

Corporate income tax subjects: Spain

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1. General overview of Corporate Income Tax in Spain

The income of legal persons has been taxed in Spain since 1900 when the tax on utilities was approved.¹ The third rate of this tax was applicable to certain corporations and other legal persons. However, it was not until the 1920s that it became a general tax on legal persons.² This primitive corporate income tax was applicable to corporations and other legal persons, taxing their net profits according to a progressive tax rate based on the return the company offered to its equity holders.³ In this respect, this tax could be regarded as a tax on corporate “profitability” rather than a tax on corporate income.

The actual taxation of corporate income or profits was introduced in 1957 when the General Corporate Income Tax was approved.⁴ Since then, the different Corporate Income Tax Acts regulating, firstly, General Corporate Income Tax and later Corporate Income Tax, have followed the same pattern of taxing “income” obtained through corporations rather than profitability or other figures.⁵

Currently, Spanish Corporate Income Tax (CIT) is regulated by the Royal Legislative Decree 4/2004 enacting the consolidated version of the Corporate Income Tax Act (CITA). Although it will be explored in depth in the following sections of this report, not all legal entities are subject to CIT, some forms of partnerships (“sociedades civiles”) to which the look-through approach applies falling outside its application, i.e. it is not legal persons whose income is taxed but rather its members by means of personal or corporate taxes, respectively, according to their ownership interest in the partnership. Other legal persons organized under Spanish legislation apart from these partnerships are subject to CIT on the income they earn.

According to the most recent data, there are approximately 3.2 million enterprises in Spain.⁶ Half of them (nearly 1.65 million) are organized in the form of sole proprietorships, i.e. enterprises owned by individuals, which are not subject to CIT. 1.2 million enterprises are run by corporations, mostly closely held companies or “sociedades de responsabilidad limitada” (nearly 1.15 million), while open corporations (“sociedades anónimas”) only own 0.1 million enterprises. Only the latter form of corporations can be listed on stock exchanges and most of the largest Spanish enterprises are organized under this legal form. The remaining enterprises (0.3 million) are run either by legal entities subject to CIT (around 0.16 million) or by partnerships and other entities not subject to CIT (around 0.14 million).⁷

¹ Cf. Act of 27 March 1900.

² See Act of 19 October 1920.

³ See article 7 of the third rate envisaged by Act of 19 October 1920.

⁴ Cf. E. Santafrotos Gambín, *Breve historia del Impuesto sobre Sociedades en España*, in *Impuesto sobre Sociedades. Régimen General, Tomo I*, pp. 23-42 (p. 30) (Cizur Menor: Aranzadi-Thomson Reuters, 2010).

⁵ Apart from several Acts that amended each corporate income tax Act, since 1957 another four Acts have regulated the CIT or its equivalent tax: Decree 3359/1967; Act 61/1978, Act 43/1995 and Royal Legislative Decree 4/2004.

⁶ Source: Instituto Nacional de Estadística. Directorio Central de Empresas. Base 2012.

⁷ Source: Instituto Nacional de Estadística. Directorio Central de Empresas. Base 2012.

Revenue raised by CIT in Spain has fallen in recent years from 35,254 million euro in 2007 to an estimated 13,383 million euro in 2011.⁸ The main cause for this decrease is the economic crisis, whereas other factors, such as the reduction of the nominal tax rate in 2008, may have influenced this pattern. In 2011 the revenue raised by CIT in Spain only amounted to 8.44% of total revenue, while this figure was 19.08% in 2007.⁹ Similarly, the CIT revenue/GDP ratio has decreased from 3.34% to 1.25% in the same period.¹⁰

Apart from CIT, business activities undertaken by legal entities are subject to a local tax which can be somewhat regarded as a tax on income earned by legal entities (“Impuesto sobre Actividades Económicas”).¹¹ However, the amount of this tax, depends, inter alia, on the nature of the business activity undertaken by the entities and their turnover in the former year, and therefore, it does not directly tax their income.

Since 1968, the foundational aspects of corporate income taxation have not undergone a drastic change. However, there have been some relevant changes which affect the subjective scope of CIT. First of all, although in the 1967 and 1978 corporate income tax Acts, legal personality was a prerequisite for being subject to CIT, in the subsequent Acts regulating CIT passed since 1995, other entities without legal personality such as investment funds and certain joint ventures without legal personality or cooperation agreements, were included within the scope of CIT.¹² This trend has been confirmed in the subsequent amendments to the CITA where more and more entities without legal personality have been included within its scope. On the other hand, in 1998, due to the introduction of the Non-Resident Income Tax (NRIT), non-resident entities ceased to be within the scope of CIT, instead being subject to the new tax.¹³

2. Legislative technique

CIT subjects are defined in article 7.1 of the CITA. This article provides for an exhaustive list of entities which are subject to CIT by means of a mixed legal drafting technique where a general criterion is used together with an exhaustive list of entities subject to CIT.¹⁴

⁸ Source: Agencia Estatal de la Administración Tributaria. Informe anual de recaudación tributaria 2011, p. 44.

⁹ Source: Agencia Estatal de la Administración Tributaria. Informe anual de recaudación tributaria 2011, p. 9 et seq.

¹⁰ Ibid.

¹¹ This tax is regulated in articles 78 et seq. of the Local Finances Act (Royal Legislative Decree 2/2004).

¹² Cf. article 4 of Act 61/1978, where the prerequisite for becoming a subject of CIT was legal personality, and article 7 of Law 43/1995 which included other entities without legal personality within the scope of CIT. Nonetheless, civil law partnerships with legal personality were subject to a look-through approach, despite having legal personality, which created doubts about their possible subjection to CIT. Cf. J.M. Sánchez-Cortés y Alguacil-Carrasco, *Los sujetos pasivos en el Impuesto sobre Sociedades*, in *Impuesto sobre Sociedades*, pp. 251-267 (pp.256-260) (Instituto de Estudios Fiscales: Madrid, 1982). That situation was clarified by Act 48/1985 which expressly excluded civil law partnerships from the scope of CIT. Additionally, before 1995 some entities without legal personality were progressively included within the subjective scope of CIT through specific legislation. Cf. S. Colmenar Valdés, *El sujeto pasivo, residencia y domicilio fiscal*, in *Impuesto sobre Sociedades. Régimen General, Tomo I*, pp. 275-319 (pp. 278-279) (Cizur Menor: Aranzadi-Thomson Reuters, 2010).

¹³ It was Act 50/1998 which introduced the Non-Resident Income Tax as an independent tax.

¹⁴ Cf. J. Almuñá Cid, *Los sujetos pasivos del Impuesto sobre Sociedades*, in *El Impuesto sobre Sociedades* pp. 71-98 (p. 72-73) (Rodríguez Ondarza ed. Madrid: Civitas, 2010, 2nd ed.).

In this respect, it should be noted that the general criterion used by the CITA to define which entities are taxable relies on legal personality. According to this criterion, all (resident) entities with legal personality are subject to CIT with the exception of civil law partnerships (“sociedades civiles”), which are not liable to CIT, it being their members which are liable to tax on income arising from these partnerships. It should be noted that according to the CITA all Spanish resident legal persons, other than civil law partnerships, are subject to CIT irrespectively of whether they carry out commercial activities or whether they have a lucrative goal. Therefore, foundations and associations which do not have a lucrative goal, as well as public bodies, are subject to CIT, although in some cases their income is totally or partially exempt from CIT.

