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AN APPROACH TO THE SPANISH TAX SYSTEM

Adapted to European Higher Education Area (EHEA)

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THE SPANISH TAX SYSTEM.

THE SPANISH TAX SYSTEM; STATE, REGIONAL AND LOCAL SYSTEMS.

1.- GENERAL CONSIDERATIONS ABOUT THE SPANISH TAX SYSTEM.

1.- Some necessary conditions for the existence of a tax system.

A tax system does not simply consist of a mere set of regulations. It requires a certain degree of rationality and a technically correct design for achieving the aims of the system.

Furthermore, a system cannot work adequately if is not accompanied by certain necessary elements, such as the existence of an efficient financial public administration, known as the “Administración Pública” in Spanish, which is able to apply the regulations, as well as an important degree of social acceptance and compliance.

The ideas expressed in this text can help us to understand some of the characteristics required to speak of a tax system proper:

- Clarity of each regulation, and of the whole body of regulations. Legal certainty. Flexibility, i.e. the ability to adapt to every economic situation.
- Application of the principle of personality, according to which the obligations and amounts owed to the Tax Office must be specified with regard to subjects, i.e. persons or corporations, not with regard to groups of people, e.g. a global obligation on all the traders of a commercial activity sector in a city. The same applies to liabilities.
- Absence of tax avoidance and, at the same time, absence of duplications and redundancies, e.g. when a system is not designed correctly and the same taxable event is taxed twice. The limitation of exemptions and deductions, as these kinds of measures can misrepresent the real justice of the system, e.g. a system in which all people are apparently subject to taxes, as all are included in the taxable event, but some, however, do not pay the taxes, or do not pay the same

amount as others, because they are beneficiaries of exemptions or deductions without any regard to a constitutionally recognized purpose.

- Progressive taxation scales, at least in some of the most important taxes. The Spanish Constitution demands some degree of progressiveness as the result of the application of the system as a whole - not for every tax but, as can easily be imagined, for some of the most important taxes, e.g. Personal Income Tax, which, in Spain, is levied on the income of natural persons. The progressiveness must be expressed within certain limits and it is the legislator who must define them.
- The existence of different taxes levied on different situations.
- Coherence.

Coherence between the purposes and the means, between the general and the specific rules, and between the four territorial systems existing in Spain: the European Union, Spain, the Regions, known in Spanish as the 'Autonomous Communities' or 'Comunidades Autónomas', and Local Authorities, or City Councils, generally known in Spanish as 'Ayuntamientos', or 'Corporaciones Locales'.

Coherence between direct and indirect taxes. Direct taxes are levied on income and on the ownership of assets, or wealth. Indirect taxes are levied on consumption.

- The existence of reliable and agile conflict resolution mechanisms, capable of responding within an acceptable period of time.
- The existence of an effective sanctioning regime, normally consisting of fines, but with possible imprisonment in serious cases.

2.- Concept and range of the sources of law.

Spanish Law is a written law, which means that it mainly consists of written and, in many occasions, codified sources of law, not of judicial opinions and decisions. In this system, the role of judges does not lie in making legal decisions as the primary way of solving conflicts, whether independently or without consideration of the laws, but only in interpreting and applying these laws. Accordingly, the Spanish legal system, a continental system, consists of a structure of laws. Therefore, the sources of law, i.e. the formal ways or means of obliging or

compelling people to observe certain forms of behaviour, are constituted by written laws and rules.

What is a source of law? A source of law is a public act that contains a mandatory provision, applicable to a generality of people and subjects, so that anyone who is under its sphere of influence, which is to say, under the scope of its provisions, is obliged to observe it.

Tax law forms part of the general legal system and, in general, is similar to other laws. It is generally considered to a rather complicated system for several reasons:

First, the legal system is composed of several kinds of regulation, some of which are international and others national. These regulations are arranged in a hierarchical system consisting of different levels. Lower-level regulations can never contradict, modify or derogate higher-level regulations. The levels and kinds of regulation consist of the following:

- Level one, the highest level: the Spanish Constitution and international treaties. The main international regulations to be considered are those treaties that Spain has signed with other nations and international organizations. It is very important to take into consideration, within this group of regulations, the treaties that Spain has signed with the European Union, of which it is a member.
- Level two. Parliamentary laws and certain kinds of law that, in special cases, can have the same level of enforceability, always with the condition that there exists parliamentary agreement. These laws are simply known as ‘leyes’ in Spanish.
- Level three. Regulations that do not originate in a democratic assembly or parliament, but in government. These regulations are known as ‘reglamentos’ in Spanish. These regulations are only able to develop the main laws in secondary issues, such as formal matters, the fixing of deadlines, and so on. These regulations can never contradict a higher-level law.

Hereon, the word “norm” will be used to refer, as a general expression, to any kind of source of law. The word “law” will refer to norms in the level two, i.e. parliamentary norms. The norms originated in the government, located in the third level, will be mentioned with the word “rule”.

There are many laws and they change frequently, which is not a good thing for legal certainty, but appears to be an unavoidable drawback all over the world.

Additionally, Spain has a complex political structure, with three different kinds of administrations:

The Central State, which has the power to organize the whole system, and which also provides, according to the Constitution, important margins of political and economic discretion to the other administrations. These, in short, are:

The seventeen autonomous communities, plus two autonomous cities, Ceuta and Melilla. The parliaments of the autonomous communities, provided they act within the scope of the competences available to them as defined in the Constitution, are able to pass laws, or 'leyes'.

On the other hand, town and city councils, or 'ayuntamientos', are not entitled to pass second-level laws, or 'leyes', but only third-level laws. They can only pass those laws known as 'reglamentos', or rules, and cannot create, derogate or modify important issues concerning taxes.

3.- State structure, constitutional provisions and the tax system.

Regarding the internal Spanish system, some distinctions should be made:

First, the distinction between state, regional, and local tax systems, each with their own different capacities and competences.

In accordance with constitutional mandate, the original tax power resides in the state. However, a part of the power must be exercised by the Autonomous Communities, or Regions, and Local Authorities, or "Ayuntamientos". The logic of the system is the following: the state has the power to organize the whole system, but when it does so, it must reserve certain competencies for the Regions and the Local Authorities. Otherwise, the state law would be unconstitutional.

Furthermore, the competences or capabilities of the Regions and Local Authorities are different. In Spain, a parliamentary law, not a simple regulation passed by government, is needed to take important decisions concerning taxes, such as the creation of taxes, the definition of those subjects obliged to pay or declare taxes, exemptions and deductions, and the derogation of taxes, among others, including the main procedural regulations and assurance standards.

Each region has its own parliament in Spain, and this parliament is able to adopt decisions related to taxes, within certain limits, e.g. they cannot apply taxes to taxable events which have already been taxed by the State, or on taxable events located outside of the territorial limits of the region, or that make or imply a limitation to freedom of residence or of entrepreneurial activities.

Local authorities are not able to pass parliamentary laws, only regulations located on a lower hierarchical level, and therefore the only thing they can do is develop the taxes created and regulated by the State in certain parts of its structure.

2.- A LOOK AT THE STRUCTURE OF THE SPANISH TAX SYSTEM. THE SO-CALLED GENERAL PART OF THE SPANISH TAX SYSTEM; GENERAL CONCEPTS AND THE REGULATION OF GENERAL RELATIONSHIPS.

1.- Some preliminary general questions. Financial cycle and Financial law.

There is an area of social and economic life that consists of a flow of public revenues and expenses aimed at satisfying public needs and aims, and whose owner or bearer is a public entity. This economic flow arises due to the need to obtain financial means to bear or afford to pay for these public needs.

This generation of public revenues and the bearing of public expenses is called ‘financial activity’, or rather ‘public financial activity’; ‘actividad financiera’ in Spanish. In reality, this activity does not only consist of the obtaining and spending of income but also the activity of management, understood as the activity of providing a rational, coherent or “technical” management of public funds while in the hands of the Tax Office.

The Tax Office, or “Hacienda Pública” in Spanish, is another term to be considered. The Tax Office is that part of the Public Administration devoted to maintaining public financial activity and public economic resources, and is responsible for carrying out all related procedures.

Several questions should be noted regarding financial activity, considered as an activity carried out by public entities with public means and whose aim is to satisfy and fulfil public needs.

1.- The right holder, who is legally entitled to charge taxes, is always a public entity.

Collecting taxes is an exercise of sovereignty, or public power, and, accordingly, is beyond the scope of private entities. A private entity is never allowed to be the holder of taxation rights, although private entities can collaborate in several, but obviously not all, functions, such as the collecting of taxes. It is often the case, for instance, that the work of collecting taxes is performed by private financial enterprises which have signed deals with the public services agreeing to carry out auxiliary and simple mechanical actions.

2.- The activity referred to is cyclical, i.e. its development involves inputs and outputs, with some generating and conditioning others, as in a circle.

The activity is also periodical, and is usually divided into periods of one natural year, understood as the time between January 1st and December 31st. This one-year period is usual for the accrual of many taxes and, more significantly, for the planning and implementation of public budgets, regardless of whether there exist plans and expenses intended or planned for multiannual periods.

3.- Public financial activity is a planned activity.

Of course, this does not consist of a series of random acts, but is rather intended to achieve certain aims through the defining and structuring of a plan.

4.- It is a regulated activity.

This is an activity subject to a highly restrictive law.

Broadly speaking, we can distinguish between two kinds of law:

Private law, which regulates the relationships between private persons regarding private interests and rights, and which consequently leaves very broad margins of discretion to the individuals involved.

Public law, whose different branches are devoted to regulating public principles, public organization and the relationships between individuals and power, understood as the Public Administration or, less appropriately, the government or public authorities. Public law does not allow broad margins of discretion to individuals. It would be more correct to say that, in general, it does not allow them any ability to take decisions at all, as any questions concerning public matters lie strictly in the hands of the Law.

Financial law, and what most concerns us here, Tax law, i.e. that area of financial law devoted to regulating and studying taxes, is a public law, which means that subjects are not entitled to modify any legal provision or mandate. This means that neither public entities nor private subjects involved in the tax

relationship are allowed to change legal mandates. During the carrying out of their activities, neither public entities nor particulars are allowed to choose whether to apply one regulation or another, or to modify the regulations, not even by mutual agreement between both parties involved. This would be completely illegal and the activity would be considered null and void. Tax law is, therefore, a strictly compulsory law. Hardly any margin of discretion in the application of this law is left in the hands of any of the parties involved, be they public or private, unlike the case of private law, in which some decisions are left to the discretion of particulars. Tax law is an imperative or compulsory law.

