



A Guide To:

OWNING PROPERTY IN SPAIN

NOTE

This guide is slightly out of date and will be updated shortly. However it still sets out details of the issues which may need to be addressed. If readers require further information please contact James Green & Co as shown below. [April 2009]

INTRODUCTION

There is more to planning your overseas property purchase than finding the right property in the right location at the right price. Increasing numbers of UK residents are buying second homes in Spain, but very few are aware of the lasting effect the way in which they purchase their property can have on their finances. Since the Spanish tax authorities tightened up their laws individuals buying property in Spain now find themselves liable for Spanish capital gains tax, inheritance tax, annual property taxes, tax on rental income – even when none is received, and costs far in excess of those imposed in the UK when buying and selling their property. Add to this the potential problems of Spanish inheritance laws and you will see that careful consideration has to be given in planning your property purchase in the most tax effective and cost efficient manner.

All this is daunting enough for someone intent in just buying one holiday home, but if it is your intention to retire to Spain or to build up a portfolio of investment properties to give you an income, or to buy and sell properties for profit then you will need to be even more careful in how you structure your purchase to mitigate your tax liability and ensure your heirs actually get to inherit what you want them to inherit not what some arcane law says they should.

The basic options are as follows:

- Purchase as an individual
- Purchase using a UK company and/or trust
- Purchase using an offshore company and/or trust/foundation
- Purchase using a Spanish company

For many people the option of purchasing as an individual may be satisfactory so long as they are aware of and make provision for their tax liabilities. They may also not be able to raise money via a company so will have no choice in the matter. However for someone purchasing high value property or investing in a portfolio of properties there is no doubt that owning their Spanish property through a corporate structure will greatly reduce their tax bill both during and after their lifetime.

Depending on who you speak to you will get conflicting information on the “best” way to buy your property. Many of those giving such advice will be biased towards the method which best suits them and gives them the most income. James Green & Co are totally independent of property developers, sales organisations and finance providers. We will work with your professional advisors to provide the best structure for you, whatever it may be.

This guide does not deal with the mechanics of purchasing property in Spain nor does it seek to give any advice as to how to raise finance to fund a purchase. If any reader requires such advice we will be pleased to put them in contact with an appropriately qualified source.

PROBLEMS TO BE SOLVED

Before looking at the solutions we need to consider the problems. These are set out below. Some are relevant to one type of ownership structure more than others or indeed not at all.

1. Inheritance Tax

Persons who are UK domiciled and/or UK resident are liable to 40% inheritance tax on the total value of their worldwide assets over and above £255,000 in value. With property prices continuing to rise - both in the UK and Spain - most people will find that an overseas property purchase will take them over the nil rate band.

In addition to UK inheritance tax, under Spanish law persons owning property in Spain, regardless of where they are resident, are also liable to Spanish inheritance tax. Depending on the relationship between the deceased and the recipient, the rate of tax varies between 7.65% and 34%. Credit is often not given for tax paid in one country against tax due in another, so without proper planning a double charge on the same asset can and does occur.

2. Capital Gains Tax

If the property was acquired prior to 31 December 1986 capital gains tax does not apply, but for property acquired after this date the law becomes more complex. The amount of tax due is calculated according to a range of factors, such as whether you are over 65 years of age and whether you re-invest in Spanish property within three years.

Spanish capital gains tax is charged on the net difference between the value of the old escritura (title deeds) and the sales escritura. It is payable irrespective of the tax residency of the owner and is charged at up to 35% for non-residents. To put this into perspective, if property prices on the Costa del Sol continue to rise at 15-20% a year, a property in Marbella valued at €272,450 today may be worth well over €500,000 in five years' time. With a profit of €227,550, the capital gains charge could be up to €79,642.

3. Local Taxes

There are two local property taxes which are both based on the property's theoretical rental value which is annually adjusted in line with inflation. The rates of tax will vary from region to region due to the varying rates of tax imposed by the regional and local governments.

