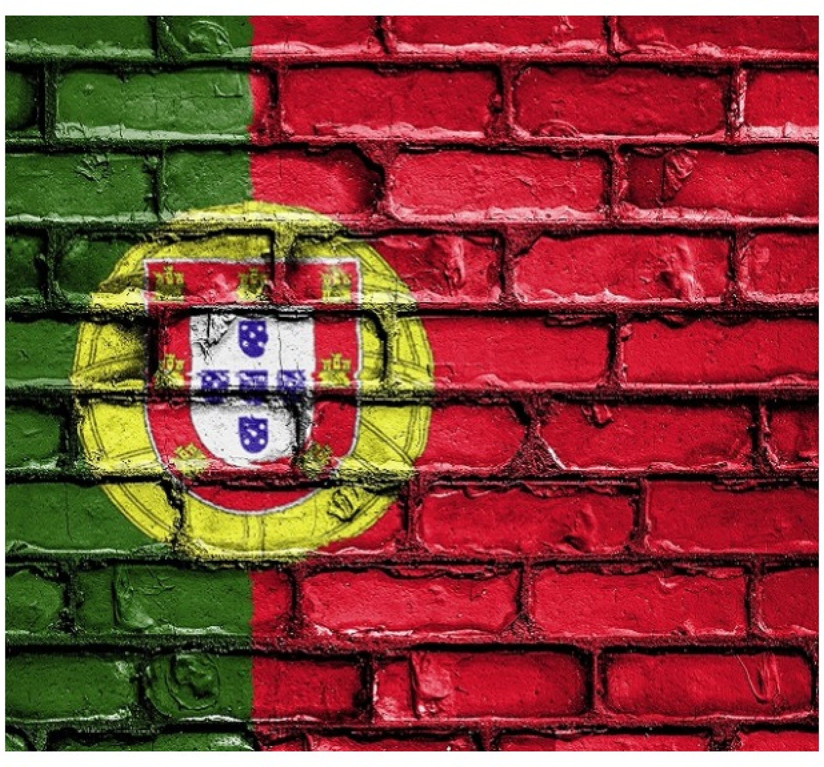
Portugal

A look at the Portuguese Budget Bill for 2021: Highlights for international investors

Ana Carrilho Ribeiro of Morais Leitão considers the scope of the permanent establishment concept in the 2021 Budget Bill.

By **Ana Carrilho Ribeiro**

October 28 2020



The measures are welcome incentives to help sustain investment

Portugal's Budget Bill for 2021 was published on October 12 2020 (the bill). Several provisions aim to stimulate an economy fragilised by the COVID-19 pandemic, such as the innovative *IVaucher* programme. This grants final consumers the opportunity to accrue an amount equal to VAT spent on purchases realised, with services' providers acting within the accommodation, restaurants and culture sectors, in the form of vouchers to be spent on future purchases within the same business sectors. Alongside such provisions, the bill also includes certain measures which may significantly impact the taxation of international corporate investors operating in Portugal.

In this context, several modifications aimed at broadening the scope of the permanent establishment (PE) concept for corporate income tax (CIT) purposes are foreseen. A few, noteworthy examples are highlighted below.

According to the bill, an enterprise's activities may be deemed to rise to PE status when a person (who is not an independent agent) acts on its behalf, and in doing so, habitually intermediates and concludes contracts binding such enterprise, namely contracts:

1. In the name of the enterprise;
2. For the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use; or
3. For the provision of services by that enterprise, or otherwise habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, or maintains, in Portuguese territory, or maintains a storage destined to deliver such goods on behalf of the company, even if such person does not intervene in the conclusion of such contracts.

Subject to specific requirements, the concept of PE is also extended to include certain activities which are generally considered as preparatory or auxiliary (and thus not deemed to constitute a PE). This includes matters such as a fixed installation or storage of goods which are utilised or maintained by an enterprise, when the latter, or a related party, carries-out a complementary activity which, when taken altogether, form part of a cohesive operating business unit.

Such provisions are aligned with the measures recommended to address the artificial avoidance of PE status, namely in Action 7 of the BEPS project, and mirrored in certain provisions included in Part IV of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI), and also addressed in the 2017 version of the Commentaries to the OECD Model Convention.

Notwithstanding, we note that Portugal has opted not to apply, namely, the provisions set forth in Articles 12 of the MLI, which may give rise to a discrepancy between the double tax treaties (DTT) in force and domestic legislation, in matters relating to PE status, which may give way to uncertainty on the practical application of these dispositions, and even lead to litigation.

Additionally, the bill foresees that a PE is deemed to exist when an enterprise provides services, including consulting services, through its own employees or other people hired by the same, to exercise such activities in Portuguese territory, when the activities take place during a period or periods which, in total, exceed 183 days in a 12 months' timeline. This provision closely follows the guidelines established by United Nations Model Convention, which may give rise to further mismatch between DTTs and domestic law on PE matters.

Separately, the bill includes a measure aimed at taxing, for property transfer tax purposes (IMT), the acquisition of more than 75% of the shares of a public limited liability corporation (*sociedade anónima*, or S.A.). This is the case when the company's assets are composed, in more than 50%, of real estate assets located in Portugal which are not allocated to an agricultural, industrial or commercial activities (not consisting of real estate buy and sell), whenever by virtue of such acquisition, a shareholder becomes the owner of at least 75% of the share capital of the company, or the number of shareholders is reduced to two, which are married or living in a registered civil partnership between themselves.

This provision creates an additional burden to the real estate business sector, in regard to share deals and restructuring transactions. However, among other questions relating to the practical implications of this provision, it remains to be confirmed by the tax authorities, whether the business of real estate property development is to be considered as included in the scope of this tax, or should be considered a commercial activity, in which case this provision should not impact acquisitions of shares of S.A. companies acting in the referred sector.

Finally, it should be noted that following the COVID-19 pandemic, other relevant provisions for corporate investors were adopted in the Supplementary Budget for 2020, of July 24 2020, namely provisions regarding taxable losses and the creation of the extraordinary tax credit (CFEI II), which also apply in 2021.

With regard to taxable losses, the loss carryforward period of 12 years applies for all companies, with respect to losses generated in 2020 and 2021 (previously, only small and medium enterprises would access this extended carryforward period). The taxable periods of 2020 and 2021 are not to be taken into account for purposes of calculating the carryforward period applicable to tax losses available in the first day of the 2020 fiscal year.

The CFEI II grants companies a CIT deduction amounting up to 20% of the investment in assets assigned to the enterprise's operations, which are realised between July 1 2020, and June 30 2021, and subject to specific conditions.

Overall, these measures are much welcome incentives to help sustaining corporate taxpayers during the present economic crisis, and not to lose more ground towards a much sought-after balance between increased public expense and tax revenue. It remains yet to be seen whether this may suffice.

Ana Carrilho Ribeiro
T: +351 213 817 489
E: acribeiro@mlgts.pt