2.- A brief mention of some constitutional principles.

As is to be expected, the Spanish Constitution makes some references to the tax system, and determines some principles. Some of these principles should be highlighted.

Generality

It is clear that an indispensable condition for achieving a fair system is generality. A good system should not show unfair or unjustified exemptions which make equal subjects pay taxes in different ways, if no other constitutional mandate is appropriately taken into consideration.

Economic capacity

Economic capacity refers to the ownership of wealth, as described by law. No tax can be imposed on a subject if it is not based on a demonstration of economic capacity, although this demonstration can sometimes be less clear than on other occasions. It is clear that a demonstration of economic capacity is less obvious in some less important taxes, but it is also clear that it is better defined in the most important taxes, such as Personal Income Taxes and taxes on consumption.

Economic capacity is taken into account by the legislator when defines the facts that will oblige to pay taxes and, sometimes, especially in important taxes, when designs the mechanisms to assess the amount to be paid.

Progressivity

This principle means that, considering the tax system as a whole and not each individual tax, the result should be that those subjects who show greater economic capacity pay more taxes than others, and not just more, but

progressively more. Progressivity will be explained in the section on the tax rate. It is important to bear in mind that progressivity is not a proviso or condition for each and every tax, but for the system as a whole. Progressivity is mainly achieved in the Spanish tax system through Personal Income Tax and through certain other taxes.

Justice

It is not easy to define Justice in just a few words. It is enough to say here that Justice is a combination of other principles, two of which include equality and progressivity.

The prohibition on a confiscatory tax system.

Although this principle could lead to more profound considerations, let us only consider the fact that the application of a fair tax system should never involve such high charges that a subject ends up without the means necessary for attaining a decent standard of living.

The constitutional principle of legal reserve.

This is a quite important principle, which is to be applied to any tax, whether it is an important tax or not.

Imposing taxes is an exercise of power and, accordingly, is reserved to the representatives of the people. This means that only parliaments can design, establish, approve and modify taxes. It concerns the main aspects of taxes, such as taxable events, subjects, the amounts to be paid and several other issues. No third-level rule can approve mandates related to the aforementioned questions. This implies a rather important difference between the State and the Autonomous Communities, on the one hand, and the Local Administrations on the other. While the State and the Autonomous Communities can pass taxes, this is not the case for the Local Administrations, who can only develop the taxes designed and enacted by the State, by rules and within certain limits.

3.- The kinds of taxes in Spain.

Taxes are not only a way for public entities to collect revenues or funds, but also a way to help society achieve certain economic and social goals. The tax system is therefore a powerful instrument of economic policy, and a rather useful

instrument for achieving certain constitutional goals, such as the fight against poverty and environmental pollution.

There exist three kinds of taxes in Spain: “impuestos”, “tasas” y “contribuciones especiales”. This classification is, to a large extent, purely national, because it does not correspond to the classification of other countries. However, it can be useful to know the individual characteristics of these three taxes.

There exist certain kinds of taxes that are due to be paid when public services provide some kind of service or allow the use, for private purposes, of public spaces, such as when a certificate is issued or a café is allowed to place tables and chairs in a public square. A tax known as a “tasa” must then be paid.

Another kind of tax must be paid when the Public Administration builds a public construction which benefits everyone, but especially benefits certain people. Let us consider, for example, the case of a construction carried out to reform a certain street. It is clear that such a construction provides an improvement for everyone in the city, but it is also clearly more important and relevant for the residents of the street. These residents must therefore collaborate with the construction by paying part of the investment. The tax paid in this case is called a ‘special contribution’, or ‘contribución especial’. However, the most important kind of tax in Spain is known as an ‘impuesto’.

The most important taxes, and those that will be the focus of our attention in this course, are the so-called ‘impuestos’. An ‘impuesto’ is a kind of tax that does not require anything other than a demonstration of economic capacity by a subject to generate, or accrue, an enforceable debt. One very important thing should be noted regarding this kind of tax: obliging a subject to pay does not require any special behaviour on the part of the Public Administration, such as providing a service, allowing the use of public land, or constructing something. This kind of tax is due to be paid only because a subject has shown economic capacity, i.e. some degree of wealth.

One can demonstrate this capacity through three indexes: the receiving or earning of income, the entitlement or ownership of wealth, and the incurring of expenditures.

Both income and assets are direct indexes of wealth. The incurring of expenditures is an indirect index of wealth, which does not correspond to wealth itself, but to its use.

4.- The tax relationship and its consequences. A mention to material and formal obligations.

The tax relationship is the group of obligations and rights that joins public entities and individuals together for the purpose of tax demands. Within the scope of the tax relationship, both public entities and individuals are subject to obligations and are entitled to demand that their rights be fulfilled. In other words, public entities do not only have certain rights, but also certain obligations.

Although pacts between the parties involved over private issues, such as prices, discounts, deadlines for payment of private obligations and so on, are perfectly legal, this is not the case for tax provisions, according to the nature of the tax relationship and of the Tax law. No pacts are admitted regarding the amount of the tax fee or the deadline for payment of the tax, for example.

The obligations involved in the tax relationship, both for public entities and for individuals, can be material or formal. Material obligations have a patrimonial content or significance, and usually consist of monetary payments. Formal obligations involve the need to act in a specific way, e.g. respecting certain rules of information and formalities regarding the filling in of declaration forms, the issuing and safekeeping of invoices, and the upholding of accounting standards.

The main material obligation consists of the payment of the tax fee, but other amounts may be added in specific situations, generally in the case of arrears, such as interests or certain kinds of surcharges.

The sum of the tax fee and any possible interests and surcharges constitutes the so-called ‘tax debt’. Most of the time, this tax debt consists only of the tax fee.

On the other hand, the Tax Office also bears certain material obligations, such as the refunding of improper payments and of interests whenever arrears on its material duties in relation to the individual occur.

Both the Tax Office and the subject bear many formal obligations. To mention just a few of the most important, the main formal obligations for the Tax Office consist of respecting several rules when notifying some decision to subjects; for example, when the Tax Office summons a subject to an inspection procedure, some formalities must be observed regarding notification, such as the mention of the matters which will be subject to inspection during the audit, or the rights of

the subject. The individual must also fulfil many formal obligations, such as carrying out proper bookkeeping and accounting, issuing and requesting correct invoices, and the safekeeping of invoices and copies, among many others. Perhaps the most important formal obligation for the individual to fulfil is the tax declaration. Making a declaration consists of communicating to the Tax Office any relevant questions or items concerning the obligation to pay taxes. Declarations may refer to any relevant issue, but the most important kind of declaration is that which refers to the realisation of a taxable event. Although, in the past, it was often enough to just declare relevant issues so that the Tax Office could assess the total amount of the tax fee, this situation is almost non-existent nowadays. The law currently imposes on individuals the obligation to not only declare relevant issues, but also the obligation to calculate the tax fee, apply the law and make all necessary calculations, without prejudice to the right of the Tax Office to check the declarations. Therefore, individuals must now calculate, declare and pay most taxes themselves.

A.- The taxable event.

Why does the tax fee exist? The origin of a tax fee is the realisation of a taxable event, which is an event or situation described in a parliamentary law and whose realisation implies payment of the tax. For instance, the obtaining of several types of income, the ownership of wealth or certain kinds of goods, or the incurring of expenses. A person who attains income has realised the taxable event of a tax on income, and so on.

Every taxable event must show the attain, possession or expense of some kind of wealth, which is to say that must represent some kind of economic capacity, regardless of the fact that, in some occasions this demonstration is more clear than in others.

Needless to say, taxable events and, in general, all the elements of the tax system mentioned hereafter must be approved by Parliament, after an open public debate and vote.

B.- The accrual of taxes.

When a taxable event occurs, the obligation to pay tax arises. The moment when this obligation to pay occurs is called the accrual. From the moment of

accrual, the subject has a liability on his equity, but the event and the moment of accrual are not identified with the moment of declaration or the moment of payment. These are usually different, so the accrual may occur on one day and the obligation to pay may occur some days or months later, or on a fixed date. Personal Income Tax, for example, is accrued on December 31st, but the deadline for declaration and payment is usually at the end of June of the following year. In certain other taxes, accrual is set at the moment of purchase, but the deadline for the declaration may be, for instance, one month later.

C.- Exemptions.

Events described within the scope of the taxable event result in the obligation for someone to pay, but the law occasionally establishes several events or acts which, despite falling within the limits of the taxable event, are not subject to taxation. These cases are exceptions to the general obligation to pay and are known as exemptions. They are mainly related to tutelage and are covered by the Constitution and by international treaties, and include education, health care, personal hardship, and so on. They may sometimes be produced for technical reasons, as in the case of VAT on exports. Exemptions must be established carefully and restrictively, and must always be based on solid arguments, previously debated in Parliament and approved by a regulation with the status of a law.

5.- Fixed and variable taxes. The taxable event, taxable base, tax rate and tax fee.

There are two possible kinds of taxes in addition to those mentioned above: fixed taxes and variable taxes.

In the case of fixed taxes, the law establishes a taxable event and, immediately, an amount to be paid, regardless of any other considerations. As a result, every subject, in every case, is to pay the same amount, e.g. a tax on an application to receive a service from the Public Administration, or a tax on the issuing of a certificate, are always the same for everyone and in every case.

For other more sophisticated taxes, the tax is variable, which means that once the taxable event has taken place, one element of it is measured and, depending

on the result, the tax fee will be different in each case. The usual mechanism applied in the case of variable taxes is the following:

Once the taxable event has taken place, it is quantified, a transaction that gives rise to the so-called taxable base, generally expressed in currency units. A tax rate, normally a percentage is applied to the taxable base, and this activity results in the tax fee. In some cases, other components may be applied, such as certain kinds of deductions or allowances.

The most important taxes are variable. A clear example of this is Corporate Income Tax. In this tax, the tax base is the amount of profits or losses resulting from the activity of the corporation and from its accounts, to which certain adjustments are made in accordance with the mandate of the law, adjustments that lead from the accounting result to the taxable result or taxable base. Once the taxable base has been calculated, a tax rate is applied, and this gives rise to the taxable fee. It is clear that each different base results in different tax fees. Therefore, the main elements in variable taxes are:

- The taxable event.
- The taxable base.
- The tax rate.
- The tax fee.