Local Property Tax

This is the main local property tax affecting owners of properties in Spain payable yearly to the Town Hall. The amount of the tax is calculated by reference to the valor catastral (official value of the property) registered in respect of all properties in Spain. The percentage charged varies from area to area, and is roughly 0.5% to 1%.

Local Mains Drainage and Refuse Collection Tax

This local tax payable by property owner and a related to rubbish collection and drainage. The amount to pay varies from area to area, and should be paid to the local Town Hall every 3 or 6 months. This tax should be between €200 and €250 per year. Also, if your Spanish property has a garage entry you are obliged to pay €18 per year.

4. Income Tax or Company Tax as applicable.

The income derived on property in Spain should be declared in Spain. If you sell your Spanish property **within** one year of purchasing it, then the profit you make is considered an income and not a capital gain, and you would have to pay Spanish income tax on any profit made. If you rent out your Spanish property, then you have a "rental income" from the Spanish property and will have to pay

Spanish income tax. This can be minimised by leasing out the property to a UK or Spanish company who will manage the rentals. Similar rules apply for rental income obtained by companies.

The rates of income tax payable by a resident and non-resident is different. An individual is considered a Spanish resident if they spend more than 183 days within a calendar year in Spain. A non-resident individual is taxed at the standard rate of company tax at 35%. A resident individual is taxed on a sliding scale between 15 and 45%

5. Deemed Rental Income Tax

If a Spanish property is not rented out or not your primary residence (i.e. a holiday home), you will be liable for the “deemed rental income tax” **even if you do not let out** your Spanish property. The local town hall will charge you according to the valor catastral (rateable value) of the your Spanish property. They will assume you are making 2% of this value each year from letting your Spanish property and charge you 25% of that “income”, which equates to a total of 0.5% of the valor catastral (rateable value) of the your Spanish property. For example, if you own a Spanish property with a valor catastral (rateable value) of €100,000 and you are not renting it out, you will still be liable for 25% of €2000, which equates to €500. This tax applies to properties owned by non resident individuals and companies.

6. Wealth Tax

As an individual you will pay wealth tax (Patrimonial) at a percentage that depends on the value of your wealth (i.e. property plus savings in the bank, etc.). The wealth value associated to a property is based on what the declared value of the property was when you purchased it. For residents, the first €108,182 euro is not taxable. There is also a €50,253 exemption on main home for residents. This wealth tax increases on a sliding scale as shown in the following table.

Wealth Bracket	Tax Rate
Up to €67,129	0.20%
€67,129 - €334,247	0.30%
€334,247 - €668,500	0.50%
€668,500 - €1,337,000	0.90%
€1,337,000 - €2,673,999	1.30%
€2,673,999 - €5,347,998	1.70%
€5,247,998 - €10,695,996	2.10%
Above €10,695,996	2.5%

The wealth tax sliding scale above is “cumulative”. For example, if you purchased a property for €300,000 then you would be liable for wealth tax every year according to the following calculation:

The first €67,129 at 0.2% is €34.26 plus the remaining €232,871 (€300,000 - €67,129) at 0.3% is €69.86. Therefore the wealth tax on an Spanish property worth €300,000 is €104.12.

The above figures are out of date and will be updated shortly.

7. Special Company Tax

If the property is owned by a foreign company, a special tax may apply. Foreign companies owning Spanish real estate, or otherwise having an interest or benefit from Spanish real estate, are charged an **annual 3% tax** on the cadastral value. This **special tax** does not apply to companies domiciled in countries which have a tax treaty with Spain containing an exchange of information clause, so long as the ultimate owners of the shares of such companies are individuals resident in Spain or in a country that has such a tax treaty with Spain.

8. Other Taxes

Before a title deed or a deed for a newly constructed building can be registered in a new owner's name, tax has to be paid by the buyer. This can either be transfer tax (ITP), which is levied at 6%, or value added tax plus stamp duty (AJD), at 0.5%, levied when buying from a developer. These taxes are calculated on the declared purchase price stated on the title deeds.

