proposals will be finalized in November at a meeting in Mumbai, India.

Work on *compliance* and *taxpayer service* issues has seen progress towards the development of certain best practice principles for identifying and countering non-compliance and for audit in the electronic world, promoting and assisting compliance, and towards an exchange of experience in the field of taxpayer service (e.g. electronic filing) from which member countries will be able to draw in pursuing their own initiatives in this field.

At the Meeting of the OECD Council at Ministerial Level held in Paris on 26–27 June 2000, Ministers welcomed the constructive contribution by business and countries outside the Organization's membership to this work and looked forward to a progress report at the next meeting on both the direct and indirect tax issues raised by e-commerce.

The Committee has also continued to work constructively with other organizations on issues of common interest (such as the European Commission on consumption tax matters and the World Customs Organization on customs duties); and to make an input into the debate in member countries (e.g. a presentation on the OECD's work on taxation matters was made to the US Advisory Committee on Electronic Commerce).

The Committee has also launched a major global initiative with CIAT, CATA, IOTA and CREDAF on 'E-Commerce and Tax Administrations'. This first truly global conference on e-commerce and taxation will bring together officials from over 100 countries and will be held in Montreal in June 2001, under the auspices of the 5 sponsoring organizations and hosted by Canada. This Conference will explore the broad tax administration issues raised by e-commerce and will also explain the ways in which new technology can be used to improve taxpayer services.

Over the coming months, the work programme on e-commerce will see an intensification of effort in the working groups and TAGs, with the aim of reporting comprehensively to the Committee on Fiscal Affairs in 2001 both on emerging conclusions and recommendations, and on the way forward in those areas where further work is required. Specific proposals and recommendations will emerge:

- to confirm the interpretation and clarification of the existing permanent establishment rules;
- to confirm how payments should be characterized for the purposes of tax treaties;
- to establish the necessary international consensus to achieve the practical operation of consumption taxes on international e-commerce transactions;
- to identify and promote certain core best practices in respect of tax administration, in terms of the assessment, audit, payment and collection of tax;
- to identify and promote current trends in using e-commerce technology to improve taxpayer service.

New Measures Envisaged by Spanish Legislation in Support of the Internationalization of Companies

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1. Introduction

In spite of appearing under the heading of 'urgent tax measures to stimulate family savings and small and medium-sized businesses', the Royal Decree-law 3/2000 of 23 June is largely concerned with regulation of the fiscal consequences of initiatives to internationalize Spanish companies. These new measures – some of which are not, in fact, so very new – may be classified in three groups, each of which modifies a provision of the Corporate Tax Act (Act 43/1995 of 27 December):

- the exemption method to avoid international double taxation;
- a new regulation of the special tax regime for companies holding foreign shares (holding companies); and
- a tax benefit for establishing companies abroad.

In addition to these measures, the Royal Decree-law amends Art. 7 of the Income Tax Act (Act 40/1999 of 9 December), extending the limits for exemption of earnings received for personal services rendered abroad, and provides in the Wealth Tax Act (Act 19/1991 of 6 June) the option for workers stationed abroad of paying tax in accordance with the personal obligation regime.

This article analyzes these new rules of international scope and is divided into four main sections, each dealing with one of the aspects referred to above.

2. The exemption method to avoid international double taxation

Of the three traditional methods to avoid international double taxation – the method of deduction or imputation, the method of exemption and the method of reducing the taxable base by the amount of tax paid

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abroad – the Corporate Tax Act 43/1995 opted for the method of imputation or deduction from the corporate tax liability of the foreign tax paid, up to the limit of the amount of domestic tax that would be imposed in Spain. In fact, Art. 29 envisaged this method for correcting the international double taxation of foreign source income or juridical double taxation, while Art. 30 envisaged correcting such taxation in the case of foreign source dividends or economic double taxation. The new Act only used the exemption method to avoid the economic double taxation of dividends of holding companies in a special tax regime (Arts. 129–132).[1]

In this respect, the 1995 reform of the Corporate Tax Act introduced very little innovation with respect to the previous Act (Act 61/1978 of 27 December); applying the same method, in order to be able to benefit from the deduction for international economic double taxation, meant that the necessary percentage of participation in the non-resident company distributing the dividends was simply reduced from 25 per cent to 5 per cent. The second innovation was that of allowing the deduction which it had not been possible to apply due to insufficient tax liability to be carried over to the following seven fiscal years.

