GARRIGUES

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In Royal Decree-Law 20/2012, of July 13, 2012, the Government finally approved the expected increase in the standard and reduced value added tax (VAT) rates (with the VAT rate charged on certain goods and services also being increased from the reduced rate to the standard rate) which is set to apply from September 1, 2012.

Apart from this relevant change, the Royal Decree-Law also contains other measures of a tax nature. In the corporate income tax area, some of the measures already approved in earlier Royal Decree-Laws (affecting tax prepayments, the offset of tax losses, and the deductibility of finance costs and of the amortization charged on intangible assets having an indefinite useful life) have been further restricted. In the personal income tax area, the withholding tax rate applying to income from economic activities has been increased while the tax relief relating to tax credits for taxpayers who bought their principal residence before January 20, 2006 has been eliminated.

Royal Decree-Law 20/2012 has also introduced a new 10% tax on foreign-source income in cases that do not meet the requirements for applying the special 8% tax recently introduced for the same kind of income.

We would also highlight the new developments that have also taken place in relation to the so-called "tax amnesty" regulated by Royal Decree-Law 12/2012 (as amended by Royal Decree-Law 19/2012) and implemented by Order HAP/1182/2012, following the report published by the Directorate-General of Taxes ("DGT") on its criteria for interpreting this special tax regularization exercise.

One of these criteria is that the rationale behind the "tax amnesty" legislation is that taxpayers can regularize unreported income and/or gains; accordingly, the regularization of spent bank account balances must be permitted, although regularization must be limited to the portion of the assets acquired with income and/or gains not yet statute-barred.

The DGT also argues that the special tax return and the traditional method for regularization are compatible and can be used simultaneously by the same taxpayer.

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1. JUDGMENTS

1.1 Corporate income tax.- Tax credit for reinvestment of extraordinary income does not apply to contribution of real estate to newly-formed company (Supreme Court judgment of June 4, 2012)

The Supreme Court held that a tax credit for reinvestment of extraordinary income could not be taken on the transfer of a property to a newly-formed company that was wholly owned by the transferor, on the ground that there had been no real investment, as the transferor obtained nothing in exchange for the contribution other than what it already had. Before the contribution the transferor was the owner of the property, and following the contribution the transferor owned 100% of a company whose sole asset was, precisely, that property. Moreover, the two companies shared the same corporate purpose, registered office and sole director.

The Court also noted, citing, among others, its judgment of April 30, 2012, that (as a general rule) reinvestment by subscribing for shares in an asset-holding company cannot give rise to the tax credit. In this respect, the Court stated that it was unreasonable to require, in the case of reinvestment in property, plant and equipment or intangible assets, that these be used for economic activities, while in the case of reinvestment in securities representing an interest in the capital or equity of entities it is irrelevant whether or not the entities pursue economic activities.

1.2 Personal income tax.- Concerning reservation of right to purchase real estate assets of a company whose shares are transferred (National Appellate Court judgment of May 30, 2012)

The owners of company A (individuals) signed an agreement whereby they sold their shares in company A for a cash price to company B. In the sale agreement, company B gave a commitment to sell the real estate assets of the acquired company (company A) to certain family companies (companies C) of the sellers for a set price.

The tax inspectors considered that:

- This was one single complex legal transaction in which a sale of shares was agreed and a commitment to sell the acquired company's real estate was established. It should, therefore, be characterized as a swap, since the price obtained by the transferors from the sale of the shares in company A included (i) not only the cash consideration received for the shares sold, but also (ii) a right for the companies owned by them (companies C) to acquire the real estate assets of company A at (what later proved to be) a below-market price.

- The swap should have been priced pursuant to the rules on related-party transactions, since the transferors of the shares and the beneficiaries of the above-mentioned right to purchase the real estate assets were, in effect, the same persons (the transferors saw the value of their companies C appreciate by virtue of the fact that the latter were able to acquire the real estate at below-market prices).

