

DOING
BUSINESS
IN

SPAIN



BOVÉ MONTERO Y ASOCIADOS

DOING BUSINESS IN SPAIN

9th edition

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Note: This booklet was prepared during the fourth quarter of 2006 and therefore includes only the law in force up until that time. Readers are requested to contact one of our offices for additional information.

ACKNOWLEDGEMENTS

It is always difficult to summarise in a booklet of this size the legal, fiscal, accounting and labour rules which govern the creation of a business in Spain. We have tried to prepare a publication that covers the basic areas, in a language accessible to the businessman; if we have achieved that, we will be happy. If moreover via the Spanish version and its translations into English, German, French and Italian, we have helped to make Spain a country whose business world is better known by foreign investors, we shall be very pleased to have contributed in this way to the development of the Spanish economy.

The updated 9th edition of this work, covering the law prevailing in 2007, was written by personnel of our tax department. The person responsible for its coordination is Belén Fernández.

The whole process of editing, translating and distributing this booklet to clients and friends of Bové Montero y Asociados has been coordinated by Mrs Pollinger.

Lastly, and especially, we are grateful to the Secretary General of the Spanish Chamber of Commerce in Great Britain, José Fernández Bragado and his team for the translation into English of this booklet, using accurate terminology.

To all of them, my most sincere thanks.

José M^a Bové

FOREWORD

This booklet has been prepared for the use of clients, partners and staff of HLB International member firms.

It is designed to give some general information to those contemplating doing business in Spain and is not intended to be a comprehensive document.

You should consult us, therefore, before taking further action. HLB Bové Montero y Asociados and HLB International cannot be held liable for any action or business decision taken on the basis of information in this booklet.

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HLB BOVÉ MONTERO Y ASOCIADOS

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I. INTRODUCTION

I.1 GEOGRAPHY

Spain occupies approximately 500,000 square kilometres, and is situated in the South-West of Europe. It includes most of the Iberian Peninsula, which it shares with Portugal, and also the Balearic Islands, in the Mediterranean, the Canary Islands, in the Atlantic Ocean off the coast of North Africa and Ceuta and Melilla on the coast of Africa. Spain has approximately 45 million inhabitants. The most important Spanish cities are Madrid, Barcelona, Valencia, Seville and Zaragoza.

I.2 POLITICAL INSTITUTIONS

The form of government of the Spanish State is a parliamentary monarchy. The King is the Head of the State, and his primary duty is to oversee the proper functioning of the country's institutions. He is the chief representative of the Spanish State with regard to international relations and carries out the functions expressly assigned to him by the Constitution and law.

The «Cortes Generales» (Parliament) represent the Spanish people and are composed of the «Congreso de los Diputados» (House of Representatives) and the «Senado» (Senate).

They are responsible for all legislation.

The Government is responsible for internal and external affairs, civil and military administration and State defence. It exercises executive and law making power. The Government is composed of the «President» (Prime Minister) and Ministers.

The Spanish State is divided territorially into municipalities, provinces that may include several municipalities, and Autonomous Communities, each of which covers various neighbouring provinces with similar historical, cultural and economic characteristics. There are seventeen Autonomous Communities and two Autonomous Cities within the Spanish State.

Autonomous Communities control certain matters, such as the organisation of self-governing institutions, the promotion of economic development or public health services. The organization of Autonomous Communities is based on a Legislative Assembly elected by universal suffrage, a Governing Council with executive and administrative functions, and a President, elected by the Legislative Assembly from amongst its members and appointed by the King. The President is the head of the governing council and is the chief representative of the community in question.

I.3 LANGUAGES

Spanish is the official language of the Spanish State. Catalan, Basque, Valencian and Galician are also officially recognised in their respective Autonomous Communities.

II. INVESTING IN SPAIN

The Maastricht Treaty of the European Union allows for complete freedom of capital movements, whilst recognising at the same time the ability of member states to have administrative requirements relating to such movements.

As a consequence of the above the current legal position in Spain, which has liberalised foreign investment, requires as a general rule the notification of foreign investments post facto. However, for certain types of investments from those territories or countries that under current rules are considered to be tax havens, notification is also required before the investment is made.

There are however special rules relating to foreign investments in Spain in certain sectors and in particular in air transport, radio, minerals and raw materials of strategic value and mining rights, television, gambling, telecommunications, private security, the manufacture distribution or trading in armaments and explosives for civilian use as well as activities connected with National Defence.

The Government can suspend this liberalised regime in the case of investments whose nature, form or method of implementation affects or may affect the exercise of public authority, the maintenance of public order, safety or public health.

The following are considered to be foreign investors:

- Non-resident individuals, defined as Spaniards or foreigners domiciled abroad or having their principal residence abroad.
- Legal entities with a foreign domicile and public bodies of a foreign state.

A change of domicile by a legal entity or the change of principal residence of an individual will also alter the classification given to a foreign investment.

II.1 FOREIGN INVESTMENTS

For administrative purposes foreign investments in Spain can be carried out as follows:

- a) Taking shares in Spanish companies, whose value is not listed on secondary markets. This includes setting up companies, subscribing and acquiring all or part of companies' share capital or joining a partnership. This heading also includes the acquiring of securities such as rights to subscribe for shares or convertible loan stocks or similar securities, which, owing to their nature, give rise to rights on the share capital or any voting rights.
- b) Investing in shares of Spanish businesses whose capital is fully or partially listed on Spanish or foreign stock markets, as well as in subscription rights or similar, whatever the place of issue and acquisition.
- c) The establishment or expansion of branches.
- d) The subscription to or acquisition of negotiable instruments relating to loans issued by residents.
- e) Investment in Investment Funds registered with the National Commission for Stock Markets.
- f) The acquisition of property situated in Spain whose value exceeds 3,005,060.52 euros or of any value if it derives from a tax haven.
- g) Other forms of investments: The establishment of, formalising of or sharing in joint ventures, foundations, consortia, co-operatives and partnerships where the total value of the foreign investment exceeds 3,005,060.52 euros, or of any amount if it derives from a tax haven.

II.2 ADMINISTRATIVE PROCEDURES

Foreign Investments in Spain, and their disposal, have to be declared to the Register of Investments at the Ministry of Industry, Tourism and Trade.

Such notifications have to comply with the following rules:

1. Prior notification:

If the investment derives from a tax haven the investor must give notice before the investment is made. This is without prejudice to the need to give notice after the investment has been made.

There are exceptions to the above rule: Investments in negotiable instruments, contributions to Investment Funds registered with the National Commission for Stock Markets and investments which give

raise to a foreign interest of less than 50% in the Spanish company in question, whether prior to the investment or after it.

Prior notification of investment plans must be presented by the main investor. This notification will be valid for a six-month period, starting on the day of notification. If the investment does not take place within that period, notification of the investment will have to be made again.

The disposal of foreign investments deriving from tax havens will not require prior notification.

2. Subsequent notification

In general investments have to be notified by the non-resident investor. In addition, if the transaction has been handled by a Spanish notary, then the latter will forward information on the transaction.

There are special procedures for certain securities. If the securities are negotiable instruments then the obligation to declare them rests on the investment business or credit institution or financial institution responsible for the transaction. Investments in securities, which are not traded on secondary markets, have to be declared by the entities holding or administering the securities or by brokers or credit institutions involved in the transaction. When investments are made in registered shares of a Spanish company, it is the company's duty to notify the authorities. Investments in Spanish investment funds are notified by the company managing the fund.

As for the form of notification and period within which the declaration of investment has to be made, the declaration relating to investments in not traded companies, branches and properties must be made within a month.

The declaration of investment regarding negotiable securities must be done by the depositary and administering institution of the securities or by those who carry out buying and selling transactions, instructed by non-residents.

Finally, under certain circumstances or by requirement, Spanish companies with foreign shareholders and the Spanish branches of non-residents must report annually on the development of the investment to the General Directorate of Trade and Investments of the Ministry of Industry, Tourism and Trade within a maximum period of 9 months from the end of their business year.

Failure to comply with obligations relating to the notification of foreign investment can be a punishable offence.

II.3 TRANSFERS ABROAD

Holders of foreign investments have the right to repatriate the proceeds of sale of such investments and any legally obtained profits.

This right is not incompatible with the administration procedures outlined above, or with the specific regulations of exchange control, which has now been completely liberalised.

II.4 INVESTMENT INCENTIVES

a) Regional Incentives

These are regulated, in certain aspects, by European Union (hereinafter «E.U.») directives. They are applicable to companies intending to establish themselves in underdeveloped zones, with high unemployment rates, or with industries in crisis.

The central Government, through various Ministries, offers assistance in specific areas. In addition, the Autonomous Communities are developing their own programmes of incentives that are carried out by various Councils and Departments.

Amongst the incentives available, the granting of loans on substantially more favourable conditions than those available on the market should be highlighted. Loans may be made to finance fixed assets, the creation of companies, and investments in research and development. Incentives are also available for the international development of companies.

b) European Union Incentives

Of the Community Funds of the EU budget the so-called structural resources play a very significant role. These resources are the so-called European Structural Funds and also the Cohesion Fund. Both are the main instruments which the European Union has to strengthen economic and social cohesion and reduce disparities between regions by funding regional development plans in cooperation with member States.

