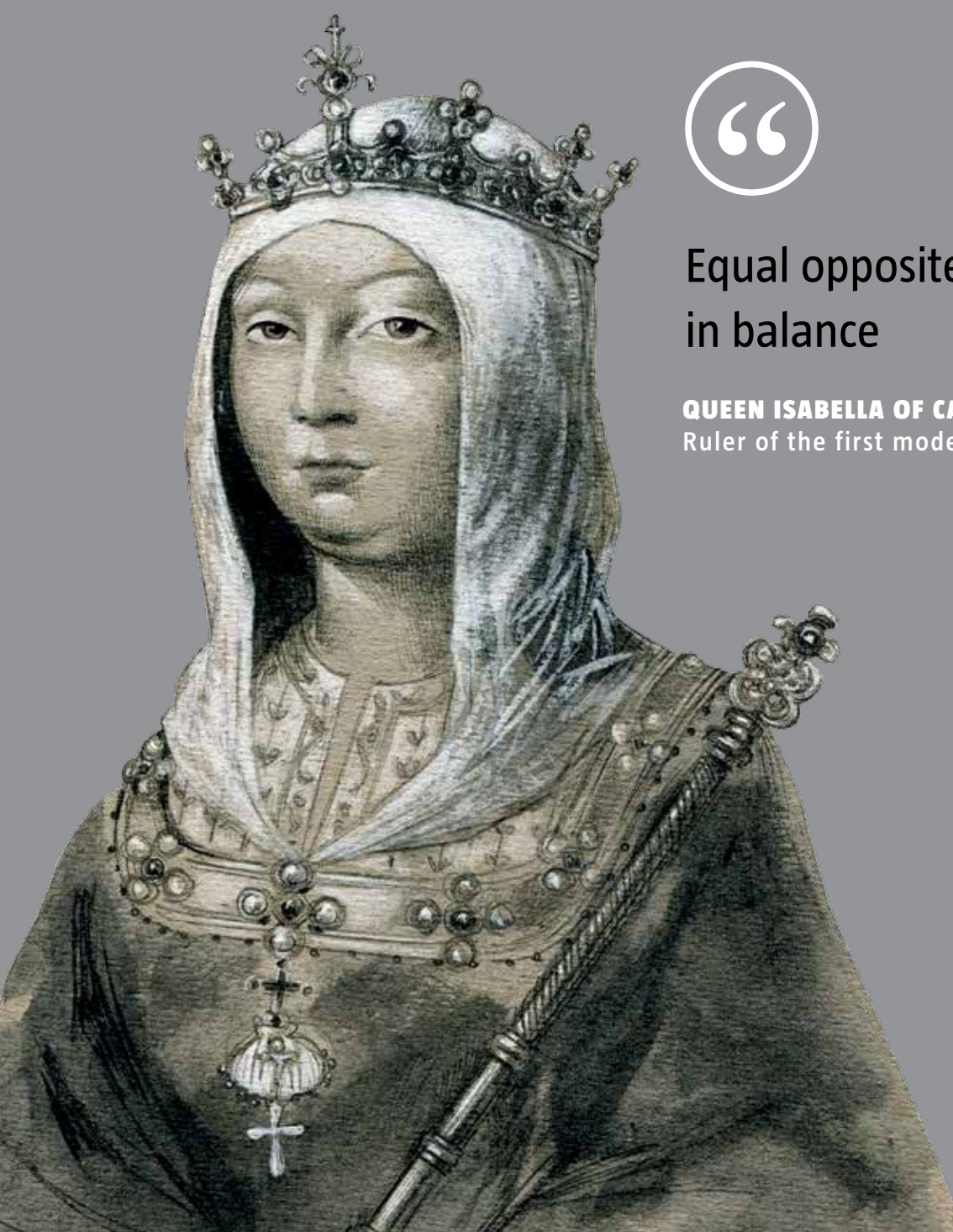


10

PRORITIZING THE FIGHT AGAINST FRAUD

It isn't possible to provide quality public services with a low level of tax revenue. Spain's problem does not lie in tax rates but in tax collection. So rather than raising taxes, what needs to be done is ensure that everybody pays what they owe, strengthening the fight against tax fraud as a primary strategy.



Equal opposites
in balance

QUEEN ISABELLA OF CASTILE (1451–1504)
Ruler of the first modern state of Spain



Taxation is a matter that affects us all

Spain's informal economy must be reduced by 10 percentage points from an estimated 25 percent of GDP to 13 or 14 percent as a priority plan to bring us in line with other countries in our context.



José María Mollinedo

Spokesperson for the Ministry of the Treasury trade union, GESTHA

We must ensure compliance with Article 31 of the Spanish Constitution, which establishes the principles of Spain's tax system:

1. Everyone shall contribute to sustain public expenditure according to their economic capacity, through a fair tax system based on the principles of equality and progressive taxation, which in no case shall be of a confiscatory scope.
2. Public expenditure shall make an equitable allocation of public resources, and its programming and execution shall comply with criteria of efficiency and economy.
3. Personal or property contributions for public purposes may only be imposed in accordance with the law.

