GARRIGUES

bulletin TAX

8-2012
August-September, 2012

The process of decentralization and of promoting the ability of the municipal and autonomous community authorities to create and define their own taxes has led to the approval of new forms of taxation in recent years. In some cases, this has happened as part of policies to protect the environment and to pass on the negative effects associated with certain activities to those who engage in them, while in others the aim has also clearly been to raise revenues, basically given the current, and now prolonged, adverse economic situation.

These forms of taxation include, most notably, charges for occupying local public land, challenged by cell phone operators against numerous Spanish municipalities in proceedings that have lasted more than 10 years.

On July 12, 2012, the judgment of the European Court of Justice ("ECJ") making a preliminary ruling on a question referred by the Spanish Supreme Court was published. The ECJ upheld the claims of two of the main cell phone operators in Spain in relation to the above-mentioned charges. The question was resolved by direct application of EU law and on terms that almost wholly defeat any attempt by Spanish municipalities to charge cell phone operators which do not own the network installed on local public land, but use it to provide their services. The ECJ has been unequivocal in its ruling on the incompatibility of the charges with the EU Directives forming part of the "Telecommunications Package."

The preliminary ruling illustrates the growing importance of knowing EU law when defending the position of certain economic sectors, as it transcends any legislative issues arising in a domestic context. Thus, the supremacy of EU law and, above all, the possibility it offers to private citizens to invoke its direct application before the national authorities and courts make it an essential tool for defending taxpayers' rights in the tax arena.

CONTENTS

1. JUDGMENTS

1.1 "Exit tax" where residence is transferred to another EU Member State (European Court of Justice. Judgments of June 12, 2012, in Case C-269/09 and September 6, 2012, in Case C-38/10)

The ECJ has held that article 14.3 of Personal Income Tax Law 35/2006 is contrary to European law because it contravenes the freedom of establishment by requiring taxpayers who transfer their residence to another Member State to include, in the tax base for the last tax year in which they were treated as resident taxpayers, any income not yet charged to tax. The Court clarifies that, regardless of whether the income has already accrued, the fact of requiring its recognition in advance when there is a change of residence has an impact on the freedom of establishment, since that rule has financial implications.

Along the same lines, the ECJ has held that a provision of the Portuguese Corporate Income Tax Law is contrary to European law and, in particular, the freedom of establishment. The provision in question imposes an immediate tax on unrealized gains, except for those arising from exclusively domestic transactions, when a Portuguese company moves its registered office or place of effective management to another Member State, or when a permanent establishment in Portugal transfers all or some of its assets to another State.

1.2 Corporate income tax.- Tax authorities cannot review tax losses incurred in statute-barred years and offset in non-statute-barred years (National Appellate Court. Judgment of May 24, 2012)

The courts have been debating, in numerous judgments, the tax authorities' ability to review tax losses offset for corporate income tax purposes in a period that has not yet become statute-barred, but which were incurred in statute-barred years.

In this judgment, which goes against the view taken by the Central Economic-Administrative Tribunal ("TEAC") and follows the interpretation repeatedly adopted by the Supreme Court, the National Appellate Court held that, although the Corporate Income Tax Law requires the taxpayer to "evidence" the "origin and amount" of the tax losses it intends to offset, the principle of the statute of limitations for tax purposes is unalterable. Thus, the taxpayer need only keep the documentary and/or accounting support enabling the tax authorities to confirm the existence of the tax loss carryforwards and the correlation between the amount offset in the year not yet statute-barred and that incurred in the statute-barred period.

Along those lines, we can mention the Supreme Court judgments of July 8, 2010, March 8, 2012 or March 29, 2012, in which the Court took this same view in relation to the legislation in force before the commencement of Law 40/1998.

What is groundbreaking about the judgment discussed here is that, according to the National Appellate Court, even though there is not yet any Supreme Court case law on this issue in relation to the periods in which Law 40/1998 already applied, the Supreme Court judgments dealing with it in the context of the corporate income tax legislation previously in force must be deemed to also apply to subsequent periods.