II.5 FOREIGN EXCHANGE CONTROL

Spanish exchange control legislation has been progressively liberalised and today exchange control is not an obstacle to doing business in Spain. Indeed, the basic principle on which the exchange control regime is established is the total freedom of capital movements and financial transactions with foreign countries so that any activity, business, transactions and operations

between residents and non-residents involving, or which may involve, overseas receipts and payments as well as transfers from and to a foreign country and changes in debtor or creditor accounts or financial positions as a result of overseas trade are unrestricted save for any special limitations imposed by law.

The basis for this liberalisation is Directive 88/361/EEC, but the Government has gone further by extending its application to transactions with all countries, whether EU members or not.

It can be said that the requirement of prior authorisation for transactions with a foreign country has disappeared.

However, the following transactions have to be declared:

- Taking out of or bringing into Spain coins, bank notes or bank cheques to bearer in euros or any other foreign currency or any physical means, including electronic, intended to be used as a means of payment in excess of 10,000 euros per person per trip.
- Movements through Spain of means of payment consisting of coins, bank notes or bank cheques to bearer denominated in euros or any other currency or any physical means, including electronic, intended to be used as a means of payment of an amount exceeding 100,000 euros.

The reference to electronic means of payment does not include personal debit or credit cards.

Notwithstanding the above, cash transactions between residents and non-residents, as well as transfers to or from abroad made through banks are not subject to any exchange control. A resident only has to give the bank, through which a receipt, payment or transfer is effected, the information necessary for the transaction. No further documents, DUAS (Single Administrative Documents) or contracts are necessary. This declaration is not required, if the amount of all receipts, payments and transfers does not exceed 12,500.00 euros.

Payments and transfers to a foreign country are not subject to prior investigation of compliance with taxation regulations.

As far as loans and credits from abroad are concerned, it is necessary to declare the following to the Bank of Spain:

- The financing and deferment of receipts and payments due in over one year, derived from commercial operations or services, for a total amount of 600,000.00 euros or more.
- The netting of credits and debits between residents and non-residents for transactions of any nature, for a total amount of 600,000.00 euros or more.

- The netting of credits and debits derived from broking operations on the financial markets, by entities that carry out the said operations.
- Financial loans received from non-residents or granted to non-residents, for a total amount of 3,000,000.00 euros or more.

Residents may open bank accounts at the overseas offices both of registered Entities and foreign banking and credit Entities. Holders of these accounts are obliged to declare their opening and closure and supply information on movements to the Bank of Spain. This duty to supply information does not exist when the total amount of receipts and payments have not exceeded during the full calendar year 600,000.00 euros or its equivalent in other currencies. For accounts in foreign currencies held by residents with registered Entities operating in Spain, there is no duty to declare.

For non-residents, the opening and maintenance of accounts in foreign currencies or in euros with offices in Spain of registered Entities is free from control.

II.6 SOURCES OF FINANCE

Spain has a diversified and modern financial system, which is fully integrated into international financial markets. The system includes credit, stock and money markets, as well as specific markets for derivatives (options and future contracts based on different assets).

Only the money market is subject to direct public-sector control, and even so it is open both to banks and investment companies as well as to broking companies. As a result a large number of dealers are engaged in this market. As far as the credit and stock markets are concerned, government involvement is confined almost exclusively to regulating the conditions of access, to maintaining a permanent presence by regular dealers and to monitoring the operations of financial enterprises, all of it conforming to the practices normally used in economically developed countries. Regulation is in the hands of the National Stock Market Commission.

Classification of operators in the Spanish financial system:

1. The central bank: The Bank of Spain
2. Lending Institutions
 - Banks:
 - Spanish
 - Foreign
 - Savings Banks
 - Credit cooperatives - Rural savings banks
3. Other lending institutions
 - Finance leasing companies
 - Spanish Official Institute for Credit
4. Investment Institutions:
 - Collective Investment Institutions
 - Investing Companies:
 - Securities
 - Real Estate
 - Mutual Investment Funds:
 - Securities
 - Real Estate
 - Money Market Assets
 - Mortgage Bonds
 - Pension Plans and Funds
 - Others
 - Venture Capital Funds and Companies
 - Other investment institutions
5. Brokers
 - Stock Exchange Market
 - Stock exchange companies and agencies
 - General
 - Banks
 - Companies managing securities and deposits
6. Insurance and reinsurance companies and insurance brokers

II.7 ECONOMIC AND MONETARY UNION

Economic and monetary union is understood to be the process intended to harmonise the economic and monetary policies of the member States of the Union for the purpose of adopting the euro as the single currency. It is an area sharing a single market, the same currency and applying a single monetary policy.

The euro is the currency of the following member States: Portugal, Spain, France, Luxembourg, Holland, Belgium, Germany, Italy, Austria, Greece, Finland, Ireland and Slovenia. Denmark, the United Kingdom and Sweden have not joined the monetary union. The other member countries of the EU will do so when their economies meet the required convergence criteria.

III EMPLOYMENT REGULATIONS AND SOCIAL SECURITY CONTRIBUTIONS

Labour relations in Spain are basically governed by the following sources:

First, by the Workers' Statute («Estatuto de los Trabajadores»).

Secondly, by the collective agreements which are negotiated between the company and representatives of the workers and which must be observed by both parties.

The fundamental points of Spanish labour legislation can be summarised as follows:

III.1 WAGES

There are certain limits:

- There is a minimum wage, fixed yearly by the Government, which at the present time amounts to 570.60 euros per month.
- Annual collective wage agreements by sector are agreed, which improve on the minimum wage mentioned setting wages levels in accordance with professional categories.

Wages, which are agreed as an annual gross amount, are normally paid in fourteen instalments per year. The workers are entitled to at least 2 months extra pay per year. There are also collective agreements that provide for pro rata payment of these extra payments over the year.

III.2 WORKING HOURS

- The maximum legal working week over the year is an average of 40 hours and the working day cannot exceed 9 hours, except when, by a collective agreement or by agreement between the employer and representatives of the employees, another way for allocating the daily

hours of work is agreed; however there must be a rest period of at least 12 hours between working days.

- Overtime may not exceed 80 hours per year.
- The annual holiday entitlement is 4 weeks and 2 days for a full year worked.
- There are also 14 local, autonomous and national public holidays every year.

III.3 EMPLOYMENT RIGHTS

These are recognised by the Constitution and set out in the «Workers' Statute»; the main points are:

- The right to belong to trade unions, including the right to set-up trade unions and to join the union of choice.
- Workers have the right to go on strike to defend their interests.

III.4 CONTRACTS OF EMPLOYMENT

Contracts of employment can be established for definite or indefinite periods. In the case of the latter the employer cannot terminate them unilaterally, unless one of the situations provided for in the Workers' Statute arises, that is to say, by dismissal on disciplinary grounds based on serious and negligent breach of duty by the employee. If these grounds do not exist and the dismissal is declared unfair, the employer has to pay compensation equivalent to 45 days' pay, per year of service, up to a maximum of 42 months' salary.

The dismissal of an employee will be declared void in the following instances:

- If the reason for it is one of the types of discrimination forbidden by the Constitution or by law.
- If the basic rights and civil liberties of the employee are infringed.

In a similar way, the dismissal of staff for taking leave or enjoying other benefits which are allowed by law to promote family or employee well-being (maternity leave, a shorter working day for taking care of family members, etc.) may be considered justified or void.

The consequence of a dismissal being declared void is the compulsory re-employment of the employee.

The Law permits the termination of a contract of employment, in the objective circumstances expressly set out in the statute. In addition, the following requirements must be complied with:

- a) Written notice to the employee, stating the reasons for the dismissal.
- b) Compensation of 20 days' pay, per year of service, payable upon delivery of the written notice, with a maximum of 12 months' wages.
- c) Thirty days' notice of the termination of the contract, to commence from the moment of the official notification to the employee, until the end of the work contract.

In addition to the contract of indefinite duration there are several other forms of contract that make the system more flexible:

- A job creation programme for 2007: businesses can obtain reductions in their social security contributions if they employ for indefinite periods people who meet one of the following criteria:
 - Women in particular circumstances
 - Unemployed young people between 16 and 30 years of age
 - People aged over 45
 - Disabled people
 - Other groups: victims of gender-based violence, people unemployed for at least six months, workers affected by social exclusion.
- Part-time contracts: This allows the rendering of services for a specified number of hours per day, per week, per month or per year provided that the number of hours worked is less than the full-time equivalent.
- Fixed duration contracts: these contracts may be used for particular pieces of work or services. They are of a temporary nature and are used where additional labour is needed for a specific reason, e.g. to meet production requirements, or for the temporary replacement of an employee or for occasional intermittent work.
- «Practice» contracts: these can be agreed with holders of one of the following qualifications: a university degree or a certificate of professional training at medium or higher level or an officially recognised equivalent certificate. These contracts can be entered into during the four years immediately following the completion of the relevant studies.
- Apprenticeship contracts: their purpose is to impart the theoretical and practical training necessary for the proper performance of a trade or a profession.

All the above contracts must be put in writing and registered with the National Employment Office. An oral contract is taken to be of an indefinite duration.

III.5 SPECIAL LABOUR SYSTEMS

There are special regulations governing employment contracts for groups of people whose work is of an unusual or special nature such as senior management, commercial travellers and professional sportsmen.

The law governing agency contracts («Ley de contrato de Agencias») may apply to personnel engaged in trading as agents or brokers, and defines a trade relation and agrees with Community Law in relation to Trade Agents.

