Spain enacts regulations on new CbC reporting obligations and amendments to transfer pricing rules

Executive summary

On 11 July 2015, Royal Decree 634/2015 was published in the Spanish Official Gazette, approving the new Spanish Corporate Income Tax (CIT) Regulations (the CIT regulations) which complement the provisions included in the Spanish Corporate Income Tax Law\(^1\) (CITL) that entered into force 1 January 2015.

This Alert summarizes the new Country-by-Country (CbC) reporting rules and amendments to the transferpricing rules set forth in the CIT regulations.

Detailed discussion

CbC reporting

On 1 January 2015, a new Spanish CIT Law entered into force (special attention must be drawn to transitory regimes) introducing, among other relevant changes, amendments that are in line with the Organisation for Economic Co-operation and Development (OECD) Base Erosion and Profit Shifting (BEPS) project.\(^2\)

In line with these amendments, new CbC reporting obligations and changes to the current transfer pricing documentation requirements have been included in the new CIT regulations. These rules are aligned with Action 13 of the OECD’s BEPS Project\(^2\) which aims to develop rules regarding transfer pricing documentation to enhance transparency for tax authorities.

The new CbC reporting obligations effective for fiscal years starting as from 1 January 2016 generally apply to Spanish tax resident entities which are the “head” of a group (as defined under the Spanish commercial law rules),\(^3\) and are not at the same time dependent of any other entity, whether Spanish resident or not, to the extent the consolidated group’s net turnover in the immediately preceding fiscal year exceeds €750 million.
In addition, these rules also apply to Spanish entities and permanent establishments (PEs) which are, directly or indirectly, held by a non-Spanish resident head entity when any of the following circumstances is met:

- The Spanish resident entity or PE has been appointed by its nonresident parent entity to prepare the CbC reporting. This circumstance is in line with the "surrogate Parent entity rule" established in the Country-by-Country Reporting Implementation Package of Action 13.
- The country in which the head entity is resident has not established CbC reporting obligations in similar terms to Spain.
- The country in which the head entity is resident has not signed an automatic exchange of information agreement with Spain in relation to these obligations.
- The country in which the head entity is resident has systematically failed to comply and this systematic failure has been notified to the Spanish tax resident companies or PEs before the reporting fiscal year end.

In all of the above cases, the CbC report shall be filed within a 12-month period from the close of the reporting fiscal year (i.e., companies subject to these obligations with FYE 31 December 2016 need to file the CbC report by 31 December 2017). A specific tax form will be published by the Spanish tax authorities for these purposes.

The content of the CbC report has not changed with respect to that set forth in the draft CIT regulations. The CbC report will have to include the following information per country on an aggregate basis:

- Group’s revenue, distinguishing between that derived from related and unrelated parties.
- Accounting result before CIT or a tax of similar or analogous nature.
- CIT (or tax of similar or analogous nature) effectively paid, including withholding taxes.
- CIT (or tax of similar or analogous nature) accrued, including withholding taxes.
- Share capital and equity at the end of the fiscal year.
- Average number of employees.
- Tangible assets and real estate investments, different from treasury and receivables.
- List of resident entities, including permanent establishments, and the main activities these are engaged in.
- Other information that is considered relevant and, if applicable, an explanation on the data included in such information.

The information to be provided in the CbC report must be denominated in Euro. The draft CIT regulations established that such information should be denominated in the local currency of each jurisdiction. Nonetheless, it is not clarified what currency exchange rate should be considered. No specific penalty regime has been included for not filing the CbC report. Moreover, the CIT regulations do not include any reference to the use and confidentiality of the CbC information either.

**Transfer pricing documentation**

**Group documentation**

The group documentation rules specifically highlight two particularly contentious areas: intangible assets and financial activity. Both areas are subject to analysis by the OECD in the context of the BEPS Project.

