GARRIGUES
bulletin TAX

4-2012
April, 2012

Royal Decree-Law 12/2012, summarized in our Tax News Bulletin 2/2012, gave individuals and enterprises the option to disclose any assets or rights not deriving from income reported for personal income tax, corporate income tax and nonresident income tax purposes, by filing a special tax return using a specific form, up to and including November 30, 2012.

This may be done by paying over 10% of the acquisition cost of the assets or rights being disclosed, without any penalties, interest or surcharges for late filing and payment falling due. The amount that is reported will be treated as "reported income" for the purposes of the three taxes mentioned above.

It was announced in the same royal decree-law, albeit without giving any specific details, that the penalty regime was going to be toughened for future fiscal years to encourage disclosure on this special tax return.

Apparently the details of the tougher penalty regime will be published shortly, in view of the tax evasion prevention bill (approved by the Spanish cabinet on April 13, 2012), which also sets out a new obligation for residents in Spain to inform the tax authorities of accounts and securities located abroad. A breach of this obligation could mean that there will be no statute of limitations for capital gains not reported for personal income tax and corporate income tax purposes.

Moreover, the bill contains tougher penalties for these unreported capital gains, as it treats this as a very serious infringement subject in all cases to a proportional fine of 150% of the amount not paid over.

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1. JUDGMENTS

1.1 Corporate income tax.- To take reinvestment tax credit, transferred assets must be used in the business, including under previous legislation (National Appellate Court. Judgment of February 16, 2012)

In 2002, the taxpayer had taken the reinvestment tax credit in respect of income obtained from the sale of real estate, which had been recognized for accounting purposes as property, plant and equipment since its acquisition (1990), but had not been used by the taxpayer itself or used by third parties; for this reason, the inspectors considered that the property was really “inventory.” Against this view, the taxpayer argued that, as it had owned the real estate for 12 years and the asset had been recognized for accounting purposes as property, plant and equipment throughout that entire period, it had clearly not been acquired in order to be sold but rather to be kept (even though it was finally sold).

The National Appellate Court held that:

- An asset is classified according to its purpose or use, not to the condition of the asset itself. Moreover, its use must be true and real, not merely possible or hypothetical.
- The reinvestment tax credit is a mechanism to encourage the renewal of productive business assets, an essential requirement being the use of the transferred and acquired assets in the business.
- This business use is required by all tax regimes put in place to encourage this type of investment (for exemption, deferral, or the tax credit in question) even if the law does not expressly say so.

1.2 Personal income tax.- Cohabitation requirement to take the family tax allowance for descendants is unconstitutional (Constitutional Court. Judgment of February 15, 2012)

In order for the personal income tax allowance for descendants to be taken, the descendant must live with the taxpayer.

The Constitutional Court held that the constitutional protection of the family is independent of the physical fact of cohabitation, there being only one definition of family for the purposes of both the parents’ obligations and the public authorities’ obligation to promote the protection of the family (Article 39.1 of the Spanish Constitution). As the tax allowance for descendants is deemed a family protection measure for the purposes of Article 39.1 of the Spanish Constitution, if it requires there to be cohabitation, that single definition of family is being denied.

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Similarly, this judgment confirmed that any legislation denying the application of the tax allowance for descendants, without justified reason, discriminates against an important group of taxpayers who provide economic assistance to their descendants, merely because they do not live with them.

The court added, however, that the contested article (Article 40.3.1.b) of Law 40/1998, of December 9, 1998) need not be rendered void as the provision is deemed to be repealed from when the judgment is issued. Additionally, the Court recognized that it does not have the authority to decide on how the allowance in question should be applied and that, in any case, another rule could trigger an automatic right to apply the allowance for all unmarried descendants under the age of 25, regardless of the circumstances involved.

Bear in mind that the contested rule is currently in force, as it is included in Law 35/2006, of November 28, 2006, in force.

1.3 Personal income tax.- Company must prove professional use of vehicles by employees (National Appellate Court. Judgment of January 25, 2012)

In this specific case, the company had provided some vehicles to its employees and had not considered it necessary to recognize income in kind to them because they were not authorized to use the vehicles outside of working hours.