The National Appellate Court stated that to interpret otherwise would be to undermine the purpose of the principle of the statute of limitations (a circumstance which does not appear to have been parliament's intention) and would place the tax authorities at an advantage with respect to the taxpayer, since they would be able to verify the amount of the tax base assessed beyond the limitation period, but the taxpayer would not be able to correct any errors detected in its tax returns for statute-barred years, even though they might affect tax losses offsettable in the future.

1.3 Personal income tax.- Method for recognizing installment sale transactions requires prior express schedule of payments identifying when they become due and payable (National Appellate Court. Judgment of May 23, 2012)

In the case at hand, there was a sale of shares with a deferral of the payment of the price so that the buyer was allowed to pay off the debt within a maximum of 12 years (there was no minimum period). Within that maximum period, the buyer could freely make such payments as he saw fit.

The seller sought to apply the special tax treatment established in the Personal Income Tax Law for installment sale transactions (thus, recognizing revenues in proportion to payments collected). In what might be regarded as an excessively restrictive stance (upheld by the National Appellate Court in this judgment) the tax authorities argued that this treatment did not apply, because:

- the contract did not stipulate a specific rule on when outstanding amounts became due and payable, as it was left to the buyer's discretion to decide on the method, amount and date of the payments, within a maximum time period, thereby contravening the provisions of articles 1115 and 1125 of the Civil Code, which prohibit the performance of contracts being left to the discretion of only one of the parties and render null and void any obligation the fulfillment of which depends on the exclusive discretion of the obligor;

- the application of the installment method of revenue recognition must be construed restrictively (given its status as tax relief), and be limited to cases in which (i) the dates of the successive payments are determined and, simultaneously, (ii) the period between the date on which the transferred asset is delivered or made available and the due date of the last installment exceeds one year.

1.4 VAT.- Six-month time period for applying for refund of input VAT paid by nonresidents is a mandatory time limit (European Court of Justice. Judgment of June 21, 2012 in Case C-294/11)

In a question referred for preliminary ruling by the ECJ, the Italian *Corte Suprema di Cassazione* asked whether the time period established in the first subparagraph of article 7(1) of the Eighth VAT Directive for taxable persons not established in the country to submit an application for a refund of VAT was a mandatory time limit.

The ECJ confirmed that it was indeed a mandatory time limit even though some language versions of article 7(1), including the Spanish, might give rise to doubts as to its nature.

1.5 VAT.- Portfolio management service that includes taking decisions on securities purchases and sales and implementing those decisions is not VAT exempt (European Court of Justice. Judgment of June 21, 2012, in Case C-44/11)

A reference for a preliminary ruling was lodged with the ECJ as to whether a portfolio management service (provided by banks), in which the service provider decided which securities to purchase and sell and implemented those decisions, was exempt from VAT. The client paid a fee which had two components: on the one hand, a share for asset management amounting to a percentage of the value of the managed assets and, on the other, a share for buying and selling securities amounting to a percentage of the value of the assets.

The Court held that, in this case, there was a *single supply* (as opposed to two supplies consisting of a principal service and an ancillary service) consisting of the management of securities-based assets, a service which is not exempt from VAT, in accordance with article 135(1)(f) and (g) of the Directive.

In this regard, the Court stated that (i) article 135(1)(g) refers to the management of special investment funds, services which, as has been held by the Court on other occasions, are only those which are specific to the business of undertakings for collective investment, which is why that exemption cannot apply in this case; and (ii) article 135(1)(f) refers to transactions in securities on the market in marketable securities, that is, transactions which are liable to create, alter or extinguish parties' rights and obligations in respect of securities, but in this case, a service of analyzing and monitoring assets (apart from the service of actually purchasing and selling securities) is also provided, thereby precluding the application of the exemption.

1.6 VAT.- Input VAT on part of a capital item used temporarily for private purposes (European Court of Justice. Judgment of June 21, 2012 in Case C-334/10)

The ECJ analyzed the deductibility of the input VAT paid on permanent alterations—installation of dormer windows and a vestibule—made to a capital item, specifically a warehouse, bearing in mind that part of the capital item was first used for private purposes.

The Court held that the fact that the assets acquired for a business are not used immediately for that activity cannot affect the right to deduct input VAT, something which is, moreover, consistent with the principle of fiscal neutrality which forms an integral part of the common system of VAT.

