

**Ten proposals for the improvement of legal certainty within  
the scope of the reform of the Spanish tax system**

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## EXECUTIVE SUMMARY

Fundación Impuestos y Competitividad (“FIC”) considers it essential to improve the legal certainty of the Spanish tax system as a basis for improving the competitiveness of our companies and the location in Spain of companies from third countries. This improvement will lead to greater equity of the system and in the medium and long term will reinforce its capacity to collect revenue.

The FIC considers that the improvement of legal certainty should form a prominent part of the debate regarding the reform of the tax system which is currently taking place in Spain and, therefore, it considers it a priority that the above-mentioned reform includes measures aimed at achieving the following objectives:

- 1. To harmonise the rules, procedures and formal obligations existing in the various authorities and reinforce the obligation to coordinate, minimizing the uncertainty and cost for taxpayers arising from the multiplicity of authorities, rules and interpretations.**
- 2. To improve the process of creation of legislation, ensuring the technical quality of tax laws, social participation in debating them, non-retroactivity of legislative changes and the grant to taxpayers of a reasonable period to fulfil the obligations imposed by new legislation.**
- 3. To clearly and specifically regulate the anti-abuse measures of domestic tax legislation, avoiding the application of legal institutions unrelated to tax law and ambiguous measures which may give rise to litigation.**
- 4. To reduce the uncertainty existing in relation to the interpretation of tax rules, by more intensely and efficiently using the power to enact regulations and by establishing mechanisms which permit the achievement of certainty regarding the tax regime applicable to the specific case.**
- 5. To establish alternative systems of enhanced relations between the Authorities and companies.**
- 6. To establish alternative mechanisms for the resolution of disputes with the Authorities which permit the enhancement of legal certainty and reduction of litigation, such as arbitration, and adapt the procedural rules so as to speed up proceedings and quickly and effectively establish general criteria.**

- 7. To improve the mechanisms for resolution of disputes arising from the adoption of different positions by the public authorities of different countries when a Convention for the Avoidance of Double Taxation (“DTC”) is applicable and review efficiency and improve the existing instruments in order to provide greater legal certainty for taxpayers.**
- 8. To improve the regulation of some of the powers of review of the Authorities and limit them in certain areas (statute of limitations, procedure for imposing penalties, etc.) in order to avoid discretion.**
- 9. Review, systematisation and simplification of the countless formal obligations which are imposed on businesses/taxpayers.**
- 10. Modification of the system of penalties, avoiding automatic mechanisms in the imposition of penalties and ensuring that mere differences of interpretation do not have criminal repercussions.**

## **Ten proposals for the improvement of legal certainty within the scope of the reform of the Spanish tax system**

The quality of tax systems is increasingly measured to a greater extent by the degree of legal certainty which they provide. There is little purpose in approving tax measures aimed at favouring productive activity and job creation if their capacity to generate real results is limited due to a lack of trust of economic operators in relation to the subsequent interpretation and effective application of such measures by the authorities and in relation to the stable maintenance of such measures over time.

Legal certainty has a value in itself since it is a central element of the rule of law. However, in the tax area it is also crucial in order to achieve the basic principles of competitiveness, equity and sufficiency.

The connection between legal certainty and competitiveness is clear. Business decisions regarding investment, contracting or finance, including the first and basis decision (whether or not to undertake a new business activity), are largely long-term decisions, which must take into account to a great extent the degree of confidence offered by the tax system. Furthermore, legal certainty promotes free competition and in that way the effective allocation of resources.

The two most important worldwide studies which measure the factors which determine the competitiveness of countries are the Report on Worldwide Competitiveness and the World Competitiveness Yearbook, the former drawn up by the World Economic Forum (WEF) and the latter by the International Institute for Management Development (IMD). In both studies the confidence in and stability of each country's legal system is one of the basis aspects present in all the "pillars" for measuring competitiveness.