This general criterion coexists with an exhaustive list of certain bodies of persons and entities which do not have legal personality but are liable to CIT, such as investment funds, pension funds or joint-ventures without legal personality.¹⁵ All entities included on this list share two common features: first of all, they do not have legal personality, although they constitute separate assets from the assets of their members; and secondly, all of them are obliged to be listed in official registers. Another feature shared by most of these entities is that they are obliged to keep accounting records under commercial or administrative laws. Although this latter condition is consistent with the Spanish CIT system which relies on commercial accounting as a starting point for the calculation of the tax base,¹⁶ there is no correlation between this requirement and subjection to CIT.

The abovementioned rules are completed with two negative criteria and a list of totally and partially exempt entities. The first negative criterion is envisaged in articles 7.1 and 8 of the CITA and excludes non-resident legal entities from the scope of CIT. Together with this rule, the second negative criterion excludes transparent entities, including civil law partnerships and other bodies of persons from the subjective scope of CIT as long as they are not included in the list envisaged in article 7.1 of the CITA. However, there is an exception to this exclusion relating to a special form of civil law partnership (“sociedades agrarias de transformación”) which, despite being organized under the form of a civil law partnership, becomes subject to the CIT by way of exception from the negative list.

Finally, it should be noted that despite being subject to CIT, some entities are exempt from this tax due to their subjective features. In this regard, article 9.1 provides a list of totally exempt legal persons which includes some public bodies with legal personality, such as the State and its subdivisions, the Bank of Spain and other public organizations; whereas articles 9.2 and 9.3 of the CITA provide an exhaustive list of entities which benefit from partial exemption from CIT, either due to the application of a special tax regime or due to their subjective nature or features. In any case, it should be noted that all these entities have not a lucrative goal irrespectively of their public or private nature.

3. Domestic entities

3.1. Entities subject (and not subject) to CIT

¹⁵ Ibid. (p. 78).

¹⁶ See article 10.3 CITA. On the relationship between commercial accounting and CIT in Spain, see A. Báez Moreno, *Normas Contables e Impuesto sobre Sociedades*, p. 30 et seq. (Cizur Menor: Thomson-Aranzadi, 2005).

According to the abovementioned criteria, the following domestic entities are subject to Corporate Income Tax in Spain, although some of them benefit from partial or total exemption regimes:

1) All entities with legal personality incorporated under Spanish law, except civil law partnerships (“sociedades civiles”). In order to provide an exhaustive list, the following classification of entities can be made:

- a) Entities with commercial purposes: public limited liability companies (“sociedades anónimas”); private limited liability companies (“sociedades de responsabilidad limitada”); partnerships limited by shares (“sociedades comanditarias por acciones”); simple partnerships (“sociedades comanditarias”); general partnerships (“sociedades colectivas”); cooperatives (“sociedades cooperativas”); European economic interest groupings (“agrupaciones económicas de interés económico”, AEIEs); and domestic economic interest groupings (“agrupaciones de interés económico”, AIEs).
- b) Non-profit entities: Foundations (“fundaciones”); associations (“asociaciones”)¹⁷, mutual organizations (“mutualidades”).
- c) Public entities: the State and its territorial subdivisions as well as public institutions and organisms, companies owned by the public sector and other bodies organized under public administrative law with legal personality¹⁸.
- d) Other entities with legal personality: Agricultural transformation companies (“sociedades agrarias de transformación”) and worker-owned companies (“sociedades laborales”)¹⁹.

2) The following entities without legal personality:

- a) Investment funds (“fondos de inversión”)
- b) Temporary groupings of companies (“uniones temporales de empresas”, UTEs)
- c) Venture capital funds (“fondos de capital riesgo”, FCRs)
- d) Pension funds (“fondos de pensiones”)
- e) Mortgage market regulatory funds (“fondos de regulación del mercado hipotecario”)
- f) Mortgage securitization funds (“fondos de titulización hipotecaria”)
- g) Qualifying asset securitization funds (“fondos de titulización de activos”)
- h) Investment guarantee funds (“fondos de garantía de inversiones”)
- i) Joint-ownerships over comunal woodlands (“comunidades titulares de montes vecinales en mano común”)
- j) Banking assets funds (“fondos de activos bancarios”)
- k) Groups of companies under the tax consolidation scheme

3) Entities formed under foreign laws, which are resident in Spain as long as they are not transparent under the criteria analyzed in section 4.2. It should be noted that according to Spanish domestic legislation, an entity is resident in Spain if any of the following criteria is met:

¹⁷ Apart from associations, this category includes other associative forms; inter alia, sport clubs and associations; religious associations, labor unions, political parties or professional associations.

¹⁸ This last category includes, inter alia, the following public business bodies (“entidades públicas empresariales”); State agencies (“agencias estatales”); local consortia (“consorcios”); fishermen guilds (“cofradías de pescadores”); watering associations (“comunidades de regantes”) and compensation boards (“juntas de compensación”). Cf. J.A. López-Santacruz Montes, *Memento práctico. Impuestos sobre Sociedades 2012*, §85 et seq. (Francis Lefbvre: Madrid, 2012).

¹⁹ This is a special form of company that can be incorporated as a public limited liability company or as a private limited liability company according to Law 4/1997.

- a) It is organized under Spanish laws
- b) Its registered office is located in Spain
- c) Its place of effective management is located in Spain

It is clear that in cases where a tax treaty is applicable, as most Spanish tax treaties follow the OECD model, it is the last criterion which will be of relevance for the purpose of the application of tie breaker rules provided in article 4.3 of the relevant tax treaty. Additionally, an anti-abuse rule is envisaged in cases where the main assets of a company established in a tax haven are directly or indirectly located in Spain. In these cases, the company will be deemed as being a resident in Spain unless it provides evidence that its place of effective management is located in the tax haven and that the structure is based on valid commercial reasons.²⁰

On the other hand, as mentioned earlier, civil law partnerships with legal personality are expressly excluded from the subjective scope of CIT, irrespectively of whether they perform commercial activities, as well as all other entities without legal personality not expressly included within the list of entities subject to CIT (for instance, states or joint- and co-ownerships).

3.2. Rationale for the inclusion and exclusion of entities within the scope of CIT. Link between company law and tax law

As mentioned earlier, the basic criterion for the inclusion of entities within the scope of CIT is legal personality. However, this criterion is not followed in all cases as some entities with legal personality are not subject to CIT and some entities without legal personality are subject to CIT. Although the reason for the inclusion and exclusion of some entities within the subjective scope of Spanish CIT is not clear,²¹ the exclusion of civil law partnerships seems to be related to the lack of publicity and accounting obligations for these entities under Spanish legislation. This factor also seems to be relevant with respect to the inclusion of entities with and without legal personality within the scope of CIT, due to the fact that it is compulsory for all these entities to be recorded in official registers.²² However, although it is necessary, this requisite does not

²⁰ Cf. article 8.1 of CITA.

