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The International Comparative Legal Guide to:

Corporate Tax 2015

11th Edition

A practical cross-border insight into corporate tax work

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The International Comparative Legal Guide to: Corporate Tax 2015

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EDITORIAL

Welcome to the eleventh edition of *The International Comparative Legal Guide to: Corporate Tax*.

This guide provides the international practitioner and in-house counsel with a comprehensive worldwide legal analysis of the laws and regulations of corporate tax.

It is divided into two main sections:

One general chapter. This chapter is entitled “The Road to (VAT) Recovery”.

Country question and answer chapters. These provide a broad overview of common issues in corporate tax laws and regulations in 41 jurisdictions.

All chapters are written by leading corporate tax lawyers and industry specialists and we are extremely grateful for their excellent contributions.

Special thanks are reserved for the contributing editor William Watson of Slaughter and May for his invaluable assistance.

Global Legal Group hopes that you find this guide practical and interesting.

The *International Comparative Legal Guide* series is also available online at www.iclg.co.uk.

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1 Tax Treaties and Residence

1.1 How many income tax treaties are currently in force in Portugal?

Portugal has 63 tax treaties in force and another four for which ratification is still pending. These include all the EU Member States (except for Croatia) and also Switzerland, Norway, Ukraine and Russia as well as many Latin American countries (Brazil, Mexico, Venezuela, etc.), the United States of America, China, Japan and several African countries.

1.2 Do they generally follow the OECD or another model?

As a member of the OECD, Portugal follows the OECD Model, a notable exception being the treaty with the USA, which follows the US Model.

1.3 Do treaties have to be incorporated into domestic law before they take effect?

Treaties do not have to be incorporated into domestic law, but they must be approved by Portuguese Parliament and ratified by the President of the Republic.

1.4 Do they generally incorporate anti-treaty shopping rules (or "limitation on benefits" articles)?

Most treaties signed by Portugal do not include limitation on benefits clauses. However, the treaty with the US includes such a clause (article 17). The most recent treaties and those which are being renegotiated include anti-avoidance clauses (e.g. number 6 of the Protocol of the Treaty with Chile) and some older treaties exclude certain types of entities from treaty benefits.

1.5 Are treaties overridden by any rules of domestic law (whether existing when the treaty takes effect or introduced subsequently)?

No. Treaties supersede domestic law.

1.6 What is the test in domestic law for determining corporate residence?

According to domestic law, a company is deemed to be resident in Portugal if it has the legal seat or place of effective management in Portugal. Cases of dual corporate residence may be solved through tax treaties.

2 Transaction Taxes

2.1 Are there any documentary taxes in Portugal?

Yes. Stamp Tax (*Imposto do Selo*) is levied on all the acts, contracts, documents, titles, papers and other facts listed in an Annex to the Stamp Tax Code. It is levied, *inter alia*, on acquisitions of real estate, leases, guarantees, financial operations, insurances, debt securities and on the transfer of business as a going concern.

The most relevant Stamp Tax rates are 0.04% per month for loans lasting less than a year to 0.6% for loans lasting more than five years on the value of the credit utilisation in any financing operations or on the value of a guarantee when not accessory to an act or contract already subject to Stamp Tax. Insurances are also taxed between 3 and 9% on the value of the policy, depending on the type of risk covered.

2.2 Do you have Value Added Tax (or a similar tax)? If so, at what rate or rates?

Yes. The applicable VAT rates are the standard rate (23%), the intermediate rate (13%) and the reduced rate (6%).

The rates in Azores and in Madeira are lower than those applicable on the mainland – from 1 to 3 percentage points.

2.3 Is VAT (or any similar tax) charged on all transactions or are there any relevant exclusions?

There are few transactions excluded from VAT, such as the transfer of a business as a going concern, but there are a significant number of exemptions, e.g. health-related services; financial and insurance services; and real estate transactions (both leases and transfers).

2.4 Is it always fully recoverable by all businesses? If not, what are the relevant restrictions?

Businesses are entitled to deduct the VAT due or paid in the acquisition of goods or services whenever used for the purposes of taxable transactions. If a business carries out both taxable and non-taxable operations, only the *pro rata* attributable to the former shall be deductible from the whole of the VAT borne. Input VAT linked to financing activities and B2C real estate operations is typically partially or fully non-recoverable.

2.5 Are there any other transaction taxes?

Property Transfer Tax (*Imposto sobre a Transmissão Onerosa de Imóveis*) is levied on the transfer of real estate situated in Portuguese territory for consideration. The rates vary between 5 and 6.5% of the tax value of the property.

