

Tax Remark

The National Court of Appeal recognises the tax exempt status of senior executive redundancy pay

21 May 2017

Reflecting the judgment of the Employment Division of the Supreme Court of 22 April 2014, which declared this type of compensation compulsory

The recent judgment of the National Court of Appeal of 8 March 2017 upholds the appeal brought by a company and cancels the tax charge and penalty for Income Tax withholding imposed by the Tax Inspectorate - which had considered redundancy pay of senior executives to be subject to Income Tax - in line with the new doctrine of the Supreme Court which holds that the compensation laid down in article 11 of Royal Decree 1382/1985 is a compulsory minimum.

This new ruling constitutes a radical change in respect of previous decisions of the administrative law courts, which had held that the compensation provided for under article 11 for redundancy of senior executives was supplementary to what was agreed in the contract rather than a minimum, and that the exemption in article 7.e) of the Income Tax Act was therefore not applicable.

The General Tax Directorate ruled on the same question two years ago in Binding Consultation number V1965-15 after the publication of the Supreme Court decision. In it the person making the consultation makes express reference to the decision, but the Directorate thought the approach it was taking remained correct and thus ruled that compensation of senior executives was not exempt.

Despite the judgment of the National Court of Appeal, the tax authorities and the administrative law courts will presumably follow the view of the Tax Directorate, which is binding on them, but there is the possibility of challenging tax rulings on compensation from years for which the limitation period has not expired, and of challenging future rulings. It would however be necessary for the taxpayer to go to court to obtain a favorable ruling, with all the drawbacks in terms of cost and time which that involves.

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