²¹ For instance, with regard to entities subject to CIT, but without legal personality, Almudí Cid, *Los sujetos pasivos del Impuesto sobre Sociedades*, in *El Impuesto sobre Sociedades*, pp. 71-98 (p. 79) argues that they share the common feature of grouping investments of a plurality of investors with exception of the case of temporary groupings of companies. Another criterion often used for the inclusion or exclusion of companies is based on the existence of a commercial goal. Cf. J.M. Tejerizo López, *Los sujetos pasivos en el Impuesto sobre Sociedades*, in *La Reforma del Impuesto sobre Sociedades*, pp. 89-123 (p. 97). This criterion was used by the Spanish Central Tax Appeal Board (“Tribunal Económico-Administrativo Central”) in its ruling of 9 February 2000 (ref. 00/3911/1996) to reclassify a (professional) general partnership as a civil law partnership for the purposes of regarding it as a transparent entity which is therefore not subject to CIT. However, this ruling refers to legislation prior to 1995.

²² See E. García Antón, *El sujeto pasivo en el Impuesto sobre Sociedades*, in *Manual del Impuesto sobre Sociedades*, pp. 85-106 (p. 89) (Instituto de Estudios Fiscales: Madrid, 2003); A López Díaz, *Impuesto sobre sociedades: Sujetos pasivos. Entidades exentas*, in *Estudios sobre el Impuesto sobre Sociedades*, pp. 29-84 (p. 53) (Comares: Granada, 1998) regarding the inclusion of agricultural transformation companies within the scope of the CIT although they are civil law partnerships since they acquire legal personality after being registered. The same is true of funds (investment funds, pension funds, etc.) included within the scope of CIT, temporary grouping of companies, associations, foundations, commercial companies or joint-ownerships over communal woodlands. The only exception, which is groups of companies, does not distort this conclusion since all the members would comply with the registration obligation.

seem to be sufficient for the inclusion of entities without legal personality within the subjective scope of CIT.

On the other hand, accounting obligations, although relevant for practical reasons, cannot be regarded as a decisive factor for the inclusion or exclusion of entities. In this respect it should be noted that some of the entities subject to Spanish CIT are not obliged to keep accounting records under commercial or administrative law.²³ Instead these obligations come directly from tax legislation, as CITA expressly obliges entities subject to this tax to fulfill accounting obligations.²⁴

Transparency for tax purposes of entities not subject to CIT has been purported as a mechanism to strengthen the information obligations of the members and partners of these entities.²⁵ This seems to be consistent with the publicity requirement relating to the recording of entities in public registers since civil law partnerships do not need to be registered or keep accounting records, of the consequence of which is the lack of registration (irregular companies) examined in supra 3.3.

In any case, it should be highlighted that company or civil law aspects are crucial for the inclusion of an entity within the scope of CIT given that all entities with legal personality, excluding civil law partnerships, are subject to CIT, irrespectively of the limited or unlimited assumption by its members or shareholders of liabilities arising from the entities. Also irrelevant for the purposes of subjection to CIT is the fact that a company has a sole shareholder. On the other hand, entities within the subjective scope of CIT cannot opt out for the application of CIT or be deemed to be outside its scope. Therefore corporations formed under Spanish laws are always subject to CIT, whereas transparent entities cannot opt in for the application of CIT.

3.3. Other issues raised by CIT subjects: Charitable organizations, silent partnership, irregular companies and state-owned entities and group taxation

Therefore, as the fundamental criterion for the inclusion of entities within the scope of CIT is legal personality, the charitable status of an entity does not have implications on whether the entity is subject to CIT (see supra 4 with respect to cross-border issues related to the subjection to CIT). However, such status is relevant for the purpose of determining whether to apply total or partial exemptions.²⁶ Similarly, no specific issues are raised with respect to whether entities owned by the State or its subdivisions are subject to CIT, as they are all subject to this tax.

²³ Some of the subjects to Spanish CIT are not obliged to keep accounting records under commercial or administrative law. This is the case of joint-ownerships over communal woodlands, which were included within the subjective scope of CIT by Law 50/1998, and are obliged to keep accounting records by CITA but not by other pieces of legislation. See R.I. Fernández López, *Régimen Tributario de las Comunidades de Montes*, pp. 138-139 (Madrid: Iustel, 2006). The same is true in the case of temporary groupings of companies. See ruling no. 6/2011 of the Institute of Accounting and Accounts Auditing (“Instituto de Contabilidad y Auditoría de Cuentas”).

²⁴ Cf. article 133.1 CITA.

²⁵ Cf. D. Carbajo Vasco, *El régimen de atribución de rentas tras la última reforma del Impuesto sobre la Renta de las Personas Físicas*, p. 15 et seq. (Instituto de Estudios Fiscales. Documentos: Madrid, 2003). Additionally, it should be noted that the preface to Law 48/1985 did not make any explicit reference to the need to treat civil law partnerships with legal personality as transparent entities.

²⁶ See in this respect, the report elaborated by A. Báez Moreno and J. Pedreira Menéndez for the 2012 EATLP Congress (Taxation of charities in Spain).

With respect to other issues relating to CIT subjects, the following aspects are of significance. Silent partnership agreements (“contratos de cuentas en participación”) are not subject to CIT, as these contracts involve an entrepreneur providing funds for the activities run by another entrepreneur without setting up a legal person or a partnership without legal personality under civil or commercial law. In these cases, income earned by the silent partner is taxed as interest given that this partner’s own capital is being loaned to the general partner for the purposes of running the latter’s business.²⁷

Moreover, companies in process of incorporation (“sociedades en formación”) and irregular companies (“sociedades irregulares”) are not subject to CIT since they do not have legal personality under commercial law²⁸. Consequently, for the period that a company is considered to have the above referred to status, it is treated as transparent from a fiscal point of view.²⁹

Finally, with regards to group taxation, although groups of companies taxed under the special consolidation scheme regime are considered to be subject to CIT, member companies retain their full tax personality, being obliged to fulfill their individual formal obligations, i.e. reporting their individual CIT returns.³⁰ The parent company will be responsible for fulfilling group obligations, including the consolidated tax return.³¹

3.4. Consistency between domestic classification of CIT subject and EU Directives

It should be noted that the list of entities subject to Spanish CIT might be not fully consistent with the lists included in the annexes to the Parent-Subsidiary, Interest-Royalty and Merger Directive as well as the annex included in the Draft CCCTB Directive. In any case, the compliance of the list of entities subject to Spanish CIT with these annexes must be examined on a case-by-case basis, as the list included in the annex of the Parent-Subsidiary Directive differs from the lists included in the annexes to the other Directives.³²

- a) In regard to the Interest-Royalty directive³³, paragraph e) of the annex provides that the following entities formed under Spanish law will benefit from the

²⁷ Cf. the ruling of the Spanish Tax Agency (“Agencia Estatal de la Administración Tributaria”) of 24 March 1997.

²⁸ The concept “sociedad en formación” refers to the period between the issuing of the company’s charter of incorporation (“escritura de constitución”) and the date on which the charter is registered with the commercial registry (“Registro mercantil”). A company becomes a “sociedad irregular” when its partners decide to not register the charter with the commercial registry or when one year has passed since the charter of incorporation was issued without the partners having requested the registration of the charter in the “Registro mercantil”. See articles 33 and 36-40 of the Royal Legislative Decree 1/2010, which approves the consolidated version of the Corporate Enterprises Act.

