SPANISH INHERITANCE AND GIFTS TAX

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Background

It is calculated that Britons own more real property assets in Spain than in any other single jurisdiction outside the United Kingdom. Many other nationalities, notably Swedes, Danes, Germans and Dutch, also own significant assets in Spain. Apart from those from the Latin American and North African nations, these five races probably also make up the majority of the foreign community resident in Spain. For all of them, Spanish Inheritance and Gifts Tax (ISD)[2] can have a notable impact.

Spain has taxed inheritances for a good many years[3]. A revised and modernised approach was introduced by the enactment in 1987 of ISD. This new law took effect from 1st January 1988, and contained within it a provision for the annual updating (neo-indexation) of such figures as band-thresholds and allowances. This particular law is rather better drafted than the average (which latter might give - say - Robert Venables either apoplexy or a lot of fun) and. contains a number of interesting anti-evasion provisions.

Aim of this Article

This article rehearses the details of ISD, and considers its effect for the foreigner (that is to say, the non-Spaniard), with an especial eye on the Briton who, by virtue of his - generally - UK domicile, is also subject to UK Inheritance Tax (IHT) on substantially similar taxable events and assets.
What may be good planning for IHT may produce unexpected and sometimes damaging results for ISD. These are not always obvious to the UK-based planner. This article therefore attempts also to signpost some of the more commonly

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2 ISD: Impuesto sobre Sucesiones y Donaciones, Law 29/1987 18th December, published in the Boletin Oficial del Estado [BOE] (the official legal gazette) on 19th December 1987.

3 Most recently, and until the introduction of ISD, under the terms of Decree 1018/1967 6 April which approved the Revised Text (Texto Refundido) of still earlier laws on the taxation of inheritances and other related matters.

encountered pitfalls.

Liability to ISD

An event triggering consideration of whether tax is due occurs when a gratuitous transfer of relevant assets is made (inter vivos or mortis causa) to a chargeable person. Also caught are transfers with a donative element (e.g., sale, at an over or under value).

*** The Taxable Person**

In line with the norm in continental Europe, ISD is an acquisitions tax, and not a transfer tax. The taxable person is therefore the recipient, not the donor. This simple fact alone can cause much confusion in the mind of the IHT-orientated planner (and in the mind of the British client who, perhaps unsurprisingly, cleaves limpet-like to the notion of his own tax liability upon death, and for whom it is helpful time and again to be walked around to the other side of the mirror in order firmly to grasp the concept of the Spanish tax and comprehend its impact).

The tax is applicable only to individuals (personas fisicas) and therefore not to any other type of person at law, such as a company[4]. Indeed, Art 3 (2) says that "juridical" (i.e., not physical) persons are not liable to this tax, but will be assessable instead to the Spanish equivalent of corporation tax (ISS[5]).

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4 ... but what of a trust? Although a signatory to the Hague Convention, there is, in Spain's law, no concept of beneficial title distinct from legal title to the same asset; and unless and until Spain ratifies the Hague Convention on Trusts, no basis for regarding trust assets as a fund distinct from that of the trustee's personal assets. Does Spain therefore regard trustees simply as principals? For example, will a non-corporate trustee in receipt of a gratuitous transfer of chargeable assets be considered simply a *persona fisica* and therefore in principle chargeable to ISD? Inevitably, the law (and the regulations, which have the force of law) are silent on the matter. This general issue is discussed later in the body of this article.

5 ISS: Impuesto Sobre Sociedades; Law 61/1978.

Although the earlier law took account of the nationality of the taxpayer, the present law does not. The sole criterion of the scope of an individual's liability is his residence in Spain. Art 6 (2) of ISD takes in the statutory definition of residence of an individual contained in the law of Personal Income Tax (IRPF[6]).

An individual resident in Spain is liable (by way of *obligacion personal*) to ISD on receipts by him of assets (etc) sited anywhere in the world.

An individual not resident in Spain is liable (by way of *obligacion real*) to ISD on receipts of assets (etc) sited in Spain. Although the IHT notion of excluded property does not exist in ISD, the effect is pretty much the same.