The improvement of legal certainty also serves equity, because it helps to avoid discriminatory or unjustifiably unequal treatment of persons or companies in objectively comparable situations.

As regards the sufficiency principle, in the medium and long term the capacity to collect revenue of a system founded on legal certainty is always greater - since it promotes the creation of wealth and the growth of tax bases - than that provided by an unreliable and volatile system.

In this document, Fundación Impuestos y Competitividad has identified the areas of the Spanish tax system to which the current tax reform should pay particular attention in order to enhance its quality from the perspective of legal certainty. A collection of proposals is briefly stated below.

**1. To harmonise the rules, procedures and formal obligations existing in the various authorities and reinforce the obligation to coordinate, minimizing the uncertainty and cost for taxpayers arising from the multiplicity of authorities, rules and interpretations**

- To harmonise the Spanish tax system (national, regional and local), avoiding excessive inequalities between taxpayers resident in different locations in Spanish territory and the fragmentation of the tax treatment of the business activity of a company when it is carried on in various Autonomous Communities (for example: environmental taxation).
- To unify the taxpayer's procedures and formal obligations (e.g. tax forms or obligations to supply information), establishing common systems and procedures coordinated between public authorities to avoid the current legislative "maze" and the proliferation of different formalities of the different territorial areas, which gives rise to legal uncertainty and reduces the competitiveness of companies.

**2. To improve the process of creation of legislation, ensuring the technical quality of tax laws, social participation in debating them, non-retroactivity of legislative changes and the grant to taxpayers of a reasonable period to fulfil the obligations imposed by new legislation**

- To avoid the abuse of the institution of the Royal Decree-Law in the tax area, restricting its use and, if it is used, proceeding to immediately have it pass through Parliament as an ordinary draft law.
- To grant to the Council of State sufficient time to be able to calmly analyse the proposals for legislative change, avoiding widespread recourse to urgent procedures in relation to taxation.
- To establish channels and promotion social collaboration in the process of producing legislation:
  - When it is possible, directly sending to members of Parliament the reports and opinion of third parties, such as associations, Professional Institutes or professional firms.
  - Obliging the Government to send to members of Parliament the reports and opinions received in the process of creating legislation.

- Establishing on a general basis public hearing procedures in significant tax reforms.
  - To create a professional team advising Parliament in relation to tax legislation, which can issue technical reports for members of Parliament on the measures proposed by the Government or analysed by the parliamentary groups and on comparative law, similar to the Joint Committee of Taxation in the U.S.
  - To provide certainty for the taxpayer in relation to legislative changes:
    - Reinforce the non-retroactivity of changes in tax law (of a medium to minimum degree), limiting the possible retroactive effects to exceptional situations identified quite clearly in the legislation.
    - Consider the “expectations of a right” created by the previous legislation when a legislative change is approved, by providing transitional periods for adaptation.
    - Ensure that legislative changes are adopted sufficiently before they come into force, so that taxpayers are allowed to establish adequate systems to adapt to them and incorporate the legislative framework into their business planning.
  - To draw up reports on the economic impact of important legislative changes, and make them public.
- 3. To clearly and specifically regulate the anti-abuse measures of domestic tax legislation, avoiding the application of legal institutions unrelated to tax law and ambiguous measures which may give rise to litigation**
- To clearly and specifically regulate the anti-abuse measures of domestic tax legislation, avoiding the application of legal institutions unrelated to tax law and ambiguous measures which may give rise to litigation with the Authorities when they are applied.

The interpretation of anti-abuse clauses must be restrictive at all times.

What seriously compromises legal certainty and should be avoided is the widespread de facto replacement of anti-abuse clauses by legal techniques for the avoidance of contractual deceptions, conceived for the law of obligations and contracts between private parties and in which the principle of freedom of contract prevails, as opposed to the principle of legality and the public and coercive nature which govern and define tax obligations.