There were two main problems with this regulation: on the one hand, the Corporate Tax Act was not neutral with regard to the juridical form of internationalization of businesses, since if the company resident in Spain exercised its activity abroad through a permanent establishment, the resulting income was included in the taxable base of the resident company as it was earned, and the amount of foreign tax it was possible to deduct was limited to the amount of tax paid in Spain. On the other hand, if an affiliated company was incorporated abroad, the income derived from this company was only included in the taxable base when it was actually distributed in the form of dividends, and in this case it was also possible to deduct the underlying tax. Consequently, deferment of the tax and the imputation method applicable in each case could make it advisable to set up affiliated companies instead of permanent establishments in countries where the tax rates are lower than in Spain. Moreover, corporate tax made the repatriation of income generated abroad inadvisable, in that it acted as a tax on the importation of capital.[2]

In addition, the Act did not provide for treatment of capital gains in the case of the disposal of shares, operations of winding-up companies or the separation of partners, in that the profits generated in these operations consist of profits produced and not distributed by the company from which they derive. Therefore, in this case neither the deduction for international economic double taxation nor the deduction for domestic double taxation was applicable.

To these defects were added others that may be considered inherent in the imputation method, in the sense that this system does not favour the competitiveness of Spanish companies abroad, since a company resident in Spain might bear a greater tax burden than that borne by other companies in the same markets.

Faced with this initial regulation of international double taxation, Act 10/1996 of 18 December embodying urgent fiscal measures for correction of domestic inter-company double taxation and incentives to internationalize businesses, initiates, in my opinion, a period of ambiguity with regard to the method for correcting international double taxation. Indeed, this Act incorporates into the Corporate Tax Act the exemption method as an option, both to correct juridical double taxation in the case of income obtained through a permanent establishment and to correct international economic double taxation in the case of foreign source dividends and capital gains. However, the denomination 'exemption method' is at present purely doctrinal,[3] since the legislator does not formally introduce the exemption of certain income, as the Royal Decree-law of 2000 now does, but rather, by means of two new Articles (Arts. 29*bis* and 30*bis*) provides for two new technical deductions:

- the deduction to avoid international double taxation of income obtained through a permanent establishment (Art. 29*bis*); and
- the deduction to avoid international economic double taxation of foreign source dividends and capital gains (Art. 30*bis*).

In both cases, in spite of the technical denomination of deduction and their application as deductions as such (they entails a reduction in the total tax liability), they are equivalent to the exemption method, since they allow 100 per cent of the portion of the total tax liability corresponding to income obtained abroad to be deducted. In other words, applying these deductions, certain income obtained abroad will not pay tax in Spain, that is, it will be exempt from taxation.

The ambiguity referred to above arises since this method or this deduction does not substitute for the previous one, but is juxtaposed with the previous

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1 The White Book for the reform of corporate tax published in 1994 by the Secretary of State for the Treasury justifies opting for the imputation method on the basis that it is considered to be the most neutral in the case of the export of capital, since investments abroad will bear the same tax burden irrespective of the country and the foreign tax incentives. These same arguments can be found in the Ruding Report, in that the imputation system may avoid competition between different countries to attract foreign capital based on their tax laws.

2 See B. Tomé Muguruza, 'Deducción para evitar la doble imposición internacional', in CISS (ed.), *Guía del Impuesto sobre Sociedades* (Valencia, 1996), p. 500.

3 The Statement of Reasons of the Royal Decree 8/1996 which introduced these deductions refers to them, from a doctrinal point of view, as the exemption method: F. Clavijo Hernandez, 'Impuesto sobre Sociedades', in Marcial Pons (ed.), *Curso de Derecho Tributario. Parte especial*, 15th ed. (Madrid, 1999), p. 367; T. Murillo Guirao, V. Hernán Carrillo and G. Rodrigo Chaqués, 'Deducciones para evitar la doble imposición internacional', in Aranzadi (ed.), *Análisis de la ley 43/1995 del Impuesto sobre Sociedades y de su reglamento* (Coord. Ernst & Young) (Pamplona, 1997), pp. 409 et seq.

regulation. This means that, with regard to income obtained through a permanent establishment, two methods have co-existed since 1996: the method of limited imputation laid down in Art. 29 and that of exemption in Art. 29*bis*. The same may be said with regard to taxpayers who obtain foreign source dividends: the imputation method set out in Art. 30 will be applied to those companies that opt for it or do not fulfil any of the requisites enabling them to apply the exemption method under Art. 30*bis*. This latter Article also applies to foreign source capital gains.