1.7 VAT.- Right to deduct input VAT cannot be refused just because issuer of invoice has committed irregularities, without proof that party seeking to deduct the VAT was aware of them (European Court of Justice. Judgment of June 21, 2012 in joined Cases C-80/11 and C-142/11)

The tax inspectors in this case refused an entity the right to deduct input VAT because the issuer of the invoice had committed irregularities in recording and assessing VATs. Their refusal was based on the idea that the recipient of the invoices ought to have been aware of the fraud committed by the issuer and should have gathered additional information to justify that the invoice issuer, or another trader of the chain of supply, had acted with due diligence.

The ECJ held that a practice of refusing the right to deduct VAT by virtue of the fact that the issuer of the invoice, or another trader of the chain of supply, commits irregularities is contrary to European law, if the competent authority does not prove that the taxable person was aware of that circumstance. The burden of proof, in this case, lies with the tax authorities.

In this regard, the Court added that traders who take every precaution which could reasonably be required of them to ensure that their transactions are not connected with fraud (invoice, delivery note for goods, etc.) must be able to rely on the legality of those transactions without the risk of losing their right to deduct the input VAT, and the tax authorities cannot require the taxable person to check that the issuer of the invoice had sufficient resources to conduct its business or that it had satisfied its obligations regarding declaration and payment of VAT.

Accordingly, the Court concluded that the only precaution that may be required of a taxable person receiving an invoice is precisely to be in possession of that invoice (as a document evidencing its deduction of VAT) and that no additional documentation is necessary.

1.8 Transfer and stamp tax.- Capital duty self-assessment must be filed even though capital increases are exempt (Madrid High Court. Judgment of June 6, 2012)

Royal Decree-Law 13/2010 established an exemption from transfer tax under the "corporate transactions" heading (i.e., capital duty) for company formations, capital increases, shareholder contributions and transfers to Spain of the place of effective management or the registered office of a foreign company not resident in the EU.

After that legislative amendment, the Directorate-General of Registries and the Notarial Profession at the Ministry of Justice issued a Direction on July 11, 2011, stating that in order to streamline and reduce existing bureaucracy, a capital duty (exempt) self-

assessment did not need to be filed in order for the above-mentioned transactions to be evaluated and registered at the Commercial Registry.

However, in this judgment, the Madrid High Court set aside that Direction as a matter of law on the ground that the above-mentioned simplification of the duty to file a self-assessment contravened the terms of article 54.1 of the Revised Transfer and Stamp Tax Law, which provides that all acts subject to capital duty, exempt or otherwise, cannot be afforded access to any public registry without proof of payment of the tax debt or its exemption having been reported.

1.9 Collection proceeding.- Late payment of self-assessed tax cannot trigger surcharge if self-assessment was filed on time (National Appellate Court. Judgment of April 4, 2012)

The appellant filed a VAT self-assessment within the voluntary filing period but did not pay the tax debt. The tax authorities considered that as the payment had not been made on time, the late-filing surcharge was applicable.

However, the National Appellate Court set aside the surcharge on the ground that the essential pre-condition for the surcharge (i.e., the late filing of a self-assessment) did not exist in this case.

1.10 Tax characterization.- Finding of existence of fraud not appropriate in years after those in which the transaction deemed to have been performed as fraud upon law took place (National Appellate Court. Judgment of July 24, 2012)

The tax authorities have been issuing numerous corporate income tax assessments following a finding of the existence of fraud, in relation to certain financing structures. Specifically, in the case analyzed in this judgment, the inspectors had questioned the deductibility of interest accrued on intra-group loans obtained by the claimant, a Spanish entity, to acquire holdings in other entities belonging to the same corporate group. The tax inspection related to corporate income tax for fiscal years 2001 to 2004, although the acquisition and financing transactions had taken place in earlier years. It so happened that the inspectors had already conducted corporate income tax inspections of those earlier years without having specifically questioned the transactions.

The Court accepted the claimant's argument applying the "doctrine of estoppel" to the tax authorities' acts, in that, if the tax authorities had not found the existence of fraud in the previous inspections, it was not lawful for them to do so in later inspections, as that would be contrary to "various essential legal principles, such as those of good faith, legal certainty and respect for legitimate expectations."