**4. To reduce the uncertainty existing in relation to the interpretation of tax rules, by more intensely and efficiently using the power to enact regulations and by establishing mechanisms which permit the achievement of certainty regarding the tax regime applicable to the specific case**

- It is essential for the Ministry for Finance to effectively exercise its regulatory function, providing the Authorities and taxpayers with clear criteria for the application and interpretation of the legislation, ensuring that the criteria are of a public nature and are applied in a coordinated manner by the various bodies and officials. This involves:
  - Issuing detailed Regulations of the tax laws and implementing rules, which are not limited to questions of procedure, but rather clarify the more complex provisions, with the necessary degree of detail to facilitate the understanding and application thereof, using, where necessary, practical examples.
  - Approving and publishing general resolutions which establish criteria on subjects on which there are differences of interpretation.
  - On factual issues which give rise to extensive litigation, such as the deductibility of certain expenses or the degree of assignment to certain activities, establish presumptions by regulations, permitting evidence to the contrary by the taxpayer (similar to those existing in relation to the deductibility of VAT borne on vehicles or for per diems to be not subject to Personal Income Tax).
  - Reducing the periods for responding to binding consultations, reinforcing, where necessary, the bodies in charge of responding to them, in order to ensure that tax consultations are responded to quickly (the current period of six months is too long) and efficiently. In addition, in order to avoid discriminatory treatment against taxpayers, it should be compulsory for the Economic-Administrative Tribunals to apply the criterion of the Directorate General of Taxes when it is favourable to taxpayers.
  - Increasing the coordination between the State Tax Administration Agency and the Directorate General of Taxes.
  - Publicising all reports, instructions, resolutions and responses to consultations insofar as they involve an interpretation of the law or have legal effects (i.e. reports of the Sub-directorate General of Legal Regulation and Legal Assistance, all the resolutions of the Central Economic-Administrative Tribunal, etc.), thereby effectively applying Law 19/2013, of December 9, on transparency, access to public information and good governance.

- Drawing up and circulating data from time to time regarding the result of the proceedings in which a difference of opinion between the Authorities and the taxpayer has been shown.
- Creation of a new concept of “prior taxation agreement” (with characteristics similar to the “rulings” existing in other countries and in the Basque Country), so that the taxpayer can be certain about the taxation of a specific transaction or activity before engaging in it.

**5. To establish alternative systems of enhanced relations between the Authorities and companies**

- To develop and regulate alternative systems of enhanced relations between the Authorities and companies, which establish relations founded on mutual trust and reciprocal transparency, which are genuinely cooperative and fair, following the criteria of the last OECD reports on cooperative relationships.
- To encourage the participation of businesses in these systems of cooperation, eliminating the inspections of small risk areas and mitigating the system of penalties.

**6. To establish alternative mechanisms for the resolution of disputes with the Authorities which permit the enhancement of legal certainty and reduction of litigation, such as arbitration, and adapt the procedural rules so as to speed up proceedings and quickly and effectively establish general criteria**

- To establish alternative mechanisms for the resolution of disputes (arbitration) inspired by the practices of our neighbours (United Kingdom/Portugal).
- To extend the scope of revocation, admitting both partial revocation and the revocation of economic-administrative resolutions, especially as a means to conclude judicial review proceedings which may be affected by subsequent changes in legislation, case law or administrative criteria.
- To introduce the optional nature of the economic-administrative claim, especially in relation to assessments concluding inspection procedures, or when the challenge is based on the illegality or unconstitutionality of the legislation applied by the Tax Authority.
- To ensure access to the cassation appeal in order to be able to form case law on all disputed tax issues, overcoming the current obstacle of a very high quantitative threshold (600,000 euros for the ordinary cassation appeal).
- To introduce the possibility of the National Court and the Superior Courts of Justice being able to seek preliminary rulings, at least in relation to newly-



enacted laws, from the Supreme Court, in order to bring forward the establishment of case law.