²⁹ See sections 3.5 and 4.2 of this report, the judgment of the Spanish Supreme Court (“Tribunal Supremo”) of 3 July 2012, appeal n° 6349/2009 and J. Almodí Cid, *Los sujetos pasivos del Impuesto sobre Sociedades*, in *El Impuesto sobre Sociedades* pp. 71-98 (p. 74) (Rodríguez Ondarza ed. Madrid: Civitas, 2010, 2nd ed.).

³⁰ Cf. article 65.3 CITA.

³¹ Cf. article 65.2 CITA.

³² It should be noted that the proposed Directive amending the Interest and Royalty Directive [COM(2011) 714 final] aims to expand the list of Spanish entities to which the Directive is applicable in the same terms as the Parent-Subsidiary Directive.

³³ Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States.

application of the Directive: “companies under Spanish law known as: “sociedad anónima (public limited liability companies), sociedad comanditaria por acciones (partnerships limited by shares), sociedad de responsabilidad limitada (private limited liability companies)” and those public law bodies which operate under private law”. Therefore, only some of the entities with legal personality subject to the Spanish CIT are covered by the Directive. The lists of entities included in paragraphs j) of Annex I, part A, of the Draft CCCTB Directive³⁴ and Annex I, part A of the Merger Directive³⁵, mirror the abovementioned list. With respect to the inclusion of the three classes of entities with commercial purposes, the main reason for their inclusion, and the non-inclusion of other entities, seems to lie in the possible disparities in the characterization of entities between member states that would otherwise occur.³⁶ In this respect, it should be noted that the three classes of domestic entities included in the annexes to the Directives (and the draft CCCTB Directive) could be regarded as corporations due to their features (separate legal personality, capital divided into shares, limited liability of the shareholders and delegated management) with commercial purposes. Thus, they will not raise cross-border characterization problems, at least prima facie. Other entities organized under Spanish domestic legislation might easily give rise to characterization problems due to the fact that their features are not those of a corporation (for instance their members have non-limited liability) or they do not have a commercial purpose.

With respect to public law bodies which operate under private law, it must be noted that the reference to this category seems to be reminiscent of the domestic classification of public sector entities prior to 1997 when a dramatic restructuring of the public sector occurred due to the approval of Law 6/1997. Nonetheless, as this reference was included in the two 1990 Directives and then maintained in the subsequent amendments to both directives as well as in the Interest-Royalty Directive and the draft CCCTB Directive, it must be assumed that the reference does not necessarily correspond to the domestic classification of public sector entities. In this respect, the current classification of Spanish public sector entities refers to public business bodies (“entidades públicas empresariales”) as public bodies which operate under private law.³⁷ However other public entities such as public foundations might also operate under private law to a certain extent.³⁸

However, interpretation of this clause according to this criterion would give rise to some issues as private foundations would not be covered by the subjective scope of the directives. In the authors’ view, the criterion for interpreting this clause must be based on operational aspects. In this respect, it must be noted that

³⁴ COM(2011)121/4 Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB).

³⁵ Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States.

³⁶ Cf. J.M. Calderón Carrero; A. Martín Jiménez, *La Directiva fusiones, escisiones, aportaciones de activos y canjes de valores entre sociedades de diferentes Estados Miembros*, in *Convenios Fiscales y Fiscalidad de la Unión Europea*, pp. 1.325-1.380 (p. 1.341) (CISS: Valencia, 2012).

³⁷ Cf. article 53.2 of Law 6/1997.

³⁸ See articles 44-46 of Law 50/2002.

public business bodies as well as other public bodies are subject to CIT, but the latter are exempt from this tax, while public business bodies are not.³⁹ As the application of each Directive requires the entities within their subjective scope to be subject to CIT without the possibility of being exempt, a purposive interpretation of the reference included in the respective annexes, would lead to the conclusion that only public business bodies are included within the list included in the annexes. This interpretation would be consistent with the exclusion of, inter alia, private foundations and associations, from the list, as long as these entities might benefit from total or partial exemption from CIT.

- b) With regard to the Parent-Subsidiary Directive, paragraph j) of Annex I, part A, provides for the inclusion of the following entities: “companies under Spanish law known as: ‘sociedad anónima’, ‘sociedad comanditaria por acciones’, ‘sociedad de responsabilidad limitada’ and public law bodies which operate under private law. Other entities constituted under Spanish law are subject to Spanish corporate tax (‘Impuesto sobre Sociedades’)”. The latter addition to the list was made in 2003 with the purpose of enlarging the subjective scope of the Directive. Due to this amendment, the subjective scope of the Directive mirrors the subjective scope of Spanish CIT, as the reference is made to “entities” and not companies or other terms that would have limited its scope to entities with legal personality. Therefore all domestic entities subject to CIT, irrespectively of whether they have legal personality, will benefit from the application of this Directive.⁴⁰

Despite the lack of inclusion of some domestic entities within the scope of the lists included in the annexes to the Directives, it should be noted that domestic legislation implementing these Directives extends the application of the benefits of the Directive to more entities than those included in the annexes.

3.5. *Partial implementation of CIT*

In Spain entities cannot opt in or out for the application of either CIT or a transparent regime (so-called in Spain “regimen de atribución de rentas”). Thus, *all CIT subjects* are not allowed to opt out in order to be treated as transparent entities. At the same time, *all transparent entities* cannot opt to be treated as opaque. This general rule applies both to Spanish and foreign entities.⁴¹

Spanish legislation envisages a full transparency regime. Look-through entities are fully disregarded and, therefore, are not totally or partially subject to CIT. The income of the transparent entity is taxed at the hands of its partners or members.⁴² However, there are

³⁹ See, for instance, the ruling of the General Directorate for Taxation (“Dirección General de Tributos”) of 31 July 2002 (ref. 1162/2002).

⁴⁰ Cf. J.M. Calderón Carrero; A. Martín Jiménez, *La Directiva relativa al sistema común de imposición aplicable en el caso de las sociedades matrices y filiales de diferentes Estados Miembros*, in *Convenios Fiscales y Fiscalidad de la Unión Europea*, pp. 1.239-1.287 (p. 1.244) (CISS: Valencia, 2012).

⁴¹ The criteria under which foreign entities are treated as transparent or opaque in Spain will be analyzed in section 4.2.

⁴² Before being attributed to the members of the entity, income is calculated at the entity’s level according to the rules envisaged in the Spanish Personal Income Tax Act (PITA), regulated by Law 35/2006. However, when all the members of the entity are subject to CIT or to the Spanish Non-Residents Income Tax (NRIT) as non-resident taxpayers with permanent establishment (PE) in Spain, the entity’s income is

a few exceptions to this general rule, which affect both some Spanish entities subject to CIT and some foreign entities classified as transparent under domestic law.

AEIEs (European economic interest groupings) and AIEs (Spanish economic interest groupings) have legal personality and are subject to Spanish CIT (see section 3.1). UTEs (temporary groupings of companies) are also subject to CIT even though they do not have legal personality.

AIEs and UTEs are subject to CIT but are taxed under a partial transparency regime, according to which the AIE/UTE is not taxed on the part of the taxable income attributable to the Spanish resident members in proportion to their share. Losses of an AIE/UTE may be imputed to its Spanish resident members. This transparency regime does not affect non-resident members, the AIE/UTE being taxed on such income while the non-resident members are taxed only upon distribution. On the contrary, AEIEs are subject to full transparency. Therefore, an AEIE's income is taxed at the hands of its members, regardless of whether they are resident or non-resident in Spain.