2.6 Are there any other indirect taxes of which we should be aware?

Excise Duties are imposed on the following goods:

- alcohol and alcoholic beverages (beer, wine, other fermented beverages, ethyl alcohol);
- manufactured tobacco;
- mineral oils (petrol, gas oil, liquid petroleum gas and methane, heavy fuel oil and kerosene); and
- energy products and electricity (natural gas, coal and electricity).

3 Cross-border Payments

3.1 Is any withholding tax imposed on dividends paid by a locally resident company to a non-resident?

Dividends paid by Portuguese companies to non-residents are subject to a general 25% withholding tax, which, however, may be reduced or eliminated under tax treaty provisions, Directive 2011/96/EU, of 30 November ('Parent/Subsidiary Directive') or domestic law.

If the dividends are paid or made available to a resident in a tax haven or in accounts held on behalf of non-identified third parties, a 35% withholding tax is applied.

Dividends paid by Portuguese subsidiaries to parent companies resident in the EU, EEA and treaty countries bound by administrative cooperation in the field of tax are exempt from withholding tax, if the recipient company:

- is subject and not exempt from corporate income tax (CIT), provided the local statutory rate is at least 60% of the Portuguese general rate; or
- has held a direct or indirect participation of at least 5% in the share capital or of the voting rights of the Portuguese subsidiary for at least 24 consecutive months.

Pursuant to the EU/Switzerland Agreement of 29 December 2004, Swiss parent companies also benefit from the above exemption, but the applicable shareholding threshold is 25%.

The dividends paid by companies licensed to operate within Madeira's free-trade zone are also exempt from CIT.

3.2 Would there be any withholding tax on royalties paid by a local company to a non-resident?

Royalties paid by Portuguese companies to non-residents are subject to a 25% withholding tax, unless a reduction is foreseen in tax treaties.

If the royalties are paid or made available to a resident in a tax haven or on accounts held on behalf of non-identified third parties, a 35% withholding tax is applicable.

Under the EU Interest and Royalties Directive, there is an exemption from withholding tax relative to royalties paid to associated companies if:

- the beneficiary is subject and not exempt from CIT;
- the beneficiary assumes one of the forms listed in the Directive's Annex; or
- the beneficiary is resident for tax purposes in another EU Member State.

A company is 'associated' with another company whenever one of them holds a minimum of 25% of the other's share capital or a third company holds a minimum of 25% of both companies' share capital, as long as, in any case, the shareholding is maintained for at least two years.

Under the Agreement referred to in question 3.1, royalties paid to a Swiss associated company are also exempt from withholding tax.

3.3 Would there be any withholding tax on interest paid by a local company to a non-resident?

Interest payments by Portuguese companies to non-residents are subject to a general 25% withholding tax, unless a reduction is foreseen in tax treaties.

If the interest are paid or made available to a resident in a tax haven or on accounts held on behalf of non-identified third parties, a 35% withholding tax is applicable.

Under the EU Interest and Royalties Directive and the Agreement referred to in question 3.2, there is an exemption from CIT on interest paid to EU and Swiss associated companies (please refer to the conditions set forth in question 3.2).

3.4 Would relief for interest so paid be restricted by reference to "thin capitalisation" rules?

No. Nevertheless, there is a general limitation on the deductibility of net financing costs, which shall not be accepted whenever their value exceeds:

- €1,000,000; or
- 30% of the Earnings Before Interest, Taxes, Depreciation and Amortisation (EBITDA) of the taxpayer.

Non-deductible net financing costs can be carried forward for five taxation periods within the aforementioned yearly threshold. They can be carried back within the same period, for the positive difference between 30% of the EBITDA of the taxpayer and the actual net financing costs incurred.

This limitation is not applicable to financial institutions and insurance companies.

3.5 If so, is there a "safe harbour" by reference to which tax relief is assured?

See question 3.4 above.

3.6 Would any such rules extend to debt advanced by a third party but guaranteed by a parent company?

The rules in question 3.4 above apply to related and unrelated entities.

3.7 Are there any other restrictions on tax relief for interest payments by a local company to a non-resident?

Interest payments from shareholders' loans are not deductible on the part exceeding:

- the 12-month Euribor rate + 1.5% spread; or

- the 12-month Euribor rate + 6% spread (if the borrower is a small or medium-sized company).

The abovementioned limitation is not applicable when lender and borrower are related companies (in practice, this limitation only applies when the lender owns less than 20% of the borrower's share capital).