III.6 SOCIAL SECURITY

Social Security contributions are paid partly by the employer and partly by the employee. Personnel are classified into a series of professional and labour categories for the purpose of determining their Social Security contributions. Each category has a maximum and a minimum contribution rate, which are usually revised every year.

At present, the professional and labour categories and the maximum and minimum rates are as follows:

CATEGORY	MIN. RATE	MAX. RATE
	Euros/month	Euros/month
1. Engineers, graduates and senior management	929.70	2,996.10
2. Qualified technicians and assistants	771.30	2,996.10
3. Clerical and workshop supervisors	670.80	2,996.10
4. Unqualified assistants	665.70	2,996.10
5. Clerical officers	665.70	2,996.10
6. Subordinates	665.70	2,996.10
7. Clerical assistants	665.70	2,996.10
	Euros/day	Euros/day
8. Foremen classes 1 and 2	22.19	99.87
9. Foremen class 3 and craftsmen	22.19	99.87
10. Unskilled workmen	22.19	99.87
11. Workers under 18 years of age	22.19	99.87

The contribution rates applicable for employers and employees are as follows:

	EMPLOYER (%)	EMPLOYEE (%)	TOTAL (%)
General contingency	23.6	4.7	28.3
Unemployment	5.75	1.55	7.3
Professional training	0.6	0.1	0.7
Salary guarantee fund	0.2	—	0.2
	30.15	6.35	36.5

These rates may be increased in proportion to the risk of industrial accidents from the type of activities carried out by a business.

The main benefits provided by the Social Security system are: medical and pharmaceutical services, as well as financial assistance to cover the following situations: temporary incapacity, risk during pregnancy, maternity, permanent disability, retirement, bereavement, loss of parents, unemployment and family support.

III.7 EMPLOYEES REPRESENTATION

Employees are represented by company committees or by employee delegates, depending on whether or not the number of employees' exceeds 50. These representatives have a right to information on the employer's financial situation and to copies of its annual report.

The members of committees are elected directly by the employees.

Where multinational companies are obliged to set up a European Works Council the (Spanish) member of it will be elected from amongst the members of the Spanish Committee.

III.8 STATUS OF FOREIGNERS

There are two different regimes:

1. Citizens of member states of the EU: As from the 1 January 1992 and in accordance with community regulations any EU citizens may work in Spain under the same conditions as a Spanish citizen. They do not need to obtain work permits and residence permits to do so.

Notwithstanding the above, and without it being a requirement for being able to work in Spain, any citizen of the EU intending to reside in Spain for more than three months should obtain a residence card.

2. The rules governing the residence of foreigners from countries outside the EU are as follows:
 - Short term: In general a period of ninety days is allowed unless an extension or a residence permit is obtained.
 - Temporary residence permits for up to 5 years. In general this is granted when the applicant has sufficient financial resources or the offer of a contract of employment.
 - Permanent residence: This is for people who have had temporary residence for 5 years. It allows the holder to work under the same conditions as Spaniards.

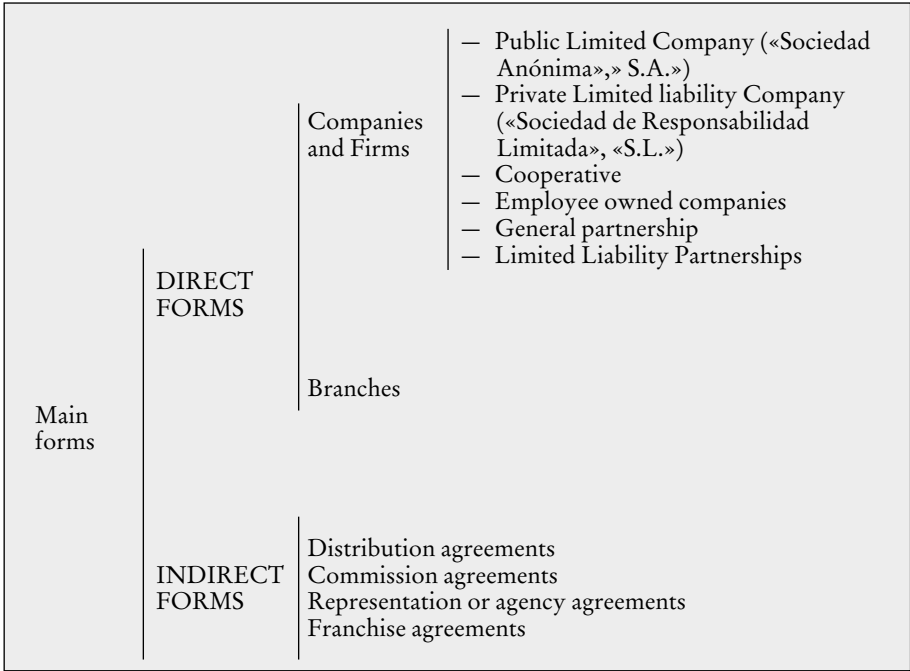
Prevailing legislation on the rights and civil liberties of foreigners in Spain and their integration into society regulates their rights, including access to education, Social Security, health care and the right of assembly on the same conditions as Spaniards. Other rights conceded are votes in local elections, access as workers to government services and the right to family reunion.

III.9 MANAGEMENT RESPONSIBILITIES

Companies' Boards of Directors and management teams can incur personal liability (civil, administrative or criminal) for the actions of the company under certain circumstances such as failing to pay social security contributions, breaches of health and safety at work regulations, the fraudulent use of subcontractors etc., and, in consequence, specialist advice is necessary in this area.

The safety at work law number 31 of 1995 and supplementary rules are of fundamental importance. They prescribe substantial penalties, up to 600,000 euros, if the company does not have a proper accident prevention scheme in place. It must not be forgotten that this is now a high priority for the Labour Inspectorate.

IV. MAIN FORMS OF BUSINESS



In addition to the forms referred to above it may be appropriate for some foreign investors to associate with Spanish businesses in one of the following ways: Economic Interest Grouping, European Economic Interest Grouping, Temporary Company Union, Joint Purse Agreements and Joint Ventures through public or private limited companies.

IV.1 FORMATION OF COMPANIES

In the last few years there have been substantial changes in commercial law for the basic purpose of adapting Spanish law to Community law.

On 1st January 1990, Law 19/1989 of 25th July came into force, revising and adapting Spanish commercial legislation to Community law in respect of companies.

Also, on 1st June 1995 a new law for Private Limited Liability Companies («Sociedades de Responsabilidad Limitada») came into force, which partially amended the legal regime for public limited companies («Sociedades Anónimas») and on the 2nd June 2003 the New Enterprise Limited Company Law («Sociedad Limitada de Nueva Empresa») came into force.

In 1996 new Regulations for the Commercial Register («Registro Mercantil») were approved.

Lastly, Law 19 of 2005 is the Spanish regulation governing the European Limited Company domiciled in Spain in compliance with Council Regulation number 2157/2001 of 8th October 2001 which approved the Statute of the European Limited Company, which imposes on member States the obligation to adopt any necessary measures to ensure the effectiveness of directly applicable rules contained in it.

There are three main types of company:

IV.1.1 Companies with a Share Capital

IV.1.1.1 *Public Limited Company («Sociedad Anónima» or «S.A.»)*

This is the most common form of company, used for investments in major projects. Their main characteristics are:

1. The capital of an S.A. is divided into shares. Each share gives its holder the right to vote, priority subscription rights, participation in the distribution of the company's profits, the right to vote on company agreements and to information. Shares may be registered in the name of the holder or bearer. Restrictions on the transfer of shares exist only in respect of the former and whilst shares are not fully paid, they have to be registered in the name of the holder. The issue of non-voting shares is also allowed; such shares are entitled to receive the annual minimum dividends, whether fixed or variable, as established by the company's Articles of Association.
2. The liability of the shareholders is limited to the nominal value of the issued shares. In the case of companies with a sole shareholder, who

does not declare this fact in the prescribed manner, the sole shareholder has unlimited liability for the corporate debts incurred during this period.

3. Only one shareholder is needed in order to set up an S.A. The minimum share capital is 60,101.21 euros, which has to be fully issued and paid in up to at least a quarter of the nominal value of each share. The remaining capital must be paid in within the period established in the company's articles or within the period agreed by the Board of Directors of the company if the articles are silent on this point. If the remaining capital is to be paid up by way of non-cash investments, the maximum period allowed is five years.
4. Incorporation requires a notarial certificate, which has to be recorded in the Commercial Register in order to create a legal entity. In the case of companies with a sole shareholder, this fact has to be specifically stated in the certificate.
5. Each company must have a Board of Directors («Consejo de Administración»), and must hold a Shareholders' General Meeting («Junta General de Accionistas»). The shareholders have ultimate control; General Meeting decisions are taken by majority. A meeting must be held within the first six months of the financial year to review the management's conduct of the business, approve the financial statements of the previous financial year and decide upon the distribution of profits. The Board of Directors may call a General Meeting whenever they consider it convenient, or when requested by shareholders representing at least 5% of the share capital.

Directors represent the company and may number one or more directors, who acting together form the Board of Directors. The Board of Directors may be held responsible if it does not act with due diligence, loyalty, fidelity and confidentiality.

We must refer here to the so-called European Limited Company «Societas Europaea», which is a new type of supranational company to add to the list of those recognised in the various Community legal systems.

