

Spanish Tax Alert

Main amendments introduced by the Royal Decree Act 3/2016

Gómez-Acebo & Pombo Tax Area

On December 3rd, 2016, it was published in The Estate Official Bulletin the Royal Decree Act 3/2016 of December 2nd, whereby several tax measures are adopted geared towards the consolidation of public finances and other urgent social measures.

By virtue of this Royal Decree Act, several tax measures have been adopted geared towards the consolidation of public finances with the aim to encourage growth, employment creation and reduction of public deficit. These measures specifically encompass certain amendments within the Act 27/2014 of November 27th regarding Corporate Income Tax; Royal Decree Act 13/2011 of December 28th on Special Taxation; Act 58/2003 of December 17th on General Taxation, Act 20/1990 of December the 19th on the Taxation regime of the Cooperatives; and Act 11/2009 of October 26th regulating the REITs. Additionally, the land registry value of 2.452 municipalities are updated.

The most significant amendments take place within the scope of the Corporate Income Tax (“**CIT**”) and in particular, affecting mainly the regime applicable to the compensation of tax losses, reversal of impairment losses on securities representing a holding in the share capital or equity and participation exemption on capital gains.

Some of these measures are applicable for tax periods beginning from January the 1st, 2016 and tax periods beginning from January the 1st, 2017.

1. Corporate Income Tax

1.1. Measures applying for tax periods commencing from January the 1st, 2016.

a) Compensation of tax losses (art. 26.1 and 67e)

a.1) Large entities

A new limit for the compensation of tax losses has been introduced within the same terms as per clause g) of the thirty fourth transitional provision of the Corporate Income Tax for those entities whose net turnover is at least 20 million euros during the 12 months prior to the date of commencement of the tax period. The new limit to compensate tax losses is:

- 50% of the tax base prior to applying the capitalization reserve and its compensation, when the net turnover was at least 20 million euros but less than 60 million euros in the 12 months prior to the beginning of the tax period.
- 25% of the tax base prior to applying the capitalization reserve and its compensation, when the net turnover was at least 60 million euros in the 12 months prior to the beginning of the tax period.

The aforementioned limits are equally applicable to the compensation of tax losses of the tax group, as well as the pending tax losses of any entity at the moment of its integration to the tax group.

a.2) Small and medium entities

The limit for compensation of tax losses has not only been granted to large entities, the limit applicable for small and medium entities has also been reduced.

Therefore, those entities whose net turnover is less than 20 million euros during the 12 months prior to the commencement of the tax period will have a limit on their compensation of 60% of the tax base prior to applying the capitalization reserve and its compensation, instead of the 70% as per the current limit of the "CIT" Act.

However, for these entities, the minimum amount of 1 million euros is kept. Likewise, it is worth mentioning that, unless there is another amendment, for 2017 tax year the limit will be 70%.

b) *New limit on non-deductible impairment losses on bad debt of a non-related debtors as the contributions to social security system which generated deferred tax assets (art. 11.12, 62.1 e) and 67 d))*

b.1) Large entities

The limits for the integration of non-deductible impairment losses on bad debt of non-related debtors on the unfulfilment of the 6 months period expiry date, as well as the contributions to social security systems which had generated deferred tax assets are:

- 50% of the tax base prior to applying the capitalization reserve and its compensation, when the net turnover is at least 20 million euros but less than 60 million euros in the mentioned 12 months prior to the beginning of the tax period.
- 25% of the tax base prior to applying the capitalization reserve and its compensation when the net turnover is at least 60 million euros in the mentioned 12 months prior to the beginning of the tax period.

b.2) Small and medium entities

For those entities whose net turnover is less than 20 million euros during the 12 months prior to the beginning of the tax period, the limit of 60% will replace the current limit of 70% applicable to non-deductible impairment losses on bad debt of non-related debtors on the unfulfilment of the 6 months period from the expiry date, as well as the contributions to social security systems which had generated deferred tax assets.

c) *Joint limit of the tax credits for the elimination of double taxation (art. 31 and 32)*

Also coming into force for tax periods starting on January the 1st, 2016, for taxpayers whose net turnover is of at least 20 million euros during the 12 months prior to the beginning of the tax period, there is a joint limit of 50% upon the tax quota for tax credit for the elimination of double taxation (*art. 31 and 32 of the "CIT"*), tax credit for the elimination of double taxation due to the imputation of positive income on application of the controlled foreign company rules (clause 11 of article 100 of the "CIT") and tax credit for the elimination of double taxation foreseen in the transitory provision 23rd of the "CIT".

