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Spain Looks Abroad to Reduce Deficit at Home

by Alan S. Lederman, Esq.
Gunster, Yoakley & Stewart, PA
Fort Lauderdale, Florida
and Dra. Mercedes Fuster Gómez
Universitat de València, Spain

The United States is far from unique in aggressively seeking to tax its residents and companies on their offshore holdings — Spain has adopted approaches strikingly similar to those of the United States. For example, the Spanish Treasury, like the U.S. Treasury, is using the following tactics: (1) broadening the network of countries that will respond to Spain's requests for tax information; (2) requiring other countries to respond to requests for information based on taxpayer behavior, and sizes and types of accounts, rather than naming specific taxpayers; (3) requiring other countries to automatically exchange tax information, rather than waiting for individual requests; (4) requiring residents to declare their foreign assets annually, with large penalties for noncompliance; (5) extending the statute of limitations for tax assessments relating to unreported foreign items; (6) increasing the size of its international audit staff; (7) introducing a voluntary disclosure regime with reduced penalties for those who come forward; (8) seeking to limit deductions for interest paid by domestic companies to foreign affiliates; and (9) scrutinizing transfer prices used in transactions with foreign affiliates. This article discusses a number of these tactics, with particular emphases on Spain's tax information exchange network and its intergovernmental agreement (IGA) with the United States pertaining to the Foreign Account Tax Compliance Act (FATCA).

SPAIN'S TAX INFORMATION EXCHANGE NETWORK

Spain in 2012 issued rules pursuant to a European Council Directive requiring European Union (EU) countries to cooperate with requests relating to income tax matters generated by another EU country.[1] Under the Directive, the requested EU country must use all the domestic measures available at its disposal to obtain the requested information, may not decline to respond because the data have no relevance to its domestic tax liability, and may not raise bank secrecy as a defense.

Pursuant to the Directive, beginning in 2015 for periods beginning in 2014, there generally is to be annual automatic exchange of information between Spain and other EU countries concerning salaries, pensions, and ownership of and income from real estate. This expands existing EU directives adopted by Spain concerning information exchange relating to savings interest income.[2] The EU has proposed to further expand the annual automatic exchange of information to include dividends, capital gains, and balances on accounts.[3]

The Directive also requires each EU country to spontaneously provide to Spain and any other requesting EU country, within one month, any information

[1] Royal Decree Law 1558/2012 (11/15/12), Article 2(9), *available in Spanish* at https://www.boe.es/buscar/doc.php?id=BOE-A-2012-14452. *See* "European Council Directive 2011/16/EU of 15 February 2011 on Administrative Cooperation in the Field of Taxation," *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2011:064:0001:0012:EN:PDF.

[2] *See* Kaye, "Direct Taxation in the European Union: From Maastricht to Lisbon," 35 *Fordham Int'l L.J.* 1231(2012). *But see* "European Union: Luxembourg, Austria Block EU Changes to Cross-Border Savings Tax Plan," 94 *DR.* I-3 (5/15/13).

[3] "EU Publishes Council Directive Proposal on Automatic Information Exchange," 2013 *WTD* 114-22 (6/13/13).

specifically requested that is foreseeably relevant to the enforcement of the income tax laws of the requesting country. Thus, for example, under the Directive, Spain can likely acquire from other EU countries information sought concerning possibly improperly high transfer prices charged Spanish affiliates for intra-EU acquisitions from a related seller in the requested EU country, improperly low transfer prices charged by Spanish affiliates for intra-EU transfers to a related buyer in the requested EU country, or improper interposition of a third-country affiliate to reduce the tax in Spain.

In 2013 Spain, as well as France, Germany, Italy, and the United Kingdom, announced their joint decision to work to establish a pilot project for the multilateral automatic exchange of account information along the lines of the bilateral FATCA IGAs.[4] Several other countries have indicated they would participate in such a program.[5]

Beyond the EU, Spain has recently concluded tax treaties and tax information exchange agreements with several countries. Following its ratification by Spain in 2012, the 2010 protocol to the OECD/Council of Europe Convention on Mutual Administrative Assistance in Tax Matters took effect in Spain in 2013.[6] The 2010 Protocol generally requires that each party supply upon request information ''foreseeably relevant'' to the tax laws of another party.[7] The 2010 Protocol also allows for other forms of assistance, such as automatic and spontaneous exchanges of information, performance of tax examinations abroad, service of documents, assistance in recovery of tax claims, and simultaneous and joint examinations.[8] Since 2010, more than 50 countries either have become signatories to the Convention or have stated their intention to become signatories.[9] U.S. ratification of the protocol is pending in the Senate.[10]

Spanish tax authorities have pointed to the revised Article 26 of the Organisation for Economic Co-Operation and Development's (OECD's) Model Tax Convention on Income and on Capital (OECD Model Treaty) as a development furthering their ability to obtain ''foreseeably relevant'' information concerning Spanish resident individuals and entities.[11] A key benefit of the ''foreseeably relevant'' standard of revised Article 26 is that treaty partners must supply data on groups of individuals or entities identified by the requesting country only by description, rather than by designation of specific individuals or entities, although ''fishing expeditions'' remain prohibited.[12]

Switzerland has not objected to revised Article 26, and has amended its internal law to accept treaty group requests beginning in 2013, at least for Swiss accounts that were not closed by the end of 2012 and in which there has been activity after 2012.[13] Revised Article 26 is incorporated in a Spain-Switzerland treaty protocol to enter into force in August 2013.[14] Under revised Article 26, Spain might obtain from Switzerland information on direct or indirect Spanish holders of Swiss accounts who meet certain described suspicious behavioral patterns, rather than Spain being required to name the account holders.[15]

Spain has entered into tax information exchange agreements with several countries, including some of-

[4] *See* ''European Union: Five EU-Member Nations Adopt Pilot Project Modeled After FATCA,'' 69 *DR.* I-1 (4/10/13).

