

The Constitutional Court Declares Tax on the Increase in Value of Urban Land to Be Unconstitutional in Cases of Decrease

The judgments of the Spanish Constitutional Court (CC) dated February 16, 2017 and March 1, 2017, decided two questions of unconstitutionality raised by the Contentious-Administrative Courts of Donostia and Vitoria, respectively, in relation to the provincial regulations regarding Tax on the Increase in Value of Urban Land (IIVTNU) of Guipúzcoa and Álava, and, in particular, the infringement of the principle of financial capacity set down in the Spanish Constitution (*Constitución Española*).

It should be recalled that IIVTNU is a tax applied to the increase in value of land from the time of acquisition until the time of transfer by the person liable to pay the tax. The increase in value is quantified by applying various coefficients to the cadastral value of the land, which is set by each town or city hall. The applicable coefficient depends on the length of time of possession, with a minimum of one year and a maximum of 20, so that there is a lineal increase in the land's value over time. This calculation produces the tax base to which the tax rate – which cannot be more than 30% – is applied.

Therefore, when dealing with a clear property-related loss (the difference between transfer value and acquisition value), the tax calculation system attributes, in every case, an increase in the value of the land, and it does not permit to avoid the taxation of actual decreases in value or to prove such a decrease, which leads to the case in which non-existent increase is being taxed.

In this regard, the aforesaid judgments stated that it is constitutional to establish or create taxes for the achievement of public aims or the satisfaction of public interests guaranteed by the Spanish Constitution, provided that the above-mentioned financial capacity shall be proved as a real or potential wealth or income in the majority of cases set down by the legislature when it created the tax.

However, in order to guarantee the constitutional principle of financial capacity to be unaffected, this tax must not take into consideration acts or events which are not examples of real or potential wealth increase – that is to say, those cases in which the financial capacity subject to the tax is non-existent, unreal or fictitious.

Therefore, even though in accordance with the regulations, the taxable event for IIVTNU is the “increase in value” that the land may have undergone in a given period of time, which is quantified and subject to taxation at the time of its transfer, that taxation is not tied to the existence of any such “increase” but rather to mere ownership of the land for a calculable period of time, which varies from one (minimum) to 20 years (maximum).

Thus, according to the CC's judgments, simply being an owner of urban land was enough to be tied, as an inseparable and irrefutable consequence, to an increase in value subject to taxation which was quantified automatically through applying to the land's value (for the purposes of real property tax) a fixed percentage for each year of ownership at the time of transfer, irrespective of the actual amount and the existence of any such increase in value.

Likewise, as the CC explains, the fact that the existence of a tax obligation is made dependent on the transfer of land may be a necessary condition in the configuration of a tax whose subject is the “increase in value”, but in no event can it be established as sufficient condition for a tax on the “increase in value” of land. Therefore, in addition to the fact of that transfer, an increase in the value of the land must actually take place, an example of actual or at least potential financial capacity. However, when there has been no such increase in the value of the land transferred, the financial capacity subject to tax ceases to be potential and becomes unreal or fictitious, thereby breaching the principle of financial capacity.

In view of the above, since the calculation of IIVTNU applies in situations of both increase and decrease, the CC reached the conclusion that the tax is illegal in cases where there was no real increase in the land's value and that said increase is a fiction, given that mere ownership of the land does not entail an increase in its value. Specifically, the CC stated:

“Imposing on the taxpayers the obligation to bear the same tax burden that applies in cases of increases deriving from the passage of time... directly contradicts the principle of financial capacity guaranteed by the Constitution.”

Therefore, the unconstitutionality of this tax cannot be applied as a general rule, but only in those cases subject to taxation when there is no actual increase in value (real increase in land value) because it would be entirely contrary to the principle of financial capacity contained in the Spanish Constitution.

It should be noted that the CC only declares the unconstitutionality of the IIVTNU calculation system established in the provincial regulations governing IIVTNU in Guipúzcoa and Álava. However, the same system is set down in articles 104 and 107 of the Local Revenue Authorities Act (*Ley de Haciendas Locales*), and therefore the CC's judgements will oblige the amendment of both provincial and national regulations. It now falls to the legislature to make the appropriate changes to the tax system so as to avoid taxation where there is no increase in value at the time urban land is transferred.