Since the fiscal consequences of Arts. 29*bis* and 30*bis* were more advantageous, it was obvious that the option proposed by the legislator was more apparent than real, and application of the imputation method would be limited to those cases in which, since some of the requisites laid down in the new provisions were not met, such provisions could not be applied.

This being the situation, Royal Decree 3/2000 replaces Arts. 29*bis* and 30*bis*, which contained the two deductions from the tax liability referred to above, with a true exemption, in the juridical-technical sense, of income in the new Arts. 20*bis* and 20*ter*. Consequently, the question is whether this reform constitutes a true innovation as compared with the previous regulation.

In my opinion, the main innovation has been the juridical adaptation of the rule to the method that had been applied since Act 10/19996 came into force. Indeed, if the objective was that certain income would not pay tax in Spain, the best method would be that of exemption, but regulated and applied as a true exemption. For this reason the reform of 2000 refers to these exemptions as measures instead of deductions, and systematically moves these exemptions to Title 1V of the Corporate Tax Act which regulates the taxable base of the tax. Including these exemptions in the provisions relating to the taxable base and not in those relating to the taxable event, as would be more correct logically, is due, in my opinion, to the fact that these exemptions will eventually become negative corrections to determine the taxable base.

However, the juxtaposition of methods continues to exist: the imputation method in Arts. 29 and 30 and the exemption method in Arts. 20*bis* and 20*ter*. As occurred in the previous legislation, it is to be assumed that the new Arts. 20*bis* and 20*ter* will be the ones to apply in most cases, unless the complex requisites laid down in these provisions prevent their application. Nevertheless, the imputation method laid down in Arts. 29 and 30 has also been improved: the seven-year period that existed for deducting the excess deduction for international double taxation, when the total tax liability to which it was applied was insufficient, has been extended to ten years.

We shall now analyse these two new exemptions.

A. Exemption to avoid international economic double taxation of foreign source dividends and capital gains (Art. 20bis)

Article 20*bis* provides the exemption from corporate tax of dividends or the sharing in profits of non-resident companies, and of capital gains generated in the transfer of shares of a non-resident company, the separation of partners or winding up of the company. In both cases three requisites must be met.

1. The percentage of direct or indirect participation in the capital of the non-resident company is at least 5 per cent. This percentage of shares must have been held continuously for a year before the day on which the dividend is due, although it is also possible for the shares to be subsequently held the time necessary to complete this period. The requisite is also considered fulfilled if another company belonging to the same group has had continuous possession of these shares. In the case of the exemption of capital gains, this requisite is understood to refer to the day on which the transfer takes place.
2. A tax that is identical or analogous to corporate tax has been levied on the affiliated company. For the first time, the new Article aims to interpret the concept of analogous tax, and does so in the broad sense, not only considering as such any tax the purpose of which is taxation of the income of the affiliated company, but also including those taxes that involve partial taxation of such income or that are imposed based on external signs of wealth. In my opinion, a tax that is not directly levied on the total net income of a company can not be considered comparable with the Spanish corporate tax.

   The tax paid is deemed analogous when the affiliate is resident in a country with which Spain has signed a double taxation convention containing an exchange of information clause.[4]
3. The profits distributed or the fiscal years during which shares giving rise to the capital gains are held, derive from the exercise of business activities. This requisite is deemed fulfilled when at least 85 per cent of the income of the fiscal year corresponds to the following.

   - Income obtained abroad which is not included in the classes of income referred to in para. 2 of

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[4] For an analysis of this concept see, J. López Rodriguez, 'Alcance del término impuesto comparable utilizado en los artículos 29 bis y 30 bis de la ley 43/1995 del Impuesto sobre Sociedades', in *Carta Tributaria*, Monografía no. 322, November 1999.