[5] ''G-20 Calls for Global Action on Automatic Information Exchange,'' 2013 *TNT* 77-7 (4/22/13). *See also* ''Mexico: Mexico Asks to Join EU Pilot Tax Information Exchange Program as Tax Evasion Measure,'' 114 *DR.* I-6 (6/13/13); ''Crown Dependencies Announce Support for U.K.'s G-8 Tax Agenda,'' 2013 *WTD* 117-25 (6/18/13) (Jersey, Isle of Man, and Guernsey to join with U.K. in pilot program); ''Tax Treaties: At G-8, OECD Says FATCA Lays Groundwork for Global Automatic Information Exchange,'' 117 *DR.* I-2 (6/18/13).

[6] Lungu, ''Spain Ratifies Protocol to the OECD-Council of Europe Mutual Assistance Convention,'' 2012 *WTD* 224-9 (11/20/12); ''Protocol to OECD-Council of Europe Mutual Assistance Convention Enters Into Force in Spain,'' 2013 *WTD* 1-6 (1/2/13).

[7] ''2010 Protocol to the 1988 OECD-CE Mutual Administrative Assistance Convention Available,'' 2010 *WTD* 103-21 (5/28/10).

[8] *See* ''The Multilateral Convention on Mutual Administrative Assistance in Tax Matters,'' *available at* http://www.oecd.org/ctp/exchangeofinformation/MAC_Question_Answer_EN.pdf.

[9] ''Convention on Mutual Administrative Assistance in Tax Matters,'' *available at* http://www.oecd.org/tax/exchangeofinformation/conventiononmutualadministrativeassistanceintaxmatters.htm.

[10] ''Obama Sends OECD-Council of Europe Mutual Administrative Assistance Treaty Protocol to Senate,'' 2012 *WTD* 97-29 (5/18/12); ''Tax Treaties: Concern Growing Among Multinational Firms as Senator Continues Hold on Three Treaties,'' 87 *DR.* G-4 (5/6/2013) (OECD mutual assistance treaty may be making its way to Senate for action).

[11] ''Spanish Treasury Adopts New Measures to Combat International Tax Evasion,'' *La Moncloa* (10/20/12), at http://www.lamoncloa.gob.es/IDIOMAS/9/Gobierno/News/2012/20121120_International_Tax_evasion.htm.

[12] Pross, Smith, and Lara, ''Update to Article 26 of the OECD Model Treaty — What the Changes Mean,'' 2012 *WTD* 195-17 (10/9/12); ''OECD Publishes Updated Exchange of Information Article in Model Tax Convention,'' 2012 *WTD* 139-26 (7/19/12); ''OECD Answers Questions About Model Tax Convention Group Information Exchange Update,'' 2012 *WTD* 139-28 (7/19/12). Revised Article 26 also permits the receiving state, if the internal laws of the receiving state and supplying state permit, and the supplying state agrees, to allow the receiving State's non-tax law enforcement agencies to use information requested and obtained by the receiving State for tax purposes.

[13] Kadar, ''Swiss Parliament Approves Group Information Requests,'' *RIA Checkpoint Int'l Taxes Weekly Newsletter* (09/18/12); ''Switzerland: Swiss Committee Rejects Retroactive Application of Group Requests for Tax Data,'' 176 *DR.* I-2 (9/12/12);

[14] *La Moncloa*, fn. 11 above; ''Protocol to the 1966 Spain-Switzerland Tax Treaty Available,'' 2011 *WTD* 145-30 (7/28/11); Lungu, ''Protocol to Spain-Switzerland Tax Treaty Will Enter into Force in August,'' 2013 *WTD* 115-9 (6/13/13).

[15] ''Switzerland Lifts Bank Secrecy and Will Give Spain Account Information,'' *Cámara* (9/20/12) *available in Spanish at* http://www.asociaciondavide.es/?q=suiza-levanta-el-secreto-bancario-y-dara-a-espa%C3%B1a-datos-sobre-cuentas (citing an

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ten considered as tax havens. For example, the 2010 Spain-Bahamas tax information exchange agreement can require the Bahamas to provide to Spain, upon a properly documented request by Spain, information concerning ownership by a named Spanish resident individual or Spanish corporation of shares of Bahamas companies (even if the accounts or other assets of those Bahamas companies are outside the Bahamas) or accounts in Bahamas financial institutions.[16]

In 2013, Spain and the United States signed a new protocol to the 1991 U.S.-Spain Income Tax Treaty. The protocol contains a ''foreseeably relevant'' standard for the exchange of tax information.[17]

FATCA: REPORTING BY THE UNITED STATES TO SPAIN

In May 2013, Spain signed a reciprocal FATCA IGA with the United States.[18] This agreement is similar to the reciprocal Model 1 FATCA IGA issued in 2012 by the U.S. Treasury.[19] The agreement will take effect when it is approved by the Spanish parliament.