The legal framework of the European Limited Company is fundamentally to extend freedom of establishment within the territory of the European Union enabling companies to operate within the community under the same rules of community Law and directly applicable in all member States, the member States being bound to adopt such measures as may be necessary to ensure the effectiveness of directly applicable community rules.

The model of the European Limited Company is in principle aimed at large investments with a minimum called-up capital of 120,000 euros but without preventing access by medium or even small enterprises.

In summary, the European Limited Company will permit companies incorporated in different member States to merge, form a holding company or a common subsidiary thus avoiding the legal obligations and practices arising under different legal systems and to organise the participation of employees in the European company, recognising their contribution and role in the company.

IV.1.1.2 Private Limited Liability Company («Sociedad de Responsabilidad Limitada» or «S.L.»)

This is the most convenient legal form for a small or medium sized business.

The minimum share capital is 3,005.06 euros, which has to be fully subscribed and paid-up at the moment when it is set-up. There is no maximum limit on the amount of share capital.

Only one shareholder is needed for its incorporation, but there is no limit on the number of shareholders.

A new form of company has been created of this type: the «New Enterprise Limited Company», whose aim is to promote the creation of small and medium sized businesses. It simplifies and makes procedures, accounting and corporate governance more flexible, as well as incorporating electronic and on-line techniques. The minimum share capital is 3,012.00 euros and it cannot exceed 120,202.00 euros. There can be a maximum of five shareholders at the time of the formation of the company and only individuals can be shareholders.

IV.1.1.3 Employee owned companies

Apart from the option open to any company to distribute its shares amongst its employees, there are two kinds of companies whose share capital is owned by its employees: Co-operatives («Cooperativas») and Labour Corporations («Sociedades Laborales»).

IV.1.2 Partnerships

Their main characteristics are the personal and unlimited liability of each partner and the fact that a partnership may not be offered to third parties without the agreement of all partners. The so-called «Regular General Partnership» («Sociedad Regular Colectiva») is a partnership of this type.

IV.1.3. Mixed companies: Limited Liability Partnership (Sociedad en Comandita)

This is a «mixed» form of company, which incorporates certain aspects of partnerships and of «share capital» companies. Two kinds of partners co-exist in it: those personally responsible, with unlimited liability, and the limited liability partners, whose liability is limited to their interest in the company.

IV.2 FORMATION OF BRANCHES

Non-resident entities in Spain may carry out transactions through a branch.

A branch is an organisation depending on its head office situated abroad. This organisation is not a legal entity of its own and is submitted to the legislation in force of the country of origin when referring to its relations with third parties.

As far as the legal regime for such investments is concerned, you are referred to what is set out in the chapter on «Foreign Investments».

A branch has to be set up through a public deed and entered in the Commercial Register. It has to operate within its «declared objects» i.e. the purposes for which the branch has been set up. Furthermore, it has to submit an annual report on the development of the investment to the General Directorate of Trade and Investment. The branch must also have a permanent address and a fiscal representative resident in Spain.

Generally speaking, the requirements, procedural formalities, accounting and initial costs for a branch are very similar to those for the constitution of a subsidiary.

The tax position of a branch is the same as for a Spanish company (see «taxation» chapter) and it has the same rights and duties, with the following differences:

- The parent company may invoice the branch for specific costs incurred in respect of the branch (cost of management, general administration and of management support). These costs are deductible from the branch's income.
- There is a tax on non-resident companies with permanent establishment (Branch Profits Tax) which taxes the income earned by the establishment that is transferred abroad at an additional rate of 18%.

This latter tax does not apply, by virtue of the non-discrimination clause in the model O.E.C.D. Treaty, to those countries with which Spain has signed Double Tax Treaties on Income and Wealth, subject to reciprocity. The treaty with the United States is an exception, as the

possibility of the introduction of this tax is specifically allowed for. The tax does not apply to companies resident in an EU member state.

IV.3 PROCEDURES FOR THE ESTABLISHMENT OF A COMPANY

- Certificate issued by the Central Commercial Register, confirming that there is no other company with a name identical to the one intended to be used.
- Prior declaration of the projected investment to the General Directorate of Trade and Investment, for those cases where this is necessary by virtue of the legislation on direct investment (see INVESTING IN SPAIN).
- Execution of a notarised public incorporation deed.
- Declaration of the foreign investment to the General Directorate mentioned above within one month of the execution of the notarised public incorporation deed.
- Registration with the appropriate tax office of its fiscal domicile to obtain a tax code number (NIF). In the case of a company with non-resident shareholders and/or representatives, non-resident individuals must obtain a foreigner's identification number (NIE) and non-resident companies must obtain a tax code number (NIF).
- Payment of the company «constitution tax» (1% of the share capital).
- Inscription in the Commercial Register.
- Payment of the relevant municipal taxes.
- Compliance with labour formalities.

IV.4 STATUTORY BOOKS

Companies must keep the following books:

1. Minute Book, to record the minutes of general meetings of the company and of the Board of Directors.
2. Register of Members, which is obligatory for private limited liability companies and in which must be shown the names of the first shareholders and details of subsequent transfers of shares together with a note of any rights of others over the shares and of any charges secured on them. This book is also compulsory for public limited companies where shares are registered in the name of the holder. Companies that

fall into the category of New Enterprise Limited Company are not obliged to keep this book.

3. Register of registered shares, which is equivalent to the Register of Members, but is for public limited companies whose shares are registered.
4. Register of contracts between the company and its shareholder where the company only has one shareholder.

The statutory books of a company have to be «legalised» (i.e. stamped) at the Commercial Register.

IV.5 LEGAL, ACCOUNTING AND AUDIT REQUIREMENTS

As previously mentioned, Spanish legislation has been subject to major changes in order to comply with the directives of the EU. The main points relating to legal, accounting and audit requirements are discussed below.

IV.5.1. Legal requirements

All companies have to be inscribed in a public register, the Commercial Register. Inscription is optional for the individual entrepreneur, with the exception of ship owners.

The legal approval required for the books of companies and individual entrepreneurs, and the deposit and publication of accounting documents are carried out via the Commercial Register.

The Register is public. The contents of registered documents can be made available in various ways:

- By a certificate issued by the Registrar.
- By an informative memorandum.
- Copies of the entries made or of the documents deposited.

The issue of a certificate is the only irrefutable way of proving the contents of documents held in the Commercial Register. Companies and individual entrepreneurs are obliged to state their inscription data on their invoices, letters, etc.

IV.5.2. Accounting requirements

The application of the International Accounting Standards (IAS) and the International Financial Reporting Standards (IFRS) became compulsory on

the 1st January 2005 in the preparation of consolidated annual group accounts where any of the group companies have issued listed securities in any member State of the EU. These rules may be applied voluntarily by other companies.

Spanish commercial accounting rules are in process of being fully reformed so as to incorporate the text of the IAS and IFRS. Furthermore, it is expected that during 2007 a new General Accounting Plan will be approved implementing the commercial accounting rules after the reform, which will be based on the new valuation principles of the international rules. In summary, Spanish accounting rules follow the model of the Fourth and Seventh Directives which, in turn, are leading – notwithstanding the obligatory political debate – towards a model of global accounting principles the main outlines of which have been set out by the IASB in London.

All entrepreneurs, individuals as well as companies, must keep accounting records, which allow their transactions to be followed in chronological order as well as the periodical listing and valuation of inventories and preparation of Balance Sheets.

They must keep two books: a book recording trial balances and the annual accounts and a journal.

Accounting records have to be «legalised» within a four month period from the end of the financial year by means of one of two procedures: legalisation prior to the utilization of bound books or legalisation after their utilization. In the latter case, if the accounting is done by computer, it can be legalised at the Commercial Register in one of the following ways: printed in paper and bound, on software or on-line.

Accounting records and supporting documentation must be retained for a period of six years from the date of the last entry in them.

Annual accounts, including a balance sheet, profit and loss account and notes, must be produced by a company within a maximum of three months from the end of its financial year.

Annual accounts together with the directors' report must be deposited with the Commercial Register during the month following their approval by the General Meeting.

Annual accounts have to be prepared in accordance with the following principles, which follow the Fourth Directive of the EU:

- Prudence
- Going concern
- Proper and immediate recording of transactions
- Assets to be accounted for at purchase price

- Accruals
- Matching of income and expenses
- Prohibition of netting off of amounts
- Consistency
- Materiality

Finally, it should be pointed out that the «General Spanish Accounting Plan», applies to all businesses, whatever their legal, individual or corporation form.

IV.5.3. Audit requirements for the annual accounts

The audit of annual accounts consists of the review and verification of the accounting records and documents, in order to determine whether they give a true and fair view of the enterprise's assets and of its financial position.

Individuals or firms which audit annual accounts must be appointed for an initial period, which cannot be less than three years or more than nine, starting from the beginning of the first audited accounting period. After this initial period they can be re-elected indefinitely.

Auditors are liable for damages arising from breach of their duties to the companies or entities audited and also to third parties.

The auditor is obliged to keep confidential information received during the performance of his duties, and may not disclose this for any purpose other than one relating to the audit.