Although the chamber confirmed the inspectors' view that the onus is on the company to evidence the private use of the vehicles (or the absence of private use, as the case may be) and that a general prohibition against private use was not sufficient (which led the court to uphold the tax authorities' assessment), it did not agree with the inspectors' view that penalties applied simply because it "was not credible" that the company considered that a prohibition was sufficient for the employees to fulfill it.

1.4 Nonresident income tax.- Antiabuse clause in the parent-subsidiary exemption (Supreme Court. Judgment of March 21, 2012)

In the case examined by the court, the parent-subsidiary exemption had been taken for dividends paid by the subsidiary to its parent. The inspectors considered that the exemption did not apply because the requirements for nonapplication of the antiabuse clause established in the Nonresident Income Tax Law had not been met.

The law specifically states that the exemption does not apply where a majority of the interest in the subsidiary is held (even if indirectly) by entities not resident in the European Union, unless it can be proven, alternatively, (i) that the parent was set up for valid reasons and not to benefit from the exemption, (ii) that the parent conducts a business activity related to that of its subsidiary, or (iii) lastly, that the parent manages its subsidiary with sufficient material and human resources.

In the appealed judgment, it was held that the taxpayer had not evidenced any of the scenarios in which the antiabuse clause does not apply. Therefore, after confirming that the parent did not conduct a business activity related to that of the subsidiary, the court ruled that:

- The fact that the parent had personnel was not sufficient proof that it managed its subsidiary, even more so since the subsidiary had other administration expenses and its management-related documents were stored at the subsidiary's premises.

- The fact that the parent had been set up in the European Union for valid economic reasons (its shareholders being US residents), and that the Group's most important production plants were located within the area of the EU where the parent was resident, was not sufficient proof either.

The taxpayer filed a cassation appeal against the appealed judgment based on incorrect evaluation of proof. Although the Supreme Court held that the erroneous evaluation of proof by a court is not one of the grounds for cassation included in the judicial review jurisdiction, it analyzed the merits of the case and concluded that the evaluation made (in the direction described) was neither arbitrary nor irrational.

1.5 Tax on increase in urban land value.- Clause establishing purchaser's liability for tax is abusive (Supreme Court. Civil Chamber judgment of November 25, 2011)

In this judgment, the court concluded that a clause in a sale and purchase agreement on dwellings, determining that the purchasers are liable for the tax on increase in urban land value, for which the taxpayer is the transferor in this type of agreement, was null and void.

The court held that this clause was null and void because it was imposed on the purchaser, without being negotiated individually, which is aggravated by the purchaser's lack of information on the seller's status as taxpayer. Moreover, the court recalled that this clause benefits the transferor, which is the party that receives the value increase, not the transferee, who is compelled to meet an economic obligation without any consideration, which overthrows the balance between the parties to the contract.

1.6 Value added tax.- Deductibility of input VAT on invoice issued to partners of a company prior to registration and identification for VAT purposes (European Court of Justice. Judgment of March 1, 2012, on case C-280/10)

National legislation which does not permit a company to exercise the right to deduct input VAT incurred by its partners, before its creation and registration, in relation to the expenses and investments necessary to enable the creation of the company and the performance of its economic activity, is contrary to the Directive.

1.7 Value added tax.- Input VAT on computers purchased for employee training is deductible, and subsequent supply of computers to employees is subject to VAT (National Appellate Court. Judgment of February 8, 2012)

The inspectors considered that the computers the appellant had acquired to be used by its employees, in order for them to be trained in using new technologies, were not used directly and exclusively in the business activity and therefore did not generate the right to deduct the input VAT on their purchase, nor could VAT be charged on the subsequent supply of the computers to the employees.

The chamber considered, however, that the purchased equipment was not meant to be used to satisfy the employees' personal or private needs but was provided to them with the sole aim of enabling them to be trained in new technologies and to serve the performance of the business activity.

Accordingly, the acquisition cost of those computers was comparable to any other training expense required to improve staff competencies to the benefit of the company's business and, consequently, the appellant was entitled to a full deduction of input VAT on that purchase, but it should also have charged VAT on the computers supplied to employees (whether they were supplies for no consideration or for below market price).

