Law to foster the Spanish start-up ecosystem

On 1 December 2022, the parliamentary process for the approval of the Law to foster the Spanish start-up ecosystem, also known as the "Start-up Law", aimed at establishing a specific regulatory framework to support the creation and growth of start-ups in Spain, concluded. The Law will be published shortly in the Official State Gazette and will enter into force the day after its publication.[1]

The Law introduces significant new tax measures, particularly in relation to start-ups, stock options, the special tax regime for expatriates to Spain and carried-interest rights.

TAX MEASURES

1.1 SPECIAL TAX REGIME FOR START-UPS

The Law introduces the following tax advantages for Spanish start-up businesses (*empresas emergentes*) with respect to Corporate Income Tax ("**CIT**"), or Non-Resident Income Tax for companies acting through a permanent establishment or branch in Spain:

- **15% CIT rate** during the first tax year in which they earn taxable profits and in the subsequent three tax years.
- If the start-up is up to date with its tax obligations in Spain and submits its tax returns in a timely manner, payment of CIT corresponding to the first two fiscal years of **taxable profits can be deferred** for twelve and six months, respectively, without the need to post collateral and without accruing late interest. Payment must then be made within one month of the end of the deferral period.
- During the first two fiscal years of taxable profits, the start-up is also **exempt from the obligation to submit payments on account** (*pagos fraccionados*) of the indicated Spanish income taxes.

The Law gives the tax authorities the power to assess whether a business meets the requirements to be deemed a start-up. But these powers could in practice be affected by the fact that ENISA (which is a public company) also assesses specific aspects concerning the qualification of a business or company as a start-up (e.g. how innovative their business model is).

[1] We greatly appreciate the assistance of Alex Pié and Reyes Nieto in the preparation of this briefing.

1.2 INCENTIVES FOR INVESTORS AND EMPLOYEES

- The Personal Income Tax ("**PIT**") exemption in connection with the **award of shares or stock options to employees** is increased for start-up employees up to a maximum annual amount of EUR 50,000 per employee (instead of the general EUR 12,000 allowance). Additionally, for start-ups, for the exemption to apply it will no longer be necessary to award shares to all of the company's employees under the same terms; instead, it will be sufficient that shares are awarded within the context of the employer's general remuneration policy and that they contribute to the employees' stakes in the company's share capital (therefore returning to the wording of the law that was in force before 2015, although now only for start-ups). If awarding shares comes from exercising stock options that a start-up has previously granted its employees, the start-up criteria should be met when the option is granted (and not necessarily when the shares are delivered as a consequence of exercising the option).
- Income from shares or stock-option plans granted to start-up employees (who are not exempt under the allowance outlined above) will be subject to a special tax-imputation rule, whereby they will be taxed when the first of the following occurs (i) the shares are listed on a regulated stock exchange or any multilateral trading system, whether Spanish or non-Spanish; (ii) the shares are disposed of by the taxpayer; or (iii) ten years have passed. This is notwithstanding the valuation rule set out below, which applies when the shares are delivered.
- A special valuation rule is introduced for PIT purposes for employment income derived from the awarding of shares (including when they derive from stock options) to employees of start-ups. If independent third parties have subscribed a share capital increase in the preceding year, the shares in the Spanish start-up awarded to its employees will be valued for tax purposes at the same value at which such independent third parties would have subscribed for the start-up shares. For all other cases, the general reference to fair market value when the shares are delivered applies.
- The **general PIT tax deduction for investment** in new companies (not necessarily Spanish start-ups) is increased from 30% to 50%, and the maximum qualifying investment for the deduction from EUR 60,000 to EUR 100,000. Finally, investments in new companies can now be made during the first five years of a company's life (this was previously limited to three years).

  Additionally, Spanish start-ups enjoy specific privileges regarding this deduction: the investment period is increased from five to seven years and the start-up's founding partners or shareholders (as stated in the articles of incorporation) are not restricted from owning more than 40% of the start-up's share capital (individually or with related persons).

1.3 CARRIED-INTEREST RIGHTS (INCOME FROM MANAGING FUNDS LINKED TO ENTREPRENEURSHIP, INNOVATION AND PERFORMANCE OF AN ECONOMIC ACTIVITY)

The Law establishes a framework for "**carried-interest**" taxation – i.e. taxation on income earned by directors, employees or managers of specific closed-end alternative-investment funds and entities (as enumerated in the Law and including venture capital entities and funds) and of their management entities, from shares or other rights, including success fees, which grant special rights over the abovementioned closed-end alternative investment entities or funds (or their managing or group entities).

The Law states that carried-interest income – including success fees – will be taxed as employment income. Nevertheless, as has already been the case in the Basque Country and Navarre (which have introduced similar measures for carried-interest rights), if specific requirements are met then the income will benefit from a 50% **tax allowance for PIT purposes**: i.e. only 50% of the income will be subject to income tax, effectively triggering a tax of around 23–27% of the full gross amount, depending on the Spanish autonomous region in which the holder of the carried-interest rights is tax resident.