Without prejudice to what is included in the auditor's engagement contract, the following are allowed to have access to the documents relating to audits of accounts, being subject to the obligation to keep confidential information:

- a) The Institute of Accountancy and Audit («Instituto de Contabilidad y Auditoría de Cuentas») for regulatory purposes only.
- b) Persons appointed by a judge.
- c) Those persons authorised by law.
- d) The Bank of Spain, the National Stock Market Committee, the Directorate General of Insurance and Pension Funds and the Audit Commission.
- e) The corporations representing auditors for the sole purpose of monitoring the audit work of their members.

The Institute of Accountancy and Audit is responsible for the control and discipline of auditing; the Official Register of Auditors («Registro Oficial de Auditores de Cuentas») is also under its control.

Accounts of the following enterprises are subject to audit, whatever their legal form:

- a) Those listed on any of the official stock exchanges.
- b) Those that issue debentures or loan stock to the public.
- c) Those that act as financial intermediaries.
- d) Those whose business includes any sort of insurance.
- e) Those receiving subsidies, assistance or which carry out works, provide services or supply goods to the State and other public entities.

In addition, the annual accounts and the management report of enterprises, including partnerships, have to be reviewed by auditors. Companies that are permitted to issue an abbreviated balance sheet are exempt from this requirement. Such companies are those in which for two consecutive years the accounts comply with at least two of the following criteria:

1. Total assets not exceeding 2,373,997.81 euros at the balance sheet date.
2. Annual turnover less than 4,747,995.62 euros.
3. Average number of workers employed during the financial year not exceeding 50.

Auditors have a period of at least one month to issue their report from the date on which signed accounts are supplied to them by the officers of a company.

The important role of auditors in financial and legal transactions such as mergers, divisions, share issue, capital increase by the conversion of debt, capital reductions to compensate for losses, share valuations, etc. is clearly outlined in the Company Audit Law.

V. TAXATION

V.1 GENERAL STRUCTURE

Direct taxes:

- On the income of residents
 - Tax on corporations' (companies') income
 - Personal income tax
- On the income of non-residents
- On capital (affecting individuals only)
 - Tax on net wealth
 - Inheritance and gift tax
- Local taxes

Indirect taxes:

- Value added tax (VAT, «I.V.A.»)
- Tax on capital transfers and legal documents
- Taxes on international trade: customs duties
- Special Taxes on certain consumable items (hydrocarbon, alcohol, etc.)

V.2 CORPORATION TAX

V.2.1 Introduction: basic aspects

Corporation Tax is applied throughout the whole of Spain without prejudice to special regimes for individual areas and to International Treaties and Conventions.

The event giving rise to a liability to tax is the obtaining by the taxpayer of income whatever its source or origin.

The tax is payable by ENTITIES RESIDENT in Spain.

Entities that fulfil any of the following conditions are considered to be resident in Spain:

- a) Those that have been established in accordance with Spanish law,
- b) Those that have their registered office in Spanish territory,
- c) Those whose management and head-office are located in Spain.

The tax Administration may presume that companies based in tax havens or nil tax territories are resident in Spain when their main assets consist of property situated or rights which are fulfilled or exercised in Spain or when their main activity is carried on in Spain.

Resident entities are liable to tax on the total income and capital gains made irrespective of the place where they were obtained and of the taxpayer's residence.

In order to prevent companies from deferring the payment of corporation tax by using non-resident companies taxed at a low rate abroad, companies resident in Spain under certain circumstances have to include in their own taxable profit, profits earned by a non-resident entity of which the resident company owns 50% or more. The intention is to tax foreign investment that is made for tax reasons rather than business purposes.

The tax base is the amount of revenue obtained in the tax period, which is the accounting year of the company, reduced by losses in previous years. The tax base comprises the accounting profit corrected, as appropriate, by the application of the tax rules. Tax will be paid by applying to the tax base the general rate of 32.5% for tax periods commencing from the 1 January 2007 and 30% for subsequent periods.

Small companies – whose annual net turnover is less than 8 million euros – are taxed at 25% on profits between 0 and 120,202.41 euros and at the general rate of 30% on the remainder.

If losses are made they can be carried forward for the 15 years following the period in which the losses arose; the company can decide how much of the losses it uses in any given period. For new companies the period of 15 years in which to use losses starts from the first period in which it makes a profit.

V.2.2 Temporal allocation of income and expenses

Income and expenses are allocated to the taxation period in which they accrue, taking account of the real flow of goods and services from which they are derived, irrespective of the period in which the cash or other financial flow takes place having regard to the correlation between them.

In exceptional cases, provided that it can be justified and that the Authorities agree to it, other allocation criteria may be used.

V.2.3 Computation of income and expenses

Income and expenses are computed by using accounting figures, provided that the accounts give a true view of the company's financial position. However, in the case of transactions between connected individuals or entities, there are certain precautions: thus, such transactions must be valued at their normal market value. The tax administration has power to check that transactions between connected persons or companies have been valued at their normal market value and to make appropriate corrections to the values taking into account all the persons or companies who have carried out the transaction so as to avoid taxing revenue higher than that actually derived from the transaction for the persons or companies who have carried it out. The valuation of the transaction must be supported by suitable documentary evidence.

Additionally, deduction of expenses for services between connected companies is subject to the services producing a benefit or advantage to the recipient. As regards the deduction of expenses under a cost distribution agreement signed by connected parties, the participants must have regard to the ownership or other similar right over the subject matter of the agreement so that the sharing of costs must be on the basis of the advantages or benefits anticipated for each of them.

It is possible to submit to the Tax Authorities a proposal on the values to be considered in transactions between connected entities before they take place.

For connected entities there is an «under-capitalisation» rule that applies to cases where the level of interest bearing debt owed to a connected non-resident entity (e.g. from a parent company to a subsidiary) is over three times the shareholders' funds (excluding current year profits or losses) of the Spanish entity. In such cases the interest payable on the excess of loans over the three times figure mentioned above is treated as a dividend with all the consequent tax effects. It is possible to suggest a different multiplier to the Tax Authorities for their approval.

The «under-capitalisation» rule is not applicable when the connected entity is not resident in Spain but is resident in another member State of the EU.

The legislation tries to prevent the usage by two entities belonging to the same multinational group of prices (i.e. transfer pricing) differing from market prices.

The net value of an asset for accounts purposes is deemed to be its cost of acquisition less accumulated depreciation and provisions against it.

V.2.4 Depreciation

Depreciation has to comply with two basic requirements: to be effective (i.e. necessary) and to be entered in the books.

The necessity of the depreciation has to be demonstrated by the taxpayer. To avoid difficulties, depreciation is considered to be demonstrated when provision is made according to one of the following methods:

- a) Method of straight-line depreciation according to official rates:

Tables of depreciation rates, included as an appendix to Royal Decree 1777 of the 30th June 2004, give maximum rates and maximum period of time, to be chosen at the option of the taxable entity. There is a minimum «straight line» rate of depreciation that is necessary to cover the value of the asset to be depreciated in the maximum period of depreciation allowed. Some examples are set out below:

	MAXIMUM RATE	MINIMUM RATE	MAXIMUM PERIOD
Industrial buildings	3	1.47	68
Commercial buildings	2	1.00	100
Office furniture	10	5.00	20

However, where productive assets are used in more than one normal working shift or are second hand an increase in the rate is applied.

- b) Reducing balance depreciation

Buildings, furniture and fittings cannot be depreciated in this way. There are two methods of calculating the amount of depreciations: a constant percentage of the brought forward net value or the so-called sum-of-the-digits method.

- c) Other depreciation systems

Those companies which for technical and economic reasons wish to depreciate their assets at rates different to those fixed by the official

tables, and which also wish to avoid the uncertainties involved in proving «effective» depreciation, may seek prior approval from the tax authorities for special depreciation programmes.

d) Free depreciation

The following amongst others, are entitled to free depreciation:

- Tangible and intangible assets (except buildings) used for research and development activities (R&D). Buildings, related to R&D Activities, will be depreciated in equal parts in a period of 10 years.
- Research and development costs that have been accounted for as intangible assets.

e) Depreciation of financial goodwill:

A tax deduction over 20 years is possible to depreciate financial goodwill provided that certain requirements are met, basically that it was declared when shares in non-resident entities were acquired for valuable consideration.

V.2.5 Provisions

Provisions are considered deductible when they are properly recorded in the accounts and comply with tax legislation. Deductible provisions include, amongst others, the following:

- Provisions for bad and doubtful debts
- Provisions against the value of portfolios of investment
- Provisions for extraordinary repairs but only for certain sectors of industry or with the prior agreement of a proposal by the tax authorities
- Provisions for various legal obligations and duties
- Provisions for the depreciation of capitalised editorial costs for recording and audio-visual businesses
- Provisions for the costs of inspection and repairs under warranties and for costs relating to returns of goods.

V.2.6 Deductions on the reinvestment of excess profits

Profits made on the disposal of both tangible and intangible fixed assets used for economic activity and of investments, provided that they have been owned for at least one year and amount to at least 5% of the capital of the company concerned, will have a tax deduction of 12% of the total tax liability;

as a transitional measure for 2007, the deduction will be 14.5% provided the proceeds of the sale are reinvested within the permitted period and in the type of assets established by law. The assets in which the reinvestment has been made must remain within the property of the taxpayer for five years or for three if it is a moveable asset, unless its economic life is inferior.

This deduction will not apply if the assets in which the reinvestment has been made are transferred before this period.

V.2.7. Tax incentives for small companies

A special tax regime with incentives exists for small companies («PYMES, Pequeñas y Medianas Empresas»), defined as all those whose net turnover is less than 8 million euros annually in the immediately previous taxable period.