This design of the taxes leads us to another important classification. Tax rates and, consequently, variable taxes may be proportional or progressive.

If a tax rate is proportional, it does not change as the tax base changes. This is the case, broadly speaking, for Corporate Income Tax. For a tax base of 10,000€, the tax rate is 25%, and for a tax base of 50,000€ or 1,000,000€, the tax rate remains at 25%. Therefore, as the tax base changes, the tax rate does not change, but the tax fee does.

In the case of progressive taxes, the tax rate increases as the tax base grows. So, for a tax base of 10,000€, the tax rate could be, for example, 10%, but for a tax base of 20,000€, the tax rate could be 25%. As can easily be seen, a change in the tax base has resulted in a change in the tax rate, and, consequently, in the tax fee. The increase of the fee in progressive taxes is more than proportional. The person who earns more not only pays more, but pays progressively more, because he pays a higher percentage. This progressivity is the feature that produces the quality of progressiveness in the system, a quality that, as

mentioned earlier, is a constitutional requirement. That said, progressiveness is only needed in some important or structural taxes. In the Spanish system, Personal Income Tax is progressive and is the main tax responsible for providing the feature of progressiveness to the system.

6.- The extinguishment of the tax obligation.

There are certain conditions that can result in the extinction of the obligation to pay the tax fee and its complementary concepts, interests and charges, but two should be mentioned as being the most important.

The first is payment. Once payment of the amount due has been made, the obligation is extinguished. Payment is the logical and most frequent way of extinguishing a tax obligation. Tax laws contain several different specifications regarding payment, such as the moment, the method and the place where payment is made, possible deferment of payments, payment by instalments, and so on. If payment is not properly made by a certain date, the Law provides several means and procedures for obtaining mandatory payment.

The second type of extinction to be mentioned is what we could call ‘limitation’, known in Spanish Law as ‘prescripción’. Limitation is based on the idea that, although the right to exercise rights, and the duty to fulfil obligations is very important, it is also essential that they be fulfilled or imposed within a certain period of time; 4 years in most cases in Spanish tax legislation. It is generally accepted that the absence of a diligent use of rights will result in the loss of these rights, and, accordingly, a waiving of any obligations involving other parties.

This way of acting on the part of the Law is based on the principle of legal certainty, which prevents a subject from having the right to exercise a right for years and years and then exercising it only when it is almost forgotten. The right to exercise a right carries with it the obligation to exercise within a certain period of time, i.e. diligently. Therefore, not demanding the enforcing of a right, accompanied by a total silence or inactivity for four years, results in the extinguishment of the right, as well as of the corresponding obligation. If the subject entitled to exercise the right exercises it in due form, or formally demands its enforcing, even if the right is not enforced, the counting of the deadline begins again from the date of the attempt. This can be done, for example, by an order

for payment, e.g. if the Tax Office or the taxpayer have the right to demand the payment or the refund of an amount of money and do nothing for 4 years, they lose the right. But if they try to enforce payment through an order for payment properly made at the end of year three, the counting of the four-year period begins again from that date. The same thing occurs when the part obliged to fulfil, formally acknowledges it, or tries to fulfil the obligation.

Another way of extinguishing the obligation to pay is through compensation. When a subject is the debtor but also has credits against the other party involved, there exists the possibility of compensation, removing any obligations between both subjects up to the limits of the coincidence of credits and debts.

The waiving or forgiving of tax debts, such as fees, interests and charges, is not possible and not available for the government or its departments, including the Tax Office. This may only be done by parliamentary law.

7.- Advance payments.

Once the taxable event has occurred, there is a period of time in which to declare and pay. On many occasions, and especially in the case of income taxes, there exists the obligation to make certain payments in advance, which will be deducted from the final fee when it is calculated. There are, broadly speaking, two kinds of advance payment: withholdings and instalment payments.

These advance payments are usually applied in relation to taxes on income, (Personal Income Tax, Corporate Income Tax and Tax on the Income of Non Residents), taxes in which are very important, and thoroughly regulated and controlled.

Withholdings.

In the case of withholdings, when someone pays taxable income to a beneficiary, he withholds a certain percentage and pays this amount to the Tax Office, but this payment is made on behalf of the beneficiary, who will be obliged to pay the total fee at a later time. The beneficiary will then calculate the total fee and deduct the sums withheld and paid in advance on his behalf. If these amounts are lower than the final fee, he will have to pay the difference, and if they are higher than the final fee, he will have the right to obtain a refund for the surplus.

Let us consider for a moment the situation of an employee who receives a salary of 25,000€ a year. When he receives each payment, he bears a withholding tax of 20 per cent, so 5,000€ have been paid in advance. Once he is obliged to declare and pay, the final resulting tax fee comes to 3,500€. He is therefore entitled to request a refund for the remaining 1,500€. If the final tax fee is less than the total advance payments, he will have to pay the difference.

The law imposes the obligation to withhold on those subjects who pay taxable income and who, moreover, are supposedly able to assume several administrative obligations or duties, but not, in general, on those individuals who are natural persons and are not acting as entrepreneurs or professionals at the moment of payment. It could be said, in general, that corporations and entrepreneurs are the subjects obliged to withhold when they pay income to other subjects, which these subjects will then have to declare and to pay for in their income tax declarations.

Instalments.

In other cases, it is the beneficiary of the income himself who is obliged to make certain advance payments on his future tax. In this case, the beneficiary must calculate and make certain advance payments that will be offset later and result in either a refund or in payment of the remaining amount. We can refer to these payments as instalments.

These two situations may be applied to the same subject, who receives some payments that are subject to withholdings and others that are not. These last mentioned payments oblige him to calculate and pay in the corresponding amounts for an income tax. It is therefore possible for a beneficiary to receive incomes from both entrepreneurs and corporations, which are subject to withholdings, and from clients who are not entrepreneurs or corporations, but only natural persons with no management infrastructure, and who therefore do not have to fulfil certain obligations, i.e. they do not have to withhold. The beneficiary must bear withholdings and, additionally, may be obliged to make certain advance payments until he reaches the percentage due to be paid.

8.- Charges of tax fees on third parties.

On other occasions, the law may oblige a subject to pay the tax fee but, at the same time, authorises and compels him to charge the exact amount of this tax fee to another subject, normally the person who has purchased something from him or to whom he has provided a service. This mechanism is frequently used in indirect taxes, which are usually levied on consumption and which require the tax to be borne by the consumer but, for practical reasons, the Public Administration prefers to interact with the provider of the service rather than the client. In these cases, the provider charges the tax fee to the consumer and pays these amounts separately to the Tax Office.

One thing should be noted regarding the tax fee charge. This charge has nothing to do with the general expression ‘charge’, generally understood as the effect of a tax on the price of a product or service. The expression ‘tax charge’ does not refer to this fact, and is completely independent of it. ‘Tax charge’ does not refer to the effects of costs, including tax costs, or specifically the charged tax cost, on the final price fixed by a provider, but to the legal obligation to charge the specific and perfectly delimited amount of a certain tax fee on a third person. Moreover, most of the cases in which the tax charge is established by law are related to certain rights to deduct borne tax fees, which implies that the charge will not influence the price, as will be seen with Value Added Tax, (VAT).

9.- The importance and legal regime of withholdings and charges.

These two mechanisms are extremely important. Let us consider each in turn.

In the cases of withholdings and instalments, the Tax Office continuously, or successively, receives amounts of money, which is of much greater benefit than receiving one lump sum once a year and then not receiving any more payments until the following year. On the other hand, the subject pays gradually (pay-as-you-earn) and does not pay one lump sum on a specific date.

Along with this greater benefit, withholdings and charges (but not instalments) made by a third person other than the subject who must bear the cost of the tax on his assets, are an important source of information. Withholders and subjects who charge tax fees hold important and strictly imposed obligations of information

concerning every payment and charge. They must communicate to the Tax Office many details about the transaction and the subjects involved in it.

As is known, the tax relationship is governed by public law and is easily understood, as it brings together a personal subject and a public department, i.e. it is a public relationship aimed at fulfilling public duties. In the cases of withholdings and charges, however, and as can easily be seen, the relationship is generally established between two individuals or corporations that are private subjects. Nevertheless, although both parties involved in the relationship are private and are acting as private subjects in the fulfilment of private interests, the part of this relationship related to taxes is regulated by Tax law, which, as is known, is a compulsory law that does not allow subjects a margin of discretion.

10.- The personal or subjective aspects of the tax relationship. Some useful expressions.

Behind every obligation or right that has just been analysed, there are subjects involved.

The person who has experienced the taxable event and who has thus demonstrated economic capacity is called a ‘taxpayer’, or ‘contribuyente’ in Spanish.

The person obliged to withhold, or ‘retener’, is known as the withholder, or ‘retenedor’. The obligation to charge is called the ‘obligación de repercutir’, and the charge is known as a ‘repercusión’. There are no special names assigned to the subject who charges or bears this charge, who is simply known as the ‘sujeto que repercute’ or ‘sujeto que soporta la repercusión’.

11.- . Tax infringements. Sanctions as a completely different concept from tax concepts.

The non-compliance of tax duties, when done through deceit, i.e. with wilful and malicious intent or with negligence, results in the imposing of penalties or sanctions. Although there are other kinds of sanctions, such as the privation of the right to contract with public entities or to apply for allowances or grants, most consist of monetary sanctions. Sanctions are a completely different concept from the other aforementioned material obligations. Their nature is completely different

and, by a Constitutional mandate, are subject to a different material and procedural regime from the obligations that represent the tax debt.

When the infringement is considered to be extremely serious, criminal penalties, including deprivation of liberty by a prison sentence, can be imposed, but only by the Judicial Power.

3.- THE MAIN TAXES IN SPAIN. A BRIEF OVERLOOK.

As it has been said before, there are three kinds of taxes in Spain, called “tasas”, contribuciones especiales” e “impuestos”. Any of the three administrations that are going to be mentioned hereafter can collect any kind of these. But, being the “impuestos” the most important, the analysis is going to be focused only on these. That way, the expression “taxes” will be usually referred to “impuestos”, regardless of the fact that the other kinds of taxes also exist.

The different taxes collected by each administration, at state-wide, regional and local levels, include the following:

1.- The State-wide system.

