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CORPORATE INCOME TAX PREPAYMENT FOR APRIL 2012

Saturday, March 31, 2012 saw the publication in the Official State Gazette of Royal Decree-law 12/2012, of March 30, 2012, which makes a change to the system for making corporate income tax prepayments, a change that must be taken into account when preparing the prepayments to be made in 2012, alongside those made to the prepayment system by Royal Decree-law 9/2011, of August 19, 2011.

These changes have a direct effect on the prepayment that large enterprises must make within the first 20 days of this month of April. With this in mind, although we described these changes in our previous tax newsletter (issue 2-2012), below is a reminder of the rules applying to the prepayment that needs to be made over the next few days, plus a detailed analysis of some of the most significant rules.

1. PREPAYMENT CALCULATION METHODS

There are two prepayment calculation methods that can be used for the payment to be made in April 2012:

(a) The calculation method using the gross tax payable for the previous tax period, where the statutory filing period for the return for the period has expired, less the tax credits and reductions under chapters II, III and IV of Title VI of the revised Corporate Income Tax Law (method a). As a general rule, where the fiscal year is the same as the calendar year, the prepayment to be made in April 2012 must be based on the gross tax payable for 2010.

This method has not been modified by the two Royal Decree-laws mentioned above.

(b) The calculation method using the tax base for the period consisting of the first three months of 2012 (method b).

For taxpayers whose tax period is not the same as the calendar year, the portion of the tax base relating to the months between the start of the tax period and March 31, 2012 must be used.

The tax reductions under chapter III of Title VI of the revised Corporate Income Tax Law must be deducted from the resulting tax payable figure, along with any tax withholdings, payments on account and prepayments relating to the tax period.

The two new Royal Decree-laws have made significant changes to this method. The changes that apply to the prepayment due in April 2012 are described briefly below:

- Royal Decree-law 9/2011 raised the prepayment percentage to 21%, 24% or 27% depending on the taxpayer's net revenues.

- Royal Decree-law 12/2012 has brought in a “minimum prepayment” which is calculated on the basis of the positive earnings figure recorded in the income statement (generally, 4% for the April 2012 payment, and 8% for subsequent prepayments).

Both Royal Decree-laws have also amended several rules on determining the corporate income tax base, which therefore affect the prepayments calculated under this method, as follows:

- Royal Decree-law 9/2011 placed a restriction on the offset of tax losses (75% of their tax base before the offset, for taxpayers whose net revenues[1] for the preceding 12 months were equal to or above €20 million, and 50%, if their net revenues for the same period were equal to or above €60 million).

- Both Royal Decree-law 9/2011 and Royal Decree-law 12/2012 have amended several rules on determining the tax base before the offset, for example by (i) reducing the maximum annual percentage of goodwill that can be deducted each year, (ii) eliminating unrestricted depreciation and amortization for new assets, or (iii) placing ceilings on the deduction of borrowing costs.

All these changes will affect the April 2012 prepayment, depending on the taxpayer’s fiscal year, and subject to a blanket exception: the rule placing a 30% ceiling on the deduction of borrowing costs does not apply to this prepayment.

This method is mandatory for taxpayers whose turnovers[2] were above €6,010,121.04. Other taxpayers can elect to use this method, in which case they will have to use it for payments relating to the same and subsequent tax periods, until they elect not to use it. For an election not to use this method to be effective, it must be made:

- In February, where the tax period is the same as the calendar year.

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[1] “Net revenues” for the purposes of calculating the prepayment are those which relate to the 12 months preceding the start of the tax period. “Net revenues” is essentially an accounting term which is defined in section 11 of Part Three of the Spanish National Chart of Accounts (rules on preparing financial statements).

[2] “Turnover” for the purposes of the prepayment is calculated in accordance with the provisions of article 121 of VAT Law 37/1992, of December 28, 1992, and refers to the 12 months preceding the start of the tax period.

The terms “net revenues” and “turnover” are different.

- Otherwise, within two months after the start of the tax period or between the start of the period and the end of the period for making the first prepayment in the tax period, where this period is shorter than two months. In other words, taxpayers that end their fiscal year after February 20 have until April 20, 2012 to elect not to use this method.

The two Royal Decree-laws mentioned above do not make any specifications regarding prepayments for tax groups. Given, however, that the taxpayer is the tax group itself under the consolidated tax group system, the changes made by these two new pieces of legislation will apply to tax groups. In these cases, a question arises, concerning the "minimum prepayment" brought in by Royal Decree-law 12/2012, as to what must be taken as the positive earnings figure recorded in the income statement for the period (…) determined in accordance with the Commercial Code and other implementing accounting legislation which must be used as the basis for the "minimum prepayment". Although this is open to interpretation, it seems reasonable to use the positive earnings figure from the consolidated income statement for the entities in the tax group.

Lastly, it should be remembered that the return for the prepayments should be used to notify the tax authorities of any changes in the composition of the tax group.

2. CALCULATION OF THE PREPAYMENT FOR APRIL 2012. VARIOUS SCENARIOS

2.1 Taxpayers with turnovers <u>above</u> €6,010,121.04 that commenced their last tax period in <u>2012</u>

(a) With net revenues below €20 million.

Although these taxpayers have turnovers above €6,010,121.04 (which makes them "large enterprises"), insofar as their net revenues are below €20 million, they are not subject to the new rules brought in by Royal Decree-laws 9/2011 and 12/2012 specifically regarding prepayments and the offset of tax losses.

That means they do not have to calculate or pay over a "minimum prepayment", nor are they subject to the increased prepayment rates or the restriction on the offset of tax losses. There are, however, other new rules on determining the tax base before the offset of tax losses which these taxpayers need to take into account in their final corporate income tax return (except for the rule placing a 30% ceiling on the deduction of borrowing costs, brought in by Royal Decree-law 12/2012).