In addition, local municipalities charge a tax on the increase of the value of the previous sale. This tax is known as "plusvalia" and is not based on the seller's capital gain but on calculations and values set by the local town hall. By law, Plusvalia is the responsibility of the seller, but it is not uncommon for the liability to be contractually transferred to the buyer.

On a property worth €500,000, taxes, lawyer and notary fees could total up to €43,000.

9. Probate, Forced Inheritance etc

Despite Spain being part of the EU, their laws regarding Wills, probate and inheritance are radically different from those in the United Kingdom. Wills made in the United Kingdom are valid for property assets owned in Spain but proving inheritance rights through the Spanish system can be a lengthy and expensive exercise, which may not always succeed. Any documents in English will need to be translated and authenticated for use in Spain, which means delay and expense.

If a husband and wife buy a property jointly then there is no right of survivorship as there is in the UK. The husband's share and vice versa will pass to his wife under the terms of a Will. There is no exemption from Inheritance Tax on an inheritance by a spouse. Each beneficiary is entitled to a personal exemption, which varies according to the relationship to the deceased, but this is much smaller than in the U.K. After this personal exemption has been exhausted, Inheritance Tax is charged on a sliding scale with the rates starting at approximately 7.65%. Any Spanish Inheritance Tax can be offset against any liability to English Inheritance Tax.

If you die owning a property in Spain without having made a Will either in England or in Spain then your property will pass in accordance with Spanish inheritance laws. These impose restrictions on who can inherit property, which can produce unfortunate effects. Therefore, when purchasing a property in Spain, we strongly recommend that you make and register a Will in that country as well as one in the UK.

HOW TO SOLVE THE PROBLEMS

There is very little that an individual can do to reduce their tax liabilities in either Spain or the UK unless they are prepared to structure their ownership using companies or trusts or foundations. Whether the costs involved in doing this are justifiable is a matter that will have to be carefully considered. James Green & Co will be happy to give guidance on this upon request.

Until a few years ago most of the above problems could be successfully avoided by simply using a limited company or trust, preferably located in an offshore tax haven (such as the Isle of Man, Jersey or Gibraltar) to purchase a Spanish property. However realising that they were losing a considerable amount of money the Spanish government took steps designed to halt the use of this simple and effective solution including the imposition of the Special Company Tax and a withholding tax on money remitted abroad.

Whilst this has increased the amount of tax that the Spanish government collects, the only real effect on corporate ownership has been to make the structures required more complex and more costly. However whilst the cost of avoiding tax using an offshore company may have increased there can be no doubt that there are still worthwhile tax planning opportunities to be exploited.

Don't believe anyone who tells you that you can't save money by owning Spanish property via an "offshore" structure. You can, and so long as the mathematics add up it is really quite simple. For example if that €272,450 property in Marbella makes a capital gain of €227,550 over the next five

years, then if the cost of running a company structure per annum is €3,000 you will still save €4,642 capital gains tax. If the cost was to be €5,000 per annum the saving would still be €4,642. Of course these savings are just on capital gains tax, put inheritance tax savings into the equation and the figure is even more impressive.

There is no legal way that you can avoid paying any tax at all. For example, however you structure your ownership you will still have to pay local taxes, deemed rental income and at least some income or company tax. But the laws of both the UK and Spain allow you to organise your affairs in order to pay as little tax other taxes as legally possible so you can reduce or avoid the others with some careful planning.

We are now going to examine the following options in more detail:

- Purchase using a UK company and/or trust
- Purchase using an offshore company and/or trust/foundation
- Purchase using a Spanish company

Please bear in mind that the information contained in this publication is based upon our understanding of legislation in effect at the time of publication. It is provided for guidance only and should not be relied upon as appropriate tax planning advice for all readers. The structures described are examples of some which have been developed in association with solicitors, accountants and financial advisors for their clients. Readers are advised to seek appropriate advice for their own individual circumstances and we can arrange for qualified professionals to provide such advice on a chargeable basis.

