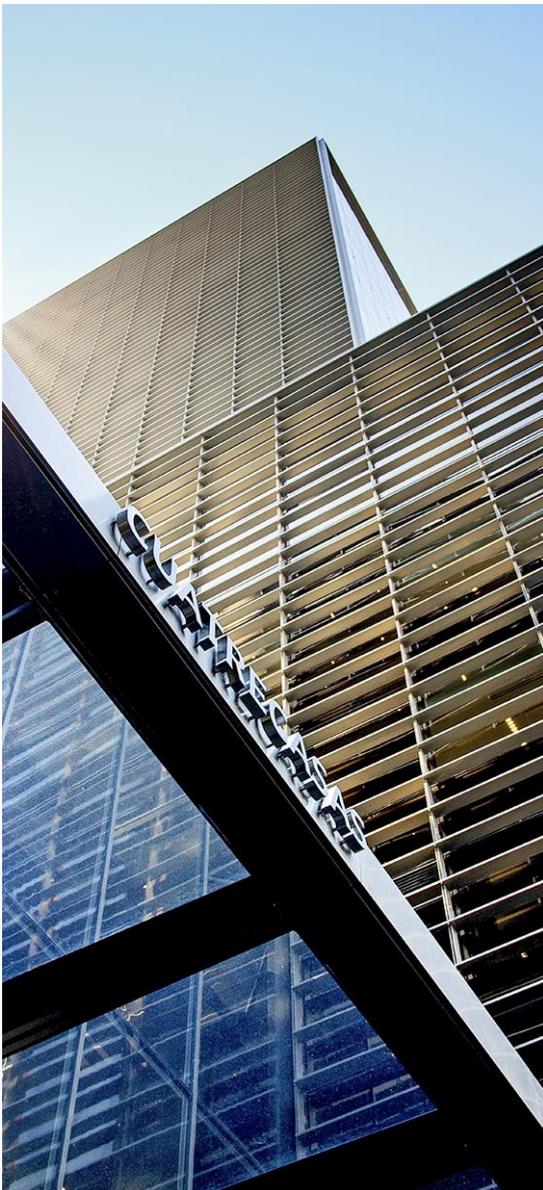

New developments affecting funds, entrepreneurs and impatriates

The bill to promote startups introduces significant changes affecting the venture capital industry, entrepreneurs and impatriates.

Legal flash

December 28, 2021



Key aspects

- Additional remuneration paid to managers of private equity and venture capital funds in compensation for their successful management (known as “**carried interest**”) qualifies as employment income for personal income tax purposes and will be included in the taxable base at 50% of its amount (if certain requirements are met) with the aim of promoting investment.
- To foster startups driving innovation, it **introduces tax benefits and flexibility** by applying certain rules to attract talent and investment in startups (taxation of stock options, investment tax deductions and the reduced taxation of startups).
- It modifies the **impatriate tax regime** to attract entrepreneurs and workers residing abroad, including so-called “digital nomads.”



Objectives and key measures

The **bill to promote the start-up ecosystem** (the “**Bill**”) has been submitted for parliamentary processing and **final approval is expected by mid-2022**. To foster startups driving innovation, it adopts measures to attract talent and investment in startups (tax benefits, simplification of procedures and flexibility in the application of certain rules), it promotes public support instruments and public-private partnership (e.g., innovation at universities) and it regulates regulatory sandboxes so that, during one year, startups in regulated sectors can carry out tests in an environment controlled by the corresponding regulator (as already implemented in the financial system under Act 7/2020).

As well as specific measures to foster the startup ecosystem, the Bill adopts other significant general tax measures aimed at favoring the establishment in Spain of highly skilled digital nomads and investors in qualifying startups, and at attracting investment from private equity and venture capital firms by establishing a tax break for fund managers’ carried interest.

According to the Bill, it is expected to enter into force on the day following its publication in the Official Gazette of the Spanish State, although the main tax developments would not be applicable until January 1, 2023. Moreover, several measures require authorization from the European Commission, as provided under state aid legislation.