- Accordingly, the transferors obtained a capital gain that should have been calculated, not only taking into account the cash consideration received but also the value of the right to purchase the real estate assets. However, to calculate that value, the tax inspectors did not use the value of companies C (i.e. the holders of the right to purchase the real estate assets), but rather the value of company A. Thus, what the tax inspectors did was to:

  - take the market value of the real estate assets at the time of their sale by company A to companies C;

  - subtract the net worth of company A and the capital gain reported by it on the sale of the real estate assets from that market value;

  - treat the difference as an increase in value received by the transferors on the sale of company A (since, in reality, what was received by them was the right to acquire in the future the real estate assets at a below-market price).

The National Appellate Court noted, first, that the underlying element in the transaction was the intention of the purchaser to acquire the economic activities of a company (company A) rather than its real estate assets, hence the purchaser's commitment to sell the real estate assets at a price that was lower than the market price, but higher than their previous book value.

The Court then stated that this was not a related-party transaction, since the party giving the commitment to sell the real estate assets (company B) and the beneficiaries of that commitment (companies C, belonging to the transferors of company A) were independent parties.

Lastly, the Court concluded that, in any case, the assessments should be set aside because, even if the transferors had obtained a taxable gain, the valuation made by the tax inspectors was incorrect, because they valued the real estate assets or, ultimately, company A instead of the increase in value of the family companies (companies C), an approach that was contradictory.

1.3 VAT.- Legal and financial advisory expenses borne by an entity for which a tender offer is made are part of its general expenses and the input VAT thereon can therefore be deducted (National Appellate Court judgment of May 10, 2012)

A tender offer was made for an entity which, as a result, had borne certain expenses relating to the attendant financial and legal advice, deducting the input VAT thereon.

The tax inspectors and the Central Economic-Administrative Tribunal ("TEAC") disallowed the deduction of the input VAT on the ground that from the standpoint of the target entity, a mere change of shareholders could not represent a benefit for its economic activity; in the view of the tax authorities, that benefit corresponded, instead, to the company making the tender offer.

The National Appellate Court disagreed, concluding, on the basis of European Court of Justice (ECJ) case law, that a tender offer for an entity may be understood to benefit the economic activity of that entity, and that therefore the cost of the services indicated may reasonably be borne by it. Accordingly, the input VAT charged on the relevant fees was tax deductible by that entity.

1.4 Tax on large retail outlets (Cataluña).- Compatibility with tax on economic activities (Constitutional Court judgment of June 5, 2012)

In 2001 an appeal was filed against Large Retail Outlet Tax ("IGEC") Law 16/2000, of December 29, 2000, enacted by the Cataluña Parliament on the ground that it was unconstitutional because: (i) it infringed article 6.3 of the Autonomous Community Financing Organic Law ("LOFCA") as worded originally (prohibition against autonomous community taxes encroaching on the revenue-raising powers reserved to local authorities); (ii) it was levied on the same taxable event as that for the local tax on economic activities ("IAE"); and (iii), in the alternative, it also constituted double taxation as real estate tax ("IBI") was also being charged where the owner of the large retail outlet was also the owner of the property.

Subsequent to the appeal being filed, article 6.3 LOFCA was amended and the above-mentioned prohibition was lifted. For that reason, based on settled Constitutional Court case law, whereby in appeals for unconstitutionality the statute in question must be judged according to the constitutional body of laws as it stands when the appeal is decided upon, even the Government Lawyer considered that the rationale for the appeal had been lost. However, counsel for the Cataluña Autonomous Community Parliament and Government argued that a ruling was needed to address the issue of double taxation under IAE and IBI.

The Constitutional Court held that IGEC is compatible with both IAE and IBI and underlined, among other things, that IGEC has an additional fiscal purpose (at least in part) that it does not share with the others.