The state-wide system:

Direct taxes.

Direct taxes are levied on the income and on the property and assets, or wealth, of natural persons:

On income:

- Personal Income Tax.
- Corporate Income Tax.
- Non-residents income tax.
- Tax on inheritances and donations.

On general assets:

- Tax on the Wealth of Natural Persons, or property taxes.

Indirect taxes.

Taxes levied on consumption:

- Tax on transfers of property made outside of a business environment, certain business transactions, and the documentation of certain actions,
- Value Added Tax. For entrepreneurial or business transactions.
- Excises on the production or commercialization of certain kinds of products and services, such as electricity, fuel, alcoholic beverages and insurance, among others.

2.- Common regional system.

The Regions of Spain regulated by the general system, (all, with the exception of the Basque Country and Navarra, which have certain particularities within the general State frame), function as follows:

Ceded or transferred taxes.

- First, they have the right to receive a certain amount of some State taxes, defined as a percentage of the tax revenue.
- Additionally, they have certain recognized rights in some taxes, such as the right to regulate particular issues, predefined by the State through law.
- And, finally, they can manage and carry out the proceedings in several taxes.

Therefore, the State can cede, (some, two or all):

- All or a part of the collection of some taxes;
- the possibility of regulating certain specific questions in some taxes;
- the possibility of managing certain matters or carrying out certain procedures.

These possibilities are predefined, tax by tax, by State law.

The main transferred taxes are:

Personal Income Tax.

Tax on the Wealth of Natural Persons.

Tax on inheritances and donations.

And, in general, all indirect taxes.

Own taxes.

In addition to this, the Regions can design and enact their own taxes, different from the aforementioned. However, they are subject to certain restrictions when establishing new taxes. The most notable of these is that the Regions cannot tax those taxable events which have already been taxed by the State or by the city councils. For this reason, the Regions have frequently applied environmental taxes, which do not exist within the scope of the State or the city councils.

3.- Local taxes.

City councils cannot create and enact taxes, as they are not able to pass laws, only regulations subject to laws. However, they can develop certain questions regarding those taxes which have been specifically enacted for them by the State. The most important taxes which can be collected, and whose regulation may be partially developed, by the local entities are:

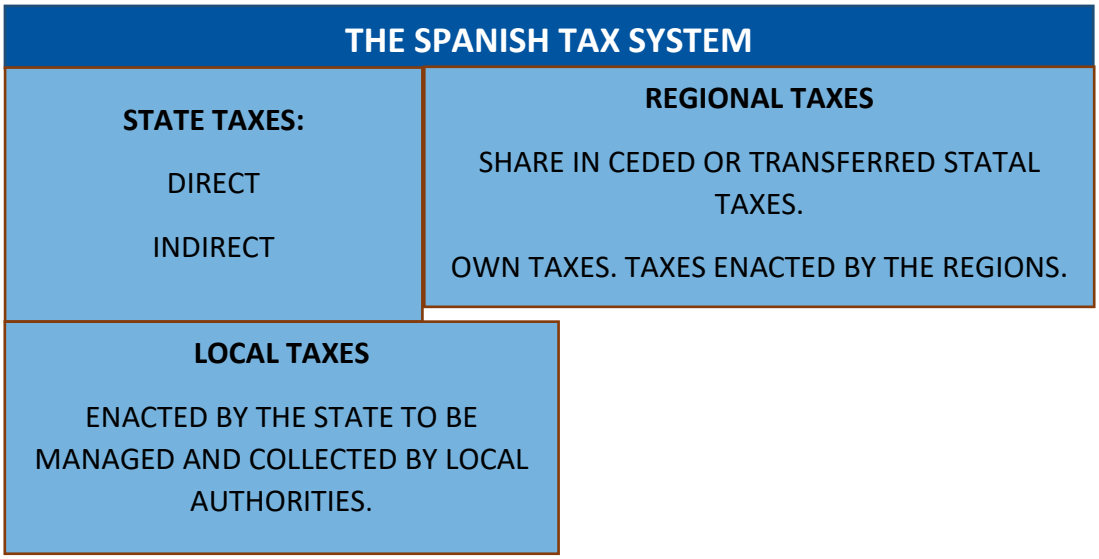
Tax on entrepreneurial or professional exercise.

Tax on the ownership of rights on immovable property.

Tax on the ownership of motor vehicles.

Tax on the execution of constructions and installations.

Tax on the increase in value of urban lands.



4.- THE MAIN DIRECT TAXES IN SPAIN.

As has already been said, the main direct taxes in the Spanish tax system are the following:

PERSONAL INCOME TAX. This tax is levied on the income obtained by natural persons residing within Spanish territory.

CORPORATE INCOME TAX. This tax is levied on the income of corporations residing in Spain.

NON-RESIDENTS INCOME TAX. Levied on income obtained by subjects, be they natural persons or corporations that, regardless of whether they reside in Spain, obtain some kind of income in Spain or an income which originates in Spain.

INHERITANCE AND DONATIONS TAX. Levied on inheritances and donations received by natural persons.

PROPERTY TAX. Unlike the taxes mentioned above, this tax is not levied on income, understood as a flow of wealth received by the subject, but on property, understood as a static concept, regardless of any income obtained.

1.- Personal Income Tax.

Personal Income Tax (PIT) is a direct, variable, progressive and periodic tax which, for determining the tax fee, considers not only the economic circumstances surrounding any income the subject may obtain, but also personal and family circumstances, such as the number of children under 25 years of age in the family, whether the subject or a person within the family is affected by a disability, and certain kinds of investments made by the subject, among others.

It is a progressive tax, as the tax rate grows as the tax base grows.

It is periodical, as it is declared and calculated every year.

This tax is direct, as it is levied on an unquestionable direct index of wealth, the clearest example probably being the income of a subject.

The tax is levied on all income obtained by a subject residing in Spain. Although there are exceptions, as in nearly everything we will mention later, the Law considers any person living or residing in Spain for more than 183 days every natural year to be a resident, with a natural year understood as the period between January 1st and December 31st. The number of days a person is

resident must be counted every year and will determine whether the person is subject to the tax or not. Once a person is considered to be resident, he must declare this tax on all income, no matter where in the world it was obtained.

The kinds of taxable income are diverse, and are thoroughly governed by law, as this tax is levied on several groups of income in different ways. Therefore, calculating this tax can be a little complicated.

The different kinds of income.

The tax is levied on several kinds of income:

- Those derived from labour relationships.
- Those derived from the exercise of professional or entrepreneurial activity in the market, as a self-employed worker.
- Those derived from capital exploitation.
- Those derived from several changes in wealth resulting from inputs and outputs of assets.
- Other special concepts.

It may be said that, in general, the Law taxes monetary income, as well as income in kind, i.e. the obtaining of certain goods or services, such as cars, housing, and tuition assistance for employees and their families.

Let us consider each of these in closer detail.

Labour income.

The law considers as labour income all compensation received as remuneration for labour carried out for an enterprise or the Public Administration by a salaried worker who is not responsible for organizing the enterprise or for making deals with clients. This is a kind of relationship between the worker and the entrepreneur which generates the right to earn a salary. These salaries are taxed as labour income. Moreover, some concepts are classified and levied in the same way, the main example being pensions, both public pensions and incomes derived from private pension plans.

Income from self-employment.

This is the case for self-employed workers who do not work for the entrepreneur, corporation, or public administration who contracted them. These self-employed workers form part of the mercantile traffic, the traffic of goods and services, and act within the market on their own behalf, which involves dealing with customers, organizing business activity and assuming the risks of the transactions carried

out. Accordingly, these kinds of income must be distinguished from labour income. The situation of a salaried lawyer working for a company or the Public Administration is not the same as that of a self-employed lawyer who is in a direct relationship with the client.

Income obtained from the exploitation of capital assets.

Income obtained by a natural person, and derived from his own wealth, can be subject to PIT. The main condition for an income to be considered as being obtained from capital, and therefore considered as capital income, is that the capital asset from which the income is derived must not form part of an entrepreneurial or professional activity. In other words, the assets must not be entrepreneurial or business assets.

These incomes can derive from movable, immovable or real property. There exist different kinds of income from capital assets and methods for calculating the net income to be taxed but, in general, it can be said that the most frequent kinds are the following:

Firstly, those resulting from the distribution of dividends by a corporation.

Secondly, compensation for lending capital, as when a subject lends or transfers an amount to a financial entity so that it may use the funds, and charges interest on the loan.

Thirdly, rental income, when a natural person rents out a property and, as a result, receives payment.

Income derived from the inputs and outputs of assets

This special kind of income is marked by two conditions:

- On the one hand, when a variation in the total amount of the subject's wealth occurs.
- On the other hand, this variation is the consequence of a change in the composition of the wealth, a change that usually consists of the input or output of an element.

When these two conditions occur together, the incomes are not considered in the same way as those incomes derived from the exploitation of capital assets, as mentioned earlier, but as capital gains or losses.

Capital gains and losses can derive, essentially, from two situations, inputs and outputs:

The first consists of the input of an income that changes the composition and value of a subject's wealth, such as prizes in games of chance. For example, consider a subject who wins a car or a house in a competition. This subject has won some wealth that is not derived from his own previously existing capital. There has been a gain in wealth, but not through the exploitation of a personal asset, as in the case of income obtained from capital assets.

The second consists of the output of an asset. The most frequent case is represented by the selling of an asset, i.e. a house. If a subject sells a house, he receives an amount of money and the house no longer forms part of his wealth. The subject must make a comparison between the purchase price of the house and its selling price. This subject will then make a profit or a loss, and this must be declared as it is subject to PIT.

As can easily be seen, the difference between income derived from the exploitation of assets and income derived from capital inputs or outputs consists of the fact that, in this last case, there is a change in the composition of the subject's wealth, i.e. there is both a qualitative and a quantitative change.

Other kinds of income

This tax covers other additional incomes, the most important of which are certain kinds of presumptive income.

Taxable bases in PIT

PIT is extraordinarily thorough, in that it categorizes and measures every kind of income differently, with the different kinds of income being classified into two groups which are subject to different methods of taxation.

PIT distinguishes between:

A. So-called "general income", i.e. all income other than 'income derived from savings'. The sum of other incomes, i.e. from salaried labour or self-employment, income derived from capital assets or composed of capital gains not categorized as being 'derived from savings', is taxed according to a progressive rate.

