

THE SUCCESSION AND DONATION TAX IN SPAIN:

The European Commission considers the biggest taxation, that the non-residents have to endure as discriminatory and contrary to the communitarian law

CURRENT SITUATION IN SPAIN

In Spain, currently high taxes are paid to the State in inheritances and donations between non-residents, even though these transmissions are between direct relatives (between spouses, from parents to children, etc.), because such taxes must be calculated based on the state regulations with a progressive scale, which goes from 7.65% up to 34% of the real value of the assets and transmitted rights.

However, in inheritances and donations between residents, direct relatives, taxes paid are much less, or even no taxes are paid in some cases, because the Autonomous Regions are the ones which charge these taxes, based on their own regulations, and the reality is that practically all the Autonomous Regions have approved considerable discounts for their residents.

This is so, because in Spain the Succession and Donation Tax is a State tax, but regarding the residents in Spain, it is under the regulation of the Autonomous Regions, which have very important regulation competences, that all have used in order to lower the transmission tax between near relatives to the maximum. The problem is that in the inheritances, for example, these Autonomous discounts are NOT applicable and this tax must be paid to the State Treasury, applying the state regulation (up to 34% or more):

when the heirs are residents in Spain, but the deceased is non-resident,
or when the deceased is a resident in Spain, but the heirs are non-residents.

CURRENT TAXATION IN THE BALEARIC ISLANDS

In order to see up to what point the Autonomous Regions have lowered the tax on Successions and Donations, on their residents, we can look at the Balearic Islands.

Since the 1st of January 2007, the inheritance tax between direct relatives in the Balearic Islands is 1% maximum, always when two conditions are fulfilled simultaneously:

that the deceased has his fiscal address in Spain and specifically, in the Balearic Islands (if he is from another Autonomous Region, he must have lived more than 5 years in the Balearic Islands, and if he is a foreigner, it might be considered, that it would be sufficient to be a resident in Spain - the Balearic Islands, in the moment of death),
and that his heirs are fiscal residents in Spain (even though not in the Balearic Islands).

It might happen that in the same inheritance, with the death of one parent, residing in the Balearic Islands, in favour of two children, one of them has to pay the Succession and Donation Tax to the Balearic Treasury, 1% maximum if he was a fiscal resident in Spain, and the other one has to pay the State Treasury a much higher tax for not having his fiscal residency in Spain. In this way, for example in an inheritance of 500.000 Euros (in real estate or money) in favour of these two children, in equal shares, the resident in Spain would pay 2.500 Euros (1%), while the non-resident would have to pay 38.875 Euros (15.55%). If the inheritance was 1.000.000.000 Euros, the resident would pay 5.000 Euros (1%), while the other would pay 106.021,59 Euros (21,20%).

POSSIBLE CHANGES IN A SHORT-RUN OR LONG-RUN PERIOD

On the 5/5/2010 the European Commission sent a report to Spain (IP/10/513), requesting the modification of the fiscal regulation in Succession and Donation matters, which requires more taxes in relation to the non-residents or the ones situated abroad, based on the actual autonomous regulation, considering the Commission that these dispositions are incompatible with the free circulation of people and capital.

More recently, on the 16/2/2011, the Commission has given an ultimatum to Spain, through “a complementary motivated report” (IP/11/162), insisting again on the modification of the regulation of the Succession and Donation Tax. Upon not receiving a satisfactory reply in the period of two months, the Commission could decide to take the matter to European Union Justice Court.

It is very important and significant that the Commission has pressed so much Spain in that matter, remitting “a complementary motivated report”, a step, which Brussels makes very rarely. This makes us think that, in the short run it is very possible that important changes are being introduced into the Spanish Regulations on the Succession and Donation Tax, which could mean an important discount on the taxes to be paid, for these transmissions between non-residents, who are direct relatives, at least for the ones who live in the European Union.

This has happened recently, in other very similar cases, after motivated reports from the European Commission aimed at Spain:

On the 14/7/2005 the European Commission requested Spain, through a motivated report (IP/05/933), the modification of the discriminatory legislation in fiscal matters of the patrimonial profits for the sale of property of non-residents. Specifically, the Commission denounced that the non-residents paid 35% on these profits, while the residents paid 15%, if they have been owners more than a year. A few months later, through the Law 35/2006, from the 28/11/2006, the applicable regulations have been reformed, in such a way that from the 1st of February 2007, the residents, as well as the non-residents, started paying the tax in the same way (18%).

On the 16/10/2008 the European Commission requested Spain, through a motivated report (IP/08/1533), the modification of the fiscal regulations, which taxed the non-residents without a permanent establishment for their (gross) Income, while the residents were only taxed for their Net Income. Some time later, through the Law 2/2010, from the 1/3/2010, this regulation has been reformed, in such a way that the non-residents, who have their residence in another State, a member of the EU, are allowed to, with effect from 1/1/2010, discounting the expenses related directly to the obtained yields in Spain and tax in this way the Net Income.

CONCLUSION

There are solid arguments to consider that the regulation in force of the Succession and Donation Tax is contrary to the freedoms of the EU Treaty, requiring in the transmissions between non-residents, taxes a lot higher than the ones paid by residents in the different Autonomous Regions, based on the regulation approved by these.

Facing this pressure from the European Commission to Spain it is very probable that in the short run, this regulation is modified, in order to avoid this discrimination, which would mean a considerable discount in the taxes to be paid for the inheritances or donations between direct relatives, non-residents, at least for the ones who live in the European Union. In a published report by the Fiscal Studies Institute, by the Ministry of Economy and Treasury, in mid 2010 it was offered to

try, a fixed amount in the Succession and Donation Tax, with a minimum exempt for the nearest relatives, in such a way that the Autonomous Regions have competences to modify that, but within limits, in order to minimize the competence problems between territories within Spain, and this can be applied as well to the non-residents to avoid the denounced discrimination by the EU.

In any case, before becoming effective this possible modification of lowering the applicable Inheritance and Donation Taxes between non-residents, who have paid the already excessive taxes (non prescribing), superior to the applicable ones to the residents in the different Autonomous Regions, or they have to pay them, it could be suggested to start administrative and judicial proceedings in order to try to recover the paid in excess taxes in Spain. There are similar precedents to the one mentioned, where the Spanish Court has clearly seen the infringement of the Communitarian Rights and has allowed to recover these taxes without having to appeal to the Justice Court of the EU. These proceedings can last years, and because of its value, depending on the possible excess paid and logically would make no sense if the input tax in Spain could have been discounted completely by the non-resident or almost completely in his country of residence.

Benjamin Franklin said approximately 250 years ago that, "in this world there is nothing sure, except death and taxes". It could be added that, the worst is when both things join together and that to be prepared for such contingency and so that the fear could be the least possible, there is nothing better than to count on specialized, legal and fiscal advice.

Palma, 13th of April 2011

A handwritten signature in black ink, consisting of several overlapping loops and a long horizontal stroke extending to the right.

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