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Contributed by:
Bruno Santiago, António Lobo Xavier, António Pedro Braga and Francisco de Sousa da Câmara
Morais Leitão, Galvão Teles, Soares da Silva & Associados, SP, RL

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1. Types of Business Entities Commonly Used, Their Residence and Their Basic Tax Treatment

1.1 Corporate Structures and Tax Treatment

Businesses generally adopt a corporate form, with the most commonly used being joint stock companies (Sociedades Anónimas or S.A.) and limited liability companies (Sociedades por Quotas or Lda). Portuguese company law also establishes other forms, but these are used less commonly. In general, joint stock companies and limited liability companies are taxed according to similar rules, with both being treated for legal purposes (including tax) as separate entities, unless they are caught by the tax transparency regime.

Joint stock companies are subject to a minimum share capital of EUR50,000, represented by shares, and incorporation generally requires at least five shareholders. The capital is divided into shares and the shareholders' liability is limited to the value of the shares subscribed. The disposal of shares held in this type of company is generally not subject to restrictions. Unless otherwise established in the articles of incorporation, or approved by a majority corresponding to three quarters of the vote in a general assembly specifically convened for this effect, joint stock companies must distribute at least half of the annual profits, after having covered accumulated losses and complied with legal or contractual obligations imposing the composition or re-composition of mandatory reserves. Unless a larger amount is required under the articles of incorporation, a legal reserve equal to one fifth of the share capital must be created. To that extent, 5% of each fiscal year's profit cannot be distributed and must be used in the composition or re-composition of such legal reserve, until the aforementioned requirement is fully observed.

Limited liability companies are formed by at least two shareholders (although limited liability companies with a single shareholder are also admitted, as mentioned below). There is no minimum share capital required. Shareholders may be jointly responsible up to the amount of initial paid-in capital agreed in the articles of incorporation. The disposal of shares is generally subject to the company's authorisation, unless otherwise established in the articles of incorporation. The rules regarding distributable profits, legal and other mandatory reserves mentioned above for joint stock companies also apply to limited liability companies with minor specificities (eg, the legal reserve cannot be lower than EUR2,500). Limited liability companies may be held by a single shareholder (Sociedade Unipessoal por Quotas), either upon formation or upon the redemption of the interest held in the company by other shareholders. In general, the same rules apply as for limited liability companies, except for those that suppose the existence of more than one shareholder.

1.2 Transparent Entities

Partnerships – whether de facto or in the form of limited partnerships or limited liability partnerships – have not been recognised as such or established in either the company laws or the tax laws of Portugal. Accordingly, Portuguese tax law does not provide a comprehensive set of rules establishing how resident or non-resident partnerships/partners are taxed. Furthermore, no clear guidance is provided regarding how foreign partnerships should be respected as such or taxed as separate entities.

Notwithstanding, the Portuguese Corporate Income Tax Code ("CIT Code") establishes a transparency regime that applies inter alia to certain family-owned companies dedicated to asset management, to certain companies that fall into the definition of Professional Services Firms, and to certain joint venture entities such as complementary groups of companies (Agrupamento Complementar de Empresas) and European Economic Interest Groups (Agrupamento Europeu de Interesse Económico).

Complementary groups of companies can be formed by a group of corporate entities/individuals, generally to facilitate collaboration between members in a specific business venture. A complementary group of companies has separate legal personality from its members. These entities are not subject to minimum registration capital, and members are jointly liable for the entity's debts.

European Economic Interest Groups are meant to facilitate or develop the economic activities of their members via a pooling of resources, activities or skills, and can be formed by legal entities governed by public or private law which have been formed in accordance with the laws of an EU country and have their registered office in the EU, as well as by individuals developing an industrial, commercial, craft or agricultural activity or providing professional or other services in the EU. They must have at least two members from different EU countries. Each member of a European Economic Interest Group has unlimited joint and several liability for the entity's debts.

In addition, Portuguese Collective Investment Vehicles, including venture capital funds, apply taxation schemes that privilege investor-level income taxation to fund-level income taxation (see **2.3 Other Special Incentives**).

1.3 Determining Residence

Portuguese tax residency of corporate entities is determined based on the location of the head office or place of effective management.

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1.4 Tax Rates

The general CIT rate applicable on the Portuguese mainland and in the Madeira Archipelago is 20%, while the general rate applicable in the Azores Archipelago is 16.8%.

Entities qualifying as small and medium enterprises (SMEs) are subject to a 17% rate, which applies to the first EUR15,000 of taxable profits. The remaining profits are subject to the applicable general rates.

A state surtax applies to taxable profits in excess of EUR1.5 million, as follows:

- from EUR1.5 million up to EUR7.5 million: 3%;
- from EUR7.5 million up to EUR35 million: 5%;
- profits in excess of EUR35 million: 9%.

Local surtax up to 1.5% of taxable profits is levied by municipalities.

Certain expenditures incurred by entities subject to CIT are separately subject to Autonomous Taxation ("Tributação Autónoma"). The following expenditure items may be subject to autonomous taxation at variable rates:

- undocumented expenses;
- certain expenses incurred with private or commercial vehicles as well as motorcycles;
- entertainment expenses;
- certain allowances granted for costs incurred by employees, including, in certain conditions, for the usage of the employee's own vehicle; and
- certain expenses with bonuses and severance payments paid to board members and other managerial personnel.

Generally, taxable income derived from businesses operated directly by individuals is subject to personal income tax (PIT) and taxed as business income (Schedule B income). As such, a progressive rate structure applies:

- general rates range from 14.5% to 48%; and
- a solidarity surcharge, also levied at progressive rates (2.5% to 5%), applies to taxpayers with taxable income over EUR80,000. Further detail on this regime may be found under **3.2 Individual Rates and Corporate Rates**.

2. Key General Features of the Tax Regime Applicable to Incorporated Businesses

2.1 Calculation for Taxable Profits

Taxable profits are defined in the CIT Code as the sum of profits and losses ("p&l") as well as the net variation in equity not reflected in p&l, as accrued and determined for accounting purposes, subject to the adjustments set forth in the CIT Code. These adjustments include:

- cancellation of the equity and the proportional consolidation methods;
- correction of fair value accruals/deductions;
- correction of amounts deducted as provisions and impairments in excess of deductible amounts as determined in the CIT code;
- correction of amounts deducted with CIT, autonomous taxation and other taxes levied on profits paid by the taxpayer, penalties, fines, late payment and other compensatory interests paid and taxes levied on third parties which the taxpayer is not legally authorised to bear;
- deferred taxes;
- undocumented expenses;
- amounts paid or owed to entities subject to a privileged tax regime as defined in Portuguese tax laws;
- excessive depreciation and amortisation;
- bad debt deductions above the limits established in the CIT code;
- unrealised capital gains and losses, as well as adjustments in connection with the capital gains' roll-over relief mechanism;
- gains or losses registered for accounting purposes with respect to derivative instruments;
- transfer pricing adjustments;
- interest deductibility limitations and excessive deduction carry forwards;
- excessive deductions taken with respect to gifts and donations;
- tax regimes based on territoriality, including the deductions for dividends received and capital gains realised from the sale of certain securities as well as the application of the exemption method to foreign permanent establishments; and
- patent box regime and tax depreciation for certain assets, including intangibles.

2.2 Special Incentives for Technology Investments

Patent Box

The Portuguese patent box grants a deduction corresponding to 50% of the income derived as consideration from the disposal or temporary use of certain industrial property rights (patents and industrial models), including income from the violation of such rights ("qualifying income"). Qualifying income is defined as the net positive balance between the revenues and gains derived in a given taxable year as consideration from the disposal or use of qualifying industrial property rights and the research and development (R&D) expenses or losses incurred or borne in the same period by the taxpayer in connection with the industrial property right from which the gain is obtained. This regime does not apply to any services supplied which are ancillary to a qualifying disposal or temporary use of industrial property. As such, consideration for this type of service must be segregated and cannot be embedded in the consideration established for the disposal or temporary use of industrial property.