You may recall that this interpretation had already been made by the Directorate-General of Taxes (in a ruling dated March 23, 2011, among others) when applying the ECJ judgment in case C-40/90 (Astra Zeneca UK, Ltd), which we have discussed in past tax bulletins.

1.8 Value added tax.- VAT exemption for publicly traded companies that obtain recognition as private welfare entities (National Appellate Court. Judgment of December 22, 2011)

An enterprise must meet the following requirements to be deemed a "private welfare entity" and thus be able to take the VAT exemption provided for this type of entity: (i) it must be a not-for-profit entity, (ii) its income must be reinvested in the same type of activities, (iii) its management posts must not be remunerated, (iv) it must not obtain income from the services supplied to its shareholders or relatives up to the second degree of kinship, and (v) it must obtain express recognition of that status from the tax authorities.

In the case examined, the issue under debate was whether a *sociedad anónima* (a publicly traded company) met the requirement of being a not-for-profit entity; the tax authorities did not consider this requirement had been met because, due to the very nature of this corporate form, one of its intrinsic features is its profit-making aim.

The National Appellate Court held, however, that the fact of a company having, in principle, a profit-making aim as a result of its legal form does not preclude it from actually being able to operate without having that aim.

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1.9 Inheritance and gift tax.- The taxable amount of liquidations of specific bequests must not include the proportional part of household furnishings (Castilla y Leon High Court. Judgment of November 14, 2011)

Household furnishings are generally computed as part of the value of the estate for inheritance and gift tax purposes.

The proportional value of household furnishings is not computed in relation to specific bequests (as those bequests refer to a specific object).

The court clarified, however, that the tax base should include the proportional value of household furnishings in the same proportion as the other nonspecific or indeterminate goods belonging to the estate that might have been received by the legatees.

1.10 Inspection proceedings.- Decision extending term for inspection proceedings is null and void when issued while criminal proceeding is in progress (Supreme Court. Judgment of March 15, 2012)

In the case examined, the administrative proceeding had been sent to the Public Prosecutor's Office. While the criminal proceeding was in progress, the chief tax inspector decided to extend the period for inspection proceedings to the maximum 24 months due to the special complexity involved. After the criminal case was dismissed, the enterprise was notified of the resumption of the inspection and a final assessment decision was issued after the initial 12-month period had already ended.

The Supreme Court ruled that the decision extending the inspection proceedings infringed the *non bis idem* or double jeopardy principle, because it was issued during the criminal proceeding, that is, when the inspection proceedings had, theoretically, ended.

1.11 Criminal proceeding.- Aggravated offense due to particular extent and seriousness of evasion (Supreme Court. Criminal Chamber judgment of January 19, 2012)

In a case involving a tax offense, it had been held in the previous judgment that the offense was aggravated due to the particular extent and seriousness of the evasion, on the ground that in two of the inspected fiscal years, the evaded tax was more than three times higher than the sum of €120,000. In another of the years, the opposite conclusion had been reached, as the evaded amounts were less than twice that sum.

The Supreme Court's Criminal Chamber applied the same reasoning and made a similar calculation, based on the mathematical average of the evaded amounts of tax in the tax offenses that chamber had examined since 1990. The evaded amounts in a total of 108 cases referring to different taxes totaled €56,064,694.70 which, if divided by 108, results in an average evaded amount of tax equal to €519,177.54. That amount is approximately five times the sum of €120,000 and was set (in this judgment) as the cap for establishing aggravation of the offense.

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1.12 Administrative proceeding.- Notification by public notice can only be used when authorities cannot determine interested party's address by other means (Castilla y León High Court. Judgment of December 9, 2011)

The tax authorities notified an assessment through the procedure for notification by public notice after two failed notification attempts. Later, however, they successfully notified the order initiating enforced collection proceedings, without needing to do so by public notice.

There was proof, however, that the tax authorities had on record (before notification of the assessment by public notice) another address provided by the appellant for notification purposes, as well as her place of work, which was precisely the Department of Taxation of the Madrid Autonomous Community (where, as a public official, withholding taxes were deducted from her salary income).

Accordingly, the court held that, after the failed attempts to notify the assessment, the authorities should have carried out a minimum amount of activity to verify and confirm the taxpayer's address, as they had (in fact) done later, to notify the order initiating enforced collection proceedings.

