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Amendments to Spanish Act on patronage benefit foreign non-profit entities

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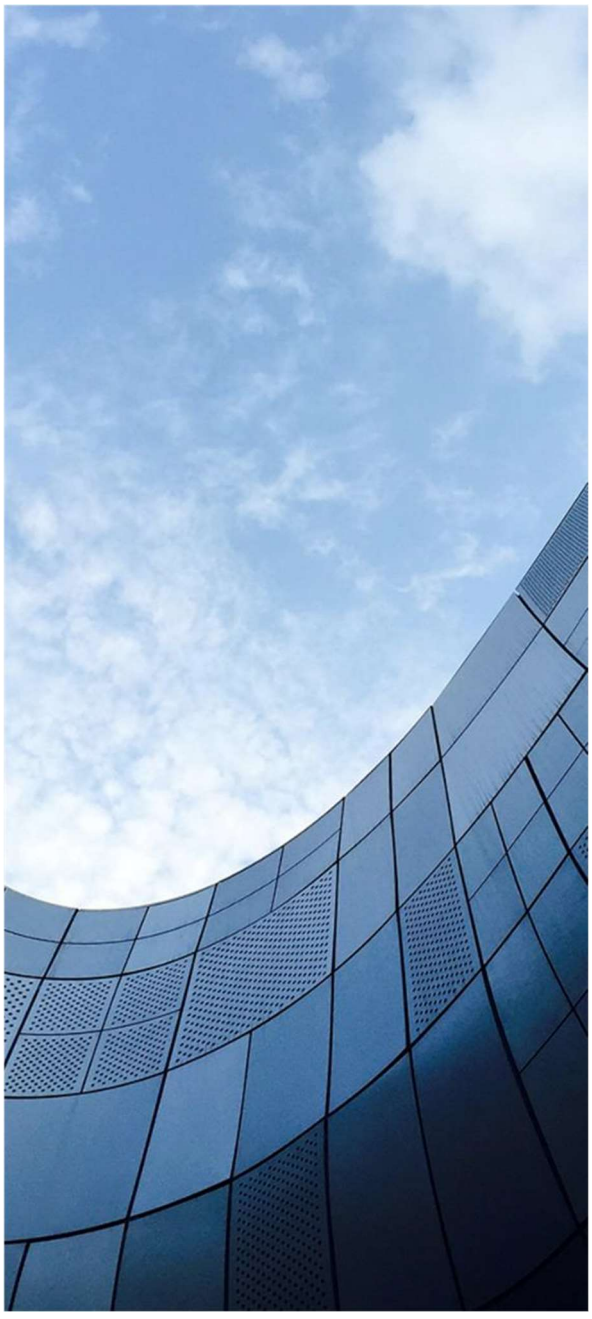

- As a new development, effective from January 1, 2021, the list of foreign non-profit entities with and without a permanent establishment in Spain has been extended. Now, those that meet certain requirements can apply the special tax regime provided under Act 49/2002 on patronage.

- From now on, Spanish individuals and companies that make donations to foreign EU non-profit entities that are taxed under Act 49/2002 (**"crossborder philanthropy"**) will be entitled to apply the tax incentives for patronage in their income tax (as in cases where the donation is made to a Spanish entity).

- Article 5 of Act 49/2002 has been amended to clarify that the regulations applicable to foreign non-profit entities will be those set out for non-resident income tax.

Introduction

In November 2015, the European Commission asked Spain to adapt its legislation, specifically Act 49/2002, of December 23, on the tax regime of non-profit organizations and tax incentives for patronage ("**Act 49/2002**") and its implementing regulation, to homogenize taxation in two ways:

1. The same tax treatment must apply to certain income obtained by foreign non-profit entities (particularly, those established in another EU or EEA state) and to certain contributions to those entities, allowing them to benefit from the same exemptions as Spanish non-profit entities.

   In the words of the Commission's press release: "*A foreign foundation deriving income, e.g. rent, from Spain should be exempt from taxation on that income, in the same way that a Spanish foundation would be*."

2. Spanish donors that make a gift to a foreign non-profit entity must be entitled to apply a deduction on their payable income tax as they would be allowed to deduct if the same gift had been made to a Spanish foundation according to Title III of Act 49/2002, for example.

The European Commission, in accordance with well settled case law of the Court of Justice of the European Union (**"CJEU"**) of cases C-386/04, *Centro di Musicologia Walter Stauffer* and C-318/07, *Persche*, made the request because it considered that the treatment given in Spain was discriminatory and restricted the free movement of capital in both cases.