This regime is subject to the verification of certain conditions:

- the transferee must use the industrial property in a business activity qualifying as an "agricultural, industrial or commercial activity";
- the product of the use of the industrial property must not consist in a supply of goods or services that generate tax-deductible expenses to the transferor or to any company pertaining to the same group of companies to which the Special Taxation Regime for Groups of Companies (Regime Especial de Tributação de Grupos de Sociedades, or RETGS) applies, whenever the transferor and the transferee are considered to be closely related entities for transfer pricing purposes;
- the transferee cannot be a resident of a blacklisted country, territory or region; and
- the transferor must keep accounting records that identify the R&D expenses corresponding to the industrial property right disposed of or temporarily utilised and are organised in order to distinguish the qualifying gains from any other gains obtained.

The amount of qualifying income to which the 50% deduction applies is reduced by the accumulated negative balance of the revenues and gains related to each of the industrial property rights and the corresponding R&D expenses and losses incurred, both registered in previous taxable years. The amount deductible is further limited to the fraction of qualifying income corresponding to the weight of "eligible R&D expenses" (ie, R&D expenses, as defined in the Investment Tax Code, related to the industrial property item incurred by the taxpayer or supplied by unrelated parties) over "total R&D expenses incurred" (ie, all the R&D expenses incurred or borne by the taxpayer with industrial property rights, including, where applicable, the purchase of such property). The amount of eligible expenses is marked up by 30%, capped at the amount of the total expenses incurred.

2.3 Other Special Incentives

Portuguese tax law establishes several tax incentives aimed at promoting certain behaviour (eg, savings) or stimulating certain activities, industries and sectors. Notable sector-specific incentives include those granted to capital markets and to the financial sector in general, to real estate development and rehabilitation, to the shipping industry, wine production, sports and cultural activities, cinema, forestry management, patronage, philanthropic activities and the co-operative sector.

Pension Funds

Generally, pension funds established according to Portuguese law are exempt from Portuguese CIT and the municipal transfer tax applicable to the sale of real estate. This tax treatment may be extended to pension funds established under the law of another EU or EEA Member State, provided the latter is bound by administrative co-operation or mutual assistance in taxation matters, when the following requirements are met:

- the pension fund should provide exclusively for retirement benefits in relation to aging, incapacity, survival, pre-retirement or anticipated retirement, health benefits post-employment, and, when accessory to the referred benefits, death grants;
- the pension fund should be managed and supervised by an entity to which Directive 2003/41/EC of the European Parliament and of the Council applies;
- the pension fund should be the beneficial owner of the income; and
- if the income to be received by the pension fund is a profit distribution, the corresponding shareholdings must be held, uninterrupted, for at least one year.

Collective Investment Vehicles (CIVs)

Investment funds in securities, real estate investment funds, investment companies in securities and real estate investment companies established according to Portuguese law are technically subject to tax at the general CIT rate imposed on their taxable income, determined according to the accounting standards applicable to CIVs and modified by the CIT code.

However, income typically derived by CIVs, including interest, dividends, capital gains and rents as well as certain fees and commissions, is generally excluded from CIT. This exemption does not apply when the income is paid by an entity resident in a blacklisted country, territory or region. CIVs are exempt from municipal and state surcharges.

In addition, stamp duty applies on the net asset value of these funds (0.0025% or 0.0125%, depending on the investment policy pursued).

Investors resident in Portugal, whether individuals or entities, are subject to tax on distributions, redemptions and the disposal of units or shares issued by CIVs (different rates apply). Non-resident investors are exempt, except with respect to investments in real estate investment funds and companies, in which case a 10% rate applies.

REITs were introduced in Portugal at the beginning of 2019. REITs and their shareholders have an income tax regime similar to the real estate investment funds and real estate investment companies, with the particularity that income from the sale of real estate by the REIT is only excluded from tax when the immovable property has been held for renting purposes for at least three years.

Exemptions Applicable to Foreign Financial Entities

Interest payments agreed upon in relation to loans granted by non-resident financial institutions without a permanent establishment in Portugal to resident financial institutions are generally exempt from CIT (blacklisted entities as well as non-resident financial institutions substantially held by resident entities are excluded). Furthermore, gains realised by non-resident financial institutions, in the context of swap transactions entered into with a resident financial entity, are also generally exempt from CIT (similar exclusions apply).

Exemption Applicable to Debt Instruments

Non-resident entities and individuals (except those that are resident in blacklisted jurisdictions) are exempt from CIT and PIT otherwise imposed on interest and capital gains derived in connection with qualifying debt instruments that benefit from the regime set forth in Decree Law 193/2005.

Debt instruments qualifying for this regime include bonds issued by public and private sector entities, money market instruments, namely treasury bills and commercial paper, perpetual bonds, convertible bonds, other convertible securities and tier 1 and tier 2 capital instruments, regardless of the currency of issue. Qualifying instruments must be integrated in a centralised system managed by a Portuguese resident entity or by an entity established in the EU/EEA that manages an international clearing system (in the latter case, provided that the state of establishment is bound to administrative co-operation for tax purposes equivalent to the rules in force in the EU).

The beneficiaries of this exemption include central banks and government agencies, international organisations recognised by Portugal, and entities resident in a country or jurisdiction that has entered into a double tax treaty or an Exchange of Information Agreement with other entities that are not resident in a blacklisted country, territory or region.

Tonnage Tax and Seafarer Schemes

Following approval by the European Commission, two new schemes have been implemented:

- a special tax regime based on the amount of tonnage operated by ship owners, applicable to eligible maritime transport activities, exempting the companies concerned from the general obligation to pay corporate income tax irrespective of the companies' actual profits or loss ("Tonnage Tax Scheme"); and
- a special tax and social contributions regime applicable to seafarers involved in eligible maritime transport activities, partially exempting them and their employers from the general obligation to pay income tax and social contributions ("Seafarer Scheme").

2.4 Basic Rules on Loss Relief

For resident entities, there is no distinction between ordinary income/capital gains and ordinary losses/capital losses. The carry-forward of losses is available for five years, unless the entity is a certified SME, in which case the carry-forward of losses is available for 12 years. For each year, the deduction of tax losses is limited to 70% of the taxable profit. Carry-back is not allowed.

Portuguese law establishes a general anti-loss trafficking rule, under which loss carry-forwards are lost if more than 50% of the entity's ownership (share capital or voting rights) has changed between the taxable year in which such losses were generated and the end of the taxable year in which a deduction is claimed. However, several exceptions apply to the general rule (eg, when the ownership is converted from direct into indirect or from indirect into direct, and when an interest is exchanged between entities whose share capital or voting rights are held directly or indirectly by a common entity).

When no exception applies, the Minister of Finance may approve the transfer of losses to the extent that a motion is filed with the tax authorities and it is considered that there is a recognised economic interest in authorising such transfer.

In the case of non-resident entities, no carry-forward of losses is available for business income unless such entities have a permanent establishment in Portugal. Non-residents that derive Portuguese-source capital gains and do not have a permanent establishment in Portuguese territory to which such gains are attributable are subject to tax on the balance of Portuguese-source capital gains and losses. In the case of securities, exemptions may apply (see **7. Anti-avoidance** for more details).

2.5 Imposed Limits on Deduction of Interest

In general, business expenses, including interest, are deductible for tax purposes to the extent they are necessary to obtain or guarantee income subject to corporate income tax. There are, however, certain limitations that are applicable to interest expenses deductibility.

Interest-barrier Rule
Net interest expenses may be deducted up to the greater of the following limits:

- EUR1 million; or
- 30% of EBITDA as determined by accounting rules and corrected for tax purposes.

It is possible to carry forward excess interest deductions and unutilised limits for five taxable years. Excess interest deductions and unutilised carry-forwards are applied on a first-in, first-out basis, after the current year's interest is deducted. Rules similar to the anti-loss trafficking rules detailed above also apply to excess interest deductions and unutilised limits.

Companies taxable under the RETGS may elect to apply these rules on a group basis. Likewise, certain rules limit the deductibility of interest as well as the application of excess limits pertaining to pre-grouping or post-grouping taxable years of specific entities.