The court ruled therefore that the assessment was not notified in due form, meaning that the order initiating enforced collection proceedings should not have been issued and, consequently, that order and the subsequent proceedings confirming it were null and void.

1.13 Management proceeding.- Tax authorities can rectify *ex officio* their assessment decisions when clerical errors are evident (Castilla y León High Court. Judgment of November 30, 2011)

In this case, the Tax Management Office had rendered a decision that no adjustment was required by the taxpayer. The same office later rectified that decision on the ground that a clerical error had been made, since what had happened (as was reflected in the new decision) was that the limited review had ended because of the commencement of an inspection proceeding relating to the same tax and fiscal year.

The court held that there were a number of circumstances in the case analyzed that were sufficient to uphold the lawfulness of the second decision, since the error in the first one was obvious and undeniable, evident and clear and, therefore, it was not necessary to make an interpretation of legal provisions to conclude that the error had been made, even more so when the error was a "computer" error.

2. DECISIONS AND RULINGS

2.1 Corporate income tax.– No obligation to document market value of loans made to subsidiary for below market value (Directorate-General of Taxes. Ruling V0407-12, of February 23, 2012)

This ruling analyzed whether it is obligatory to document, for transfer pricing purposes, a loan made to a wholly owned entity for below market interest.

The Directorate-General of Taxes (DGT) clarified, firstly, that this type of loan is not included in the tax base because, according to recognition and valuation standard no. 18 of the Spanish National Chart of Accounts, it is not a gift but rather an increase in the equity of the borrower and an addition to the value of the holding at the lender (unless there are other shareholders of the subsidiary and the parent makes a contribution in a higher proportion than would relate to its effective holding).

That said, the Corporate Income Tax Law contains a special provision for this type of transaction (Article 15) according to which, the assets contributed to entities and the securities received as consideration must be priced at market value.

Although market value is the price that would have been agreed by independent parties according to the methods set out in the law itself (Article 16), the special rule (Article 15) prevails over that general transfer pricing rule (Article 16) so this type of transaction is not subject to the documentation obligations established for related-party transactions (Article 16.2).

2.2 Corporate income tax.– Impairment adjustment to shares that was not deducted due to insufficient cost may be deducted later when cost increases (Directorate-General of Taxes. Ruling V0349-12, of February 16, 2012).

Under certain circumstances, the Corporate Income Tax Law allows an entity to write off its shares in a subsidiary for tax purposes (Article 12.3) which will generally enable it to use its losses (through that write-off for tax purposes). The amount that can be deducted is restricted to the acquisition cost of the shares, as once that cost has been written off in full, any losses incurred later by the subsidiary cannot be used by the parent.

The DGT confirmed, however, that the parent can use those losses (through the deduction of impairment of the subsidiary) in a fiscal year after these new losses are incurred, if the cost at the parent is increased through a contribution to the subsidiary's equity.

According to the DGT, arguing otherwise would be tantamount to disregarding the tax effects of the decline in value of the holding and, moreover, would have a negative impact on the deduction according to the fiscal year in which the contribution is made to the subsidiary's capital.

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2.3 Corporate income tax.– Income from activities abroad exempt for members of joint venture even where they are not performed through permanent establishments (Directorate-General of Taxes. Ruling V0293-12, of February 13, 2012)

According to Article 50 of the Revised Corporate Income Tax Law, the members of a joint venture which operates abroad may apply the exemption method for foreign-source income. In this ruling, the DGT held that the exemption was not conditional on the joint venture's operating abroad through a permanent establishment.

2.4 Corporate income tax and value added tax.– Real estate must be priced at arm's length for corporate income tax and VAT purposes according to methods established in respective legislation (Directorate-General of Taxes. Ruling V0296-12, of February 13, 2012)

A number of tax provisions establish the obligation to apply arm's length values in transactions between related persons or entities.

Specifically, Article 16 of the Corporate Income Tax Law defines "normal market value" as the value which would have been agreed on by independent persons or entities at arm's length, and Subarticle 4 establishes various methods for determining that value.

Moreover, Article 79.5 of the VAT Law defines normal market value as the amount which a customer (at the marketing stage at which the supply of goods or services to be valued takes place) would have to pay to an independent supplier within the territory where VAT applies on an arm's length basis.