Art. 121 which may be included in the taxable base in application of the international fiscal transparency system.[5]

Remission to Art. 121.2 poses no problem of interpretation when it is a case of income that does not derive from business activities. However, when it is a case of activities pertaining to 'credit, finance, insurance and rendering of services' we believe that the correct interpretation is the following: when the non-resident company obtains income of this type, and moreover fulfils the requisites necessary to be included in the international fiscal transparency system, such income should be included in the taxable base of the resident company and tax paid on it in accordance with this system.[6] In other cases in which the income is derived from business activities and the international fiscal transparency system is not applicable, the dividends received from non-resident companies will be exempt from taxation.

The provision is aimed at encouraging the internationalization of businesses and not their delocalization in order to benefit from the exemption. For this reason, in the case of activities pertaining to wholesale trade, services, credit, finance, insurance and re-assurance, they are considered to be provided abroad when the placing of goods at the disposal of the buyer, the rendering of the service, the grant of the loan or the risks insured are located in the country in which the affiliated company resides or any country other than Spain, and are realized by means of the material and human resources of the affiliated company. In other words, an authentic company located abroad.

- Dividends or sharing in profits of other non-resident companies in which the taxpayer holds 5 per cent shares and which fulfil the requisite of the type of income from which the dividends must derive. In other words, in order to be able to benefit from the exemption, the exempt capital gains or dividends may in turn come from other dividends. In this case it may be difficult to prove, in the chain of companies and dividends, the ultimate origin of the income from which they derive.

With regard to the exemption of capital gains, the provision lays down a series of special situations, which prevent, in some cases, companies from being artificially set up abroad with the purpose of benefiting from the exemption, and in others, the exemption being applied to income that entitled reductions to be made in the taxable base in previous fiscal years or in other companies of the same group.

The three special situations are as follows.

- When the non-resident company has shares in companies which are resident in Spanish territory or the assets they hold in Spain account for over 15 per cent of the market value of their total assets, the exemption does not apply to the capital gains but to the part of the income that corresponds to the net increase in undistributed profits generated by the affiliated company during the time the shares were held. In other words, the same limitation set out in Art. 28 for the deduction for domestic double taxation applies.
- When the taxpayer carries out a correction in value of the transferred shares which is tax deductible, the exemption will be limited to the excess income obtained in the transfer over and above the amount of such correction.
- When the shares are acquired from a company belonging to a group of companies: if the income is negative, that is, instead of a capital gain there is a loss, this will be deducted from the amount of positive income obtained in a previous transfer of the same shares to which the exemption was applied. Conversely, the capital gain will be taxed up to the amount of negative income obtained in previous transfers which was included in the taxable base.

Finally, the rule stipulates three instances in which exemption does not apply. Two of these are, in fact, a case of incompatibility of systems. In other words, the exemption does not apply during the time the taxpayer is considered a transparent company, or when the company applies the deduction for international double taxation provided in Arts. 29 or 30 of the Corporate Tax Act.

The third instance is an anti-fraud provision, according to which the exemption will not apply to those affiliated companies that exercise their activities abroad with the main purpose of taking advantage of this system. It is assumed that such a situation arises when the activity exercised by the affiliate had previously been exercised in Spain by another company

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[5] International fiscal transparency (Art. 121 of the LIS) is a tax system according to which certain types of income obtained by non-resident companies associated with companies or individuals resident in Spanish territory and subject to lower taxation than would be the case if tax were paid on this income in Spain, is imputed to the resident companies or individuals. The level of association between the two companies is fixed at 50 per cent of the company's capital, funds, results or voting rights. The tax paid by the non-resident company on the imputed income must be less than 75 per cent of the tax. Under para. 2 of this provision, to which the new rule refers, imputation is limited to the positive income that comes from the following sources:
(a) ownership of urban or rural real estate or the corresponding real property rights, unless they are related to a business activity;
(b) participation in the capital of any type of company and transfer of own capital to third parties;
(c) activities pertaining to credit, finance, insurance and rendering of services, except those directly related to export activities, carried on with associated companies resident in Spanish territory, which give rise to tax deductible expenses in the resident companies.