Under this FATCA IGA, the IRS has agreed to report to Spain on Spanish Reportable Accounts at certain U.S. financial institutions. ''Spanish Reportable Accounts'' include certain depository and non-depository accounts of individuals resident in Spain, and also non-depository accounts of entities that certify they are residents of Spain.[20] Depository accounts generally include accounts, including time deposits, that pay more than $10 of interest annually; thus, non-interest-bearing accounts are not depository accounts. The Spain FATCA IGA effectively reverses the IRS decision in Rev. Proc. 2012-24.[21] In Rev. Proc. 2012-24, issued before the Spain FATCA IGA was signed, the IRS declined to exercise its discretion under the U.S.-Spain Income Tax Treaty to automatically inform Spain of post-2012 interest paid on U.S. deposits to individual Spanish depositors.

However, even under the Spain FATCA IGA, in the case of an entity, depository accounts are not Spanish Reportable Accounts, whether or not the entity is a resident of Spain and whether or not the account is interest-bearing. Thus, for example, an interest-bearing U.S. bank account owned by a Spanish corporation whose sole shareholder is a Spanish resident is not a Spanish Reportable Account.

In the case of an account that is not a depository account, such as a stock brokerage account, a Spanish Reportable Account includes any account owned by an individual or entity resident in Spain that generates U.S.-source income (e.g., dividends on U.S. publicly traded stock or income from a publicly traded U.S. partnership) and that is subject to information reporting.

The United States will provide to Spain, with respect to each Spanish Reportable Account, the name, address, and generally the Spanish taxpayer identification number of the Spanish resident account holder. The United States will supply the account number and the name and identifying number of the U.S. financial institution. The United States will report to Spain the gross amount of interest paid on a depository account, the gross amount of U.S.-source dividends credited to the account, and the gross amount of other U.S.-source income credited to the account that is subject to U.S. information reporting.

Similar to other U.S. FATCA IGAs, the U.S. obligations enumerated in the Spain FATCA IGA to spon-

estimate of $59 billion of Spanish-owned accounts in Switzerland); Bibler and Hongler, ''Group Requests in Switzerland — Recent Developments and Uncertainties,'' 2013 *WTD* 111-17 (6/10/13).

[16] Available at http://www.oecd.org/spain/44785378.pdf. *See also* ''Treasury Report — Foreign Affairs and International Cooperation,'' *La Moncloa* (4/13/13), *available in Spanish at* http://www.lamoncloa.gob.es/ConsejodeMinistros/Referencias/_2013/refc20130412#CumplimientoFiscal (tax information exchange agreements are in effect with Andorra, Aruba, the Bahamas, Barbados, Hong Kong, Jamaica, Luxembourg, Malta, Netherlands Antilles, Panama, San Marino, Trinidad and Tobago, and United Arab Emirates; negotiations have been concluded with Guernsey, Isle of Man, Jersey, and Monaco; administrative agreements have been signed since 2011 to exchange information pursuant to tax treaties with the Canada, Panama, the United States, and Uruguay; and tax agreements to exchange information pursuant to tax treaties are being processed with Brazil, Belgium, and Italy).

[17] ''Protocol Amending U.S.-Spain Tax Treaty,'' *BNA TaxCore* (1/15/13). The new protocol also provides for exclusive residence-based taxation of interest, royalties, certain direct dividends, and non-real-estate capital gains, but imposes new Limitation on Benefits rules. The protocol also has a new arbitration provision. *See* ''Tax Treaties: Numerous Technical Changes Modernize New U.S.-Spain Tax Treaty, Treasury Official Says,'' 11 *DR.* G-3 (1/16/13).

[18] http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Spain-5-14-2013.pdf. See Notice 2013-43, 2013-31 I.R.B., §IV (the signed Spain FATCA IGA will be treated by the IRS as in effect provided that its approval by the Spanish parliament is not unreasonably delayed.

[19] *See* http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Model-1A-Agreement-to-Implement-Reciprocal-11-14-2012.pdf.

[20] Under the Spanish income tax law, an entity is considered to be resident in Spain if it meets any of the following requirements: (1) it was incorporated in accordance with Spanish law; (2) its registered office is in Spain; or (3) its effective management headquarters, or the management and control of its overall activities, are situated in Spain. The Spanish Tax Administration can presume that an entity situated in a no-tax jurisdiction or a tax haven is resident in Spain when its principal assets, directly or indirectly, are situated in Spain or when its principal activity takes place in Spain. This presumption can be rebutted by the entity if it proves that its effective management takes place in the territory of the no-tax jurisdiction or tax haven and that its incorporation and operation are justified by valid economic and substantive business reasons other than mere asset holding activities. Sánchez López and Ortiz de Juan, 984 T.M. (Bloomberg BNA Tax & Accounting), *Business Operations in Spain*, at V, A, 2 and VI, B. A Spanish resident's willfully failing to certify Spanish residence to a reporting U.S. financial institution in order to avoid FATCA reporting to Spain could raise issues as to U.S. criminal liability. *See Pasquantino v. United States*, 544 U.S. 349 (2005).

[21] 2012-20 I.R.B. 913.

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taneously forward account information to Spain on Spanish Reportable Accounts are far narrower than the corresponding Spanish obligations to spontaneously forward account information to the United States on U.S. Reportable Accounts in Spanish financial institutions. The Spain FATCA IGA, as applied to accounts indirectly or directly owned by Spanish residents in U.S. financial institutions, fails to squarely address the central tax evasion behaviors addressed by FATCA.