- To admit the judicial appeal, for the sole purposes of establishing criteria, against the binding consultations of the Tax Authorities (Directorate General of Taxes).
- 7. To improve the mechanisms for resolution of disputes arising from the adoption of different positions by the public authorities of different countries when a Convention for the Avoidance of Double Taxation (“DTC”) is applicable and review efficiency and improve the existing instruments in order to provide greater legal certainty for taxpayers**
- To include in all the new DTCs an arbitration clause for the resolution of disputes similar to that included in the new agreements with Switzerland and the U.S., and renegotiate the existing DTCs so as to include it.
  - To effectively regulate the Mutual Assistance Procedures (MAP) and amicable procedures provided in the DTCs in order to guarantee their full legal effectiveness, ensuring that they are conducted with sufficient speed, and institutionalising the participation of the interested parties in the process.
  - The amicable procedures must be conducted before the administrative assessments are issued.
  - To study in depth the making of bilateral and, when possible, multilateral Transfer Pricing Agreements, establishing adequate procedures and providing the bodies in charge with the necessary resources.
- 8. To improve the regulation of some of the powers of review of the Authorities and limit them in certain areas (statute of limitations, procedure for imposing penalties, etc.) in order to avoid discretion**
- To expressly limit in the law the scope of the verification of tax credits and tax losses pending application from tax years that are statute-barred, as well as the requirement to maintain documentation for excessive periods.
  - To reinforce, on the basis of the estoppel principle, the binding nature of the conclusions reached in a certain inspection by the Inspection bodies.
  - Changes of criteria in applying taxes to a taxable person should only apply from the time that the Authority states them.
  - To clearly state the power to review the accounting result granted to the Authorities for the purposes of Corporate Income Tax (Article 143 of Royal Legislative Decree 4/2004 approving the Revised Corporate Income Tax

Law), so that it guarantees greater legal certainty for the taxpayer, consistent with the conclusions reached in the external audit reports (if applicable), and granting to the taxpayer the possibility to request a report from the accounting regulator (Spanish Institute of Accounting and Auditing (ICAC)) in the course of an inspection.

#### **9. Review, systematisation and simplification of the countless formal obligations which are imposed on businesses/taxpayers**

- There are too many formal obligations imposed on businesses/taxpayers which, in many cases, overlap between the different authorities and give rise to costs and risks not proportionate to the objectives pursued. Therefore, it is essential to limit them to what is strictly necessary, to simplify and make more flexible the manner in which data can be supplied, to avoid the existence of an obligation to convey the same information to different territorial or institutional authorities or at least to standardize the formats for presentation.
- To complete the approval of new levies and the establishment of new formal obligations with studies on their management cost, both for the authorities and for taxpayers.
- A Commission should be created for the formal simplification of the tax system.

#### **10. Modification of the system of penalties, avoiding automatic mechanisms in the imposition of penalties and ensuring that mere differences of interpretation do not have criminal repercussions**

- To correct the automatic mechanisms in the imposition of penalties. However, the evolution of the rules which regulate the procedure for the imposition of penalties and the position of the tribunals, in the administrative area is still found to be automatic in the commencement of proceedings to impose penalties, the possible culpability of the taxpayer being ignored. The penalty should always presuppose the existence of culpability.

In general, there should be no penalty if there is no concealment, so that the “true and complete” declaration of the taxpayer excludes liability.

- To make progress in the definition of the tax offense under Article 305 of the Criminal Code in order to avoid the penalization of differences of interpretation in the classification of legal transactions for tax purposes.

The current configuration of the criminal offense facilitates the possibility that, in practice, a mere difference of interpretation (for example, regarding the legal classification of certain transactions, regarding the interpretation of the purpose of the transaction or regarding the boundary between cases of tax

mitigation, conflict in the application of tax legislation and simulation), the result of which exceeds the quantitative threshold of the offense, may give rise to proceedings for a tax offense. Therefore, it is considered appropriate to insert in the regulation of the offense of tax fraud an explanatory rule which avoids the penalization of this type of scenarios, focussed on mere differences of interpretation.