Setting up your Business in Spain
Issues to consider

Spain is one of the most attractive destinations for foreign investment, being the 6th largest developed economy receiving Foreign Direct Investment according to the "World Investment Report 2013" and offering access to the market of the EMEA region and Latin America. The highly qualified population and a decline in labour 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 overseas 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
- Have to file Spanish company accounts at Companies House for public view
- Accounts require auditing if for two consecutive years the company fulfills at least two of the following conditions: (i) Revenues > €5.7m p/a (ii) Total Assets > €2.85m (iii) Average number of employees > 50

Partnership:

- Members (partners) do not 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 Partnership 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:

Tax rate (%)		**Taxable profit (€)**	
Small co rate Net sales revenue<€5m and <25 employees	20	0 – 300.000	Excess subject to Intermediate rate
Intermediate rate Net sales revenue<€10m	25	0 – 300.000	Excess subject to Full rate
Full rate	30	The whole profit	

(NB: rates are for the tax year to 31/12/2013)

The thin-capitalization rules are no longer applicable when the associated enterprise is resident in another EU Member Estate, so the repayments in respect of a loan capital will not be considered as a covert distribution of profits.

Capital allowances are deductible from profits. Depreciation is reflected in the accounts and that depreciation is deductible in order to determine the tax liability, but there are some limits established by law.

Interest payments are deductible from profits with the limit of 30% of operating Profits when interest amount exceeds 1 Million Euro.

Payments of royalties are also deductible. If the payee is a non-resident, the payment will be subject to tax at 24.75 %. However, if royalties are paid to other European Member resident associated companies they will be exempt from non-resident income tax.

Research and development tax credits may be available at a rate of 25% of the expenses incurred in the tax period. The activity must be carried out in Spain or in any member state of the European Union of the European Economic Area. Other tax credit rates can apply in some circumstances and advice should be obtained.

The Spanish Corporate Income Tax law permits companies to carry forward the losses incurred in one year to the following 18 years. During 2012 and 2013 limitations for tax losses compensation are applicable for companies with gross turnover higher than €20 M:

- Gross Turnover from €20M to €60M maximum compensation of 50% of profit
- Gross Turnover over €60M maximum compensation of 25% of profit

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

A special regime for International Holding Companies (ETVE) makes Spain a very attractive place to set up a holding company.

According to this special regime dividends and capital gains received by an ETVE (International Holding Company) from its foreign subsidiaries are exempt if the following requirements are fulfilled:

- The ETVE held a participation of at least 5% in the nonresident entity for a one-year period or the stake in the non-resident company exceeds €6M.
- The foreign subsidiary is subject to a tax comparable to Spanish corporate income tax.
- At least 85% of the profits of the foreign subsidiary have been derived from business activities in a foreign country other than listed tax haven.

Furthermore, dividends distributed by the ETVE to a nonresident shareholder will not be subject to Spanish income tax, and capital gains obtained by such shareholder as a result of the participation in the ETVE will not be subject to Spanish income tax, either, provided certain other requirements are met.

In general, dividends paid to a non-resident are subject to a 21% withholding tax unless a lower rate applies under a tax treaty. Intercompany dividend payments made to residents of other EU member states are exempt from Spanish withholding tax if the foreign parent has held at least 5% of the share capital of the Spanish company for one year before dividends are declared or if the one year holding period is subsequently completed.

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.

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 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.

A business will need to prepare a Transfer Pricing Report proving the arm's length basis of transactions with the following exceptions:

- entities that belong to the same Spanish Tax Consolidated group for the operations performed within the Spanish group
- operations of entities with a net business revenue under €10M, and when the total volume of the related party transactions does not exceed €100.000
- intra-group transactions realized with the same related party with a total volume of less than €250.000

The report will include a functional and risk analysis, analysis of the adopted pricing model and benchmarking of the arm's length basis.

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

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.

Current Personal Income Tax rates in Spain are:

Tax basis (up to euros)	Gross tax due (euros)	Remaining tax basis (up to euros)	Tax rate
0,00	0,00	17.707,20	24,75%
17.707,20	4.382,53	15.300,00	30,00%
33.007,20	8.972,53	20.400,00	40,00%
53.407,20	17.132,53	66.953,00	47,00%
120.000,20	48.600,44	55.000,00	49,00% (1)
175.000,20	75.550,44	125.000,00	51,00% (2)
300.000,20	139.300,44	onward	52,00% (3)

(1) In certain regions of Spain an additional rate of 2%, is applicable resulting 51%
(2) In certain regions of Spain an additional rate of 4%, is applicable resulting 55%
(3) In certain regions of Spain an additional rate of 4%, is applicable resulting 56%
(NB: rates are for the tax year to 31/12/2013)

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 24.75% on the gross amount of the income. To qualify for non-resident taxation, 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.

Employers and employees also have to pay Spanish social security contribution:

Current Social Security rates are:

	Band of income (£)	**Rate (%)**
Employer	Up to 3,425.70	29.90
	Over 3,425.70	0.00 on excess
Employee	Up to 3,425.70	6.35
	Over 3,425.70	0.00 on excess

NB: (rates are for the tax year to 31/12/2013)

The total employer contribution rate is increased by higher percentages for the occupational accident and occupational disease contingencies provided for in the State Budget Law which will depend, as a general rule, on the activity of the company.

It is the employers' legal responsibility to pay over employee's tax and social security deductions to the Spanish tax authorities.

Spain has Reciprocal Agreements with 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 Spanish 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%. There is a reduced rate 10% for passenger transport, toll roads, sporting events of an amateur nature, exhibitions and fairs, health products and equipment, non-basic food products and water, rubbish collection and treatment and a super-reduced rate of 4% for books, newspapers and magazines, human medicine, basic foodstuffs (bread, milk, cheese, eggs, fruits, vegetables, cereals and potatoes).

Registration is mandatory for all taxpayers that carry out transactions in Spain and a special VAT identification is required when a company carries out intra-community transactions.

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 Spain advice needs to be sought as to what rate of VAT, if any, to use.

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.

In Spain Share Option plans, meeting some requirements, give tax benefits to employees.

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 cover 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 usually includes housing, lunches, nurseries, pension plans, low-cost loans, training courses, medical insurance, etc.

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

Kreston International

Kreston International Limited is a global network of independent accounting firms. Offering reliable and convenient access to efficient and seamless advisory and assurance services through member firms located around the globe, Kreston:

- Is ranked the 13th largest accounting network in the world
- Covers 105 countries
- Has 700 offices
- Has a resource of 21,000 professional and support staff.

Our members are accustomed to working together to deliver cohesive international solutions to ensure clients receive the highest quality of expertise available in their respective countries. Beyond assurance, quality and experience, clients will enjoy the unique synergy that stems from the trusted relationships that Kreston members have created globally and which support the consistent delivery of exceptional international service.

This information is provided for guidance only and is not a substitute for professional advice. Neither Kreston International Limited nor its member firms accept any liability for any loss arising as a result of actions taken or not taken based on the information contained in this document.

The information in this document was prepared as at 12 September 2013.