

Special regime for expatriates in the Personal Income Tax Law.

From 1st January 2004 a new provision was established in the Personal Income Tax Law (PITL) by which those individuals that become tax residents in Spain, can choose to be taxed as non-residents if several requirements are met.

This provision was focused to improve Spain as a tax effective country to establish foreign multinationals. In the last years, several Laws have been implemented to achieve this goal, as Article 21 and 22 of Corporate Income Tax Law, that establish respectively exemption on dividends and capital gains derived of the participation in foreign subsidiaries and exemption on income obtained by foreign permanent establishments. With this purpose it was also approved in year 1995, the Spanish holding company regime, so called “*Entidad de Tenencia de Valores Extranjeros*”.

This new provision points out that individuals coming to Spain as a consequence of an employment contract, and that are considered tax residents in Spain, have the option to be taxed as residents or non-residents in the year in which the tax residency is obtained and in the five subsequent years. An individual is tax resident in Spain if:

- a) He is physically in Spain for more than 183 days in any calendar year or,
- b) The main centre of the individual’s economic interests is located in Spain, or
- c) The individual’s spouse (unless are legally separated) and minor dependent children are resident in Spain.

The main difference between taxation of individual residents and non-residents is that, residents are taxed on their world-wide income, meanwhile non-residents are only taxed on income obtained in Spain. Another difference is the tax rate applicable, since non residents are taxed at a 25% rate and tax residents are taxed at a progressive rate up a maximum 45%. Thus, this regime could be interesting for employees with a high level of income (i.e. foreign executives, sportsman, etc.). In addition, individuals with a high level of income outside Spain could get important tax advantages.

The requirements which in principle have to be met are as follows:

- § The individual has not been resident in Spain during the last 10 years.
- § The taxpayer is coming to Spain as a consequence of an employment contract.
- § The work is effectively carried out in Spain.
- § The individual is employed by a company resident in Spain or by a Permanent Establishment of a foreign company.
- § That the payroll income obtained is not tax exempt in the Non Resident Income Tax regime.

As established before, the main question in being taxed as non resident is that the tax is only levied on income obtained in Spain and in the case of payroll income it is taxed at a 25% tax rate. However, personal deductions for children, contributions for pension plans, etc are not applicable.

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