Moreover, after comparing the taxable event and the quantitative elements of IAE and IGEC, the Court concluded that they are two different taxes: (i) a general tax (IAE), which is levied on the mere pursuit of economic activities of all kinds and taxes the potential profits to be obtained from the pursuit of such activities; and (ii) a specific tax (IGEC), which is levied only on certain retail activities, i.e. those carried on by individual large retail outlets that sell certain products and organize their business in a way that differentiates them from other retail activities, not on the basis of purely internal organizational aspects but as a result of their impact on consumption, territorial planning and the environment.

The judgment does not enter into a detailed analysis of the differences between IGEC and IBI, but it does conclude that they are not incompatible, since the person liable for IGEC is the owner of the individual large retail outlet and not the owner of the property (which is liable for IBI).

1.5 Valuation review procedures.- Sufficient reasoning by the tax authorities in real estate valuations (Castilla-León High Court judgment of April 9, 2012; Galicia High Court judgment of March 26, 2012)

Both judgments analyze the requirements that real estate valuations by the tax authorities must satisfy in order to be considered sufficiently reasoned. In keeping with the line taken by the Supreme Court, both Chambers held that the key element of valuations, especially when the reported value is modified, is a reasoned and detailed explanation of the factors that are responsible for the modification, with particular reference to the specific case at hand.

In the first judgment, the Castilla-León High Court dismissed the appeal filed by the taxpayer on the ground that the reasoning set forth in the tax assessment was sufficient and consistent, since in that case: (i) the land and construction valuation modules updated for each year and the tables used to obtain the coefficients applied were correctly indicated; (ii) it was stated that there had been an onsite inspection of the property; and (iii) the characteristics ascribed to the property were described.

This conclusion was reached, albeit recognizing that generally accepted explanations had been used, since the valuation reflected, overall, that regard had been had to the specific features of the property. For these purposes, the Chamber considered that the important point was that such general explanations reflected reality, and for that to be the case physical or objective data were needed to justify the use of such classifications, data which could only be obtained by means of an onsite inspection (or by submission of the specific documents and data used, in order to justify that such inspection was not necessary). This was a requirement which, in the view of the Court, had been satisfied in the case at hand (as an onsite inspection had been made).

In the second judgment, the Galicia High Court, applying the same criterion, upheld the appeal filed by the taxpayer, precisely because an onsite inspection was needed in order to value real estate and in this case no such inspection had been made. The High Court also ruled that the use of comparable prices (i.e., prices offered in other transactions in real estate deemed to be similar) was not the correct way to determine market value, as there was an underlying real-world transaction that might or might not result in a final price, depending on supply and demand, but there was no transactional basis for using the prices offered to determine market value.

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2. DECISIONS AND RULINGS

2.1 Corporate income tax.– Net revenues used to determine prepayments and tax losses of a tax group will be net revenues of that group (Directorate-General of Taxes. Ruling V1154-12 of May 28, 2012)

Royal Decree-Law 9/2011 made two provisional amendments to corporate income tax for the 2011, 2012 and 2013 fiscal years: the rate to be used to calculate prepayments was raised and limits were placed on the offset of tax losses.

In both cases the impact of the amendments differs depending on the amount of the taxpayer's net revenues. A request was submitted for a ruling on how this figure should be calculated in the case of tax groups.

The DGT ruled as follows:

- It is the tax group (and not the companies that form part of it) that is liable for corporate income tax.
- For that reason, the parent company must prepare, for tax purposes, a balance sheet, an income statement, a statement of changes in equity for the year and a consolidated cash flow statement, applying the full consolidation method to all the companies that form part of the tax group.
- Accordingly, in the case of a tax group, the net revenue figure referred to in Royal Decree-Law 9/2011 must be understood to be the net revenue figure per the tax group's income statement, determined by the full consolidation method, i.e., once the corresponding eliminations have been made, including eliminations of internal transactions and their results.

2.2 Corporate income tax.– Determination of prepayments applicable to enterprises of a reduced size (Directorate-General of Taxes. Ruling V1157-12, of May 28, 2012)

One of the methods for calculating corporate income tax prepayments uses the tax base of the first three, nine or eleven months of each calendar year. The tax rate is applied to that tax base, multiplied (at present, and in general) by five sevenths, i.e., 21% (in the case of the standard rate of 30%).