In ISD there is no concept of an exempt beneficiary. Significantly, this means that a spouse is not an exempt beneficiary. This latter piece of information generally has, upon communication to British clients resident in Spain, the same stunning effect as a sock full of wet sand around the ear. Pragmatically, that effect can be quite valuable since it commonly motivates them into thinking about planning for ISD; wives will usually goad husbands into action.

*** Assets Affected by ISD**

The rule on situs of assets is analogous to that in IHT. Only two geographical "classes" of asset are described:

Worldwide: Art 6 describes the charge to tax " ... irrespective of the situs of the

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6 IRPF: Impuesto sobre la Renta de las Personas Fisicas; Law 18/1991 6th June. IRPF Art 12 says:
<u>One</u> An Individual shall be habitually resident in Spanish territory in any of the following circumstances:
 a) when he remains more than 183 days in the calendar year in Spanish territory
 b) when the principal centre of his business or profession activities or his economic interests lies in Spain
<u>Two</u> Save proof to the contrary, an individual shall be presumed to be habitually resident in Spanish territory when his spouse from whom he is not legally separated and minor dependent children are habitually resident in Spain.
<u>Three</u> In computing the number of days spent in Spanish territory absences therefore shall be included (*as days spent within Spain*) unless the taxpayer can demonstrate habitual residence in another country during 183 days of the calendar year.

(*This is a faithful translation. There is no effective difference between "Spain" and "Spanish territory". "More than 183 days" and "183 days" are correctly given. The word "and" in Art 12 Two has the same sense in the original as it has in the translation. "Another country" is just that.*)

assets or rights".

Sited in Spain: Art 7 refers to " ... assets or rights of whatever nature which are sited or could be exercised or accomplished in Spanish territory".

In principle, there is no parallel to the IHT Exempt Gift. This is so partly because, strictly, it is the receipt and not the gift which is taxable, but largely because the recipients of gifts for, say, national purposes, the Holy See, public benefit and so forth, would have to look for exemption to the codes, laws, decrees, or regulations governing the taxation of their own income and other receipts. Since such recipients will generally be juridical and not physical persons, such exemptions are normally to be found in ISS (to which reference is made in ISD Final Disposition Four). Certain receipts, however, are excluded from charge to ISD:

* The Spanish Treasury from time to time has authorised the issue of certain bonds (usually with a penally low coupon) as a sort of public-sector launderette for domestic funny-money. ISD Transitional Disposition Three confirms the continuing exclusion from ISD of those bonds when acquired by the transferor before 19 Jan 1987 and owned by him for not less than two years before the (otherwise taxable) transfer.

* The Regulations[7] (Reglamentos) exclude from charge to ISD the following receipts (prudent advisors will also check the list of exempt receipts for Personal Income Tax [IRPF]):

    - prizes received from authorised games (National Lottery and so forth).

    - other prizes and compensatory payments which are exempt from IRPF.

    - grants, scholarships, prizes, and other aid of a similar nature awarded by public or private organisations with objectives of a charitable, educational, cultural, sporting, or social welfare nature.

    - loans, "utilities", or other amounts provided by corporations, societies, associations and businesses to their workers arising directly from a contract for service ("work contract"), even where paid via an insurance scheme.

    - sums received from pension plans and schemes by the beneficiaries thereof.

    - amounts received by a creditor from a life assurance policy, written to guarantee the payment of a debt.

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7 *Reglamentos del Impuesto sobre Sucesiones y Donaciones* (RISD) authorised by Royal Decree (*Real Decreto*) 1629/1991 of 8th November, published in the BOE 16 Nov 91.

*** Gifts Inter Vivos and Mortis Causa - Any Difference?**

With one minor exception, there is no difference in the taxation of net gifts inter vivos and those made mortis causa. The exception is that, inter vivos, no personal allowance is available. In short, lifetime gifting is not encouraged by ISD, and, indeed, is faintly discouraged[8].

Valuation

Spain's is a self-assessment regime. It is therefore incumbent on the taxpayer to report the value of a gratuitous receipt (and, of course, calculate and pay the tax due[9]).