Moreover, the Court held that legal acts, transactions or operations cannot be deemed fraudulent, for the purpose of taxing them, when they have been arranged in different periods preceding those to which the finding of fraud relates (in other words, according to this interpretation and notwithstanding the necessary caveats given the particularities of this specific case, it would seem inappropriate to make a finding of fraud upon the law in relation to transactions carried out in statute-barred years).

1.11 Charges.- Charge for the special use of local public land by cell phone companies that do not own the networks is contrary to European Law (European Court of Justice. Judgment of July 12, 2012, in Joined Cases C-55/11, C-57/11 and C-58/11)

The Spanish Supreme Court referred several questions to the ECJ for a preliminary ruling in relation to the charges created by various Spanish municipal councils on the special use of local public land by cell phone service providers. These charges are levied on both the proprietors of the facilities needed to provide the services and on service providers using non-proprietary facilities.

The Court held that a charge on rights to install facilities on public or private property (or above or below it) to proprietors that use them to provide cell phone services without owning those facilities, is contrary to Directive 2002/20/EC of the European Parliament and of the Council of 7 March 2002, on the authorization of electronic communications networks and services.

The Court added that the Directive has direct effect, meaning that private citizens can invoke it directly before national courts.

2. DECISIONS AND RULINGS

2.1 Corporate income tax – Tax treatment of implicit interest in deferred price transaction without interest (Directorate-General of Taxes. Ruling V1674-12, of July 31, 2012)

This ruling analyzed a share acquisition in which part of the price was deferred. The deferred part of the price would be payable in seven annual installments, and it was stipulated that no interest would accrue as a result of the deferral.

The Directorate-General of Taxes ("DGT") recalled that under accounting legislation, the purchaser must account for the debt associated with the purchase of shares at the agreed sale price, excluding the interest included in the nominal value, which must be recognized as an expense (income for the recipient) in the year in which it accrues, having regard to a time/proportion method, until the maturity date of the transaction.

Based on these accounting considerations, the DGT ruled that from a tax standpoint:

- The finance cost relating to interest would be tax deductible, subject to the limitation in article 20 of the Revised Corporate Income Tax Law ("TRLIS") as amended by Royal Decree-Law 12/2012.

- The accrued interest would be subject to withholding tax when it fell due, which, in the case analyzed, would be determined by the due date of each of the installments established by the parties.

2.2 Corporate income tax.- Time limit on offset of losses does not apply in fiscal year in which company is dissolved and liquidated (Directorate-General of Taxes. Ruling V1583-12, of July 19, 2012)

Royal Decree-Law 9/2011 restricted the right to offset tax losses in 2011, 2012 and 2013 in the case of taxpayers whose volume of transactions exceeded €6 million in the twelve preceding months. The aim of that measure, according to the Preamble to the Royal Decree-Law, was to bring forward tax revenues without increasing the tax burden. That limit was subsequently modified by Royal Decree-Law 20/2012 for 2012 and 2013.

This ruling analyzed the case of the liquidation of an entity in one of the years in which the restriction applied. The application of the restriction to the company being liquidated meant an actual increase in the tax burden, since when the company ceased to exist, it would forfeit the right to offset its tax losses in the future.

Given this scenario, the DGT concluded that based on an inclusive and reasonable interpretation of the Royal Decree-Law, this restriction should not apply in the tax period in which the company ceases to exist.

2.3 Corporate income tax.– Cooperatives cannot apply reduced rates for reduced-size enterprises to noncooperative earnings (Directorate-General of Taxes. Ruling V1510-12, of July 12, 2012)

Tax-protected cooperatives enjoy a special tax treatment that permits them, in accordance with article 28.3 TRLIS, to be taxed at a reduced rate of 20%, except for noncooperative earnings, which are taxed at the standard rate.

In response to the question of whether noncooperative earnings could qualify for the 25% rate envisaged for enterprises of a reduced size if the requirements are met, the DGT ruled that they could not. Article 114 TRLIS provides for the application of the reduced rate to entities that meet the requirements in article 108 TRLIS unless, pursuant to article 28, they are subject to a tax rate other than the standard rate, as in the case of specially protected cooperatives.

