,47	121,40
11. Workers under 18 years of age	25,47	121,40

From these contribution bases it is possible to calculate what to pay to Social Security for each worker. As noted in the preceding paragraphs, the contribution is shared by employee and company, although the percentage to be paid by the employer is substantially higher. To know how much the contributions to Social Security amount to, it is only necessary to multiply the base by the contribution rate, which comes out as a percentage. Contribution rates are also reviewed annually and are published in the annual Budget Legislation. The following table shows a summary of current contribution rates and sets out how much the employee pays and how much the employer pays.

It can be said, without being over-cautious, that the calculation of contribution bases and rates requires the advice of a professional who knows the current legislation in detail and the particular characteristics of the company, since any error in this regard may lead to a penalty.

	EMPLOYER %	EMPLOYEE %	TOTAL %
General contingency	23,6	4,7	28,30
Unemployment (perm. contract)	5,50	1,55	7,05
Unemployment (temp. contract)	6,70	1,60	8,30
Professional training	0,60	0,10	0,70
Salary guarantee fund	0,20	-----	0,20

3.9. Employers Liability

As just mentioned in the previous section, the administrative and management bodies of a company are responsible for any breach of the law. Non-payment of contributions to Social Security, non-compliance with rules on health and safety at work or fraudulent subcontracting, to name just a few examples, may incur a civil, administrative and even criminal penalty, for which the employer is personally responsible. For this reason, and given the complexity of many of the procedures which companies must follow, it is always advisable to have the opinion of an expert.

Of all the contraventions that can be committed in the development of a business, all the provisions of Law 31/95 on prevention of occupational hazards and supplementary regulations are of great importance. Its articles provide for significant penalties of up to 819,780 euros for the lack of proper preventive measures in the company. It is vital, therefore, to provide workers with adequate training on the prevention of occupational hazards inherent to business as well as provide the suitable material (as set by law) to reduce the incidence of accidents at work. It should not be forgotten that it is now a matter of the highest order for the Labour Inspectorate, on a par with non-payment of contributions and irregular recruitment.

3.10. Social Status of Foreigners

Until the mid-1990s, the foreign population percentage in Spain was much lower than in most countries of the European Union; it barely exceeded 1% of the population. But since 1998, and especially following the economic boom the country underwent between 2002 and 2008, Spain has

been seeing growth in its foreign-born population that is unmatched at any time before. If in 2002 the percentage of foreigners reached 4.73%, in 2010 it came to more than 12%.

Organic Law 4/2000, which was later revised in 2003 and 2009, develops all the regulations applicable to the entry and residence of non-EU foreigners in Spain. In this regard, it should be noted that there are major differences between the conditions for remaining in Spain that apply to foreign citizens from the European Union and those governing people from other countries, to the point of forming two completely different regimes.

From 1 January 1992, **citizens with passports from the European Union**, under European Community regulations, may work in Spain in the same conditions as a Spanish national citizen. They can perform any work from the first day of arrival in the country without it being necessary to obtain any kind of work or residence permit. If their stay is less than three months, whatever their reason for remaining, they need nothing more than to be in possession of their passport or identity card. This regulation also applies, since 1994, to citizens of Iceland, Liechtenstein and Norway, who, although not members of the EU, do form part of the European Economic Area (EEA).

While EU citizens can extend their stay in Spain as long as they wish, if they intend to remain for longer than three months they need to apply, personally, for registration in the *Registro Central de Extranjeros* (Central Register of Foreign Nationals). That single step will provide them with an NIE (Foreigner Identification Number), which will allow them to carry out any transactions in Spain, including any which are economic in nature. Thus, for example, holding an NIE is required when opening a bank account, creating a business or

purchasing a vehicle. The same applies when carrying out an economic activity with tax significance.

In contrast, **non-EU foreign citizens** have much more limiting conditions on their stay, and need to be in possession of a residence permit to remain in Spain legally. Currently, there are three different types of residence permits, as set out below:

- **Short term.** Allows a stay in Spanish territory for up to 90 days within a six-month period from the date of first entry. This is without prejudice to provisions on admission for the purposes of studies, mobility of students, unpaid work placement or volunteer work. After 90 days, in order to remain in Spain, an extended-stay or residence permit is required.
- **Temporary residence.** This allows non-EU foreign citizens to remain in Spain for more than 90 days and less than 5 years. Again, without prejudice to provisions on studies, mobility of students, unpaid work placement or volunteer work. There are four types of temporary residence permits: non-profit, family reunification, with exception of work permit, and for exceptional circumstances.
- **Permanent residence.** When non-EU citizens have remained in Spain continuously and legally for more than five years, they acquire the right to reside in Spain indefinitely. This entitlement enables them to work without any kind of limitation and on equal terms with any other Spanish citizen.

Some professional categories, such as researchers, sportsmen, senior management and highly qualified staff can benefit from certain facilities when pursuing their residence

permits in Spain. In any event, entry into the country requires the appropriate visa, while processing any variation in the residence permit requires going to the immigration offices of the Ministry of the Interior.

Beyond regulating the conditions of entry and residence, the Immigration Law also sets out the rights and freedoms enjoyed by foreign citizens as well as any steps intended to ensure their social integration. Specifically, the Law recognizes that foreign citizens enjoy the right of association and assembly as well as free access to education, social security and health services, under the same conditions as Spanish citizens. In addition, residents can vote in local elections held in the municipality where they are registered, can have access to posts in government service and have the right to family reunification, under the conditions set by the legislation.

4

Creating and Setting Up a Business

Any investor wishing to start a business in Spain must complete a formation process before beginning operations. This process is divided into two main stages. The first is the choice of the legal form it will take. Although many forms exist, the main choices involve either setting up a company in Spain, under various forms provided by the law, or by setting up a branch of a foreign parent company. After choosing the most appropriate legal form for the activity to be performed, the next stage involves the investor fulfilling a number of procedures and requirements, which are not particularly difficult but require appropriate professional advice.

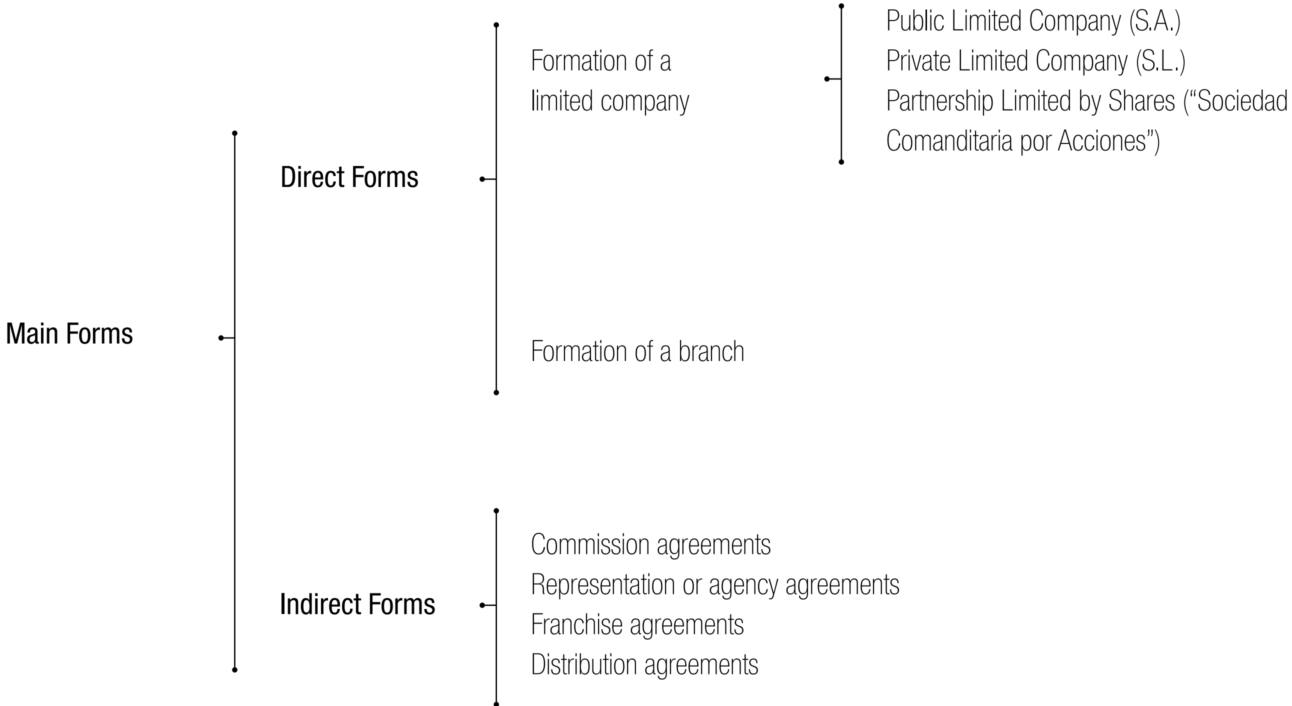
Beyond the most common legal forms, there are other ways that may be useful to investors wishing to operate in Spain, such as the possibility of partnering with Spanish

businessmen through one of the forms established for such purpose: Economic Interest Grouping (EIG), for the Spanish domestic market or European Economic Interest Grouping (EEIG), at EU level; UTE (temporary association of companies), for providing certain services or work; joint-purse agreements, good for entrepreneurs and business angels; and joint ventures through public or private limited companies.

