

Setting up your Business in Spain

Issues to consider



Spain is one of the most attractive destinations for foreign investment, offering access to the market of the EMEA region and Latin America. Spain is one of the Top 10 Greenfield FDI destination in Europe in the period 2012-2015. The highly qualified population and a decline in labor costs, together with state-of-the-art infrastructure, make Spain well placed for the future growth of economy, especially as an international centre for innovation.

However there are a number of issues which you must consider when you are looking to set up your business in Spain. This document takes you through some of the common questions we come across and gives you practical information about the issues you need to consider.

What type of Business Structure should we use?

There are advantages and disadvantages to all of them, and there is no one correct answer, it's all dependent on your specific business circumstances and needs. A brief overview of the main structures is below:

Establishment (a branch of your overseas business)

- Not a separate legal entity but an extension of the overseas parent company
- No limited liability or ring-fencing of the Spanish operations
- If have a permanent establishment in Spain then profits from this PE are liable to Spanish Corporation tax
- Must file **parent company accounts**, prepared under Spanish Company Law, at Companies House for public inspection, even if these are not made publically available overseas.

Limited Company:

- Provides limited liability and ring-fencing to Spanish operations.
- Gives a perception of a local business, with longevity.
- Corporation tax to be paid on company profits.
- Companies, must have their annual financial statements audited when two of the below conditions are met for two consecutive years:

	March, 31st
Company Turnover, exceed	5,700,000.00 €
Company Balance Sheet total assets, exceed	2,850,000.00 €
Company average number of employees, exceed	50

Limited Liability Partnership:

- Members (partners) have limited liability
- Profits are allocated to members who then pay Income Tax on these profits personally
- The tax residence of the member, and where the profits in the LLP originated will determine in what jurisdiction and how these profits are taxed



How much Corporation Tax will the business pay?

- **Current Corporation Tax rates in Spain are:**

The Corporate Tax general rate in Spain has been reduced from **28% in 2015** to **25% in 2016**.

For small and reduced-sized companies, up to 2014 there were reduced rates, which have now been eliminated (as the reduction in the general tax rate renders them meaningless), except for a transitory period in 2015, when the rate is 25%, for the profit up to 300.000€ A company is defined as reduced-sized if the turnover of the previous year was less than 10 million€.

A lower tax rate is applicable for newly-formed companies, which applies to the first two years in which it obtains a taxable profit :The rate is 15%.

- **Payment of Company Tax:**

The company tax return must be filed within 6 months and 25 days after end of accounting period.

Payment by instalments of company tax is in April, October and December.

As a general rule, each instalment is 18% of the previous year's company tax liability.

A separate method of calculation, based on the result of the current year, applies to large companies whose turnover in the previous year exceeds a set limit.

- **Calculation of taxable income**

The Starting point is net profit per accounts, calculated in accordance with the General Accounting Plan. Movements in the following provisions are allowable for tax purposes: Doubtful debts, legal expenses, stock obsolescence, devaluation of securities, extraordinary repairs, unsold publications.

There is no distinction between long and short term gains.

Tax losses can be carried forward indefinitely. However a limitation equivalent to 70% of profit is applicable for tax losses compensation exceeding 1 M Eur.

- **Financial expenses:**

Thin - capitalization rules are not applicable. Nevertheless interests derived from participative loans are considered non deductible. Moreover interest payments are deductible with the limit of 30% of the Operating Profits when interest amount exceeds 1M Eur.

- **Disallowable expenses:**

Penalties and fines. Corporation tax payments. Gifts and donations (exception applicable for Non Profit recognised entities).

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- **Group relief:**

A consolidated tax return may be filed if an election is made before start of tax year. Resident companies with a common resident or non resident Ultimate Holding Company are included in the same tax group.

There must be a 75% direct or indirect ownership for whole of both the current and prior tax year.

- R+D Tax credits: this tax credits may be available at a rate of 25% (in certain cases 42%) of the R+D expenses and investments incurred in the tax period. The activity must be carried out in Spain or EU economic area. Additional tax credits can apply in some circumstances and advice should be obtained.

What if we use Spain to set up our holding company?

The Spanish regime for international holding companies compares favourably with traditional European centers. It can provide effective solutions to Groups operating worldwide.