In the DGT's opinion, these special rules must be applied to price real estate at arm's length for corporate income tax and VAT purposes, and it is not allowed to apply the actual values determined in autonomous community legislation for the purposes of other taxes (for example, transfer and stamp tax or inheritance tax).

2.5 Personal income tax.– Definition of uniform securities (Directorate-General of Taxes. Ruling V0381-12, of February 21, 2012)

Personal income tax legislation makes several references to the term "uniform securities" (for example, where securities are transferred and it needs to be determined which are deemed transferred for tax purposes); the personal income tax regulations establish that in order for securities to be deemed uniform:

- They must form part of a same financial transaction or have the same purpose, including the purpose to systematically obtain financing, be of the same nature and subject to the same transfer rules and confer on their holders substantially similar rights and obligations.

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- Their uniformity will not be affected by any differences existing between the securities or shares as to their unit value or the dates on which they were issued, among other factors, and, in particular, by the division of the issue into successive tranches or by expected extensions.

Furthermore, based on the Corporate Enterprises Law, it transpires that the general rule is for the shares to be equal, and for any inequality regarding different voting and/or economic rights to be determined in a strict sense, by reference to the proportion they represent in the company's capital stock .

Accordingly, the DGT concluded that shares with different par values cannot be deemed non-uniform if the rights they confer are proportional to their par value, an interpretation that sits comfortably with the provision in the Personal Income Tax Regulations establishing that differences in relation to unit value or par value are not a determining factor to rule out uniformity.

2.6 Personal income tax.– Application of the 40% reduction to salary increases relating to previous years and agreed in a later collective agreement (Directorate-General of Taxes. Ruling V0250-12, of February 6, 2012)

The DGT analyzed the clause of a collective agreement setting out the payment, in a year after its entry into force, of the amounts resulting from applying the salary increases or reviews relating to the three preceding years and, specifically, whether those increases constitute multiyear salary income.

The conclusion was that they do, based on the retroactive effect given in the collective agreement to salary increases, together with the fact that they are payable together and the period for payment over a period comprising more than two years, even though the salary review clause was not agreed before the start of the period to which it applies.

2.7 Value added tax.– Patron's display of its status as such, in a collaboration agreement with a foundation, does not constitute a service for VAT purposes (Directorate-General of Taxes. Ruling V0316-12, of February 14, 2012)

Entities which benefit from patronage (foundations, associations declared to be of public use, etc.) can enter into collaboration agreements where they agree to publicize, by any means, the patron's participation in those activities in exchange for economic aid to carry out their activities. The law establishes that the dissemination of the patron's participation in the context of these agreements does not constitute a supply of services.

Based on that provision, the DGT has held in various rulings, and confirmed in this one, that the commitment to publicize the patron's participation by including its logo or mentioning it in communications does not constitute a supply of services for VAT purposes, nor will it form part of the taxable amount of its transactions or be included in the calculation of its VAT deductible proportion.

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In this context, the DGT also analyzed whether the patron's use of its status as such in all of its public communications and advertising materials could have VAT implications. The DGT concluded in this ruling that the fact that patron displays its status at a specific event does not allow "it to be concluded that there is a legal relationship evidencing the existence of a direct link, under which the patron agrees to publicize that event of special interest or the requesting entity agrees to pay any consideration," meaning that "*there is not a service for the purposes of the tax due to the display of the status of patron through the insertion of the logo and of the authorized phrase relating to a specific event that is subject to Article 27 of Law 49/2002, in favor of the entity or body that organizes it*."

2.8 Inheritance and gift tax.– Determination of autonomous community of residence in case of donee's relocation to Spain from abroad (Directorate-General of Taxes. Ruling V0256-12, of February 7, 2012)

The legislation of various autonomous communities, Madrid, among them, provides reductions for gifts to certain individuals resident in those communities. However, as a form of antiabuse provision, and in order to prevent changes of residence to benefit from those reductions, Law 22/2009, of December 18, 2009, provides that gifts will be subject to the legislation of the autonomous community where the donee has spent the greatest number of days in the five-year period immediately preceding the date on which the tax falls due.