This chapter includes a full description of the direct forms to enable the formation of a business in Spain and a list of legal, accounting and auditing requirements that must be met to complete the whole process. Additionally, apart from the limited companies described here, it should be noted that there are other forms based on partnerships. However, in practice, such associations are rarely used, mainly due to the problems arising from their unique characteristics. Most notably, such characteristics include the unlimited personal liability of each partner and the inability to transfer equity to third parties without the consent of all involved. As an example of a general partnership, the *Sociedad Regular Colectiva* may be cited.

4.1. Limited Company as a Model for Formation

Spanish legislation has introduced in recent years major reforms in commercial matters, with the primary aim of adapting existing regulations to European Community regulations. This reform process culminated with the entry into force of Royal Decree Law 1/2010, which recasts in a single text the legislation on limited companies. Until the adoption of the new text, *Sociedades Anónimas* and *Sociedades de Responsabilidad Limitada* (the most common forms of limited companies) were governed by two separate laws, resulting in


Main Forms
Direct Forms
Formation of a limited company
Public Limited Company (S.A.)
Private Limited Company (S.L.)
Partnership Limited by Shares ("Sociedad Comanditaria por Acciones")
Formation of a branch
Indirect Forms
Commission agreements
Representation or agency agreements
Franchise agreements
Distribution agreements

the existence of certain inconsistencies and loopholes that the new text has resolved.

Until recently, a public limited company (S.A.) was the most common legal form when it came to choosing a limited company to finance far-reaching investment projects. However, in recent years, economic operators have preferred to make use of the private limited company (S.L.) when choosing a legal form. It was unquestionably the smaller amount of share capital required to start up an S.L., combined with greater simplicity in its management, which reversed the traditional trend.

4.1.1. Public Limited Company ("*Sociedad Anónima*", "S.A.")

The capital of an S.A. is divided into shares. A share confers on its holder the status of shareholder and a set of rights, among which are the following: the right to vote and to information, the preferential subscription of shares, participation in the distribution of company profits and to challenge company resolutions. The company's shares can be in registered or bearer form, but restrictions on their free transfer are only allowed for the former. Shares must also be in registered form while not fully paid up. In addition, the issue of shares without voting rights is also allowed; such shares do however have the right to receive the annual minimum dividends, whether fixed or variable, as established by the company's Articles of Association.

The formation of an S.A. requires a single shareholder and a minimum share capital of 60,000 euros. It is necessary to execute a notarial instrument before a civil-law notary, which has then to be recorded in the Commercial Register in order

to have legal personality. The capital must be fully subscribed and paid up to at least a quarter of the nominal value of each share. The remaining capital must be paid within the period set by the articles of association. However, in the event that the payment is made by non-monetary contribution, the deadline may never exceed five years.

In any event, the liability of the shareholders is limited to the nominal value of shares subscribed. There is, however, an exception to this rule: in an S.A. which has a single shareholder, and where such a circumstance has not been declared in the established legal terms, that sole shareholder has unlimited liability for company debts incurred for that period.

An S.A. is governed by the *junta general de accionistas* (shareholders' general meeting) and the directors. The main functions of the governing bodies are as follows:

- The **general meeting** is where the ultimate decisions are made within an S.A. It can be convened by the directors whenever they deem it necessary. They are also obliged to do so if requested by a group of shareholders holding at least 5% of the share capital. It is also imperative to call a general meeting within the first six months of the financial year to review company management, approve the financial statements for the previous year and decide upon the distribution of profits. During a general meeting, any resolutions are adopted by majority vote.
- The **directors** represent the company and there may be one or more of them. In the latter case, if acting jointly and their number exceeds two, they will form what is known as the *consejo de administración* (Board of Directors). The directors may be held responsible whenever not acting with due diligence and loyalty.

Beyond the standard form, it is essential to mention in this section the so-called *European limited company 'Societas Europaea'*. This is a supranational form of company to be added to the list of those already recognized in the respective legal systems of EU countries. The main purpose of the legal framework of the European limited company is to extend freedom of establishment in the territory of the European Union. This allows companies to operate within the scope of the EU under the same rules of European law directly applicable in all member states. Therefore, countries are required to adopt any provisions needed to ensure direct application of European Community rules.

The European limited company model is geared initially towards large investments, since the minimum capital required amounts to 120,000 euros. However, its very definition does not prevent medium or even modest-sized initiatives from taking this legal form. The fact is that, ultimately, the real purpose of the European limited company is to enable companies in different EU countries to form a holding company, merge or create a joint subsidiary without running into the legal obligations and practices arising from different legal systems. Furthermore, it brings significant added value: organizing worker involvement in a European company, recognizing their role and activities within the company.

4.1.2. Private Limited Company ("*Sociedad de Responsabilidad Limitada*", "S.L.")

This legal form is, without doubt, the best way to set up a small or medium-sized business. Firstly, the minimum share capital is only 3,000 euros, which must be fully subscribed and paid-up at the time of its formation, and to which amount, it should

also be noted, there is no maximum limit. Secondly, only one shareholder is needed for its formation, again without their number being limited.

Within this form, a special kind of company must be mentioned. It concerns the *Sociedad Limitada Nueva Empresa* (New Enterprise Limited Company or SLNE), especially designed to encourage the creation of small and medium-sized enterprises in more advantageous conditions. Specifically, forming this type of S.L. involves simplified and more flexible procedures, governing bodies and accounting, and the option is available for its formation electronically or telematically. As is the case with a traditional limited company, the share capital cannot be less than 3,000 euros. However, unlike it, there is an upper limit, which is 120,000 euros. Furthermore, there can be no more than five shareholders at the time of formation, and only natural persons can be shareholders.

4.1.3. Partnership Limited by Shares ("*Sociedad Comanditaria por Acciones*")

This legal form is rarely used in practice, but as it is recognized in current legislation, a brief mention of its characteristics should be made. In short, it could be said that it is a form which combines aspects of partnerships and limited companies. It is, in essence, a derivative form of company in which ownership is divided into partners who have personal unlimited liability and shareholders whose liability is limited to their interest in the company.

It is precisely this hybrid structure which makes it a *rara avis* among the legal forms, and why most investors decide to opt for a public or private limited company.

4.2. Formation of a Branch

Foreign investors wanting to conduct their business directly are not required to form a company based in Spain. Current regulations provide for the ability of non-resident entities to conduct all their transactions through a branch, which is subject to the legislation in the country of origin concerning relations with third parties. A branch is always dependent on the head offices based abroad, and has no legal personality.

Nevertheless, the setting up of the branch requires a public document to be executed before a civil-law notary and its subsequent entry in the Commercial Register. Such a document must specify the purpose of setting up the branch in Spain, which will then determine the scope of its operations. Naturally, the branch must have a permanent address and a fiscal representative resident in Spain. Requirements include the submission of an annual report on the development of the investment to the Directorate General for Trade and Investment. Generally speaking, it can be said that the set of procedures, formalities, requirements and accounting is very similar to those needed to set up a subsidiary.

Branches are subject to the same tax as a Spanish company. This equal footing in taxation also carries over to rights and obligations, which, except for some slight differences, are also very similar. Those minor differences arise from the absence of legal personality and of their dependence on a company based abroad.

For instance, the parent company can allocate certain expenses incurred in connection with the branch, such as anything related to management costs and general administrative costs, which is an amount that can be deducted from the income of the branch. Furthermore, it should be taken into account that there is a tax on non-resident companies

with a permanent establishment: *Branch Profit Tax*, which is levied on the income earned by the branch to be transferred abroad at an additional rate of 19%.

This tax is not applicable, by virtue of the non-discrimination clause founded by the OECD Model Convention, to countries with which Spain has signed treaties to prevent double taxation on income and wealth, on condition of reciprocity, unless the treaty expressly provides for the possibility of its introduction in Spain, as is the case for the treaty with the United States. Nor does it apply to entities resident in another EU member state, unless that country or territory is considered a tax haven.

4.3. Procedure for the Formation of a Company

Below is a complete list of the steps that must be completed by a foreign investor wanting to create and set up a company in Spain.