[6] The resident company may deduct from the imputed income the foreign tax actually paid on the distribution of dividends or sharing in profits, and from the imputed taxable base, the tax analogous to company tax paid by the non-resident company.

of the group which had ceased to exercise this activity. The assumption allows evidence to the contrary consisting, according to the Act, of 'the existence of any other "valid economic motive"'. This expression belongs to the category of so-called indeterminate legal concepts which makes it possible to argue any reason that is not exactly fraudulent.

B. Exemption of certain income obtained abroad through a permanent establishment (Art. 20ter)

The new Art. 20*ter*, as in the case of foreign source dividends and capital gains, has definitively established the exemption method to avoid double taxation when the income of a permanent establishment is taxed in Spain and abroad. Also, as in the previous case, the taxpayer may opt for application of the deduction for international double taxation set out in Art. 29. In this case the option must be exercised for each establishment located outside Spanish territory, even when there are various establishments in the same country.

The provision adopts the traditional concept of permanent establishment found in Spanish legislation based on the OECD Model Convention, and rounds it off by express remission to Art. 12.1(a) of the Non-Residents' Tax Act.[7]

The new Article requires the income of the permanent establishment to derive from exercising the same activities that entitle foreign source dividends and capital gains to exemption. It also establishes the same exclusions from the system as in the previous case.

Regarding the requisite that an identical or analogous tax must have been levied on the income obtained by the permanent establishment and that the permanent establishment is not located in a tax haven, it is surprising that the new Article does not define, as the previous regulation did, the concept of analogous tax or establish the presumption that an identical tax exists when a double taxation convention has been signed.[8]

The treatment given to the losses of a permanent establishment is similar to that which existed in the previous regulation: if negative income of the permanent establishment has been included in the taxable base in previous fiscal years, the exemption will only apply to the amount of positive income subsequently obtained in excess of such negative income.

C. Exemption of dividends and capital gains in the regime for holding companies (Arts. 129–132)

In 1995 the Corporate Tax Act only envisaged the exemption method to eliminate double taxation of foreign source dividends in a special tax regime for holding companies.[9] In this way Spain joined a series of European countries which had been introducing special regimes for this type of company, consisting in most cases of a series of measures to attract foreign capital.[10] This regime was developed by means of Act 10/1996.

It was precisely from 1996 on that this special system lost part of its attraction, in that the deduction laid down in Art. 30*bis*, was in economic terms equivalent to the exemption system. In this respect, the old Art. 30*bis* remitted to Art. 130 for development of some of the requisites necessary to take advantage of the exemption, whereas now Arts. 129 and 130 remit to Art. 20*bis*. Indeed, the introduction in legal terms of the exemption system for foreign source dividends and capital gains has made it necessary to reform the special regime for holding companies in order to avoid duplication.[11] The new regulation considers this system optional and its application requires notification to be given to the Treasury.[12]

The concept of a holding company has broadened, in the sense that companies whose corporate activity includes that of management and administration of securities representing the capital of companies which

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7 Para. (a) of Art. 12 of Act 41/1998 of 9 December provides that 'A person or company will be deemed to operate through a permanent establishment in Spanish territory when he has, in any capacity, continuously or habitually, installations or any kind of work premises in Spain where he exercises all or part of his activity, or acts therein through an agent who is authorized to contract in the taxpayer's name and on his behalf, and habitually exercises such powers of attorney.
In particular, headquarters, branches, offices, factories, workshops, warehouses, shops and other establishments, mines, oil or gas wells, quarries, forestry, agricultural or livestock exploitations or any other place of exploration or extraction of natural resources, and construction, installation or assembly work that lasts for more than twelve months are deemed to constitute a permanent establishment'.

8 The original wording of Art. 29*bis*, which was replaced by the provision we are commenting on, stipulated that the permanent establishment must be located in a country with which there was a double taxation convention. The amendment to the provision introduced by Act 66/1997 of 30 December, changed this requisite to the presumption of the taxes in both countries being analogous or identical.

9 Regarding this tax regime see S. Barrenechea Elorrieta and L. Soto Rodriguez, 'Régimen de las Entidades de Tenencia de Valores Extranjeros', Rev. Impuestos (1998), T-II, pp. 248 et seq.