The following requirements must be met to benefit from the 50% income tax allowance:

- The special economic rights of these shares or rights are conditional on the rest of the fund's investors (of the entity or closed-end alternative investment fund) reaching a minimum guaranteed rate of return on the investments made by the collective investment vehicle – a rate of return that must be defined in the articles of association or regulations of the investment entity.
- The special shares or carried-interest rights must be kept by their holder as part of their assets for a minimum of five years, unless (i) they are redeemed or become ineffective before that; (ii) are totally or partially forfeited as a consequence of a change in the managing entity (in which case they must have been kept uninterruptedly up to the point these events occur) or (iii) upon the death of their holder. If applicable, this requirement will apply to the entities holding the shares or rights.

It is important to note that the 50% tax allowance for the carried-interest holder will not apply when the special economic rights derive directly or indirectly from an entity resident in a country or territory that is classified as a non-cooperative jurisdiction (i.e. a tax haven) for Spanish tax purposes, or in a country or territory with which Spain has not entered into a tax information exchange agreement.

1.4 SPECIAL INCOME TAX REGIME FOR WORKERS POSTED TO SPAIN

The Law eases the requirements for applying this special tax regime (the so-called **expatriates tax regime**) and includes new beneficiaries:

a) First, the regime can be applied if the taxpayer was not a Spanish tax resident during the five tax years preceding the taxpayer's move to Spain (as opposed to the preceding ten-year period that is currently required).

b) In addition, the reasons for moving to Spain that entitle a taxpayer to apply the regime have been made more flexible. In addition to those that already existed (in particular, as a consequence of a new job or an employer relocating an employee to Spain), the taxpayer can also qualify if they move to Spain to

   i. work remotely from Spain through the exclusive use of computer, electronic and telecommunication means and systems (in this case a travel order from the employer is not necessary). This requirement will be deemed fulfilled by employees who have a visa for international remote-working;

   ii. carry out in Spain an economic activity that qualifies as an entrepreneurial activity;

   iii. be a highly qualified professional who provides services in Spain to start-ups or who carries out training, research, development and innovation activities in return for remuneration that represents more than 40% of the total income he/she earns.

   The restriction preventing expatriates from obtaining income that would classify as obtained through a permanent establishment does not apply to the activities listed in (ii) and (iii). However, all such income is subject to taxation in Spain regardless of whether it is Spanish sourced or not, in the same way as is already the case for work income.

   The requirements to apply this regime are also extended to persons who become directors of a Spanish company: they are allowed to opt for the regime (if the other conditions are fulfilled) regardless of whether they hold a direct or indirect share in the company in which they are appointed directors. As an exception, persons who become a director of a company that is an asset-holding entity (within the meaning of article 5 of the CIT Law) may apply this regime provided they do not directly or indirectly hold 25% or more of that entity's capital stock (as was the case under the previous regime).

c) Moreover, the **expatriate's spouse and children** under the age of 25 (or those of any age if they are legally disabled), as well as the other parent of the children if both parents are not married, will also be entitled to apply the special regime (as already applies in the Basque Country territories) if they move to Spain at the same time as the expatriate or within the first tax year in which the regime applies. They too cannot have resided in Spain in the five preceding tax years and, roughly speaking, their net taxable income (*base liquidable*) must be lower than that of the expatriate.

   No employment requirements apply to them (they can in fact not work and still benefit from the regime).

d) Lastly, an exemption is introduced (in the same terms as in the PIT Law) for earned income in-kind obtained by the expatriate (or their family members, in accordance with the previous point).

However, a negative aspect is that the previously announced extension of the regime's application from six to eleven tax years has been omitted from the final wording of the Law.

Moreover, although the Law allows the regime to apply to those who moved to Spain after the Law enters into force, or in the previous year, it remains silent on the transitory regime applicable to individuals who are already applying the regime when the new regulation enters into force, as well as on what will happen to individuals who did not qualify for the previous regime when they moved to Spain but could qualify for the new one. A future amendment to the PIT Regulation would ideally resolve some of these issues.

1.5 OBTAINING A SPANISH TAX ID NUMBER AND NEW REPORTING OBLIGATION

Finally, the Law introduces the following measures regarding compliance with formal obligations and a new reporting obligation:

- **Obtaining a NIF/NIE.** The requirements for investors in start-ups that will not reside in Spain are simplified: they will no longer have to obtain a foreigner identity card number (NIE) and the electronic application to request a tax ID number (NIF) from the tax authorities is made easier.
- **New reporting obligation for CIT or equivalent or similar taxes for specific companies or branches**. In the context of corporate groups, the parent company of a Spanish group that prepares consolidated accounts and the annual turnover of which has exceeded EUR 750 million in the past two financial years must prepare, publish, deposit and make available a report on specific matters (income, employees, their activities, taxes paid, etc.) for CIT or equivalent or similar taxes. This also applies to branches incorporated in Spain by companies that are not subject to the law of an EU Member State. These obligations are intended to transpose Directive (EU) 2021/2101 of the European Parliament and of the Council of 24 November 2021 amending Directive 2013/34/EU as regards disclosure of income tax information by certain undertakings and branches and will apply for financial years starting on or after 22 June 2024.

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