- Certificate issued by the Central Mercantile Register stating that there is no other company with a name identical to the one intended to be used. Once obtained, it is valid for two months.
- In cases where required by law (see Chapter 2), prior notification of the investment to the Directorate General for Trade and Investment.
- An affidavit, in the presence of a notary, by the founding members of the new company regarding its beneficial owner.
- Execution of a notarized copy of the memorandum of association.
- In those foreign investments not subject to prior declaration, notification is to be given to the General

Directorate for Trade and Investment within one month of execution of the notarized memorandum of association.

- Registration with the appropriate tax office to obtain the Tax Identification Number (NIF). In the case of a company with non-resident shareholders or representatives, non-resident natural persons must obtain a Foreigner Identification Number (NIE) and non-resident legal persons must obtain the Tax Identification Number (NIF).
- In the cases provided by law, Declaration of Exemption from transfer tax and stamp duty, in its “company transaction” form.
- Registration in the Commercial Register of the province where the entity has its registered office.
- Payment of any municipal taxes that may apply, such as Business Activity Tax (IAE).
- Implementation of all employment formalities, from recruitment to Social Security registration.

None of these steps is particularly complex, however the process of setting up a company usually requires proper professional advice.

4.4. Statutory Books

Companies must keep the following books:

- **Minutes Book.** Containing the minutes of the general meetings as well as of the Board of Directors if the latter is formed.
- **Shareholder Register.** Required for private limited companies. It must include detailed information on

the original ownership and successive transfers of shares, as well as the establishment of any real rights and encumbrances on them. Companies that fall into the category of New Enterprise Limited Company (SLNE) are not obliged to keep this book.

- **Share Register.** Required for public limited companies, it would be the equivalent of the Shareholder Register of private limited companies. It contains the owners of registered shares and any changes arising in their ownership.
- **Book of contracts entered into by the sole shareholder.** Here, any contracts between the sole shareholder and the sole proprietorship are reproduced. Details recorded are then included in the notes to the financial statements.

Statutory books must be certified at the appropriate Commercial Registry.

4.5. Commercial Register

All companies must be registered with a public registry known as the *Registro Mercantil*. Registration is optional for the individual entrepreneur, with the exception of ship owners.

The Commercial Registry is also responsible for certifying the books of companies and individual entrepreneurs, the deposit and publication of accounting documents and the centralization and publication of information of bankruptcy resolutions.

The Commercial Registry is public. The records it keeps can be made available in various ways:

- A certificate issued by the Registrar.
- An informative note.
- Copies of entries made or documents deposited.

The issue of a certificate is the only irrefutable way of proving the contents of documents entered into the Commercial Register. Companies and individual entrepreneurs are required to state their registration details on their invoices and letters, etc.

4.6. Accounting Requirements for All Companies

The process of convergence between Spanish legislation and that of EU countries has also led to changes in the accounting procedures that companies must follow. In this regard, Spanish legislation on the subject has undergone a long reform process in order to incorporate the body of International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS). On 1 January 2005 it became compulsory to apply those standards in the preparation of the financial statements of certain business groups; in particular, those with any company that has issued listed securities in any country of the European Union. Other companies can also apply these rules on a voluntary basis.

The process of convergence of legislation culminated in 2007 with the adoption of a new National Chart of Accounts, which implements the rules set out in company law, and which is based on the new measurement principles of international standards. Ultimately, Spanish accounting regulations are modelled after Directive 2013/34 of 26 June, which modernizes European law on the subject and puts it in line with the global model on accounting principles (the IAS mentioned above). The broad lines of those International Accounting Standards

are set by the IASB, the International Accounting Standards Board, based in London.

Today, Spanish legislation requires all business owners, individuals as well as companies, to keep appropriate accounting records, which allow all their transactions to be chronologically tracked, and to regularly produce stock accounts and balance sheets. Such a requirement means that all companies must necessarily keep one book of Inventories and Annual Accounts, plus another Journal. Those accounting books must be certified telematically in the Commercial Registry, after duly being filed electronically, within four months from the end of the financial year. Those same accounting books, along with the supporting documents for verification, are to be kept for a period of six years from the date of the last entry recorded.

In addition, the directors of the company are required to draw up, within a maximum period of three months from the end of the financial year, the financial statements, the management report and the proposed appropriation of earnings. The financial statements include the balance sheet, income statement, statement of changes in equity, cash flow statement and the annual report.

The financial statements, together with the management report, must be filed with the Commercial Registry within the month following their approval at the General Meeting.

It is imperative that all company accounting and, in particular, the recognition and measurement of items in the financial statements, is to be carried out by applying the accounting principles of accrual, consistency, prudence, no offsetting, materiality and going concern.

Finally, it should be noted that the National Chart of Accounts in force in Spain is mandatory for all companies, whatever their legal form, both individual and corporate.

4.7. Audit Requirements for Annual Accounts

The auditing of accounts consists essentially of checking and verifying the annual accounts, as well as any other financial statements or accounting documents, drawn up in accordance with the applicable regulatory framework for financial reporting, whenever such activity is aimed at issuing a report on the reliability of those documents which may have implications for third parties.

The auditing of accounts must necessarily be completed by an external auditor or audit firm by issuing the appropriate report and being subject to the requirements and formalities established in the *Ley de Auditoría de Cuentas* (Law on Auditing).

External auditors and audit firms are to be engaged for a specified period of time initially, which shall not be less than three years or more than nine, from the date on which the first year to be audited begins, and can be engaged for successive periods of up to three years once the initial period has ended.

Auditors are liable for damages arising from breach of their duties to the companies or entities audited and also to third parties.

Auditors must maintain the confidentiality of any information made known to them in the exercise of their activity, and may not use it for any purpose other than for the actual audit.

Without prejudice to the above, the documents relating to any audits may be accessed, under the obligation of confidentiality of information, by:

a) The *Instituto de Contabilidad y Auditoría de Cuentas* (Institute of Accounting and Auditing), either in the exercise of its supervisory role or for the purpose of international cooperation.
b) Persons appointed by a judge.
c) Those persons authorised by law.
d) The Bank of Spain, the National Securities Market Commission (CNMV), the General Directorate of Insurance and Pensions (DGFSP) and the Autonomous Community bodies with powers for monitoring insurance companies. Similarly, any competent bodies for monitoring the financial and economic management of the public sector.
e) Corporations representing auditors for the sole purpose of monitoring the internal performance practices and procedures of their members.
f) External auditors and audit firms for the auditing of consolidated accounts, as well as in the event of replacing the external auditor or audit firm of the entity.
g) The competent authorities of the Member States of the European Union and other countries within the framework established by law.

The Institute of Accounting and Auditing is responsible for the monitoring and discipline of the exercise of external audit activities; the Official Register of Auditors ("*Registro Oficial de Auditores de Cuentas*") is also under its control.

Companies or entities meeting any of the following conditions must always undergo an external audit regardless of their legal status:

a) Those that issue shares admitted to trading on official secondary securities markets or multilateral trading systems.
b) Those that issue debentures or loan stock to the public.
c) Those acting on a regular basis as financial intermediaries.
d) Those whose business purpose is any activity related to private insurance, as well as pension funds and their management companies.
e) Those receiving subsidies or aid, or perform work or services, or supply goods to the State and other public bodies within the limits set by government regulation.

In addition, the financial statements and company management report must be reviewed by the auditors. Companies are exempted from this requirement whenever, for two years after the financial year end date, at least two of the following conditions are fulfilled:

1. Total assets not exceeding 2,850,000 euros.
2. Annual net turnover less than 5,700,000 euros.
3. Average number of workers employed during the financial year not exceeding 50.

Auditors have a period of at least one month to issue their report from the date on which the signed accounts are supplied to them by the company directors.