This interest limitation rule does not apply to entities that are subject to the supervision of the Bank of Portugal or the Portuguese Insurance Authority, nor to the Portuguese branches of credit institutions and other financial institutions or insurance companies, or securitisation companies formed under Decree-law 453/99, of 5th November.

Transfer Pricing and Shareholder Loans
In addition to the above, transfer pricing rules may limit the deductibility of interest in the case of debt arrangements entered into between related parties, as defined for tax purposes, to the extent such interest is not established according to the arm's length principle.

Unless transfer pricing rules apply, interest and other forms of compensation agreed under financial arrangements, qualified as shareholder loans (suprimentos), cannot be deducted in excess of the rate established in a ministerial decree issued by the Minister of Finance.

2.6 Basic Rules on Consolidated Tax Grouping
The RETGS is not a consolidation regime, but rather an optional tax regime under which the "Dominant Company" of a "Group of Companies" may elect to aggregate the taxable profits and losses of any other company pertaining to the same group of companies ("Member Companies").

Under the RETGS, a Group of Companies exists when a company (the Dominant Company) directly or indirectly holds 75% of the share capital of another company or companies (the Member Companies), as long as such interest provides the Dominant Company with the majority of the voting rights in each of the Member Companies.

An election to apply the RETGS can only be filed when certain conditions applicable to the Dominant Company and to the Member Companies are cumulatively fulfilled. Such requirements include, inter alia:

- that all the entities forming the Group of Companies have their headquarters or place of effective management in Portugal (under certain circumstances it is possible for the Dominant Company to be a resident of an EU or EEA country or a Portuguese-situs permanent establishment of a EU/EEA resident company);
- that all the entities forming the Group of Companies (including the Dominant Company) are subject to the general CIT regime, with all income being taxed at the highest general CIT rate applicable;
- the Dominant Company must hold a qualifying interest in a (the) Member Company(ies) for more than one year, on the date it intends to start applying the regime. The RETGS can apply with respect to newly incorporated Member Companies immediately, provided that the ownership/vote requirements are fulfilled as of the date of incorporation of such Member Company;
- the Dominant Company should not be controlled by another Portuguese company that fulfils the requirements to be the Dominant Company of a RETGS group;
- the Dominant Company should not have opted out of the RETGS in the three years preceding the date on which it intends to start applying the regime; and
- the Member Companies cannot adopt a different tax period from the Dominant Company.

The RETGS ceases to apply when any of the mandatory requirements concerning the Dominant Company are no longer fulfilled, or when the taxable profits of any of the entities forming the Group of Companies (including the Dominant Company) are determined according to an indirect assessment. When a Dominant Company becomes controlled by another Portuguese company that fulfils the requirement to be considered a Dominant Company (other than the requirement with respect to losses during the three previous tax periods) during the application of the RETGS, the latter may elect to continue to apply the RETGS.

Specific and strict rules apply to the carry-forward of losses during the application of the RETGS, including in cases where a non-recognition transaction occurred. Also, pre- and post-RETGS loss carry-forward is limited.

2.7 Capital Gains Taxation

In general, capital gains are considered taxable profits and are taxed at the general CIT rate. Capital losses may be deducted if the general deductibility rules are fulfilled, but not to the extent of profits or reserves distributed in previous years or capital gains realised from the disposal of shares that benefited from the participation exemption or from the foreign (indirect) tax credit.

Under the participation exemption regime, capital gains and losses realised by Portuguese-resident companies from the disposal of shares are exempt, provided that the following requirements are met:

- the company disposing of the interest must hold – directly and/or indirectly – at least 10% of the share capital or voting rights of an entity;
- such interest must be held for a minimum period of one year;
- the entity disposing of the interest must not be taxed under the tax transparency rules;
- the company whose shares are disposed of must either:
  - (a) be liable to CIT in Portugal without benefitting from an exemption;
  - (b) if resident in the EU, be liable to a tax mentioned in article 2 of Directive 2011/96/UE without benefiting from an exemption; or
  - (c) if resident outside the EU, be liable to a tax which is similar to the CIT, where the applicable rate is not below 60% of the Portuguese CIT rate (this condition may be waived under certain circumstances, which depend on the type of business of the subsidiary);
- the entity whose shares are being disposed of should not be a resident of a country, territory or region included in the Portuguese Blacklist; and
- no more than 50% of the value of the subsidiary's total assets should not comprise real estate located in Portugal, unless such properties are used in connection with an agricultural, industrial or commercial activity (other than a real estate buy and sell activity).

Additionally, a roll-over relief mechanism may be used to exclude 50% of the positive balance of capital gains and losses realised on the sale of tangible fixed assets, intangible assets and non-consumable biological assets, held for at least one year, from taxable income, to the extent the realisation value of such assets is wholly or partially reinvested in the acquisition, production or construction of similar assets during a four-year reinvestment period that corresponds to the two years before and the two years after the taxable period in which the realisation occurs. The law establishes specific rules to be observed, including regarding the type of assets qualifying for this regime.

When the reinvestment is not wholly or fully made until the end of the reinvestment period, the income that was not previously recognised for tax purposes must be subject to taxation in that period, increased by 15%.

Non-resident taxpayers who do not have a Portuguese-situs permanent establishment may be subject to Portuguese-source capital gain taxation on the disposal of the following assets:

- Portuguese-situs real estate;
- the disposal of shares in real estate-rich companies (whether or not such companies are resident for tax purposes in Portugal); or
- the disposal of shares in Portuguese companies.

There is an exemption that applies to non-resident entities or individuals deriving Portuguese-source capital gains from the disposal of shares and other securities issued by Portuguese entities, but this exemption does not apply in the following cases:

- to non-resident entities domiciled in a blacklisted country, region or territory;
- to non-resident entities that are directly or indirectly held, by more than 25%, by resident entities, except when:
  - (a) the non-resident entity is liable to a tax mentioned in article 2 of Directive 2011/96/UE without benefiting from an exemption, or, if resident outside the EU, to a tax which is similar to the CIT, where the applicable rate is not below 60% of the Portuguese CIT rate;
  - (b) the non-resident disposing of the interest has held directly and/or indirectly at least 10% of the share capital or voting rights of the Portuguese issuer for a minimum period of one year prior to the disposal; and
  - (c) the non-resident entity is not part of an artificial arrangement, or a series of artificial arrangements, put in place with the main purpose of obtaining a tax advantage;
- when more than 50% of the total assets of the Portuguese entity whose shares are being disposed of consists of immovable property located in Portugal; and
- when the entity whose shares are disposed of actively manages or passively holds control in other Portuguese resident companies, whose assets, in turn, are made up by more than 50% of immovable property located in Portugal.

2.8 Other Taxes Payable by an Incorporated Business

Other taxes may apply to specific transactions, such as:

- Value Added Tax (VAT), which is generally levied on the supply of goods and services;
- stamp duty, which may apply to contracts, acts, papers, documents, titles, books, and other items occurring or deemed to be occurring within Portuguese territory listed in the General Table which are not subject or exempt from VAT. In this regard, it is worth noting that stamp duty applies, inter alia, to the following transactions:
  - (a) the acquisition of immovable property (including by virtue of donation);
  - (b) gifts and other gratuitous transfers to individuals;
  - (c) guarantees, including fees charged thereto;
  - (d) the use of credit (including capital and interest);
  - (e) sales as a going concern;
  - (f) repos; and
  - (g) the net asset value of CIVs; and
- property transfer tax (IMT), which may be levied on the transfer of real estate located in Portugal.

2.9 Incorporated Businesses and Notable Taxes

Other than the taxes mentioned in **2.8 Other Taxes Payable by an Incorporated Business**, it is noteworthy that a company owning real estate in Portugal is generally subject to property tax (IMI), which is levied at a rate ranging from 0.3% to 0.45% (urban properties) of the tax registration value. There is also an addition to the property tax, called AIMI, that applies in certain circumstances.

Special levies may also apply to companies operating in specific industries, such as the energy and banking sectors, amongst others.

3. Division of Tax Base Between Corporations and Non-corporate Businesses

3.1 Closely Held Local Businesses

Generally, most closely held local businesses operate in corporate form.

