Sports Law & Taxation

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Spain:

The use of personal service companies

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Introduction

In recent years, there have been numerous tax audits on the use of personal service companies in Spain from the Spanish Tax Authorities ("STA"), and it has also been applicable to the companies of sports persons.

In many cases, these companies were used to ensure that the services provided were included in the scope of the Corporate Income Tax (with an estimated tax burden of 20-25%), instead of the Personal Income Tax (with a taxation of approximately 50% depending on the autonomous community where the taxpayer effectively resided).

Additionally, the use of corporate entities allows a greater deduction of expenses than in the case of personal income tax.

A large part of these tax enquiries concluded with an imputation of the income to the shareholder and, consequently, to pay additional tax (25-30% because of the difference between 50% and 25%-20%).

These tax audits largely concluded with the signing of disagreement statements and have been appealed both in the economic-administrative and judicial fields.

Even though in most cases the administrative courts have agreed and confirmed the criteria of the STA, we find ourselves in certain cases where they rule in favor of the taxpayer.

In this article, we will analyze the reasons for such discrepancies and what are the latest developments in this regard.

Background and tax arguments of the STA

It has been common in Spain to use limited liability companies to canalize the income from artists, actors, TV hosts, radio, and press journalists or even for the exploitation of the image rights of athletes and artists. In some cases, sports persons have implemented structures in order to allocate there the income derived from the exploitation of their image rights (not only from their clubs, but also from different brands or advertisements).

It was fairly common that the income and the positive cash-flow of the company was lately destined to real estate investments or equity investments for the shareholder. So, the company was effectively used to perceive the income from third parties and as an instrument for investments for the owner.

In general, the STA, the Administrative Court, and the *Audiencia Nacional*, consider that it is perfectly legal, from a commercial perspective, to use the companies in order to carry out economic activities. Even though the company is entirely participated by a sole shareholder or administrator.

It is true that, in cases related to image rights companies, those bodies have alleged the entire or partial simulation or the doctrine about the *"piercing of the corporate veil"* to eliminate the scheme implemented and mechanically allocate the income into the individual ignoring the presence of the company. The STA in its *"Nota de la Agencia Tributaria sobre interposición de sociedades por personas físicas"* [3] provides as follows[4]:

"In the event that the company lacks the structure to carry out the professional activity that it appears to be carrying out, by not having sufficient and adequate personal and material resources for the provision of services of this nature, or having it, it would not have actually intervened in the performance of the operations, we would find ourselves before the mere formal interposition of a company in

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3 Agencia Tributaria, *Nota de la agencia tributaria sobre interposición de sociedades por personas físicas*, available at www.agenciatributaria.es/static_files/AEAT/Contenidos_Comunes/La_Agencia_Tributaria/Segmentos_Usuarios/Empresas_y_profesionales/Foro_grandes_empresas/Criterios_generales/Sociedad_Interpuesta.pdf (accessed 1 June 2021).

4 Translation by the authors.

commercial or professional relationships in which it would not have participated at all, especially taking into account the highly personal nature of the activity carried out."

In cases where the simulation rules are not pertinent, the STA and the Administrative Court have based their criteria to allocate the income on the valuation of the market price, as well as on the application of the "arm's length principle". So, the shareholder – company must value their transaction attending to the fair market value of that deal.

Considering that, in most of the cases, the company is paid by third parties (*i.e.*, broadcaster, club, sponsorship companies, radio or tv producer), the amounts paid by such third independent party is considered as the market price of the shareholder. The "free price compared" method is then the preference of the STA and the Administrative Court to allocate the income of the company into the individual.

In this sense, the STA and the Administrative Court (in most of the cases) do not admit the application of a profit margin of the company, due to the fact that the entity does not provide any value added to the individual.

That being said, the STA have analyzed which tax consideration shall be applied for the shareholder over the income allocated into their individual level in its statement *Consideraciones sobre el tratamiento fiscal de los socios de entidades mercantiles*[5]. The STA consider that the category of the income for the shareholder would depend on the following issues:

- the use of human resources in order to carry out the activity;
- the existence of the means of production provided by the shareholder. In this sense, the STA have stated that[6]:

"In particular, it should be noted that in the case of professional services (law, consultancy, architectural services, medicine ...) the main means of production resides in the partner himself, that is, in the professional training of the natural person who provides the services – these are services whose contracting has a marked "intuitu personae" character, so that the material means necessary for the performance of its services provided by the entity are of little relevance compared to the human factor.

Consequently, from the fiscal perspective, it is essential to analyze in each concrete case the presence or absence of the notes of dependency and alienation and the existence or not of means of production at the partner's headquarters, so that, existing such means of production at the partner's headquarters, only in the absence of such notes will it be understood that the partners of the entity carry out their activity by ordering the factors productive activities on their own account in the sense of article 27 of the LIRPF and therefore they carry out an economic activity. On the contrary, their qualification will be of labor relationship when the aforementioned dependency notes exist and someone else or when the aforementioned means of production are lacking."

Therefore, in the cases related to companies of actors, TV, image rights or journalists, the STA and Administrative Courts consider that, if the companies do not provide a value added to the individual in terms of organization, human or material resources and the core business of the company is the individual itself, the income obtained by the company shall be allocated into the personal income tax return of the individual.

However, there are some cases in which the Courts consider that the companies have effectively provided to the individual a real service and, therefore, a profit margin shall remain in the company.