10 See J. de Grado and B Morilla, 'Regímenes tributarios Europeos de Entidades Holding y su comparación con el régimen de la ETVE de la Ley 43/1995', Rev. Impuestos (1998), T-II, pp. 293 et seq.

11 Some authors, as a result of this latest reform, suggest consolidating both provisions. According to J.L. de Juan Peñalosa, 'The rule remits to the conditions of article 20 bis in such a way that the difference between the two is not clearly seen or, in other words, who would want to apply article 20 bis when he has the possibility of applying article 129? It would seem necessary to consolidate both provisions'.

12 The procedure for submitting a request for application of this system to the authorities is set out in Arts. 46,48 and 49 of the Corporate Tax Act. It is only necessary to provide proof of fulfilment of the conditions enabling advantage to be taken of this system, if requested by the authorities.
The third transitory provision of the Royal Decree 3/2000 lays down that, companies which were entitled to apply the holding companies regime when the new rules came into force, may renounce this regime by notifying the Treasury before the end of the first assessment period which terminates after the new Royal Decree came into force.

are non-resident in Spain may avail themselves of this system by means of the corresponding organization of human and material resources. The previous regulation required this corporate activity to be fundamental, which gave rise to many interpretations of the term 'fundamental'.[13] In this new concept, it is possible to include many companies provided they took the precaution of including the management of foreign securities in their corporate activity at the moment of their incorporation or subsequently. Corporate activity is a formal concept (Art. 9 of the Public Limited Companies Act and Art. 13 of the Limited Liability Companies Act) which does not prevent other activities from being exercised.

Another important innovation is that application of this regime does not depend on the level of participation in the non-resident company (5 per cent of the affiliate's capital), but on the amount paid for the shares (6 million Euros). This will enable a large number of investments which do not reach the level of participation required by Art. 20*bis* to benefit from the exemption provided in this tax system.

This regime is incompatible with that of transparency, and the securities representing the participation in these companies must be registered.[14] This greater control may also be one of the determinants in deciding whether to opt for this system.

The remaining requisites necessary to be able to take advantage of the exemption of dividends and capital gains refer to those which we have already analyzed in Art. 20*bis*. Up to now, opting for this system has seemed to depend only on the requisite of level of participation in the foreign affiliate not being complied with. However, the greater stimulus to this system, together with the consequent incentive to the domiciliation in Spain of foreign holding companies, resides in the distribution of profits.

Indeed, in accordance with the previous regulation, when profits charged to tax-exempt income were distributed, the recipient of the dividends could not apply the deduction for domestic double taxation, since there was no domestic double taxation, and only the deduction for international double taxation could be applied.

However, in the new Art. 131, when the recipient of the distributed profits charged to exempt income is a company subject to corporate tax (a resident company in Spain), the profits received entitle a deduction for double taxation of dividends to be made under Art. 28 of the Corporate Tax Act. In other words, if the resident company has a participation of 5 per cent in the holding company resident in Spain, a double exemption occurs, and if it owns a smaller participation a deduction of 50 per cent of the dividends received may be applied.

In the same way, when the recipient is a company or individual that is not resident in Spanish territory, the profits distributed will not be considered to be obtained in Spain, in which case application of this exemption is based on the fact that the entrance and exit of profits and capital gains through Spanish territory are not subject to taxation. This, in my opinion, is the great incentive to the domiciliation of parent companies in Spain.[15]

In the case of capital gains from the transfer of shares, the treatment given to the distribution of profits is similar. If the company receiving the profits is resident in Spain, the exemption envisaged in Art. 20*bis* will apply when the difference in value attributable to the shares in non-resident companies complies with the requisites specified in the Article, while the remaining income obtained will entitle the deduction for domestic double taxation to be made as laid down in Art. 28 of the Corporate Tax Act. When the company or individual receiving the capital gains is a non-resident, the income corresponding to reserves charged to exempt income referred to in Art. 20*bis*, or to differences in value attributable to shares in companies which fulfil the requisites set out in para. 1 of said Article, will not be deemed obtained in Spain.

With regard to the share contributions of companies which are not resident in Spanish territory, they may take advantage of the deferment system provided in Art. 108 of the Corporate Tax Act, irrespective of the percentage of participation such contributions represent in the holding company.