The limit affects the tax credit accrued in the tax year and those pending tax credits which have been generated in previous years.

d) *Minimum yearly for the reversal of impairment losses on securities representing a holding in the share capital or equity deducted prior to January the 1st, 2013 (DT 16)*

With the approval of the "CIT" Act, impairment losses on share value which were

tax deductible during the tax periods beginning before January the 1st, 2013, had to be reverted in the tax base of the period in which the increase of the net equity was produced, with the limit on such increase, or when the distribution of dividends was to take place on the amount received.

Notwithstanding, the Royal Decree Act 3/2016 introduces a minimum yearly reversal independent of a positive variation of the net equity or of the dividends distribution, by virtue of which those impairment losses on share value deducted prior to January the 1st 2013 will be included, as a minimum, on equal parts on the tax base, during the five tax periods beginning as from January the 1st, 2016.

In the cases where, on applying the limit on the increase of the net equity or income from dividends a larger amount than the amount corresponding to the minimum yearly reversal had been reverted, the remaining amount to be reverted will be included by equal parts during the remaining tax periods until the 2020 tax period.

Furthermore, in case of share transfers during these five tax periods, the amount pending to be reverted should be included with the limit of the positive income obtained in the transfer.

1.2. Measures applicable for tax periods starting on January the 1st, 2017

a) Participation exemption on capital gains and applicable regime to loss income from the transfer of shares (art.21)

By the approval of Royal Decree Act 3/2016 some special issues regarding the participation exemption are introduced, according to the nature of the shareholder of the participated entity:

- for those restructuring transactions in which the non-inclusion of income on the "CIT" or on the Non Resident Income Tax tax base had been determined, the exemption will not be applicable on the deferred income derived from asset contributions and contribution of shares, when these do not fulfill the share participation percentage or acquisition value threshold, or when the entity whose shares are contributed, do not fulfill in any of the tax years, the minimum nominal taxation requirement of 10%.
- when the non-inclusion of income in the tax base occurs within the scope of personal income tax and is derived from contributions of shares in companies, any transfer of such shares by the receiver during the two years following the date of the contribution shall lead to the non-applicability of the exemption due to the positive difference between the tax value (i.e., the contributing natural person shareholder's acquisition value) and the market value at the time they were contributed, unless the individual shareholder transferred the shares in the company after paying the personal income tax.

Similarly, as a result of the amendments introduced by art. 21 CIT, the full amount of

negative income may not be included when the entity fulfils the requirements to apply the participation exemption on share transfers under article 21(3) IT, regardless of whether or not it belongs to a group pursuant to article 42 of the Code of Commerce. If it partially fulfils such requirements, the non-inclusion of the loss shall also be partial.

The total or partial non-inclusion of losses is also applicable to those companies with a permanent establishment that pay CIT and Non Resident Income Tax, have an interest in a REIT and fulfil the requirements set out in art. 21 CIT. However, the non-applicability of the participation exemption to capital gains on share transfers remains the same.

It also adds a new limitation on the inclusion of negative income derived from share transfers when the investee is dissolved. In this case, the negative income will be reduced by an amount equal to the dividends received in the ten years prior to the dissolution which qualified for the exemption or the allowance for elimination of double taxation and did not reduce the acquisition value.

- b) *Non-deductibility of decreases in the share value due to application of fair value criteria (trading portfolio; Art. 15(I))*

In line with the restriction on integrating losses derived from share transfers in the scope of application of art. 21 CIT and the non-deductibility of impairments in share value, a new case of non-deductibility has been added under article 15.

Thus, as of 1 January 2017, impairments in the value of shares of resident companies that fulfil the requirements of art 21 CIT and non-resident companies that do not comply with the minimum taxation of 10% provided for in paragraph 1 (b) of that article due to application of the fair value criterion shall be non-deductible unless an increase in value of the same amount has been previously included in the tax base.