3.8 Is there any withholding tax on property rental payments made to non-residents?

Yes. There is a 25% withholding tax whenever the tenant is a corporation or an individual subject to mandatory bookkeeping.

This withholding tax is paid on account of the final tax due and the beneficiary must file an annual tax return.

3.9 Does Portugal have transfer pricing rules?

Yes. Portuguese transfer pricing rules follow the OECD's guidelines. They apply to any commercial transactions between two entities deemed to be *specially related* (roughly, those that have a direct or indirect 20% shareholding relationship or may exercise a significant influence in the other's decisions). For taxpayers with an annual turnover exceeding €3,000,000, a transfer pricing tax file documenting all related party transactions must be kept and updated annually.

4 Tax on Business Operations: General

4.1 What is the headline rate of tax on corporate profits?

The headline CIT rate is 23%.

For small- and medium-sized companies there is a reduced 17% rate applicable to the first €15,000 of the taxable profit.

A Municipal surtax with a maximum rate of 1.5% is levied on the net taxable profits amount.

In addition, a State surtax is levied on the same amount when higher than €1,500,000, at the following rates:

- Between €1,500,000 and €7,500,000: 3%.
- Between €7,500,000 and €35,000,000: 5%.
- Above €35,000,000: 7%.

In the Azores, the headline rate of CIT is 18.4%.

4.2 When is that tax generally payable?

The periodic tax return must be filed annually until the last day of May of the year following that to which the income relates (or until the last day of the fifth month following the end of the taxable period concerned whenever that taxable period does not match the calendar year).

CIT is payable in three payments on account, due in July (or the 7th month), September (or the 9th month) and 15 December (or the 15th day of the 12th month) of the taxable year concerned.

Payments on account are based on the CIT paid in the previous tax year net of withholding taxes that cannot be either offset or refunded.

There is also a special payment on account that is due in March (or in two instalments in March and October) of the respective year. The special payment on account corresponds to a percentage of roughly 0.2% of the turnover with a floor of €1,000 and a cap of €70,000.

4.3 Is the tax base accounting profit subject to adjustments, or something else?

The corporate taxable income is based on the accounting profit of the entity subject to specific CIT adjustments.

4.4 If the tax base is accounting profit subject to adjustments, what are the main adjustments?

The main adjustments are related to excessive depreciation, non-deductible interest (see questions 3.4 and 3.7 above), impairment losses, provisions, and others costs presumed not to be borne for business purposes (e.g. undocumented expenses, criminal and administrative fines, expenses related to boats for recreational use, aircrafts, and part of the travel, lodging and representation expenses).

4.5 Are there any tax grouping rules? Do these allow for relief in Portugal for losses of overseas subsidiaries?

A group can opt for a special group taxation regime when:

- the parent company holds directly or indirectly at least 75% of the share capital and more than 50% of the voting rights of the other group companies;
- the parent company has held the eligible shareholding for more than one year; or
- the parent company is not controlled by any other company in Portugal and has not renounced the regime in the previous three years.

The group taxable profit is equal to the sum of the individual taxable profits of each company. Carry-forward losses may be deducted in each taxable year for 70% of their amount and for as long as 12 years. Any non-deductible carry-forward losses in a given year – i.e. in excess of the 70% threshold – may be deducted in the following 12 years, subject to the same yearly threshold.

There is no relief for losses of overseas subsidiaries.

4.6 Do tax losses survive a change of ownership?

As a general rule, if 50% or more of the capital or voting rights of an entity changes hands, tax losses may not be carried forward unless so authorised by the Minister of Finance.

Such authorisation shall not be needed in case of:

- Change of ownership of the entity from direct to indirect or from indirect to direct.
- Change of ownership resulting from a tax neutral reorganisation (mergers, divisions, partial divisions, transfers of assets and exchanges of shares).
- Change of ownership arising from *mortis causa* succession.
- Change of ownership when acquirer has held, directly or indirectly, more than 20% of the share capital or of the majority of the voting rights of the entity since the beginning of the taxable period to which the losses concern.
- Change of ownership when the acquirer is an employee or a board member of the entity.

4.7 Is tax imposed at a different rate upon distributed, as opposed to retained, profits?

Since January 2014, small- and medium-sized resident entities for tax purposes can deduct up to 10% of the retained profits that are reinvested in the acquisition of investment assets deemed eligible.

This deduction can be made within two taxation periods at a cap of €5,000,000 per period, and cannot exceed 25% of the CIT payable.