This legal flash sets out the main developments—mostly tax related—introduced under the Bill affecting fund managers, startups, entrepreneurs and impatriates.

Developments affecting managers and funds: carried interest tax treatment

From January 1, 2023, the tax treatment of carried interest (referring to the additional remuneration paid to managers of private equity and venture capital funds in compensation for their successful management) will be regulated in line with the provisions in the legal systems of neighboring countries and of the chartered communities of the Basque Country.



Thus, to foster the investment of private equity and venture capital firms in all types of companies, the special economic rights resulting from certain entities and benefiting certain individuals will be considered employment income for personal income tax purposes and will be included in the taxable base at 50% of its amount.

Requirements to apply this rule:

- > **Entities granting special rights:** a) Closed-ended Alternative Investment Funds as defined in Directive 2011/61/EU included in some of the following categories: i) entities regulated under [Act 22/2014](#), ii) European venture capital funds, iii) European social entrepreneurship funds, iv) European long-term investment funds; and b) investment entities similar to these funds.
- > **Recipient:** The recipient must be a director, manager or employee of those institutions, or of their management companies or companies of their group.
- > **Special economic rights from shares or other rights:** These rights must be made conditional on the investors obtaining a minimum guaranteed return defined in the regulations or bylaws of the entity, and they must be maintained for at least five years, with some exceptions, such as an anticipated liquidation. Moreover, these rights cannot derive directly or indirectly from an entity resident in another country or territory classified as a non-cooperative jurisdiction or with which no rules have been established on mutual assistance for the exchange of tax-related information.

Developments affecting startups and entrepreneurs

To benefit from the support measures provided in the Bill, the company must be classified as a startup. This classification is for a fixed period of time, which means that the benefits associated with being classified as a startup will no longer apply when the company ceases to be considered as such, or at the end of the term specified in each case.

Concept of startup and accreditation requirements

Startups are defined as any legal entity that meets and maintains the requirements set out in the Bill, the most noteworthy of which are listed below:



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- The startup must have been in existence **for up to five years** (or **seven years** in the case of biotechnology, energy, industrial and other strategic companies, and companies that have developed their own technology in Spain, a requirement to be further developed by ministerial order).
- The startup must be **innovative**, i.e., it must be dedicated to solving problems or improving existing situations by developing products, services or processes that are new or substantially improved compared to the state of the art and involve a risk of technological or industrial failure.

Accreditation must be requested from the National Innovation Company (*Empresa Nacional de Innovación, S.A.* or ENISA), responsible for assessing the fulfillment of the requirements to be classified as a startup.

The startup must be registered as such in the commercial registry. This registration will be sufficient to access the benefits and specific rules applicable to startups.

More flexible commercial regulations

The legal form the vast majority of newly created companies choose is that of a private limited company (*sociedad limitada*, or “SL”). Therefore, the Bill offers several commercial advantages to startups that are incorporated as an SL, the most noteworthy of which are listed below:

- To favor the recruitment and retention of talent, the Bill adds **greater flexibility to the general treasury stock system** provided under the Spanish Companies Act to facilitate the adoption of stock option plans, which is currently a complex process owing to restrictions imposed on SL to purchase treasury stock. Thus, SLs considered startups can include in their bylaws that the remuneration scheme of directors, employees and other staff can involve the delivery of shares, and that the purchase of treasury stock is allowed up to 20% of the share capital to carry out the remuneration scheme (under a system similar to that adopted by public limited companies). This measure is complemented with a better tax treatment of stock options, as explained below in the section on tax benefits.
- The **term for registration** of startups incorporated as an SL and their corporate documents is five business days (instead of the 15 days generally given under [article 18.4 of the Spanish Commercial Code](#)).