The recent judgement in the José Antonio Abellán case

Regarding this matter, we must mention the case of the Spanish journalist and radio broadcaster José Antonio Abellán.
José Antonio Abellán has been recently acquitted by *Audiencia Nacional* of the payment of nearly € 2 million to the STA, due to the lawsuit maintained for his personal income tax regarding the 2006, 2007 and 2008 tax years.[7] During that period, he invoiced his services to COPE radio channel, amongst others, through a company called Power Media, SL., from which he was the sole administrator and shareholder.

Following the prosecution of this type of companies, especially when it comes to entertainers and sportspersons, the STA reviewed his personal income tax return from 2006 to 2008. Their investigations were mainly focused on the alleged non-existence of human and material resources in Power Media SL and the consideration of the company as an artificial instrument implanted to reduce the taxes to be paid. Also, the involvement of the company´s main shareholder was considered by the STA as the essential element of those services, which consisted of direction, production and presentation of radio shows and collaborations in the sports press. Thus, they considered that most of the amounts received by the company corresponded to the participation of the journalist himself.

According to STA conclusions, the income obtained by Power Media SL and invoiced by José Antonio Abellán should be reclassified as labor income and, consequently, allocated into the journalist´s personal income tax return, without any deductible expense.

As a result of the above, the STA required Jose Antonio

5 Available at www.agenciatributaria.es/static_files/AEAT/Contenidos_Comunes/La_Agencia_Tributaria/Segmentos_Usuarios/Empresas_y_profesionales/Foro_grandes_empresas/Criterios_generales/Consideraciones_entida_merc.pdf (accessed 1 June 2021).

6 Translation by the authors.

7 Audiencia Nacional no. 556/2021; 12 February 2021, application no. 463/2017.

Abellán to pay around € 2 million of personal income tax and, in return, a reimburse of nearly € 1 million derived from Power Media´s corporate income tax, due to the allocation of the income in the journalist's personal income tax return. It means that the STA refund the corporate income tax and, at the same time, require that the taxpayer bears the tax liabilities under the personal income tax. Nevertheless, the Audiencia Nacional has accepted the journalist's defence arguments, as we explain below.

Abellán's defence stated that, in 2006, the company has enough human resources to develop its activity with both labour and commercial contracts and sufficient material resources, consisting of an office and two recording studios. In fact, the STA itself distinguished two types of income: income from services in which the involvement of Abellán and his personal qualities are required, and income from other services in which that intervention is not essential.[8] As an example, the STA recognized that, in the musical programme broadcast for COPE, there was no personal or any other intervention, because the programme was performed by a robot, although such robot required the permanent assistance of one or two professionals.

The STA also affirmed that, regarding the contracts in which the personal intervention of José Antonio Abellán is required, if the journalist himself is not computed, Power Media SL has not justified that it had sufficient or adequate personal resources to provide the contracted services. But, according to the *Audiencia Nacional*, it is not possible to value separately the activity carried out by the company and the activity carried out by the individual in favour of Power Media SL. In essence, if it is proven that Power Media has material and personal resources, it has them to all effects and purposes, regardless of the involvement of Abellán in a specific activity.

As a result, the *Audiencia Nacional* considered that it has been proven that the company has the material and personal means to carry out its economic activity, and that such activities had a real economic content, independent of the professional activity of the sole administrator. Consequently, the court accepted Abellán's application and cancelled the personal income tax and company tax assessments from the STA.

Another favourable judgement

In this sense, we could also highlight the María Teresa Campos (a journalist and famous broadcaster) case,[9] who invoiced services through her company Producciones Lucam SL.

Similar to Abellán's case, she litigated with the STA and Administrative Courts and the *Audiencia Nacional* admitted the existence of human and material resources in her company.

Her arguments were that Producciones Lucam SL had hired several people as scriptwriter, logistics assistant, assistant editor, assistant director, hairdresser, make-up artist and driver. As for the material means, the company had the domicile of the activity, supplies associated with the activity, various professional services, and elements of the tangible fixed assets.

Regarding Producciones Lucam's contracts and services, it earned most of its revenues from television production companies. In particular, the services provided to one of their main clients, called Europroducciones, corresponded to the direction of programmes that were not instructed or presented personally by María Teresa Campos.

In the end, the services rendered by the company, which consisted of the presentation and direction of some programmes, were contracted without requiring the presence and personal intervention of María Teresa Campos.

In addition, the court concluded that the length of the programme (two hours per day, five times per week) makes materially impossible for a single person to render that service on their own. The argument is clear: to create the content of a programme, write the scripts and direct you need many professionals, and it is not enough with the sole intervention of the broadcaster.

Conclusions

- The STA, during the last years, is considering the companies of professional services as a mere instrument to avoid taxes by applying the corporate income tax instance of the personal income tax. This is also applicable to sports persons that have implemented structures to exploit their image rights.

- In order to avoid the application of the STA criteria that allocate all the amounts in the personal income tax of the individual, it is essential that:

  - the company has the adequate human and material resources;
  - all the income of the company should not be directly related with services exclusively rendered by the individual;
  - it is not possible to separately value the activity carried out by the human resources of the company and the activity carried out by the individual;
  - it is essential to analyze if the company only provides services to a sole entity or to others, which would advise about the value added of the company;
  - finally, it is quite relevant to examine if the individual always provides services to third parties, and what is the specific scope of such services.

- As a general conclusion, a case by case analysis shall be made, taking into account the specific industry and involvement of the activity and the individual in each transaction.

8 Audiencia Nacional no. 52/2021; 4 January 2021; application no. 1092/2017.

9 Audiencia Nacional no. 83/2017; 9 February 2017; application 1/2015.