16 October 2020

Global Tax Alert

Spanish DST is enacted, effective 2021

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Executive summary

On 16 October 2020, the Spanish law (the Law) on Digital Services Tax (DST) was published in the Spanish *Official Gazette* after its prior approval by the Spanish Congress and Senate (See EY Global Tax Alert, *Spain sends bill on Digital Services Tax to Parliament for approval*, dated 3 March 2020).

Spain has finally approved a unilateral DST after its failure to approve the bill drafted in 2019 (See EY Global Tax Alert, *Spain sends bill on Digital Services Tax to Parliament for approval*, dated 29 January 2019).

The text of the final Law has not experienced any relevant modification from the initial text sent by the Spanish Council of Ministers to the Congress and Senate for vote on 28 February 2020. Its main features are similar to the DST initially proposed by the European Union (EU) Commission on 21 March 2018, with a rate of 3% imposed on gross income derived from certain digital services for which user participation is essential for creating value; namely, targeted online advertising, online intermediation services and the sale of user data. Only companies with worldwide revenues of at least €750 million per annum, with a total amount of taxable revenues earned in Spain exceeding €3 million per annum, would be subject to the DST.

Building a better working world

Apart from the exclusions contained in the original EU DST proposal, the following transactions are excluded from Spanish DST pursuant to the Law:

- Transactions involving only entities with 100% direct or indirect ownership or common ownership.
- Regulated financial services rendered by regulated financial entities.
- Income derived from the transfer of data by regulated financial entities.

Detailed discussion

Spanish DST within the European and international framework

In accordance with the Law's explanatory statement, the DST would be a first interim response to the challenges arising from the new global economy development.

The Spanish Government has acknowledged that the ideal approach to address these tax challenges would be to find a multilateral, international solution within the Organisation for Economic Co-operation and Development (OECD).

Nevertheless, the Spanish Government also notes that, since the adoption and implementation of practical measures are taking a long time, the adoption of a unilateral interim measure is needed to address this problem.

As per the above, the temporary nature of the DST is two-fold, as follows:

- The Government has committed to adapt the DST to the solution adopted by the EU as soon as it becomes available.
- The Law's preamble states that the Spanish DST is conceived as a temporary transitional measure which will apply until the Spanish rules implementing the internationally-agreed solutions enter into force.

The Government's view is that since the DST is focused on the services rendered, irrespective of the providers' features (among others, their economic capacity), it should not be considered as a tax on income or wealth and, therefore, falls outside the scope of the double tax treaties entered into by Spain.

The above is the key reason why the tax would be implemented as an indirect tax, in accordance with Article 1 of the Law, as in the original European Commission's proposal.[1] Additionally, the Government considers that the DST would be compatible with the Value Added Tax (VAT), harmonized throughout the EU.

Spanish DST's main features

The Spanish DST will apply to services where the participation of a user in a digital activity constitutes input for the business and that enables that business to obtain revenues therefrom.

In particular, the tax is imposed on the provision of the following digital services:

(i) The placing on a digital interface[2] of advertising targeted at users of that interface (*online advertising services*).

(ii) The Law expressly defines the notion of "targeted advertising" as any form of digital commercial communication, the purpose of which is to promote a product, service or brand, which is directed to users of a digital interface based on the data collected from them.

(iii) The Law also includes a presumption that all advertising will be considered as "targeted advertising," unless proved otherwise.

(iv) Services consisting of making available multi-sided digital interfaces to users which allow them to find other users and to interact with, and which may also facilitate the provision of underlying supplies of goods or services directly among users (*online intermediation services*).

(v) The transmission of data collected about users which has been generated from such users' activities on digital interfaces (*data transfer services*).