In relation to foreign entities classified as transparent according to Spanish domestic law (see section 4.2), the Spanish Non-Residents Income Tax Act provides two different tax regimes. Article 38 and 39 of the NRITA distinguishes between foreign transparent entities with presence (“entidades con presencia en territorio español”) and without presence in the Spanish territory (“entidades sin presencia en territorio español”).

Foreign look-through entities *without presence* in the Spanish territory are fully transparent. The entity's income is attributed to its members. Spanish resident members are taxed under the PIT or the CIT depending on whether they are individuals or entities subject to CIT. Non-resident members are subject to NRIT as non-residents without PE and can claim the benefits envisaged in the corresponding tax treaty.

On the other hand, foreign look-through entities *with presence* in Spain are subject to a partial transparency regime. Before explaining how this regime works, the meaning of “presence in the Spanish territory” should be briefly clarified. This concept is similar, but not equivalent, to the concept of PE provided in article 5 of the OECD Model and article 13.1 of the NRIT. According to article 38.1 of the NRITA, a foreign transparent entity has presence when it habitually carries on an economic activity in Spanish territory, wholly or partly, through installations or places of work, or through an agent who is authorized to conclude contracts on behalf of the entity.

When a foreign look-through entity has presence in Spain the entity itself is not subject to CIT but is subject to NRIT. However, it is a partial transparency regime to the extent that it only affects the part of the income attributable to non-resident members Spain. This income is calculated at the entity level according the PITA rules and the tax due must be paid by the entity at a tax rate of 30%-. On the other hand, income attributable to resident members in Spain is taxed at their own hands; thus it is not the entity itself which is subject to taxation for that part of income.

calculated according the CITA (see article 89.1 PITA). The NRIT is regulated by Royal Legislative Decree 5/2004.

As has been shown, a particular feature of this regime is that the entity is subject to the Non-Residents Income Tax and not to CIT, as opposed to in the cases of AIEs and UTEs. At the same time, it is noteworthy to point out that in this regime the non-resident members of the look-through entity are not completely disregarded. There is a possibility that these members reside in a country which has concluded a tax treaty with Spain, and this treaty may exclude or lower the tax liability faced in Spain by the member through the entity, especially when the Spanish concept of "presence" does not give rise to a PE according to the tax treaty. If this were the case, article 38.4 of the NRITA entitles the member to request a total or partial refund of the tax paid by the entity in proportion to his or her share in the entity's income.

3.6. Tax planning

Generally, the differences between the fiscal benefits of setting up a corporation rather than a partnership are not significant, since almost all Spanish partnerships are subject to CIT. In fact, from the point of view of civil and commercial law, it would make little sense to invest through one of the few Spanish transparent entities, since the partners are personally liable for the debts of the entity –nevertheless, the later also occurs with certain Spanish partnerships subject to CIT (“sociedad colectiva” and the general partners of the “sociedad comanditaria”). From this point of view, investors probably would prefer to invest through Spanish limited liability companies, even though they are subject to CIT without exception. However, there are at least certain advantages to using a transparent entity, especially when the partners are individuals resident in Spain.

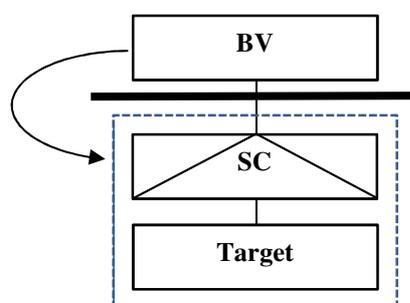
If the entity's income is taxed directly at the hands of its members, economic double taxation will be avoided. This is relevant in Spain because the current method for mitigating this phenomenon in the case of individual shareholders is to exempt dividends up to 1,500 euros per year from PIT. Any excess is taxed according to the rates envisaged in the following chart –additionally, it should be noted that dividends cannot be offset against negative income, except for certain income from movable assets (interest and life insurance proceeds):

Income bracket (EUR)	Tax Rate
0 – 6,000	21 %
6,001 – 24,000	25 %
24,001 +	27 %

Moreover, transparent entities could be useful because transfer pricing rules would not be applicable, at least in the case of transactions between the entity and its members. Finally, when an investment generates negative income in its first stage, a member of a transparent entity can offset those negative results against his own positive income (if any) from other sources⁴³. The latter is not possible when the entity is opaque, unless group taxation is allowed. In Spain group taxation is only applicable to companies of the group subject to CIT.

⁴³ However, article 89.1.3° PITA restricts the deduction of negative income obtained by the look-through entity in a country or territory that has not signed a tax treaty with an exchange of information clause with Spain. Negative income may only be offset against positive income derived in the same country. Any excess may be carried forward for 4 years to be offset against any positive income from the said countries.

From the point of view of international tax planning, there may be some additional advantages to using look-through entities, especially when investing in Spain. A usual practice has been for foreign investors to acquire or finance business in Spain using partnerships which are subject to CIT according to Spanish domestic legislation, but regarded as transparent entities in the state where the members are resident. This tax planning model based on the use of hybrid entities looks as follows⁴⁴:



In this scheme, a Dutch “besloten vennootschap” (BV) loans money to its Spanish subsidiary, incorporated as a “sociedad colectiva” (SC). The SC is subject to Spanish CIT but it is transparent in the Netherlands according to Dutch tax laws⁴⁵. Therefore, the loan granted by the Dutch company to SC should be disregarded for Dutch tax purposes and thus the interest received by BV from SC does not constitute taxable income in the Netherlands. In Spain the interest paid by SC to BV is treated as a deductible cost for Spanish tax purposes and because the SC is part of a fiscal unity together with the target company, the loss of SC can be offset against the profit of the target company. SC uses the loan either to acquire the shares of the target company or to contribute to its capital.

3.7. Others

Entities subject to CIT have significant formal obligations. However, there are no noteworthy differences between these obligations and those of individuals and transparent entities, both national and foreign, which undertake economic activities. Hence, from this point of view, formal and procedural obligations are similar.

The Spanish CIT envisages several special regimes that are not applicable to individuals or look-through entities. From this point of view, the use of an entity subject to CIT instead of a transparent entity could be justified in some scenarios.

Moreover, for some economic activities, Spanish legislation provides a regime where taxable income is assessed on a lump-sum basis to a certain extent (e.g. bars, certain restaurants, hairdressing salons, taxi services, pharmacies or carpenters). In this scheme, known as “estimación objetiva”, the net income is calculated by reference to the standards set out by the Ministry of Finance for the listed activities (e.g. area of premises, employees, tables, kW consumption, km driven per year for taxis, gambling machines, all multiplied by a notional amount per year). This regime could be very beneficial, particularly when the real income arising from the activity is much higher than the amount resulting from the application of the official standards. This tax scheme

⁴⁴ Cf. R. Russo, *Fundamentals of International Tax Planning*, pp. 135-136 (Amsterdam: IBFD, 2007).

⁴⁵ Cf. F. Snel & C. Mas, *The Classification of Partnerships for Tax Purposes: A Comparative Analysis (Netherlands/Spain)*, *European Taxation* 10, pp. 367-376 (p. 375) (2003).

is only applicable to individuals resident in Spain, and therefore, it is not applicable to entities subject to CIT, even though they carry out activities included in that list⁴⁶. Transparent entities are not eligible for this tax regime, unless all of its partners are individuals resident in Spain.