B. 'Incomes derived from savings':

- Incomes derived from movable capital assets, such as dividends.
- Incomes derived from the transfer of a capital asset, consisting of income derived from the output of assets, such as the sale of a house.

The sum of these two incomes is taxed according to a proportional tax rate.

The Law contains previsions to prevent the taxation on certain amounts considered as vital minimum, or regarding to specific situations, such as family situations or disabilities.

In general, PIT is accrued on December 31st, but declaration and payment are generally made between May and June of the following year.

Certain provisions are made in the Law so that, under certain circumstances, the members of family units can declare, calculate and pay the tax together, i.e. jointly.

2.- Corporate Income Tax

Corporate Income Tax (CIT) is an important figure of direct taxation. This is a state tax, not ceded to regions in any of the possible competences, i.e. collection, regulation or procedural actions.

The law that governs this tax contains the so-called 'general' regime, as well as certain special regimes, i.e. for corporations with a low turnover, joint ventures and the mining industry, among others. But there are two kinds of corporative subjects whose legal tax regime is contained in other different laws: cooperatives and non-profit organisations.

CIT is a direct tax levied on the income of entities, mainly corporations. It is a periodic and, broadly speaking, proportional tax, as the tax rates stipulated by law are usually proportional.

The taxable event is the attainment of income by the subject. The subjects subject to this tax are legal entities, mainly corporations but sometimes other kinds of subject, such as joint ventures and pension funds. Public entities, such as the State, are subjects but enjoy an exemption, and certain others, such as non-profit organisations, enjoy an exemption, (total in some cases, and partial in others), for income derived from contributions made by people whose sole aim is to help others, generally through donations, or for income derived from certain activities run by the non-profit entity that form part of its legal registered aims and are conducted without any profit-making intention.

In order for a corporation to be subject to this tax, it must reside in Spain, i.e. it must be a 'resident' of Spain. The law defines as residents those corporations that fulfil any of the following conditions:

- The corporation was constituted, or founded, in accordance with Spanish law.
- Its registered office is located in Spanish territory.
- The main headquarters or head office, or the place where transactions are directed and carried out, is located in Spain.

Once it is considered that a corporation resides in Spain and, as a result, is considered to be a taxpayer, it must declare and pay taxes on all income received from around the world, no matter the place or residence of the payer, or of the activity carried out to generate the income, (global income).

Regarding the taxable event and the taxable base, it is of interest to keep in mind one fact that differentiates Corporate Income Tax from Personal Income Tax. Unlike Personal Income Tax, which distinguishes between different types of income and uses different rules for determining and calculating their tax rates, Corporate Income Tax is a 'simple' tax, which means that it does not differentiate between the different kinds of income: once an income is considered to form part of the total income to be taxed, it is subject, broadly speaking, to the same regime of quantification and the same tax rate as others.

Regarding the measurement of the tax base, it is, in principle, quite simple from a fiscal, i.e. taxation, point of view: the tax base coincides with the accounting results. However, certain questions should be mentioned. Despite what has just been said, several adjustments are mandated by fiscal law. These adjustments can be positive or negative, and their underpinnings are related to the large differences between accounting laws and Tax laws. While accounting regulations, due to their nature, allow the subject a certain degree of elasticity, based on criteria such as accounting prudence, Tax laws cannot allow the subject important or wide margins of discretion, but define concepts and measurement procedures in a very narrow and strict way, mainly to avoid certain kinds of manoeuvres for deferring or even avoiding payment of the tax.

Therefore, with regard to the measurement of the taxable base, the starting point is the accounting result, but certain positive and negative adjustments must then be carried out based on this result.

Positive tax or fiscal adjustments are applied in those situations in which there exist accounting expenses that cannot be calculated for tax purposes, or that must be calculated to a lower amount. This is the case, for instance, for the

payment of a sanction. Sanctions will, of course, form part of the results of the entity, but they are not deductible for CIT purposes. Therefore, if the accounting allowed the deduction of the fee in order to determine the accounting result, the amount of this fee must be added to determine the taxable base. The same situation occurs when the expenses to be taken into consideration for accounting purposes are higher than the amounts allowed by Tax laws, e.g. when accounting rules allow a provision to prevent possible insolvencies and allow the subject some margin of discretion for determining the amount of the provision and, unlike in accounting, the taxable base sets limits on the amounts to be taken into account. In these cases, when the accounting amounts are higher, the difference between these and the limits established by Tax law must be added to the taxable base, thereby constituting a positive adjustment.

Let us consider, for instance, a fine of 1000€. This is an accounting expense but not an expense susceptible to be deducted for tax purposes. Therefore, a positive adjustment, adding 1000€ to the taxable base, must be made.

Tax law sometimes prescribes that certain kinds of income, or certain amounts of income, be computed, even when these incomes may not have actually been obtained, as may be the case for activities carried out in tax havens. When certain conditions exist, such as a lack of information, the corporation must compute a theoretical income, irrespective of the real amount of income received.

On other occasions, the tax adjustments are negative. In some cases, the deductions allowed by Tax laws may be greater than the amounts derived from the accounting rules. This may happen, for instance, when a fiscal law allows deductions for the depreciation of fixed assets that exceed the accounting limits. These kinds of legal provisions are intended to facilitate tax benefits for subjects. If the accounting criteria admit a depreciation consideration for a fixed asset, such as a machine, of 10% per year, and Tax law allows an accelerated depreciation of, for instance, 20%, this difference makes the taxable base lesser than the accounting result and results in a negative adjustment. The same situation can occur when the law allows what is generally known as freedom to depreciate certain kinds of fixed assets. In these cases, the subject is allowed to calculate into his taxable base, if he decides to do so, a deduction for the total cost of the asset from the moment of purchase. It is clear that accelerated depreciation, or depreciation freedom, produces a deferral in the payment of the tax, because it

allows sums of money to be deducted during the first years of use of the asset that will not be deducted in the future. In this way, if a subject is entitled to assess the depreciation of an asset, for accounting purposes, at 10% of 50,000€, and the tax limit is double that figure, there will be an account deduction of 5,000€, and a deduction on the tax base of 10,000€. In this case, a negative adjustment must be made for 5,000 extra euros.

Once the taxable result of the current exercise is calculated, the subject can deduct the negative tax bases proceeding from previous exercises, so that he can assess the final tax base. If previous negative bases total a larger amount than the current amount, the base of the current exercise cannot be converted into a negative amount. The remaining negative amounts from previous years can be deducted in successive exercises.

Once the taxable base is calculated, the tax rate must be applied. Corporate Income Tax regulates several rates, depending on different factors or situations, e.g. non-profit organisations, pension funds (0%), companies with a low turnover, and some others. But, in general, the rates are always proportional, which means that when a corporation finds the appropriate rate, it will apply it regardless of the value of the tax base.

In addition to what was previously explained, some deductions can be applied to the tax fee resulting from the application of the rate to the base, e.g. for employing disabled persons, or undertaking research and development projects.

CIT is a periodical tax; the taxable period, or period for taxing income, coincides with the financial or social year, a period of time registered with the company statutes. But in any case, the tax period can exceed twelve months, and so, if the social year is a period of more than twelve months, the tax period will be of twelve months. Once the taxable period is over, the accrual of tax is produced. Six months after the accrual, there are twenty days to declare, calculate and pay, if this is the case, the tax.

3.- Non-residents Income Tax.

This tax is levied on income received by non-residents in Spanish territory which originates in Spain. This tax closes the circle composed of PIT, CIT and itself,

which are levied, as a general concept, on income. Non-residents Income Tax is a direct tax, in exactly the same way as PIT and CIT.

The rules for determining whether a subject is resident or not are provided by Personal Income Tax.

The tax is levied on those cases in which a natural person, or entity, being non-resident in Spain, receives income that originates in Spain, or which has been earned in Spain, a situation that includes several cases, the main of which are the following:

When a person comes to Spain and, without satisfying the conditions necessary to be considered as a resident, earns income in Spain by, for example, providing some kind of service.

When a person, without coming to Spain, obtains income paid by a resident in Spain, i.e. when a Spanish corporation pays an amount to a person or corporation that does not reside in Spain and has not come to Spain, but the cash flow has left Spain.

When the income is derived from assets located in Spain, i.e. in the case of the renting out or selling of land or flats located in Spain, but is conducted by a non-resident owner, who receives the income.

The two most important modalities for being subject to this tax are the following:

- The subject may have set up in Spanish territory what is known by law as a ‘permanent establishment’. A permanent establishment is a location in Spain that belongs to a non-resident, and which operates continuously. Examples of permanent establishments include mines, shops, branches, offices, department stores and other kinds of installations. Note that in all these cases, the establishment in Spain is not an entity with legal personality. If this were the case, it would be taxed as a resident. It is, instead, a mere establishment belonging to a subject, with legal personality, residing outside of Spain.

  In the case of permanent establishments, the rules to be applied are mainly those contained in Corporate Income Tax, and the establishment is taxed on all its global income. The tax functions as a periodical tax.
- In other cases, the tax is levied on isolated transactions, with some carried out independently or separately from others. In these cases, the tax is accrued at the moment of each transaction, and operates, in

general, as a proportional tax. Therefore, each accrual implies a declaration and payment of the tax.

4.- Inheritance and Donations Tax.

Inheritances and donations are subject to taxation in Spain, paid by the person who receives the goods or money. Inheritance and Donations Tax is levied on income but, unlike the three taxes seen above, only in some very specific cases.

The tax is only levied on natural persons; corporations must pay Corporate Income Tax on any inheritances and donations received. Any income subject to inheritance and Donations Tax obtained by natural persons is not subject to Personal Income Tax.

The accrual is produced at the moment of death of the deceased or at the moment of the donation and, if there are several beneficiaries, each is taxed for their share of the inheritance or the donation. It is a progressive tax, which takes several factors into account, such as, of course, the amount received, the degree of kinship or the previously existing fortune of the subject who receives the inherited or donated wealth.

5.- Tax on the Wealth of Natural Persons.

It has been said on many occasions that this much debated and highly controversial tax, will soon disappear. Nevertheless, it is still currently in force. It is levied, not on the receiving of income, but on the ownership of wealth, and on the total amount of the wealth. The taxable base is composed of the addition and subtraction of all the assets, rights, debts, and burdens on wealth, quantified on December, 31st of every year.