The first of these principles affects the level of compliance with tax obligations. Spain's informal economy increased by €60 billion during the crisis,

(Graphic 1)

	2008	2009	2010	2011	2012	Variation 2012/2008
Informal economy	193.626	220.895	233.173	247.980	253.135	59.509
Rate as % of GDP	17,80%	21,10%	22,30%	23,70%	24,60%	6,8

Report entitled *La economía sumergida pasa factura. El avance del fraude en España durante la crisis* (The Costs of the Informal Economy: The Growth of Fraud in Spain during the Crisis), directed by Professor Jordi Sardà of the University Rovira i Virgili in collaboration with Ministry of the Treasury (GESTHA) experts.

reaching a share of 24.6 percent of GDP at the end of 2012, or more than €253 billion. (see Graphic 1).

The second principle affects the level of public spending. In times of crisis and public deficit, it is particularly interesting to compare spending on policies concerning the welfare state with EU averages. (see Graphic 2).

Calculations: Ministry of the Treasury expert (GESTHA) calculations based on Eurostat reports. In other words, Spanish governments with a budget deficit resort to

debt in order to sustain public spending, and even so, spending on welfare policy is below the EU average.

Before dealing with the principles of economic capacity, equality, progressiveness, and tax justice, it is worth analyzing Spain's real capacity to raise revenue through the evolution of the tax burden in comparison with the EU average. (see Graphic 3).

The Spanish tax burden is seven points below the European average as a percentage of GDP, which means that there is a margin for collecting increased tax revenue in



Building housing the Spanish Ministry of Economy and Finance, Madrid (left)

Headquarters of the Banco de España in Madrid (right)

(Graphic 2)

	Spain % of GDP	EU-28 % of GDP	Differential with Europe in billions*
Health	7,15	8,53	-14.427,7
Disability	17,80%	2,22	-4.017,8
Old age	9,11	11,56	-25.595,6
Survivors	2,33	1,70	6.628,6
Family/childhood	1,41	2,31	-9.457,7
Unemployment	3,81	1,62	22.890,8
Housing	0,24	0,60	-3.823,7
Social exclusion policy	0,22	0,46	-2.495,6
Total spending on social protection	26,11	29,00	-30.298,7
Total spending on pensions	11,40	12,90	-15.684,3
Total spending on education	5,30	5,38	-936,6
Total spending on state welfare policy	42,80	47,29	-46.919,6

* Calculated as % differential and applied to Spanish GDP. Calculations: Ministry of the Treasury expert (GESTHA) calculations based on Eurostat reports.

Spain without endangering economic growth.

There are many countries with higher tax revenue and higher growth rates, which suggests that increased growth does not seem to be negatively influenced by increased tax revenue. (see Graphic 4).

The previous table also shows that shifting the tax burden from direct taxes to indirect taxes does not have a significant influence on a country's economy.

Meanwhile, VAT (Impuesto sobre el Valor Añadido, IVA) is the tax that contributes most to indirect tax revenue, but increased rates jeopardize purchasing power for the 85 percent of the population whose income is less than €30,000. VAT has a lesser impact on the 4 percent of taxpayers with an income of more than €60,000 and who can save, since such savings are generally unaffected by VAT.

Given the effect of the tax system on the national economy and the population, and with a view to analyzing the other principles involved, we can

(Graphic 3)

Evolution of the tax burden (% of GDP)	2007	2008	2009	2010	2011
Spain	37,1	33,0	30,7	32,1	31,4
Weighted average for the EU-27	39,4	39,3	38,4	38,3	38,8
Differential with Spain	-2,3	-6,2	-7,7	-6,2	-7,4
Reduced tax revenue in Spain based on tax burden differential compared with the EU average*	-20.310	-63.244	-83.880	-64.454	-78.956

*Differential applied to Spanish GDP. Calculations: Ministry of the Treasury expert (GESTHA) calculations based on Eurostat reports.

(Graphic 4)

2011 (% of GDP)	Real GDP growth rate	Total tax including social security contributions	Direct taxes	Indirect taxes	Social security	Amounts calculated with uncertain possibilities of their collection
Spain (all government authorities)	0,1	31,41	9,92	10,2	12,13	-0,8
Weighted average for EU-27	1,7	38,84	12,88	13,41	12,68	0
Germany	3,3	38,67	11,6	11,54	15,53	0
France	2	43,89	11,8	15,53	16,86	-0,01
Austria	2,8	42,05	12,98	14,58	14,55	0
Sweden	2,9	44,33	18,69	18,61	7,04	0
Estonia	9,6	32,85	6,56	14,15	12,13	0

Calculations: Calculations by experts at the Ministry of the Treasury (GESTHA) based on Eurostat reports.