The important role of auditors in financial and legal transactions such as mergers, group demergers, issuing shares,

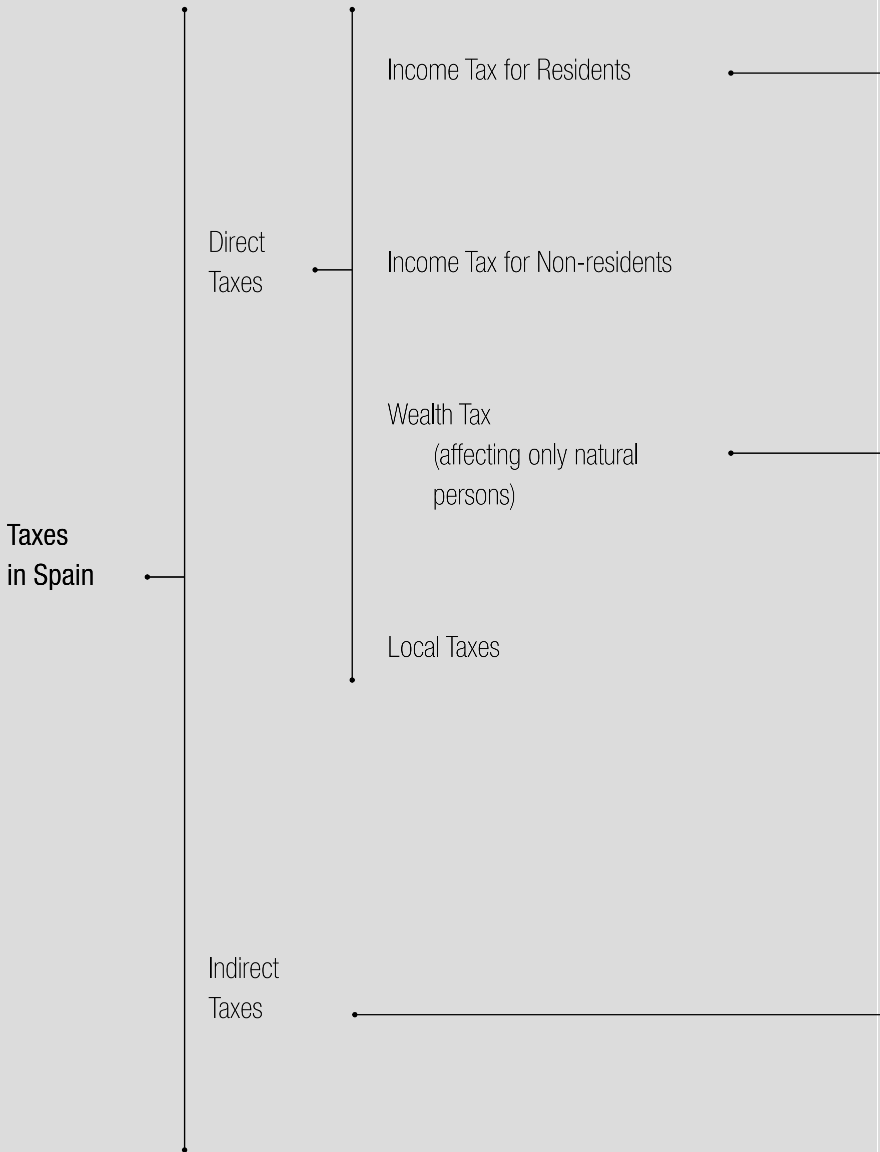
capital increase by offsetting credit, capital reductions to offset losses or equity valuation is clearly outlined in the regulations governing external audits.

Law 22/2015 of 20 July on Auditing, following the provisions of EU Regulation No. 537/2014, imposes more restrictive criteria on audits of public-interest entities, including the mandatory rotation of auditors after a 10-year engagement, with the option of further extending that period for up to four years if engaged in the form of joint audit.

Fees for providing non-audit services are also limited to an amount not exceeding 70% of the fees paid for the external audit.

5

Taxation



General structure of the taxes that may be levied on foreign investment in Spain.

Company Tax
Personal Income Tax

Net Wealth Tax
Inheritance and Gift Tax

Value Added Tax (IVA)
Transfer Tax and Stamp Duty
Foreign Trade Tax – Customs duties on imports
Excise duties on specific goods
(fuels, alcohol, tobacco, etc.)

Of all the obligations associated with developing a business, few worry investors more than those concerning taxation. Whether it is because of the complexity and multiplicity of taxes that there are or because of the risk of committing errors in managing them, it is essential to know how the tax system works and get proper advice. That recommendation is crucial in the case of foreign investors, who are unfamiliar with the peculiarities of the Spanish system.

The highest tax authority in Spain is the *Agencia Estatal de la Administración Tributaria* (AEAT), ultimately subject to the Ministry of Finance. The task of the AEAT is to collect and manage taxes which are due to the State, including the duty to provide citizens with all the information and advice necessary to meet their tax obligations. All actions of the AEAT

are derived from the current law on fiscal matters, a body of regulations built up from various sources, from the Spanish Constitution to the regulations implementing tax laws.

The last section contains a part specifically concerning taxes at municipal level, since they ultimately affect a large number of companies, but here it is worth mentioning that the autonomous communities have developed taxes which are levied on certain sectors, such as industries emitting gases into the atmosphere or department stores, in addition to having the power to determine the taxable base of inheritance and gift tax.

The first section below on current taxes in Spain concerns Company Tax, the most important tax companies have to confront, and is regulated by Law 27/2014 of 27 November. It is a direct and proportional tax, which must be paid in each financial year. It is important to remember that the Basque Country and Navarre, in accordance with their financial arrangement, manage and collect a large majority of taxes from their own legislation, outside the AEAT. This particularity means, for example, that those two autonomous communities have their own Company Tax.

5.1. Company Tax

5.1.1. Tax Basics

Company Tax applies throughout the whole of Spain without prejudice to special regimes for reasons of territory and international treaties and conventions. The taxable event is the obtaining of income, regardless of its origin, and the taxpayers are all those entities resident in Spain.

Entities that fulfil any of the following conditions are considered to be resident in Spain:

a) Those which have been formed under Spanish law.
b) Those which have their registered office in Spanish territory.
c) Those whose head office is located in Spain.

It is important to note that Spanish tax authorities have a very inclusive attitude towards what is considered a resident entity. Thus, companies located in tax havens or nil tax territories will also be resident entities whenever their main assets consist of property situated, or rights which are fulfilled and exercised, in Spanish territory. Similarly, companies will be considered resident entities when their principal business activity is conducted on Spanish territory. Along the same lines, resident entities are taxed on the total income they earn, regardless of where it took place and the taxpayer's residence.

In order to prevent companies from deferring the payment of Company Tax in Spain through the instrumental use of non-resident companies taxed at a low rate abroad, resident entities must include in their tax base certain income earned by a non-resident entity, in which they have a holding equal to or higher than 50%, whenever the circumstances expressly provided for under legislation arise. The intention is to tax foreign investment made for tax reasons rather than business purposes through "controlled foreign corporation" rules.

When calculating the tax, it must be assumed that the tax base is the amount of income earned during the period of taxation, which coincides with the financial year of the company. That amount is reduced by offsetting tax losses from prior years. Similarly, and where appropriate, the tax base will consist of the accounting profit adjusted by the application of tax rules.

In the end, the tax is calculated by applying the following rates to the tax base:

Year	General	SMEs*
2015	28%	25%-28%
2016	25%	25%

Should the tax base be negative, its amount may be offset without any time limit from 1 January 2016. However, a quantitative limit of 70% of the tax base prior to such offset can be expected. As a transitional step for the year 2016, the limit is 60%.

In any case, an amount up to 1 million euros can be offset in the period.

For newly-created entities, the above limit will not apply in the first 3 tax periods in which a positive tax base is produced.

The regulations governing Company Tax contain safeguards aimed at preventing the use of tax losses in the case of acquisitions of inactive or quasi-inactive companies.

5.1.2. Timing of Recognition of Income and Expenses

Income and expenses shall be allocated to the tax period in which their accrual occurs, under accounting rules, irrespective of the date of their payment or collection, respecting the proper correlation between them.

(*) For this purpose, in the year 2015, SMEs are considered as small-sized companies which have at least one employee with a full-time work contract and whose annual net turnover is less than 10 million euros. Such companies may apply a rate of 25% to the portion of taxable income between 0 and 300,000 euros; the general rate of 28% will apply for the remainder. Furthermore, small-sized companies have other tax advantages.

The tax efficiency of the timing of recognition of income and expenses, other than as set out in the preceding paragraph, used exceptionally by the taxpayer in order to show the true and fair view of the equity, financial position and earnings in accordance with the provisions of commercial law, shall be subject to approval by the tax authorities.

5.1.3. Measurement of Income and Expenses

Income and expenses are calculated by their book values, provided that the accounts reflect the true financial position of the company. However, in the case of transactions between related persons or entities, there are certain precautions: thus, such transactions must be measured at their fair market value. The tax administration has power to check that transactions between related persons or entities have been measured at their fair market value, and to make any appropriate measurement adjustments, taking into account all the persons or entities that were party to the transaction so as to avoid taxing revenue higher than each party actually derived from the transaction. Measurement of the transaction must have adequate supporting documentation.

Additionally, deduction of expenses for services between related entities is conditional upon the services producing a benefit or advantage to the recipient. As regards the deduction of expenses arising from a cost-sharing agreement signed between related parties, participants will need to acquire ownership or other similar rights on the subject of the agreement, and the allocation of costs must be based on the anticipated benefits or advantages for each of them.

It is possible to submit to the tax authorities a proposal for measuring transactions made between related entities before they take place.

Interest deduction is limited in certain cases.

The net value of an asset for accounts purposes is deemed to be its cost of acquisition less accumulated depreciation and possible impairments.