Activities that are not subject to taxation in general match the ones outlined in the European Commission's proposal and include:

- Online sales of goods or services through the website of their supplier, in which the supplier does not act as an intermediary (e-commerce related to retail activities), are excluded. In such cases, the value creation for the retailer lies with the goods or services provided and the digital interface is simply used as a means of communication.
- The Law expressly excludes from its scope the sale of goods or services between end users within an online intermediation service (i.e., the underlying transaction, for example, a rental service price).
- Online intermediation services are also excluded when the main objective is to provide digital content to users or provide them with communication or payment services.
- Transactions when there is a direct or indirect participation of 100% of the group entities involved.

- Regulated financial services rendered by regulated financial entities.

  Regulated financial services are defined as financial services for which a regulated financial entity is authorized.

  Regulated financial entity is defined as a financial services supplier that is subject to authorization, or registry, and supervision due to any domestic law or EU-harmonized measure to regulate financial services. This includes those financial services suppliers subject to supervision according to any non-EU rule that, according to a legal act by the EU is considered as equivalent to EU measures.
- The provision of data transmission services by regulated financial entities.

The tax base of the DST will be the gross income, excluding the VAT or other equivalent taxes (if any), earned by the taxpayer upon the provision of the digital services covered by the DST and which are rendered within the Spanish territory. For such purposes, the Law establishes certain allocation keys to allow the determination of the portion over total revenues that must be taxed depending on, basically, their relation to Internet Protocol (IP) addresses located in Spain.

Certain thresholds are established in order to ensure that the DST is only applied to companies of a certain scale with a significant Spanish digital footprint in Spain. This is intended to protect the initial phases of highly-digitalized economic activity development, where it is usually necessary to make a substantial investment and the period to reach a profit-making position may be long.

Hence, the companies subject to this tax will be those with a total amount of worldwide revenue for the previous calendar year exceeding €750 million (a reference is now made to the EU Directive on Country-by-Country Reporting) and with a total amount of taxable revenue earned in Spain in the same period exceeding €3 million. Special rules apply to calculate these thresholds during 2021.

Special rules are established for entities belonging to a group. The thresholds above must be assessed at a group level in order to determine if a company exceeds the thresholds and, therefore, should be considered a taxpayer.

In line with the initial European Commission's proposal, the nexus with the Spanish territory that allows taxation in Spain is based on the location of the users (i.e., users located in Spain), regardless of whether the user has paid any consideration that contributes to the generation of revenue for the company.

For these purposes, a specific set of location rules are established for each of the digital services listed above, based on the place where the devices of these users have been used, generally located by their IP addresses.

However, proof to the contrary (in particular, other geo-location methods) is accepted. This is a protection mechanism for the tax administration and the taxpayer against potential errors, concealment or falsification of the IP address of the devices used, aimed at locating services in or out of Spanish territory.

The Law also sets forth that the data that can be compiled from users for the purpose of applying the provisions of the Spanish DST Law is limited to those which allow the localization of the users' devices located in Spanish territory.

The tax rate is set at 3% on the gross income derived from the referred services.

In contrast to the accrual in the original EU Directive proposal, as per which the DST is calculated on the basis of the taxable revenues accrued in a given period, the accrual of the tax is immediate, taking place for each taxable digital service (or at the time of the total or partial collection of the price for the amounts actually received, whichever event takes place first). The corresponding tax return must be filed quarterly with the Spanish tax authorities.

Next steps

The entry into force is foreseen as three months following the publication of the Law in the Spanish *Official Gazette*, so the Spanish DST will be applicable as of 16 January 2021.

Highly digitalized groups should conduct a detailed analysis of the terms of the Law, as well as the legal and economic substance of their transactions, to consider the potential impact of this measure.

On the other hand, now that the Spanish DST final text has been approved, EY will monitor the development of negotiations at the European Union and OECD levels as well as bilateral discussions with other countries to anticipate potential changes to the tax in Spain.

Endnotes

1. The Directive proposal is based on Article 113 of the EU treaty referred to "other forms of indirect taxation."
2. The Law defines "digital interface" as any program, including websites or parts thereof, or application, including mobile applications, or any other means, accessible to users, that enables digital communication.

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EYG no. 007138-20Gbl

1508-1600216 NY
ED None

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