2.4 Corporate income tax.– Loss incurred from sale of shares repurchased on same day is deductible, provided shares not sold under a repurchase agreement (Directorate-General of Taxes. Ruling V1506-12, of July 10, 2012)

A share portfolio was sold at a loss, and on the same day and at the same time, the same shares were purchased for the same price. Accordingly, a ruling was requested on the deductibility of the loss for corporate income tax purposes.

The DGT stated that, given that the law does not establish any specific rule on the sale of shares and their purchase on the same day, the provisions of the Spanish National Chart of Accounts ("PGC") will apply, according to which, in order to derecognize a financial asset, the risks and benefits inherent in its ownership must have been transferred substantially, something that will not occur in cases such as factoring with recourse, sales

under repurchase agreements or transfers where the seller substantially retains the risks or benefits.

Where those circumstances are not present, the loss included in book income will be treated as a tax deductible expense, since there is no specific provision establishing otherwise.

2.5 Corporate income tax.- Directors' fees only deductible if recognized for accounting purposes in income statement as expense (Central Economic-Administrative Tribunal. Decision of June 26, 2012)

A company paid fees to its directors but did not account for them as an expense but rather as an income distribution. Thus, the fees were deducted by means of a negative adjustment to the corporate income tax base.

The tax inspectors eliminated the adjustment made by the company on the ground that corporate income tax legislation contains no provision permitting such a nonaccounting adjustment. The TEAC confirmed this interpretation and stated that according to corporate income tax legislation, only expenses that have been recognized for accounting purposes in the income statement will be deductible, save for certain legislative exceptions, which do not include directors' fees.

In this connection, we would highlight that one of the claimant's arguments was that the inspectors, in the exercise of their powers, should have corrected the accounting records to allow the deductibility of the expense, on the understanding that such power of the inspectors should operate for the benefit of both government and citizens. Despite the reasonableness of this argument, the TEAC concluded that such a modification of the accounting records would contravene the principle of legality: given that the company had treated the amount paid as remuneration for equity rather than as an expense, the law does not permit the tax inspectors to record it as an expense.

2.6 Corporate income tax.– In unrestricted depreciation/amortization, the depreciation/amortization recorded is the minimum limit (Directorate-General of Taxes. Ruling V1301-12, of June 15, 2012)

The DGT rejected the possibility of charging decelerated depreciation/amortization, that is, by making positive nonaccounting adjustments for the amount of depreciation/amortization recorded in order to recognize it in later fiscal years.

Based on the deductibility under article 11.1 TRLIS of amounts that relate to the actual impairment suffered by assets due to operation, use, enjoyment or obsolescence, the DGT ruled that the depreciation/amortization for accounting purposes will be deductible as long as the requirements in the applicable legislation are met, although there is no provision permitting taxpayers to elect not to deduct that expense. Thus, when charging unrestricted depreciation, regard will always be had to the depreciation/amortization recorded as minimum depreciation/amortization for tax purposes.

2.7 Corporate income tax.– Adjustments to reserves resulting from first-time application of PGC will be taken into account when calculating double taxation tax credit provided for in article 30.5 TRLIS (Directorate-General of Taxes. Ruling V1287-12, of June 14, 2012)

Article 30.5 TRLIS regulates the tax credit for avoidance of double taxation of capital gains from the transfer of holdings, which is calculated by applying the tax rate to the net increase in undistributed income.

In the case on which a ruling was requested, the company's reserves were affected as a consequence of the debits and credits resulting from the first-time application of the PGC, which were characterized as revenues and expenses to be included in the tax base for the 2008 fiscal year, which is when the first-time application took place.

Considering that the balancing entries for the adjustments to be made to fulfill the requirements of the first-time application of the PGC are in a reserve account, the decrease (or increase) in reserves must be taken into account in determining the base of the tax credit under article 30.5 TRLIS.