Finally, such important consequences of this system have rightly led the legislator to consider that the answers given by the tax authorities to taxpayers' enquiries regarding the interpretation and application of this system will be binding. In this respect a new paragraph is incorporated into Art. 107 of the General Tax Act regulating tax enquiries and increasing the legal certainty in the application of this special tax regime

3. Deduction in corporate tax for establishing business abroad

Of the deductions intended to encourage the exercise of certain activities, corporate tax has traditionally envisaged a deduction for export activities. At present, in accordance with Art. 34 of the Corporate Tax Act, it is possible to deduct 25 per cent of

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13 See. T. Murillo Guirao et al., n. 3 above, at p. 1027.

14 The third transitory provision of the Royal Decree 3/2000 stipulates the first assessment period in which the new system applies as the time limit in which to convert the securities representing the participation in the capital of these companies into registered securities.

15 However, when the recipient of the profits charged to exempt income is an individual taxpayer (natural person resident in Spain) these profits still do not entitle the deduction for double taxation of dividends to be made. However, the deduction for international double taxation envisaged in Art. 67 of Act 40/1998 of 9 December may be applied.

investments made abroad or related to export from the tax liability.[16]

The deduction envisaged in the new Art. 20*quarter* is not, technically speaking, a deduction as such. Indeed, the incentive envisaged in this provision is not a deduction from the tax liability but a temporary reduction in the taxable base. In other words, it is possible to deduct from the taxable base the investment made during the fiscal year in acquiring shares in non-resident companies, which enable the majority of voting rights to be reached. This reduction in the taxable base will result in a negative adjustment in the accounting results, since the deduction is not conditioned by its entry in the profit and loss statement. However, the incentive consists only in deferring the moment of payment of the tax, since the sums deducted will be incorporated into the taxable base, in equal instalments, over the following four assessment periods. In other words, the negative adjustment made during the year of the investment will result in four equal positive adjustments spread over the following four years

Two limits on the amount of the deduction are laid down: it can not exceed 5,000 million pesetas or 25 per cent of the taxable base in the assessment period prior to computation of the deduction. Furthermore, the amount of the deduction is reduced, if the value of the shares has depreciated, by the amount of this depreciation which was tax-deductible.

The requisites that must be fulfilled by the non-resident company for the taxpayer to be able to take advantage of this deduction are as follows.

- The company must engage in business activities abroad of the same characteristics as those required for application of the exemption for international double taxation. The main activity of the affiliated company can not be real estate, finance or insurance; neither can it consist in rendering services to associated companies resident in Spanish territory.
- The activities engaged in by the non-resident company can not have been exercised previously under another name. We must assume that this requisite refers to activities exercised abroad by an affiliated company, since the last paragraph of Art. 20*quarter* lays down that the deduction will not apply to those affiliated companies whose main purpose in exercising their activity abroad is the deduction, and establishes the presumption that such a situation exists when the same activity exercised by the affiliate abroad, in relation to the same market, had previously been exercised in Spain by another company, belonging to the same group, which no longer exercises that activity. In this case, the provision allows evidence to the contrary. The provision aims to prevent, in the first case, companies being dissolved and then established abroad in order to benefit twice from the deduction, and in the second case, affiliates being artificially domiciled abroad.
- The affiliated company must not reside in the European Union or in a tax haven.

These requisites must be met for a period of at least four years, otherwise the total amount deducted or outstanding will be included in the taxable base during the assessment period in which the requisites were not met.

Finally, sums deducted from the taxable base are incompatible with the deduction from the tax liability laid down in Art. 34.

4. Tax regime for personal services rendered abroad

Royal Decree 3/2000 provides another two measures with international implications, although in this case they refer to individuals and therefore modify provisions of the Income Tax Act and Wealth Tax Act respectively.

With regard to earned income received abroad, the limit of the exemption has been raised to 10 million pesetas (60,101.21 Euros) as compared with the 3.5 million peseta limit that existed in the previous regulation. Also, the new rule incorporates into the Act, in para. (p) of Art. 7, what had previously appeared as the regulatory implementation of this exemption in Art. 5 of the tax regulation. In order to be able to take advantage of this exemption, the following requisites must be met.