(Graphic 5)

Year	Personal income tax (IRPF)	Corporate tax	VAT	Special taxes	Other	Total tax revenue
2007	72.614	44.823	55.851	19.786	7.601	200.676
2008	71.341	27.301	48.021	19.570	7.220	173.453
2009	63.857	20.188	33.567	19.349	7.062	144.023
2010	66.977	16.198	49.086	19.806	7.469	159.536
2011	69.803	16.611	49.302	18.983	7.061	161.760
2012	70.619	21.435	50.464	18.209	7.840	168.567
2013	69.951	19.945	51.931	19.073	7.947	168.847
2014	72.662	18.713	56.174	19.104	8.334	174.987

Tax collection reports published by the Spanish National Tax Agency (AEAT). Amounts in billions of euros

(Graphic 6)

Effective rate of corporate tax as a proportion of accounting profits (%)	2007	2008	2009	2010	2011	2012 provisional
Enterprises that do not form part of a business group	22,6	19,8	13,2	15,4	15,8	16,0
Established business groups	9,9	5,3	6,4	5,0	3,8	5,3

Source: Tax collection reports published by the Spanish National Tax Agency (AEAT).

see that of the taxes paid by people and enterprises, personal income tax (impuesto sobre la Renta de Personas Físicas, IRPF), VAT and special taxes have maintained the level of revenue they generate throughout successive tax increases from 2010 to 2014. In contrast, revenue from corporate tax (Impuesto sobre Sociedades) has plummeted, despite the restrictions approved to avoid tax deferral. (see Graphic 5).

Second, the crisis, welfare policies on a budget below the European average and an unequal tax system with a high evasion rate have caused inequality to increase by 10.8 percent, with more than nine million people living below the poverty line in Spain. The richest 20 percent of Spaniards take home 44 percent of total income, while the remaining 80 percent of the population receive just 56 percent. This situation worsens when we take into account that the poorest 20 percent represent just 6.6 percent of total income, a figure that reveals a high level of social and economic inequality.

Third, improvements to the progressiveness of income tax with the surtaxes in force between 2012 and 2014 have been diluted by the lower number of taxpayers declaring an income of more than €60,000, since there are many instruments that can be used to avoid income tax contribution.

A fourth point is that Spain's wealth tax (Impuesto sobre el Patrimonio), which was withdrawn in 2008 and only partially reinstated in 2011, has still not been applied to 14,208 large fortunes in the Autonomous Region

of Madrid, offering those fortunes savings of nearly €602 million a year. Comparing wealth tax with private banking reports, we can see that as wealth increases, so does tax evasion. This does not necessarily mean that people with vast assets do not declare them; rather, the amount of wealth declared is less than it ought to be. The payment of personal income tax and wealth tax is avoided through the use of holding companies in the case of property, open-ended collective investment schemes called SICAVs (Sociedad de inversión de capital variable) for stocks and securities, and a host of other practices.

The fifth important observation to make is that SMEs pay three times more business tax than large business groups in real terms. (see Graphic 6).

In fact, if business groups paid the same amount of taxes as SMEs (16 percent), it would result in almost €8.3 billion extra in tax revenue a year.

Proposals

Faced with plummeting tax revenue since 2008 and an increase in tax fraud, the experts working for the Ministry of the Treasury are of the opinion that Spain's informal economy must be reduced by 10 percentage points to 13 percent or 14 percent. This should be considered a priority plan to bring us in line with other countries in our context, in conjunction with other tax and organizational measures, and awareness-raising activities. This would make it possible to collect an additional €25 billion in taxes every year.



The richest 20 percent of Spaniards take home 44 percent of total income, while the remaining 80 percent of the population receive just 56 percent. This situation worsens when we take into account that the poorest 20 percent represent just 6.6 percent of total income, a figure that reveals a high level of social and economic inequality.

Improvements to the progressiveness of income tax with the surtaxes in force between 2012 and 2014 have been diluted by the lower number of taxpayers declaring an income of more than €60,000, since there are many instruments that can be used to avoid income tax contribution



The Spanish tax burden is seven points below the European average as a percentage of GDP, which means that there is a margin for collecting increased tax revenue in Spain without endangering economic growth.

There are many countries with higher tax revenue and higher growth rates, which suggests that increased growth does not seem to be negatively influenced by increased tax revenue

The vast catalogue of measures that GESTHA proposes include the following priority measures to combat tax fraud: an official evaluation of Spain's informal economy, tax fraud and employment fraud; temporary planning of measures to reduce these types of fraud; effective coordination and collaboration between the Spanish National Tax Agency (AEAT) and tax offices in Spain's Autonomous Regions to share tax databases; monitoring by the courts of the results reported by AEAT to guarantee their transparent and independent management; a maximum of €1,000 restriction on cash transactions; aligning timeframes for the administrative and criminal prescription of tax offenses and unifying thresholds and sanctions for the range of such offenses (Article 305 to 310 bis of the Criminal Code); and seeking agreements in the OECD on the automatic avail-