2.8 Personal income tax.– In installment sale or deferred-price transactions, change in period when price becomes due and payable will not affect initial time schedule for recognition for tax purposes of capital gain or loss (Directorate-General of Taxes. Ruling V1484-12, of July 10, 2012)

In installment sale or deferred price transactions, the taxpayer can elect to recognize the income obtained as and when the relevant amounts to be collected become due and payable.

The DGT analyzed a transaction in which part of the price was deferred for three months and another for thirteen months; after the first period had elapsed without the debtor having been able to make the first payment, both parties signed a new agreement to extend the period for repayment of the total agreed price until a later date, due to the purchaser's inability to pay by the deadlines initially agreed.

The DGT concluded that electing to apply this special rule on timing of recognition means that the capital gain or loss obtained must be recognized as and when the amounts to be collected under the terms of the deferral become due and payable, without this being affected by the new deferral agreed on due to the purchaser's inability to pay.

2.9 Value added tax.- Late charging of VAT is no bar on its deductibility (Central Economic-Administrative Tribunal. Decision of June 21, 2012)

A party contributing a building to a company took the view at the time of the contribution that the transaction was not subject to VAT. Later, the parties making and receiving the contribution realized that the transaction *was* subject to VAT, so the contributing party issued an invoice, charged the related VAT and the company that received the building deducted that VAT in its VAT return.

The tax inspectors disallowed the deduction of the input VAT on the ground that it had been incorrectly charged, given that it was charged more than one year after the contribution of the building (the tax point).

However, the TEAC confirmed the deductibility of the input VAT, in accordance with the Supreme Court judgments of March 18, 2009 and December 5, 2011. In those judgments, the Supreme Court concluded that the aim of the rule which places a time limit on the charging of VAT is to protect the taxable person who pays it, but does not prohibit charging the VAT after that period has elapsed. Thus, the input VAT will be deductible if the party to be charged it decides to voluntarily pay, even if it is charged late.

3. LEGISLATION

3.1 Corporate Income Tax Regulations amended by new Collective Investment Undertaking Regulations

Royal Decree 1082/2012, of July 13, 2012, approving the Regulations implementing Collective Investment Undertakings Law 35/2003, of November 4, 2003, and which we summarized in the Garrigues Corporate/Commercial Law Newsletter 21 of July 2012 (click on link below for the Spanish version), was published in the Official State Gazette on July 20, 2012.

http://www.garrigues.com/es/Publicaciones/Novedades/Documents/Novedades-Mercanti-21-2012.pdf

One of the notable tax changes made concerns the exemption from the obligation to withhold tax on gains from the transfer or redemption of shares or other interests in the capital or equity of collective investment undertakings, in order to adjust the minimum percentage investment required of undertakings that invest in just one fund (currently 80%) to the new minimum percentage established in the Directive (85%).

However, the exemption from the withholding obligation will only apply until collective investment undertakings that invest in just one mutual fund as a matter of policy, and that are registered on the administrative register of the Spanish National Securities Market Commission ("CNMV") on the date of entry into force of the Collective Investment Undertaking Regulations, adjust to the provisions of articles 54 to 70 of the Regulations (undertakings have one year to do so). If they fail to make such adjustment, their authorization will be revoked and they will automatically be removed from the administrative register.

3.2 Spain-Germany tax treaty

July 30, 2012 saw the publication in the Official State Gazette of the new Spain-Germany tax treaty, which was signed in Madrid on February 3, 2012, amending the former treaty signed in 1966.

The following aspects are worthy of note:

- Income from immovable property (article 6): A new paragraph has been included so that where the ownership of shares or other rights attribute, directly or indirectly, to their holder the right of enjoyment of immovable property, income derived from the direct use, letting, sharecropping or use in any other form of his right of enjoyment may be taxed in the Contracting State in which the immovable property is situated.

- Associated enterprises (article 9): A new paragraph has been added relating to transfer pricing adjustments. Thus, adjustments made by a Contracting State could have effects at the associated enterprise of the other Contracting State, provided that that other Contracting State recognizes that such adjustments are appropriate.

- Dividends (article 10): The withholding tax rate has been reduced from 10% to 5% in cases where the beneficial owner is a company (but not a partnership or a listed real estate investment company) directly holding at least 10% of the capital of the company paying the dividends. The 15% rate continues to apply in all other cases.