3.2 Individual Rates and Corporate Rates

The CIT Code comprises a tax transparency regime that applies to the following entities in specific situations:

- companies incorporated under the form of civil companies with commercial capacity;
- "professional services firms" ("Sociedade de Profissionais"); and
- companies established for the passive administration of certain assets, values or goods held for the fruition of their shareholders.

A "professional services firm" is defined as a company where all the shareholders undertake the same type of professional activities listed in a ministerial order – examples include doctors, dentists, lawyers, architects, biologists, artists, etc – and more than 75% of the income is derived from at least one qualifying professional activity, as long as its shares are held by not more than five shareholders for more than 183 days per tax year, with none of them being a public company, and at least 75% of the share capital is held by professionals who carry out such activities, totally or partially through the company.

Accordingly, the taxable profits are computed at a corporate level but are attributable to the shareholders and taxed as business (Schedule 'B') income. If the shareholder receives payments on account of future dividends during a given tax period, and such payments are in excess of the income attributed via the tax transparency regime, then the total amount of such payments should be taxed as self-employment/business income ("Categoria B") for PIT purposes.

3.3 Accumulating Earnings for Investment Purposes

As mentioned above, the tax transparency regime applies to the income generated through companies established for the passive administration of certain assets, values or goods held for the fruition of shareholders, including real property used as the shareholder's place of abode; it also applies to companies established for other purposes but whose average income in the previous three years related to the aforementioned goods, values or real estate exceeds 50% of the average income in the same period, considering all the income derived by such company.

The regime applies to such companies where more than 50% of the share capital is held, directly or indirectly, for more than 183 days by a family group or by five or fewer shareholders, none of whom is a public sector company. Accordingly, the taxable profits are computed at a corporate level but are attributable to shareholders and are taxed as business (Schedule 'B') income. If the shareholder receives payments on account of future dividends during a given tax period, and such payments are in excess of the income attributed via the tax transparency regime, then the total amount of such payments should be taxed as self-employment/business income ("Categoria B") for PIT purposes.

Furthermore, if a closely held corporation is domiciled in a blacklisted jurisdiction, it may be considered a controlled foreign company (CFC), in which case anti-deferral rules could apply. In this case, the CFC profits or income may be attributable to the individuals holding an interest in the CFC, in the proportion of such interest. Income so attributed is characterised as business (Schedule 'B') income if the interest is used in a business activity, or as investment (Schedule 'E') income in all other cases.

Assuming that the tax transparency regime applies, the taxable profits of the tax transparent entity are directly attributable to the shareholder, and are taxed as business income for PIT purposes. If the shareholder receives payments on account of future dividends during a given tax period, and such payments are in excess of the income attributed via the tax transparency regime, then the total amount of such payments should be taxed as self-employment/business income ("Categoria B") for PIT purposes.

3.4 Sales of Shares by Individuals in Closely Held Corporations

Capital gains realised on the sale of shares by resident individuals are generally taxed at a special 28% tax rate (Schedule 'G' income), unless the taxpayer chooses to include this income and submit it to the progressive rate structure and the solidarity surcharge, or unless it is shares from a non-listed micro or small sized company that are taxed at the effective rate of 14%.

3.5 Sales of Shares by Individuals in Publicly Traded Corporations

The rules that apply to the taxation of dividends and capital gains derived by individuals from publicly traded corporations do not differ from those applicable to income derived from privately traded corporations.

Dividends received by resident individuals are taxed at a 28% flat tax rate, unless the taxpayer elects to include this income and apply the general progressive rate structure. In this case, when dividends are distributed by Portuguese-resident companies or EU/EEA companies (in the latter case, provided that the state of establishment of the distributing company is bound to administrative co-operation for tax purposes equivalent to the rules in force in the EU) and the same requirements established in the Parent-Subsidiary Directive are fulfilled, the taxpayer will be able to include an amount corresponding to 50% of such dividend.

Capital gains realised on the sale of shares by resident individuals are generally taxed at a special 28% tax rate (Schedule 'G' income), unless the taxpayer chooses to include this income and submit it to the progressive rate structure and the solidarity surcharge.

4. Key Features of Taxation of Inbound Investments

4.1 Withholding Taxes

As a general rule, interest, dividends and royalties paid by Portuguese-resident companies to non-resident companies are subject to withholding tax at the rate of 25%, which shall take place when the dividends are paid/made available to the shareholders, when the interest reaches its maturity, or when the royalties are assessed.

Furthermore, dividends, interest and royalties, among other forms of capital income, paid or made available to accounts held by one or more holders on behalf of unidentified third parties, or to entities deemed to be tax resident in blacklisted jurisdictions, should be subject to withholding tax at the rate of 35%.

Nonetheless, the withholding tax on distributions of dividends may not take place if the Portuguese participation exemption regime is applied.

According to the Portuguese law, the dividends distributed by resident entities to non-resident entities should be exempt from CIT if the following requirements are met:

- the beneficiary of the income is resident in another EU country, an EEA country that submits to administrative co-operation in a similar manner as between EU countries, or a country with which Portugal has executed a double taxation treaty (DTT) that is in force and provides for the possibility of the exchange of information;
- the beneficiary of the income holds, directly and/or indirectly, at least 10% of the share capital or voting rights of the distributing company;
- such participation has been held uninterrupted during the 12 months prior to the distribution of the dividends; and
- the beneficiary of the income is subject to and not exempt from any of the income taxes referred to in the EU Parent Subsidiary Directive, or is subject to and not exempt from a tax of a similar nature with a rate that cannot be lower than 60% of the Portuguese CIT rate (ie, currently such tax rate cannot be lower than 12.6%).

In order to benefit from this tax exemption, the beneficiary of the income shall provide (prior to the payment of the dividends) a statement to the distributing company evidencing its tax residence status and the applicable CIT regime, duly signed and certified by the tax authorities of the country of residence of the beneficiary.

The above-described exemption regime also applies to dividends distributed by a resident company to permanent establishments located in other EU or EEA countries of an entity that meets the above-mentioned requirements.

On the other hand, it is worth mentioning that these tax exemptions are not applicable if there is an arrangement – or several arrangements that are not genuine – whose primary purpose, or one of its primary purposes, is to obtain a tax advantage that defeats the object and purpose of eliminating the double taxation of dividends, taking all the relevant facts and circumstances into consideration. This regime should also not apply if the Portuguese distributing company has not complied with the declarative obligations imposed by the Portuguese legal regime of the central registry and its effective beneficiary.

Regarding interest and royalties income, the withholding tax may be eliminated by the tax framework set forth by the EU Interest and Royalties Directive (I&RD), pursuant to which no withholding tax should be due on payments of interest and royalties made by Portuguese companies, provided that the following requirements are met:

- the entity that pays and the entity that benefits from the relevant income should be subject to and not exempt from corporate tax, and is incorporated under one of the legal forms listed in the annex of I&RD;
- both entities should be deemed to be EU residents for DTT purposes;
- a direct 25% shareholding should be held by one of the companies in the share capital of the other, or a third company should directly hold at least 25% of the capital of both companies, and in any scenario the shareholding must be held for at least a two-year period; and
- the entity that receives the interest payment should be its effective beneficiary.

The payment of interest and royalties to a company or a permanent establishment resident in Switzerland may also benefit from the exemption established by this regime, provided that the aforementioned requirements are duly fulfilled.

In order to benefit from this tax exemption regime, some formal requirements should be met before the tax becomes due. Such formal requirements should involve the lodging of tax forms (Model 01-DJR) duly certified by the tax authorities of the country in which the beneficiary is tax resident and a certificate of residence issued by such tax authorities, to confirm that the requirements to apply such regime are fulfilled.

The beneficiary may also apply for the later reimbursement of the withheld tax by lodging a Model 02 – DJR. This reimbursement request should be made within two years of the respective payment.

Finally, this tax exemption regime on interest and royalties payments should not be applicable to the part of the income that is not in accordance with the arm's-length principle.