ability of tax information and the eradication of abusive practices. Measures to improve the efficiency of expenditure and making the tax system more progressive and fair are also very important, and include the following: reduce the contradiction in the way employment and capital income are taxed at different levels; restrict the use of the objective assessment scheme (Estimación Objetiva por Módulos); modify the Law on Collective Investment Schemes to establish a maximum limit for participation in SICAVs to a maximum share capital of 2 percent to 5 percent to avoid abuses. Additional measures: approve the Tax on Financial Transactions (Impuesto a las Transacciones Financieras) without further delay; seek an agreement with the OECD on aligning nominal rates for investment funds and societies with the rates applicable to industrial or ser-

vice enterprises; create a wealth tax to prevent tax evasion and restrict regional allowances reducing the rate paid; bring the average nominal rates paid in business tax by large enterprises in line with those paid by SMEs; strengthen the audits in force to improve the efficient control of public spending, including that of public entities; ensure effective coordination between the control bodies managed by the different regional authorities; and publish information on interventions and public accounts. We can highlight the following organizational and human-management measures in the sphere of the AEAT and the Ministry of the Treasury and Public Administrations: create a higher technical body within the Tax Office to increase the range of duties performed by staff and redouble efforts in tax control and customs, as well as the control of grants and public assistance; set out the essen-

tial characteristics of jobs in lists of job categories; establish protocols for the prevention of psychological harassment within the AEAT and the Ministry; and increase staff numbers at the Spanish National Tax Agency, given that Spain has at its disposal barely one tax office employee per 1,928 taxpayers, as compared with 860 in France, 729 in Germany, or 551 in Luxembourg. Spain can hardly be surprised that the country has an informal economy more than double the size of its counterparts when it has half the staff for dealing with the fight against fraud. Finally, we might highlight the following measures to raise awareness of tax issues and the efficiency of public spending among the general public: tax assessment programs for taxpayers and initiatives providing information on the list of services offered by government authorities; and programs to raise awareness

in society and promote attitudes that condemn corruption, tax evasion, contraband, the consumption of counterfeit goods, the informal economy, and abuses in public services. In this sense, the list of public debtors and tax crimes that the government aims to include in the draft amendment to the General Taxation Law should also include a list of the debts detected with a value of over €1 million—even if they have been paid or deferred—as well as a list of sales, accounting profits and taxes paid by the 4,752 enterprises reporting revenue of more than €45 million a year (0.3 percent of the total). This expansion of public information would allow the population to assess the social responsibility of this country's largest companies which, along with large fortunes, are where 72 percent of tax fraud is concentrated.



Antoni Zabalza

Professor of Economic Analysis at the University of Valencia and Ex-Secretary of State for the National Treasury

POINT

Something is wrong with our system

The problem isn't tax rates: Spaniards pay rates similar to those of other European countries. The issue lies in the narrowness of tax assessment bases due to the high quantity of deductions, exemptions, and preferential treatments available, and the significant rate of tax fraud.

When compared to those of other European countries, Spanish taxes do not raise as much revenue as they should. Something is wrong with our taxation system. The revenue it generates in relation to the nation's income is abnormally low. In 2013, the Spanish tax burden stood at 33.2 percent of GDP, way below other countries in our context such as France (47.4 percent), Italy (43.4 percent), and Portugal (37.2 percent). Our tax burden is actually more similar to those of the Czech Republic (34.9 percent), Estonia (32 percent), Cyprus (31.6 percent), and Slovakia (30.4 percent), all of which have much less consolidated tax systems than we do.

The problem isn't tax rates: our rates are similar to or higher than those paid by residents of other European countries. The issue lies in the narrowness of tax assessment bases "due to the high quantity of deductions, exemptions and preferential treatments available" and the significant rate of tax fraud.

In 2014, the tax advantages budgeted on income tax, business tax, and VAT were worth almost €38.4 billion. And if we add the concessions set out in Spain's wealth tax and those applicable to inheritance and gift taxes, the total value of tax advantages reached over €52.6 billion. The elimination of these benefits would increase tax revenue by almost 30 percent, equivalent to 5 percent of GDP. Some of the aims that these tax breaks intend to achieve could be considered reasonable. But if they are reasonable, then they should be

addressed via public spending, not by depleting the tax system's revenue-raising capacity.

But the problem of fraud is even more grave, if that's possible. It is curious that a country with a technically very advanced tax administration system should have such a high level of fraud. While increasingly advanced IT in our system undoubtedly makes it much easier for the population to manage tax processes, this technology seems to have been designed more to control taxpayers and ensure that they comply with their obligations than to stem the flow of fraud and identify hidden tax bases.

Apart from perverting the natural course of the tax system, the existence of significant levels of fraud discourages law-abiding taxpayers from fulfilling their tax obligations and erodes their confidence in the system. This is a particularly serious consequence of fraud, since acceptance of the tax system is only achieved thanks to the great efforts of a great many people, and following many years of awareness-raising and social education. All of this can be lost—or seriously damaged—in a relatively short time. And without this social acceptance, a tax system simply cannot work.

