

Spain allows for the conversion of DTAs into effective tax credits, improving banks' capital positions

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New tax rules should allow banks not to be required to deduct certain deferred tax assets ("DTAs") from Core Equity Tier 1 ("CET 1") under EU Regulation 575/2013 of 26 June 2013 ("Capital Requirements Regulation" or "CRR").

New tax rules allowing for the conversion of DTAs into effective tax credits apply to DTAs arising from temporary differences originating from the impairment of loans and assets received in exchange for loans, from pension and early retirement schemes, and from tax losses caused by the reversal of the aforementioned temporary differences.

Background

CRR, which will become effective on 1 January 2014, introduced restrictions to the nature of DTAs which are exempt from direct deduction from CET 1. These should be limited to DTAs originating from temporary differences that are mandatorily and compulsorily converted into a tax credit in case of loss, insolvency or liquidation that can be offset against any tax liability, and in the case of excess tax credit, converted into a direct claim against the state.

Italy in year 2011 and, more recently, Brazil (for similar Basel III purposes), introduced tax measures for mitigating the impact on CET 1 of such a limitation.

Scope

The new measures introduced in Spain have a broad scope of application: they apply to all corporate tax payers irrespective of the sector of activity in which they operate, although, considering the impact on regulatory capital, the

greatest benefit would be for credit and investment services firms.

Content

DTAs covered

For fiscal years starting in 2014, DTAs corresponding to the impairment of loans or of assets acquired in payment of loans, and contributions to certain pension schemes, will be converted into an effective credit against the tax administration in either of the following circumstances:

- a) The taxpayer registers accounting losses in its annual accounts, which are audited and approved by the corresponding body. In this case, the amount of DTAs converted will be the result of multiplying the total amount by the percentage that the accounting losses represent with respect to the sum of capital plus reserves.
- b) The entity is liquidated or declared insolvent by a court.

DTAs corresponding to tax losses which have been generated through the reversal of the abovementioned DTAs from the year 2014 will also be covered by the conversion.

Timing of the conversion

The conversion will take place at the time of filing the corporate tax return corresponding to the fiscal year in which circumstances a) or b) above occur (for those companies with a calendar fiscal year, the filing term is between the 1st and the 25th of July of the following year). The credit can be directly claimed or offset against any tax liability generated after the conversion. After 18 years, counted from the date on which the DTAs were recorded for accounting purposes (or from the date on which this law comes into force with respect to DTAs registered before), such DTAs can be converted into government bonds if not refunded or offset earlier.

Retroactivity and other measures

With effects beginning in fiscal year 2011, DTAs with origin in the abovementioned items would only revert to the extent they did not exceed the taxable profit of the year before offsetting the prior year's tax losses. The excess will be carried forward with the same limits.

Special rules are defined for the application of the same principle to tax groups and to the incorporation or exclusion of companies from said groups.

Conclusions

The tax measures enacted will improve the regulatory capital position of credit and investment services firms under CRR; however, the practical application of the rules may be difficult and guidance from the tax authorities is likely to be issued. PwC will provide further updates in this case.

PwC contacts

If you would like further advice or information in relation to the issues outlined above, please call your local PwC contact or any of the individuals listed below:

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