Only natural persons are liable to pay this tax, which establishes an important exemption regarding the tax base, for which no obligation of payment exists.

5.- THE MAIN INDIRECT TAXES IN SPAIN.

1.- The Tax on Transfers Made Outside of the Sphere of Business.

This is a complex tax which is levied on three kinds of transactions.

- First, those which consist of the transfer of goods or rights from one subject to another, where these transactions are not business transactions, but are made outside of the entrepreneurial or professional activity; i.e. the sale of a good by a person who is not an entrepreneur, or maybe the sale of a good by an entrepreneur, but completely outside of his entrepreneurial activity.
- Secondly, certain corporate transactions, such as capital contributions at the moment of creation of the corporation, increases in capital and, in some cases, capital reduction or liquidation of the company.
- Thirdly, the documentation of certain specific acts.

The most interesting transaction subject to taxation, according to the aims and contents of this course, is the first - the transfer of goods outside of a business environment. In this case, the taxpayer is the purchaser, and the rateable base is the fair market value of the transferred good, regardless of the actual price paid. The accrual is produced at the moment of the transaction, and must be declared and paid to the Tax Office within a period of one month.

The tax is levied on certain other transactions, such as leases.

The tax rate is a proportional percentage, between approximately 2 and 7 per cent, depending on the nature of the good, on whether it is movable or immovable, and on the Autonomous Community where the transaction takes place.

2.- Value Added Tax.

Introduction.

The Value Added Tax, (VAT), is the cornerstone of the indirect tax system, not only in Spain, but in every country of the European Union. It is the main piece of

the indirect tax subsystem, and one of the main pieces of the whole tax system. Its application is compulsory in all the member states of the EU.

VAT is levied on those transactions which occur within an entrepreneurial activity. This is one of the most important differences between VAT and the tax on transfers referred to above. In general, as there are exceptions, a transaction is considered to have occurred within an entrepreneurial activity when the subject who carries it out, i.e. the person who supplies the good or provides the service, is an entrepreneur acting within the scope of his entrepreneurial or professional activity.

VAT is a multiphase tax levied on each and every one of the transactions conducted at every phase of production or commercialization of a good or service. Its aim is to tax consumption, but it is designed to impose the obligation to declare and pay, not on the consumer or purchaser, but on the seller or provider. This subject must charge VAT to the following subject in the chain of production and commercialisation. This situation is repeated until the end of the chain, where the consumer is situated. The consumer cannot charge the tax to any other person, as this person simply does not exist; there is no further trade transaction possible.

Those subjects who have purchased goods or services in order to provide new business-related goods or services and, accordingly, have charged VAT to the following subjects in the chain, have the right to deduct all the VAT amounts paid when they made the purchase. This is because the right to deduct only exists for those who can demonstrate that charge.

The consumer is not the subject, but the person who purchases goods or services for personal use, not in order to produce more goods and services. Therefore, there is, broadly speaking, an important difference between the VAT subject and the consumer; the VAT subject bears the VAT costs at the moment of the purchase, and later charges VAT when he sells the good or provides the service to the next subject in the chain. Only those subjects who can show that they have charged VAT have the right to deduct the borne VAT. The consumer or, in legal terminology, the end consumer, bears the VAT fees but, as he cannot charge another subject because the purchase was made for personal use, he cannot deduct the borne VAT, and must bear it as a final expenditure on his wealth.

The mechanism of charge and deduction transfers the final expense to the end consumer, such that those entrepreneurs who play a part in the production chain are completely free of tax fees. VAT is levied on consumption, but the obligations to declare and pay are borne by the entrepreneurs in the chain.

Both the charging of VAT quotas and the deduction of borne quotas are strictly compulsory for subjects, are not optional, and are usually seriously regulated and controlled.

The functioning of this system is, essentially, as described in the following table, assuming a trade margin of 100%, and a tax rate of 10%.

ENTREPRENEUR	ACQUIRES (buys or receives a service)	INPUT VAT	PROVIDES (sells goods or services)	OUTPUT VAT	PAYMENT MADE TO THE TAX OFFICE
1	-	-	100	10	10-0: 10.
2	100	10	200	20	20-10: 10.
3	200	20	400	40	40-20: 20.
4	400	40	800	80	80-40: 40
END CONSUMER	800	80, (FINAL PRICE: 880; 800+80).	-	-	-
					TOTAL: 80.

As can be seen in the table above, none of the entrepreneurs assumes any cost due to the payment of the tax, because each of them, before paying the Tax Office, adds the VAT fee charged to the following subject and deducts the VAT rate charged to him earlier by the previous subject. They are therefore in a zero-sum game. It is the end consumer who bears the charges and who therefore cannot charge anyone else in the chain, as he has acquired the good or service for personal consumption and bears the expense on his wealth. No-one who does not charge has the right to deduct and ask the Tax Office for any kind of compensation or return.

The Taxable Event

Taxable events for VAT purposes are defined by a double method.

- First, by a general declaration which defines the general conditions and requisites in order for a transaction to be subject to VAT.
- Later, by defining specific kinds of transactions.

The elements to be considered in order to get an approximate idea of the VAT taxable events are the following, while taking into account that, as is usual in relation to VAT, there are significant exceptions that cannot be analysed in these pages:

- It mainly refers to the provision of goods and services.
- The transaction must be carried out, i.e. the supply of the good or service must be provided, by an entrepreneur or a professional.
- The taxable event must be carried out within the professional field of activity of the subject.
- It does not matter if the transaction is typical of the specific enterprise or activity, i.e. if a factory which usually produces toiletries sells a computer used for work purposes and which formed part of its fixed assets, it must charge VAT, because the event has occurred within the field of activity of the enterprise.

The aim of VAT is to tax consumption carried out within the borders of the EU. Accordingly, transactions in which consumption takes place outside the territories of the EU are not subject to taxation. Specifically, exports are not subject to taxation, and the exporter has the right to obtain the refund of the VAT charged to him in the previous process to the transaction.

Although the law states that the transaction must be onerous in order for it to be subject to VAT, this is not completely true, as most gratuitous transactions conducted by an enterprise are also subject to taxation, such as any donations made and the consumption or use by the enterprise or entrepreneur of merchandise or services that, therefore, are not destined to be sold or provided to third subjects.

After these general questions, the VAT rules regulate the specific taxable events.

- Internal transactions:
    - Supply of goods.
    - Provision of services.
- External transactions:
    - Imports.
    - Exports.
    - Supply of goods between different EU States.

The most important differences between Tax on Transfers Made Outside of the Sphere of Business and VAT.

General criteria.

VAT is levied on different taxable events, e.g. the supply of goods and services and certain exterior transactions, such as imports and exports, among others. The tax on transactions made outside the entrepreneurial scope is levied on, among other taxable events, the supply of goods. As can easily be seen, one of the taxable events is the same in both taxes: the supply, delivery or handing over of goods. The nature of the subject that provides the good or service and the area or sphere in which the provision is carried out determines whether one tax or another is applied. Supplies, deliveries, made by an entrepreneur within the field of entrepreneurial activity are subject to VAT. Supplies, deliveries, made outside of the entrepreneurial field of activity are subject to tax on transfers. Of course, supplies made by an entrepreneur, but outside of trade activity are treated as non-commercial, entrepreneurial or professional events. The aim of VAT is to submit commercial events to taxation, and consequently, events carried out by entrepreneurs or professionals, but outside of their business activity do not fall within its scope, such as the sale, by an entrepreneur, of an object that has never formed part of his enterprise, but has only been used for personal consumption or use.

Under no circumstances may the supply of a good be subject to both taxes. However, the situation becomes a little more complicated when the supply or provision of a service involves real estate, such as the sale or renting of a house. In several cases, real estate supplies are subject to VAT but frequently enjoy certain exemptions. In these cases, the supplies are subject to the tax on transfers, even when performed by an entrepreneur within the scope of his business activity. As can be seen, there is a difference between real estate and other kinds of goods. If a supply is subject to VAT, but enjoys an exemption, it is simply not paid. But if the exempt supply involves real state property, then a tax on transfers must be paid.

Other differences between the treatment of one transaction and another are significant. Two should be noted carefully:

First, the taxpayer is different. With VAT, it is the supplier, whereas for tax on transfers, it is the purchaser.

Secondly, and most importantly, the taxable base in VAT consists of all the issues or concepts that compose the remuneration of the transaction, whereas, in the tax on transfers, it consists of the 'real' or 'market' value of the supplied good. As can easily be understood, the 'real value' is a separate concept, which often represents a different amount from the remuneration or payment received for the good. The 'real' or 'market' value is always an estimate based on the average market price or on expert assessment, the two most frequent methods for assigning a value to a good.

Charges and deductions. Charge on outputs and deduction of charges on inputs. The taxpayer and the end consumer in VAT, and the main differences between them.

VAT is a somewhat paradoxical tax, as it is levied on consumption but considers the taxpayer to be not the consumer, but the provider or supplier, who obtains an added value, the precise opposite of consuming. The taxable event is not the consumption but the receiving of income. In order for the consumer to assume the cost of the tax, the law strictly imposes the obligation for the provider, or taxpayer, to charge and collect the tax fee from his client. If the client is an entrepreneur, and acts as such at the moment of purchase, i.e. he purchases for professional or entrepreneurial reasons, he can deduct the fee paid. But if he is acting outside of an entrepreneurial activity, he cannot deduct any amount. This is the difference between the taxpayer and the end consumer.

The taxpayer bears the input VAT and afterwards charges output VAT to his clients. As he charges, he can deduct, because charging is a necessary requirement for being entitled to deductions on input VAT. But the end consumer does not purchase for his professional or entrepreneurial activity, and therefore does not charge any output VAT, as these outputs do not exist. He acquires for his own consumption or enjoyment, and consequently is not allowed to deduct the input VAT that he has paid; he must bear the cost on his own wealth.

Once a subject is able to demonstrate that he charges VAT to others, he is entitled to deduct the borne VAT. A subject acting as a professional or entrepreneur pays to the Tax Office the resulting sum to be deducted from the VAT amount charged on his outputs, the VAT amount borne during his purchases. In this way, no entrepreneur bears the VAT cost at the expense of his own wealth, which remains the same. The end consumer is in a totally different

situation altogether. As he does not charge VAT, he is not allowed to request a deduction or refund for the amount paid. He must therefore bear the cost on his wealth. In this way, if the regulations are respected, no entrepreneur will bear the VAT costs, as they are transmitted to the following subject in a kind of chain which ends with the end consumer, who has acquired the good or service for his or her own consumption.