Although at the time the Commission gave Spain two months to provide a satisfactory response and avoid the Commission referring it to the CJEU through an infringement procedure, Spain did not amend its rules until October 2021.

With the approval of Act 14/2021, of October 11, amending Royal Decree-Law 17/2020, of May 5, adopting measures to support the cultural sector and tax measures to face the social and economic impact of COVID-19 ("**RDL 17/2020**"), article 2 of Act 49/2002 has been modified, extending the subjective scope of non-profit entities that are eligible for and may apply the tax incentives provided under that act, and granting foreign non-profit entities comparable to a domestic one the same benefits from January 1, 2021.

Thus, Spain has adapted its rules, allowing foreign non-profit entities similar or comparable to Spanish entities to benefit from the special tax regime set out under Act 49/2002, also offering legal certainty to crossborder philanthropy provided by Spanish donors.

Below is an overview of the changes introduced under articles 2 and 5 of Act 49/2002, and other matters of interest that foreign non-profit entities are advised to take into account from now on to be able to benefit from the special tax regime.

Foreign non-profit entities under article 2 of Spanish Act 49/2002

Traditionally, Spanish law has granted special tax protection to certain non-profit entities, the most noteworthy of which, for the purposes of this legal flash, are those listed in article 2 of Act 49/2002 (among which we highlight foundations and associations declared of public interest). As long as they meet the requirements set out under article 3 of this act, these entities can voluntarily apply and benefit from corporate income tax and local tax incentives, while offering tax incentives to donors for any donations those entities receive.

Until the recent amendments were made under Act 14/2021, the only international foundations eligible were those referred to in article 2.d) of Act 49/2002, namely "delegations of foreign foundations registered on the Register of Foundations," which were also obliged to fulfill all the requirements set out under article 3 of Act 49/2002 to benefit from the special tax regime. As explained above, these rules and the fact that Spain had not brought them into line with EU law meant that the treatment given in Spain was discriminatory and restricted the free movement of capital because it did not grant tax benefits to foreign non-profit entities without a branch in Spain, despite being established in another EU or EEA Member State.

From January 1, 2021, the amendments to section f) and the addition of section g) of article 2, affect foreign non-profit entities as follows:

- Entities that are not resident in Spanish territory, but that operate in Spain through a permanent establishment and are comparable to those provided for in sections a) to e) of article 2 of Act 49/2002. That is, those similar to a foundation, an association declared of public interest or a sports federation, for example.

  Note that the regulations exclude entities residing in a non-cooperative jurisdiction for tax purposes, unless it is an EU Member State and it is accredited that the incorporation and operational setup is for valid economic reasons.

  Non-resident entities with a permanent establishment are treated in the same way as provided under the previous rule applicable to delegations of foreign foundations registered in Spain. Also, unlike the entities listed below, barring the exceptions specified in the previous paragraph, the Spanish legislator does not prevent foreign non-profit entities from non-EU countries with a permanent establishment in Spain from applying for the special tax regime.

- Entities resident in an EU or EEA Member State with which rules have been established on mutual assistance for the exchange of tax-related information as provided under Act 58/2003, of December 17, the General Taxation Act, without a permanent establishment in Spain, and are comparable to those provided under the previous sections of article 2 of Act 49/2002.

  Again, the regulations exclude entities residing in a non-cooperative jurisdiction for tax purposes, unless it is accredited that their incorporation and operational setup is for valid economic reasons.

Although the list of entities has been extended, it is not yet clear whether amendments will be made to the implementing regulation of Act 49/2002 to regulate, for the sake of clarity and harmonization with the CJEU doctrine, the conditions for a non-resident entity to be sure it will be considered comparable to a Spanish entity, among others.

Finally, to be able to benefit from the special tax regime established in Act 49/2002, non-resident entities operating in Spain, regardless of whether they do so through a permanent establishment, must fulfill all the requirements set out in article 3 of that act.

Rules applicable to foreign non-profit entities under Act 49/2002

Now that the list of non-profit entities has been extended, article 5 of Act 49/2002 has also been amended (effective from January 1, 2021) to clarify that the rules applicable to foreign non-profit entities, provided in sections f) and g) of article 2, will be those set out for non-resident income tax, not corporate income tax.

For additional information, please contact Cuatrecasas.