Fraud is the most serious threat to the smooth running of the tax system: it creates imbalances in the set of taxes, it distorts competition, reduces effective revenue collection, and forces compliant taxpayers to shoulder a greater tax burden. Fraud is behavior that redistributes wealth to those practicing fraud, siphon-

ing off revenue from those who comply with their legal obligations.

In Spain, the advances achieved in matters of compliance and the fight against fraud that followed the introduction of personal income tax—and in particular, the creation of the Spanish National Tax Agency—seem to have ground to a halt or even been reversed. It is clear that the economic context has also changed. Increased fraud may be due to a range of factors: the more globalized world we live in; the existence of more opportunities to divert the flow of financial returns abroad; the use of Spain as a suitable location for money laundering activities; the recent surge in immigrants coming into our country; or the spectacular housing bubble of 2002 to 2007. But such fraud may also be the result of an insufficient provision of the resources required to face these changes in an effective way. It seems that in recent years the technology and means available for committing fraud have far outstripped the resources and innovations invested in the fight against non-compliance with tax obligations.

Tax reforms seek to improve the efficiency and effectiveness of tax collection in order to make it easier for the taxpayer to make their contribution and ensure that the tax system does not distort the economy. However, in the case of Spain these improvements are of little use if the existing level of fraud is not drastically and urgently reduced. The fight against fraud is an inescapable duty of Spanish society. It is a task in which tax agencies have a primary and immediate responsibility; nevertheless, by its nature, tax fraud is much more than just a sectorial administrative challenge. This task must involve the entire government on all levels, since it is government authorities who decide what resources to allocate to tax agencies. They also have the power to improve social education in favor of respect for the rule of law, as well as to eliminate corruption in all spheres at the same time. The government must fight against the informal economy, which is no more than another of the many forms of tax fraud. Such coordinated action is the only way of achieving positive and long-lasting results.

Spain's informal economy is estimated to be worth

around 25 percent of GDP, an extremely high percentage for a developed economy like ours. Such a high level of economic activity outside the reach of the tax authorities is always going to distort competition and reduce productivity. The eradication of a significant proportion of this fraud would help to increase Spanish tax revenue and improve the individual and collective morale of those taxpayers who do fulfil their obligations.

To give us an idea of the amounts of revenue in play, if combating fraud led to the formalization of a quarter of the current informal economy, tax revenue would rise by 8.3 percent and Spain's tax burden would increase from the current 33.2 percent to 36 percent. If half of the submerged economy was formalized, tax revenue would be increased by 16.7 percent, and the country's tax burden would grow to 38.7 percent. This would still leave Spain behind France and Italy, but 1.5 percentage points ahead of Portugal. If the whole of the informal economy was legalized, the increase in tax revenue would reach 33.3 percent, and Spain's tax burden would swell to 44.3 percent of GDP, almost one point ahead of Italy and just three points behind France.

These calculations are entirely illustrative. They work on the premise that the level of economic activity would remain the same, whether legal or otherwise, when in fact we know that taxation represents a cost that affects efficiency, reducing GDP to a certain extent. Nevertheless, it is a price that without a doubt it is worth paying with a view to ensuring compliance with legislation and achieving a greater level of equality in tax payment.

Advocating a reduction in tax fraud is not the same as calling for an increased tax burden. The revenue obtained from combating fraud can actually be used to reduce the tax burden of those who do pay taxes without having to make cuts to public services. Similarly, this revenue can be invested in providing better public services without incurring higher levels of debt. Alternatively, it can be used to reduce debt without having to raise taxes or cut services. Advocating an end to tax fraud does not have the aim of simply annoying those tricksters who currently escape the tax man; rather, it is linked to the aspiration of living in a better and fairer world.

COUNTERPOINT

Weaknesses in the design of the tax system

The central problem in Spain's tax system is that it is full of loopholes that allow the country's enterprises and richest individuals to evade taxation. The result is an unfair system with a very limited revenue-raising capacity. This weakness has only been made clearer by the crisis.

The central problem in Spain's taxation system is that it is full of loopholes that allow enterprises and the richest individuals to evade taxation. These loopholes in the system have to do both with design (bases, deductions, concessions) and management (fraud). The result is an unfair system with a very limited revenue-raising capacity. This weakness has only been made clearer by the crisis. During the first years of the slump, although Spanish GDP fell below EU averages, tax revenue (as a percentage of GDP) decreased more than in any other country (seven times the average). Since then, although nominal tax rates have soared, situating Spain in the highest band in the EU, tax revenue has increased very little and is still well below the European average.

Some interested parties are given to exaggerate the effects of taxes on incentives, offshoring, and competitiveness. Leaving aside cases that have no practical relevance, the fact of the matter is that where there are broad tax assessment bands taxes have little or no impact on incentives. With regard to offshoring, tax rates may affect where nonresidents invest their financial capital (and they do not have to declare their finances in this country) but not where residents invest (unless they are committing fraud). So the risk of offshoring due to taxation is actually rather small. What many companies do is to relocate (fictitiously) the profits of their business offshore, but not the production itself. Finally, competitiveness depends far more on other factors—such as the capacity for innovation, market strategies, and so on—than on taxation. Therefore, taxes are linked more to evasion and the fictitious relocation of profits than to the level of economic activity itself. In fact, Spain has emerged from the crisis with the highest tax rates in its recent history.