- Interest and royalties (articles 11 and 12, respectively): Withholding tax on interest and royalties paid to a resident in the other Contracting State has been removed, provided that the resident is the beneficial owner and that the interest and royalties are not connected with a permanent establishment in the other Contracting State.

  The definition of royalties has been widened to include *"the right to use the name or image of a person or any other identity or image right, or to record the activity of sportspersons or the performances of artistes for radio or television."*

- Capital gains (article 13): An addition has been made so that gains derived from the alienation of shares in companies, or of similar rights, at least 50% of whose assets consist, directly or indirectly, of immovable property situated in the other Contracting State may be taxed in that other Contracting State.

  Moreover, the article also envisages the possibility that, in the event of a change of residence of an individual, the Contracting State of which such person was previously a resident may tax any gains derived from the alienation of shares in a company that relate to the period in which he/she was a resident of that Contracting State, where the alienation takes place within five years from the change of residence.

- Pensions and annuities (article 17): Pensions and annuities are taxed in the Contracting State of which the recipient is a resident. The foregoing notwithstanding, payments made by a Contracting State in accordance with its domestic social security legislation may be taxed in that State when the event that gives the right to receive the payment occurs after December 31, 2014. When the event that gives the right to receive the payment occurs between January 1, 2015 and December 31, 2029 the tax payable will not be more than 5% of the gross amount of the payments. On or after January 1, 2030 the tax payable will not be more than 10% of the gross amount of the payments.

The provisions of the above paragraph also apply to other payments received on or after December 31, 2014 in the following cases:

- In the case of Germany: where the payments arise by reason of incentivized contributions made over a period of more than 12 years and are not included in the taxable income received by reason of employment in that State, if such contributions were tax deductible or somehow incentivized by the State unless, as a result of the recipient of the incentive having emigrated, the incentive has been repaid to the State.

- In the case of Spain: where the payments are based on contributions made that were not included in taxable income in that State or were tax deductible and made over a period of more than 12 years.

Payments made in the form of a benefit due to political persecution or as a result of armed conflict or terrorist acts may only be taxed in the Contracting State making the payments.

- Capital (article 21): For the purposes of taxation in the Contracting State where immovable property is situated, shares in a company at least 50% of whose assets consist of immovable property are treated the same as shares or rights that grant their holder the right to enjoy immovable property.

- Elimination of double taxation (article 22): In the case of Spain, the ordinary credit method (crediting the tax paid in Germany, up to the limit of the tax payable in Spain on the income taxed in Germany) has been established for the elimination of double taxation.

- Limitation on treaty benefits (article 28): This new article has been included to allow the Contracting States to apply their domestic anti-abuse laws and the international fiscal transparency legislation. Article 28 also establishes that the benefits of the tax treaty will only apply to the "beneficial owner" of the income from the other Contracting State.

The following provisions, among others, have been included in the protocol to the tax treaty:

- Articles 4 (resident), 6 (income from immovable property) and 21 (capital) of the tax treaty will not apply to Spanish taxpayers who have elected to apply the inbound expatriates regime.

- In the case of certain dividends and interest, the possibility of their being taxed in their State of origin and pursuant to the legislation of that State now exists in the following cases:

  - where they are derived from rights, including debt-claims, that permit "jouissance" shares or "jouissance" rights, income derived by a limited partner from his interest as such, or from a loan the interest rate of which is linked to the borrower's profits or from profit participation certificates; and

- on condition that they are tax deductible in determining the profits of the party paying the income.

The foregoing notwithstanding, if the beneficial owner is a resident of the other Contracting State, the tax thus levied will not exceed 15% of the gross amount of such dividend and interest payments.

The tax treaty will enter into force on October 18, 2012, although it will not have effect until January 1, 2013.

3.3 Clarification of increase in VAT rate for certain supplies of goods and services

The DGT decision of August 2, 2012 on the VAT rate applicable to certain supplies of goods and services was published in the Official State Gazette on August 6, 2012.

The decision has clarified certain questions relating to the changes made to the VAT Law by Royal Decree-Law 20/2012, with effect as from September 1, 2012.