Spain's extensive and growing double taxation treaty network provides substantial leverage in reducing withholding taxes on dividends remitted to a Spanish holding company by a foreign subsidiary located in a double taxation treaty country.

Additionally Main Tax Benefits of Spanish Holding Company are:

- Total exemption for dividends and capital gains realized on the disposal of shares (participation of at least 5% and minimum 10% of Corporate Tax applicable to the subsidiary);
- Absence of withholding tax on distribution of non-Spanish source dividends (ETVEs companies)
- Full deductibility of interest payments (fulfilling certain requirements);
- No capital duty on the issue of share capital for entities established in certain provinces, and on share-for-share contributions;
- Exemption of overseas branch income (provided similar tax paid abroad);

What if we make cross-border transactions between group companies?

Spain follows internationally recognized **Transfer Pricing** (TP) rules where cross-border trading and financial transactions between affiliated entities have to be conducted on an arm's length basis. The price and terms should be the same as if the transactions had been between completely independent parties.

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The Spanish transfer pricing legislation is based on the OECD transfer pricing guidelines and the work of the European Union Joint Transfer Pricing Forum. Although pan-European comparable should be acceptable, in practice the Spanish tax authorities have expressed a strong preference for the use of local comparable whenever possible.

Management fees are deductible if they're at arm's length, and the service yields or may yield a profit to the company receiving the services. This benefit must be proved and documented, together with the substance and reality of the services.

Taxpayers must provide information regarding related party transactions in the corporate income tax return .

Taxpayers should update their transfer pricing documentation on a yearly basis, including all relevant changes in the conditions of their commercial and financial relations in light of the pertinent documentation requirements.

Deadline to submit documentation: The tax authorities may request documentation at any time after the taxpayer files the annual corporate income tax return.

From a strategic perspective, it is preferable to prepare documentation in Spanish. If the documentation is needed as evidence (especially in court), it should be translated into Spanish.

Typical transactions between affiliated entities that are covered by TP regulations are:

- Sale and purchase of goods
- Provision of management services
- Property rental charges
- Transfer of intangible assets e.g. trademarks, patents
- Sharing of knowledge, expertise, business contacts etc.
- Provision of financial support e.g. inter-group loans and charging a "market" interest on loans

A business will need to prepare a Transfer Pricing Report proving the arm's length basis of transactions. The report will include a functional and risk analysis, analysis of the adopted pricing model and benchmarking of the arm's length basis.

A taxpayer may conclude an advance pricing agreement (APA) with the tax authorities that entitles the company to use its proposed method of valuing transactions for four fiscal years.

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The above explained Transfer Pricing Report will not be compulsory in the following circumstances:

- entities that belong to the same Spanish Tax Consolidated group for the operations performed within the Spanish group
- intra-group transactions realized with the same related party with a total volume of less than €250.000 This threshold does not apply for transactions involving intangible assets, transfers of real state, transfers of shares, and entities located in tax havens.

Small-size companies can apply abridged Transfer Pricing Documentation regime.

However even if an entity is exempt from Spain transfer pricing regime it may fall under the scrutiny of the other international tax jurisdictions where it transacts. There may also be other tax regulations which ensure transactions are undertaken at a commercial value.

What Employment Taxes and Social Security will need to be paid?

If an individual is resident in Spain becomes subject to Spanish tax laws.. Taxpayers considered resident in Spain are liable for Spanish tax on their worldwide income.

An individual is considered resident in Spain for tax purposes if: (1) he is present in Spain for more than 183 days in a calendar year: or (2) Spain is the taxpayer’s main center or business base or the place where his professional activities or economic interests are located, either directly or indirectly; or (3) the taxpayer’s spouse and dependent children habitually reside in Spain.

We would advise any new entrant to Spain or person who spends time working in Spain to take professional advice to determine whether they are Spanish tax resident.

Personal Income Tax rates in Spain are:

State tax

From (Euros)	To (Euros)	State tax %
0	12.450	9,50%
12.450	20.200	12,00%
20.200	35.200	15,00%
35.200	60.000	18,50%
60.000	+	22,50%



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Regional tax

From (Euros)	To (Euros)	Regional tax %
0	12.450	9,50%
12.450	17.707,20	11,20%
17.707,20	33.007,20	13,30%
33.007,20	53.407,20	17,90%
53.407,20	+	21,00%

Note: Regional tax rates vary between the different regions of Spain (Comunidades Autonomas). The above rates are valid for region of Madrid.