Art 9 characterises the value to be used for ISD as the "net value" of the assets received. Significantly it goes on to say that the starting point for valuation shall be the "real" or market value. The especial significance of this point is twofold:

a) Different laws can take different prices or valuation bases for different purposes, including taxation. Popular imagination takes this to imply that one can select the valuation basis most favourable to one's purpose for the time being. Where real property is concerned, for example, the range of values can include full market value, a value attributed by a lender when assessing the property as security for a loan, catastral value[10], or even the price of acquisition (often illegally understated[11]) given in the title deed. Popular imagination is fevered and wrong; full market value is the only

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8 Further discouragement is to be found in the taxation of realised gains (*incrementos del patrimonio*). The new IRPF (Law 18/1991) which came into effect on 1 Jan 92, releases from charge to capital gains tax gifts made on death (formerly charged at a flat rate of 8%). Gains realised on gifts inter vivos remain chargeable to IRPF; there is no provision for holdover relief.

9 Compliance and adminstration are dealt with more fully later in this article.

10 catastral value - *valor catastral*. Broadly equivalent to a sort of "rateable value". Each piece of land or property has such a value which can be ascertained from the local town-hall, and is used as the basis for a number of taxes on property. Historically, catastral values have seemed not to exceed 60%-70% of market value, but recent increases in catastral values combined with soggy market prices have generally eroded the differential.

11 Already illegal, this practice was then doubly outlawed by the enactment of a special law (Ley de Tasas), combined with fierce new enforcement procedures.

starting point for ISD valuations.

b) Market value is in the eye of the beholder. ISD Art 18 removes the possibility of endless and furious debate on the matter by giving to the tax administration the right of verification of reported values (although there is no direct equivalent of the District Valuer). The verified value prevails over the reported value, unless the reported value is higher ... in which case, the latter prevails! Art 19 takes this beastly little mincing machine a degree further by giving the administration the right of compulsory acquisition at the reported value where the verified value is more than 100%[12] greater than the reported value, such right to be exercised within six months of the date of finalisation of the tax due. Especially where real property is concerned, unwary taxpayers can find their fingers - if not the whole arm - caught in the mangle, unless adequately advised.

In the case of acquisitions mortis causa, Arts 12 - 14 describe the encumbrances, debts, and costs which may be deducted from the gross value of the asset. There are no surprises here, and the words of these Articles are designed to ensure that only items which genuinely reduce the value of the inheritance are deductible. National and local taxes, and also Social Security contributions due from the deceased, are deductible from the general estate (caudal hereditario).

Gifts inter vivos are treated somewhat differently. Deductible encumbrances are precisely as for acquisitions mortis causa. Debts are deductible only if they attach directly to the asset transferred and the recipient formally assumes and guarantees payment of the debt; this is inevitably a somewhat narrower definition than that for transfers on death. There is no provision for the deduction of costs.

Personal Allowances

Personal allowances are not available on lifetime gifts. For acquisitions mortis causa, an allowance may be deducted from the net value. This allowance is, of course, that of the recipient; the more recipients there are, the more allowances there are. The quantum of the allowance depends on the degree of kinship[13] (parentesco) between

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12 Before 1 Jan 92, this figure was 50%. In the current market conditions for real property, this degree of valuation discrepancy is more common than one might imagine. Patently, in the relatively volatile fields of, say, fine art and jewellery the risk of such a discrepancy is always present. Moral: choose your valuer with care; if he happens also to do Hacienda's valuations, so much the better.

13 A simple matter to the Spanish eye, and one defined in careful detail in the Civil Code (*Codigo Civil*) at Arts 915-920. To the British eye, it appears initially opaque, later baroque, and finally susceptible to mathematical calculation whilst continuing to elude emotional comprehension. A simple example may help: one draws a family tree, showing names and lines of direct descent. Each line represents a

transferee and transferor, and the Group into which that kinship falls for ISD purposes. Prior to the enactment of ISD there were seven Groups; happily, ISD reduces the number to 4.

Group 1 consists of children[14], grandchildren and so forth in direct (i.e., not collateral) line of descent who are under the age of 21[15].

Group 2 consists of the same descendants listed above in Group 1 but of the age of 21(+), ascendants in direct line, and spouses. One may therefrom deduce, correctly, that spouses are not favoured beneficiaries and are treated in no way differently from adult children or, indeed, parents and grandparents.

Group 3 consists of those in the next degrees of kinship out to, but not including, first cousins. (For the technically inclined, that is to say including the collateral third grade).