This ruling analyzed the case of a gift to an individual who resided in Madrid when the gift was received, after moving there from another country. In this case, the DGT held the antiabuse provision mentioned above would not apply since it is established for cases of relocation between autonomous communities but not for relocations from outside Spain to the autonomous community where the reduction applies.

2.9 Oil and gas tax.- Adjustment through annual assessments constitutes material defect that does not preclude new assessments (Central Economic-Administrative Tribunal. Decision of February 14, 2012)

As the Special Cassation Chamber of the Central Economic-Administrative Tribunal (TEAC) had held in the decision dated November 24, 2010 in relation to VAT, the TEAC held in this decision that it is also incorrect in relation to oil and gas tax, to adjust the taxpayer's tax liability through annual assessments rather than assessments for the "normal" tax periods in the voluntary filing period.

The TEAC concluded once again, however, that the adjustments through annual assessments is a non-material factual defect meaning that once the incorrect assessments are rendered void, the proceedings can be backdated, subject to the restrictions deriving from the statute of limitations and the prohibition against *reformatio in peius*.

2.10 Administrative proceeding.- Actions by taxpayer to have proceeding held statute-barred do not toll statute of limitations for tax debt (Galicia Regional Economic-Administrative Tribunal. Decision of March 13, 2012)

This decision ruled on a case in which a tax assessment was issued and then rendered void because it was statute-barred.

The Galicia Regional Economic-Administrative Tribunal, in keeping with the TEAC decision of October 26, 2010, held that acts carried out before the assessment was held statute-barred, that is, the actual assessment and the subsequent economic-administrative claim in which the decision held that the assessment was statute-barred, cannot toll the statute of limitations for the debt.

2.11 Collection proceeding.- Interest due for partially upheld decisions on assessments with stayed enforcement (TEAC. Decisions of February 16 and March 1, 2012)

The TEAC had ruled in various decisions that Article 26.6 of the General Taxation Law, determining that interest is payable at the legal rate where the debt has been stayed by providing a bank guarantee, did not apply when the appeal in question was partially upheld and a new assessment was issued. In those cases, the TEAC had been concluding that late-payment interest was payable.

The court has now changed its view, by concluding that:

- In these cases, a new assessment must be issued and the interest must be calculated on the tax payable figure determined in the new assessment.
- The period for computing the interest will run from the date of the reversed assessment until the new assessment is issued (and cannot go beyond the maximum period for enforcement of the partially upheld decision).
- While the debt is subject to stay with the relevant guarantees, the interest rate to be taken will be the legal interest rate in force at any given time; in the remainder of the accrual period, the applicable rate will be the late-payment interest rate.

According to the TEAC, this new interpretation is not only in keeping with the aim of the law but it heads off the undesirable effect of the recipient of a partially upheld administrative or court decision reversing an assessment or replacing it with another, being in a worse condition than a person whose appeal has been rejected in full without a new assessment having been issued.

Moreover, the TEAC decision of March 1, 2012 recalled that late-payment interest must not be charged after the maximum term for a decision to be issued on the economic-administrative claim has run, that is, once one year has run from the date on which that claim was filed.

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3. LEGISLATION

3.1 Correction of Royal Decree-Law 12/2012 in relation to prepayments and the special tax on foreign-source dividends and income

Royal Decree-Law 14/2012, of April 20, 2012 (published in the Official State Gazette on April 21, 2012) on urgent measures to rationalize public spending on education, includes amendments to Royal Decree-Law 12/2012, of March 30, 2012, introducing various tax and administrative measures to reduce the budget deficit (summarized in our Newsletter 2-2012):

- Prepayments: in the case of taxpayers whose tax period is not the same as the calendar year, the minimum prepayment must be calculated on the income of the period between the first day of the fiscal year and the day before the start of each prepayment period (under the previous wording, the result had to be calculated in all cases from January 1 of each year, regardless of when the fiscal year started).

- Special tax on foreign-source dividends and income: in cases where the taxation requirement for the nonresident entity that pays the income is not met, the special tax is confined to the dividends and income payable up to November 30, 2012. Under the previous wording, it applied up to December 31, 2012.