The incentives, apart from the lower rate tax band of 25% for the first 120,202.41 euros and 30% on the remainder, are:

1. Free depreciation provided it is accompanied by the creation of employment or is in respect of tangible fixed assets whose individual value does not exceed 601.01 euros up to a limit of 12,020.24 euros per tax period.
2. Accelerated depreciation, multiplying by 2 the maximum straight-line percentage allowed by the official tables of depreciation rates.
3. An increase in the provision for doubtful debts of up to 1% of the total debtor balances at the balance sheet date.
4. The assets in which is reinvested the whole amount derived from the disposal of tangible fixed assets can be written down promptly, by multiplying the maximum rate allowed by the official tables by 3.
5. Deduction for the promotion of information and communication technologies will, for the financial years 2007 to 2010 respectively be 12%, 9%, 6% and 3% of the amount of the investments and expenses for the period relating to those activities. As can be seen, the percentage deduction has been progressively reduced so that it will disappear completely in 2011 as a way of offsetting the reduction in corporation tax rates.

V.2.8 Tax regime for entities holding foreign securities («Holding companies»)

Companies whose main object is the management and administration of investments in non-resident entities by the corresponding organisation of material and human resources, can opt for the Foreign Securities Holding Companies Regime.

The shares representing the capital of the holding company must be registered.

The main benefit of this regime is that the profit distributed by the holding company to a non-resident, even if resident in a non-EU member state, is not considered as generated in Spain, provided it is distributed from exempt income, that is to say, dividends from non-resident entities and revenue arising from the transfer of shares in a non-resident entity meeting the following requirements:

- The percentage shareholding, whether direct or indirect, is at least 5% and has been owned uninterrupted for at least one year.

The minimum shareholding requirement is deemed to be met if its acquisition value exceeds 6 million euros.

- The non-resident entity in question is subject to a tax identical or similar to Spanish Corporation Tax and is not resident in a tax haven.
- The non-resident entities from which the dividends or the revenue arising from the transfer of a shareholding are paid carry on trading activities abroad.

No previous approval from the Tax Authorities is required to benefit from this regime. Entities opting for this regime need only notify the Ministry of Economy and Finance.

V.2.9 Tax credits for 2007

- a) Relief for double taxation within Spain: dividends and capital gains

Double taxation arises when the income of a company, included in its taxable income and later distributed as dividends, suffers Corporation Tax in the first company (payer) and in turn the company receiving the dividends includes the dividends as income in its taxable income. To avoid double taxation, certain companies are allowed a general deduction of 50% of the income deriving from such dividends. In other cases, this deduction may be extended up to 100%.

Similarly when a taxable profit is made on the sale of an interest in another resident company then, provided certain conditions as to the size of the interest are met, relief is available to the vendor company to prevent double taxation of profits within Spain since the taxable profit will include the value of the undistributed profits made by the other company whilst the interest in its shares was held and these undistributed profits will have already been taxed.

b) Relief for international double taxation

This deduction attempts to avoid both «legal» and «economic» double taxation. «Legal» double taxation is defined as the same taxpayer being taxed in two countries on the same income. «Economic» double taxation is defined as a source of income being taxed in two countries on two different taxpayers.

1. Deduction for taxes paid abroad: «legal» double taxation.

Corporation tax legislation allows the deduction of the lower of the following amounts:

- Tax of a similar nature paid abroad.
- Tax that would be payable in Spain if the income were obtained in this country.

2. Deduction in respect of income earned through permanent establishments abroad: «legal» double taxation.

Income obtained from permanent establishments abroad is tax free in Spain, provided the permanent establishment's income is subject to a tax similar to corporation tax, is not exempt from tax, is derived from business activities and is not located in a tax haven.

3. Deduction for dividends and shares of profits or capital gains: «economic» double taxation.

3.1 Imputation Method

A resident company receiving the dividends may deduct the tax actually paid by the non-resident company on such dividends. Also treated as tax actually paid is that paid by companies in which the subsidiary has a shareholding and by those in which, in turn, the former have direct shareholdings, and so on, so far as it can be imputed to the profits from which dividends are paid. This relief has a joint limit with that described at the beginning of this section: the sum of both may not exceed the amount that would have to be paid, if the income had been obtained in Spain.

3.2 Exemption method

In some cases, dividends and capital gains from abroad are exempt from Corporation Tax. This is the so-called «exemption method» and is an alternative method to that in 3.1 above.

c) As has been stated, deductions to encourage the carrying out of particular activities have been progressively reduced and will eventually disappear completely, the reason being the reduction already approved for 2007 of the Corporation Tax rates. We would refer in particular to the following deductions:

- Deduction for research, development and technological innovation of 9% – 64%, the exact percentage depending on various factors. From 2008 the above percentages will be between 8% and 59% and will disappear in 2012.
- Deduction for export activities: the deduction percentage for 2007 to 2010 will be 12%, 9%, 6% and 3% respectively, disappearing in 2011.
- Deduction for investments in connection with World and Spanish Heritage: 14%; film production: 5% – 18%; book publication: 5%. These deductions will be progressively reduced until they completely disappear in 2014.
- For the investments mentioned below the deduction percentage for 2007 to 2010 will be 8%, 6%, 4%, and 2% respectively, disappearing in 2011:
 - investments in material assets intended for environmental protection
 - company contributions to employment pension plans or mutual social security schemes
 - investments in vehicle satellite navigation and tracking systems
 - investments in public transport vehicle access systems for disabled people
- Deduction for vocational training costs: 4% – 8% for 2007 which will be progressively reduced until it disappears in 2011.
- Deduction for the creation of employment for disabled persons: 6,000.00 euros per person per year for the increase in the average number of disabled persons employed.

The deductions described above may not exceed the percentage of the total tax liability fixed by prevailing legislation for each case, which is normally 35% but which can reach 50%.

Future annual budgets may introduce other tax incentives to encourage investments.

V.2.10 Withholding tax and pre-payments of tax

Some types of income receivable by entities liable to corporation tax are subject to a withholding tax that is a payment on account of corporation tax. The normal percentage withheld is 18%, but it can vary depending on the type of income.

In addition, during the first twenty days of the months of April, October and December, companies have to make a payment on account of corporation tax payable for the current financial year. Each payment is of 18% of the total figure for the previous financial year, after deducting any withholding tax suffered and any other allowable deductions.

Alternatively there is an option to make payments on account based on the taxable income of the first three, nine or eleven months of each calendar year. The payment on account is at 5/7ths of the tax rate, rounded down. This method is obligatory for entities with a turnover in excess of 6,010,121.04 euros during the twelve months preceding the date at which the tax period begins.

Withholding taxes and payments on account of taxes may be deducted from the corporation tax for the corresponding year and, if they exceed the final amount payable, the company has the right to ask for a repayment of any excess payments.

V.2.11 Consolidated tax return

When a company resident in Spain owns during the relevant period directly or indirectly 75% or more of the capital, and exercises control over another company or over other companies that are also resident, the whole group may present one tax return, (with the prior approval of the Tax Authorities).

V.3 PERSONAL INCOME TAX

V.3.1 Introduction: basic aspects

Tax on the income of individuals, like Corporation Tax, applies throughout Spanish territory without prejudice to special local regimes and to international agreements and treaties.

Tax liability arises on the obtaining of income by the taxpayer.

INDIVIDUALS HABITUALLY RESIDENT in Spanish territory are liable to this tax.

A stay of more than 183 days of the year on Spanish territory is deemed to be habitual residence. For the calculation of the numbers of days occasional absences are counted, except when fiscal residence in another country is proved.

In addition it is assumed that a taxable individual has habitual residence in Spain when the main centre of his or her business or economic interests is situated in Spain.

Habitual residence is presumed, unless there is proof to the contrary, when an individual's spouse and minor children habitually reside in Spain.

Individuals with Spanish nationality who transfer their residence to a tax haven remain liable to pay this tax in the year in which they move and for the next four years.

Employees transferred to Spain who acquire tax residence in Spain as a result of such transfer may opt to pay Non-Resident Income Tax for the period in which the change of residence occurs and the five following periods when the following conditions are met:

- they have not been resident in Spain for the 10 years prior to their new transfer
- the transfer has occurred as a result of an employment contract
- the work is actually done in Spain
- the work is done for a company resident in Spain
- the income from the employment is not exempt from Non-Resident Income Tax

A taxpayer opting for this special regime will be subject as a non-resident to Wealth Tax.

Taxpayers are taxable on the whole of the net income and capital gains obtained, irrespective of the place where they arise and the residence of the payer.

The tax is on the income of the taxpayer and the law prescribes a personal and family minimum which must be taken into account when calculating the total tax liability.

As for Corporation Tax, resident individuals have to include in their taxable income, income received from non-resident entities in which they own an interest of at least 50% and comply with certain rules.

Families may opt either for joint taxation or for separate taxation for each of their members.

V.3.2 Tax allowances for 2007

The following may be mentioned, amongst others:

- a) Deduction for the cost of acquiring or restoring the taxpayer's habitual residence: 15% . The maximum base of this allowance is 9,015.00 euros per annum.
- b) Deduction for business activities: taxpayers who are in business are eligible for the incentives and aids to investment available under

Corporation Tax rules, except deductions for reinvestments of excess profit.