In the case of enterprises of a reduced size, the tax rate for the first €300,000 of the tax base is 25%; the rest of the tax base is subject to the standard rate of 30%. In consequence, the prepayment rate will be 17% for the initial part of the tax base and 21% for the remainder. A request was submitted for a ruling on how prepayments should be calculated in the case of enterprises of a reduced size that use this system, bearing in mind the tax scale.

The DGT ruled that the part of the tax base to be taxed at 17% (in each prepayment) is that resulting from applying to the sum of €300,000 the proportion that the number of days of the tax period elapsed up to the start of the period for making each prepayment bears to 365 days.

2.3 Corporate income tax.– Expense derived from collective layoff deductible when it is authorized, even if authorization not notified to company until following year (Directorate-General of Taxes. Ruling V1092-12, of May 21, 2012)

The case concerned a collective layoff that was authorized by the labor authorities in one year, but the authorization was not notified to the company until the start of the following year. A ruling was specifically requested on which year was the one in which the related severance pay expense should be deductible.

After requesting a report from the Spanish Accounting and Audit Institute ("ICAC"), the DGT ruled as follows:

- The company should, for accounting purposes, recognize a provision or, where appropriate, a specific debt to the workers in the first fiscal year, as the administrative authorization already existed and evidenced the specific commitment to make severance payments.

- The fact that the authorization was not notified until January of the following year had no bearing on this conclusion. Notification of the administrative decision after year-end constituted disclosure of a circumstance that already existed at year-end, i.e., the creation of an obligation, and must be treated as a "subsequent event" for the purpose of preparing the financial statements.

- The expense was, therefore, deductible in the year in which the authorization was granted.

Note that following the recent labor market reform, administrative authorization is no longer needed for collective layoffs.

2.4 VAT: Application for refund of tax paid incorrectly.- Apportionment of burden of proof in applications for refund of VAT paid incorrectly (Central Economic-Administrative Tribunal. Decision of May 24, 2012)

The taxable person in this case applied for a refund of VAT paid incorrectly, pursuant to a judgment of the National Appellate Court that had concluded that certain transactions, on which the taxable person had paid input VAT, were in fact not subject to VAT, and that consequently the tax paid should be refunded to the party that had paid it. The application was rejected by the tax authorities on the ground that the entities that had charged the output VAT had failed to pay it over to the Public Treasury when they filed their self-assessments (i.e., they had reported the output VAT, but as a result of the input/output VAT offset system there was no amount payable under the self-assessments filed).

In light of this rejection, the taxable person filed a monetary claim with the TEAC. In its decision, the TEAC considered that:

- In order to qualify for a refund of VAT incorrectly charged, a number of requirements must be satisfied (apart from the fact that the input VAT must not be deductible):
  - the output VAT must have been charged in an invoice;
  - the output VAT charged must have been paid over to the tax authorities.
  - The input VAT must not have been refunded to the party that paid it or to a third party.
- The burden of proof for fulfillment of each of these requirements lay with the taxable person in some cases and with the tax authorities in others. Thus, the party that paid the output VAT had to prove that it had been charged in an invoice whereas, by virtue of the principle of ease and proximity of evidence, the onus rested with the tax authorities to prove that:
  - The taxable person who charged the output VAT had included it in its self-assessment.
  - The input VAT had been refunded (if the party that paid it denied that this was the case).
- Lastly, the TEAC concluded that the requirement to pay over the output VAT does not imply that there will be an amount payable under the relevant self-assessment; rather, it will be sufficient for the output VAT to be reported in the self-assessment.

2.5 Economic-administrative proceeding.- In expedited proceedings inspection of case file is claimant's right and tax authorities must guarantee exercise of such right if claimant so requests (Central Economic-Administrative Tribunal. Decision of May 10, 2012)

The TEAC analyzed the right of a claimant to inspect the administrative case file where it had filed an economic-administrative claim under an expedited proceeding.