The right level of taxation

The right level of taxation depends on the level of public services that we want to enjoy. As set out in the Spanish budget stability plan (in which the essential austerity measures take the form of spending cuts), and as con-

firmed by the tax reductions implemented as soon as the economy began to recover, the current government's aim is to situate tax revenue at around 34 percent of GDP or less. At these levels, it will not be possible to finance the infrastructures or research needed, or maintain—let alone improve—the social benefits available in a country with an increasingly aging population that requires more health, social, and pension benefits. The tax burden in Spain should be increased to 40 percent as a minimum, in line with the EU average. This is the only way of guaranteeing a reasonable welfare state. A large proportion of this income would come not from increases in tax rates but by closing evasion and avoidance loopholes.

The reforms required

Personal income tax. Spain's personal income tax (IRPF) should be a progressive tax reflecting each taxpayer's capacity to pay. To this end, tax advantages must be eliminated, and channels for tax evasion and avoidance must be closed, basing contribution levels solely on increases in taxpayer income. The first step would be to eliminate contradictory tax levels (taxing all incomes together), reduce exemptions (the reinvestment of capital gains in the taxpayer's primary residence, foreign income, and so on) and allowances (certain rents and income from economic activities), as well as deductions (pension plans and maternity leave). Second, Spain needs to close the loopholes that allow tax avoidance, by making SICAV schemes pay taxes annually on any increases in value, ensuring transparency in order to avoid the use of dummy corporations, eliminating certain corporate tax schemes, and so on. Moreover, Spain must adjust the deductions system to make deductions fairer (linked to work, for example), and reform the way it deals with inflation (updating of capital gains tax, indexation of taxes). Rates should not be changed over the short term, although there is room for tax increases in the rates in force for 2015 and 2016. The maximum marginal rate should never exceed 50 percent, in any case.

Ignacio Zubiri

Professor of Public Finances at the University of the Basque Country



Corporations. The aim must be to ensure that the neutrality of taxes. All corporations excepting financial institutions should pay the same tax rate. Almost all of the current reductions (on use of patents, capitalization reserves, etc.), advantages and deductions (even in the case of R&D, except in sectors where they are exceedingly low) should be eradicated. We should also eliminate certain special schemes such as those related to foreign assets, venture capital firms, etc., while some others should be subject to review. Applications to the special fiscal consolidation scheme should be limited. It is necessary to tighten and limit deductions based on double taxation of dividends and make permanent the restriction on the offsetting of tax losses to 25 percent of the base rate. We must limit and control certain deductions so that they cannot be used by corporations to avoid personal income tax. In order to reduce fraud and financial engineering, incentives should be introduced to encourage voluntary collaboration. Enterprises with low profit in relation to revenue should undergo inspections, and a new tax on the diversion of profits could be created.

VAT. Spain should be looking to aim for a system with few exemptions and a single rate. The country also needs to eliminate special schemes. Selling and buying goods without VAT should be classified as an offense. There is a margin of between zero and four points where rates can be increased, although this should not happen over the short term.

Other taxes. Wealth tax bases should be subject to reform in order to ensure that all types of wealth (property, real estate, and partially productive wealth) are taxed at the same rate. The tax on inheritance and gifts should be increased where direct relatives are involved. Environmental taxes and levies on tobacco and alcohol should also be increased. Taxes on the financial sector and speculative activity must also be raised.

Social security contributions

The social security contributions made by enterprises should not be reduced in general terms because it would prevent companies from paying acceptable pensions, while any effects on employment would be short term only. Substituting these contributions with other taxes

would not yield profits. Over the medium term, in order to ensure funding for pensions, contributions toward unemployment should be transferred to pensions, raising the rates paid by workers and—marginally—those applicable to business owners.

The fight against fraud

The real struggle has yet to be won. The fight against fraud should focus on a very simple concept: it must not be profitable to commit tax fraud. This requires progress in several directions: increasing the likelihood of being detected, bigger sanctions (financial and non-financial), more effective collection and enforcement, and a sense of collective responsibility.

First, the weight and duties of the National Fraud Investigation Office should be expanded, and its work accompanied by specialized judges and prosecutors, as well as tax police. Second, Parliament must monitor the effectiveness of the Tax Agency. More resources should be dedicated to inspection, improvement of information, and analysis of data.

Financial sanctions must be increased substantially and expanded to include tax avoidance, also eradicating the possibility of pleading mitigating circumstances. Non-financial sanctions must include the publication of details in certain cases, the automatic inspection of years still not subject to statutes of limitations for all taxes, and the prohibition of taking part in public procurement processes. Buying goods without VAT should be classified as an offense.