Group 4 consists of the rest of the family (collateral fourth grade and beyond) and unrelated persons. This latter category (unrelated persons) would include not only stepchildren, but also the so-called common-law spouse[16]. This latter is a common (neither pun nor social comment intended) condition amongst, say, joint property owners. As will later become apparent, marriage can be a vastly

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degree (*grado*) of kinship. Thus a son (son 1) has a kinship of first degree with his father; with his grandfather the kinship is second degree; with his brother (son 2), however, the relationship is of collateral second degree since the line passes first from son 1 up to father, and then collaterally from him down to son 2. If that brother (son 2) in turn had a son (grandson), son 1's relationship with his nephew would be of the collateral third degree (son 1 direct to father; thence collaterally to son 2; and finally to grandson). Spouses are treated as if they were the same person for this purpose.

14 This includes natural and legally adopted children, but not step-children (unless legally adopted which can only be done during the child's minority).

15 As in the UK, the legal age of majority is 18 (Spanish Constitution Art 12). ISD is specific about age 21 for the purpose of the kinship Groups.

16 By which I mean a man and a woman living together as if married. Patently, this journalist's expression is wrong; it is especially nonsensical in a civil code jurisdiction. Equally clearly, a couple married under the common law are spouses for all the purpose of the law (including ISD). There are no "mistress's rights" - nor, I hasten to add, the male equivalent, whatever that may be - in ISD.

successful tax-planning manoeuvre (I say nothing of other consequences).

The allowances for 1992 are:

Group 1: 2,386,000 pesetas (pts)[17] plus 596,000 pts for each year of the taxpayer's age under 21. The maximum allowance is capped at 7,158,000 pts

Group 2: 2,386,000 pts[18]

Group 3: 1,193,000 pts

Group 4: Nil

Note: Handicapped persons (with a physical, mental or sensory handicap[19]) receive an allowance of 7,158,000 pts in addition to that derived from the relevant kinship Group.

The Initial Calculation of the Tax

The net value of the receipt, less any allowance due, is calculated against the rate-bands to produce an initial, "raw", tax figure. There is no 0% band. The marginal rates start at 7.65% on the first 1,193,000 pts and proceed across a total of 16 bands to a top marginal rate of 34% on amounts over 119,250,000 pts. The tax due on an amount of precisely 119,250,000 pts is 29,800,278 pts, being an average rate at that point of almost exactly 25%.

That doesn't sound too horrendous, especially with a top marginal rate of 34%. It is not, however, the end of the story, since ...

The Co-Efficient

... to the raw figure is then applied a co-efficient ranging between 1 and 2.4[20]. The amount of the co-efficient in a particular case is determined by reference to a table. The indices of the table are, firstly and more importantly, the relevant ISD kinship Group referred to above, and secondly the net wealth[21] owned by the recipient, before

17 a good rule-of-thumb exchange rate for current conditions (May 1992) is 180pts : £1 sterling.

18 This Group 2 allowance is the pivotal one, the others all being functions of this amount. The fiddly numbers result from indexation of a figure which, in 1988, started as 2,000,000 pts.

19 As defined in IRPF.

20 ... that's "two point four" (in case typescript may make it look like vastly more!).

21 Valued according to rules for Wealth Tax (Impuesto sobre el Patrimonio - [IP]). This is an annual tax on an individual's

receipt of the gift currently being taxed ("pre-existing net wealth"). For non-resident recipients, it is their Spanish-sited wealth that is relevant; for residents, their worldwide wealth is taken into account.

The table of co-efficients is as follows:

Pre-existing net wealth (millions of pesetas)	Kinship Groups		
	One & Two	Three	Four
	CO-EFFICIENT		
0 to 60	1.0000	1.5882	2.0000
60 to 300	1.0500	1.6676	2.1000
300 to 600	1.1000	1.7471	2.2000
Over 600	1.2000	1.9059	2.4000

A swift glance at the table above will reveal that degree of kinship has a far greater influence on the co-efficient than does pre-existing net wealth. It can be seen that the unmarried "common-law spouse" (... however much one dislikes the term, one has to admit to its shorthand value) with not a bean of wealth will have to apply a co-efficient of 2, resulting in an effective top marginal rate of 68%. The same is true of, say, the unadopted step-child. Their greatly wealthier counterparts could be facing a top marginal rate of 81.6% [34% x 2.4] (and an average rate at the top-rate threshold of 60%)

An Intermediate Summary

It may be helpful to summarise the bare bones so far:

* Value the asset received
* Deduct any allowable deductions
* Determine the degree of kinship between donor and donee (the taxpayer)
* Establish into which kinship Group the taxpayer falls
* Deduct any available personal allowance

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wealth (world-wide for residents; Spanish-sited for non-residents) which tax is, in general, monetarily insignificant but which acts as a remarkably effective control for capital and income taxes.