For example, the Spain FATCA IGA does not require a U.S. financial institution to report on U.S. accounts held by a non-Spanish-resident, tax haven corporation that is partially or wholly owned by an individual Spanish resident. Moreover, even if a Spanish resident corporation or Spanish individual has a reportable U.S. brokerage account, U.S. sales proceeds or gains realized within the account will generally not be reported to Spain, because sales proceeds or capital gains of a foreign person from securities sales are generally exempt from U.S. statutory broker information reporting.[22]

In the Spain FATCA IGA, as in other FATCA IGAs, the United States agrees to pursue the adoption of regulations and to advocate and support relevant U.S. legislation to achieve such equivalent levels of automatic exchange with Spain. Unless and until such equivalent levels are reached, however, as in the case of other FATCA IGAs, the automatic information exchange mechanism of the Spain FATCA IGA seems largely ineffective from the U.S. side.[23] Rather, at least in the near future, it seems likely Spain will have to continue to rely on non-FATCA sources to ferret out unreported U.S. financial accounts indirectly owned by Spanish residents through tax haven or other entities.

FATCA: REPORTING BY SPAIN TO THE UNITED STATES

Spain's broad obligations listed in the Spain FATCA IGA are similar to those in the reciprocal Model 1 FATCA IGA issued in 2012 by the U.S. Treasury. The Spain FATCA IGA covers Spanish branches of both Spanish and non-Spanish financial institutions, but does not cover non-Spanish branches of either Spanish or non-Spanish financial institutions.

Under the Spain FATCA IGA, Spain is to gather from Spanish branches of financial institutions data on U.S. Reportable Accounts. "U.S. Reportable Accounts" generally include accounts held by U.S. individuals, non-publicly-traded U.S. corporations, and other U.S. entities. However, data generally need not be gathered or reported concerning U.S. individually owned depository accounts whose aggregate balance is no more than $50,000, and insurance policies whose cash surrender value is no more than $50,000. U.S. Reportable Accounts also generally include accounts held by non-U.S. entities, such as tax haven entities and Spanish entities, that are controlled by one or more U.S. individuals or entities. Spanish branches of financial institutions are to perform certain due diligence to determine if an account is a U.S. Reportable Account. Account data gathered are to include identifying information concerning the account, the U.S. direct owners (or U.S. controlling indirect owners of a foreign entity account), the account balance, interest paid on a depository account, and proceeds paid to a custodial account.

The key U.S. tax benefit to Spanish financial institutions from compliance with their obligations described in the Spain FATCA IGA is that such Spanish financial institutions receive relief from FATCA. A Spanish financial institution will not be subject to §1471 withholding, provided that the financial institution timely identifies and reports U.S. Reportable Accounts to Spain, complies with certain registration requirements, and meets certain reporting and withholding obligations with respect to certain payments to non-participating financial institutions. There is no need for the Spanish financial institution to enter into an agreement with the IRS, nor generally to supply information directly to the IRS. Moreover, a Spanish financial institution need not withhold with respect to accounts held by recalcitrant account holders or close the accounts, provided that the United States receives information with respect to such accounts. Further, the Spanish financial institution is relieved from the U.S. statutory pass-through payment withholding rules.

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[22] Regs. §§1.6045-1(c)(3)(i)(B)(*1*), 1.6045-1(g)(1).

[23] See Bouma, "11 Reasons Why FATCA Must Be Repealed," 41 *Tax Mgmt. Int'l J.* 651 (12/14/12) ("The audacity of the Treasury Department to enter into 'reciprocal' FATCA Intergovernmental Agreements that are such one-way streets is unbelievable," and "Treasury officials have little interest in imposing FATCA-type reporting burdens on U.S. [financial institutions]"). See also Nauheim and Cousin, "The Evolving FATCA Guidance," 54 *Tax Mgmt. Memo.* 163 (May 2013). The White House 2014 Budget Proposal states, "The proposal would provide the Secretary of the Treasury with authority to prescribe regulations that would require reporting of information with respect to nonresident alien individuals, entities that are not U.S. persons, and certain U.S. entities held in substantial part by non-U.S. owners, including information regarding account balances and payments made with respect to accounts held by such persons and entities." U.S. Office of Management and Budget, "Analytical Perspectives, Budget of the United States Government, Fiscal Year 2014," p. 202, *available at* http://www.whitehouse.gov/sites/default/files/omb/budget/fy2014/assets/spec.pdf.

However, one commentator concludes that this language does not contemplate supplying to foreign countries with FATCA IGAs information on U.S. accounts held through tax haven entities with substantial investors resident in that foreign FATCA IGA country. *See* "Financial Institutions: FATCA Budget Language Could Spell More Reporting for U.S. Financial Institutions," 76 *DR.* GG-1 (4/19/13) ("Laurie Hatten-Boyd, head of KPMG LLP's Tax Information Reporting and Withholding Group, . . . noted that a U.S. financial institution would only be required to 'look through' U.S. entities, not all entities. For example, she said, if two U.K. residents formed a corporation in the Cayman Islands that had a presence in a U.S. bank, the United Kingdom still would not know that it had residents investing into the United States because information would be exchanged only at the corporate level").

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The fact that a Spanish financial institution has a branch outside of Spain that is prevented by local law from complying with FATCA will not necessarily disqualify the Spanish operations from the benefits of the Spain FATCA IGA, provided that certain criteria are met.