4. Cross-border situations

4.1. Legal background

From a Spanish point of view, as other countries, the first question arising in relation to a foreign entity is whether the taxpayer of the income obtained through the entity is the entity itself or its partners. Therefore, foreign entities must be classified in order to establish if they are transparent or opaque. This important decision is not only relevant to the entity itself, but also to its partners and members. Thus, for example, if a partner of a foreign transparent entity is a resident in Spain, the income attributable to this partner will be taxed fully upon being earned, regardless of whether the entity's income has been effectively distributed or not. On the contrary, when a foreign entity is characterized as a taxable entity (i.e. opaque, non-transparent, subject to CIT, etc.), taxation on the Spanish partners will be deferred until distribution.

Until the approval of Law 46/2002, Spanish legislation did not envisage statutory rules on foreign entity classification.⁴⁷ Before the aforementioned law was passed, the classification fundamentally rested on certain administrative rulings and academic literature. Firstly, the situation prior to Law 46/2002 is briefly explained and afterwards the method provided by this Law is studied in depth. Before 2002, the criteria used to classify foreign entities changed over time. However, the method currently envisaged in the law is more controversial, especially because it is not clear if it establishes a "resemblance test" (i.e. the foreign entity is opaque provided that its features are comparable to those of a domestic CIT subject) or a different method to classify foreign entities.

Legal scholars have considered the method for categorizing foreign entities used by the Spanish tax administration until the entry into force of the 1978 CITA (Law 61/1978) to be the following: all entities formed under the law of another state are opaque regardless of their individual characteristics, i.e., all foreign bodies are taxed as corporations.⁴⁸ The 1978 CITA switched from the former method to one based on the legal personality of the entity. A foreign entity was classified as opaque if it had legal personality under the law of its incorporation. This method relied on international private law to determine whether or not the foreign entity had legal personality. Nevertheless, during this period

⁴⁶ However, the CITA envisages a sort of lump-sum regime for shipping companies managed and registered in Spain, since they may elect to be taxed under a tonnage tax regime in respect of ships used primarily for international transport. Under the tonnage regime, the calculation of the taxable income is based on the net tonnage per qualifying ship. See articles 124-128 CITA.

⁴⁷ Cf. A. Delgado, *Las entidades en atribución de rentas y el régimen fiscal de partnerships y trusts en España*, in *Manual de fiscalidad internacional* pp. 479-536 (p. 480) (Cordón Ezquerro ed. Madrid: Instituto de Estudios Fiscales, Vol. 1, 2007, 3rd ed.).

⁴⁸ See, among others, A. Gota Losada, *Tratado del Impuesto sobre Sociedades* p. 69 (Madrid: EXTECOM, 1988); J.M. Calderón Carrero, *Tax Treatment of Partnerships Under U.S.-Spain Tax Treaty*, 17 *Tax Notes International* 16, pp. 1205-1209 (p. 1206) (1998); F.A. Vega Borrego, *Entidades extranjerías e impuestos sobre la renta: ¿Quién es el contribuyente?*, *Revista de contabilidad y tributación* 259, pp. 3-30 (p. 11) (2004).

the method applied in practice by the Spanish administration was the same as the method using during the first period (-1978), since in practice foreign entities were not required to give evidence of their legal personality in accordance with the law of the state of incorporation.⁴⁹

The second period (1978-2002) ended with the entry into force of Law 46/2002. The submission to the Spanish Parliament (“Cortes Generales” which is composed of two bodies, the Congress and the Senate) of the draft bill that led to the approval of the aforementioned could be considered the first official time that this important matter was expressly dealt with in law. The draft bill envisaged a concept of foreign transparent entity (“entidad extranjera en régimen de atribución de rentas”) whose purpose was precisely to determine if the entity’s income should be taxed at the entity or at the partners’ level. The method was applicable to all entities established, formed or incorporated under a foreign law and followed a clearly tax-oriented approach, as the classification was based on how the entity was treated for tax purposes in its state of establishment, formation or incorporation. If the entity was considered to be opaque in that state, Spain would treat the entity likewise, and vice versa, i.e. if the entity was transparent according to tax law in the state of origin, it would also be included under this regime in Spain. During the discussion of the draft bill in the Congress, the rule was modified for the purpose of making it even clearer that the classification method followed the aforementioned tax oriented approach. However, the draft bill was significantly modified during its discussion in the Senate and the original version of the rule was replaced by the following wording: *foreign entities whose nature is similar or identical to the nature of Spanish transparent entities will be treated as transparent entities for Spanish income tax purposes.*

This is the wording of the rule finally passed by the Spanish Parliament and it has remained unchanged since then, even though Law 46/2002 has been already repealed. Currently the rule is envisaged in article 87.1 of the PITA and article 37 of the NRITA.

4.2. The current method used in Spain for classifying foreign entities: a resemblance test or a tax-oriented approach?

The wording of the Spanish statutory rule seems to establish a similarity or resemblance test approach. Therefore, whether to treat foreign entities as transparent or opaque for tax purposes in Spain, is decided by means of their comparison to Spanish entities. This comparison is made by first examining the legal characteristics of the foreign entity, taking into account the general law (civil and/or commercial) governing that entity, which is normally the law of the state where the entity was established, formed or incorporated. As in the case of other countries, it is not clearly stated whether or not it is necessary to assess also the entity’s charter of incorporation and/or articles of association. Furthermore, the Spanish rule does not expressly establish which features of the foreign entity should be given the most priority for the purpose of this analysis. Legal scholars have pointed out that, inter alia, the following features should be examined: whether the entity has legal personality separate from that of its members; whether the assets are jointly owned by all its members; whether at least some of the members act as managers of the entity; whether profits are accrued directly by the members (i.e. no need for a formal decision to distribute profits); and, whether the

⁴⁹ Cf. A. Gota Losada, *Tratado del Impuesto sobre Sociedades* pp. 69 and 89-90 (Madrid: EXTECOM, 1988).

members are held personally liable for the debts of the entity to third parties⁵⁰. Once the features of a foreign entity have been determined, it will be compared with Spanish entities in order to establish to which one it resembles the most. Finally, the foreign entity will be treated as opaque or transparent depending on the regime applicable to the comparable Spanish entity.

According to this method, foreign entities will be treated as fiscally transparent provided that their legal features are comparable to any of the Spanish transparent entities, which, as pointed out in section 3.1, are the following: civil law partnerships (“sociedades civiles”), estates (“herencias yacentes”), co-ownerships (“comunidades de bienes”) and other entities without legal personality which constitute an economic unity or separated taxable patrimony (“entidades carentes de personalidad jurídica que constituyan una unidad económica o un patrimonio separado susceptibles de imposición”), excluding Spanish entities without legal personality expressly subject to Spanish CIT (investment funds, temporary groupings of companies, venture capital funds, etc.).⁵¹ On the contrary, a foreign entity will be classified as opaque if its essential legal features are similar to those of a Spanish entity subject to CIT (e.g. a foreign entity similar to a Spanish “sociedad colectiva” will be considered opaque because this entity is subject to CIT).