* Tax the resultant figure through the bands
  Calculate the taxpayer's wealth
* Determine which co-efficient is applicable
* Apply the co-efficient to the tax figure obtained earlier

Compliance and Administration

It is the taxpayer's duty to present in the due form all the documents reporting the taxable transaction and necessary to the calculation of the tax due. He may opt himself to calculate the tax due and present his declaration (which includes the calculation) together with the money (a procedure called *autoliquidacion*).

ISD Art 24 defines the moment of accrual of the liability to tax as follows:

(i) Death:

The date of death of the transferor; or when this is not known, the date on which declaration of death is duly signed in accordance with the Civil Code Art 196.

(ii) Lifetime:

The date on which the gift is conveyed (in whatever form is appropriate to the asset in question).

(iii) General - gifts with conditions:

The date on which any condition, limitation, term or other form of suspension attaching to the gift is satisfied or discharged.

ISD Art 31 leaves to the Regulations the matter of timing of presentation of documents. RISD Art 67 says of that matter:

(i) Death:

within six months of the date of death of the transferor. (RISD Art 68 gives the tax office the ability to extend this period by a further six months, provided the request is made to them within the first five months following death. If that request is denied, the original six months will be extended by the number of days from presentation of the request to its refusal).

(ii) All other cases:

within 30 calendar days of the day following the conveyance of the gift.

In the case of receipts mortis causa, deferred payment (lump sum and schedular) of the tax due is possible in certain defined circumstances, but always subject to the payment of interest at the official rate and provision of adequate guarantees for both principal and interest. In general, it is necessary to demonstrate that the taxpayer has insufficient liquidity to meet the tax in cash. Deferred payment of the whole may be agreed for one year, or in up to five equal annual payments. In the case of the latter, the guarantee must be for 125% of the total of principal and interest.

Deferred payment is also possible in the transmission mortis causa or inter vivos of a trading or professional business[22]. The same is true, but only mortis causa, of an habitual residence. In the latter case, only a Group I or II relative (spouse, children or parents) or a sibling over the age of 65 who has lived with the transferor during the two years preceding his death may request deferment of payment. In these cases, tax may initially be deferred for a period of up to three years (subject to the provision of a 125% guarantee); at the end of the three years,
and subject to the same conditions, the Collector of Taxes may agree to further deferment by seven equal six-monthly payments.

The tax administration is proscribed[23] from seeking payment, or applying sanctions for non-payment of tax once a period of five years has passed counting from the day of, in the one case final presentation by the taxpayer of all the required documents, or in the other case the date of the infraction[24].

Anti-Evasion/Avoidance

This is an interesting area of the legislation and regulations, which clearly demonstrates the reliance placed in the Spanish legal system upon bureaucratic control. The emphasis is upon anti-evasion. Avoidance - in the British tax sense of the word - is little contemplated. The general intention of the various Articles in ISD and RISD is to weave a web of reports around the taxable event, such that the taxpayer is effectively enmeshed by the system. That which follows is an illustrative sample of the various provisions, rather than what might become a rather tedious rehearsal of the whole.

The Law dives straight into the heart of the matter at ISD Art 4 with some presumptions of chargeable transfers within the family. At Art 4 (1) a transfer is presumed to have been made when from the records available from the Fiscal

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22 This is the closest ISD gets to any form of Business Property Relief.

23 By ISD Art 25, and RISD Art 48.

24 This is not a charter for evaders with stamina; patently the playing field is more than somewhat levelled in favour of Hacienda, by providing many opportunities for them to stop the clock. The provision seems designed to alleviate the potentially otiose burden on a taxpayer of an historical unnoticed/unreported liability.