The Spain FATCA IGA also contains an Annex listing exempt account owners, e.g., certain Spanish governmental entities and Spanish retirement funds; deemed-compliant Spanish financial institutions, e.g., not-for-profit Spanish entities and Spanish financial institutions with a local client base meeting certain requirements; and exempt products, such as certain Spanish retirement accounts, which are effectively exempt from FATCA.

Under the Spain FATCA Agreement, generally, information exchange is to begin during 2015, with information supplied annually thereafter. Article 7 of the Spain FATCA IGA includes a ''most favored nation'' clause, generally granting to Spain the benefit of any more favorable terms afforded to another foreign country by the United States under a signed FATCA IGA. Under the signed but not yet ratified Germany and Norway FATCA IGAs, as well as the May 2013 version of the reciprocal Model 1 FATCA IGA (now called Model 1A), the non-U.S. signatory is not obligated to obtain and send to the IRS information with respect to a calendar year that is prior to the calendar year with respect to which similar information is required to be reported by U.S. financial institutions to the IRS pursuant to relevant U.S. Treasury regulations, nor to begin exchanging information prior to the date that U.S. financial institutions are required to report similar information to the IRS pursuant to relevant U.S. Treasury regulations.[24] As a consequence, some commentators conclude that, unless and until U.S. Treasury regulations requiring expanded reporting by U.S. financial institutions are promulgated, Spain's obligations to supply reciprocal data to the IRS in order to avoid U.S. withholding on Spanish financial institutions may likewise be indefinitely suspended.[25]

SPANISH INTERNATIONAL ENFORCEMENT INITIATIVE

Spain has undertaken various initiatives to force disclosure of unreported foreign holdings. Beginning in 2013, individuals and entities that are subject to Spanish personal income tax or Spanish corporate income tax on their worldwide income must file an annual declaration of assets abroad that they owned, or had authority over, or were beneficiaries of, or held effective title for, during the preceding year.[26] Reporting generally applies to financial accounts, securities, equity interests, life and disability insurance, and real estate. Amounts generally need not be initially reported if they aggregate less than $65,000, and items first reported need not be reported again unless they have increased by $26,000. Assets adequately identified on financial statements of entities generally need not be reported.

Failure to adequately disclose will carry penalties. Moreover, if a taxpayer is found to have a foreign asset that is not properly disclosed, the asset may be deemed to have been acquired from unreported income, the statute of limitations may be extended to permit assessment on such income in an otherwise closed year, and an additional penalty of 150% of the income tax deficiency may apply.[27]

Payment in cash, bank checks payable to bearer, and other cash-equivalent items, involving companies or professionals, is limited to $3,250 in the aggregate for any overall transaction.[28] The penalty is generally 25% of the amount of the cash or cash-equivalent payment. However, if either the payor or payee, within three months after the payment, is the first to voluntarily disclose having made or received the payment on a special Spanish governmental website already established for this purpose, that first repentant person will be exempted from the penalty. The penalty is in addition to other possible penalties, such as the penalty for individuals taking from Spain to outside Spain, or bringing to Spain from outside Spain, cash-equivalents of above $13,000 without making the required declarations.

Effective in 2013, the Spanish Penal Code was amended to extend the statute of limitations for the most serious tax crimes from five to 10 years, with

[24] The Germany, Norway, and May 2013 Model 1A FATCA IGAs are *available at* http://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA.aspx.

[25] *See* ''U.S. Signs Sixth FATCA IGA, With Norway,'' 23 *J. Int'l Tax.* 9 (June 2013). Because the Germany and Norway FATCA IGAs, unlike the Spain FATCA IGA, generally allow the non-U.S. signatory to use definitions in the FATCA final Treasury regulations in lieu of the definitions in each agreement, by operation of the Article 7 clause, commentators similarly conclude that Spain should be able to likewise use FATCA regulatory definitions. *See* ''U.S. and Switzerland Sign Memorandum of Understanding on FATCA Agreement,'' 2013 *TNT* 111-8 (6/10/13).

[26] Law 7/2012 (10/29/12), *available in Spanish at* http://www.boe.es/boe/dias/2012/10/30/pdfs/BOE-A-2012-13416.pdf; Royal Decree 1558/2012, fn. 1, above; ''Spanish Government to Approve Anti-Tax Evasion Decree,'' 2012 *WTD* 72-2 (4/13/12); Carreño and de Vicente, ''Spain's New Requirement for Declaring Assets Held Abroad,'' 2013 *WTD* 106-23 (6/3/13). A Spanish resident is deemed to have ''effective legal title'' to a foreign asset if, for example, the asset is owned by a non-publicly-traded non-Spanish company in which the Spanish resident owns, directly or indirectly, more than 25% of the vote or value, or otherwise exercises management or control, or if the foreign asset is owned by a non-Spanish trust in which the Spanish resident exercises control over 25% or more of the assets or under which the Spanish resident is a principal intended beneficiary. *See* Law 10/2010 (4/28/2010), *available in Spanish at* http://www.boe.es/boe/dias/2010/04/29/pdfs/BOE-A-2010-6737.pdf.

[27] Law 7/2012, fn. 26, above.

[28] *Id.* Spanish Association of Tax Advisors, ''Limitations on Cash Payments,'' *available in Spanish at* http://www.aedaf.es/gestion_documental/documentos/Limitación%20de%20pagos%20en%20efectivo.pdf.

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prison sentences of up to six years.[29] Such serious crimes include tax crimes involving the use of tax havens and tax crimes where the tax defrauded exceeds $780,000.

