

REAL PROPERTY IN SPAIN SHOULD I BUY IN MY OWN NAME OR IN THE NAME OF A COMPANY?

Jonathan Miller¹

That which follows is a mere lollipop. At best it constitutes a swift reconnaissance - a skip from peak to peak - of the principal features of the landscape of its subject matter. The matter is serious enough, however. The volume of property purchases in Spain by UK (and other non-Spanish) residents has been huge in recent years, and shows little sign of falling back significantly.

If our own experience is any measure, the title of this article is a question frequently asked by clients about to buy land or buildings in Spain, or by their advisors on their behalf. Inevitably, there is no easy answer. A recommendation may be made, but only based on a detailed analysis of the full circumstances and both the medium-term and long-term objectives of the client. And defining those often means that the client has to address - and decide on - some difficult and subtle issues which may not even have occurred to him before.

If there is any general rule (and all general rules are more or less dangerous if applied prescriptively) it is probably that ownership should be personal unless there are compelling reasons why it should be otherwise.

In attempting to arrive at an answer to the question, probably the first issue to be addressed is that of what has motivated the client to consider that personal ownership may not be satisfactory or adequate. In short, what is the perceived problem which he is looking to solve? Often the answer will be the somewhat ill-defined one that it seems to be a good idea, and that it probably saves taxes. Whether either of those may be valid will depend on the analysis referred to above. In any event, there is rarely a single clear rationale, but rather an agglomeration of vague expectations, even amongst the most sophisticated of clients.

¹ Jonathan Miller, Managing Director, Windram Miller & Company SL, Jacinto Benavente 17 - 2A, 29600 Marbella (Málaga) Spain. (T) (+34) 95 282 0779 / 4910 (F) (+34) 95 277 8468 emails: email@windrammiller.com and wmiller@readysoft.es
website www.windrammiller.com

In this brief review, I focus entirely on companies, and not on other types of structure such as trusts and *anstalts* or *stiftungs*. In the case of these entities, the vast majority of what I say below may be applied analogously. But they also bring their own range of considerations which are outside the scope of this short paper. In any event (and for reasons for which there is not here space to discuss) it is generally advisable for a trust (and an *anstalt* or *stiftung*) to interpose a company between itself and the Spanish property.

Possible Benefits

It is usual, though not inevitable, that the company in question is assumed a priori to be an offshore² company. Whether it is to be offshore or not should really be part of the answer rather than the main premise, which latter is regrettably often the case. In any event, the client or his advisors may have considered some or all of the following (and the reader should note that inclusion of an objective in the generalised wish-list below does not suppose that it is necessarily achievable in any particular case):

- Avoidance of the Spanish equivalent of capital gains tax³ on the alienation of real property on a resale or gift.
- Avoidance of the costs, on a resale or gift, of conveyance of real property, and the associated stamp duty [ITP⁴], which together can add up to as much as 9%-11% of the value of the property.
- Simplicity of transfer on a resale or gift (stock transfer form versus legal conveyance of real property).
- Avoidance, on a re-sale, of the often under-considered “plus valia”,⁵ which

² by which I mean a company registered and resident in a tax haven.

³ For non-residents of Spain, whether individuals or companies, a flat 35% of the gain is applied.

⁴ On most real property transactions, the stamp duty rate is 6%. Where a new property is sold by a developer/constructor, VAT at (generally) 7% is charged, plus 0.5% documentary stamp duty on the deed of conveyance.

⁵ Strictly *Impuesto sobre el Incremento en el Valor de los Terrenos de Naturaleza Urbana* (Tax on the Increase in Value of Urban Land). The tax is assessed on the catastral (quasi-rateable) value of the land, at rates in the range 2% to 3.7% depending upon the population size of the municipality in which the land is sited, and the number of years since the last assessment.

is a municipally-collected tax, charged on the increase in the *catastral* value of the land underlying the property, when there is a change of title to the land. Strictly this tax is not avoided since a non-resident property owner can be charged plus *valia* every ten years, although some municipalities can be forgetful in this regard.

- Avoidance of ISD⁶ (Spain's equivalent of Inheritance Tax).
- Avoidance of the rules of *legitima* (forced heirship) in which testamentary freedom can be severely limited, even for those of non-Spanish domicile, when disposing of Spanish-sited immovable property.
- To achieve or maintain confidentiality of ownership (for the multitude of reasons for which confidentiality may be sought).
- A desire to transact a sale of the property - that is to say, of the shares of the owning company - outside the purview of Spain's investment reporting controls.
- Avoid a declaration for IP (Wealth Tax).
- Property developers have found uses for corporate structures. These may include, for example, building a land bank without alerting neighbouring potential vendors to the possibility of price escalation, by using different companies to acquire individual land-plots, and to attempt to take development gains outside Spain. In consequence, therefore, the potential purchaser of a Spanish property may be presented with a *fait accompli* corporate structure, and no access to title of the property other than by acquisition of the owning company.

