



New tax incentive approved in Madrid for foreign taxpayers

Tax Alert



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Madrid Region approves new tax incentive for foreign individual taxpayers coming from abroad to invest and reside in Madrid.

With a view to attracting fresh foreign investment, the Madrid Regional Assembly has approved a new regional PIT credit for investments in certain securities by foreigners acquiring tax residence in Madrid.

This tax credit will apply to all transactions performed as of 1 January 2024.

The main features of this new tax credit, soon to be published in the Official Gazette of the Madrid Assembly, are explained below. However, it should be noted that the wording of the Draft Law regulating this new credit may be amended during its passage through parliament.

Who is eligible for the tax credit?

Natural persons not resident in Spain who relocate to the Region of Madrid and become personal income taxpayers, provided **they have not been tax resident in Spain during the five years preceding** the year in which the change of residence takes place.

Additionally, they must hold personal income taxpayer status in the Region of Madrid until the final year of the six-year mandatory investment period.

PIT credit rate and eligible investments

The PIT credit will amount to **20%** of the acquisition value, including the related expenses and taxes and excluding interest, of any of the following assets:

- a. Securities representing the assignment to third parties of equity traded on organised markets or otherwise.
- b. Securities representing holdings in the equity of Spanish or foreign entities, traded on organised markets or otherwise.

Where the relevant investments are in unlisted securities representing a holding in the equity of any kind of entity, eligibility for the tax credit will be subject to three requirements:

- ✓ The entity in question must not be incorporated or domiciled in a tax haven.
- ✓ The direct or indirect holding of the taxpayer, combined with any such stake as may be held in the same entity by their spouse or individuals to whom they are directly or indirectly related, by consanguinity or affinity, up to and including

the second degree, **may not exceed 40%** of the capital or voting rights of the entity on any day of the six calendar-year period for which the investment must be held.

- ✓ The taxpayer must not exercise executive or management duties at, or have an employment relationship with, the entity in which the investment is held.

Deadline for investment

Investments consisting of **securities representing the assignment to third parties** of equity issued by **Spanish entities**, or **securities representing a holding in the equity of Spanish entities** may be made in any of the following three years:

- in the year preceding that in which tax residence in Madrid is acquired;
- in the year in which tax residence in Madrid is acquired; or
- in the year following that in which tax residence in Madrid is acquired.

In the case of **eligible investments other than those described above**, the investment may be made:

- in the year in which tax residence in Madrid is acquired; or
- in the following year.

Minimum investment period

The taxpayer must maintain the acquired assets for a minimum period of six years.

However, this minimum investment period requirement will not be deemed breached where an investment is disposed of and the proceeds are fully reinvested in any eligible assets within one month.

When is the tax credit to be taken?

Generally speaking, the tax credit may be taken in the year in which the investment is made or, where the taxpayer in question has insufficient tax payable in that year to use it, within the five years immediately following it.

In the specific case of investments in securities representing the assignment to third parties of equity issued by Spanish entities, or securities representing a holding in the equity of Spanish entities made in the year preceding that in which personal income taxpayer status in Spain is acquired, the tax credit may be taken in the year in which tax residence is acquired or within the five years immediately following it.

Any other regional tax credits to which the taxpayer may be entitled will be applied before this new credit is taken.

Can entitlement to the tax credit be lost?

Yes, entitlement to the tax credit will be forfeited in the event of loss of tax residence in Madrid during the six-year minimum investment period, and in the event of breach of the obligation to maintain the investment (i.e. if the assets - the securities referred to above - are transferred before the above period elapses without the requisite full reinvestment).

Is it incompatible with other tax credits?

The new tax credit envisaged in the Draft Law is incompatible -in respect of a single investment- with regional tax credits for the acquisition of shares or holdings in new or recently created entities, or for investments in companies listed on the Alternative Stock Market.

And with the inbound expatriates regime?

The tax credit is incompatible with the inbound expatriates regime as it is not envisaged in such scheme. Application of the special inbound expatriates regime involves calculating the taxpayer's PIT liability in line with the provisions set forth in the revised Non-Resident Income Tax Law, the assessment structure of which does not factor in regional tax credits for the purpose of determining the tax due.

Practical implications

The future tax credit requires a detailed analysis of each particular case, as whether or not a given investment may be optimised depends on the specific circumstances of each investor and the taxpayer's expected income throughout the entire period in which it may potentially apply (the year of the investment and the following five years in the event of insufficient gross tax payable). Thus, when deciding how much to invest, taxpayers should take into consideration not only the income earned in the year of the investment, but also that which will be earned in subsequent years, to assess whether they have a sufficient amount of gross tax payable to be able to take advantage of the credit.

Subject to individual analysis, this tax credit may prove more beneficial for high-income taxpayers with sufficient personal income tax liability to avail themselves of it.

Nonetheless, the impact of the investment on wealth taxation in the Region of Madrid, and on the tax on large fortunes, should also be considered.

For a non-resident who is thinking of coming to Spain, and specifically to Madrid, it is important to analyse what the inbound expatriates regime (if they meet the relevant requirements) and the ordinary regime would mean for them and, where appropriate, apply the tax credit for investment in Madrid.

One potentially significant difference between the two regimes is the following:

There is one major difference between the two regimes:

- Under the inbound expatriates regime, wealth tax and/or the tax on large fortunes is only paid on assets or rights located, exercisable or enforceable in Spain, while PIT is only levied on Spanish-source income, deemed to include all earned income and income from economic activities officially classed as entrepreneurial activities, and not on other income not received in Spain (foreign-source dividends, capital gains, rent, etc.).
- If the taxpayer does not opt for the inbound expatriates regime, and therefore opts for the general regime for residents in Spain, potentially taking advantage of the Madrid tax credit, as an ordinary resident they must, in principle (except where there are double taxation treaties in place) declare their worldwide wealth and income and report their assets located abroad (tax form 720) if the minimum threshold (€50,000 for each group of assets) is exceeded for such purpose.

It is thus extremely important for individuals who are considering the possibility of relocating to Spain, and specifically to the Region of Madrid, to analyse their circumstances in order to determine their taxation.

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