In early 2013, the Spanish Treasury Department established a special Department of International Tax Affairs.[30] This department is composed of international tax specialists, who will undertake centralized planning and will support examinations.

In March 2013, the Spanish Tax Agency released an overall audit plan.[31] It has focus on such international compliance areas as undisclosed non-Spanish assets, unreported cash transactions, and fictitious claims of non-Spanish residency. The audit plan also includes the use of tax investigations as an aid to non-tax investigations of corruption. It also includes base erosion and profit shifting by multinational corporations, including e-commerce firms, such as by means of improper charges to Spanish affiliates by tax haven affiliates, or underpayment by non-Spanish affiliates for intangible or tangible assets produced in Spain.

The 2013 audit plan thus indirectly responds to Spanish press reports of individual tax non-compliance by well-known Spanish personalities, some based on account data revealed by a former Swiss bank employee.[32] Moreover, it responds to Spanish press reports of very low effective Spanish corporate income tax rates imposed on revenues originating in Spain of major U.S.-based multinationals, especially companies in the field of digital information.[33]

In preparation for expanded 2013 and subsequent audit initiatives directed at undisclosed offshore holdings, Spain in 2012 established an income tax voluntary disclosure program.[34] During 2012, Spanish resident individuals and corporations that might otherwise have been taxed at a much higher rate were able to declare previously undeclared earnings, including those kept in tax havens, and pay a tax rate of no more than 10% on the asset value declared, rather than normal income tax rates which, in the case of individuals, can exceed 50%. In the sense of tax rate reduction, the voluntary disclosure program had elements of an ''amnesty,'' a characterization applied by Spanish critics of the program. Further, certain deferred foreign income ineligible for the Spanish participation exemption, such as income accumulated in certain tax haven subsidiaries, could be repatriated by Spanish parent corporations in 2012 at a tax rate of 8%. However, beginning in 2013, the assets declared or repatriated in this 2012 program will themselves be subject to the regular Spanish income taxes applicable to their Spanish resident owners, so the 2012 program had elements of a ''regularization,'' the characterization applied by the Spanish government officials promoting the program. This 2012 voluntary disclosure program resulted in collections of $1.6 billion, about half of the amount projected by the Spanish government when the program was adopted.[35]

SUBSTANTIVE TAX LAW CHANGES

In an effort to raise revenues, beginning in 2012 various Spanish corporate income tax deductions and credits were curtailed. For example, in 2012 new interest-expense-stripping limitations were adopted.[36] Interest expense on debt due to related parties is gen-

[29] Institutional Law 7/12 (12/27/12), *available in Spanish at* http://www.boe.es/boe/dias/2012/12/28/pdfs/BOE-A-2012-15647.pdf.

[30] ''Spain: Spanish Government Creates International Taxation Office,'' 54 *DR.* I-1 (3/20/13); *La Moncloa*, fn. 11, above.

[31] ''Annual Treasury Plan of Income Tax and Customs Duty Enforcement'' (3/12/13), *available in Spanish at* http://www.boe.es/boe/dias/2013/03/12/pdfs/BOE-A-2013-2680.pdf; ''Spain: Spain Reveals 2013 Anti-Fraud Strategy With Closer Scrutiny of E-Commerce, MNCs,'' 50 *DR.* I-1 (3/14/13).

[32] *See* ''The First Falciani List of Names,'' *El País* (4/21/13), *available in Spanish at* http://politica.elpais.com/politica/2013/04/21/actualidad/1366522419_772068.html (court documents from 2010 through 2013 show that list of names from former employee of HSBC in Switzerland permitted Spain to identify 659 apparent tax evaders and to recover $338 million in additional Spanish taxes); ''Spanish Court Denies Swiss Extradition Request for Falciani,'' *El País* (5/8/13), *available in Spanish at* http://politica.elpais.com/politica/2013/05/08/actualidad/1368011173_885224.html.

[33] ''Spanish Treasury Will Stop the Tax Abuses of Google, Apple and Amazon,'' *Valencia Ciudad* (10/22/12), *available in Spanish at* http://www.vlcciudad.com/hacienda-frenara-los-abusos-fiscales-de-google-apple-y-amazon/). *See also* ''Google Uses Tax Havens to Pay Only a 2.4% Tax Rate,'' *El País* (10/22/10), *available in Spanish at* http://elpais.com/diario/2010/10/22/economia/1287698406_850215.html; ''Apple Uses Affiliates Without a Tax Domicile,'' *El País* (5/21/13), *available in Spanish at* http://economia.elpais.com/economia/2013/05/21/actualidad/1369092199_397078.html (U.S. Senate report points out that Apple's Irish holding company, for certain of Apple's Spanish and other non-U.S. operations, earned $30 billion from 2009-2012, yet paid no taxes anywhere). In 2012, the Spanish Central Tax Court upheld the Spanish Tax Agency's position that the Irish affiliate of Dell was liable for tax on its Spanish sales, because its activities there gave rise to a ''permanent establishment.'' See Sprague, ''Spanish Court Imposes Tax Nexus by Finding a 'Virtual PE','' 42 *Tax Mgmt. Int'l J.* 48 (1/11/13); Martinez-Matosas/Calderón, ''The Spanish Substantialist Approach to Fragmented Structures of Business: The Dell Case, a subsidiary as Permanent Establishment,'' *Spanish Tax Alert, Gómez-Acebo&Pombo* (Sept. 2012), at http://www.gomezacebo-pombo.com/media/k2/attachments/the_spanish_substantialist_approach_to_fragmented_structures_of_business_the_dell_case_a_subsidiary_as_permanent_establishment.pdf.