Provided that the requirements set forth by Decree-Law no. 193/2005 of 7th November are met, interest from debt securities issued by Portuguese companies and made available to non-resident companies and/or individuals may also be exempt from tax withholding.

4.2 Primary Tax Treaty Countries

Portugal has so far executed 80 double tax treaties, 78 of which are in force. The last DTT to enter into force was with Angola, and has been applicable since 22 September 2019. Finland has denounced its DTT with Portugal, so that DTT has not been available since 1 January 2019. The primary tax treaty countries that are usually employed by foreign investors to pursue direct investments in local corporate stock or debt are Brazil, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Spain, Switzerland, the United Kingdom and the United States of America.

4.3 Use of Treaty Country Entities by Non-treaty Country Residents

Over the last few years, the Portuguese tax authorities have increased their focus on cross-border tax matters in order to tackle treaty shopping practices, following the best international practices on the matter.

However, there are no particular updates to highlight regarding the capacity of the Portuguese tax authorities to co-operate with other tax administrations in order to address these types of challenges.

Additionally, in the last reports on activities developed for the combat of fraud and tax evasion that were released by the Portuguese tax authorities to tackle cross-border abusive practices, an increase in the use of the international mechanisms available for the exchange of tax information has been highlighted as a point on which tax inspectors should concentrate their efforts.

In accordance with the above-mentioned reports, the Portuguese tax authorities also intend to increase their control over cross-border transactions made between related parties belonging to the same corporate groups. When this concerns international corporate groups, and provided that the respective requirements are met, this control is usually enacted by the Large Taxpayers Unit. A way to mitigate any risk arising from a related party's transactions may be to execute an Advanced Pricing Agreement (APA), which may have a unilateral nature (executed only with the Portuguese tax authorities) or a bilateral/multilateral nature (executed not only with the Portuguese tax authorities but also with other foreign tax authorities).

4.4 Transfer Pricing Issues

The biggest and most common transfer pricing issues that foreign investors usually have to deal with regarding local corporations are related to the terms and conditions set forth between the related parties regarding interest on financing, as well as on the amount of management fees and royalties.

As mentioned above, a way to mitigate the tax risks arising from a related party's transactions could be the execution of an APA.

It should be noted that the Portuguese transfer pricing regime has been amended in 2019, with amendments including a legal provision expressly stating that the transfer pricing rules are applicable to corporate restructuring transactions whenever they include the transfer of tangible or intangible assets, rights on intangible assets or compensation payments for losses.

4.5 Related-Party Limited Risk Distribution Arrangements

As a general rule, Portugal follows the OECD standards on transfer pricing issues; therefore, the Portuguese tax authorities are legally entitled to challenge the agreements established by related parties with reference to limited risk distribution for the sale of goods or the rendering of services. The control of such arrangements is common for international corporate groups. These arrangements may also be included within the scope of an APA.

4.6 Comparing Local Transfer Pricing Rules and/or Enforcement and OECD Standards

Considering that Portugal tends to follow the OECD standards on transfer pricing matters, there are no particular differences to emphasise.

5. Key Features of Taxation of Non-local Corporations

5.1 Compensating Adjustments When Transfer Pricing Claims are Settled

According to the Portuguese transfer pricing regime, when the Portuguese tax authorities execute a transfer pricing adjustment for one related party in the relevant transaction, a correlative adjustment may be made by the other related party involved in such transaction.

Additionally, at an international level, several DTTs entered into by Portugal provide a mechanism under which transfer pricing adjustments made by the tax authorities in one state may lead to a correlative adjustment in the other party's state of residence for the avoidance of potential double taxation. In potential situations of double taxation arising from adjustments, the MAP should be applicable.

Finally, where a transfer pricing adjustment leads to additional tax liability towards the Portuguese tax authorities, the relevant company should be bound to pay compensatory interest to said authorities at a rate of 4% per year. Specific penalties may also be applicable.

It should be noted that, in the execution of an APA with the Portuguese tax authorities, the parties may have to renounce the possibility of executing correlative adjustments with reference to the transactions covered by the APA.

5.2 Taxing Differences

As a general rule, local branches and local subsidiaries of non-local corporations are taxed on the same basis. However, the following aspects in the tax regime applicable to a local branch of a foreign corporation should be taken into account:

- general administrative and management expenditures made by the head office of the non-local corporation for its local branch may be allocated to the latter;
- income paid by the local branch to its head office should be exempt from withholding tax; and
- some limits on the deductibility of some expenditures charged by the head office to the local branch may apply, namely regarding royalties and interest.

5.3 Capital Gains of Non-residents

As a general rule, capital gains made by non-resident entities from the transfer of stock in local corporations are subject to CIT withholding tax at the rate of 25%, but may be exempt from taxation in Portugal if:

- more than 25% of the non-resident company is not held – directly or indirectly – by Portuguese tax residents, unless the following requirements are cumulatively met:
  - (a) the non-resident company is resident in an EU country, in an EEA country that submits to administrative co-operation on tax matters with Portugal in a similar manner as between between EU countries, or in a country with which Portugal has executed a DTT that is in force and provides for the exchange of information on tax matters;
  - (b) the beneficial owner is subject to and not exempt from a tax identified in article 2 of Directive 2011/96/UE of 30 November 2011, or subject to and not exempt from a tax of a similar nature with a rate not lower than 60% of the Portuguese CIT rate (ie, 12.6%);

(c) the beneficial owner uninterruptedly holds, directly or indirectly, at least 10% of the share capital or voting rights of the transferred entity for at least one year; and
(d) the beneficial owner is not part of an arrangement or several arrangements with an artificial nature, that have been put in place with the main purpose of gaining a tax advantage;

- the non-resident entity is not domiciled in a blacklisted jurisdiction listed in the ministerial order 150/2004, of February 13, as amended; or
- the capital gains obtained by the non-resident are not reported to the direct or indirect transfer of shares of a resident company whose assets are composed more than 50% of real estate property located in Portugal.

Some DTTs entered into by Portugal also establish a waiver of taxation regarding capital gains obtained from the sale of a local company, provided that such capital gains are not allocated to a permanent establishment located in the Portuguese territory.

Additionally, assuming that the beneficiary of the income is not deemed a Portuguese tax resident, no taxation should be triggered in Portugal on capital gains arising from the transfer of non-local holding companies unless the assets of such non-local holding companies are essentially constituted by rights over real estate properties located in Portugal.

5.4 Change of Control Provisions

The following tax issues potentially triggered by a change of control are the most relevant:

- the tax losses registered by the local company may be lost in the event of a change of ownership of 50% of its share capital or the majority of its voting rights;
- if the local company is included in the tax perimeter of a corporate tax group, such group may register changes in its perimeter and, in a worst-case scenario, may cease to exist;
- the possibility of deducting interest that was not deducted in previous financial years as a result of the application of the limits established by the interest barrier rules may also be lost in the event of a change of ownership of 50% of its share capital or the majority of its voting rights; and
- some tax benefits, particularly tax benefits of a contractual nature, may be lost as result of the change of ownership.

5.5 Formulas Used to Determine Income of Foreign-owned Local Affiliates

The rules that apply to the determination and assessment of the respective taxable income are the same for local-owned and foreign-owned affiliates, including the transfer pricing rules that apply to transactions made between related parties.

5.6 Deductions for Payments by Local Affiliates

As a rule, and assuming that they are deemed necessary for the business of the local affiliate, payments regarding management and administrative expenditures made to non-local affiliates are deductible for tax purposes. Formal requirements regarding the documentary support of such expenses should be observed.

Finally, the terms and conditions related to the rendering of said services and the payment of the relevant fees are subject to the Portuguese transfer pricing rules and therefore should be made according to the arm's length principles. Otherwise, the Portuguese Tax Authorities may totally or partially deny the deductibility of such expenses for tax purposes.

5.7 Constraints on Related-Party Borrowing

As a general rule, there are no specific constraints. However, as mentioned above, such transactions should be made in accordance with the transfer pricing rules and the arm's length principle, or they risk being challenged by the Portuguese Tax Authorities.

