

## LEGAL ALERT

# REIMBURSEMENT OF WITHHOLDING TAX BORNE ON DIVIDENDS, INTEREST AND ROYALTIES PAID TO NON-RESIDENT SHAREHOLDERS

Portuguese tax law foresees a 25% withholding of Corporate Income Tax (CIT) on outbound dividends, interest, and royalties to non-resident corporate shareholders. Provided some substantial and formal requirements are met a participation exemption may be applicable or a reduction of withholding tax due to the operation of a Double Tax Treaty (DTT).

One of the important features of this withholding tax regime is the possibility of reimbursement, totally or in part, of the tax withheld due to the non-compliance with the substantial or formal requirements for the exemption or the reduced rates to apply when withholding was due.

### 1. Dividend payments

An **exemption of withholding tax** is available for payments to corporate shareholders with a minimum stake of at least 10% in the share capital or voting rights in the subsidiary uninterruptedly held for one year prior to the distribution, provided those shareholders are residents *i)* in a Member State of the EU, *ii)* in a state member of the EEA bound to administrative cooperation in terms similar to the EU, or *iii)* in a State with which Portugal has in force a DTT that foresees exchange of information, and are subject (and not exempt) to a tax similar to the Portuguese CIT (and in the case of *iii)* above besides having a tax similar to the Portuguese tax, the standard rate of such tax cannot be less than, presently, 12,6%).

The exemption is not applicable if there is an arrangement put in place in which the primary purpose or one of its primary purposes is to obtain a tax advantage that defeats the purpose of eliminating the double taxation of dividends. In this case, it is not considered genuine (*i.e.*, it is not

made for valid economic reasons and does not reflect economic substance) taking all the relevant facts and circumstances into consideration. This regime should also not apply if the Portuguese subsidiary has not complied with the declarative obligations imposed by the legal regime of the central registry of the beneficial owner or if any of the declared beneficial owner is resident in a blacklisted tax haven except if it is possible to demonstrate that the beneficiary of the dividends is not part of a construction to contravene the purpose of the exemption.

Despite the exemption, the subsidiary resident in Portugal will withhold the CIT due when the one-year participation requirement is not yet met or when the companies do not demonstrate the compliance with the requirements to benefit from the exemption.

In these cases, the shareholder may request afterwards a **refund** of the tax withheld.

If the tax has been withheld because the one-year participation requirement was not yet met when the distribution occurred, a refund request should be filled and submitted to the Portuguese Tax Authorities (PTA) within two years counted from the fulfillment of the said one year period. It should be provided evidence of the exemption requirements and we can help you in this regard. The PTA have until the end of the third month following the request to reimburse the taxpayer and if they fail to comply with this time limit due to a cause not attributable to the taxpayer, interest is due at the rate of, presently, 4% per year.

If the tax has been withheld because the shareholder did not prove the compliance with the legal requirements to benefit from the exemption, a refund request should be filled and submitted to the PTA within two years counted from the end of the year when the withholding occurred. It should be provided evidence of the exemption requirements and we can help you in this regard. The PTA have one year after the request to repay the tax to the taxpayer and if they fail to comply with this time limit due to a cause not attributable to the taxpayer, interest is due at the rate of, presently, 4% per year.

When the exemption regime is not applicable, dividend payments can also be subject to a **reduced withholding tax rate under a DTT**, provided that the beneficiary of the dividends presents evidence to the withholding entity of the compliance with the requirements to benefit from the applicable DTT until the date the withholding has to be delivered to the State. If evidence is not

shown in a timely manner, withholding at the standard domestic rate is due but the beneficiary may ask for a refund of the excess withholding tax. We can assist you with the refund that is to be submitted through the presentation, to the PTA, of the [22-RFI form](#) (for dividends from shares) and of the [23-RFI form](#) (for dividends of participations other than shares) submitted within two years counting from the end of the year in which the withholding has occurred, with the evidence of the accomplishment of all the legal requirements. The mentioned form might have to be accompanied by other elements and documents enabling the legitimacy of the reimbursement. The PTA have one year after the request to repay the tax to the taxpayer and if they fail to comply with this time limit due to a cause not attributable to the taxpayer, interest is due at the rate of, presently, 4% per year.

## **2. Interest and royalties payments**

Following to the implementation of the [Interest and Royalties Directive \(2003/49/EC\)](#) there is also an **exemption of withholding tax** in connection with the payment of interest and royalties payments to associated companies, provided that the following established requirements are met:

- i.* The beneficiary of the income is an EU resident, subject and not exempt of one of the taxes listed in the Directive and takes one of the legal forms listed therein;
- ii.* There is a minimum 25% direct participation by one of the companies in the capital of the other, or a third company directly holds at least 25% of the capital of both companies;
- iii.* Such shareholdings are held for at least a two-year period prior to the payment;
- iv.* The beneficiary of the income is the actual beneficial owner of such income.

The exemption shall not apply when the majority of the capital or of the voting rights of the beneficiary of the income is held by one or more residents of third countries, except if it is demonstrated that the chain of participations does not have as its main purpose or as one of its main purposes to benefit from the exemption, in what seems to us as an illegal inversion of the burden of proof. The exemption shall also not apply to the part of the income that is not in accordance with the arm's-length principle.

Despite the exemption, the entity paying the income will withhold the CIT when the two-year holding requirement is not yet met or when the companies do not prove by the right means the compliance with the legal requirements to benefit from the exemption.

When tax was withheld because the two-year holding requirement was not yet met when interest and royalties were paid, there may be a **refund** of the tax withheld until the date on which that two-year period of uninterrupted holding of the participation is completed. For this, it should be filled a [02-DJR form](#) certified by the beneficiary's residence State tax authorities and submitted to the PTA within two years from the date of verification of the holding requirement. Provided he documentation is in order, the PTA have one year after the request to reimburse the taxpayer and if they fail to comply with this time limit due to a cause not attributable to the taxpayer, interest is due at the rate of, presently, 4% per year.

When tax was withheld because the beneficiary did not prove to the paying entity the compliance with the requirements to benefit from the exemption before withholding was due to the State, the same [02-DJR form](#) certified by the beneficiary's residence State tax authorities should be filled and submitted to the PTA but in this case within two years from the end of the year in which the taxable event occurred, with the respective proof of the legal requirements. The mentioned form may have to be accompanied by other elements and documents enabling the legitimacy of the reimbursement. We have experience and we may help you in this matter. The PTA have one year after the request to repay the tax to the taxpayer and if they fail to comply with this time limit due to a cause not attributable to the taxpayer, interest is due at the rate of, presently, 4% per year.

In case the beneficiary of the interest and royalties could not benefit from the exemption but could have benefited from the reduced rates foreseen in the DTT except for the fact that it did not presented the required documentation before withholding was due, it can ask for a refund of the excess withholding tax. We can assist you with the refund that is to be submitted through the presentation to the PTA of the [23-RFI form](#) submitted within two years counting from the end of the year in which the withholding has occurred, with the evidence of the accomplishment of all the legal requirements. The mentioned form might have to be accompanied by other elements and documents enabling the legitimacy of the reimbursement. The PTA have one year after the request to repay the tax to the taxpayer and if they fail to comply with this time limit due to a cause not attributable to the taxpayer, interest is due at the rate of, presently, 4% per year.

The tax team