5.1.4. Calculating Depreciation

Depreciation represents the irreversible loss in value undergone by non-current assets or fixed assets, consisting of tangible assets, intangible assets and investment property. For depreciation to be deducted, two basic requirements must be met: it is to be effective and recorded. On the first point, effective depreciation will always require proof from the taxpayer. To overcome this difficulty, depreciation is deemed proven when the provision is made according to any of the methods described in this section.

First would be the **straight-line method of depreciation according to the official table**. The text of the law governing the tax includes a table for depreciation setting out the maximum rates and periods of time. Whatever the case, the taxpayer can operate within these limits. There is also a minimum rate necessary to cover the value of the item to be depreciated over the maximum period set out in the tables. It will become clearer in the following example:

	MAXIMUM RATE	MINIMUM RATE	MAXIMUM PERIOD
Industrial buildings	3	1,47	68
Commercial buildings	2	1,00	100
Office furniture	10	5,00	20

Beyond the above, rates sustain an increase in cases in which production items are used in more than one work shift, or when they are purchased as used items.

The second accepted method for proving calculations is **declining balance depreciation**. However, not all assets can benefit from this system of depreciation; specifically, buildings, furniture and fixtures are excluded. There are two ways to perform calculations using this method: either with a fixed percentage of the net book value, or with the sum-of-digits method.

Thirdly, there are a number of assets eligible for **unrestricted depreciation**. Among those assets which can be freely depreciated are the following:

- Research and development (R&D) expenditure that has been recorded as intangible assets.
- Tangible and intangible assets (excluding buildings) used for R&D purposes. Buildings are to be depreciated on a straight-line basis over a period of ten years insofar as they are used for R&D purposes.

- New fixed asset items, whose unit value does not exceed 300 euros, with a limit of up to 25,000 euros per tax period.

5.1.5. Impairment of Assets and Provisions

As set out in the first section on the basic rules for the tax, the tax base is calculated from earnings. However, when it comes to costs incurred by impairment losses and provisions, company tax legislation does not fully embrace the accounting principles. This anomaly is due to three basic reasons: first, because it sets quantitative limits on their deductible value; second, because it also lays down certain qualitative requirements to be met in order to be deductible; and third, because the deduction of impairment or, where appropriate, provisions recorded as expenses is denied.

A first limitation appears in the event that there is any impairment of receivables for insolvent debtors. Losses associated with this concept are only regarded as deductible when, at the time the tax accrues, they fulfil any of the following conditions.

1. A period of six months has elapsed since maturity of the obligation.
2. The debtor is declared bankrupt.
3. The debtor is prosecuted for the crime of concealment of assets.
4. Obligations have been claimed through legal action or are the subject of litigation or arbitration proceedings whose settlement depends on collection.

Unless certain conditions are met, impairment losses of receivables owed by public entities or related parties are also not considered deductible, nor are any corresponding to global risk estimates.

The list of items that are not tax deductible does not end here. The following are also not tax deductible:

a) Impairment losses of tangible assets, investment property and intangible assets, including goodwill, all of which is without prejudice to the appropriate systematic depreciation under the tax law.
b) Impairment losses of securities representing shareholders' equity or ownership equity.
c) Impairment losses of debt securities.

Regarding provisions, company tax regulations provide for the non-deductibility of certain provision expenses, including:

a) Implicit or tacit liabilities
b) Long-term staff payments
c) Onerous contracts
d) Restructuring
e) Customer refunds
f) Staff remuneration with payments based on equity instruments

5.1.6. Reductions in the tax base: Patent Box and capitalization reserve

Transfer of intangible assets

This tax incentive, also known as "Patent Box", is designed to encourage activities in producing technical knowledge with an industrial application within the framework of an innovative

activity, so that the use of such knowledge, by transferring its use a third party, has special tax treatment if the legally established requirements are met.

Such special treatment is based upon integration into the tax base of only 40% of the revenues from licensing the use of certain intangible assets: patents, designs, drawings, plans, secret procedures, industrial experiences, etc. The same special tax treatment applies to the transfer of those intangible assets.

Capitalization reserve

In order to encourage business capitalization, taxpayers can reduce the tax base by 10% of the increase in its own funds, which means, since this reduction is based on taxable income, having obtained profits which are not subject to distribution, as long as the amount of such undistributed profits remains in the company's funds for a period of five years.

5.1.7. Tax Incentives for Small-Sized Enterprises

A special tax regime with incentives exists for small and medium-sized enterprises (SMEs), which are defined as businesses with a net turnover of less than 10 million euros per year, in the preceding tax period.

Incentives, in addition to the reduced tax rate of 25% in 2015 for the first 300,000 euros and 28% on the remaining taxable income mentioned earlier, are:

1. Unrestricted depreciation of new tangible fixed assets and investment property as long as an increase in staff is involved. The amount of investment that can benefit from the unrestricted depreciation regime will be determined by multiplying the figure of 120,000 euros by that increase.

2. Accelerated depreciation, multiplying the maximum straight-line rate set out in the official depreciation table by two.
3. Credit impairment losses due to doubtful debts of up to 1% of the total debtor balances at the balance sheet date.
4. Reduction in the positive tax base of up to 10% of its amount by funding a restricted reserve known as a **levelling reserve**. This is a timing difference since the reduction is reversed as the entity obtains negative taxable income, with a time limit of five years. If negative taxable income is not produced in that period, taxation of the reserve created is deferred for five years. It can be said that we are dealing with a kind of "carry-back" offsetting system of negative taxable income.

5.1.8. Tax Regime for Entities Holding Foreign Securities ("Holding Companies")

Companies whose business purpose includes the activities of management and administration of securities representing the equity of entities not resident in Spain, through the appropriate organization of material and human resources, may qualify for treatment as Entities Holding Foreign Securities.

The shares representing the capital of the holding company must be registered.

The main benefit of this regime is that the profit distributed by the holding company to a non-resident, even if resident in a non-EU member state, is not considered as generated in Spain, provided it is distributed from exempt income, that is to say, dividends from non-resident entities and revenue

arising from the transfer of shares in a non-resident entity meeting the following requirements:

- The percentage shareholding, whether direct or indirect, is at least 5% and has been owned uninterruptedly for at least one year.

  The minimum shareholding requirement is deemed to be met if its acquisition value exceeds 20 million euros.
- The non-resident investee entity has been subject to a tax of an identical or similar nature to Spanish Company Tax at a nominal rate of at least 10%. This requirement is deemed to be met if the investee is resident in a country with which Spain has signed an international treaty to prevent double taxation, which is applicable to it, containing an Exchange-of-Information Clause.

Finally, additional requirements are set for the exemption of income from the transfer of holdings in non-resident entities that are deemed to be "*Entidades Patrimoniales*" (Equity Entities) or non-resident entities receiving passive income (Controlled Foreign Corporation).

To benefit from the regime, no prior request to the Tax Authorities for its application is required; they just need to be notified if opting for it.

5.1.9. Measures to Avoid Double Taxation

These measures seek to prevent the so-called juridical double taxation as well as economic double taxation. Juridical double taxation arises when the income of the same taxpayer is taxed in two different countries. Economic double taxation

occurs when the same income of two different taxpayers is taxed either by two different countries (international double taxation) or by the same country (domestic double taxation).

There are two methods of preventing double taxation: the exemption method and credit method.

a. Exemption Method

1. Dividends and capital gains of resident and non-resident entities.

Exemption on dividends is instituted in order to prevent economic double taxation arising when the appropriate company tax is imposed on the income of one company (the taxpayer company), which is included in its tax base and later distributed as a dividends, and on the company receiving the dividends when included as income in its tax base.

Similarly, when a positive taxable income arises through the transfer of an interest in the capital of another company, the transferring company may apply the appropriate exemption in order to prevent economic double taxation since the capital gain generated will include the undistributed profits arising for the holding period of the interest, which will have already been taxed on the investee company.

Exemption of dividends and capital gains shall apply as long as the legally established requirements are met.

2. Income obtained abroad through a permanent establishment.

Income obtained abroad through a permanent establishment situated outside Spanish territory, as well as positive income derived from its transfer will

be exempt as long as the requirements and conditions under Company Tax regulations are met.

It is important to note that inclusion in the tax base of negative income obtained abroad through a permanent establishment is not permitted, except in the event of its transfer or cessation of activity.

b. Credit Method

1. Tax credit for taxes paid abroad.

Company Tax legislation allows the deduction of the lower of the following amounts:

- Tax of a similar nature paid abroad.
- Tax that would be payable in Spain had income been earned there.

2. Dividends from non-resident entities.

In certain cases, a resident company receiving dividends may deduct the tax already paid by a non-resident company on such dividends. Also considered tax already paid is the tax paid by companies in which a subsidiary has a shareholding and, in turn, by any in which those have a direct shareholding and so on, insofar as it is attributable to profits out of which dividends are paid. In practice, this tax credit will be applied when it is not possible to apply the "exemption".