Tax havens

The concept of privileged tax areas should be created to encompass all territories that do not collaborate to a sufficient level with the Spanish tax authorities. A deterrent tax regime must be established for these areas (taxing certain payments to these areas at 40 percent and not allowing any expenses incurred in such zones to be deducted from taxes), while a special tax should be created on the diversion of profits (similar to that created by the United Kingdom in 2015) in order to tax enterprises that operate from tax havens or employ financial engineering mechanisms.



TALK ABOUT THE FUTURE

Is the fight against tax fraud the main challenge faced by Spain's tax system?

It is one of the big challenges facing Spain, but it isn't the only challenge or the most important one. But from the point of view of the economy and the country's development it is a very important challenge, above all when we compare ourselves to our peers in the European Union. Tax collection isn't always linked exclusively to tax increases or changing laws. It is important to achieve an increase in the number of contributors. This is what will bring about a radical change to tax collection.

How can this problem be dealt with using the available measures and through the tax culture in Spain?

Culture is a primary aspect. In the United States there is a very strong tax culture, but this culture is achieved by putting measures in place. To compare with our European counterparts, in Germany every tax worker or inspector is responsible for eight hundred inhabitants, while this figure stands at two thousand in Spain.

Is the Spanish system full of loopholes for enterprises?

I don't entirely agree that it is. There is a bit of demagogery when it comes to examining how large companies pay their taxes in comparison to medium-sized or small companies. If the ratio is compared with the tax bases applied it is actually quite similar: 18 percent as opposed to 20 percent. Tax laws determine certain types of behavior.

What changes would you recommend in the tax system?

Resources, communication, and transparency. It is important that

the authorities apply consistent criteria. The law should be worked on to ensure that it is adequate. Courts and opinions should be in agreement on the issue of criteria. And when it comes to resources, we need to increase the number of taxpayers.

Are the disparities in the taxes paid between Madrid and Barcelona, for example, sustainable?

This is not advisable from any perspective. It doesn't make much sense for Catalonia to be paying five or six percentage points more on their income than Madrid or Andalusia. Why is there a wealth tax in Catalonia and not in Madrid? We are a single market. We are one country, and we should have a single tax system. If we are part of a single market in Europe we should also ideally have a unified tax systems.

How can this be achieved?

With a change in the way the autonomous regions are financed.

What does innovation mean in your field?

Technology is disruptive and cruel. Today, you can find contracts and other items online that were unimaginable in the past. Why does a member of the general public have to go to a lawyer if someone else can offer them the same service? Technology obliges us to provide types of services that others cannot provide.

Has there also been innovation unrelated to technology?

Yes. I can't ask my young lawyers to do the same things we did forty years ago. Their aspirations are different. The balance between work and personal life is different, and that also means that ways of working have also changed. Some 55 percent of our lawyers are women. This normally tends to happen only in the first years of professional careers, but in our case we don't want to lose female talent as it matures over time. We have to talk about these changes, since society has to go along with them.

Rafael Fontana

President of Cuatrecasas, Gonçalves Pereira

“We are a single market, we are one country, and we should have a single tax system”

“Would many activities in the informal economy survive the collection of all the taxes and social contributions required in the formal economy?”

Ricardo Gómez Barreda

Senior Partner at Garrigues

Is the fight against tax fraud the main challenge faced by Spain's tax system?

Tax fraud has many incarnations with totally diverse origins that require completely different approaches. For example, the tax fraud taking place in the informal economy is likely to be a consequence of the situation of people who cannot enter the formal economy because their income is too low to be able to pay all of the contributions required by the system. There is another type of tax fraud that is probably not truly fraud because it derives from the poor regulation of our tax management system, where opportunities are created allowing certain parties to take advantages beyond those that the legislator would have wanted to concede. That is tax evasion.

Is it a question of instruments and culture?

All of the reports produced over the last three years in Spain value the informal economy at some 23 to 25 percent of GDP, which is about €250 billion. If we could collect the same proportion of taxes from this amount as we do from the formal economy—around 35 percent in taxes and social contributions—we would achieve additional tax revenue of some €75 billion, and we'd no longer have a fiscal deficit problem. But the question is, of course, would many activities in the informal economy survive the collection of all the taxes and social contributions required in the formal economy? I have my doubts. We have a popular image of this informal economy as a construction company, for example, that hoards a fortune in banknotes and under-the-table accounting, but it isn't like that in general. Rather, we are talking about unemployed people who take on hobbies, domestic workers who don't pay contributions, people who teach classes off the books, or physiotherapists who work wherever they can. That said, we have to do everything we can to ensure that this whole segment of economic activity transitions progressively toward legal activity, and that means paying for these workers to enter the social security system and leaving the past behind us. It is also time to

eliminate the modular systems of income tax and VAT since they are a clear source of problems.

What else would you change?

Without a doubt, the first change I would make is to make labor cheaper by reducing social security contributions and increasing indirect taxes. VAT is a delicate issue because it is added on to the consumption of the whole population. We also have to make further increases to special taxes (such as the tax on fuel, tobacco or alcohol), given that these are still low in comparison to other countries. Social security contributions cannot be lowered because they fund pensions, and this is something absolutely sacred in Spain. Perhaps at some point a proportion of state pensions, above all non-contributions-based pensions, will have to be financed to a greater extent with funds from the general state budget.