- c) Deductions for donations: donations made to certain bodies give rise to an Income Tax deduction.
- d) Income obtained in Ceuta and Melilla: 50% of the amount of tax corresponding to such income.
- e) Investments and expenditure connected with World and Spanish Heritage: 15%.

The basis of calculation of the allowances set out in c) and e) above is limited to 10% each of the tax base.

- g) Deduction for international double taxation: if a tax similar to Spanish Income Tax has been paid abroad on earnings or capital gains received abroad then a deduction from Spanish tax is available at the lower of the following amounts:
 - the actual amount paid abroad
 - the amount arising from applying the average rate of charge to the tax base charged abroad.

V.3.3 Tax rates for the financial year 2007

Personal Income Tax covers two kinds of income: general income and savings income. Savings income comprises, amongst other things, dividends, interest (except interest obtained from connected persons or companies) and capital gains irrespective of the period when such gain arose.

Savings income is taxed at the fixed rate of 18%.

General income is taxed according to the following scale of charge:

Taxable income up to euros	Total payable in euros	Rest of taxable income up to euros	Rate applicable %
0	0	17,360.00	24.00
17,360.00	4,166.40	15,000.00	28.00
32,360.00	8,366.00	20,000.00	37.00
52,360.00	15,766.40	remainder	43.00

V.3.4 Withholding Taxes

Companies, non-residents operating in Spain through a permanent establishment, entrepreneurs and professionals who are in business must deduct and pay to the Revenue authorities as a payment on account the following amounts when receiving occupational income, unearned income or income from professional activities:

- Occupational income: depends on the amount involved and other circumstances.
- Income derived from giving courses, lectures: 15%.
- Unearned income (dividends, interest etc): 18%.
- Income from professional work: 15%, except in the first year of practice and in the two following years: 7%.
- Payment to Members of the Board of Directors: 35%.
- Prizes received as a result of taking part in games, competitions etc: 18%.
- Income from letting property: 18%.
- Income from intellectual or industrial property, technical assistance and leasing of movable property: 18%.

Where some of the income mentioned above is not paid in cash but in kind, there is still a requirement to make a payment on account.

Non-residents without a permanent establishment basically have to withhold tax on income for work done.

V.4 NON-RESIDENT INCOME TAX

Non-resident Income Tax is payable on income obtained in Spain by individuals and entities which are not resident in Spain. The tax distinguishes between:

V.4.1 Income obtained by means of a permanent establishment

The taxable income of a company's permanent establishment is computed according to the normal rules of Corporation Tax with the following peculiarities:

- Payments made to its parent company or any other of its permanent establishments of royalties, interest, commission, for technical assistance or for the use of any assets or rights are not deductible.

- Management and general administration costs payable in respect of the permanent establishment are deductible provided that they are reasonable and consistently applied and shown in the Annual Report and Accounts.

Taxable income is charged at the general Corporation Tax rate of 32.5% for tax periods commencing from the 1st January 2007 and 30% for subsequent periods.

The foreign entities' permanent establishments are subject to the same formal registry and accounting obligations as entities resident in Spain.

The most striking feature of the use of a permanent establishment to operate in Spain is the fact that profits may be transferred abroad. However, as already mentioned, (see FORMATION OF BRANCHES) an additional 18% is payable on the transferred income (except where there is a Double Taxation Treaty, other than the Treaty with the United States, or when the non-resident entity is resident in a member state of the EU), without having to prove payment of Corporation Tax before the income is transferred.

Special rules are used to compute the taxable income of permanent establishments in the following cases:

- a) Establishments having occasional or intermittent business activities: construction, installation or assembly contracts lasting more than 6 months, seasonal businesses or prospecting for natural resources.

The rules for profits earned in Spain without permanent establishment are applied and they are exempt from the normal accounting and registration requirements but must keep supporting documents for their income and expenses and, if applicable, for any tax paid, withholding tax deducted and prepayments made. The rate of tax in these cases is 24%.

Such businesses may, if they so choose, be taxed on the same basis as permanent establishments at the general Corporation Tax rate. This is only possible if the business in question maintains separate accounting records for revenue obtained in Spain.

- b) Establishments with an incomplete business cycle:

These include businesses that have premises where work is carried out in Spain, but use the goods produced or services performed therein for their own purposes. Consequently they do not receive income but simply reimbursements of costs incurred. The taxable income of such entities can be arrived at by applying the percentage determined by the Ministry of Economy and Finance to the costs incurred by the entity during the accounting year and other income such as interest or royalties and capital gains or losses have to be added to this figure. The

resulting figure is taxed at the general Corporation Tax rate, the reliefs and allowances available under the usual rules not being applicable in this case.

V.4.2 Income obtained without a permanent establishment

The taxable income is the gross income amount received by the non-resident, in other words expenses and costs cannot be deducted except in the case of certain businesses (technical assistance, installation or assembly work, the provision of services, and in general economic activities in Spain) where personnel costs and the cost of materials and supplies can be deducted.

As far as capital gains are concerned the taxable amount is the difference between the value on disposal of the asset in question and its acquisition cost updated, only for immovable property, by the application of the indexation rates approved annually in the Finance Act.

Each source of income or capital gain is taxed separately.

Tax rates are as follows:

- The normal rate is 24%.
- 18% for dividends, interest and capital gains.
- Income from work by virtue of a contract of fixed duration for seasonal foreign workers: 2%.
- Payments to non-resident staff working in Spanish embassies and consulates abroad: 8%.
- Pensions: the rate depends on the level of income.
- Reinsurance operations at 1.5 %.
- Sea and air transport businesses, which are resident abroad and whose ships or planes enter Spanish territory, are taxed at 4%.
- Royalties: 10% when the recipients are EU residents and meet the other requirements prescribed by law.

Lastly, in case of the transfer of real estate located in Spain by non-resident taxpayers without a permanent establishment, the buyer will be obliged to withhold and pay into the tax office 3% of the agreed price as a payment on account of the tax payable by the former. If the payment of the tax withheld is not made, the transferred real estate will be subject to the payment of the tax.

In any event, the depository or manager of the assets or rights of non-residents without a permanent establishment, or the payer of the income

obtained without a permanent establishment, are severally liable for the payment of tax debts relating to income from the property or rights which they hold or manage or income which they have paid.

V.4.3 Exempt income

The following sources of income, amongst others, are exempt:

- a) Income and capital gains deriving from investments owned by non-resident entities which have no permanent establishment in Spain and are resident in other member states of the E.U.

This very beneficial arrangement is not available for capital gains arising from the disposal of shares or other interests in companies in the following cases:

- a') the assets of the company in question consist mainly of real estate in Spain.
- b') the year preceding the date of disposal the tax paying entity had an interest of at least 25% in the share capital or assets of the company in question.
- b) Income and capital gains obtained by non-resident entities without a permanent establishment in Spain from Spanish Government Debt.
- c) Income arising on accounts held in Spain by non-residents and paid to non-resident entities unless the payment is made to a permanent establishment located in Spain by a Spanish financial entity, like the Bank of Spain, Banks, Savings banks, etc.
- d) Income derived from securities issued in Spain by non-residents without a permanent establishment whatever the residence of the financial institutions that act as paying agents or are involved in the issue or transfer of the securities.
- e) Income derived in Spanish territories, without permanent establishment, from finance leases, disposal or transfer of containers or of an unequipped ship or plane used in international shipping or aviation services.
- f) Profits distributed by subsidiary companies resident in Spain to their parent companies resident in other EU member states, provided the conditions outlined in the current law are met.
- g) Income derived by non-residents without a permanent establishment in Spain from the transfer of securities or the repayment of units in investment funds carried out on officially recognised secondary markets for Spanish securities provided that they are resident in a country which has a Treaty with Spain containing an exchange of information clause.

- h) Dividends and shares in profits obtained without a permanent establishment by individuals resident in another member State of the European Union or in countries with which there is an effective exchange of information, with a limit of 1,500 euros, which will be applicable to all the income obtained during the calendar year.

The exemptions described under letters a), b), g) and h) are in no event applicable to income obtained from tax havens.

V.4.4 Fiscal representative

Taxable non-resident entities in Spanish territories are required in some cases, to appoint an individual or a legal entity residing in Spain to represent them before the tax authorities. The same obligation exists for persons or companies resident in countries or territories with which there is no effective exchange of tax information who own property situated or rights which are fulfilled or exercised in Spain, excluding securities negotiated in official secondary markets.

The fiscal representatives of companies operating in Spain by means of a permanent establishment are considered to be the person or legal entity named as such in the Commercial Register and, if no name is given, then those people stated as empowered to contract in the name of these establishments.

The failure to comply with this requirement is considered a punishable offence.

V.4.5 «Special» tax on real estate

Non-resident entities that are owners of or possess real estate or rights to the possession or use of it in Spain, are subject to a special tax on real estate that accrues on 31st December of each year and has to be paid during the following month of January. The tax rate at present is 3% and it is applied to the official value of the real estate. This special tax is not applicable to:

- a) Foreign States and Public Institutions and International Organisations.
- b) Entities with the right to benefit from a Double Tax Treaty which includes a clause allowing the exchange of information provided that the ultimate owners of the property are people who are either resident in Spain or entitled to benefit from a Double Tax Treaty with a clause allowing the exchange of information.
- c) Entities that carry on businesses in Spain continuously or habitually other than the simple ownership or renting of property.