In its decision, rendered as a definitive ruling on the interpretation to be followed, in response to an extraordinary appeal to a higher administrative body [*recurso de alzada*] filed by the Director of the Tax Collection Department of the State Tax Agency (AEAT), the TEAC concluded that:

- In expedited proceedings relating to economic-administrative claims, given the lack of express rules in this respect, it was necessary to apply by analogy the rules on appeals for reconsideration [*recursos de reposición*] (in which, as in expedited proceedings, submissions must be made in the notice of intention to file the claim), concluding that the tax authorities must allow the claimant to inspect the case file upon request.

- For that purpose, the taxpayer must approach the body that rendered the contested administrative decision within the time period allowed for filing an economic-administrative claim, and the tax authorities must allow the taxpayer to inspect the complete case file, placing on record in the file that this has been done.

However, the TEAC warned that if the claimant failed to exercise this right, it could not plead that it had been denied its right to a defense for want of access to the case file. Accordingly, the TEAC recommended that the request by claimants to exercise this right be made in writing, in order to ensure that there was a due record of such request.

3. LEGISLATION

3.1 Royal Decree-Law 20/2012

Royal Decree-Law 20/2012, of July 13, 2012 on Measures to Ensure Budgetary Stability and on Encouraging Competitiveness, was published in the Official State Gazette on July 14, 2012. It contains new tax legislation on a range of taxes which, in some cases, amends or expands on the reforms introduced by Royal Decree-Law 9/2011, Royal Decree-Law 20/2011 and Royal Decree-Law 12/2012, all targeted at reducing the budget deficit. Although we describe the measures in a special newsletter, following is a summary:

- Starting on September 1, the standard and reduced VAT rates will go up from 18% to 21% and from 8% to 10%, respectively. The new legislation has also increased the VAT rate for certain goods and services from the reduced rate to the standard rate.

- In the personal income tax area, starting in 2012, the tax relief relating to the tax credit for acquisition of a principal residence, available for taxpayers who bought their homes before January 20, 2006, is eliminated.

- In the corporate income tax area, large enterprises have temporarily had restrictions placed on their ability to use tax loss carryforwards and have had their tax prepayments increased. Moreover, the maximum annual limit on the deductibility of the amortization expense for intangible assets with an indefinite useful life has been reduced (in general for all taxpayers).

- Some clarifications and explanations have also been provided for the rules on deductible finance costs, which add insurers to the list of enterprises not eligible to deduct these expenses.

- A new special 10% tax on foreign-source income is established (but only up to November 30, 2012), similar to the tax introduced by Royal Decree-Law 12, 2012, albeit with fewer requirements for its application and affecting a larger volume of dividends or the transfer of a larger volume of holdings.

- The rates applicable to tobacco products have also been changed.

3.2 Labor market reform. Personal income tax exemption on severance for dismissal and tax credits for job creation

July 7, 2012 saw the publication in the Official State Gazette of Law 3/2012, of July 6, 2012, on Urgent Measures to Reform the Labor Market, which supersedes Royal Decree-Law 3/2012, of February 10, 2012. The Law entered into force on July 8, 2012.

While the provisions of the Royal Decree-Law remain largely unchanged (for a description of that legislation, see our previous Labor Law Update 3-2012), there are nonetheless certain new developments taxwise, most notably the change in the rules on the tax exemption for severance payments in cases of unjustified dismissal.

Specifically, article 7.e) of the Personal Income Tax Law is amended to eliminate the reference to "fast-track dismissal," that is, to the possibility of claiming the exemption where the employer acknowledges the unjustified nature of the dismissal in the notice of dismissal or at any other time before the conciliation hearing (without needing to attend that hearing). Therefore, following the entry into force of Law 3/2012, the exemption for unjustified dismissal will require employers to at least appear before the conciliation service.

In any case, on a transitional basis, the exemption will still apply to dismissals taking place between the entry into force of Royal Decree-Law 3/2012 (February 12, 2012) and the entry into force of Law 3/2012 (July 8, 2012), even if they take the form of fast-track dismissals.