3.2 Spain-Hong Kong tax treaty

The Spain-Hong Kong tax treaty, signed in Hong Kong on April 1, 2011, was published in the Official State Gazette of April 14, 2012. Its key provisions are as follows:

- The applicable withholding rates according to the type of income obtained will be as follows:

  - Dividends: 0% if the beneficial owner is a company (other than a partnership) which holds directly at least 25% of the capital of the company paying the dividends; 10% in all other cases.

  - Interest: 5%. The interest received or paid by the State, and other kinds of interest expressly established in Article 11 of the tax treaty, will be exempt.

  - Royalties: 5%.

- The gains deriving from (i) immovable property, (ii) shares or holdings, or comparable interests deriving more than 50% of their value directly or indirectly, from immovable property, or (iii) other rights which directly or indirectly entitle their owner the right to the enjoyment of immovable property, may be taxed in the State where that real estate is situated.

However, in the case of dividends, interest, royalties, capital gains and other income, the treaty benefits will not apply where the main aim, or one of the main aims of any person involved in the creation or assignment of the rights giving rise to that income, is to obtain those benefits through that creation or assignment.

This tax treaty entered into force on April 13, 2012 (one day before its publication in the Official State Gazette) which is the date when Hong Kong ceased to be deemed a tax haven, and its provisions will take effect:

- In respect of taxes withheld at source, on the amounts paid or credited to nonresidents, on or after April 1, 2013.
- In respect of other taxes, for taxation years beginning on or after April 1, 2013.
- In all other cases, on or after April 1, 2013.

3.3 Spain-Armenia tax treaty

The Spain-Armenia tax treaty, signed in Madrid on December 16, 2011, was published in the Official State Gazette of April 17, 2012. Its key provisions are as follows:

- The applicable withholding rates according to the type of income obtained will be as follows:
  - Dividends: 0%, if (i) the beneficial owner is a resident of the other State, (ii) and has owned directly or indirectly at least 25% of the capital of the company paying the dividends for at least two years before the date of that payment, and (iii) those dividends are not subject to income tax in the other State; 10% in all other cases.
  - Interest: 5%.
  - Royalties: 5% for the use of or the right to use copyrights on literary, dramatic, musical, artistic or scientific work, including cinematographic films or tapes and any means of image or sound reproduction for use in radio or television broadcasting; 10% in all other cases.
- The gains deriving from (i) immovable property, (ii) shares or holdings, or comparable interests deriving more than 50% of their value directly or indirectly, from immovable property, or (iii) other rights which directly or indirectly entitle their owner to the enjoyment of immovable property, may be taxed in the State where that real estate is situated..

This tax treaty entered into force on March 21, 2012, and its provisions will take effect:

- In relation to taxes that fall due periodically, for those relating to the fiscal year beginning on or after the date of entry into force of the tax treaty.

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- In all other cases, on the date on which the tax treaty enters into force (March 21, 2012).

3.4 Personal income tax and net wealth tax forms for 2011

The personal income tax and wealth tax forms for 2011 have been approved by Order HAP/638/2012, of March 26, 2012.

The filing period for both the personal income tax and the wealth tax returns will run from May 3 to July 2, 2012. However, (i) the period for confirming the draft personal income tax return remotely or by telephone commenced on April 10, and (ii) the period for filing returns where the payment of both taxes is made by direct debit commences on May 3 and runs only until June 27, 2012.

A new change worth noting is that the wealth tax return can only be filed online, although, in addition to the electronic signature system, it can be filed by giving the reference number of the draft return or the personal income tax fiscal data.

Moreover, taxpayers that file a wealth tax return must also file their personal income tax return, or confirm their draft return as appropriate, remotely or by phone.

3.5 New tax treatment for timeshare agreements for tourist properties

Royal Decree-Law 8/2012, of March 16, 2012 (Official State Gazette of March 17, 2012) has updated the tax provisions applicable to timeshare rights in tourist properties, as follows:

- For <u>wealth tax</u> purposes, timeshare rights in tourist properties will be priced at their acquisition price.
- For <u>transfer and stamp tax</u> purposes, a 4% charge will be payable on transfers between private individuals (not subject to VAT or to Canary Islands general indirect tax) of the rights governed by the royal decree-law, regardless of their nature.
- Lastly, for <u>value added tax</u> purposes, the 8% rate will apply to the transfer of timeshare rights in buildings, developments or architecturally separated sections thereof, where the property has at least ten accommodation units.

