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GUIDE TO THE WORLD'S LEADING

# Trusts and Estates Practitioners



PUBLISHED BY

LEGAL MEDIA GROUP

E U R O M O N E Y

## SPAIN

## A Sudoku of sorts



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A fair number of tax specialists in cross-border trusts and estates advising clients with Spanish connections or interests did not fail to notice that on May 5 2010 the European Commission issued a Reasoned Opinion requesting Spain to amend its inheritance and gift tax provisions, on the basis that they impose a higher tax burden on non-residents or assets held abroad and are consequently in breach of the free movement of workers and capital principles. It reminded Spain that failure to react will lead to a referral to the European Court of Justice.

So how did it all begin and what is this all about?

The Spanish 1978 constitution introduced a form of government which involved the creation of 17 Autonomous Communities. Over the years the central government has devolved an increasing number of powers to the regional governments, including, generally since 2002, the power to legislate and collect inheritance and gift tax (with separate special provisions applicable in the Basque country and Navarre). Regional provisions will only apply to individuals deemed resident in a given region and in certain circumstances. Non residents or individuals who do not meet the criteria for applicability of regional provisions will be chargeable to Spanish inheritance and gift tax by application of the mainstream Spanish inheritance tax laws.

Some Spanish regions have made active use of their power of legislate this tax, introducing a system of exemptions or near-exemptions to certain free transfers, mostly between spouses and to descendants. At present, with more or less generous capping limits and with some only covering transfers by reason of death and not donations, this is the case in Cantabria (materially capped), La

Rioja, Asturias (materially capped), Galicia (material rates), Balearics, Castille and Leon, Canary Islands, Andalusia (materially capped), Aragon (materially capped), Murcia (materially capped), Extremadura (materially capped), Castille La Mancha, Valencia, Madrid, Catalonia (materially capped at present), Ceuta and Melilla, the Basque country and Navarre.

This means that, for example, free transfers on death between a Spanish resident individual to his/her children, all resident in Madrid, will benefit from a 99% reduction in the inheritance and gift tax payable.

While regional communities have been very active in introducing family reductions and exemptions, the mainstream Spanish tax legislation has remained untouched. Consequently, under mainstream Spanish inheritance and gift tax provisions, free transfers between close family members (typically spouses and children) remain fully chargeable to tax with no material exemptions and/or reductions. The marginal rates fluctuate between 34% and 40.8% for death transfers to spouses and descendants.

As a result of the above, following on the previous example, a free transfer on death between a foreign individual to his non-resident children of a second home in Madrid will not be able to benefit from any reduction in the Spanish inheritance tax payable, whereas the same transfer between residents in Madrid would have enjoyed a 99% reduction. A clear case of discrimination.

So who may benefit and who may not benefit from regional exemptions and reductions in cross-border situations?

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The legislation setting out the scope of application of mainstream versus regional legislations is of particular complexity and has been modified materially over time. Again, special rules apply in the Basque country and Navarre. For the rest of Spain, and at present, mainstream Spanish provisions will always apply to free transfers on death where the deceased and/or the heir is non-resident in Spain.

### SPAIN WILL BE FORCED TO MODIFY THE LEGISLATION TO ALIGN IT WITH THE NON-DISCRIMINATION PRINCIPLES PREVAILING IN THE EU

If the deceased is non-resident and the heir is resident, mainstream Spanish inheritance tax will be levied on the heir's worldwide share of net assets inherited. Application of regional benefits is barred because of the non-resident status of the deceased. If the deceased is resident and the heir is non-resident, mainstream Spanish inheritance tax will be levied on the heir's share of Spanish-located assets inherited. Application of regional benefits is barred because of the non-resident status of the heir.

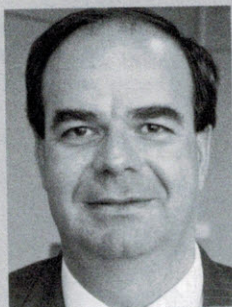
Consequently, in general terms foreign nationals will only be able to benefit from regional benefits provided that both the deceased and the heir are Spanish tax resident and the deceased is deemed resident in a region with material family reductions as per the list above.

Following the Reasoned Opinion of the European Commission, it is likely that, sooner or later, Spain will be forced to modify the legislation to align it with the non-discrimination principles prevailing in the European Union. When or how this will happen remains to be seen. In the meantime, inheritance tax planning is the more crucial, in order to both maximise the benefits of regional laws and minimise the scope of application of mainstream Spanish inheritance tax provisions.