Moreover, it should not be forgotten that Law 3/2012 also provides for corporate income tax incentives, inserting a new article 43 into the Revised Corporate Income Tax Law, entitled "tax credits for job creation" (also applicable to personal income taxpayers who engage in economic activities, as they are deductions from gross tax payable that can be made by these taxpayers under personal income tax legislation).

These tax credits are basically as follows:

- Entities hiring their first employee under an indefinite-term contract in support of entrepreneurs may deduct €3,000 from their gross tax payable if that employee is under the age of 30.

- Entities with less than 50 workers hiring unemployed persons receiving contributory unemployment benefit under an indefinite-term contract in support of entrepreneurs may deduct 50 percent of the lower of the following amounts from their gross tax payable: (i) any unemployment benefit not yet received by the worker, or (ii) twelve months of the unemployment benefit recognized to the worker.

In a change from the previous wording of the provision after the publication of the Royal Decree-Law, Law 3/2012 adds that the credit can be taken in relation to these contracts until a maximum of 50 workers is reached and on condition that, in the twelve months following the commencement of employment, there is an increase, with respect to each worker, in the total average workforce at the entity of at least one unit compared with the existing workforce in the preceding twelve months.

The right to take this credit is conditional on the hired worker having received unemployment benefit for at least three months prior to the commencement of employment.

Law 3/2012 establishes that the credits will be taken against the gross tax payable for the relevant tax period at the end of the one-year trial period and will be conditional on the employment contract remaining in force for at least three years from its commencement date. A breach of those requirements will imply forfeiture of the credit, and the requirement relating to termination on objective grounds or dismissal on disciplinary grounds will not be deemed to have been breached where one or the other is held or acknowledged to be justified or is the result of the worker's resignation, death, retirement or total permanent, absolute or comprehensive disability.

Lastly, Law 3/2012 adds (as a new aspect that was not in the Royal Decree-Law) that any hired workers giving rise to entitlement to any of the credits under the new article 43 of the Revised Corporate Income Tax Law will not be counted for determining the increase in the workforce for the purpose of accelerated depreciation being charged by enterprises of a reduced size.

3.3 Agreements on timeshares in properties for tourism use

Law 4/2012, of July 6, 2012, on Agreements on Timeshares in Properties for Tourism Use, on Acquisition of Long-Term Vacation Products, on Resale and on Exchanges, and Tax Provisions, was published in the Official State Gazette of July 7, 2012.

Mirroring the amendments already introduced by Royal Decree-Law 8/2012, of March 16, 2012, published in the Official State Gazette of March 17, 2012, Law 4/2012 updates the tax provisions applicable to timeshare rights in immovable properties for tourism use, establishing the following:

- In the wealth tax area, timeshare rights in immovable properties for tourism use will be measured at acquisition cost.

- Transfer and stamp tax will apply at the rate of 4% to assignments between private parties (not subject to VAT or to Canary Islands general indirect tax) of the rights regulated by the Royal Decree-Law, regardless of their nature, subject to the powers of autonomous community governments in this area.

- Lastly, in the VAT area, the 8% rate will be charged on assignments of timeshare rights in buildings, real estate complexes or architecturally differentiated areas of such complexes, where the immovable property comprises at least ten accommodation units.

Law 4/2012 entered into force on July 8, 2012.

3.4 General State Budget Law for 2012

The General State Budget Law for 2012 (summarized in our July bulletin 1-2012) was published in the Official State Gazette of June 30, 2012, and includes the measures usually contained in this type of legislation and having an impact on the main taxes in the tax system, as well as some taxes.

In relation to corporate income tax, as in previous years, the Law raises by 1% the adjustment coefficients applicable to transfers of real estate and regulates the method for calculating corporate income tax prepayments in 2012 (in the latter case, having regard to the changes made by Royal Decree-Law 9/2011, of August 19, 2011). In addition, it reiterates the amendment made by Royal Decree-Law 20/2011 raising the general corporate income tax withholding rate applicable for 2012 and 2013 to 21%.