- d) Companies listed in officially recognised secondary stock markets.
- e) Charitable or cultural organisations which are non-profit making and are recognised as such by the laws of a state with which Spain has a Treaty with a clause allowing the exchange of information provided that, of course, the property is used for the stated purposes of the organisation.

V.4.6 Place and time of the tax return

Normally, within a month of the accrual date of any individual, which usually coincides with the due date of its payment, a declaration for each type of operation has to be made to the Tax office of the fiscal domicile of the tax representative. Capital gains deriving from the assignment of real estate are excluded; return of such gains has to be made to the Tax office of the place where the said real estate is located.

In a general way the legislation allows the payer of income to a non-resident to make quarterly declarations covering all income paid in the previous quarter.

V.4.7 International Treaties and Agreements

Taxation of income obtained by non-resident companies in Spain may be modified by the application of International Treaties and Agreements. The treaties override Spanish internal law. If the income obtained in Spain was acquired by a company resident in a country with a Double Tax Treaty, it would be necessary to consult the text of the treaty in order to establish the correct treatment.

SUMMARY OF DOUBLE TAX TREATIES

COUNTRY	(1)	(2)	(3)	
	Dividends (General)	Dividends capital	(Parent/ Subsidiary) Withholding	Interest
	%	%	%	%
AUSTRIA	15	50	10	5
BELGIUM	15	25	—	0/10
BRAZIL	15	25	10	15/10
CANADA	15	—	15	15
DENMARK	15	—	15	10
FINLAND	15	25	10	10
FRANCE	15	10	—	10
GERMANY	15	25	10	10
ITALY	15	—	15	12
JAPAN	15	25	10	10
NETHERLANDS	15	50	10	10
NORWAY	15	25	10	10
POLONIA	15	25	5	—
PORTUGAL	15	25	10	15
RUMANIA	15	25	10	10
SWEDEN	15	50	10	15
SWITZERLAND	15	25	10	10
UNITED KINGDOM	15	10	10	12
UNITED STATES	15	25	10	10

- (1) Maximum rate of tax to be charged in the State in which the dividends arise.
- (2) Maximum rate of taxes to be charged in the State from which the dividends arise; the tax rate given in the table is appropriate where the parent company controls at least the percentage of the subsidiaries capital shown. It is important to bear in mind the incorporation into Spanish law of EU Directive 90/435/EEC on the common fiscal regime applicable to the parent companies and subsidiaries of Member States. The Directive establishes that, if its requirements are fulfilled, dividends distributed by a subsidiary to its parent company are not taxed and that the withholding tax system does not apply (see V.4.3).
- (3) Maximum rate of taxes to be levied in the State in which the interest arises. By application of the most favourable internal rules, the interest received by residents of other member states of the E.U. is exempt from taxation (see V.4.3).

V.5 WEALTH TAX

This tax is applied to the ownership of all types of assets and goods and of economic rights by an individual at 31st December every year.

Resident taxpayers have to lodge a tax return when the amount of their net wealth exceeds 108,182.18 euros, or when the value of their assets or rights is over 601,012.10 euros.

In case of individual non customary residents holding assets or rights in Spain, they have to lodge a tax return on the whole of their wealth in Spain whatever the amount.

The assets and rights of individuals are exempt if they are necessary for an individual's business or professional activity, provided the legal requirements are met.

V.6 INHERITANCE AND GIFT TAX

This tax applies to the acquisition of goods and rights by inheritance and by gift, as well as the receipt of amounts by the beneficiaries of life insurance policies, when the person paying the insurance is different from the beneficiary.

If the assets or rights are acquired by a legal entity rather than an individual, then they are subject to corporation tax and not to inheritance and gifts tax.

Taxpayers with customary residence in Spain are taxable irrespective of the place where the acquired assets or rights are situated.

Non-residents will be taxed on assets located in Spain or rights that may be exercised in Spain.

When an unincorporated business or certain shares in a company or normal dwelling place are acquired by close relations, then the taxable amount is reduced by 95%.

V.7 LOCAL TAXES

The following local or municipal taxes are worthy of special mention:

a) Council Tax (Impuesto sobre Bienes Inmuebles or IBI)

Liability to the tax derives from the ownership of real estate or from the ownership of a life interest or right of use of property and from the holding of an administrative concession. The tax payable is based on the council tax value of the property and is payable annually.

b) Tax on economic activities (IAE)

This arises on the exercise of a business, professional or artistic activity. It also accrues on an annual basis. This tax is not applicable during the first two years of the trade or if the turnover of the individuals or companies does not exceed 1,000,000.00 euros.

c) Tax on the increase in value of land

This tax is levied on the increase in value of urban land and arises as a consequence of its transfer or the constitution of any legal rights of enjoyment of it (life interest, right of use...)

V.8 VALUE ADDED TAX

Value Added Tax (IVA) is a tax on consumption in general which applies to the following: the supply of goods and services, imports and the acquisition of goods from other EU members.

The standard tax rate is 16%.

A reduced rate of 7% is applied to the supply of certain goods and services, for example:

- Certain foodstuffs
- Water
- Prescription lenses and medical goods
- Housing in general
- Medical and dental care

A «super-reduced» rate of 4% VAT is applied, amongst other things, to the following products:

- Bread, cereals, milk, cheese, eggs
- Medicines and other pharmaceutical products
- Books, newspapers and magazines

Entrepreneurs or professional people who are not established in the area of application of Spanish Value Added Tax are entitled to apply for the return of VAT provided that they are established in an EU country or in a third country subject to reciprocity. The application for reimbursement must be submitted by the 30th June of the year following that in which Spanish VAT was paid and the application may be submitted electronically. The entrepreneur or professional person will receive default interest fixed for 2007 at 6.25% if the reimbursement applied for is not obtained within six months.

V.9 TAX ON ASSET TRANSFERS AND LEGAL DOCUMENTS (STAMP DUTY)

This tax applies to «inter vivos» transfers of all classes of goods and rights, and the granting of rights and concessions as well as company transactions: the setting up of companies, increases and decreases of share capital, mergers, divisions and liquidations of companies, in certain cases transfers of domicile to Spain, and contributions made by shareholders to restore fund losses.

Transfers of real estate are taxed at a rate of 6% on the value of the real estate transferred, except where an Autonomous Community has fixed its own rate, e.g. Catalonia 7%. The transfer of movable assets are taxed at 4%.

Company transactions are taxed at the rate of 1%.

In general this tax does not apply where VAT is payable; however there are some exceptions to this rule.

This tax in its modality of legal documents is levied on stamped legal documents; it applies to notarised documents both of commercial and administrative character.

V.10 CUSTOMS DUTIES

Standard customs duties are generally payable when goods are cleared by customs. With very few exceptions, the duties are «ad valorem», i.e. calculated on the CIF value or on a similar invoice value.

As a result of Spain joining the EU from 1st January 1986, a programme of gradual decreases of the customs duties between Spain and the EU was established, resulting in their elimination on 1st January 1993. From this date, transactions between EU members are not treated as imports. What before 1993 were imports are now «intercommunitarian acquisitions of goods», which are subject to VAT when the goods are in the possession of the purchaser in the EU state of destination.

V.11 ECONOMIC AND TAX SYSTEM OF THE CANARY ISLANDS

The Canary Islands have a special tax system established in order to boost economic activity and job creation, as well as to attract entrepreneurial initiative and external investment.

The most important aspects of the tax regime are as follows:

1. Measures applicable to all of the Canary Islands:

- Tax on Asset Transfers and Stamped Legal Documents: companies tax resident in the Canary Islands and those which trade in the Canary Islands through a permanent establishment are exempt:

From a property transfer tax on the acquisition at a time of the initial investment of investment assets or intangible fixed assets (in the latter case the exemption is only up to 50%, with exceptions).

In respect of «company operations» on the incorporation of companies or increase of capital for the purpose of acquiring or importing investment assets or the acquisition or assignment of certain intangible fixed assets.

- Canary Islands General Indirect Tax: A complete exemption from this tax is available for telecommunication services provided in the Canary Islands. Also exempt is the assignment of intangible fixed assets and investment assets which the companies mentioned in the previous paragraph deliver or import which are not entitled to the full deduction of amounts paid in respect of this tax.
- Corporation Tax: a 50% reduction is granted on profits arising from the sale of goods produced in the Canary Islands.

This credit is also applicable to companies domiciled outside the Canary Islands, trading in them through permanent establishments.

Individuals subject to Personal Income Tax carrying out the above mentioned activities, fulfilling the relevant criteria, and taxed on their actual income, may also take advantage of this credit.

An «investment reserve» is available in the Canary Islands with the result that companies are entitled to deduct from their taxable income, within certain limits, the sums which, in relation to their establishments in the Canaries, they allocate from their profits to the «investment reserve».

The tax regime described above is not applicable to certain industries, shipbuilding, synthetic fibres, motor vehicles, steel making and coal.

2. Measures applicable to entities of the ZEC («Zona Especial Canaria», Special Canary Islands Zone):

The EU has extended the period of validity of the Special Canary Islands Zone until the 31st December 2019. However, so-called ZEC companies may only be registered in its Official Registry until the 31st December 2013.

The prime objectives of this special regime are the economic and social development and diversification of the economy of the Canary Islands

and to achieve this a low tax area has been created within the European Union enabling companies, amongst other benefits of a fiscal nature, to apply a reduced rate of Corporation Tax of 4%.



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