- The personal services are rendered to a company which is not resident in Spain or a permanent establishment located abroad.
- The territory in which the services are rendered is not a tax haven and an identical or analogous tax is levied therein. This requisite has been established in a more generous form than in the previous regulation. Indeed, the previous Article required tax to have effectively been paid on the earnings, and it was necessary to provide documents certifying this fact. Furthermore, Art. 5 of the regulation considered the requisite of effective payment of tax to be met when the taxpayer had deposited at least 50 per cent of the amount that would be levied on such earnings in Spain

The new regulation simply requires an identical or analogous tax to apply in the country where the

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[16] Art. 34 of the Corporate Tax Act considers the following to be export activities entitling the deduction to be made: the creation of branches or permanent establishments abroad, acquisition of shares in foreign companies or the incorporation of affiliates, directly related to the export of goods and services, or contracting of tourist services in Spain. Also included in the deduction are the costs of propaganda and advertising campaigns projected over several years to launch products, of opening markets and carrying out market research abroad, and of attending fairs, exhibitions and other analogous shows, including such international events held in Spain.

personal services are rendered. This will be easy to demonstrate in those countries with which there is a double taxation convention or which are not classified as a tax haven.

As in the earlier version, this regime is incompatible with certain sums in excess of the per diems received by civil servants and employees of public authorities stationed abroad being considered tax exempt *per diems*.

As a second measure, the Wealth Tax Act envisages, in a new paragraph of Art. 5, the option for residents of Spain who become residents of another country of paying tax according to the personal obligation system.[17] As is obvious, this possibility is intended for persons who, while their wealth is located in Spain, lose their residence due to labour reasons. Consequently, it is still in their interest to pay tax according to the personal obligation regime in the country where their wealth is located, even though the centre through which they obtain their earned income is temporarily or permanently in another country.

Both measures encourage the international mobility of workers and are more in keeping with the tax consequences to the individual that may arise from the internationalization of businesses.

5. Conclusions

The corporate tax rules containing the unilateral Spanish measures to correct international double taxation are the ones that have undergone the greatest number of amendments since the Corporate Tax Act came into force. As a result of these successive amendments, the exclusive use of the imputation method has given way to a fiscal policy committed to the exemption method. In this respect, I believe that, from a technical-juridical point of view, Royal Decree 3/2000 has improved this method, establishing the exemption for income obtained abroad. This method, in addition to being simpler, is conducive to the competitiveness of Spanish businesses abroad and the neutrality of the tax.

Nevertheless, the Spanish legislator continues to be rather reticent regarding the implementation of this method, in that its co-existence with the imputation system and the multiple requisites necessary to be able to take advantage of the exemption may, in practice, make the application of these provisions difficult. Of the necessary requisites, those related to the origin of the income are particularly complex, especially when the dividends come from other dividends or the references made to the market value of assets in Art. 20*bis*.

The regime for holding companies has become more competitive in attracting foreign capital, thanks to its wider scope of application and a very advantageous regime for companies participating in these holding companies. It would be interesting to analyze, not merely in the case of Spain, whether these special regimes are in keeping with a future fiscal conduct code of the Member States of the European Union.

As always, the tax benefit from deferring tax in the case of investments abroad will be welcomed by Spanish businesses, even though it will give rise, if applied, to a new difficulty in the assessment of the taxable base, since it introduces a new temporary difference between the accounting results and the tax base.

Finally, although less important reforms may appear, the Spanish legislator has favoured the international mobility of labour and therefore of businesses as well, through the exemption of foreign earned income, and the option of paying wealth tax in accordance with the personal obligation regime.

In conclusion, we can say that the objective of the Spanish legislation is to establish an international tax system that both favours the presence of Spanish businesses abroad and attracts foreign capital to Spanish territory. In my opinion, it will be necessary to provide this system with greater stability, since the constant reforms it has undergone do not favour the principle of legal certainty.

Notes

17 Under Art. 9 of the Income Tax Act, a taxpayer is deemed to have his habitual residence in Spain when either of the following circumstances exist: he remains more than 183 days in Spanish territory or the main nucleus or base of his economic interests or activities is located in Spain.