[34] ''Spain: Austerity Plan Offers Controversial Tax Amnesty, Modifies Corporate Taxes,'' 63 *DR.* I-1 (4/3/12); 984 T.M., ''Business Operations in Spain,'' fn. 20 above, at IV, K; Spanish Association of Tax Advisors, ''Voluntary Disclosure: Features and Basic Issues,'' *available in Spanish at* http://www.aedaf.es/gestion_documental/documentos/ria41DECLARACION%20TRIBUTARIA%20ESPECIAL.pdf.

[35] ''Spain Raises $1.6 billion with Its Tax Amnesty, Half of the Forecast,'' *Reuters* (12/3/12), *available in Spanish at* http://es.reuters.com/article/businessNews/idESMAE8B203Q20121203.

[36] Royal Decree — Law 12/2012 (3/30/12), *available in Spanish at* http://www.boe.es/boe/dias/2012/03/31/pdfs/BOE-A-2012-4441.pdf; Treasury Regulation, *available in Spanish at* https://

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erally disallowed if the loan proceeds are destined for the purchase from other related group members of equity interests in any type of entity, or destined for equity contributions to other group members, unless a business purpose can be shown.

Annual interest paid, whether to unrelated parties or to related parties but not disallowed under the preceding rule, in excess of interest income can generally be deducted currently, but only to the extent of $1.3 million or, if greater, 30% of operating cash flow. This limitation generally applies in lieu of a case-by-case ''thin capitalization'' determination. Deductibility of any annual interest expense in excess of the limitation is carried forward for up to 18 years, until annual limitation becomes available in a carryforward year. Accordingly, U.S.-based multinationals may wish to consider whether it may be advantageous to reduce the use of debt financing by Spanish subsidiaries.[37]

In November 2012, the OECD indicated that it would be necessary for Spain to collect even more tax revenues to reduce its budget deficit.[38] In December 2012, the Spanish government adopted new tax measures.[39] These included up to a 30% reduction of otherwise available depreciation and amortization allowances in determining the 2013 and 2014 corporate income tax liabilities of large corporations. However, the amount disallowed in 2013 and 2014 will be allowed ratably as a deduction, beginning in 2015, over the shorter of 10 years or the asset's useful life. The December 2012 law also grants Spanish-resident individuals and corporations, and non-Spanish-resident individuals and corporations with respect to their Spanish permanent establishments, an election to revalue upwards, by an indexed amount, but not above fair market value, the net tax book value of their fixed tangible and intangible assets acquired before 2012, for purposes of computing their depreciation deductions beginning in 2015. However, electing taxpayers must pay with their 2012 tax return, in exchange for this opportunity to reduce their 2015 and later taxes, a toll-charge tax equal to 5% of the amount of the step-up.

In 2013, the Spanish government approved a bill, aimed in part at Spanish multinational corporations, that would generally preclude Spanish corporations from deducting depreciation in the value of their stock in non-Spanish and Spanish corporations, and from deducting operating losses incurred through their non-Spanish permanent establishments until the sale or abandonment of those permanent establishments.[40]

EUROPEAN COMMISSION RECOMMENDATIONS

The European Commission, in December 2012, recommended EU-wide actions to prevent Spanish and other EU resident individuals and companies from evading their EU home country taxes through transactions in other EU and non-EU countries.[41] The Commission recommended that, in 2013, uniform electronic automatic information exchange procedures be pursued for automatic exchanges pursuant to the EU Directive, and other automatic exchange procedures. To facilitate future joint examinations, EU tax authorities are encouraged to ensure during 2013 that their domestic legislation and regulations do not prevent other EU country tax officials from being present at their offices and at the premises of taxpayers.

The Commission also proposed to study the issuance of EU-wide taxpayer individual and entity identification numbers to help EU-wide identification of transactions by a single taxpayer. The Commission also expected to propose coordinated software or hardware to reduce the costs of exchange of information. For the longer term, the Commission proposed joint audits, and direct EU access to other EU national databases.

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www.boe.es/boe/dias/2012/07/17/pdfs/BOE-A-2012-9483.pdf; Carreño and Rodríguez, ''News Analysis: Spanish Cabinet Shakes Up Corporate Tax Regime,'' 2012 *WTD* 65-4 (4/4/12). In 2011, the European Commission declared non-deductible the tax amortization of financial goodwill for European stock acquisitions allowed by Spain, on the theory that this tax deduction represents illegal state aid. Non-deductibility for stock acquisitions has certain exceptions, such as where it can be demonstrated that legal barriers to cross-border business combinations exist (as may be the case in China and India). *See* ''European Union: EU Commission Demands Repeal of Spanish Tax Breaks for Foreign Company Acquisitions,'' 9 *DR.* I-2 (1/13/11).

[37] Gerdes, Dantas, and Royuela, ''Investing in Pan Latin American Operations through Europe,'' 23 *J. Int'l Tax.* 22 (Nov. 2012).

[38] ''More Tax Increases Unavoidable If Spain Is to Rein in Deficit,'' 2012 *WTD* 232-4 (12/3/12).

[39] Law 16/2012 (12/27/12), *available in Spanish at* http://www.boe.es/boe/dias/2012/12/28/pdfs/BOE-A-2012-15650.pdf.