Registries or other sources an individual's wealth[25] is seen to have diminished simultaneously with or before (though always within the 5-year period of proscription mentioned above) an increase in wealth of his/her spouse, descendants, heirs or legatees. ISD Art 4 (2) presumes a chargeable transfer when parents or grandparents, acting as representatives for their minor children (under 18 years) purchase assets on their behalf unless there is proof that the minors owned sufficient means in their own right, and that those means were applied to the purchase in question. Art 4 (3) says, rather comfortingly, that these presumptions will be brought to the attention of the taxpayers concerned in order that they may formulate such rebuttal or proofs as they deem appropriate, before any assessment is made.

ISD Art 8 introduces the neat concept of subsidiary responsibility. Financial intermediaries, bankers, insurance companies, stockbrokers and other such persons, and also official functionaries, concerned in the transmission and the registration thereof of cash, bank accounts, stocks, proceeds of life assurance policies, or any similar matter without first assuring themselves that the transfer has been duly reported to the taxing authority, become subsidiarily liable for the payment of tax (ISD) which may be due.

ISD Art 32 requires at clause (1) the courts to inform the tax administration monthly of any judgments which may give rise to an increase in a person's wealth. At clause (2), those in charge of the Civil Registry must, within the first 15 days of each month, inform the tax administration of all deaths during the previous month, and the addresses of the deceased. At clause (3), Notaries are required upon request by the tax administration to send, without charge (a deeply distressing requirement for this essential but lucrative profession) and within 15 days, copies of any deed or document concerning which they have acted professionally, and must also furnish such other detail as may be requested. They are also required to send within the first 15 days of each quarter a comprehensive list of all documents authorised by them in the preceding quarter which may have a bearing upon deeds or contracts which may give rise to an increase in wealth chargeable to ISD. Clause (4) sweeps up most of the rest of the population by prohibiting the transmission of assets by judicial organs, financial intermediaries, associations, foundations, companies, any other entity public or private, functionaries and private individuals, without first checking that ISD has been paid, unless authorised to do so by the tax administration. Insurance companies are similarly caught by clause (5).

Reference has been made earlier to the adminstration's right of compulsory acquisition when an asset is reported for tax at a significant undervalue.

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[25] Here, as throughout the whole canon of Spanish personal tax law, one can perceive the control provided by Wealth Tax (Impuesto sobre el Patrimonio).

The Regulations underscore these provisions from the law. But at RISD Arts 99 and 100 they tighten the web still further by prohibiting public offices and registries, and specifically the Property, Mercantile, and Industrial Property Registries, from registering any document unless appropriate reference has been made to the tax administration.

As I observed earlier, most of this is aimed at evasion. Such small neo-anti-avoidance measures as there are tend to aim at intra family manoeuvres, such as renunciation of rights under the forced heirship rules. They are, in general, designed to ensure that a lower co-efficient is not thereby achieved. The Deed of Family Arrangement has no place, and could give rise to a double charge to ISD; practitioners considering such variations where there is Spanish-sited property involved would be well advised to check the effect for ISD.

Other Matters

Business Property Relief

There is none (other than the ability to request deferral of payment of the tax). This, of course, is in sharp contrast to UK experience (and even more so under the recent UK Budget proposals). Planners need to bear this in mind.

Quick Succession Relief

There is no form of quick succession relief. In the light of this, it seems strange that commorientes clauses are rarely seen in Spanish wills. Perhaps the very limited degree of testamentary freedom under the Civil Code is responsible for that.

Life Assurance

Spanish life assurance is nearly always written on an own-life basis. Naturally there is no opportunity to write policies in trust for a beneficiary. It is always possible to nominate a beneficiary, but this is a purely administrative annotation, and has no effect upon title. The proceeds of a life assurance policy are therefore assessable to ISD when the recipient is anyone other than the policyholder (usually the life assured), and are treated as any other asset passing to that recipient. A life assurance policy written in trust (say, a UK policy) for a spouse stands the risk of attracting twice the rate of tax: trustees will be unrelated to the recipient, and hence Group IV transferors, where the spouse would have been Group II. It is good planning for a policy to be held on a life-of-another basis, since the recipient of the proceeds will also be the policyholder hence there is no transfer to be taxed[26].

