

## **Constitutional Court (Plenary session), Judgement 59/2017 of 11 May**

The Constitutional Court (TC), in its judgment number 59/2017 of 11 May, has ruled on the matter of unconstitutionality posed by Contentious-Administrative Court number 1 of Jerez de la Frontera, due to a violation of the principle of economic capacity in relation to application of the Tax on the Increase in Value of Urban Land (IVITNU), also known as municipal capital gain.

The TC has declared that application of the municipal capital gain is unconstitutional when there is no increase in the value of land or if a loss may have occurred. This court has previously ruled in this manner, resolving the matters of unconstitutionality raised by the Contentious-Administrative Courts of Donostia and Vitoria, respectively, even though they concern regional schemes that could be subject to substantial differences.

In this case, the court analysed the unconstitutionality of Article 107 of the Law of Public Treasuries (hereinafter, the "LHL") regarding the potential violation of the principle of economic capacity contained in Article 31.1 of the Spanish Constitution. Thus, Contentious-Administrative Court number 1 of Jerez de la Frontera deemed that said law, in any event, attributes a positive value increase in application of the rules for determining the tax base that must be applied, given its mandatory nature, without contemplating the possibility that there might be a decrease in the value of the land at the time when the property is transferred. Consequently, since the precept in question does not contemplate events of a decrease in value in the sale of real property, even though it is a real possibility, non-existent or fictitious manifestations of wealth are subject to taxation.

In turn, the state counsel's office supported the position of said court, using previous judgments as references, and considering that it is necessary to declare the unconstitutionality and consequent invalidity of Articles 107.1, 107.2 a) and 110.4 of the LHL, albeit only to the extent that a non-existent situation of a value increase is subject to taxation, given that the law does not allow local corporations to disregard the legally established calculation rule.

The aforementioned notwithstanding, the state's attorney maintained a radically opposed position, whose arguments were based on the existence of confusion between the terms "real value" and "cadastre value", given that the legislature opted to objectively calculate the value increase derived from the transfer of a piece of urban property, without considering the circumstances of the specific case. Thus, for the state's attorney, the value of the land to be considered for calculating the tax is the cadastre value. Therefore, the amount of the tax increases according to the number of years that elapse between acquisition and transfer of the land (with a maximum of 20 years), regardless of the real gain earned with the transfer. Consequently, said tax should not be understood as contrary to the principle of economic capacity and should therefore not be unconstitutional.

However, the Constitutional Court deems in the current judgment that this case is comparable to the cases posed in the previous judgments, given that the treatment given by the regional laws to the events of no increase, or even a decrease in the value of urban land, lacked any reasonable justification, because taxpayers were forced to bear the same tax charge as if there were an increase in the value of the land due to applying a mandatory rule for the determination of value increases, and there was no precept that provided for the possibility of using any other alternative method. In this regard, the court explains that, while it is constitutionally admissible that the legislature might be able to establish taxes that are aimed at satisfying the public interests guaranteed by the Constitution, this should be done in any event without establishing a tax that considers acts or events that do not represent real or potential wealth, or also when the economic capacity burdened by the tax is non-existent or fictitious. In the words of the court, "one thing is to tax a potential income (the increase in value that presumably occurs with the passage of time in all urban land), and something far different is subjecting unreal income to taxation".

Consequently, the Constitutional Court deemed that the municipal capital gain violates the constitutional principle of economic capacity to the extent that it is not necessarily linked to the existence of a real increase in the value of the asset, rather to the mere ownership of the land for a period of time. Therefore, the court declared the unconstitutionality and invalidity of Articles 107.1, 107.2 a) and 110.4 of the LHL, not without first making two clarifications: first, in general it deems that the tax is not contrary to the Spanish Constitution; and second, it urges the legislature to make all the pertinent modifications or adaptations to the legal scheme of the tax to allow judging a way to not submit non-existent situations of a value increase in urban land to taxation.