OWNERSHIP USING A UK COMPANY

On the surface there would appear to be little point in avoiding Spanish taxes just to become liable to UK taxes. However in general UK taxes are lower than in Spain and there are fewer problems with inheritance. For some people this alone would be sufficient but there are other possibilities to be taken into account.

The main benefit of using a UK company is that because it is liable for tax in the UK it is not, because of tax and EU treaties, liable to pay the special company or withholding taxes in Spain. However, because the property is located in Spain there would be capital gains tax when the property is sold unless steps can be taken to remove this liability.

How It Works

1. The client establishes a UK company via a Licensed Corporate Service Provider (CSP) or Trust Company. The UK Company is then funded with sufficient monies to purchase the property.
2. The UK Company will then purchase the property in Spain (using a local lawyer who will be granted a power of attorney) the company name. In doing so it will obtain a Spanish fiscal number and an Inland Revenue certificate of tax residency.
3. The UK Company will issue a nominee Agreement to the client stating that the company holds the property as nominee for the client.
4. Whilst establishing a Registered Office in the UK, the CSP provides Directors, Nominee Shareholders, Secretary and management to the UK Company from its offshore base. There are advantages in using an Isle of Man based CSP for this.

Principal Advantages

By utilising a Nominee Agreement between the company and the client, the asset of the company (the Spanish property) is not on the balance sheet of the company. Therefore the company is able to file abbreviated accounts, saving the expense of auditing.

The Company does not have an asset on its balance sheet, nor shareholders or Directors in the UK, therefore when the property is sold (by transfer of the Nominee Agreement) it has no liability to Capital Gains Tax. Similarly, should any rental income be received by the Company it is received as Nominee and passed straight on by the Company to the client - therefore no Corporation Tax liability will arise to the Company in the UK.

Some clients are reluctant to use the company route of property ownership because they are not comfortable with the ultimate ownership resting with a Company. The Nominee Agreement therefore provides added comfort in that they will now have something, which states the company holds the property on their behalf. The Nominee Agreement is a simple one page document and if required this document can be notarised and legalised and is held by the Company in the Isle of Man.

Within Spain, the UK Company is the registered owner of the property and recorded as such at the local Land Registry.

The Benefits

1. Anonymity
2. Through transfer of the Nominee Agreement (or the UK company) rather than the property itself there is no liability to capital gains tax and inheritance tax in Spain.
3. No transfer of property means savings in time and costs to future purchaser.
4. Avoids problems with succession laws in Spain.
5. Funds on purchase/sale protected by using the CSP as stakeholders if required.
6. The client can still borrow to finance the purchase subject to status.
7. Renting the property out via a UK agent reduces Spanish company tax, avoids the withholding tax, and even if UK corporation tax is payable will result on a tax saving.
8. In due course more sophisticated structures can be built as a clients needs and aspirations change.
9. Double taxation treaty guards against any future changes in Spanish taxation.
10. Inexpensive, simple and flexible.

The Drawbacks

1. Unless used in conjunction with offshore companies or trusts could give rise to UK capital gains and inheritance tax.
2. It may be possible in the future that the Spanish authorities seek to look behind the nominee structure. This is not a major threat or problem but could increase costs.

The Costs

This is a low cost structure, which can typically can be established for a fee of around £550 (including obtaining IR certificate and opening a bank account) and with an annual running cost of about £750. These fees do not include costs relating to the buying and selling of property or other non-routine management activities. Some fees may be subject to VAT.

Options

There are a number of options that may be added into the mix. For example:

1. The Nominee Agreement can be entered into with an offshore company, an offshore trust, or another UK company to further reduce UK taxation liability.
2. The UK Company can become a subsidiary of another UK company, an offshore company, or a combination of both or it could be owned by a trust.