Is the difference in certain taxes between autonomous regions sustainable?

I think that 99 percent of Spaniards will never agree on whether there should be a wealth or heritage tax, but they do agree that there shouldn't be any difference between the autonomous regions since this implies that there are different categories of Spaniards. A broad national pact is required to establish a common tax system with certain thresholds, avoiding the distortions of the past that have been so damaging.





FISCAL STRATEGY



TALK ABOUT
THE FUTURE

Fernando Santiago

President of the Spanish General Association of Administrative Agents

Is the fight against tax fraud the main challenge faced by Spain's tax system?

It should be one of the main challenges. The problem is that the fight against tax fraud means nothing unless it is accompanied by an attendant series of measures and ways of doing things. We have to deal with a range of issues linked to tax fraud. First, the very nature of our laws should discourage fraud. We must establish working methods and systems that will put a stop to fraud and the informal economy because there are many circumstances that tempt people to commit fraud that could be avoided in other situations.

What are the main measures that you would strengthen?

If we do not emphasize from the start that failing to pay taxes and contribute is something that goes against Spain's interests and all Spanish citizens we are not going to be able to combat fraud, no matter how many laws we make: ultimately, compliance with the law depends on people's behavior.

Is there an excessive number of loopholes in the Spanish tax system?

Yes. The Spanish tax system is so wholly complex and difficult to follow that it has a great deal of legal loopholes. Apart from that, there are no resources, money, or political will to tackle tax fraud as such.

Is the tax system too complicated for ordinary members of the general public?

Given that there are local, regional, and national tax regulations, some of which contradict each other, yes: it is absolutely impossible for a normal person to know everything about tax regulation in Spain. And so people cannot comply with it. Nobody in this country complies with tax regulations 100 percent because it is simply impossible; they don't have the knowledge to do so.

What main reforms would you implement?

First, it is very important that somebody remembers to think about small companies, above all, as well as medium-sized companies and the self-employed. If no specific tax legislation is created to cover the self-employed and small and medium-sized enterprises, we are not going to be able to survive in terms of taxes. We self-employed people and small companies have done much more than the big players to pull us out of the crisis. But we must be careful: we must take into account that when we are talking about tax legislation we should often discuss everything that affects all tax types in general as opposed to solely fiscal taxes, since on many occasions when talking about tax cuts what we are really referring to is decreases to fiscal or contributory taxes. Nevertheless, social security taxes continue to increase, the most important fiscal item in the country.

Is it possible to reduce taxes on capital gains, for example, in one country and not in another?

Everything can be reduced, but we have to remember that this would implicate cuts to public spending. Such taxes can perfectly well be reduced in times of crisis. But we have to apply logic. We have to continue to establish the line of growth in tax on consumption and reduce certain taxes such as income tax.

“If no specific tax legislation is created to cover the self-employed and small and medium-sized enterprises, we are not going to be able to survive in terms of taxes”

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THE BUSINESS PERSPECTIVE

REDUCING CONTRIBUTIONS

One of the general demands made by businesspeople is for a reduction in social contributions, with these being covered by the public budget—as in many other countries in our context—as opposed to being shouldered by companies. They also call for tax legislation to be harmonized between Spain’s Autonomous Regions and within the EU. Casimiro Gracia, President of AXIS CORPORATE, is of the opinion that “it would be beneficial to harmonize tax regulations between the various Autonomous Regions and try to be more competitive when it comes to direct taxes. In this respect, advancing in the harmonization of European tax policy would be a very positive move toward ensuring that investments made in one place or another are subject to the same rules. Businesses have to be very responsible, creating

wealth and well-being in the country where they are located as opposed to some other country.”

TAX AWARENESS

In relation to tax fraud, Joan Roca, Executive Vice-President of Roca Junyent, points out that “while the informal economy is an essential task, the headlines don’t reflect the real problem, which is that this country would not stay afloat if it were true that just 1 percent of the population has an annual income of over €100,000.” He continues: “The problem lies in a lack of involvement and awareness. There is no doubt that the Spanish tax authorities should perform large-scale inspections, but it would be more appropriate and effective to make sure all actors were given the opportunity to comply with the law first. Often, not even the inspectors know how to explain what

someone needs to do in order to comply with their obligations.” “Whether or not there is growth, it would be possible to cover the public deficit if we could regularize just 25 to 30 percent of the informal economy,” says Eduardo Serra, President of Fundación Transforma España. “That said, the most direct way of getting rid of the deficit is not by squeezing taxpayers but by eliminating large and generalized pockets of fraud and reducing public spending. Nevertheless, we continue to see excessive spending from municipal, provincial, and regional governments, as well as from central government.” Meanwhile, María José Álvarez, Vice-President of Grupo Eulen, is of the view that “putting an end to the informal economy can only be achieved by one means, and that is for everyone to realize that paying taxes is what makes us citizens.”

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