Cumulation

Lifetime gifts from the same donor to the same donee are cumulated over a rolling three year period. Upon death, lifetime gifts made by the deceased within five years

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[26] If there is a savings element, there may be a charge to income tax on the policy gain.

of his death are accumulated with transfers at death to the same recipient.

Double Taxation Relief

There is no treaty with the UK concerning inheritances and gifts tax. ISD Art 23 provides a unilateral relief for "similar taxes paid abroad" to those liable by way of *obligacion personal* (i.e., those resident in Spain). The lesser of two sums may be deducted from the Spanish tax:

a) the amount of foreign tax paid or

b) the result of applying the average rate of ISD on the gift/inheritance in question to those foreign assets on which foreign tax has been paid.

Patently, no relief is available where no foreign tax has been paid. The prime example of this would be the death of one of an English domiciled couple resident in Spain. There is no UK IHT to be relieved against the ISD on any transfer between those spouses.

Planning

General

It should be remembered firstly that Spain's is an acquisitions tax, and that there may be some mismatch with the UK's transfer tax (IHT); secondly that a spouse is not an exempt beneficiary and that therefore first death planning is crucial.

Trusts

Unsurprisingly, the *Direccion General de Tributos* cannot give any general guidelines for the tax treatment of interests in trusts, and can only deal with them on a case by case basis. It should be remembered by planners that the trigger for consideration of a charge to ISD is an increase in an individual's wealth. Receipts from trustees can fall with a resounding thud into this definition; the thud is due to the fact that trustees are by definition unrelated to the recipient, and that therefore the tax can be double that of a direct receipt from a close relative (spouse or parent, for example).

Spouses

As signalled above, inter-spouse planning is quintessential. This is particularly true of residents and the family home. The problem is exacerbated if the "spouses" are not married. Often, the most practical solution (where health, age, and so forth permit) is to write cross-held life assurance policies on a life-of-another basis.

This whole area can be vastly complicated by the forced heirship rules (which I think I will need to cover in a separate article if the Editors permit), under the terms of which the children of the deceased are in general entitled to one third of the estate absolutely and a reversionary interest in a further third, leaving the surviving spouse with a life tenancy in one third of the estate, and an absolute interest in the final third only if those were the terms of the deceased spouse's will (that final third being the only portion subject to full testamentary freedom).

Children

As the reader will have deduced, ISD draws no distinction between adult children and spouses, both being Group II recipients. The common "second death" approach to planning for IHT is therefore inappropriate as an approach to ISD. Provision for the surviving spouse is in general more important.

Use of Offshore Companies

In considering the use of offshore entities to hold Spanish-sited assets, there are many factors to be taken into account. Where real property is concerned, not the least of these is the new 5% Impuesto Especial, and the potential effects of Art 70 of the new tax Regulations[27].

In general a resident recipient will gain no ISD advantage from the simple interposition of a company. A trust superimposed on the company may avoid ISD but will bring other taxes with it, together with a greatly more complex compliance scene. This may be worth considering in some circumstances.

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27 ... both of which were covered in earlier editions of the OTPR.

A non-resident recipient may benefit from the use of a property-owning company, but should be aware of that tide in the affairs of Spain which is moving to negate such advantages.

It is possible to hypothesise circumstances in which the use of an offshore company, even for residents, would result in a saving of ISD. An example would be a wealthy man whose only remaining family is an unadopted stepson, also wealthy in his own right, both resident in Spain. In the hypothesis, the stepson would suffer the top marginal rate (34% x 2.6 = 81.4%) on his inheritance from stepfather. Instead, stepfather elects to leave his estate to a company which is not resident in Spain and has no permanent establishment there. The company would be assessable to Corporation Tax (ISS) on the value of the receipt, and so would pay 35%. The shares of the company are owned by non-resident trustees, and the stepson is a discretionary beneficiary of that trust. The immediate effect is a substantial saving of ISD. Getting the value into the stepson's hands is a whole further three-ring circus - but at least that can be deferred for later and provides his tax planner with space and time for manoeuvres and an average rate of, say, 60%.

Conclusion

This has been a somewhat breathless skate over the key features of an important tax. Inevitably it has left much unsaid; and much of that is to do with the interrelationships between this and other taxes when considered in the real world of how to handle a live client's affairs.