Regarding personal income tax, the Law maintains for 2011 the tax relief compensating for the change in legislation in 2006 for (i) taxpayers who acquired their principal residence before January 20, 2006, and for (ii) taxpayers who received in 2011 certain income from movable capital accrued over more than two years, in accordance with the provisions of the personal income tax legislation in force up to December 31, 2006. It also reiterates the amendment made by Royal Decree-Law 20/2011 in respect of the supplementary tax charged on top of the central government component of the gross tax payable, applicable in 2012 and 2013, and the calculation of the withholdings and payments on account in those periods. Additionally, as it does every year, the Law raises by 1% the adjustment coefficients applicable to the acquisition cost of real estate assets where they are transferred.

In the nonresident income tax area, the Law extends, subject to certain requirements, the scope of the exemption applicable to income distributed by subsidiaries resident in Spain to their parent companies resident in another EU Member State, to the States of the European Economic Area.

The Law also introduces technical amendments to VAT and to tax on oil and gas, in order to bring Spanish law into line with EU legislation. These amendments include the repeal of the tax on the retail sale of certain oil and gas products and its inclusion in the tax on oil and gas.

Lastly, the stamp tax rates for the transfer and reinstatement of noble titles, in the “administrative documents” category is increased by 1%, as are central government charges, dues and fees;, and the Law declares certain programs to be events of exceptional public interest.

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3.5 Autonomous Community Administrative and Tax Measures Law (Canary Islands)

Autonomous Community Law 4/2012, of June 25, 2012, on Administrative and Tax Measures Law was published in the Official Canary Islands Autonomous Community Gazette of June 26, 2012. The main aim of the Autonomous Community Law is to implement the budget cuts to be made in the Canary Islands following the enactment of the General State Budget Law for 2012. For more details, please see our Canary Island Tax News publication of June 2012.

Below we highlight in any case the key aspects of the above-mentioned Autonomous Community Law:

- Increase in Canary Islands general indirect tax (IGIC) rates: the standard rate rises from 5% to 7%, the reduced rate from 2% to 3%, and the increased rates from 9% to 9.5% and from 13% to 13.5%.

- Elimination of the IGIC-exempt status of telecommunications services, which will now be taxed at the standard rate.

- Introduction of three new autonomous community taxes: (i) on large retail outlets; (ii) on customer deposits at financial institutions in the Canary Islands; and (iii) on certain activities that impact on the environment, specifically electricity and telecommunications distribution networks.

- Increase in the autonomous community component of personal income tax with effect from January 1, 2012, and limitation of the autonomous community personal income tax credits available.

- Elimination, with effect from July 1, 2012, of the 99.9% tax reduction for kinship and for life insurance in cases of transmission "mortis causa", and modification of certain inheritance and gift tax reductions.

- Introduction of new tax rates for supplies of fuel subject to the excise tax on oil-derived fuels.

- Change in the way in which transfer and stamp tax is levied on the sale of used motor vehicles, so that it will now be charged in the form of a flat amount.

- Creation of new charges, dues and fees.

4. MISCELLANEOUS

4.1 Tax regularization: Report from the Directorate-General of Taxes

The DGT has released a report dated June 27, 2012 expanding on its interpretation of certain issues raised about the special tax return (*declaración tributaria especial* or "DTE") (regulated in Royal Decree-Law 12/2012, of March 30, 2012, amended by Royal Decree-Law 19/2012, of May 25, 2012, and implemented by Order HAP/1182/2012, of May 31, 2012). The following observations can be highlighted:

- The nature of the DTE and the effects thereby entailed:

  - The DTE is a tax return but it cannot be used to settle tax obligations pre-dating the taxes it can regularize (personal income tax, corporate income tax and nonresident income tax). The DTE therefore does not toll the limitation period for obligations it can regularize (in relation to the taxes indicated).