This legislation came into force on March 18, 2012.

4. OTHERS

4.1 Combating tax evasion

In a meeting held on April 13, 2012, the Spanish cabinet approved a bill proposing measures to prevent and combat tax evasion, designed to have a direct impact on certain areas of evasion identified as the source of important losses to public revenues. Other measures are proposed for improving the provisions guaranteeing tax revenue, in order to update them or clarify their correct interpretation. The most notable among these measures contained in the current wording of the bill set out:

- New rules on succession to the liability of legal entities and entities without a legal personality, to prevent activities to get rid of the assets of those entities before they are liquidated.

- A new case of secondary liability, which will allow debts to be collected from the directors of companies which have no assets but have a regular economic activity, and repeatedly and systematically file formal tax returns but pay no tax, with the intention of evading tax.

- In the context of insolvency proceedings, elimination of the option to request a deferral or split payment of the post-insolvency order claims, to avoid an artificial deferral of the payment of government claims.

- Regarding the statute of limitations for tax purposes, clarification of the rules on cases where the statute of limitations on the tax authorities' right to determine the tax debt is tolled, where the authorities initially take action regarding a different tax obligation because the taxpayer filed an incorrect tax return.

- In relation to the rules on tax penalties, the changes proposed by the bill include:

    - The introduction of a series of tax infringements relating to breach of the obligation to file tax returns or informative returns remotely, and modification of the infringements already existing for resistance, obstruction, pretext or refusal to cooperate with the tax authorities in the context of inspection proceedings.

    - A change to the period for initiating penalty proceedings, to the effect that the three months available to the tax authorities for that purpose commences when the decision to impose a pecuniary penalty, with which the potential imposition of a nonpecuniary penalty is linked, is notified or deemed notified.

    - In cases where the rules for unreported increases in wealth apply for personal income tax and corporate income tax purposes, where the commission of a tax infringement is evidenced due to the failure to pay over the tax debt that should have been assessed in a tax return, the bill proposes the classification of these infringements in all cases as very serious, attracting a proportional fine equal to 150% of the amount of the basis for the penalty (which would be the amount not paid over in respect of the self-assessment due to the commission of the infringement).

- The bill proposes a new obligation for residents in Spain to disclose accounts and securities located abroad. The failure to fulfill this obligation would remove the statute of limitations for unreported increases in assets for personal income tax and corporate income tax purposes.

- A limit of €2,500 would be placed on transactions in cash where at least one of the parties is a trader or professional (€15,000 if the transaction is carried out with a nonresident not acting as a trader or professional). Breach of this limit would constitute an administrative infringement attracting a penalty of 25% of the total transaction amount.

- The bill proposes a reform of the personal income tax “modules” system.

- For VAT purposes, it sets out two new cases triggering the reverse charge mechanism in supplies of real estate; one, where the exemption is waived and another, where the supply takes place as a result of foreclosure on collateral.

4.2 General State Budget Bill for 2012

The General State Budget Bill for 2012, currently going through the Lower House of the Spanish Parliament, includes the tax measures usually contained in this law, most notably:

- <u>Personal income tax</u>:

  - Updating to 1% the index-linked adjustment coefficients applicable to transfers of real estate not used in economic activities.

  - Rules on the payments for the loss of tax benefits under the current legislation affecting (i) the buyers of a principal residence and (ii) recipients of certain income from movable capital generated over more than two years in 2011 with respect to the benefit established in the personal income tax legislation in force up to December 31, 2006.

- <u>Corporate income tax</u>:

  - Updating to 1% the index-linked adjustment coefficients applicable to transfers of real estate assets.

  - Regulation of the method for determining corporate income tax prepayments in fiscal year 2012.

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- Nonresident income tax: extension of the exemption applying to dividends distributed by Spanish companies to parent companies resident in another EU Member State or to states in the European Economic Area.

Furthermore:

- Technical aspects of VAT and the taxes on oil and gas have been modified.

- The transfer and stamp tax rate applicable to the transfer and reinstatement of titles of nobility has been updated to 1%.

The fixed rate for levies charged by the central government tax authorities has been updated, generally, to 1%, except for levies that have been specifically created or updated by laws enacted in 2011.

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