In practice, applying this method has become quite complex, inter alia, for the following reasons: the Spanish statutory rule does not establish which factors are of importance for the resemblance test. Similarly, sometimes it may be impossible to determine which Spanish entity is comparable to the foreign one. In this case, the rule does not envisage any residual criterion for the purpose of deciding which tax treatment should be given to foreign entities that are not comparable or similar to any entity in Spain. Lastly it should be highlighted that, unlike other countries, the Spanish tax administration has not published any general guidelines or lists on foreign entity classification.⁵²

Spanish scholars have pointed out the significant problems raised by the application of purely legal comparison method for the purpose of classifying foreign entities. In this respect, most authors have highlighted that when this comparison takes place, in addition to the legal characteristics of the foreign entity, it is also possible to take into account the tax treatment of the entity in its state of origin.⁵³ Thus, in this comparison both legal and tax features of the foreign entity would be taken into account. In this regard, for the purpose of determining whether the entity is transparent or opaque in Spain, relevance will be placed on the tax treatment of the entity in its home country,

⁵⁰ Cf. J.A. Bustos & F.J. Sánchez & F.J. Seijo, *Comunidades de bienes*, p. 24 (Madrid: Francis Lefebvre, 2004). Under this method, in principle, whether or not the foreign entity is regarded as transparent or opaque in its home country is not decisive for the purpose of classifying the entity. However, as will be shown below, this is the feature which has been given the most relevance by the Spanish tax administration.

⁵¹ See section 3.1 of this report.

⁵² Cf. R. Amman, *German tax guide*, pp. 1022-1145 (The Hague: Luschterhand/Kluwer Law International, 1999); J. Barenfeld, *Taxation of Cross-Border Partnerships*, pp. 115-116 (Amsterdam: IBFD, 2005); R. Rademakers & M. Swets, *New Decrees on the Classification and Tax Treatment of Foreign (Hybrid) Entities in the Netherlands*, European Taxation 5, pp. 171-179 (2005).

⁵³ See, among others, A. Rodríguez Vegazo, *El régimen de atribución de rentas tras la Ley 46/2002*, Carta Tributaria 15, pp. 1-28 (p. 24) (2003); L. Ruibal Pereira, *La tributación de las rentas obtenidas por las entidades en atribución de rentas*, p. 54 (Cizur Menor: Aranzadi, 2003); A. Mosquera Mouriño, *Régimen de atribución de rentas: especial referencia a las actividades económicas*, Carta Tributaria 4, pp. 3-16 (p. 5) (2012).

and as will be shown below, this feature has been given the utmost relevance in practice, at least in view of the rulings handed down by the Spanish tax administration since Law 46/2002 entered into force.

So far, the Spanish courts have not issued any judgment on how to interpret the statutory rule for classifying foreign entities as transparent or opaque for tax purposes. Additionally, only a few administrative rulings have been handed down by the Spanish General Directorate for Taxation (“Dirección General de Tributos”) in reply to written queries made by taxpayers. With respect to the latter, it is noteworthy to highlight that the Spanish tax administration makes its decision taking into account exclusively the information about the foreign entity’s features provided by the taxpayer in its written query. Indeed, the tax administration does not make any inquiry to ascertain the foreign entity characteristics as part of the procedure for answering written queries. Therefore the ruling is handed down taking into account exclusively the information provided by the taxpayer. In their queries it is usual for taxpayers to set forth the main legal features of the foreign entity and its tax treatment as opaque or transparent in its state of establishment.

Hereinafter the cases where the Spanish tax administration has issued a ruling are studied. As a general remark, it should be noted that all rulings follow the same pattern: they replicate the legal and fiscal features provided by the taxpayer in its query and immediately state whether the entity is opaque or transparent, but without making any reference to which Spanish entity is comparable to the foreign one. As it will be shown, the criterion that appears to be weighed the most is the entity’s tax treatment in its home country. This explains why many foreign entities have been classified as transparent despite the fact that their Spanish comparable entity is subject to Spanish CIT.⁵⁴

The ruling of 22 April 2003 (ref. V0037-03) of the Spanish General Directorate for Taxation refers to a “Closed Commanditaire Vennootschap” (CV) incorporated in the Netherlands. Given the legal features of this Dutch entity it should have been concluded that the comparable Spanish entity was the “sociedad comanditaria”. Hence, the ruling should have stated that the CV was opaque in Spain, to the extent that the Spanish “sociedad comanditaria” is subject to CIT.⁵⁵ However, without any further explanation, the ruling states that the Dutch entity should be treated as transparent. This allows the authors to conclude that the feature weighed the most by the “Dirección General de Tributos” was the fact that the CV was transparent according to Dutch tax law⁵⁶.

The following relevant ruling⁵⁷ was issued on 1 June 2005 (ref. 0196-05) and refers to a Scottish general partnership. This entity has legal personality and is comparable

⁵⁴ Cf. A. Delgado, *Las entidades en atribución de rentas y el régimen fiscal de partnerships y trusts en España*, in *Manual de fiscalidad internacional* pp. 479-536 (p. 502) (Cordón Ezquerro ed. Madrid: Instituto de Estudios Fiscales, Vol. 1, 2007, 3rd ed.).

⁵⁵ In fact, this was the position of Dutch and Spanish authors before this administrative ruling was issued. See F. Snel & C. Mas, *The Classification of Partnerships for Tax Purposes: A Comparative Analysis (Netherlands/Spain)*, *European Taxation* 10, pp. 367-376 (p. 376) (2003).

⁵⁶ The ruling of 4 December 2007 (ref. V2614-07) concerns the same Dutch entity and reaches an identical conclusion.

⁵⁷ Rulings of 30 December 2004 (ref. 2110-04) and 25 July 2007 (ref. 24-07) will not be analyzed here since both refer to a British partnership but without making any reference to its specific form. In any case, both rulings considered that the partnership should be treated as transparent in Spain insofar as they were included in this regime under UK tax law.

according to its legal features to a “sociedad colectiva”, which in Spain is subject to CIT. However, the administration considered the Scottish partnership to be transparent. Without a doubt, once again, the fact that the entity was transparent in UK was the feature given the most relevance for the purpose of the ruling. Similar was the Spanish tax administration’s classification of a UK Limited Liability Partnership (see ruling of 25 July 2007, ref. V1319-05). In this case, even though it may have been complex to determine the exact Spanish entity to which the partnership was comparable, it is clear that the Spanish entities which are most comparable to the UK limited liability are opaque in Spain, since they are subject to CIT (e.g. “sociedad comanditaria, “sociedad colectiva”). However, the ruling provides for the transparency of the entity given that it was a look-through company according to UK tax law.

In another ruling of 28 November 2006 (ref. V2634-06) a Dutch real-estate cooperative (“cooperativa inmobiliaria”) was considered as opaque in Spain. Once again, the ruling avoided the required resemblance test, although it did appear to place great significance on the fact that the cooperative was subject to Dutch CIT.

The last ruling refers to a foreign venture capital fund, for which no information about its state of formation was given.⁵⁸ In this case, unlike the rulings described above, the taxpayer did not provide any information on the capital fund’s tax treatment in its home country. The query and the ruling only describe the following characteristics of the venture capital fund: partners have limited liability; the fund is represented and managed by a third party (the “general partner”), since partners are not allowed to manage the fund; the distribution of profits depends on a decision made by the “general partner”, on which partners have no influence.