Thus, the goods and services to which the increased VAT rate applies have been specified in certain cases: (i) items that, owing to their characteristics, can only be used as classroom materials; (ii) ornamental plants and flowers; (iii) combined hospitality/entertainment services; (iv) hairdressing services; (v) services supplied to individuals engaging in sport or physical education; (vi) services provided by performers, artistes, directors and technicians; (vii) health and dental care and spa treatments; and (viii) supplies of residential housing.

The decision has also determined the prevailing VAT rate as a result of the change to the rates in the following cases:

- Prepayments made before September 1, 2012 relating to supplies of goods and services under domestic transactions affected by the change in VAT rates:

  The applicable rate will be the rate prevailing on the date on which the payments were actually made and should not vary subsequently even if the goods or services to which the prepayments relate are supplied after August 31, 2012.

- Cases envisaged in article 80 of the VAT Law in which the taxable amount is modified (return of containers and packaging; post-transaction discounts, allowances and volume rebates; price alterations; and termination, in whole or in part, of transactions):

  The rectification must take into account the rates applied when the VAT on the transactions in question became chargeable, rather than the rate prevailing when the transactions were performed.

  The same procedure will apply in the case of other causes for the modification of the taxable amount (inapplicability of an exemption, error in calculating the taxable amount, etc.) or if the applicable VAT rate is incorrectly recorded.

- Public procurement:

  When VAT rates are increased, the public authorities are obliged to pay VAT at the rate prevailing at the time at which the transactions are performed, even if it is higher than the rate indicated when the bid was made.

- Transactions of an ongoing nature:

  In such transactions, the VAT becomes chargeable when the part of the price of the good or service actually received falls due; accordingly, the new VAT rates will apply to all amounts that are contractually payable after August 31, 2012, even if they relate to services or goods supplied before that date.

3.4 Transfer of real estate and of securities in real estate companies by credit institutions

August 31, 2012 saw the publication in the Official State Gazette of Royal Decree-Law 24/2012, of August 31, 2012, on the Restructuring and Resolution of Credit Institutions which was summarized in our Corporate/Commercial Newsletter of September 23, 2012 (click on link below).

http://www.garrigues.com/es/Publicaciones/Novedades/Documents/Novedades-Mercantil-23-2012.pdf

Additional provision four establishes relief for the indirect taxation of the (i) sale of the institution's business, (ii) sale of assets or liabilities to a bridge bank, and (iii) transfer of assets or liabilities to asset management companies, provided that this is as a result of the intervention of the FROB.

In these cases, any sales of securities made in the context of such transactions will be exempt from transfer tax (under the "transfers for consideration" heading). Additional provision four expressly states that such transactions will not qualify for the exception in article 108 of the Securities Market Law (which makes certain transactions involving securities representing the capital of companies whose main asset is real estate or to which contributions of real estate have been made in the previous three years liable to transfer tax under the "transfers for consideration" heading).

Furthermore, the additional provision indicates that the above-mentioned exemption will also apply in cases where the taxpayers are bridge banks, asset management companies or third parties acquiring securities as a result of intervention by the FROB.

4. MISCELLANEOUS

4.1 Bill on Tax Measures for Energy Sustainability

On Friday, September 14, 2012, the Council of Ministers agreed to submit the Bill on Tax Measures for Energy Sustainability to Parliament. The Bill aims to harmonize the Spanish tax system with a more efficient use of energy resources, respecting the environment and achieving a sustainable electricity system.

The Bill creates the following new taxes and a new charge:

- A tax on production of radioactive waste from nuclear power generation.
- A tax on storage of radioactive waste: the aim is to unify the various taxable events currently taxed in this respect by Spain's autonomous community governments.
- A tax on the sale of electricity: the taxable event is the sale of electricity output, and the tax base the total revenues received by the taxpayer for the electricity it sells at each facility. Tax rate: 6%.
- Charge on the use of inland water for electricity generation.

In the area of excise and special taxes, the Bill envisages: (i) setting a tax rate for natural gas; (ii) raising the special tax rate for coal so that coal-based and natural gas-based electricity generation receive the same tax treatment; and (iii) creating specific excise tax rates on fuel oil and diesel oil used to generate electricity.