The end consumer remains unknown in the majority of cases, e.g. purchases made in retail shops where, unlike in the case of wholesale trade, the clients are not traders and are not required to identify themselves.

The moment of accrual of Value Added Tax.

Accrual is a very important matter in the tax system, as it refers to the moment when obligations and rights arise and the origin of duties or credits. VAT law considers several cases, some general and others more specific.

The general cases are simple: VAT charges are accrued at the moment of supply or provision of the service. This may be at the moment of importation or purchase of an intra-Community acquisition. Certain specific rules are considered by law:

- Cases in which advance payments are made. Although the accrual is generally produced at the moment of provision or supply, when advance payments are made, VAT is accrued for every payment, depending on the amount and the moment of this payment.
- Cases in which payments are delayed or deferred. In these cases, however, the VAT accrual is not deferred. For instance, if a contract specifies that delivery will be made on a certain date but payment of all or part of the price is postponed, such that it will be made sometime after the good has been received, the VAT charge must be made at the moment of receipt of the good, not at the moment of payment.
- Cases in which there are long-term relationships, normally longer than one year, and no provisions for the payment and charging of VAT have been made in the deal, or the provisions of scheduled payments are made in terms of over one year. Let us consider, for instance, the case of the leasing of a warehouse for a term of five years, and where one only payment is to be made, scheduled for the last day of the fifth year. In these cases, VAT is accrued on December 31st each year, for the

proportional amount, considering the time elapsed in relation to the total time.

Tax base and tax rate.

Although there are some exceptions, the general rule is that the tax base is composed of all the items that are included in the remuneration of the transaction. VAT law distinguishes between several cases, depending on the kind of transaction subject to taxation. First, it distinguishes between the tax bases of internal and external taxable events. It then distinguishes between the bases of intra-Community transactions and imports. As exports enjoy an exemption, the base will not be analysed.

Regarding internal transactions, it may be said that the base, in the general case of the supply of goods, includes the acquisition price, as well as several other items, the most important of which are the following:

- Expenses paid for containers or packaging.

  If packages or containers are returned, the base can be consequently modified, and proportionally reduced.

- Transport costs.
- Insurance costs directly related to the transaction.
- Some kinds of compensations, i.e. for damages.
- Taxes on the transaction, except on VAT itself, and certain specific cases. Note that, in many cases, other indirect taxes and VAT are not only compatible, but the other indirect taxes are included in the tax base to be subject to VAT.

On the contrary, some concepts are not included as part of the tax base. The most important are the following:

- Discounts.

  Two cases may occur.

  Discounts may be produced at the moment the invoice is made, or even earlier. The amounts of the discounts must then be reduced when the base is being calculated, so that the tax rate is not applied to them. The discounts must appear on the invoice, but they are deducted before the calculation of the tax.

  In other cases, discounts are not known when the invoice is made, so it is impossible to apply them, i.e. discounts for prompt payment, or due

to the volume of acquisitions. In these cases, once the discounts are known, the base, and consequently the tax fee, are reduced by the same amount.

- Certain amounts of money that the provider of the good or service pays in advance on behalf of the customer and which are returned when the invoice is made and recovered. These amounts do not form part of the base.

The general considerations regarding the base in the case of the provision of services are similar to those for supplies: the base is made up of the remuneration for the service and the complementary concepts to be paid by the customer.

The base in the case of intra-Community transactions is calculated in the same way as for supplies. It should be clear that intra-Community transactions always consist of the supply of goods, and never of services.

In the case of imports, the base consists of the dutiable customs value plus all the accessory or complementary expenses to be paid until the first destination within the European Union. Services cannot be imported or exported. Exports and imports always refer to the supply of material goods, as in intra-Community transactions.

In some cases, such as when a client goes bankrupt or becomes insolvent, or when there is a serious delay or default in the payment, the law allows a modification of the base fee until payment is made.

Tax rates in VAT

European law allows countries a certain margin of discretion for fixing their tax rates. Spanish law has established three tax rates:

- 21 per cent. This is the general tax rate. It is the most often applied, and is the rate to be applied when no specific norm assigns another different one.
- 10 per cent. Also known as the reduced rate, it is applied to certain transactions, such as the supply of substances or products fit for human or animal consumption, such as seeds, water, medicines, pharmaceutical products, several feminine hygiene products, houses supplied by the builder, the transport of people and luggage, hostelry services, public cleaning services, waste disposal and treatment, some sporting events, and cultural exhibitions.

- 4 per cent. Currently known as the super-reduced rate, applicable to bread, flour, eggs, books, newspapers, videos, some computer programs, and medicines for human use, among others.

It should be noted that, although VAT law provides three different rates, VAT is not a progressive tax, but rather a proportional tax. In a progressive tax, the rate increases as the base gets higher. For instance, the Personal Income Tax rate is higher for a base of 70,000€ than for a base of 45,000€. Unlike Personal Income Tax and other progressive taxes, with VAT, transactions subject to a tax rate of, for example, 21 per cent always pay the same rate, regardless of whether the base is 45,000€ or 70,000€.

Some questions regarding the charging and deduction of VAT.

The charging of the VAT fee is compulsory, and is not an option for the provider or supplier, who has certain legal rights to help him pass on the charge. Stipulations or provisos between the subjects involved in the transactions cannot modify the legal terms regarding the base on which the rate must be applied, or the rate itself, the time limit for passing on the charge, or any of the features and specifications connected with the obligation to charge. The charge must be made at the moment of formalization of the invoice, and the right to charge is lost if the charge is not made within a year of the transaction taking place.

The charge implies several legal formalities: it must be recorded in a document, normally the invoice, duly documented in appropriate books and, of course, declared on time.

The symmetrical part of the charge is the fact of having borne the fees charged. The client who has borne the charge can be, essentially, in two situations. He may be a person who, acting as an entrepreneur or professional, charges VAT to other people, and so the VAT borne is aimed at generating other VAT fees when he carries out new transactions. Then, as the tax has been borne to generate trade or business transactions, this person can deduct the amounts paid.

On the other hand, the subject who pays the VAT may be acting outside of the scope of his entrepreneurial or professional activity, i.e. he may be acting as a private individual and acquiring for personal use and enjoyment. The subject who purchases may also be doing so for business reasons, but where the services provided enjoy an exemption and, therefore, no VAT is charged on the activity. In this case, the subject does not have the right to deduct for any VAT paid,

because he may only do so when he is able to demonstrate that the goods or services acquired, for which VAT was paid, were devoted to generating entrepreneurial or professional transactions that resulted in him paying VAT.

To be able to deduct the paid VAT, the subject must be in possession of the invoice, or other appropriate document, and must have duly accounted the transaction, although in some occasions, and under certain circumstances, the VAT can be deducted, regardless some formal duties have not been accomplished correctly, if the reality of the acquisition can be proved.

The mechanism of deduction and possible refund of fees.

Every tax period, determined by law, the subject adds up all the VAT fees charged, and deducts all the fees paid. If the fees charged are more than those paid, the subject must pay the difference. If the result is that the fees paid are more than those charged, he can claim tax back from the Tax Office, which can be used to offset other fees charged by him in the future or to request a refund after January 1st of the following year. The deadline for exercising this right is four years from the aforementioned date.

Restrictions and limitations on the right to deduct borne VAT charges.

Once a subject is entitled to deduct, generally for borne VAT charges, he must bear in mind that several kinds of borne charges are not deductible or are not wholly deductible. In some cases, Tax law restricts the right to deduct the complete charge, or excludes the right completely.

Several constraints of the deduction are produced when the acquisition of goods or services is related to the private enjoyment of the subject, (maybe hostelry or restaurant expenses). On other occasions, the restriction operates because the acquisitions do not appear in the accounts, i.e. they are hidden goods or services.

But the main or most frequent problems regarding deductions may be produced in cases in which the subject acquires a good or service whose use is shared between business and personal or non-professional activity. This situation frequently arises with motor vehicles. It can also occur, for instance, with services, such as the case of an insurance contract valid for both entrepreneurial and personal risks. In many cases, a certain subject owns a vehicle that is used for both business and personal activity. This behaviour is considered legitimate, but the problem arises at the moment the deduction must be decided. The solution provided by law consists of allowing a deduction of 50% on the borne tax, unless

the subject or the Tax Office can prove a different percentage of use, in which case the proven percentage prevails.

On other occasions, the situation is different. In certain cases, the law completely restricts the right to deduct due to the nature of the services or goods acquired. The charges borne in the acquisition of jewellery, precious stones, food, beverages, alcohol, tobacco, eyeglasses and payments resulting from gifts or hospitalities to clients or employees, are not deductible. Obviously, the charges are deductible if the acquisitions are a necessary part of the running of the subject's business. A jeweller, for example, can deduct the charges resulting from the acquisition of jewels, or an enterprise whose activity consists of organizing events at which dinners are served can deduct the VAT charges paid when hiring catering services.

Several questions regarding the invoice.

The invoice is a fundamental document for controlling VAT, and is therefore governed by law, which makes reference to the moment at which it must be issued and sent, and the data that it must contain. The main data which must be included in an invoice are:

- The invoice number and, when applicable, the serial number.
- The date of issue.
- The first name and surname(s) of those natural persons, or the registered name of corporations, involved in the transaction, i.e. the provider or supplier and the purchaser.
- The tax identification number of all people involved in the transaction. The acronym in Spanish is C.I.F. or N.I.F., meaning the fiscal identification code or number.
- The address of each subject involved in the transaction.
- A brief description of the transaction, containing enough information to identify the main circumstances and components involved in the transaction.
- The tax base, and separately, the tax rate applicable to the transaction, as well as the resulting tax fee.

3.- Other indirect taxes. Taxes on the production or consumption of goods and services, or excises.

Introduction.

There is a group of indirect taxes that are levied on some kinds of specific forms of consumption. Unlike VAT, these taxes are not levied at each step or stage of the production and consumption chain, but instead only at the final stage of consumption.