These allow more complex tax planning which may, as an example, be suitable for property trading – the buying and selling of property, including off-plan, for profit. A group structure would permit the sale of either a nominee agreement or a subsidiary company without tax liability.

OWNERSHIP USING A “TRADITIONAL” OFFSHORE COMPANY

This is a structure that many people have used successfully for a number of years. It is a simple solution having the great advantages in that when the property is sold all that is necessary is to sell the shares of the company. In this manner because there is no transfer of ownership in the property all Spanish taxes and several fees, including those of the lawyer and utility companies are effectively bypassed. Because the change of ownership is not in the property but the offshore company, the capital gain takes place offshore, where there is no tax liability.

The imposition of the special company tax on properties owned by offshore companies has led many people, mainly Spanish lawyers, to suggest that this is no longer such a good option. We disagree because whilst the tax does increase costs remember that it is only 3% of the cadastral figure not the resale value of the property and that may not be a very high figure. Also there are a number of offshore jurisdictions that do not appear on the Spanish blacklist, such as Delaware, where the tax will not be imposed – though we cannot guarantee the Spaniards will not make changes.

How It Works

1. The client establishes an offshore company in a suitable jurisdiction using a licensed Corporate Service Provider (CSP) or Trust Company.
2. The offshore company will purchase the Spanish property using a local lawyer (who will be granted a power of attorney) in the company name. In doing so it will obtain a Spanish fiscal number.
3. The CSP provides Directors, Nominee Shareholders, Registered Office, Secretary and management to the offshore Company. Irrespective of the jurisdiction where the offshore company is established there may be advantages by establishing management in the Isle of Man. This is because the Isle of Man is within the UK VAT system and is well regulated.
4. A Spanish representative will be appointed to deal with tax and similar matters. Within Spain, the company is the registered owner of the property and recorded as such at the local Land Registry.

The Benefits

1. Anonymity.
2. Through transfer of the shares in the offshore company, rather than the property itself, there is no liability to capital gains tax and inheritance tax in Spain or in the UK.
3. No transfer of property means savings in time and costs to future purchaser.
4. Avoids problems with succession laws in Spain.
5. Funds on purchase/sale protected by using the CSP as stakeholders if required.

6. The client can still borrow to finance the purchase subject to status.
7. Renting the property out via a UK agent reduces Spanish company tax, avoids the withholding tax, and even if UK corporation tax is payable will result on a tax saving.
8. Flexible and able to be developed as needs change.

The Drawbacks

1. There is the possibility that now the special tax has been imposed the rate may be increased and so add to costs. However as the tax was originally charged at 5% and has now been reduced to 3% this may not be a major concern. Also given that ownership is offshore it would be a simple matter to transfer the property to a UK company as detailed previously.
2. Potential for delays and expense in arranging initial funding as lenders will need legal opinions on the ability of the offshore company to own property in Spain and to borrow against its value.
3. Potential for delays and expense in initial purchase as Spanish authorities will need legal opinions on the ability of the offshore company to own property in Spain and to borrow against its value.
4. A more expensive option so important that proper computation of financial benefits is made.

The Costs

As an example we set out a realistic fee schedule for a Delaware company.

	FIRST YEAR £STG	EACH FOLLOWING
Incorporation	450.00	0.00
Opening of Bank Account	395.00	0.00
Provision of resident agent and registered office for the year	400.00	400.00
Provision of company officials and shareholders for the year	400.00	400.00
TOTAL ANNUAL FEES	£1,645.00	£800.00

These fees do not include costs relating to the buying and selling of property or other non-routine management activities. Depending on location of clients some fees may be subject to VAT.

Options

There are a number of options that may be added into the mix. For example:

1. The offshore company could be owned by a Trust (or a Foundation which is similar) in order to facilitate tax efficient income for the clients.
2. Where several properties are owned or property trading takes place, the offshore company can set up subsidiaries to hold individual properties so these can be sold individually and easily.