Apart from documentation already required by current regulation, the following documentation must be included:

- Main activities of the group, with a description of the principal geographic markets where it operates, principal sources of revenue and supply chain of activities representing at least 10% of the group turnover.
- Information on the group intangible assets: general description of the group overall strategy with reference to the intangible assets’ development, ownership and exploitation.
− Both the location of the main facilities where the research and development (R&D) activities are carried out and who is responsible for those activities management are to be identified

• Amounts of the consideration paid for that purpose by group related entities

• Significant transfers of intangible assets must be reported as well, indicating the involved parties and countries, and amounts paid

• Financial activity

• Overall description of the group’ funding structure, including main agreements with entities outside the group

• Identification of the group entities carrying out main financing activities: incorporation country and effective center of management location

• A brief description of any advance pricing agreements in force and any other decision with any tax authority affecting the distribution of the group’ benefits among countries (As a result, the Spanish tax authorities will have access to any administrative decision, whether or not it relates to Spanish resident entities)

Documentation with regards to a group will not be compulsory for groups with turnover under €45 million for the previous year, as anticipated by the current wording of CITL.

Taxpayer documentation
In respect of taxpayer documentation, the regulation requires new information to be included:

• Management structure, organizational chart and people or entities receiving reports on taxpayer activities evolution, indicating the tax residence’ countries. It consists in the reporting structure, i.e., it aims at clarifying where relevant decisions concerning the group and entities’ business are made.

• Taxpayer activities and its business strategy description. Indication of intangible assets’ restructuring, assignment or transfer operations it has been involved.

• Main competitors.

• Reconciliation among data used in economic analyses with annual financial statements, when appropriate and relevant. Financial data of comparable and its source.

In accordance with section 18.4 CITL, it is emphasized again that the use of methods other than those stipulated therein are accepted, provided they are of common use. The regulation refers to future cash flow discount method, as an example, without limitation. Notwithstanding the aforementioned, the use of other methods must be sufficiently sustained, irrefutably supported, in any event, by means of verifiable references of assumptions and scenarios used to carry out the corresponding valuation.

Entities with turnover under €45 million (taking into account the entire commercial group turnover), the documentation must contain the following streamlined content:

• Nature and characteristics description, and amounts of related party transactions

• Complete identification of taxpayer and entities with which it carries out related party transactions

• Identification of valuation method used

• Comparables obtained and value or range of values derived from their use

Changes in the valuation rules and verification of related party transaction procedures
Section 17 of the regulations, in line with section 18.10 of CITL, allows the recharacterization faculty in the context of related party transactions system. Namely, the provision allows the possibility to replace the transactions declared by the taxpayer by those the Administration considers compliant with the arm’s length principle, or the construction by the Administration of those transactions not registered for accounting purposes by the taxpayer.
For the purposes of determining the market value, in addition to aspects stipulated in the text of the previous regulations, now it is necessary to analyze other aspects relevant to that process, such as: existence of losses, impact of public authorities' decisions, existence of location savings, or integrated groups of workers.

Thus, the regulation echoes very topical aspects at the moment concerning transfer pricing practice, such as location savings or integrated groups of workers, while there is no common international consensus on its treatment.

On the other hand, the regulations' express reference to the possible use of a range of values and of statistical measures to minimize the error risk due to comparability defects stands out, which seems to concern the compulsory adjustment of comparable values median in connection with provisions of section 3.62 of 2010 OECD Guidelines. However, possible statistical measures to be used by taxpayers are not specified, giving rise to some degree of uncertainty to the detriment of legal certainty.

Entry into force and enforceability
This documentation will be required for subsequent years and from the following dates:

- CbC information:
  - In all applicable cases, for fiscal years commencing from 1 January 2016, concluding the submission period after 12 months from the end of tax year it relates

- Group and taxpayer documentation:
  - New document requirements: for fiscal years commencing from 1 January 2016
  - During 2015 the documentation requirements in force up to date will still be applicable

Implications
Multinational groups with a presence in Spain should focus on the actions that may be necessary to ensure their ability to produce the required information, including preparing protocols for gathering the information and developing internal processes and responsibilities with regard to the CbC reporting obligations.
Endnotes


3. Article 42 of the Spanish Code of Commerce.


5. This systematic failure circumstance was not included in the draft CIT Regulations, and is in line with the Country-by-Country Reporting Implementation Package, albeit the Spanish rule does not contain any definition of the relevant concept.

6. Note under the draft CIT Regulations multinational groups meeting any of the circumstances mentioned were not obliged to file the CbC report until 1 January 2018. Now both Spanish and such multinational groups will have to file the CbC report as from fiscal periods starting 1 January 2016 onwards.

7. See EY Global Tax Alert, Spain proposes new country-by-country reporting obligations and changes to transfer pricing documentation requirement, dated 26 March 2015.

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