6. Key Features of Taxation of Foreign Income of Local Corporations

6.1 Foreign Income of Local Corporations

The Portuguese CIT Code subjects its resident companies to the worldwide income principle, pursuant to which they should be subject to tax for all their income, regardless of the country of source. On the other hand, all deductible expenses are also taken into account in order to determine the taxable income of the local company, independently from the location where such expense is incurred.

Furthermore, the Portuguese CIT Code expressly provides different methods to eliminate double taxation, namely tax credit and tax exemption methods.

Regarding tax credit methods, a credit deduction for international double taxation is available for situations in which income generated abroad is included in the taxable income.

The tax credit should correspond to the income tax paid in the foreign country, or to the amount of CIT assessed before the deduction, corresponding to the net income that may be taxed in the foreign country, whichever is lower.

Additionally, if a DTT applies, the tax credit should not exceed the tax that should have been borne abroad pursuant to the terms established by the DTT.

For the exemption method, the participation exemption regime should be highlighted, as well as a special regime applicable to foreign permanent establishments that allows the tax exemption of the income generated by such permanent establishment in order to mitigate distinctions in the tax treatment provided to foreign subsidiaries and foreign permanent establishments.

It should be noted that this regime is optional and, if exercised, has to include all the permanent establishments located in the same territory, and should remain in force for a period of at least three years. Additionally, the following requirements should be met:

- the permanent establishment should be subject to and not exempt from any of the income taxes identified in the Parent Subsidiary Directive, or subject to and not exempt from a tax of a similar nature with a rate not lower than 60% of the Portuguese CIT (ie, 12.6%);
- the permanent establishment should not be considered resident in a blacklisted jurisdiction; and
- the amount of tax effectively paid should not be less than 50% of the amount of tax that would be due under the terms of the CIT Code.

This last requirement may not apply if the following types of income obtained by the relevant entity do not exceed 25% of its global amount of income:

- royalties and other income regarding intellectual property rights, image rights and other similar rights;
- dividends and income arising from the sale of shares;
- income arising from financial leasing;
- income arising from banking business activities, even when not obtained by a credit institution, as well as from insurance activity or any other financial activities entered into with related entities;
- income obtained by invoicing entities whose income arises from transactions made with related entities; and
- interest and other types of capital income.

Moreover, the Portuguese company cannot choose to exclude the profits assessed by the foreign permanent establishment from its taxable income, up to the amount of tax losses assessed by such permanent establishments as have concurred to determine the Portuguese company's taxable income in the previous five fiscal years, or the previous 12 fiscal years for small and medium companies.

The Portuguese company also cannot choose to include the losses assessed by the foreign permanent establishment in its taxable income, up to the amount of profits that such permanent establishment has assessed that have not concurred to determine the Portuguese company's taxable income in the previous five fiscal years, or the previous 12 fiscal years for small and medium companies.

6.2 Non-deductible Local Expenses

The optional regime mentioned above with reference to foreign permanent establishments of Portuguese companies should be considered in light of local expenses. Provided that the same regime applies, the expenses made by the foreign permanent establishment are not deductible to determine the taxable income of the Portuguese company.

6.3 Taxation on Dividends from Foreign Subsidiaries

As a general rule, dividends from foreign subsidiaries should be considered to determine the taxable income of the Portuguese resident corporate shareholder, being subject to taxation at the rates stated in the Portuguese CIT Code. However, tax relief or even a tax exemption may be obtained in accordance with the applicable DTT.

Furthermore, in order to avoid the economical double taxation, the Portuguese CIT Code sets out a participation exemption regime, pursuant to which inbound dividends may be exempt from CIT, provided that the following requirements are met:

- the Portuguese company holds, directly or directly and indirectly, at least 10% of the share capital or voting rights of the distributing company;
- the shares have been held uninterruptedly for a 12-month period prior to the distribution of dividends (or, if held for a minor period, they are kept until the completion of such period);
- the Portuguese company is not subject to tax transparency;
- the distributing company is subject to and not exempt from CIT or any of the income taxes identified in the Parent Subsidiary Directive, or a tax of a similar nature with a rate not lower than 60% of the Portuguese CIT (ie, 12.6%). This requirement may not be applied if the tax effectively paid was not less than 50% of what would have been paid if the distributing company was resident in Portugal; and
- the distributing company is not deemed to be a tax resident in a blacklisted jurisdiction.

This tax exemption is subject to a specific anti-abuse clause, pursuant to which it should not be applicable if there is an arrangement or several arrangements, not deemed as genuine, that have been executed with the main purpose of obtaining a tax advantage defeating the object and purpose of eliminating the double taxation of dividends, taking into consideration all the relevant facts and circumstances.

For this purpose, an arrangement, or a set of arrangements, should be considered as non-genuine when it is not executed for valid economic reasons and does not reflect economic substance.

6.4 Use of Intangibles

Please see **2.2 Special Incentives for Technology Investments** regarding the patent box regime.

6.5 Taxation of Income of Non-local Subsidiaries Under CFC-Type Rules

The Portuguese CFC rules contained in the CIT Code closely follow the CFC regimes that have been adopted by several other EU countries.

According to the Portuguese CFC rules, the income generated by a CFC should be subject to taxation regardless of any dividends distribution, provided that some requirements regarding the percentage of shareholding, the location of the foreign entity in a tax haven territory and the evaluation of profit generated by the respective economic activity are met.

As regards the shareholding percentages, the resident shareholders – whether individuals or companies – should hold at least 25% of the shares, voting rights, profit rights or assets of the relevant non-resident entity, either directly, indirectly or by means of a fiduciary or an interposing agent.

With reference to the location criteria, a controlled company is an entity domiciled in a tax haven jurisdiction contained in the list of tax haven jurisdictions approved by Ministerial Order, or an entity that is subject to an amount of tax on income that is lower than 50% of the amount of tax that would be due in taxation under the rules set forth by the CIT Code.

Finally, regarding the business activity requirement, CFC rules may not apply if the following types of income obtained by the relevant entity do not exceed 25% of its global amount of income:

- royalties and other income regarding intellectual property rights, image rights and other similar rights;
- dividends and income arising from the sale of shares;
- income arising from financial leasing;
- income arising from banking business activities, even when not obtained by a credit institution, as well as from insurance activity or any other financial activities entered into with related entities;
- income obtained by invoicing entities whose income arises from transactions made with related entities; and
- interest and other types of capital income.

These CFC rules do not apply when the foreign entity is resident in another Member State of the EU/EEA (in the latter case, provided that the state of establishment is bound to administrative co-operation for tax purposes equivalent to the rules in force in the EU), and the resident company shows that the setting up and activity of such foreign entity is grounded in valid economic reasons and that the entity develops a business activity that involves employees, assets and business facilities.

6.6 Rules Related to the Substance of Non-local Affiliates

With the exception of the previously mentioned CFC rules, as well as the substance rules provided by the participation exemption regime and the exemption regime applicable to capital gains made by foreign entities, there are no specific rules regarding the substance of non-local affiliates. Nevertheless, the Portuguese CIT Code sets forth that a company may be considered to be a tax resident if its effective management takes place in Portugal. Therefore, if a non-local affiliate does not respect some standards of substance – such as the appointment of local directors, and the scheduling and execution of local board meetings or, at least, the board meetings to take key decisions – there might be a risk of such non-resident company being deemed a tax resident entity.

6.7 Taxation on Gain on the Sale of Shares in Non-local Affiliates

Please see **2.7 Capital Gains Taxation**. The gains should benefit from the participation exemption regime, provided that the following requirements are met:

- the local corporation holds, directly and/or indirectly, at least 10% of the share capital or voting rights of the transferred company;
- the local corporation is not subject to tax transparency;
- the transferred shares were held uninterrupted for a 12-month period prior to the transfer;
- the non-local affiliate is subject to and not exempt from CIT, any of the income taxes identified in the Parent Subsidiary Directive, or a tax of a similar nature with a rate not lower than 60% of the Portuguese CIT (ie, 12.6%). This requirement may not be applied if the income tax effectively paid was not less than 50% of what would have been paid if the distributing company was resident in Portugal; and
- the non-local affiliate is not deemed to be a tax resident in a blacklisted jurisdiction.

