

GMS Flash Alert



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Spain - Supreme Court Ruling on Exemption for Directors' Overseas Work

On 20 June 2022, Spain's Supreme Court issued an important ruling (STS 2485/2022) that was published in the first days of July on a subject that has been traditionally very controversial, regarding the eventual applicability to directors of the exemption contained in article 7.p) of the Spanish Personal Income Tax Law ("PIT Law") for income related to work performed outside Spain.¹

WHY THIS MATTERS

The customary restrictive criterion followed by the General Directorate of Taxes in its rulings has inhibited companies and taxpayers from applying the exemption contained in article 7.p) of PIT Law for work performed outside Spain when the individual performing the services outside Spain was a director or member of the Board.

Considering the arguments contained in the Supreme Court's ruling STS 2485/2022 of 20 June, the mere condition of the individual performing the services outside Spain, being a director should now not automatically imply that the exemption does not apply. Therefore, if in fact the services performed by the director are rendered for the benefit of a nonresident entity or permanent establishment and do produce a utility or advantage to it, the remuneration corresponding to those duties performed abroad could qualify for the article 7.p) exemption and be left exempt from taxation in Spain.

Companies should therefore analyse the specific tasks performed by their directors when performing services outside Spain to evaluate whether they could benefit from the article 7.p) exemption for the work performed abroad, with an annual maximum limit of EUR 60,100.

Article 7.p) Exemption for Income Obtained for Work Performed outside Spain

Spanish tax resident individuals are subject to taxation on their worldwide income, meaning that, in principle, work income for services rendered abroad will be taxable. However, an exemption for work income corresponding to work performed outside Spain regulated in article 7.p) of PIT Law may be applied, if the following conditions (among others) are met:

- ◆ Services are physically rendered outside of Spain for the benefit of a nonresident company or a permanent establishment located abroad.
- ◆ The country/jurisdiction where the services are rendered is not a tax haven and has a tax similar to Spanish PIT (this requirement will be regarded to be met when the country/jurisdiction in which the services are performed has a tax treaty to avoid double taxation in force with Spain with an exchange of information clause).

The income that may benefit from this exemption has an annual maximum limit of EUR 60,100.

What Type of Work Income Qualifies for Exemption?

From a formal point of view, PIT Law considers remuneration received by directors and members of the Board as work income. In this regard, article 17 of PIT Law contains the regulation of what type of income should be considered as work income, with a section 17.1 that defines as such any compensation derived from labour or a statutory dependant employment relationship, but also a section 17.2 that formally classifies as work income some other types of income. Especially included in section 17.2 is remuneration received by directors and members of a Board.

Given that article 7.p) indicates that the exemption for qualifying services performed outside Spain applies to work income in general without any further specification or restriction about which particular type of work income, it could have been understood that the expression “work income” (and therefore the application of the exemption) also applies to remuneration obtained by directors when performing their services outside Spain for the benefit of a nonresident entity or permanent establishment.

Resolution of the Controversy

Nonetheless, the traditional position of the Spanish General Directorate of Taxes in the rulings issued on this subject has been to limit the application of the exemption only to that work income described in article 17.1 of PIT Law (i.e., to income deriving from a dependant labour relationship) and to deny its application to other types of work income contained in article 17.2 of PIT Law, including remuneration received by directors for their services performed outside Spain, as it is not deriving from such a dependant employment relationship.

However, the Spanish National Court, in a ruling issued 19 February 2020, established that directors and members of the Board might have access to the exemption considering that, no matter their eventual mercantile relationship with the company, their remuneration is formally regarded as work income by Spanish PIT Law.

An appeal was filed by the State Attorney against the aforementioned court ruling; that has now been resolved by the Supreme Court in the relevant ruling STS 2485/2022 of 20 June 2022. The Supreme Court has confirmed the position raised by the National Court’s ruling and rejected the appeal. The Supreme Court has also established that the restrictive interpretation followed by the General Directorate of Taxes has no support in a literal, logical, systematic, and final interpretation of article 7.p) of PIT Law and that, in principle, the application of the exemption cannot be rejected for the mere fact of the taxpayers involved being directors or members of a Board.

KPMG NOTE

The above however does not imply that directors and members of a Board will always be able to apply the exemption in respect of income from work performed abroad as contained in article 7.p) when performing their duties outside Spain. It will be necessary to analyse on a case-by-case basis the actual content of the services performed abroad to determine whether they are in fact rendered for the benefit of a nonresident entity or permanent establishment located abroad.

It must be noted in this regard that the Supreme Court ruling of 21 March 2021 (STS 1141/2021), had rejected the applicability of the article 7.p) exemption to a case in which the director travelled abroad to attend Board meetings of a foreign subsidiary merely exercising a supervisory capacity of the Spanish parent company.

FOOTNOTE:

1 For the complete text of the Supreme Court ruling, in Spanish, see Cendoj 28079130022022100194, *Consejo General de Poder Judicial*, Roj: STS 2485/2022 - ECLI:ES:TS:2022:2485 at: <https://www.poderjudicial.es/search/TS/openDocument/e8955c522dd656b1a0a8778d75e36f0d/20220701> .

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