- Until three years have passed since their incorporation, startups will be exempt from **grounds for dissolution due to qualifying losses**, as provided under [article 363.1. e of the Spanish Companies Act](#) (i.e., when the losses reduce the equity to an amount lower than half of the share capital), which means they are not subject to the requirements of equity balance set out in the Spanish Companies Act, enabling them to consolidate their business model.

Tax benefits

The Bill introduces three categories of measures:

- **Taxation of startups for corporate income tax purposes:** The Bill determines the following rates, effective for tax periods beginning after the Bill enters into force, presumably for companies whose tax year coincides with the calendar year, starting January 1, 2023:
 - A 15% tax rate (instead of the general 25% rate) applicable to the first tax period in which the tax base is positive and the following three years, as long as the company still qualifies as a startup.
 - A deferral, with no need to provide a guarantee, of corporate income tax during the first two tax periods in which the tax base is positive (12 months for the first period and 6 months for the second), if certain requirements are met. Moreover, during these periods, startups are exempt from making payments on account corresponding to corporate income tax.
- **Taxation of stock options granted to employees:** The Bill seeks to improve (effective from January 1, 2023) the remuneration schemes of startup employees:
 - **Increased exemption.** The exemption applicable to this income is increased from the generally established €12,000 to €50,000, as long as certain requirements are met (less demanding than those established for non-qualifying startups). It is expressly stated that the startup condition should be met exclusively when the stock options are granted.
 - **Extended exemption.** The Bill extends the exemption to non-resident individuals, modifying the regulations on non-resident income tax (“NRIT”). The new wording includes all compensation in kind that is exempt under article 42 of the Personal Income Tax Act (such as meal vouchers), and not just stock options.



- **Deferral.** Any excess on the €50,000 mentioned above, qualified as employment income, will be taxable in whichever of the following terms occurs first: 10 years, or when the share or stock is transferred, or the startup is admitted on a stock exchange or any other Spanish or foreign multilateral trading facility.
 - **Valuation.** The Bill provides rules for the valuation of these shares: the value will be the one given by an independent third party in the last capital increase carried out in the year before the one in which the shares are delivered (if no capital increase has taken place, the shares will be given the market value at the time they are delivered to the employee).
- **Taxation of startup investors:**
- From January 1, 2023, resident investors will benefit from a higher personal income tax deduction applicable to investments in new or recently incorporated companies. The deduction rate is set at 50% of the invested amounts up to €100,000, subject to the fulfillment of certain requirements (the current deduction rate is set at 30% and the maximum amount at €60,000).
 - Investors who are also directors or members of the board of directors of these companies can apply for the impatriate regime, as explained below.
 - From the date the act enters into force, non-residents will no longer be required to have a foreigner identification number (NIE), although they are obliged to have a Spanish tax identification number (NIF), which they can request through a simple online process.

Developments affecting impatriates

The Bill makes several amendments to the impatriate regime regulated under [article 93](#) of the Personal Income Tax Act in an attempt to make moving to Spain an attractive option for employees and entrepreneurs residing abroad.

Note that this regime allows individuals who become tax residents in Spain to only pay NRIT for the year they move to Spain and the following five years. This means, among others, that



non-Spanish earnings are not subject to taxation, while Spanish income and worldwide employment income is subject to Spanish tax (earnings obtained from work up to €600,000 will be subject to a set rate of 24%, and 47% for earnings exceeding that amount).

Below we list the main developments in the Bill that will enter into force on January 1, 2023:

- The regime will apply to individuals working abroad who have not lived in Spain during the five tax periods before moving to Spain (the current term established by law is ten years).
- It will also apply to “digital nomads” (professionals that work for a foreign company, providing their services remotely through the exclusive use of computer and telecommunication systems and resources).
- Startup entrepreneurs who are also a director or member of the board of directors can also benefit from the regime as long as there are no restrictions as to the share directors can hold in these companies.
- The regime also extends to entrepreneurs’ spouses and children up to the age of 25 years, or disabled children of any age. The regulations impose specific requirements for the above individuals to benefit from this regime.

For additional information, please contact Cuatrecasas.

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