[40] The text of this bill, No. 121/000054, which has not yet entered into effect, is at http://www.congreso.es/portal/page/portal/Congreso/PopUpCGI?CMD=VERLST&BASE=pu10&DOCS=1-1&DOCORDER=LIFO&QUERY=%28BOCG-10-A-54-1.CODI.%29#(Página1); ''Spain: Spain Approves Plan to Eliminate Some Corporate Deductions, Raise Indirect Taxes,'' 126 *DR.* I-1 (7/1/13); ''$6.1 Billion More in Taxes,'' *El País* (4/21/13), *available in Spanish at* http://economia.elpais.com/economia/2013/06/28/actualidad/1372423170_831566.html.

[41] ''Communication from the Commission to the European Parliament and the Council — An Action Plan to Strengthen the Fight Against Tax Fraud and Tax Evasion; Recommendations on Tax Havens,'' ''Commission Recommendation of 6.12.2012 Regarding Measures Intended to Encourage Third Countries to Apply Minimum Standards of Good Governance in Tax Matters,'' and ''Commission Recommendation of 6.12.2012 on Aggressive Tax Planning,'' *available at* http://ec.europa.eu/taxation_customs/common/publications/com_reports/taxation/index_en.htm;

''European Union: European Commission Calls for Larger Crackdown on Harmful Business Taxation,'' 235 *DR.* I-2 (12/7/12). *See also* ''European Council — 22 May 2013 — Conclusions,'' sec. II, *available at* http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/137197.pdf (''It is important to take effective steps to fight tax evasion and tax fraud, particularly in the current context of fiscal consolidation, in order to protect revenues and ensure public confidence in the fairness and effectiveness of tax systems. Increased efforts are required in this field, combining measures at the national, European and global levels'').

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The Commission also made recommendations that could assist Spain in seeking a greater allocation of profits to Spanish affiliates of multinational corporations. The Commission proposes that EU countries establish a ''blacklist'' of countries that engage in harmful tax practices and seek to renegotiate or terminate tax treaties with such blacklisted countries. ''Harmful tax practices'' is defined broadly to include not only failing to exchange tax information, but also exempting or providing special low rates of income tax on transactions involving other countries, or providing local tax advantages that do not affect the national tax base.[42]

The Commission also makes specific recommendations concerning aggressive tax planning. It recommends a uniform anti-abuse rule, applicable to both cross-border and domestic arrangements, whereby transactions entered into for the essential purpose of avoiding taxation are ignored and characterized by their economic substance. Moreover, in order to avoid double non-taxation, the Commission recommends that a member condition any concession of non-taxation in a tax treaty by a requirement that the item be taxable in the other country. The Commission also wishes to revise, during 2013, the EU Parent-Subsidiary Directive (which generally eliminates from payor country withholding tax and payee country corporate tax dividends received by an EU parent from an EU subsidiary) to prevent mismatches due to the use of hybrid loans and hybrid entities. Some Spanish tax inspectors have praised the December 2012 Commission proposals, but note that they are only non-binding recommendations.[43]

In June 2013 the European Council recommended to Spain that it ''take further measures to address the debt bias in corporate taxation, and intensify the fight against the shadow economy and undeclared work.''[44] The OECD, of which Spain is a member, is preparing an action plan to address base erosion and profit shifting. Among the topics to be dealt with are countering base erosion by eliminating asymmetries between tax systems and hybrid instruments, clarifying tax jurisdiction in e-commerce transactions, and adjusting transfer pricing rules.[45]

CONCLUSION

Faced with a large budget deficit, Spain has turned, in part, to international enforcement activities to raise revenues. Some Spanish measures, such as the 2012 voluntary disclosure program, have already produced modest short-term revenue and will continue to generate taxable yield for the foreseeable future. Other measures may require implementation by non-Spanish authorities, such as FATCA reciprocal reporting to Spain by the IRS of U.S. accounts owned by tax haven entities controlled by Spanish residents, and EU Directives in support of the European Commission's December 2012 anti-tax-avoidance recommendations. In the meantime, Spain must continue to look to other internal tax measures and spending cuts to meet its deficit reduction goals.

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[42] See ''European Union: European Commission to Launch New Plan Against Tax Havens, Corporate Tax Loopholes,'' 234 *DR.* I-2 (12/6/12) (''The proposal does not mention any by name. However, speaking on the condition of anonymity, European Commission officials say Switzerland is at the top of the list . . . . In order to attract multinational corporations to set up their headquarters in Switzerland, some of the Swiss nation's cantons provide tax exemptions on company profits from earnings outside the country. As a result many companies are based in Switzerland, but much of their business is in the EU'').

[43] ''Tax Examiners: Defrauding Spain Is Very Feasible for the Rich,'' *ABC* (12/7/12), *available in Spanish at* http://www.abc.es/economia/20121207/abci-defraudar-espana-asequible-para-201212071112.html.

[44] Council of the European Union, ''Country-specific recommendations on economic and fiscal policies'' (6/21/13), *available at* http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ecofin/137558.pdf, approving the draft recommendations set forth in http://register.consilium.europa.eu/pdf/en/13/st10/st10656.en13.pdf. *See also* ''European Union: EU Panel Seeks Lower Financial Transactions Tax Rates for Sovereign Bond, Pension Trades,'' 118 *DR.* I-3 (6/19/13), discussing a possible EU financial transaction tax.

[45] ''OECD Issues Declaration on Base Erosion and Profit Shifting,'' 2013 *WTD* 106-41 (6/3/13).

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