4.8 Are companies subject to any significant taxes not covered elsewhere in this chapter - e.g. tax on the occupation of property?

Municipal real estate tax (*Imposto Municipal sobre Imóveis – IMI*) is due on the tax value of the immovable property by its owner, usufructuary, or holder of the surface right. IMI rates vary between 0.3 and 0.8% of the tax value of the property (7.5% for properties owned by entities domiciled in tax havens) and are paid on an annual basis.

5 Capital Gains

5.1 Is there a special set of rules for taxing capital gains and losses?

No, there is no special set of rules for taxing capital gains and losses.

5.2 If so, is the rate of tax imposed upon capital gains different from the rate imposed upon business profits?

Please see question 5.1 above.

5.3 Is there a participation exemption for capital gains?

Yes.

Capital gains and losses from the disposal of shares are excluded from CIT computation if the company whose shares are alienated meets the following requirements:

- it is subject and not exempt from CIT, provided the local statutory rate is at least 60% of the Portuguese CIT general rate;
- it has held a direct or indirect participation of at least 5% in the share capital or of the voting rights of the Portuguese subsidiary for at least 24 consecutive months; and
- the entity whose shares are being disposed of is not resident or domiciled in a tax haven.

This regime is applicable, under the same conditions, to the disposal of equity items other than shares (e.g. the so-called supplementary capital contributions).

5.4 Is there any special relief for reinvestment?

Capital gains arising from the disposal of tangible, intangible and biological assets benefit from a CIT exclusion in half of their amount if the respective proceeds are reinvested in the acquisition, production or construction of same kind of assets in the previous taxable period or until the second taxable period after the disposal. There is no such relief for disposals of shares.

5.5 Does Portugal impose withholding tax on the proceeds of selling a direct or indirect interest in local assets/shares?

Technically speaking, Portugal does not impose withholding tax on the proceeds of selling a direct or indirect interest in local assets/shares. However, capital gains from the sale of assets in Portuguese territory are taxed at a 25% flat rate, unless provided otherwise in the applicable tax treaties. Indirect interests on Portuguese assets may only be taxed in the terms set forth in question 8.2 below.

6 Local Branch or Subsidiary?

6.1 What taxes (e.g. capital duty) would be imposed upon the formation of a subsidiary?

No taxes are imposed upon the formation of a subsidiary in Portugal.

6.2 Are there any other significant taxes or fees that would be incurred by a locally formed subsidiary but not by a branch of a non-resident company?

There are no significant differences, in terms of taxes or fees, between the formation of a subsidiary and the formation of a branch in Portugal.

6.3 How would the taxable profits of a local branch be determined in its jurisdiction?

The taxable profit of the branch is determined according to the same rules applicable, *mutatis mutandis*, to companies with legal seat or place of effective management in Portugal which exercise a commercial, industrial or agricultural activity.

6.4 Would such a branch be subject to a branch profits tax (or other tax limited to branches of non-resident companies)?

From a tax standpoint, the status of a branch is similar to that of a subsidiary.

The branch is subject to the same tax rate as the subsidiary (please refer to question 4.1) and this tax rate is charged on the income attributable to the Portuguese branch.

6.5 Would a branch benefit from double tax relief in its jurisdiction?

As a rule, branches are not entitled to treaty benefits because they are not deemed to be residents in Portugal for tax treaty purposes.

However, tax treaties signed by Portugal have non-discrimination clauses according to which a branch cannot be treated differently than a Portuguese-domiciled company.

Moreover, the participation exemption regime (see question 5.3 above) is also applicable to Portuguese branches of entities domiciled in the EU (as far as the requisites of article 2 of the Council directive 2011/96/EU are met), in the EEA, or in a treaty country (as long as liable to administrative cooperation on tax matters with Portugal).

6.6 Would any withholding tax or other similar tax be imposed as the result of a remittance of profits by the branch?

No, this is not applicable in Portugal.

7 Overseas Profits

7.1 Does Portugal tax profits earned in overseas branches?

Portugal taxes its resident companies on their worldwide income and therefore profits earned in overseas branches are subject to tax in Portugal.

However, a Portuguese-resident entity with overseas branches profits may elect to exclude the profits (or losses) thereof from CIT computation provided:

a) the profits attributable to the branch are subject to an income tax whose statutory rate is not lower than 60% of the Portuguese CIT normal rate of 23% (i.e., the tax rate may not be lower than 13.8%); and

b) the branch is not located in a tax haven.

