

NEWS

TAX

Index

Corporate Income Tax (CIT)	1/2
Property Tax (IMI)	3
Tax News	4

CORPORATE INCOME TAX (CIT)

Payments to non-resident entities: the end of the nightmare?

Pedro Manuel

Imagine a scenario where Company X, tax resident in Portugal, contracts Company Y, tax resident in Spain, in order to provide the former a service. Consequently, the Portuguese company pays for the service that was rendered by the Spanish company.

The situation exemplified above raises no questions, right? Wrong!

According to Portuguese tax law, payments to a non resident entity, in our scenario Company Y, are subject to a final withholding tax – this withholding must be assured by the payer, i.e., the Portuguese entity.

In our scenario, as we are dealing with the rendering of a service, the Portuguese company should withhold tax at a 15% rate of the total amount paid to the Spanish company and deliver the said amount to the Portuguese tax authorities.

In the situation under analysis we are dealing with the rendering of a service, but Portuguese tax law, regarding payments made to non resident entities, is much broader and more vague, by applying final withholding tax rates, among other realities, to interest, royalties, dividends and capital gains obtained in Portuguese territory.

However, taxation by final withholding in Portuguese territory may be limited or even eliminated by applying a Double Taxation Treaty (DTT), duly approved by the Portuguese State.

DTT's are simply treaties duly signed by the Portuguese State and other countries, in which tax authorities or, better said, in which two countries try to avoid double taxation of income. In our situation, if the tax treaty between Portugal and Spain did not exist, income obtained by Company Y would be subject to double taxation, in Portugal, by withholding, and then in Spain, on the grounds that the company is tax resident in this territory.

[continue page 2](#)

Tiago Marreiros Moreira,
Conceição Gamito,
Joana Domingues,
Rita Magalhães,
Joaquim Pedro
Lampreia,
Ricardo Seabra
Moura,
Filipa Correia Pinto,
Catarina Belim,
André Gonçalves,
Pedro Manuel,
Francisco Matos and
João Riscado Rapoula.



Nevertheless, it is not as simple as that! According to Portuguese domestic law, in order to apply a DTT duly signed by the Portuguese State, the non resident entity must prove, in conjunction with the Portuguese tax authorities, that it is resident in the other country.

This proof of tax residence of a non resident entity, in conjunction with the Portuguese tax authorities, has some special conditions:

- ✓ The proof of tax residence is established through official forms distributed by the tax authorities (the legendary RFI Forms);
- ✓ These tax forms are then certified by the tax authorities of the non resident entity;
- ✓ The tax forms, duly certified, must be in the possession of the Portuguese entity until the tax triggering event (in service-rendering this day corresponds to the day of payment);
- ✓ If the tax forms are not in the Portuguese entity possession before the date of the triggering tax event, tax must be withheld at the domestic rate.

When the proof is not produced on time, the entity that was subject to withholding tax in Portugal can file for reimbursement within two years of the date of the triggering event, by presenting an official form duly signed by the tax authorities of the non resident entities.

It is easy to understand that all these steps are very difficult to comply with, within the timing set by Portuguese tax law, and therefore additional tax assessments, regarding payments made to non resident entities, have flourished in the last few years, generating a huge revenue stream for the Portuguese tax authorities.

It is important to state that, in this type of

situation, although tax is due from the non resident entity, it is the Portuguese entity that is legally bound to withhold the tax, and will be responsible for a subsequent additional assessment (including compensatory interest and penalties)!

In order to obtain net income, most of the contacts made between resident and non resident entities, include “gross up” clauses, which means that the payment of any tax falls, in all situations, on the Portuguese entity.

On these terms, only the Portuguese entities are worried about the application of DTT’s signed by Portugal, in order to reduce or eliminate the operation costs arising from transactions with non resident entities, as a vast majority of non resident companies obtain all income free of charge.

It is to this chaotic backdrop, that some changes in the tax law were proposed in the State Budget proposal for 2008, regarding this matter.

According to the State Budget proposal for 2008 the reference date to present the official tax form, in order to apply a DTT signed by Portugal, was changed.

If the State Budget is approved, the non resident entity will have to prove its tax residence before the last day in which the withheld tax must be paid, i.e., by the 20th day of the following month of the triggering tax event, extending the deadline for the presentation of proof.

However, the major change foreseen in the State Budget regards a new rule, added to CIT Code, in which, notwithstanding the possible penalties, the Portuguese entity that is legally bound to withhold tax has the possibility to prove, by means of the relevant tax form, the verification of the facts in order to reduce or eliminate withholding tax in Portugal.

The major change foreseen in the State Budget regards a new rule, added to CIT Code, in which, the Portuguese entity that is legally bound to withhold tax has the possibility to prove, by means of the relevant tax form, the verification of the facts in order to reduce or eliminate withholding tax in Portugal.

This new rule means that the Portuguese entity is not responsible for the tax due (and also compensatory interest and penalties) if it has managed to obtain a form duly certified by the non resident tax authorities even after the foreseen deadline, i.e., the 20th day of the following month of the triggering tax event, extending the deadline for the presentation of proof.

Nevertheless, this proof, presented after the deadline, obliges the Portuguese entity to pay a penalty, also projected for this meaning, which may vary from 500 Euros to 5.000 Euros, in the case of companies. Never before was a penalty so celebrated by the taxpayers...

Although it is not foreseen in the State Budget proposal for 2008, it is important to note that when discussed in Parliament, the majority party stated that these new tax rules should apply retroactively.

