



TAX | Effective taxation on distributed profits

Administrative Circular 24/2011 of the Corporate Income Tax Directorate, regarding the effective taxation on distributed profits, was recently released.

This Circular follows a formal request for clarification submitted by Vieira de Almeida & Associados to the Director General of Taxes, concerning the changes introduced by the 2011 State Budget Law to the rules on the relief of double taxation of distributed profits.

The amendments concerned two essential aspects:

- (i) The elimination of the possibility to apply this scheme to a shareholding whose acquisition cost is of at least € 20,000,000, when it is below the 10% shareholding threshold. The application of this regime is therefore always subject to a minimum holding of 10% in the capital of the subsidiary, regardless of its acquisition cost;
- (ii) The elimination of the waiver of the requirement of effective taxation when the recipient company is a pure holding company (SGPS – Sociedade Gestora de Participações Sociais). Therefore, the application of this regime to SGPS is now always subject to the requirement of effective taxation of the distributed profits.

In order to clarify several doubts raised by this last change, Administrative Circular 24/2011 discloses, in general terms, the following answers to the questions raised by Vieira de Almeida & Associados:

The concept of the effective taxation

Requires income at the level of the parent company to be originated from profits that bore final Corporate Income Tax (CIT), or a similar or analogous corporation tax, and that were neither exempt nor excluded from such tax, at the level of the subsidiary

Objective and subjective exemptions and exclusions from taxation

The requirement for effective taxation presupposes that the subsidiary that generated the profits has not benefited from a CIT subjective exemption, but also that such profits were originated from income that neither benefited from a CIT objective exemption, nor was disregarded for the purposes of the assessment of the amount of CIT payable

Tax losses, deductions to taxable income and temporary differences

The requirement for effective taxation is considered to be verified when the absence of any burden in respect to CIT is a result of a deduction of tax losses, deductions to taxable income or temporary differences between the taxable income and the net accounting result

Payments on account and autonomous taxation

The requirement for effective taxation is not considered to be met by the simple fact of the application of the withholding tax mechanism, as well as the tax payments made on account (including the special payment on account) and the autonomous taxation

Cascading distribution of profits

The requirement for effective taxation on the distributed profit can be verified at any level of the profits distribution chain, i.e. either at the level of distributing company or at the level of any sub-affiliated companies that contributed to generate those profits



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Pure holding companies (SGPS) – Capital gains not subject to tax	The requirement for effective taxation is not considered to be met in respect of profits derived exclusively from capital gains obtained by pure holding companies and that have not been included in the taxable income pursuant to number 2 of the Article 32 of the Tax Benefits Code
Special Regime for the Taxation of the groups of companies	CIT assessed by the dominant company shall be deemed to have been borne by all companies belonging to the group. Thus, the requirement for effective taxation is considered to be met in respect of each company that contributed to generate the group's taxable profit
Relevant tax period of distributed profits	For the purposes of assessing whether the requirement for effective taxation is met, the tax period in which the profits to be distributed were generated is determined according to the profit distribution resolution. If this resolution does not specify such tax period, the "First In, First Out" (FIFO) method applies
Unitary profit	For the purposes of assessing whether the requirement for effective taxation is met, profits of a given tax period shall be considered in their totality and in an aggregated way. Therefore, the possibility to apply an apportionment system or to calculate a partial deduction of the distributed and effectively taxed profits is expressly excluded
Minimum threshold of taxation	The requirement for a minimum threshold of taxation for the distributed profits is expressly left out
Directive 90/435/EC	The requirement for effective taxation is considered to be met provided that the distributing company is resident in another EU Member State that takes one of the forms and is subject to one of the taxes listed in Directive 90/435/EC, without the possibility of an option or of being exempt
General Anti-avoidance rule	<p>The general anti-avoidance rule can be applied in relation to profits distributed either by Portuguese companies or by companies of another EU Member State.</p> <p>The application of this rule allows the deduction made (under the relief of double taxation of distributed profits) to be disregarded on a case-by-case basis – examples of circumstances that may lead to the disregard of this deduction:</p> <ul style="list-style-type: none">(i) Creation of a chain of share participations by artificially interposing companies for the purpose (or being this one of the main purposes) of benefiting from the deduction under the relief of double taxation of distributed profits;(ii) Schemes of abusive tax planning aiming, exclusively or predominantly, at obtaining advantages through that deduction;(iii) Artificial schemes where the income subject to and not exempt from tax is negligible when compared to the total amount of the profits of a certain tax period or where the income subject to the tax does not result from a real economic activity of the company

Although this Circular replies to some of the doubts raised following the changes introduced by the 2011 State Budget Law to the rules on the relief of double taxation of distributed profits, a number of relevant doubts still needs to be addressed and/or further clarified. Vieira de Almeida & Associados will pro-actively continue to seek clarification of these outstanding doubts.