7.2 Is tax imposed on the receipt of dividends by a local company from a non-resident company?

As a general rule, dividends received by Portuguese companies from non-resident companies are subject to the normal CIT rate, unless the participation exemption regime applies. Under this regime, dividends paid by Portuguese subsidiaries to parent companies resident in the EU, the EEA and treaty countries bound by administrative cooperation in the field of tax are exempt from CIT, if the distributor:

a) is not domiciled in a blacklisted tax haven, is subject and not exempt from corporate income tax (CIT), provided the local statutory rate is at least 60% of the Portuguese normal rate;

b) has held or commits to hold a direct or indirect participation of at least 5% in the share capital or of the voting rights of the Portuguese subsidiary for at least 24 consecutive months; and

c) is not a look-through entity.

In the event the above conditions are not met, a Portuguese entity receiving profits previously charged with income taxes throughout the dividend distribution chain may still be entitled to a full tax credit for the elimination of the international economic double taxation.

7.3 Does Portugal have "controlled foreign company" rules and, if so, when do these apply?

Yes.

Portuguese CFC legislation applies when a Portuguese resident entity, directly or indirectly, holds a minimum shareholding of 25% or of 10% – where more than 50% of the share capital of the CFC is owned (directly or indirectly) by Portuguese resident shareholders – whenever that CFC is located in a blacklisted tax haven or (i) it is not subject to income tax, or (ii) the local statutory rate is lower than 60% of the CIT statutory rate.

With some peculiarities, the rule is that, if the CFC carries on an active business in the country where it is domiciled, its income will not be imputed to the Portuguese parent company.

This regime will not be applicable to any CFC domiciled in EU or EEA Member States (administrative cooperation in tax matters with Portugal being a requisite) when the Portuguese-resident entity demonstrates that the CFC was created for substantive economic reasons and earns income from the exercise of commercial, industrial, agricultural activities or from the rendering of services to other entities.

8 Taxation of Real Estate

8.1 Are non-residents taxed on the disposal of real estate in Portugal?

Yes. Non-resident companies which derive income from the disposal of real estate in Portugal are subject to a flat 25% rate.

8.2 Does Portugal impose tax on the transfer of an indirect interest in real estate located in Portugal and, if so, what constitutes an indirect interest?

Yes. Portugal imposes tax on the capital gains derived from the sale of shares in resident companies, 50% of whose assets are immovable. However, some tax treaties signed by Portugal disallow such taxation at source.

8.3 Does Portugal have a special tax regime for Real Estate Investment Trusts (REITs) or their equivalent?

Yes. Portugal has a special regime for Real Estate Investment funds (*Fundos de Investimento Imobiliário*).

Pursuant to this regime, income of Real Estate Funds is subject to the following taxation:

- Rental income – autonomous taxation at a 25% rate on the income net of maintenance and conservation expenses as well as of Municipal Property Tax.
- Capital gains from the disposal of immovable property – autonomous taxation at a 25% rate levied on 50% of the positive difference between capital gains and losses (i.e., 12.5% effective rate).
- Other income – 20% (income from debt securities, dividends and income from investment funds), and 25% for other items of income.

Acquisitions of immovable property benefit from an exclusion of 50% of the Municipal Property Tax and Property Transfer Tax normally due, but this incentive is directed only at open-end funds or closed-end real estate investment funds of public subscription.

9 Anti-avoidance

9.1 Does Portugal have a general anti-avoidance or anti-abuse rule?

Yes.

According to the Portuguese general anti-abuse rule (GAAR), acts and legal transactions are ineffective for tax purposes if they are essentially or mainly directed at, through artificial or fraudulent means and with abuse of juridical forms, the reduction, elimination or deferral of the taxes that would be due as a result of facts, acts or legal transactions with identical economical purpose, or at obtaining tax advantages that would not be achieved, totally or partially, without the use of those artificial or fraudulent means.

Should the GAAR be applicable, taxation is made in accordance with the legal framework foreseen in the absence of the artificial or fraudulent acts or legal transactions.

9.2 Is there a requirement to make special disclosure of avoidance schemes?

According to Decree-Law 29/2008 of 25 February, tax planning schemes aimed at obtaining tax advantages related to income, indirect and property taxes must be communicated to the Portuguese tax and customs authorities.

As a rule, the obligation to disclose falls upon the so-called "promoters", namely financial institutions, accountants, chartered accountants, lawyers and solicitors. If the promoter is a non-resident entity, the obligation to disclose switches to the beneficiary of the scheme.

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He was the President of the Portuguese Corporate Tax Reform Committee that drafted the 2014 Reform Law.
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