This tax credit has a joint limit with the one described in the previous section: the sum of both may not exceed the tax that would be payable if yields had been obtained in Spain.

5.1.10. Deductions to Provide Incentives to Perform Certain Activities

Such deductions include the following:

- Research and development activities, as well as technological innovation, can benefit from a deduction of between 8% and 59%. The final percentage depends on several factors.
- Deduction for Spanish film productions of between 20% and 18%, foreign film productions of 15% and live entertainment of 20%.
- Deduction for the creation of employment for disabled persons: 9,000-12,000 euros per person/year for increasing the average number of disabled persons employed.

Deductions described above cannot exceed the limit on the total tax liability, which, depending on the case, ranges from the standard 25% to a maximum of 50%.

Successive annual Government Budgets may introduce other tax incentives on investment.

5.1.11. Withholding Tax and Instalment Payments

On certain income earned, payers of company tax are required to withhold tax as a payment on account. The withholding percentage is, in general, 19%, although it may vary depending on the type of income. In addition, within the first twenty days of April, October and December, companies must make a payment by instalment to the settlement account for the fiscal year in progress on the first day of each of the months indicated. That instalment payment will be 18% of the tax payable for last financial year where the deadline for filing a

return was on those dates, less any applicable deductions and credits and the appropriate withholdings.

Alternatively, there is the option to make payments on account for the part of the tax base corresponding to the first three, nine or eleven-month period of each calendar year. This method is compulsory for entities with a turnover in excess of 6,010,121.04 euros during the twelve months preceding the date on which the tax period begins. The percentage is the result of multiplying the tax rate by 5/7, rounded down; that is, for a tax rate of 28%, 20% will apply. This percentage of payment on account will increase depending on the turnover, reaching 27% if exceeding 60 million euros.

Any withholdings and instalment payments already made can be deducted when declaring Company Tax for the relevant year. If they exceed the final tax payable, the entity has the right to claim back what it overpaid during the tax period.

5.1.12. Consolidated Tax Return

When a company exercises control over one or more other resident companies, the group may be treated as a whole for Company Tax purposes, after notifying the tax uthorities, as long as the parent company directly or indirectly owns, for the period required by law, at least 75% of the capital and the majority of the voting rights of the subsidiary company or companies.

5.2. Personal Income Tax

Undoubtedly, income tax is the most important tax to be managed by the Tax Authorities both in terms of the number of taxpayers and the total amount collected. The time period in

which all the information on the tax needs to be filed begins in April and ends in June. All applicable regulations concerning this tax are contained in Law 35/2006 on Personal Income Tax and the regulations approved by Royal Decree 439/2007.

This tax, known by the acronym IRPF, applies throughout Spain without prejudice to any special regimes regarding territory or any international treaties and conventions. Taxpayers of this tax are individuals habitually resident in Spain, and the taxable event is the obtaining of income.

5.2.1. Basics: Habitual Residence and Income Subject to Taxation

First, it should be pointed out what is meant by habitual residence. It refers to staying in Spanish territory for more than 183 days in the calendar year. To determine the length of stay, sporadic absences will be counted unless tax residency in another country can be proved. At the same time, taxpayers are regarded as having habitual residence in Spain when the main centre or base of their economic activities or interests is situated there.

Additionally, unless proven otherwise, habitual residence is presumed when the spouse and minor children of the taxpayer habitually reside in Spain. Individuals of Spanish nationality who transfer their tax residence to a tax haven do not lose their status as taxpayers. This rule applies to the year in which the change of residence takes place and to the following four periods.

Taxpayers are taxed on all income they earn regardless of where it occurred and irrespective of the payer's residence. Personal income tax is levied on economic capacity of taxpayers and the law sets a personal and family minimum,

which must be taken into account when calculating the gross tax liability. Households may opt to be taxed either jointly or each of its members separately.

As with Company Tax, taxpayers must include in their tax base certain income earned by non-resident entities whenever they have a holding of at least 50% and when the circumstances set by the regulations are met. It should be taken into account that there is a special regime on capital gains for change of residence known as *Exit Tax*, which applies in most countries of the European Union.

5.2.2. Special Regime for Relocated Workers

Anybody who, for reasons of work, becomes tax resident in Spain can pay Non-Resident Income Tax, the characteristics of which are described in full detail in section 5.3 of this chapter. Relocated workers may benefit from this special regime for the tax period in which the change of residence takes place and for the next five periods.

In order to be taxed under this special regime, relocated employees will have to fulfil two conditions. First, having not been residents in Spain for the ten tax periods prior to their relocation and, second, that such relocation is the result of an employment contract or becoming directors of a company in which they have no shares, or else when the shareholding in that company does not result in it being regarded as a related entity. A taxpayer opting to make use of this special regime will be subject as a non-resident to Wealth Tax.

Under this special regime, all income from work shall be construed as earned in Spanish territory and, in the years 2015 and 2016, will be taxed at the rates set out in the following scale.

Taxable Income	Rate applicable	
	2015	2016
Up to 600,000 euros	24%	24%
From 600,000 euros	47%	45%

5.2.3. Tax Relief

As with Company Tax, Personal Income Tax legislation includes the possibility of applying a number of deductions under certain circumstances. The relief described below will be of particular interest to foreign investors:

1. **Deduction for investment in newly or recently formed companies.** 20% deduction for amounts paid during the fiscal year for the subscription of shares in newly or recently formed companies. The maximum deduction base is 50,000 euros per year.
2. **Deductions for economic activities.** Taxpayers engaged in economic activities may benefit from the business investment incentives under Company Tax regulations.
3. **Deductions for donations.** Donations made to certain entities are eligible for the corresponding deduction in income tax.
4. **Deduction for income obtained in Ceuta and Melilla.** Such income is entitled to a 50% deduction in the tax payable on that portion.

5. **Investments in heritage.** Any actions related to Spanish or World Heritage are eligible for a deduction of 15%.
6. **Deduction for international double taxation.** For income including earnings or capital gains obtained and taxed abroad, the smaller of these two amounts will be deducted: either the amount paid abroad for a tax of identical or similar nature to the IRPF or Non-Resident Income Tax, or the result of applying the average effective rate to the taxable income taxed abroad.

Nevertheless, when calculating the deductions for donations and investments in heritage described in paragraphs 3 and 5, it should be taken into account that there is a limitation. The basis for calculating such deductions may not in any case exceed 10% of taxable income for either of them.

5.2.4. Applicable Rates of Income Tax

Personal Income Tax covers two kinds of income: general and savings. Savings income comprises, among other things, dividends, interest (except where obtained from related persons or entities) and capital gains irrespective of the period when such gains were made.

The rates applicable to those two income groups are described in the two following tables. The first includes the general tax scale, while the second sets out the scale for savings income; both are valid for the year 2016.

Rates applicable to general income			
Taxable income Up to euros	Gross tax payable Euros	Remaining taxable income Up to euros	Rate applicable in 2016
-	-	12.450,00	19%
12.450,00	2.365,50	7.750,00	24%
20.200,00	4.225,50	15.000,00	30%
35.200,00	8.725,50	24.800,00	37%
60.000,00	17.901,50	Onwards	45%

Rates applicable to savings income	
Tax Base Euros	Rate applicable in 2016
Up to 6.000	19%
6.000 - 50.000	21%
From 50.000 onwards	23%

5.2.5. Withholding Tax Rates

Entrepreneurs and professionals paying out income in the performance of their activity, legal entities and persons and non-residents operating in Spain through a permanent establishment, are required to withhold and pay to the Treasury, as payment on account, the following amounts relating to the fiscal year when paying earned income, investment income or income for professional activities:

- Earned income: the percentage will be determined on a basis of the amount and various circumstances.
- Income from teaching courses or giving conferences: 15%.
- Investment income such as dividends or interest: 19%.
- Income for professional activities: 15%, except in the first year of beginning the activity and in the two following years, when 7% applies.
- Remuneration to members of management bodies: 35% generally.
- Prizes awarded as a result of participation in games and competitions: 19%.
- Income from the letting of property: 19%.
- Income from intellectual or industrial property, technical assistance or lease of goods: 19%.

When any of the above income is not paid in cash but in kind, there will still be an obligation to make a payment on account. With regard to non-residents operating without a permanent establishment, they must essentially withhold tax on any earned income they may have to pay in the course of their business.