  - Likewise, the DTE is not reviewable in isolation, but only if, in a procedure to review tax obligations related to personal income tax, corporate income tax or nonresident income tax, the taxpayer elects to file a DTE.

- The value to be reported: the Royal Decree-Law establishes that, as a general rule, the value to be reported is the acquisition cost of the assets or, in the case of amounts in bank or credit accounts (at the taxpayer's election) the balance at December 31, 2010 (or at such date as is appropriate depending on the tax year) or a higher balance where the difference has not been included in other assets included in the DTE.

  In this connection, the DGT clarifies that:

  - The objective of the Royal Decree-Law is that, through the DTE, unreported income and/or gains not yet statute-barred (i.e., income and/or gains that can yet be reviewed by the tax authorities) can be regularized.

  - Therefore, in the case of amounts held in bank accounts, taxpayers can report the balance that allows them to regularize all of the income. Accordingly, balance withdrawals can be regularized, meaning that a higher amount than the largest balance that existed in the period open to the statute of limitations (which will be equal to the sum of the unreported amounts of income) can be reported.

  - Furthermore, in general, taxpayers can only report the portion of their assets acquired with unreported, non-statute-barred income and/or gains not. However, in the case of assets resulting from successive transfers, the DGT warns that taxpayers must be able to show what portion of the assets existing at December 31, 2010 (or at such date as is appropriate depending on the tax year) has been acquired with non-statute-barred income and/or gains. Otherwise, 10% of their acquisition cost must be reported.

- Lastly, the acquisition cost can be reduced by concealed debts (the existence of which can be evidenced) incurred to acquire the assets included in the DTE (it must also be possible to prove they were incurred for that purpose), less any loan repayments until December 31, 2010 (or such date as is appropriate), with unreported income and/or gains.

- The reporting of cash: The above-mentioned Order establishes that it will be deemed that the cash was held before December 31, 2010 (or such date as is appropriate depending on the tax year) if it is deposited in a certain type of account before the DTE is filed and, in addition, a declaration is made as indicated. The DGT reminds taxpayers that the DTE does not allow cash relating to unreported income and/or gains obtained after the indicated dates to be regularized.

- The immediate effects of the DTE:

  The legislation establishes the following:

  - The filing of the DTE regularizes unreported income and/or gains. The DGT clarifies that income and/or gains that cannot be used to acquired assets reported in the DTE (such as incorrectly deducted expenses) or income and/or gains used to acquire assets not included in the DTE are not regularized.

  - The filing of the DTE results in the acquisition of regularized assets being deemed to relate to reported income and/or gains. This, in the DGT's view, means that they cannot be treated as unjustified gains or imputed income. Furthermore, if such assets are disposed of after the filing of the DTE, the new assets acquired cannot receive such treatment either.

  Lastly, the DGT points out that the tax paid over will not be treated as a deductible expense.

- The future effects of the DTE: The reported value has tax effects. However, certain limitations are established, including where the value is higher than the market value at the date the DTE is filed. In such case, in a future transfer with capital losses, only the amount by which such losses exceed the unrealized loss at that date will be computed. However, the DGT clarifies that if gains are obtained on the future transfer, they will not be increased by such excess amount.

- The impossibility of filing the DTE in the event of verification or investigation: the DGT states that if the verification procedure is finalized before the DTE is filed (and such verification was partial and did conclude with the regularization of aspects of the tax obligation which must be affected by the DTE), the DTE can be filed.

Lastly, the DGT stresses that the DTE and supplementary DTEs must be filed by no later than November 30, 2012 and that payment cannot be deferred or made in installments.

4.2 Denunciation of Spain-Argentina tax treaty

The Argentinean Official Gazette of July 13, 2012 published the formal denunciation of the Spain-Argentina tax treaty that had been in force since July 28, 1994. The tax treaty was denounced on June 29, 2012, which means that if that were the notification date, bearing in mind that the tax treaty itself provides that it may be denounced by either of the contracting states at least six months before the end of any calendar year, the tax treaty would cease to have effect on January 1, 2013.