The ruling considered the venture capital fund as opaque, albeit, as in previous cases, avoiding the resemblance test. Additionally, in this case it is not possible to conclude whether the tax treatment in the home state was a relevant criterion, due to the fact that no information was given in that respect. Yet, if the previous rulings are taken into account, it is possible that the Spanish tax administration would have reached the opposite decision if the foreign venture capital fund had been treated as transparent in its state of incorporation.

In view of the above, the following conclusions can be drawn. Theoretically, the wording of the Spanish statutory rule establishes a resemblance test, where only the legal features of the foreign entity are examined and the tax treatment applicable to the Spanish entity resembling the foreign entity the most is applied. However, it is evident that in practice, in addition to the legal features of the foreign entity, the Spanish tax administration has considered the tax treatment of the entity in its state of origin to be a factor which should also be taken into account. In fact, this last feature is the one (and most likely the only one) on which the most relevance has been placed in practice. Therefore, the tax treatment of foreign entities does not really follow a similarity approach but rather a tax-oriented approach, where the classification is mainly based on how the entity is treated for tax purposes in its home country. To a certain extent, Spanish tax administration accepts the tax regime of the state of origin and, according to this, if the entity is transparent in its home country it will also be treated as transparent

⁵⁸ Ruling of 11 January 2011 (ref. V0012-11).

in Spain and, on the contrary, if the entity is opaque, it will also be classified as opaque in Spain.

Although it is true that the Spanish tax administration's interpretation ("Dirección General de Tributos") of the statutory rule is debatable –the use of a tax oriented approach rather than a resemblance test–, the fact is that this is the approach that has prevailed in practice. Therefore, whenever there is a doubt about the treatment in Spain of a foreign entity as transparent or opaque, it is advisable to submit a written query, especially due to the fact that the ruling handed down has binding effects for the Spanish tax administration.

4.3. The “subject to CIT” condition under the Parent-Subsidiary Directive

The interpretation of the “subject to CIT” condition envisaged in Article 2 a (iii) of the Parent-Subsidiary Directive has not raised any controversy in Spain, to the extent that hardly any administrative rulings and court decisions have been handed down on this subject, the same being true of Article 3 a (iii) of the Interest-Royalty Directive.

In this respect, this requirement might not be controversial, at least from a Spanish point of view, regardless of whether it refers to parent companies or subsidiaries resident in Spain. This lack of controversy owes to the fact that as seen in section 3.4 of this report, the Directive was modified in 2005 and the number of Spanish entities listed in the annex that could benefit from this Directive was significantly expanded by introducing a “residual entity clause” which reads as follows⁵⁹: “other entities constituted under Spanish law subject to Spanish corporate tax (‘Impuesto sobre Sociedades’)”.⁶⁰

Therefore, in practice almost all (if not all) entities subject to the Spanish CIT will fulfil the “subject to CIT” condition. It should be also pointed out, as was explained in sections 3.5 and 4.2, Spanish legislation does not allow Spanish and foreign entities to opt to be treated as either transparent or opaque. Hence, Spanish transparent entities are not eligible for the Parent-Subsidiary Directive since they are not subject to Spanish CIT. On the other hand, it is clear that Spanish entities subject to CIT are not eligible for the Directive's benefits when they are completely exempt.

Notwithstanding the foregoing, some questions have been raised about whether the UTEs (temporary grouping of enterprises) satisfy the “subject to CIT” condition –see ruling of 23 November 2005, ref. V2373-05.

UTEs are associations usually formed by companies to carry out a specific project or formed for a fixed period of time. As was explained in section 3.5, these entities do not have legal personality, but their income, including capital gains, is subject to CIT on a worldwide basis. However, UTEs are subject to taxation under a partial fiscal transparency regime under which the UTE is not taxed on the part of the taxable income

⁵⁹ J.M. Calderón & A. Martín Jiménez, *La directiva relativa al sistema común de imposición aplicable en el caso de las sociedades matrices y filiales de diferentes Estados miembros*, in Carmona (ed.) *Convenios fiscales internacionales y fiscalidad de la Unión Europea*, pp. 1239-1287 (p. 1243) (Valencia: CISS, 2012).

⁶⁰ To date, the Interest-Royalty Directive has yet been updated. Therefore, the only Spanish entities covered by this Directive are the following: “companies under Spanish law known as *sociedad anónima*, *sociedad comanditaria por acciones*, *sociedad de responsabilidad limitada* and those public law bodies which operate under private law”.

attributable to the Spanish resident members in proportion to their share, but the losses of an UTE may be imputed to its Spanish resident members. This transparency regime does not affect Spanish non-resident members. Here the UTE is taxed on such income and the non-resident members are taxed only upon distribution.

The aforementioned ruling refers to a UTE that was to pay dividends to one of its partners who was resident in an EU country. The question raised by the taxpayer was if the UTE had fulfilled the Directive's requirements in order to allow to one of its partners to benefit from the exemption that the Directive establishes for dividends in the state of source. The ruling supports the applicability of the exemption, to the extent that the UTE is subject and not exempt to CIT. According to the ruling, the fact that the UTE is "half-transparent", when it has Spanish resident partners, cannot be considered as a breach of this requirement, to the extent that income attributable to non-resident partners is subject to CIT and is taxed at the UTE level –the taxation of non-resident partners will be deferred until the UTE pays dividends. This conclusion should also be applicable to Spanish AIEs (economic interest groupings), since their tax regimes in the CITA is the same.

Finally, it should be mentioned that no administrative rulings or court decisions have been handed down on the fulfillment of this requirements by entities from EU countries. In this regard, the problems that article 4.2 of the Parent-Subsidiary Directive is meant to solve, will not be likely to arise in Spain, since, as was explained in section 4.2, the Spanish tax administration recognizes the entity's home country tax regime as opaque or transparent.⁶¹ Thus, it seems unlikely that Spain as the state of residence of a parent company would consider a subsidiary to be fiscally transparent when it is treated as opaque in its EU home country.

Finally, it should be noted that the Directive does not provide any rule concerning cases in which the parent company is regarded as transparent under the domestic law of the subsidiary.⁶² This is an unlikely scenario in Spain because, as was previously discussed, under Spanish tax law the parent company will be classified as opaque if it is subject to CIT in its home country.

⁶¹ This article reads as follows: "Nothing in this Directive shall prevent the Member State of the parent company from considering a subsidiary to be fiscally transparent on the basis of that Member State's assessment of the legal characteristics of that subsidiary arising from the law under which it is constituted and therefore from taxing the parent company on its share of the profits of its subsidiary as and when those profits arise. In this case the Member State of the parent company shall refrain from taxing the distributed profits of the subsidiary. When assessing the parent company's share of the profits of its subsidiary as they arise the Member State of the parent company shall either exempt those profits or authorise the parent company to deduct from the amount of tax due that fraction of the corporation tax related to the parent company's share of profits and paid by its subsidiary and any lower-tier subsidiary, subject to the condition that at each tier a company and its lower-tier subsidiary fall within the definitions laid down in Article 2 and meet the requirements provided for in Article 3, up to the limit of the amount of the corresponding tax due".

⁶² Cf. M. Tenore, *The Parent-Subsidiary Directive*, in *Introduction to European Tax Law on Direct Taxation* pp. 111-130 (p. 116) (Lang/Pistone/Schuch/Staringer eds. Wien: Linde, 2010, 2nd ed.).