OWNERSHIP USING A SPANISH COMPANY

This is an option that is often put to prospective property purchasers and there is no doubt that it will work – but in order to maximise tax savings there still has to be an offshore element so this is a more costly option.

For example Inheritance Tax will be avoided because a company is considered to be a distinct legal entity, and thus never dies, but a Spanish company will still be liable to tax on rental income and on capital gains made when the property, or company, is sold. Capital gains tax may be avoided by using an offshore company which in turn owns a Spanish company that in turn owns the property. Rather than “selling” the property, there is a change of ownership in the offshore company by transferring the shares. The capital gain is therefore offshore, where there is no tax liability.

How It Works

1. The client establishes an offshore company using a licensed CSP or Trust Company in a suitable jurisdiction such as the BVI or Delaware, although others are available.
2. The offshore company establishes a Spanish company which is then funded, preferably by the offshore company, with sufficient monies to purchase the property.
3. The Spanish Company will then purchase the property in Spain in its own name.
4. The Spanish agent provides the Registered Office, Officers, legal and accounting services for the Spanish company. This takes place in Spain.
5. The CSP provides Directors, Nominee Shareholders, Registered Office, Secretary and management to the offshore Company. Irrespective of the jurisdiction where the offshore company is established it can be advantageous to establish management in the Isle of Man.

Within Spain, the company is the registered owner of the property and recorded as such at the local Land Registry.

The Benefits

1. Anonymity.
2. Through transfer of the shares in the offshore company, rather than the property itself, there is no liability to capital gains tax or inheritance tax in Spain or in the UK.
3. No transfer of property means savings in time and costs to future purchaser.
4. Avoids problems with succession laws in Spain.
5. Funds on purchase/sale protected by using The CSP as stakeholders if required.
6. The client can still borrow to finance the purchase subject to status.
7. Renting the property out via a UK agent reduces Spanish company tax, avoids the withholding tax, and even if UK corporation tax is payable will result on a tax saving.
8. Flexible and able to be developed as needs change.

The Drawbacks

1. The Spanish company will be liable to tax in Spain and whilst the offshore ownership will help to mitigate this there is less opportunity and potentially high costs in using this sort of structure.

2. The Spanish authorities may decide that where the ownership of a Spanish company is offshore they are still losing too much tax income and could seek to impose some sort of new tax. Indications are that this is under consideration as the Spanish government has recently produced a list of offshore jurisdictions that it will not seek to tax. These include Delaware, the Cook Islands and Cyprus. In practical terms, due to costs, Delaware is likely to be preferred by most clients.
3. Not very flexible as the Spanish authorities will be aware of changes in ownership and any selling of properties will be obvious and easy to tax. Again ways around this but costly.
4. A costly option so best suited for high value properties or as part of a group structure.

The Costs

There are too many variables for us to be able to indicate likely costs. We will advise on an individual basis.

TAXATION OF RENTAL INCOME

The solutions described above are primarily designed to save capital gains and inheritance tax. On their own they will not reduce liability to pay Spanish company tax on the profits made by renting out property. In computing the profit companies can deduct costs such as advertising, management and interest paid but they will have to pay 35% on the final profit.

There are ways to reduce this such as by entering into an agreement with a UK property or holiday company for them to manage the letting etc. They will pay the owner an agreed lease fee in Spain against which deductions can be made. A profit share can then be paid offshore (or in the UK) moving the tax liability from Spain to a lower tax jurisdiction. Where a portfolio of properties is concerned it may be advantageous to set up another offshore company to manage the lettings on behalf of the company that owns the property which work could be sub-contracted back to a property or holiday company.

Readers may also be interested in reading some other guides published by James Green & Co, particularly the following:

A Guide to the Use of Trusts in Spain

Nominee Structures

These are available from the download sections of the following websites

<http://link4business.info>

<http://jamesgreenandco.co.uk>

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