- c) *Exclusion of negative income derived from the transfer of foreign permanent establishments (art. 22)*

As a result of the amendments introduced by Royal Decree-Act 3/2016 in art 22 CIT, as of 1 January 2017, negative income derived from the transfer of permanent establishments may no longer be included. However, the inclusion of such negative income may be included in the case of cessation of business, with the same limits as prior to the amendment.

- d) *Negative income derived from the transfer of securities representing a holding in the share capital or equity when the acquirer belongs to the same group (art. 11.10)*

Owing to the restrictions introduced in article 21 CIT on the inclusion of losses from

share transfers, article 11(10) introduces a clarification, establishing that negative income from an intra-group transfer shall be reduced by the positive income obtained from transfers to third parties, provided that the requirement of interest or minimum acquisition value under article 21 CIT is not met and, in the case of non-resident entities, the requirement of 10% minimum nominal taxation under sub-article 1(b) of the aforementioned article is met.

- e) *Impairment losses on securities representing a holding in the share capital or equity (arts. 13 and 15)*

Although the non-deductibility of impairment losses on securities representing a holding in the share capital or equity was already provided in the CIT, as an addendum to the amendments introduced in article 21 of the Act, lawmakers have had to qualify such non-deductibility in those cases that fulfil the minimum shareholding or acquisition value requirement (art. 15(k)) as well as in those that do not fulfil it (art. 13(2)).

2. Tax regime for cooperatives

With respect to the amendments introduced in the Special Tax Regime for Cooperatives for financial years starting as of 1 January 2016, the offsetting of negative taxes is limited in the following way:

- 50%, when the net turnover was at least 20 million euros but less than 60 million euros in the 12 months prior to the beginning of the tax period.
- 25%, when the net turnover was at least 60 million euros in the 12 months prior to the beginning of the tax period.

3. Excise Duties

Royal-Decree Act 3/2016 introduces changes in the rates of Duties on Intermediate Goods, on Alcohol and Alcoholic Beverages as well as the tax regimes for artisan distillery and harvesting.

In general, the rates will go up as of 3 December 2016. Notably too, where the duties are payable in the Canary Islands.

In respect of the duties on tobacco products, the Royal-Decree Act increases the weighting of the specific component as opposed to the ad valorem component, for both cigarettes and rolling tobacco.

4. General Tax Law

New instances of debts that can be deferred or paid in instalments are effective as of 1 January 2017 and the following applications are declared inadmissible:

- In the case of withholder debts, which were already non-deferrable, the exception provided until now for the cases set out in art. 82(2)(b) of the Act is abolished.

- Debts resulting from the enforcement of decisions fully or in part against the complainant which had been previously stayed during appeals or applications.
- Debts derived from output taxes, such as VAT, unless it can be proved that the taxes were not paid.
- Debts for unpaid instalments of corporate income tax.

5. Private Wealth Tax

The application of the Private Wealth Tax is extended to 2017 on the same terms as in 2016. Therefore, unless similar legislation is approved, a state-wide tax credit of 100% will be applied in 2018.

6. Adjustment coefficients for cadastral values

The Act modifies the adjustment coefficients for cadastral values set out in article 32(2) of the Real Estate Cadastre (Recast) Act, which shall be applied to the municipalities included in Order HAP/1553/2016 of 29 September.

7. Immediate Provision of Information (SII)

We should highlight that, together with the measures adopted by virtue of Royal-Decree Act 3/2016, the Cabinet has approved a Royal Decree introducing amendments to the Value-Added Tax Regulations in order to regulate the new VAT-related Immediate Provision of Information System (SII).

This system will allow the Tax Agency to improve its tax control while establishing a new VAT management system based on the keeping of VAT records through the AEAT's website, supplying invoicing records practically in real time.

Taxpayers required to file a VAT self-assessment on a monthly basis (taxpayers registered with the Monthly VAT Refund Register, large companies and VAT groups) must be included in the SII system, while other taxpayers not required to do so may choose to take part in the system.

The SII will enter into force on 1 July 2017. For the first half-year it is in force, information must be provided within the eight days following issuance of an invoice; once this transitional period ends, the time limit will be four days.