In regions such as Catalunya and Andalucia the rates for the top tax bands are higher, rising to 48% for the very top band.

Capital Gains Tax Rates

Residents

First 6,000 Euros:	19%
6,000 to 50.000 Euros:	21%
50.000, + Euros:	23%

Non-residents

UE Residents:	19%
Rest:	24%

The personal income tax legislation contains a regime that is very attractive for expatriated staff of multinational companies. An individual who is assigned to work and live in Spain may opt to be taxed as a nonresident for the first six years of the assignment. Under such an agreement, the individual is taxed at a flat rate of 24 % on the gross amount of the income. To qualify for the benefits of the mentioned non-resident taxation regime, the individual must; (1) not have been a tax resident in Spain for the previous 10 years; (2) work in Spain for a Spanish tax resident company or a PE of a non-resident company; (3) not derive tax-exempt income in Spain under the Spanish non-resident income tax law; and (4) not derive more than €600,000 of personal employment income.

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Employers and employees also have to pay Spain social security, which is called Seguridad Social:

Current Social Security rates are:

Percentage of gross paycheck			
Reason for contribution	Employer	Employee	Total
Standard	23,60%	4,70%	28,30%
Unemployment*	5,50%	1,55%	7,05%
Other**	0,8%	0,10%	0,9%

*These percentages may be slightly different depending on your work contract.

**Salary guarantee in case of bankruptcy; professional studies; additional amount based on the employee's professional classification.

Whereas the amount paid by the employee is included in the gross paycheck; the employer contribution is not. So the employer can calculate the total cost of an employee as the gross paycheck + 29,9% (assuming a simple pay slip where the base amount for social security is equal to the gross paycheck).

It is the employers' legal responsibility to pay employee's tax and social security deductions to the Spanish tax authorities. The Social Security contribution rates can slightly vary according to the professional level and type of activity.

Spain has a Reciprocal Agreement with the USA, EU countries and many others whereby when an overseas national of those countries is seconded to Spain for a defined period of time and continues to pay social security in their home country, then the employer and employee are exempt from paying Spain social security.

What is Value Added Tax (VAT) and should the business be registered?

VAT is a "goods and services tax" on supplies made, the standard rate of which is 21%. If a business makes taxable supplies then it **MUST** be registered for VAT.

There are three types of supply

- Taxable – must charge VAT on supplies, can reclaim input VAT
- Exempt – cannot charge VAT nor reclaim input VAT
- Outside the scope – not in the Spanish VAT system

The supply of most types of goods and services in Spain would be classed as Taxable supplies. However when these supplies are made to companies which are outside of the Spanish territory advice needs to be sought as to what rate of VAT, if any, to use.

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If a Spanish entity sells goods or provides services to its non EU parent then there is no VAT chargeable on this overseas supply, however on the basis that the supply would be VAT'able if made in the UE then the entity will be able to reclaim all its input VAT.

Vat taxable entrepreneurs are obliged to submit quarterly VAT returns if annual turnover is less than € 6,010,121.00 or monthly statements if annual turnover is higher than € 6,010,121.00. The presentation of the declaration must be obligatorily by electronic means, for which a digital certificate is required.

Can we provide Share option plans to our staff?

Many companies see Share Option plans as being an important way of attracting, motivating and retaining key staff.

Spain has a number of “approved” share option plans which give tax benefits to employees and employers alike and it is often possible to adapt an overseas stock option plan to fit into one of these “approved” plans.

However this is a very technically complex area and careful planning needs to be undertaken as soon as share option plans are being considered for implementation in Spain.

How else can we compensate our employees?

Spain has a very comprehensive range of compensation and benefit options available for companies to offer their employees.

Pensions, private medical insurance, life and disability coverage are now commonplace benefits provided by many Spanish businesses to their workforce.

Flexible benefit packages are also gaining in popularity, giving employees options on how they wish to “spend” their benefits allowance; which can range from “purchasing” additional holiday entitlement to obtaining full family medical cover.

To discuss your requirements please contact the International Office on +44 (0) 1245 449266 or [email](#) us directly.

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