5.3. Non-Resident Income Tax

Non-resident Income Tax is payable on income obtained in Spain by individuals and entities which are not resident in Spain. The tax distinguishes between:

5.3.1. Income Obtained through a Permanent Establishment

The concept of *permanent establishment* refers to the existence in Spain of a fixed place, such as a branch, where the economic activity providing income to the non-resident person or entity is performed. The tax base for that income obtained through a permanent establishment is determined according to general Company Tax rules. In point of fact, the tax base is commonly taxed at the standard Company Tax rate. However, there are two major particularities highlighting the uniqueness of Non-Resident Income Tax regarding companies:

1. The first is that any payments made by the permanent establishment to the head office, or any of its permanent establishments, by way of royalties, interest, commissions, technical assistance or by the use and transfer of property or rights, are non-deductible.
2. The second point to note is that any management costs and general administrative expenses belonging to the permanent establishment are deductible as long as they meet the requirements of reasonableness and continuity in their allocation and are shown in the financial statements and in the accompanying annual report.

Permanent establishments are subject to the same formal registry and accounting obligations as entities resident in

Spain. Among the most notable aspects of using a permanent establishment is the ability to transfer profits abroad. However, as already it mentioned in the second paragraph of the fourth chapter "Formation of a Branch", transferred income is subject to the additional rate of 19%.

Irrespective of the above, legislation provides for two cases in which transferred income is exempt from being taxed at that 19%. The first possibility is upon there being a double taxation treaty, in which it is not expressly stated otherwise, as long as treatment is reciprocal. The second would be that the taxpayer is resident in a member state of the European Union.

It is worth noting that, in the case of tax liabilities of permanent establishments of non-resident taxpayers, the persons designated as their representatives are jointly and severally liable for them (see 5.3.4 below on tax representatives).

Special rules are used to compute the taxable income of permanent establishments in the following cases:

a) Establishments with sporadic activity: construction, installation or assembly of longer duration than 6 months, seasonal business or natural resource exploration.

The rules for income earned in Spain without permanent establishment apply, relieving them of accounting and registration requirements but, however, they must retain proof of any income obtained and tax paid as well as, where appropriate, any withholdings and payments on account made.

Such establishments may opt to be taxed under the general regime described for income obtained through a permanent establishment at the general Company Tax rate. This will only be possible if the

establishment keeps separate accounting records for income obtained in Spain.

b) Establishments with an incomplete business cycle: These include establishments that have work premises in Spain but where any goods produced or services performed in them are intended for their own use. Consequently, they do not receive income but simply reimbursement of costs incurred. In such cases, the tax base can be arrived at by applying the percentage determined by the Ministry of Finance, currently 15%, to the costs incurred for the year, and any non-core revenue, such as interest or royalties as well as capital gains or losses, is to be added to the result. The standard Company Tax rate is applied to a tax base so determined, without any tax deductions or credits under the general regime being applicable.

5.3.2. Income Obtained without a Permanent Establishment

In this case, the tax is levied on any income directly obtained in Spanish territory by the non-resident taxpayer. The tax base is calculated, therefore, from the gross income of the non-resident. Here, it is not possible to deduct expenses except in cases of provision of services, technical assistance and installation or assembly work. At the same time, it is possible to deduct expenses, as a general rule, for financial operations carried out in Spain, where staff costs and the cost of materials and supplies are deducted.

When the taxpayer is resident in another member state of the European Union, the costs under the regulations governing Personal Income Tax and Company Tax may be

deducted in determining the tax base. The only requirement for the reduction is to be able to prove that the costs are directly related to income received in Spain and have a direct financial link with the activity carried out in Spanish territory.

In the case of capital gains, the tax base is determined, in general, by the difference between the transfer value of the item in question and its acquisition value. It should be noted that each source of income or capital gain is taxed separately.

Having set out how to calculate the tax base for this type of tax, it is time to include a list of tax rates that apply to the various concepts. They can be summarized as follows:

- A general rate of 24% is set. However, the tax rate will be 19% in the case of taxpayers resident in another member state of the European Union or the European Economic Area with which there is an effective exchange of tax information.
- In the case of dividends, interest and capital gains, the rate for 2016 will be 19%.
- For income from work under a fixed-term contract for seasonal foreign workers, it will be 2%.
- On employment income earned by non-residents serving in diplomatic missions and consular offices of Spain abroad, the rate will be 8%.
- The rate applicable to pensions is set on a basis of the level of income.
- Reinsurance transactions are taxed at the rate of 1.5%.
- The rate of 4% is applied in the case of sea and air transport businesses resident abroad and whose ships or planes enter Spanish territory.

To finish, any cases involving the transfer of a property situated in Spain by non-resident taxpayers, acting without a

permanent establishment, should be mentioned. In such cases, the person acquiring the property is required to withhold and pay 3% of the agreed price, as payment on account of the tax for non-resident taxpayers. Should the payment of the tax withheld not be made, the transferred property would be subject to the payment of the tax.

In any event, the depository or manager of the assets or rights of non-residents without a permanent establishment, or the payer of the income obtained without a permanent establishment, are severally liable for the payment of tax debts relating to income from the property or rights which they hold or manage or any income they have paid.

5.3.3. Tax Exempt Income

The desire to avoid double taxation of income earned in Spain, combined with the possibility that non-resident taxpayers may come from countries of the European Union, with whom a common economic area is shared, has led to Non-Resident Income Tax bringing in a long list of exemptions. Among others, the following income is exempt from taxation:

a) Income and capital gains derived from movable property, obtained without a permanent establishment in Spain by residents in other member states of the E.U.

This very favourable regime does not apply to capital gains derived from the transfer of company shareholdings in the following cases:

1. The assets of such a company directly or indirectly consist mainly of real estate located in Spanish territory.
2. Individual taxpayers who at some earlier time during the 12 months preceding the transfer, directly or indirectly held at least 25 percent of the share capital.
3. Non-resident entities, where the transfer does not meet the requirements for application of the exemption to avoid double taxation.

b) Income derived from public debt, obtained without a permanent establishment in Spain.

c) Income from non-resident accounts which are also paid to non-resident taxpayers, unless the payment is made to a permanent establishment located in Spain, by the Bank of Spain, any bank or duly registered entities.

d) Income derived from securities issued in Spain by non-residents without a permanent establishment, irrespective of the place of residence of the financial institutions acting as paying agents or involved in the issue or transfer of the securities.

e) Income derived in Spanish territory, without permanent establishment, from the lease, assignment or transfer of containers or ships and planes without crew used in international shipping or aviation.

f) Profits distributed by subsidiaries resident in Spain to their parent companies resident in other countries of the European Union or in the member states of the European Economic Area, as long as the conditions expressly set in current regulations are met.

g) Income derived from the transfer of securities or redemption of units in investment funds made in the official secondary markets in Spain. Such income must be obtained by non-residents without a permanent establishment, as long as they are resident in a country that has signed a treaty with Spain containing an Exchange-of-Information Clause.

h) Dividends and shares in profits obtained without a permanent establishment by pension funds, as long as they are resident in other countries of the European Union or when there is a permanent establishment of such institutions in another EU member country.

i) Dividends and shares in profits obtained without a permanent establishment by collective investment institutions covered by Directive 2009/65/EC, or which are resident in the countries of the European Economic Area, as long as there is an agreement to exchange information.

j) Royalties paid by an entity resident in Spanish territory, or by a permanent establishment of a company resident in another country of the European Union, to a company resident in another member state of the EU. It is also acceptable for the recipient to be a permanent establishment in another member state as long as the legally established requirements are met and the parent company is resident in a country of the European Union.

The exemptions described in points a), g) and f) do not in any way apply to income obtained through tax havens.

5.3.4. The Figure of the Tax Representative

Non-resident taxpayers in Spanish territory are required, in certain cases, to appoint a natural or legal person residing in Spain to represent them before the tax authorities. That same obligation exists for persons or entities resident in countries or territories with which there is no effective exchange of tax information, who are owners of property situated or rights fulfilled or exercised in Spanish territory, excluding securities traded in official secondary markets.

In the case of permanent establishments, their representatives are considered to be those listed as such in the Commercial Register or, failing that, those stated as authorized to execute agreements on their behalf.

Failure to comply with this requirement is a punishable offence.

5.3.5. Special Tax on Real Estate

Entities resident in a country or territory which is treated as a tax haven, and who own real estate in Spain or real rights of enjoyment or use on them, are subject to a special tax which accrues on 31 December each year and which is to be paid in the following month of January. Currently, the rate of this special tax is 3% and is applied to the "cadastral" or registered value of the real estate. This special tax is not due for the following entities:

- **a**) States, foreign public institutions and international organizations.
- **b**) Entities conducting business in Spain on a continuous or habitual basis other than simple ownership or lease of real estate.

c) Companies listed in officially recognised secondary stock markets.

In any cases where an entity required to pay this special tax is co-owner of a property with another entity exempt from it, the tax will only be payable for the share it owns.

5.3.6. Filing the Non-Resident Income Tax Return

In general, the rules for Non-Resident Income Tax (IRNR) require a tax form to be filed for each individual income earned within the month following the date of accrual, which usually coincides with the due date of its payment. Such a declaration must be filed with the tax office of the AEAT located in the same area as the tax domicile of the representative. However, in the case of income derived from transfers of real estate, declarations must be filed with the office of the same area where such property is located.

