

## The Spanish System of Capital Gains Tax

### **Introduction**

Capital Gains Tax is one of the facts of life when selling your home in Spain. During this article I will demonstrate how the gain and tax is calculated for residents and non residents and discuss how the taxation can be minimized.

In Spain there is no separate system for assessing capital gains tax. For homeowners resident in Spain capital gains are treated as part of their taxable income in the year in which the gain occurs. A capital gain tax payment on a property transaction is determined by subtracting the purchase value from the sale value.

**Purchase value** is made up of the purchase price plus the amount of expenses (excluding interest rates) and taxes related to the acquisition paid by the vendor. These would be **price of title deed, commission from the real estate company, legal fees, Plus Valia (if applicable), notary fees and land registry**

This total value is then multiplied by a coefficient corresponding to the year of purchase established on an annual basis (every 31st December) by Spain’s General Budget.

<b>Purchase Date</b>	<b>Sale 2005</b>
1995	1.2350
1996	1.1928
1997	1.1690
1998	1.1463
1999	1.1257
2000	1.1040
2001	1.0824
2002	1.0612
2003	1.0404
2004	1.0200
2005	1.0000

If the property has been rented and those profits have been declared, the purchase value must be reduced by the amortization (updated by the relevant annual coefficient) corresponding to the rental period.

**Sale value** is the declared sale price minus the amount of the expenses and taxes the vendor paid when he bought the property. These would be **the title deed price, real estate commission, lawyer’s fees, plus valia, notary fees and Land registry.**

This amount is then multiplied by the applicable capital gains tax (whether non resident or resident see below) to get the over all sales value. This is then subtracted from the purchase value to get the amount of tax owed to the Hacienda (Tax Office).

Residents pay their capital gains tax as part of their income tax; therefore, if you sold your property in 2005 you pay the tax in May 2006. A Spanish resident will only pay 15% capital gains on the net increase in the property transaction, provided they have owned the property for more than one year, even if they are a top taxpayer. For nonresidents, capital gains tax is assessed at a flat rate of 35%.

### ***Capital Gains Tax Scenario for Non Residents***

In a non resident sales scenario the person who purchases the property is obliged to withhold and pay to the Hacienda (Spanish treasury and tax authority) 5% of the sales value (see above). The payment is considered as an advance on the tax corresponding to the transaction. The purchaser (or his lawyer) must send a copy of 211 form (the withholding order) to the non resident vendor so that he may deduct this amount from the capital gains tax bill. If the 5% exceeds the tax due then the vendor may request a refund.

Refunds are claimed by presenting the 212 form to the district or local office will be forwarded by means of a bank transfer to the account stated in the return (vendors account or person with power of attorney) or a cheque payment.

The Hacienda is obliged to carry out a provisional settlement within six months following the deadline established from the date that the 212 form is filed. If a settlement is in excess of this time frame the Hacienda will forward the excess of the assessed tax due, with interest on the amount pending payment.

### ***Minimising Capital Gains Legally***

Here are some of the things you can do to minimise the impact of capital gains tax.

#### **Become a Spanish resident one year prior to sale**

There are quite a few advantages in becoming a resident in Spain both in terms of owning and selling property. Anyone thinking about reselling should seriously consider this option for the following reasons

If you are resident and more than 65 years of age, and you have lived in your home for three years, you will not be subject to Spanish capital gains tax when you sell it, no matter how great your profit.

If you are a resident, your maximum capital gains tax is 15% and you also avoid the hassle of paying the withholding tax mentioned above. Also if the property is your principal residence and you have owned it for a minimum of three years you can claim part or all of the tax back if you buy another principal residence within two years.

#### **Starting a Spanish Company to own the property**

Using a Spanish company to own a property is discussed at length in my article 'Owning a Spanish Property Through a Company Structure'. This option is open to both residents and non residents. You can start a public limited company or sociedad limitada to buy and own the property as its sole business activity (termed as a holding company) or the company can trade as normal and purchase property as an asset.

For more information go to [www.brightsl.com](http://www.brightsl.com).

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You can also transfer property you already own privately into your company structure. The costs of setting this up are a 1% tax on incorporation of the property into the company and the costs of setting up and running the company.

In terms of capital gains there are two options open to residents and non residents.

1. Buying a property using a sl structure and then selling the property on

The company is deemed to be a Spanish entity, therefore during the sale of your property asset, the capital gains will be set between 15% - 20% with no withholding tax. This option may be desirable to non residents who either do not have the time or desire to become Spanish residents.

2. Buying a property using a sl structure and then selling the company

You can sell shares of a Spanish company in Spain and avoid a lot of the associated taxes. Under Spanish Law there is no taxation on the transfer of shares, this includes capital gains and Transfer Tax (IRTP) set at 7%. However, if the shares sold represent parts of the share capital or net worth of which s are made up of at least 50% of real estate and provided that as a result of the transfer of the shares the acquirer is in a position of control of the entity are not exempt. The property must be in the company structure for minimum of one year.

As mentioned before shares are exempt from tax, but if the taxman finds out there has been a property sale, he will certainly demand payment of transfer tax plus penalties and interests. Therefore, it is advisable that you seek advice from your financial representative in order to structure the purchase in such a way it allows you to legally avoid the taxes.

The Spanish tax authorities are starting to look into these activities and using this method as part of your exit strategy for your investment may be subject to change over the coming years.

### **Avoiding Capital Gains by owning your property longer**

If you owned the property prior to December 31st 1994, the taxable amount will be reduced by 11.11% annually for each year of ownership prior to this date. This is due to the indexation of the taxable amount for inflation which means that if you sell your property after owning it for 20 years the transaction is tax free (from 1994 to 2004).

However, bear in mind that if the property has been renovated while you owned it, and that renovation has been registered with the relevant authorities a re-valuation for the reduction in the capital gains must be undertaken as though there were two different capital gains (i.e. one prior to works and one after), with different ownership periods for the application of 11.11% annual reduction (as well as the corresponding coefficient to the purchase value for the year of purchase and the year of renovation, see above).

Years Until Dec 31st 1996	1	2	3	4	5	6	7	8	9	10	11
%	100	100	88.89	77.78	68.67	55.56	44.45	33.34	22.23	11.12	0

***Under declaration - don't do it and avoid a capital gains nightmare!***

There has been a custom for many years to under declare sales price enabling the vendor to reduce his capital gains tax liability, the purchaser may even be swayed by the advantage to reducing the amounts charged by IVA and ITP. Not surprisingly the Spanish authorities are taking a dim view of this and sever penalties are imposed if you are caught. Even if you as the purchaser are not caught, the under declared value can lead to a monumental Capital Gains tax nightmare when you try to sell on.

Tax inspection of lawyers offices and developers records are now becoming a regular occurrence and if the authorities find that the value of the property exceeds 20% or 12,000€ of the value stated in the title deeds the excess will be taxed both for you and the previous vendor at a gift tax rate which could be as a high as 83%.