



Spanish 2011 Budget Proposals

The Spanish Government has presented the proposed 2011 Budget to Parliament for voting. It goes without saying that nobody expected anything other than what is being proposed – higher taxation and Government spending slashed. However the taxation proposals are not as tough as previously feared and these are the main highlights:

**Resident Income Tax**

1. Currently the top marginal tax rate is 43% for taxable general income over €53,407. With effect from 1st January 2011, two new tax bands will be introduced, charging general taxable income between €120,000 and €175,000 at 44% and above €175,000 at 45%.

However the situation is worse for some Spanish residents who live in Autonomous Communities where the local Government have used their powers to increase the Income Tax rate (as Income Tax is shared 50/50 between the Central Government and Autonomous Communities). In 2011 the residents of some Autonomous Communities could have a top marginal tax rate of up to 49%.

As a matter of interest, Capital Gains Tax rates remain unchanged at 19% on the first €6,000 of gains and 21% thereafter (subject to amending legislation of specific Autonomous Communities).

2. Earned income which is received on an irregular basis can be subject to a 40% reduction when calculating taxable income. Examples of this type of income are golden handshakes and lump sums paid in exchange for early retirement. However with effect from 1st January 2011 there is a ceiling on the earned income which can benefit from this reduction, namely €300,000 per annum.
3. The tax allowance of €2,500 for the birth or adoption of children is abolished. Births and adoptions in 2010 must be registered in the Civil Registry before 31st January 2011 in order to receive this tax allowance.



4. Spanish High Net Worth individuals frequently use an investment vehicle called SICAV ('Sociedad de Inversion de Capital Variable' or open-ended investment company) to hold their investments. These have a privileged Corporation Tax rate of 1% and effectively allow the individuals to defer Income Tax. Changes to the law – effective from 23rd September 2010 – result in Income Tax being payable when monies are withdrawn rather than deferred to the future. This change also applies to those vehicles with similar characteristics but resident in other countries.
5. The deduction for investment in the habitual residence (in general terms the property where one has lived continuously for at least three years) is only applicable for individuals whose income (before tax allowances) is lower than €24,107 per annum.

It is worthwhile noting this only applies when the property is purchased after 1st January 2011; taxpayers who qualify for the deduction as at 31st December 2010 can continue to apply the deduction on future payments (i.e. mortgage repayments).

Similar comments apply to taxpayers who are starting work on extending or rehabilitation/restoration of their habitual residence; the work must start before 31st December 2010 and finish before 1st January 2015.

6. Individuals who rent property will have the same tax allowances as those who purchase their property- but again this only benefits those people with an income of less than €24,107 per annum.



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- To continue the 'stick and carrot' approach of persuading individuals who rent property to declare this income, the percentage of net rental income which is exempted from tax rises from 50% to 60%.

### Non-Resident Tax

Currently under certain conditions a Spanish resident company can pay dividends to its EU resident holding company without the 19% Spanish withholding tax. One of those conditions is that the holding company has a direct shareholding in the Spanish subsidiary of at least 10%.

With effect from 1st January 2011 the minimum shareholding percentage falls to 5% and the shareholding relationship can be indirect as well as direct.

### Corporation Tax

- Small companies (namely those with a net turnover of less than €8 million in the previous tax year) receive certain tax benefits, namely:
  - Greater freedom to determine tax-allowable depreciation rates for new material and intangible fixed assets.
  - 1% general bad debt provision against the total debtors figure.



- Higher depreciation rate on fixed assets (including real estate) purchased by reinvestment of the proceeds of sale of existing fixed assets (including real estate).
- A Corporation Tax rate of 25% of the first €120,202 of profit in the tax year (with any excess taxable at the standard rate of 30%).

Currently, once a company exceeds this net turnover figure of €8 million it loses the above tax benefits. However with effect from 1st January 2011 these tax benefits will be extended for a further three years after net turnover exceeds the €8 million figure.

- Under existing Spanish tax legislation it has been possible to amortize goodwill arising on the acquisition of shares in other companies (at the rate of 5% per annum). However other E.U. member countries have complained to the European Commission about this fact; companies resident in most E.U. member states are unable to treat amortized goodwill as a tax-deductible expense and this was generally considered to be illegal Spanish state aid.

Accordingly Spain has bowed to this E.U. pressure and when the acquired company shares are those of a company resident in the E.U. amortization of goodwill is not deductible for acquisitions made after 21st December 2007.

- Similar rules as outlined in paragraph 4 above under the heading 'Resident Income Tax' will apply when a company owns participations in a SICAV.

### Capital Duty

Company share capital increases generally suffer a 1% Capital Duty. However in 2011 and 2012 this duty will not apply if the company meets the requirements for being a small company (i.e. net turnover less than €8 million in the previous tax year). Note – reductions in share capital for small companies are still subject to the 1% tax.

### Legal Interest Rates

The rate of legal interest in 2011 will be 4% per annum and the rate of interest for late payment of tax will be 5% (i.e. the same as 2010).

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