In payment of this tax, and because of the difficulty of recording all transactions made by non-residents, the figure of the payer retaining the tax due and paying it into the AEAT account becomes very important. In effect, in many cases, the amount withheld becomes the taxation of the non-resident. In such situations, and in general, legislation provides for the possibility for the payer of income to a non-resident to file a declaration every three months containing all income earned in the previous calendar quarter.

5.3.7. Prevalence of International Treaties and Conventions

This section highlights the importance of bilateral agreements between Spain and other countries for the purpose of preventing double taxation of any income received. As a result

of their application, the rules on IRNR may be altered by the provisions of such agreements, which involves changes in the taxation of income of non-residents. It should be noted that the rules of any treaties take precedence over domestic law. Therefore, whenever a resident of a state with a double taxation treaty receives income obtained in Spain, the text of the treaty needs to be consulted in order to determine the appropriate tax treatment.

Below is a list summarizing the contents of the main double taxation treaties signed by Spain, which sets out the maximum percentages of tax payable in the country from where the income originates. Currently, Spain has established double taxation treaties with over 75 countries, but the table below contains only the agreements signed with the main European Union members and any other countries with which entry and exit of capital is most common. However, agreements have also been signed with countries which in recent years have significantly increased their investments in Spain such as China, Saudi Arabia and Russia, so any estimate of the tax for transactions with those countries must follow the provisions of the respective treaties.

5.4. Wealth Tax

Over the last decade, the existence of this tax has been subjected to a thorough debate, which has led to numerous changes in its regulations. For a short time it disappeared, then came back temporarily and ended up being extended without anyone knowing if and when it will again be removed from legal system.

This tax is levied on the ownership of all kinds of property and economic rights attributable to an individual to be recorded at 31 December every year.

Currently, taxpayers are only required to file a tax return where the tax liability is payable because the value of their non-exempt wealth exceeds 700,000 euros or, if not, when the value of their property or rights exceeds 2,000,000 euros. The tax applies both to residents in Spanish territory and non-residents, and it is interesting to note that the autonomous communities of Spain can change the minimum amount exempt.

The property and rights of individuals whose purpose is to conduct their business or professional activities are exempt from the tax as long as certain legal requirements are met. Holdings in entities conducting economic activities may also be exempt as long as any legal requirements are met. Similarly, a primary residence is exempt up to a maximum amount of 300,000 euros.

5.5. Inheritance and Gift Tax

Another tax assigned to Spain's autonomous communities, which is levied on the acquisition of property and rights through inheritance and gifts. It is also levied on amounts received by beneficiaries of life insurance whenever the policyholder is someone other than the beneficiary. If any such gains are obtained by legal persons, they will be subject to Company Tax rather than Inheritance and Gift Tax.

Taxpayers who have their primary residence in Spain will be taxable irrespective of where the acquired property or rights are situated. In contrast, non-residents will be taxed only on property situated or rights that may be exercised in Spain.

In the case of acquisition by close family members of an individual company, certain shareholdings in entities or a primary residence, there is a reduction in the tax base. Specifically, it will be 95% of the value of such items.

5.6. Local Taxes

There are several local or municipal taxes which are specifically worthy of mention because they affect businesses, especially those having a stable physical space where they operate. In addition to the three taxes included in this section, it is also worth mentioning the tax on motor vehicles, which is to be paid by all persons or companies with any in their name.

The following local or municipal taxes are worthy of special mention:

a) **Property Tax (I.B.I.)**
The taxable event consists of owning real property, the ownership of real usufruct or surface rights and that of an administrative concession. It is levied on the "cadastral", or registered, value of the property and is payable annually.

b) **Tax on Economic Activities (I.A.E.)**
This is levied on the mere exercise of a business, professional or artistic activity. It also accrues on an annual basis. It is a tax that does not apply for the first two years of performing the activity and is not required of individuals or entities whose turnover does not exceed 1,000,000 euros.

c) **Land Value Tax**.
This tax is levied on the improved value of urban land arising as a result of its transfer or the establishment

of any real right of enjoyment on such land (usufruct, surface, etc.).

5.7. Value Added Tax

VAT is a tax levied on consumption in general and applies to the following transactions: supply of goods and services, intra-Community acquisition of goods and importation of goods. The standard tax rate is 21%, while the reduced rate of 10% applies to certain products such as food items, water, housing in general, prescription lenses and medical supplies. There is also a super-reduced rate of 4%, which applies, among others, to medicines, staple food (bread, cereals, milk, cheese, eggs) and books, newspapers and magazines.

Every company or professional, when supplying goods or services, must add the corresponding VAT rate to their final amount. In turn, that same company or professional, in the course of their business, must pay VAT on any goods and services they have to purchase. When it comes to paying the tax, the taxpayer must deduct the VAT paid on purchases and acquisitions from the amount of VAT collected and pay the difference to the Treasury. Should the final result be negative, for example, in a quarter of heavy investment in equipment or machinery, the result can be offset in the following declarations. At the end of the year, and if the tax liability remains negative, the taxpayer can get a refund from the Treasury.

There is a special system of monthly rebates for any companies continuously having a VAT balance in their favour.

It is very important to note that any employers or professionals not established in Spain are entitled to claim

a refund on any VAT paid. To claim the refund, they must be established in a country of the European Union or in another country with which there is a reciprocity agreement. Any claim for a refund can be filed until 30 September of the year following the one in which the VAT was paid in Spain.

5.8. Tax on Asset Transfers and Legal Documents (Stamp Duty)

This tax, assigned to the autonomous communities, is levied on *inter vivos* asset transfers for payment of all kinds of goods and rights, company transactions and legal documents. It is incompatible with VAT, that is, the same event cannot be taxed by both, although there are some exceptions. This tax,

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Notes to the table on page 117

(1) Maximum rate of taxes to be charged in the country where dividends to be transferred arise.

(2) Maximum rate of taxes to be charged in the country where dividends arise, according to the holding in the capital of the subsidiary by the parent being equal to or greater than the controlling percentage shown in the table. In this regard, it is important to take into account the incorporation into Spanish law of the EU directive on the common system of taxation applicable to parent companies and subsidiaries in countries belonging to the European Union. The directive provides for, if the requirements are met, the non-taxation of dividends distributed by a subsidiary to its parent company and the non-application of the withholding system (see exemptions in section 5.3.3).

(3) Maximum rate of taxes to be charged in the country where any interest transferred originates. By applying the more favourable domestic regulations, the interest of residents in other countries of the European Union is exempt from taxation (see exemptions in section 5.3.3).

SUMMARY OF TREATIES TO PREVENT DOUBLE TAXATION

	(1)	(2)		(3)
	Dividends (General)	Dividends capital	Withholding Parent/ Subsidiary	Int.
	%	%	%	%
AUSTRIA	15	50	10	5
BELGIUM	15	25	---	0/10
BRAZIL	15	25	10	15/10
CANADA	15	10	5	10
FINLAND	15	25	10	10
FRANCE	15	10	---	10
GERMANY	15	10	5	---
ITALY	15	---	15	12
JAPAN	15	25	10	10
NETHERLANDS	15	50	10	10
NORWAY	15	25	10	10
POLAND	15	25	5	---
PORTUGAL	15	25	10	15
ROMANIA	15	25	10	10
SWEDEN	15	50	10	15
SWITZERLAND	15	10	---	---
UNITED KINGDOM	10/15	10	---	---
UNITED STATES	15	25	10	10

in its *stamp duty* form, is levied on notarial, business and administrative documents.

With regard to company transactions, the rules include a notable list of exemptions. Transactions for which no tax is payable are set out below:

- Company formation.
- Capital increase.
- Shareholder contributions not involving capital increase.
- The transfer to Spain of the effective head offices or registered offices of a company whenever neither of them was previously located in an EU member country.

Any company transactions which are not exempt are taxed at the rate of 1%. In addition, the transfer of a property is taxed at a rate of 6%. For the last case, some autonomous communities have set their own tax rate. Catalonia is one example, where the rate is 10%. Finally, the transfer of movable property is taxed at 4%.

5.9. Customs duties

As Spain is a member of the European Union, commercial transactions with other EU countries are not considered imports. In this respect, the introduction of a single European market meant the elimination of border and customs controls. What before 1993 were imports, is now called the *intra-Community acquisition of goods*, where, in general, goods are taxed when in the possession of the purchaser in the EU country of destination.

In the case of imports from countries which are not members of the European Union, standard import duty rates are usually paid when the goods concerned clear customs. With very few exceptions, customs duties are *ad valorem*, that is, they are calculated on CIF (Cost, Insurance and Freight) or on a similar assessable value. As a rule, it is the buyer or importer who is to pay the tariff costs associated with the goods concerned.

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