The requirement of the non-local affiliate being subject to a income tax with a rate not lower than 60% of the Portuguese CIT may not apply if at least 75% of its profits derive from agricultural or industrial activities in its tax residence country, or from commercial or services activity not directed predominantly to the Portuguese market, provided that its main activity is not related to:

- banking operations;
- insurance operations;
- shareholdings of less than 5% of the capital or voting rights, or any shareholdings in companies located in blacklisted jurisdictions, or other securities, intellectual or industrial property rights, and know-how in industrial, commercial or scientific sectors or regarding technical assistance services or
- lease activity, except regarding real estate located in its country of tax residence.

This exemption does not apply if the non-local affiliate has real estate in Portugal valuing more than 50% of its assets, unless such real estate is allocated to an agricultural, industrial or commercial activity (other than a real estate buy and sell activity) or was acquired before 1 January 2014.

7. Anti-avoidance

7.1 Overarching Anti-avoidance Provisions

There is a General Anti-Abuse Rule (GAAR) under which the Portuguese tax authorities can disqualify, for tax purposes, the typical effect of an arrangement or series of arrangements which, having been put into place for the main purpose of obtaining a tax advantage that defeats the object or purpose of the applicable tax law, are executed with an abuse of legal forms or are not genuine, having regard to all relevant facts and circumstances.

Where an arrangement or a series thereof is ignored and disqualified for tax purposes under the GAAR, the tax liability shall be calculated in accordance with the tax rules applicable to the arrangements corresponding to the underlying substance or economic reality – ie, the envisaged tax advantages will not apply.

For these purposes, an arrangement or a series of arrangements shall be regarded as non-genuine to the extent that it is not put into place for valid commercial reasons that reflect economic reality. An arrangement may comprise more than one step or part.

Whenever the GAAR is applied, the normal compensatory interest rate ordinarily levied by the tax authorities will be increased to 15%.

8. Other

8.1 Regular Routine Audit Cycle

While there is no routine audit cycle that applies to all companies, the Portuguese tax authorities prepare a National Tax and Customs Inspections Plan on a yearly basis. This plan sets forth the programmes and criteria for tax inspections, and should direct the tax authorities on the selection of taxpayers and set forth the targets to be accomplished by each organisational unit.

Furthermore, the Portuguese tax authorities created a Large Taxpayers Unit, which supports compliance and constantly monitors the tax activity of large taxpayers (defined based on numerical criteria, such as tax revenue and turnover).

9. BEPS

9.1 Recommended Changes

Portugal has already implemented several BEPS measures. The following are the most relevant:

- non-application of the participation exemption regime if the dividends received correspond to the costs deductible for tax purposes at the level of the distributing company or if the structure has a lack of economic substance (Action 2);
- CFC rules (Action 3);
- the introduction of interest barrier rules in order to limit interest deductibility as a way to erode taxable income (Action 4);
- amendment of the patent box regime in order to align it with the "modified nexus approach" by introducing an approach for calculating qualifying R&D expenses to determine the substantial activity requirement in relation to intangible assets (Action 5);
- disclosure of aggressive tax planning practices (Action 13); and
- country-by-country reporting (Action 13).

Portugal is also a signatory of the multilateral instrument (MLI).

Some of the actions mentioned above are the result of the implementation of EU Directives addressing some of the key factors identified by BEPS. For instance, the measures already taken with reference to BEPS Actions 2, 3 and 4 arise from the implementation in Portugal of the Anti-Tax Avoidance Directive (ATAD), the most recent development of which was in May 2019 with the approval of Law no. 32/2019, of May 3, which introduced slight amendments to the Portuguese tax framework regarding CFC rules, interest barrier rules, exit tax and the general anti-abuse rule.

Please see previous sections regarding the limits applicable to the participation exemption regime (**6.5 Taxation of Income of Non-local Subsidiaries Under CFC-Type Rules**), interest barrier rules (**2.5 Imposed Limits on Deduction of Interest**) and CFC rules (**6.5 Taxation of Income of Non-local Subsidiaries Under CFC-Type Rules**).

As regards the amendment of the patent box regime, in accordance with the Portuguese CIT Code, the tax deduction used to determine the amount of intangible taxable income should not exceed the amount given by the following formula: QE/TE x TI x 50%.

In this formula, QE stands for the "qualifying expenses" made to develop the intangible taxable income protected by an IP right; TE stands for the "total expenses" made to develop the intangible taxable income protected by an IP right; and TI stands for the "total income" generated by the intangible asset.

The disclosure of aggressive tax planning schemes was introduced by Decree-Law no. 29/2008, of February 25th. In order to increase legal certainty, a list of potentially abusive tax planning schemes that should be covered by the disclosure duty has been approved through the issuance of Dispatch no. 14592/2008, of May 27th.

Finally, CbC reporting was introduced in 2016, whereby multinational groups should submit country-specific statements disclosing detailed financial and tax information to the Portuguese tax authorities, provided certain requirements are met.

In accordance with the Portuguese CIT Code, this CbC reporting duty should be observed by:

- the ultimate parent company or the substitute parent company of a group of multinational companies whose total consolidated income is, in the immediately preceding period, equal to or higher than EUR750 million; and
- a constituent entity company in Portuguese territory, other than the ultimate parent company of a group of multinational companies, if one of the following conditions is met:
  - (a) it is directly or indirectly owned or controlled by non-resident companies that are not required to submit an identical declaration;
  - (b) in the jurisdiction where the ultimate parent company is resident there is an international agreement with Portugal in force but, by the deadline to submit the CbC report, there is no qualified agreement between the competent authorities; or
  - (c) there is a systemic failure in the jurisdiction where the ultimate parent company is resident that the tax authorities have notified to the constituent company.

Furthermore, on 11 December 2017, an order was issued (Order 367/2017) approving a new reporting model – Model 54.

9.2 Government Attitudes

As an EU and OECD member, Portugal is committed to the implementation of BEPS. As previously mentioned, several BEPS measures have already been implemented, whether by unilateral decision or by implementation of EU Directives dealing with the same tax challenges that are identified in several BEPS actions. Bearing this in mind, for the next few years BEPS should not give rise to any relevant tax reform in Portugal.

However, there are some specific tax issues that have led to some slight amendments during 2019. For instance, Law no. 32/2019, of May 3, has been approved, introducing amendments to the CFC rules, interest barrier rules, exit tax and the general anti-abuse rule in order to conclude the transposition into the Portuguese tax system of ATAD. Law. No. 119/2019, of September 18, was also recently approved, introducing amendments to the transfer pricing rules.

In the future, as a result of the influence of BEPS actions and ATAD 2, there are still some specific tax issues that may register amendments, namely regarding the prevention of treaty abuse, permanent establishment status and hybrid mismatches.

9.3 Profile of International Tax

As result of the world's financial crises initiated in 2008, Portugal has been subject to external financial assistance, which led to a major corporate tax reform in 2014 aimed at increasing competitiveness, allowing stability and attracting investment in order to relaunch the Portuguese economy.

Such corporate tax reform, along with other changes in the economic environment, contributed to bringing international investment and, consequently, international taxation to a high level of attention in Portugal, namely by the introduction of a wide participation exemption regime on dividends, at both inbound and outbound levels.

On the other hand, in order to protect the legal framework arising from said tax reform and assure stability for investors, the solutions adopted have already taken into account the international trends in corporate taxation, namely regarding BEPS action plan discussion.

Bearing in mind the high level of implementation that BEPS already has in the Portuguese corporate tax framework as a result of the solutions established by said tax reform, no relevant developments on these matters are expected in the near future.

9.4 Competitive Tax Policy Objective
Please see previous sections in relation to this matter.

9.5 Features of the Competitive Tax System
Reference should be made to the relevant preceding sections, bearing in mind that, as a general rule, the Portuguese corporate tax system is already adapted to the major implications of BEPS and there are no key features that are particularly vulnerable.