Possible Problems

Many of the less-desired consequences of corporate ownership are either not entirely understood or may have been quite overlooked. They include:

- Cost of the structure. These are likely to include initially the incorporation or acquisition costs and thereafter the annual fees of directors, registered office, and nominee shareholders, activity and transaction fees, annual government duties and compliance fees. These days it is rare for those

⁶ An acquisitions tax of potentially important impact. Spouses are not exempt beneficiaries. See article in OTPR Volume 10, Issue 1, at p.43.

continuing costs to be less than £1,500 per annum, or even more in a jurisdiction where annual accounts are required.

- Issues of title. Clients often overlook the fact that a property owned by a company is, by definition, not theirs. Ownership - whether direct or beneficial - of the company does not confer ownership of the company's assets nor, per se, a right to use those assets. This oversight can lead to some surprisingly baroque problems, only one of which may be an effective frustration of the intended consequences of separation of title from the client's own name.
- Taxation. A direct effect of ownership by an offshore company is a prima facie liability to the annual 3% Special Levy. Additionally, a range of issues arises from use of the property, amongst them those which follow. Genuine rental income should be declared to Spain and 25% of the gross thereof paid in tax. Where the company permits gratuitous use of its property, a rental income is deemed to arise at market value, and again, this should be declared and 25% thereof paid to the Spanish revenue authority. It is possible to attempt to defeat this latter provision by submitting audited accounts of the company accompanied by formal declarations from the directors to prove that no rental income has in fact been received (though Spain is less than welcoming to any documentation, however formal, with origin in a tax haven). Even this contrary proof defence is statutorily barred where the matter concerns a "connected operation" i.e. where the occupant of the company's property has an interest in the company (e.g. the beneficial shareholder). Beneficial owners should always bear in mind the many provisions of Spanish law which apply or impose a form of transparency (mostly, though not always, for tax purposes) to holdings of Spanish real property via an entity (company, trust, or any analogous structure). These include a provision to tax disposals of interests, direct or indirect, in entities whose sole or main asset is real property in Spain, as if they were disposals of the underlying property itself.
- The exit. In order to attempt to achieve or crystallize some of the possible benefits listed further above, it is necessary to persuade a purchaser to buy the company and not the property directly. This is absolutely not as simple as it sounds. Any well-advised purchaser should resist most strongly such a proposal (and if he wants corporate ownership of the property, he should probably establish his own structure). If, following due diligence investigations, he decides to purchase the existing structure, he should certainly be looking for, inter alia, some extremely powerful warranties as to tax and other liabilities from both the beneficial owners and the directors.

of the target company, which they are unlikely to want to give. And even with such warranties in place, the purchaser is still assuming all the pregnant gain in the underlying property together with the risk that he, in his turn, will not be able to pass this on by eventually selling the company and not the property.

Some Cures?

By and large, none of the above “possible problems” arise from personal ownership (save, perhaps, tax on rental income from lettings). Neither, of course, do the “possible benefits” listed earlier.

Where corporate ownership of the property is in any event intended, the non-Spanish company may be positioned to seek exemption from the 3% Special Levy by establishing it in a jurisdiction with which Spain has a double tax treaty, provided that the ultimate owners thereof are also resident in such a jurisdiction. Evidently, such a solution may bring its own compliance issues (for example, tax and company law reporting requirements) or may confound some of the objectives which corporate ownership was intended to achieve.

Where it is intended that ownership shall be via an offshore company, avoidance of the 3% Special Levy and the associated compliance costs, may be achieved by the insertion into the structure of a Spanish company, subsidiary of the offshore company, as direct owner of the real property. This solution brings with it the notable additional costs of incorporating and maintaining a Spanish company, together with the absolute need to accept and deal with some of the issues listed above in “possible problems”. It is a solution quite commonly adopted for higher-value properties.

So Why Use a Company?

There are some circumstances in which the use of a non-Spanish structure may be valuable. For example:

Trusts. Spain is a Civil Code jurisdiction and so, domestically (whether in the property registry or elsewhere), is unable to distinguish equitable interests from legal title. Where a trust is already in existence, or required, it is worth considering the interposition of a non-Spanish company between trustees and any Spanish property to be acquired, in order that beneficial interests may be reflected in the shares of the owning company.

Spanish inheritance tax. Where the potential heirs to Spanish-sited real property are not residents of Spain, interposition of a non-Spanish entity can avoid or mitigate Spanish inheritance tax. Evidently, such future capital saving is at not inconsiderable current account cost including the running costs of the company and the annual taxation matters mentioned earlier.

Forced heirship. In some circumstances, the Spanish forced heirship provisions may operate to pass an interest in or title to Spanish real property to heirs (for example, children, to the disadvantage of the wife) neither intended nor wanted by the testator. Conversion of realty into personalty by way of ownership via shares of a company (or an interest therein) can avoid this in appropriate circumstances.

It should be noted that the possible benefits/uses listed immediately above inevitably carry with them at least some of the possible problems listed further above. The issue for consideration, therefore, is always that of the balance of benefit in any particular case. And that judgement in turn, requires some finely-tuned identification and analysis of the issues by both client and advisor.

The Last Word?

From all the above, it may correctly be deduced that corporate ownership of Spanish property is powerful medicine. Indeed, it has been likened to chemotherapy. It is often an uncertain cure for a serious problem, frequently painful and bringing other problems in its wake, but sometimes, the only game in town. But you do need to be sure that both diagnosis and selection of the treatment are rigorously accurate.