

Navigating Spain's Special Inbound Expatriates Tax Regime

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PRACTITIONERS' CORNER

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In this article, the authors review the differences between the general income tax regime for Spanish tax residents and the special tax regime for inbound expatriates.

Spain consistently ranks as one of the best countries in the world in terms of quality of life. For many, Spain is the Florida of Europe. However, high-net-worth individuals and expatriates should carefully consider the tax implications when relocating to the country and the advantages that the special tax regime for inbound expatriates may provide.

Spanish Personal Income Tax

An individual is considered a tax resident in Spain if either of the following two circumstances apply during any given year (tax residency is determined annually):

- he remains in Spanish territory for more than 183 days during a given calendar year (sporadic ab-

sences are disregarded unless the individual proves he is a tax resident of another country); or

- his center of economic interest, whether directly or indirectly, is located in Spain.

Spain applies the principle of worldwide taxation. A resident taxpayer is subject to tax in Spain on his worldwide income. Spain's tax year coincides with the calendar year.

Total tax liability consists of the tax liability computed under the general rules plus any liability applicable in the taxpayer's autonomous community of residence. Tax rates and tax allowances vary depending on the autonomous community. The top marginal tax rates range from 43.5 percent in Madrid to 48 percent in Catalonia or Andalucía. Savings income is taxed at lower rates, varying from 19 to 23 percent. This rate generally applies to dividends, interest, and capital gains derived from the transfer of assets.

Exit taxation may apply to unrealized capital gains. Such gains must be included in the taxable base corresponding to the last year of Spanish residence, unless the taxpayer relocates to another EU member state. When the taxpayer moves to another EU country, taxation generally applies only when the corresponding asset is sold or otherwise transferred. Examples of situations that may trigger an exit tax (upon a move to a non-EU state) include:

- a tax deferral on account of the merger of companies in which the taxpayer is a shareholder;
- a share-for-share exchange under the tax rollover regime (Spain's implementation of the EU mergers directive) allowed for the deferral of taxes; or

- a deferred gain on an installment sale under which income is to be recognized during the years in which installments are received.

Exit taxation also applies to specified shareholdings owned by a taxpayer who moves to another country (except for a move to another EU or European Economic Area country, assuming applicable requirements are met) after residing in Spain for 10 of the past 15 years.

A number of other provisions come into play when an individual is a Spanish tax resident. Spain's controlled foreign company rules apply when the CFC is in a foreign jurisdiction deemed low-tax. Spanish tax residents also have a duty to disclose some assets located outside the country and may incur significant penalties for failing to comply.

Inbound Expatriates Tax Regime

Under Spain's inbound expatriates tax regime (also known as the "inbound expat rules" or "Beckham law"), an individual assigned to work in Spain would incur a lower tax burden than an ordinary Spanish tax resident. The election is subject to a number of conditions, the most important of which may be summarized as follows:

- The individual must not have been a Spanish tax resident in the 10 years preceding the tax year of his arrival to Spain.
- The assignment to Spain must be based on labor reasons. This requirement is fulfilled if the taxpayer has an employment agreement or works as a director of an entity. For the latter, the individual must not hold more than 25 percent of the shares of the company.
- The individual must apply for this special regime within six months of the date on which his labor activity starts in Spain. This six-month period cannot be extended.
- The individual does not generate income deemed to be obtained through a Spanish permanent establishment.

The inbound expat election has a number of tax consequences including a tax on worldwide employment income at a flat rate of 24 percent (which increases to 45 percent for any salary exceeding €600,000 per year). This is in lieu of the progressive tax-resident rates. Spanish-source dividends, interest, and capital gains are subject to a tax rate between 19 and 23 percent. Other Spanish-source income is subject to a flat 24 percent tax under this regime. Foreign-source income, aside from salary, is not subject to Spanish income taxation. Wealth tax applies to Spanish-situs assets.

The inbound expat regime is applicable during the year the individual becomes a Spanish tax resident and the five consecutive years thereafter.

During the years in which a taxpayer is taking advantage of this regime, CFC rules do not apply. Furthermore, the taxpayer need not file the above-mentioned foreign assets declaration, according to the Spanish General Directorate of Taxes in a binding tax ruling. The period to compute tax residence for the exit tax detailed above begins only as of the first year in which the individual is no longer covered by the inbound expat regime.

The table below compares some of the Spanish tax implications that arise if the taxpayer relocates to Spain under the inbound expatriates tax regime versus becoming a Spanish tax resident under the general tax regime.

Taxation Under Inbound Expat Regime Versus Ordinary Tax Resident

Income/Assets	Inbound Expatriate	Ordinary Tax Resident
Dividends and capital gains	No taxation when foreign sourced	Taxed at 19 to 23%
Properties and investments	No taxation if non-Spanish properties/investments	Personal income tax up to 48% and wealth tax up to 3.03% (certain rules and tax rates depending on autonomous community of residence)
Annual reporting of foreign assets (Form 720)	No	Yes, under a very onerous penalty regime
CFC regime	No	Yes
Exit tax	No	Yes, if tax deferral or relevant shareholdings and has been ordinary tax resident during 10 of the last 15 years