These taxes are of high importance, for several reasons:

- They are able to collect significant amounts of funds, and do not usually require the existence of large management structures or complicated procedures.
- They are easily confused with the price. In other words, a subject will not likely be aware of the hidden indirect taxes included in the price paid for a good or service. This effect is more relevant in those cases in which the subject is acquiring a good or a service that he or she particularly likes. This circumstance could make him or her forget the cost of the tax, i.e. the tax included in the price of a bottle of good wine or the price of a new car. This feature of these taxes has led to them being known as taxes which have an 'anaesthetic effect'.
- In addition to the ideas mentioned above, these taxes often provide politicians with a perfect alibi or excuse for imposing them. Health and environmental reasons, among others, are usually the legal and political arguments used for taxing the consumption of certain goods, such as alcohol, coal, and tobacco. These arguments are, of course, very important, and taxes have a role to play in relation to this, but it's not always clear the connection between the taxes and the achievement of the aims declared, or the fact that the only increase of the tax will be enough in order to this achievement.
- It is of interest to mention one more thing regarding these taxes. Although it has long been believed that these taxes are unfair, this may in fact not be a realistic assumption. Many of these products are especially suitable or appropriate for taxation, as is the case for certain luxury goods and undesirable behaviour, such as the overconsumption of energy, alcohol,

tobacco or coal, and this allows the burden of the tax charges or expenses levied on them to be borne by those people who mainly enjoy them. In many cases, it is preferable to maintain at least some parts of motorways and airports, and even environmental costs, on those that use the goods or services subject to taxation, rather than completely maintaining these costs at the expense of general taxes, such as Personal Income Tax, which are often paid by people who are not able to use these goods or services. In other words, it does not seem to be a bad idea for a part of certain expenses to be paid by those who generate those expenses.

Main excises.

There are a large number of excises in Spain, but we will only mention the most important:

Tax on Alcohol and Spirits. The taxable event consists of the production in, or the importation into, Spain of alcoholic beverages. The taxpayers are those who produce or import these products.

Special Tax on Some Means of Transport. The taxable event is the first registration in Spain of cars, motorbikes, ships and aircraft, and, in some conditions, their importation. The taxpayer is the subject who registers a vehicle for the first time or introduces a vehicle into Spain. The accrual of the tax is produced at the moment of registration or importation.

Tax on the Retail Sales of Certain Kinds of Hydrocarbons, such as gasoline and gasoil. This is levied on the commercialization and consumption of these products.

Special Tax on Coal. This tax is levied on the use or consumption of coal, and the taxpayer is the producer or seller.

Tax on Insurance Premiums. This tax is levied on several kinds of capitalisation and insurance operations. The law provides an exemption for life insurance operations. The taxpayer is the insurer, who must charge the amount of the tax to the other contracting party. The fees are accrued at the moment of payment of each premium, and the taxable base is the amount of this premium.

6.- LOCAL TAXES.

In Spain, local political authorities are considered to have legal personality, and are able to make certain political and financial decisions. It is generally thought that, in order to be politically autonomous, a subject needs a certain amount of financial autonomy, and therefore local authorities are allowed to levy taxes. However, being unable to pass laws with the category or rank of a parliamentary law, they cannot create taxes or regulate the main questions concerning them. Local authorities can demand payment, i.e. they can collect several taxes, but the main framework of these taxes is created by parliamentary law. However, local authorities can regulate certain questions with some margin of freedom, some of which will be seen later. Moreover, they can assume the vast majority of the procedures related to these taxes, including inspections and collection, which, as in all administrative decisions, are subject to possible subsequent controls by the Judiciary.

Local authorities can levy all kinds of taxes which exist in Spain, ('tasas', 'contribuciones especiales' and 'impuestos'), but as the most important are those known as 'impuestos', which are unrelated to any specific administrative behaviour or action, we will focus our attention on these.

There are five 'impuestos' enacted by state law:

- Tax on the Ownership of Immovable Assets.
- Tax on the Practice of any Entrepreneurial or Professional Economic Activity.
- Tax on the Ownership of Roadworthy Motor Vehicles.
- Tax on the Execution of Certain Kinds of Buildings, Constructions, Reforms and Installations on Real Estate.
- Tax on the Increase in Value of Urban Lands.

1.- Tax on the Ownership of Immovable Assets.

This tax is levied on the ownership of immovable assets, as well as other rights not mentioned here. The tax is levied on urban as well as rural estates, regardless of whether there are constructions on them or not.

The subjects who must pay this tax are the owners of the full ownership of the good, (or some kinds of rights on the good, such as the right to use and exploit it), both natural persons and corporations.

The taxation period is the natural year. Therefore, if the acquisition is produced on a day other than January 1st, the period comprises the time between the day of acquisition and December 31st.

The accrual of the tax is produced on the first day of the taxation period, not the last.

The procedure for calculating the tax is based on the existence of a taxable base and a taxation rate, i.e. a percentage. The taxable base consists of an administrative assessment of the amount. This amount is established by the so-called ‘catastro’, or administrative dependency, which depends on the Department of the Tax Office, and whose main occupation is to draw up and maintain an inventory of all the real estate in Spain, each with its corresponding physical, legal and economic description. The value assigned to each realty is based on the reports and decisions of the ‘catastro’ experts. Therefore, this value is usually an approximation to the market value of the realty, but may differ, and consists of a formal administrative valuation. This value includes, and expresses separately, the value of the land and the value of the constructions or buildings that exist on it. Once the realty is registered in the aforementioned administrative office, it is assigned a reference code, consisting of letters and numbers, and which must be used and recorded when any act or deal with legal consequences is carried out. As can easily be seen, the value and the reference code are assigned by the central state.

The tax fee is derived from the application of the tax rate to the tax base. This tax rate, as a structural part of the tax, must be approved by parliamentary law, so it is approved by state law, but defines one lower and one maximum limit, and each local authority can fix the tax rate between these limits. In the case of urban lands, the lower limit is 0.4%, and the maximum is 1.1%.

Local authorities can also decide the enforcement of several tax benefits, always within the limits established by law, as in the case, for instance, of several discounts or allowances for large families.

2.- Tax on Economic Activities.

This tax is levied on the practice of entrepreneurial or professional activities, which are described in exactly the same way as for PIT. It is worth bearing in mind that this tax is not levied on the receiving of income, but only on the act of running an activity, regardless of whether this activity is run at a profit or a loss.

The taxation period is the natural year, but if the activity begins on a day other than January 1st, the taxation period is comprised of the period between the date of the beginning and the last day of the year.

The tax establishes certain exemptions, mainly related to natural persons. All natural persons enjoy a total exemption from this tax. Moreover, corporations also enjoy some tax benefits, especially during the two first years of exercise.

The method for calculating the tax is completely archaic and consists of the application of a list of activities that determine the tax fee for each one of them, sometimes taking external signs into account. Therefore, although there exist some more complications, it could be said that the tax fee is fixed by law, according to some external signs, such as the consumption of electric power, the number of vehicles owned by the enterprise, and so on.

3.- Tax on the Ownership of Roadworthy Motor Vehicles

This tax is levied on the ownership of certain kinds of vehicles, especially lorries, cars, motorbikes, and any others which can circulate on public roads. The subject is the owner of the vehicle. The taxation period is the natural year, except in the case where the acquisition is carried out on a day other than January 1st. The accrual of the tax is once again the last day of the term, as is usual in periodic local taxes.

The tax fee is that set by law for each base, and is defined according to the kind of vehicle, its horsepower, and how environmentally friendly or otherwise it may be. Local authorities are permitted by state law to increase the fee within a certain limit, and to decide the application of several allowances based, for instance, on the kind of fuel used, the characteristics of the vehicles and their impact on the environment, or whether they belong to disabled people.

4.- Tax on the Execution of Certain Kinds of Buildings, Constructions, Reforms and Installations on Real Assets.

This tax is levied on the taxable event of the construction of buildings, the carrying out of reforms, and even the installation of certain kinds of facilities. In general, all those actions that require a license from the local authority, such as an administrative urban license to ensure actions are legal and respect the norms, are subject to taxation. Once the action has been defined by law as requiring a license, it is considered irrelevant whether the subject obliged to request authorisation does so or not. The mere fact of acting, regardless of whether this is in accordance with the law or not, is subject to taxation.

The taxpayer is defined as being the owner of the building, the reform or the facility, and the person who pays for it and assumes the expenses is considered to be the owner.

The tax base consists of the real and 'material', or effective, cost of the action, a different concept from the total amount, from which some concepts are deducted, such as the fees of architects and other professionals regarding project management, business profit margins, design costs, safety compliance, and Value Added Tax. A tax rate, determined by each local authority and which must not exceed 4% is applied to this base.

5.- Tax on the Increase in Value of Urban Lands.

This is a highly controversial tax, which has been the object of several recent sentences by the Constitutional Court, which annulled some parts of its contents, mainly because the Court considered that in several cases the tax was unconstitutional. The law was redacted in such a way that it was implied that, regardless of the existence or not of an increase in the value of the land, or even when there was a decrease in value, the tax had to be applied. The Constitutional Court annulled all the provisions made by the law to that effect, and has forbidden the charging of taxes in those cases where an increase in value has not taken place.

The tax is levied on an increase in the value of urban lands, not on edifications or on rural lands, but only at the moment at which a transfer is carried out. Many times, the supply consists of just the urban land, but other times the supply

includes both the land and buildings. In these cases, the tax base is calculated only on the value of the land, not of the building.

There can be, essentially, two kinds of transfer of property:

Onerous transfers of property. In these cases, each party receives a service or good from another in exchange for another good or service. The paradigmatic case is the sale, or purchase, of something. One party supplies a good and the other pays a certain amount of money. In the cases of onerous transfers, the law determines the taxpayer to be the person who supplies the urban land.

Free transfers. In the case of free transfers, one of the parties carries out the transfer with the sole intention of benefiting the other party, without expecting any kind of reward in return. The most typical transactions of this type are inheritances and donations. In these cases, the law considers the taxpayer to be the person who receives the urban land.

One thing should be noted regarding this tax: not only is the taxable event subject to capital gains tax, but also to personal or Corporate Income Tax, or, in the case of free transactions, to Inheritance and Donations Tax. This is another reason why this tax is so unpopular.

Other reason why this tax is so controversial is its calculating procedure. The base is completely theoretical and consists of the application of a percentage on the administrative value of the land, an amount assigned by the ‘catastro’, i.e. an amount completely independent of any actual profit made during the transaction. The tax rate is applied to this base.

The tax is accrued at the moment the taxable transaction is carried out.