9.6 Proposals for Dealing with Hybrid Instruments
As mentioned above, as an EU country, Portugal is subject to the two EU anti-tax avoidance directives, ATAD and ATAD 2, which establish anti-hybrid rules aimed to cover hybrid mismatches, such as double dipping between EU countries, as well as between EU countries and non-EU countries.

ATAD rules have been implemented by Portugal. Furthermore, the Portuguese participation exemption regime already encompasses an anti-hybrid rule, pursuant to which such exemption does not apply when the distributing entity deducts the distributed dividends from its taxable income.

Further anti-hybrid rules established in ATAD 2 should be implemented in accordance with the deadlines established by said directive.

9.7 Territorial Tax Regime
As a rule, Portuguese tax-resident entities and individuals are subject to income taxation based on their worldwide income. However, new territorial features were introduced by the CIT reform in 2014, including a participation exemption applicable to capital gains and losses, an exemption applicable to gains derived upon the liquidation of non-resident entities, and an elective regime under which profits attributable to foreign permanent establishments may be exempt from CIT in Portugal.

Following the trend established in Germany and Spain, in 2012 Portugal introduced a BEPS-compliant restructuring of its interest deductibility limitations, including a so-called EBITDA rule, which is line with BEPS – Action 4.

9.8 CFC Proposals
Portugal does not have a territorial tax regime. A sweeper CFC rule would likely simplify CFC rules in general (including the Portuguese), but would likely struggle with both constitutional and EU-level opposition to the extent it could no longer resemble an anti-avoidance mechanism targeted at countering unsubstantiated deferral practices. In addition, such a rule could also disproportionately affect legitimate business decisions, thus creating potential economic distortion/inefficiency.

9.9 Anti-avoidance Rules
Some of the Portuguese double tax treaties already have limitations of benefits, as well as principal purpose test (PPT) type provisions. Notwithstanding, the PPT provision should be adopted with the MLI.

Following the examples in other EU countries, the Portuguese tax authorities are expected to strengthen their scrutiny of the applicability of DTCs. As such, foreign groups with current investments in Portugal should re-evaluate the substance of their investment and financing structures, as well as how they are deploying intangibles in their Portuguese businesses. From a different perspective, Portuguese groups using EU holding platforms may also consider restructuring in light of recent developments in Portugal.

9.10 Transfer Pricing Changes
Since 2000, Portugal has had a transfer pricing regime in line with the OECD guidelines, and for the time being there are no proposed changes. Additionally, the tax authorities and clients seek direction in the guidelines, and as such any further changes to it might have consequences. Generally, the taxation of profits related to intellectual property has not triggered increased controversy in recent years compared to pre-BEPS levels. This may also be a consequence of the tax authorities not having radically changed the profile of the average transfer pricing controls, which are still very much connected to a pure scrutiny of the fulfilment of documentary obligations and the application of methods. In addition, the fact that Portugal is a net capital importer or, in other words, more often than not a target jurisdiction has not exposed the country to intense BEPS-oriented IP planning.

9.11 Transparency and Country-by-country Reporting
The transparency and CbC regimes being proposed and implemented, together with the instruments developed in recent years to exchange information automatically or upon request, contribute positively to a fairer international tax environment. While these changes are likely to affect the citizen's perception of the tax system (and hence of democracies), it is expected that these new standards will contribute to raise international equity levels, thus allowing for a better distribution of resources.

Ultimately, positive spill-overs are to be expected as governments and the international organisations with tax policy roles are able to advance the tax system by enforcing taxation where value is created, in a world where digitalised models are also changing the rules of the game.

From a different perspective, the thresholds defined – namely regarding the application of CbC – ensure that these rules will not disturb the functioning of the economy, particularly in companies that do not have a significant multinational footprint. Additionally, the issuance of sector-specific guidance has progressively contributed to a better understanding of all these new standards that are accommodating unique specificities of certain industries also via experts' contributions.

9.12 Taxation of Digital Economy Businesses

No changes have yet been implemented to address concerns regarding the taxation of digital economy for corporate income tax purposes. In any case, Portugal was one of the ten European countries to urge the European Commission to explore options to establish an equalisation tax based on the turnover generated in Europe by the digital companies in the informal gathering held in September 2017. For VAT purposes, though, relevant changes have already entered into force to tackle the challenges of allocating indirect taxation rights in a fair manner in the digital economy.

9.13 Digital Taxation

Please see **9.12 Taxation of Digital Economy Businesses**.

9.14 Taxation of Offshore IP

The income paid in relation to offshore IP is subject to withholding tax at the aggravated rate of 35%. Moreover, payments made in connection with offshore IP may not be deductible if the local paying company is not able to demonstrate that such payments correspond to operations effectively occurred, and are not in an exaggerated amount.

9.15 Other General Comments

Despite its international tax activism, the BEPS process is attempting to rehabilitate the international tax system which has been in place for almost 100 years. As such, the OECD has not yet engaged in a radical reform of taxation principles, which have actually been kept and, in some cases, reinforced. A good example is transfer pricing, where the arm's-length principle still resists criticism.

More than reforming the tax system, by engaging in more radical dialogues such as those proposed by the ideologists of a destination-based tax, this is more a "fill-in the gaps" exercise. As such, it can be expected that more gaps will be created as businesses evolve and become more sophisticated – ie, digitised. In this regard, BEPS seems to be set more like a never-ending story as the OECD transitions from the implementation phase to active surveillance.

Recent times have given rise to very relevant discussions and proposed very innovative and effective measures to tackle the challenge of aligning economic substance and value creation while avoiding double taxation. Benefitting from the co-operation of governments, tax professionals and companies, the BEPS measures are generally quite well planned to address the present international taxation challenges.

Morais Leitão, Galvão Teles, Soares da Silva & Associados, SP, RL. has the largest tax group among Portuguese firms, with seven partners and more than 30 other lawyers, who are co-headed by the four partners mentioned below. The firm's tax lawyers work closely with colleagues in the transaction and corporate department of the firm, on matters relating to banking and finance, group reorganisations, M&A (both domestic and international) and real estate, among others. The team acts for some of the largest national and foreign corporate groups from a wide range of sectors, including energy, oil and gas, mining, finance, private equity funds, media, telecommunications, and construction. The team is particularly strong in litigation matters, assisting clients in proceedings before the tax authorities and all type of courts including tax arbitration, in tax infringement matters, parliamentary and similar investigations, as well as criminal prosecutions.

Authors

Bruno Santiago is a partner at the firm and has extensive experience in corporate reorganisations, M&A, foreign direct investment in Portugal and Portuguese investments overseas, with particular knowledge of the tax systems in Angola and Mozambique. He represents clients in high-profile cases in the tax courts and arbitrations relating to corporate and international tax matters.

António Lobo Xavier is a partner at the firm and works with large national and multinational companies, in the areas of finance, telecommunications, and industry, as a member of the board of directors, and as an adviser on finance and tax law. He is responsible for several organisational and restructuring operations and M&A, mainly as an expert in subjects related to double taxation treaties, VAT and corporate income tax. He was the Chairman of the latest Corporate Income Tax Reform that was held in 2013.

António Pedro Braga is a partner at the firm, who has been very active in all areas of tax law, with a special focus on the national and international corporate taxation of finance, industrial and commercial companies. He also has training in the accounting area, having been admitted to the Statutory Auditors Association in 2003.

Francisco de Sousa da Câmara is a partner at the firm, who specialises in tax restructuring operations and M&A transactions for large companies, and in complex corporate tax litigation involving domestic and international tax issues. He also advises high net worth individuals and family structures. Francisco was notably involved in drafting tax legislation, including the General Tax Law, the Proceedings and Procedure Tax Code, and a project for a wealth tax reform. He is a frequent author in several tax-focused publications in Portugal and abroad.

Morais Leitão, Galvão Teles, Soares da Silva & Associados, SP, RL.

Rua Castilho, 165
1070-050 Lisboa
Portugal

Tel: +351 213 817 400
Fax: +351 213 817 499
Email: mlgtslisboa@mlgts.pt
Web: www.mlgts.pt

MORAIS LEITÃO
GALVÃO TELES, SOARES DA SILVA & ASSOCIADOS