For example, a foreign couple deemed resident in a regional community with favourable inheritance tax provisions and with assets in Spain and abroad may wish to consider arranging their estate so that all Spanish assets are transferred to the surviving spouse on death and all foreign assets are transferred to their non-resident children. The surviving spouse will benefit from regional reductions. The non-resident children will escape the Spanish inheritance tax net to the extent they do not stand to inherit Spanish located assets. To this effect, a joint will with specific succession and tax planning is crucial, as well as effective coordination with advisers in the home jurisdiction.

However, unlike your usual Sudoku, this will not be solved in less than 15 minutes.

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Javier Estella Lana is managing partner at Avantia Asesoramiento Fiscal y Legal and leads a team of full-time lawyers and tax practitioners assigned to the provision of tax and legal services to private wealth clients. He is a qualified Spanish lawyer and member of the Spanish Law Society and has an MA in Spanish tax from the Instituto de Empresa in Madrid (1991). He read law at Autonomía University in Madrid (1989). He is an alumni of the PDG (General Management Programme) Programme at the Spanish IESE School and of the Harvard Law School Leadership in Law Firms Program. He has been an active tax and law practitioner at PricewaterhouseCoopers, where he was one of the founding members of its Spanish private client practice, and at Ernst & Young Abogados, where he was the partner in charge of the national high net worth division in Spain. Javier specialises in the provision of tax and legal services to both domestic and international private wealth clients.

Javier is an active speaker at specialist events, conferences and seminars on Spanish taxes and has been professor at the Instituto de Empresa in Madrid and other leading institutions. He is also a regular contributor to national press articles on private-wealth taxation matters and has co-authored several private-wealth publications. He has attended national and international private wealth events on a regular basis.

Javier's services include national and international tax advice to high net worth individuals, family groups, artists and sportspersons, family businesses, entrepreneurs and company directors. The tax and legal services he provides include business and wealth restructuring processes, national and international succession planning, cross-border planning, family protocols, business ventures, acquisitions, disposals, IPOs, remuneration planning and assistance on Spanish tax audits and voluntary disclosure procedures.

The firm's practice has received a number of outstanding international recognitions, including top rankings in the Guide to the World's Leading Trusts and Estate Practitioners (Legal Media Group/Euromoney), Chambers Europe, and Leading Advisor 100 by Finance Monthly. It was shortlisted to the STEP 2010 International Legal Teal of the Year Award.

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Patricia García Mediero is a qualified Spanish tax practitioner and holds an MA in Spanish Tax from the Instituto de Empresa in Madrid (1994). She read Modern Philology at the Universidad de Deusto in Bilbao in 1990 and became a UK tax practitioner in the London offices of Price Waterhouse (now PricewaterhouseCoopers), where she acquired UK tax professional qualifications (ATTI) in 1992. She has been an active international tax practitioner in the London, Madrid and Bilbao offices of PricewaterhouseCoopers, and in the Bilbao offices of Ernst & Young, as a partner of its private client practice from July 1 2002. With over 20 years of relevant professional experience, she specialises in the provision and coordination of tax and legal services to international private-wealth clients.

Patricia is an active speaker at conferences, seminars and events organised by the Society of Trust and Estate Practitioners, International Wealth Advisors Forum and Estate Club Forum worldwide and a regular contributor to specialist publications, including *Private Client Business*. She is also a member of the experts' panel to the EU Legal Affairs Committee on cross-border succession matters.

She is the partner in charge of the international private wealth practice of Avantia Asesoramiento Fiscal y Legal and leads a team of full-time lawyers and tax practitioners assigned to the provision of international tax and legal services to private-wealth clients. The practice has received a number of outstanding international recognitions, including top rankings in Euromoney's *Guide to the World's Leading Trusts and Estate Practitioners*. It was shortlisted for the STEP 2010 International Legal Team of the Year Award.

Patricia's services are focused on private wealth and include advisory and compliance services to Spanish citizens investing or moving abroad, non-Spanish citizens investing or taking up residence in Spain, advice and probate services to cross-border estates, structuring advice and conveyance work relating to Spain-located real estate, tax and legal planning concerning marriage, testamentary arrangements and other civil law matters, as well as transactional work, both domestic and cross-border. Her clients include individuals and families, executors, trustees, company directors, family offices, private banks and legal firms in need of Spanish tax and legal advice for their client base.

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