The rate to be used to calculate the prepayment will be determined by multiplying the tax rate by 5/7 and rounding down, that is, if it is the standard 30% rate, the prepayment rate will be 21%.

(b) With net revenues equal to or above €20 million but below €60 million.

In this case, the "minimum prepayment", the increased prepayment rates and the restriction on the offset of tax losses will apply to the April prepayment. The other new rules on determining the tax base before the offset of tax losses, brought in by the two Royal Decree-laws, will apply, except for the 30% ceiling on the deduction of borrowing costs brought in by Royal Decree-law 12/2012.

Specifically:

- The restriction on the offset of tax losses will be 75% of the tax base before the offset of any tax loss carryforwards.

- The prepayment rate will be calculated by multiplying the tax rate by 8/10 and rounding down. If it is the standard 30% rate, the prepayment rate will be 24%.

- The "minimum prepayment" will be 4% of the positive earnings figure recorded in the income statement for the first 3 months of 2012 less any tax loss carryforwards, subject to the 75% restriction mentioned above.

  This rate will be 2% if at least 85% of the revenues for the first 3 months of 2012 relate to income that is exempt under articles 21 and 22 of the revised Corporate Income Tax Law, or to income qualifying for the tax credit under article 30.2 of that law.

  As noted above, although Royal Decree-law 12/2012 is silent on this matter, it would be reasonable to conclude that the income statement to be used in the case of tax groups should be the consolidated income statement for the entities in the tax group.

(c) With net revenues of at least €60 million.

In this case, the "minimum prepayment", the increased prepayment rates and the restriction on the offset of tax losses will also apply to the April prepayment. The other new rules on determining the tax base before the offset of tax losses, brought in by the two Royal Decree-laws, will also apply, except for the 30% ceiling on the deduction of borrowing costs brought in by Royal Decree-law 12/2012.

Specifically:

- The restriction on the offset of tax losses will be 50% of the tax base before the offset of any tax loss carryforwards.

- The prepayment rate will be calculated by multiplying the tax rate by 9/10 and rounding down. If it is the 30% standard rate, the prepayment rate will be 27%.

- The "minimum prepayment" will be 4% of the positive earnings figure recorded in the income statement for the first 3 months of 2012, less any tax loss carryforwards, subject to the 50% restriction referred to above.

  This rate will be 2% if at least 85% of the revenues for the first 3 months of 2012 relate to income that is exempt under articles 21 and 22 of the revised Corporate Income Tax Law, or to income qualifying for the tax credit under article 30.2 of the same law.

  Although not specified in Royal Decree-law 12/2012, as mentioned above, it would seem reasonable to conclude that the income statement to be used in the case of tax groups should be the consolidated income statement for the entities in the tax group.

2.2 Taxpayers with turnovers above €6,010,121.04 that commenced their last tax period in 2011

(a) With net revenues below €20 million.

Although these taxpayers have a turnover above €6,010,121.04 (which makes them "large enterprises"), insofar as their net revenues are below €20 million, they are not subject to the new rules brought in by Royal Decree-law 9/2011 (nor to those in Royal Decree-law 12/2012 because the tax period has commenced in 2011) regarding prepayments and the offset of tax losses.

Therefore, there is no "minimum prepayment", or increased prepayment rates, or any restrictions on the offset of tax losses. By contrast, the new rules on determining the tax base before the offset of tax losses under Royal Decree-law 9/2011 (not those of Royal Decree-law 12/2012) do apply.

The prepayment rate is calculated by multiplying the tax rate by 5/7 and rounding down. If it is the standard 30% rate, the prepayment rate will be 21%.

(b) With net revenues of at least €20 million, but below €60 million.

In this case, the increased prepayment rates and the restriction on the offset of tax losses will apply, although the "minimum prepayment" will not. The new rules on determining the tax base before the offset of tax losses will be those in Royal Decree-law 9/2011, not those in Royal Decree-law 12/2012.

Specifically:

- The restriction on the offset of tax losses will be 75% of the tax base before the offset of any tax loss carryforwards.

- The prepayment rate will be calculated by multiplying the tax rate by 8/10 and rounding down. If it is the standard 30% rate, the prepayment rate will be 24%.

(c) With net revenues of at least €60 million.

In this case, the increased prepayment rates and the restriction on the offset of tax losses will apply, although the “minimum prepayment” will not. The new rules on determining the tax base before the offset of tax losses will be those in Royal Decree-law 9/2011, but not those in Royal Decree-law 12/2012.

Specifically:

- The restriction on the offset of tax losses will be 50% of the tax base before the offset of any tax loss carryforwards.

- The prepayment rate will be calculated by multiplying the tax rate by 9/10 and rounding down. If it is the standard 30% rate, the prepayment rate will be 27%.

2.3 Taxpayers with turnovers below €6,010,121.0 that have elected to apply prepayment method b)

The rules described in sections 1 and 2 above must be applied to determine the base on which to calculate the prepayment and to apply the “minimum prepayment”.

The prepayment rate will be calculated by multiplying the tax rate by 5/7 and rounding down, regardless of the net revenues figure. If it is the standard 30% rate, the prepayment rate will be 21%.

2.4 Taxpayers with turnovers below €6,010,121.04 that have not elected to apply prepayment method b)

The prepayment will be 18% of the gross tax payable for the tax period, where the statutory filing period for the return for the period has expired, less the tax credits and reductions under chapters II, III and IV of Title VI of the revised Corporate Income Tax Law.

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