If this proposal is indeed approved, the possibility of certifying the tax residence of a non resident entity afterwards would be applicable to future tax inspections, to past tax inspections that result in additional assessments, as well as to situations now pending on decisions such as administrative claims, hierarchical appeal or judicial claims, regarding additional assessments previously made.

If these new rules are approved we may be looking at the end of a real tax nightmare!

PROPERTY TAX (IMI)

Doubled IMI tax for vacant buildings

Joana Domingues

The new rules governing the lease of Urban Properties sought – together with the boost of the properties leasing market – to improve the urban rehabilitation and renovation, creating the possibility of adopting further measures to achieve that goal. Among these measures, the introduction of a tax penalty for the owners who keep their urban residential properties vacant with the sole aim of forcing them to commercialize or occupy such properties assumes a very important role.

For this purpose, paragraph 3 of article 112 of the Property Tax Code (“CIMI”) now establishes the possibility of doubling the Property Tax (“IMI”) of vacant urban residential properties and Decree-Law no. 159/2006, of 8 August, has further defined the concept of “vacant urban residential properties”.

However, despite the fact that the announced purpose of said measures is the improvement of urban renovation, the concrete laws passed by the legislator lead us the opposite way and pervert the legislator's goal.

Decree-Law no. 159/2006, of 8 August, defines, specifically for the purpose of article 112 of the CIMI, a vacant property as one that *“has been vacant for a one year period”*, a status that should be checked by the absence of contracts or invoices related to the supply of water, gas, electricity and communications. Once these absences are confirmed, the property is classified as vacant and, according to what is provided by paragraph 3 of article 112 of the CIMI, the applicable IMI taxes should be doubled. It remains clear that the referred criteria for the classification of a property as vacant – being empty for more than one year – is strictly objective and disregards the ownership of such property, which means that any property that has not been occupied for more than one year and does not meet any of the exceptions of article 3 of the mentioned Decree-Law, may have the respective IMI doubled, even when the property has been

recently acquired by a new owner or is in its ownership for less than one year.

So, if one analyses this situation in the investors' perspective – mainly of such investors whose activity is to purchase properties for rehabilitation – it is understandable that they may preferentially purchase occupied properties in order to avoid this tax penalty, since in this situation they will have the total control over the one year term established on Decree-Law no. 159/2006. This investors' option is justified since, despite of all the tax incentives established in the CIMI and in the Portuguese Tax Incentives Statute (“EBF”) for urban renovation and rehabilitation, there is no provision establishing the reimbursement of the IMI paid under these circumstances, not even in the case of such property being then effectively rehabilitated. If, on the one hand, the EBF establishes certain advantages related to IMI in the event of the rehabilitation of the properties and if, as it results from the Extraordinary Provisions regulating Urban Rehabilitation included in the Appropriation Act's Proposal for the year of 2008, the legislator even intends to improve those advantages, on the other hand it is certain that in the event of the doubling of the IMI under paragraph 3 of article 112 of the CIMI, the tax paid will not be reimbursed in the future. Therefore, in case those intending to acquire a property for rehabilitation have the opportunity to choose between a vacant property or an occupied property, they will certainly prefer the latter (or, in the event of being two vacant properties, will prefer that that has been empty for a shorter period), perverting the legislator's purpose. This result was certainly not intended by the legislator, as becomes clear if one consider the goals of the relevant decree-law, as expressed in its preamble, and all further measures passed to boost urban renovation – mainly the tax incentives – since one may easily conclude that this solution fails as it perverts the whole system. A good solution for this problem would be to

If one analyses this situation from the investors' perspective (...) it is understandable that they may preferentially purchase occupied properties in order to avoid the tax penalty.

establish the possibility of reimbursement of the excess of the IMI paid by the purchaser of a property acquired for rehabilitation under the same circumstances established in article 40-A of the EBF – for the effective urban rehabilitation – eventually imposing the same term established in paragraph 2 of this article to begin the rehabilitation subsequently to the acquisition. This provision would ensure that those wishing to acquire a property for rehabilitation would not limit their decision of what property to purchase for tax reasons, especially determined by the concern of avoiding the possibility of that property, as a consequence of being vacant, being considered as a “vacant property”, under the provisions of Decree-Law no. 159/2006. Under these circumstances, the owners should have the possibility of requiring the reimbursement of the doubled IMI paid as soon as the rehabilitation is finished. As expectable, the implementation of such Decree-Law is generating several difficulties for those Municipalities that already begun classifying the properties as “vacant properties”, being especially interesting that some of them are the Municipalities more involved in the rehabilitation of their Historical Centres. It is however important to point out that, while some Municipalities are effectively implementing such rules, others exist that will only start classifying the properties in 2008. Although, on the one hand, this double way of acting under the referred Decree-Law leads to an incomprehensive discrimination between the owners of properties in the different Municipalities, on the other hand has the advantage of giving some room to introduce adjustments to those rules, regarding its several possible interpretations.



30 October

Tax procedure guarantees

A draft Law is now being analysed on Parliament with the objective of resetting the lapse of guarantees' regime regarding the tax procedure, which was revoked by the Budget Law for 2007. The goal is to re-establish the lapse of guarantees paid to freeze the tax enforcement proceedings within one or three years (in case of administrative or judicial claims). This draft Law prescribes that taxpayers are entitled to claim not only the amount paid as guarantee, but also a compensation for the maintenance costs of it. Notwithstanding this proposal intends to balance the taxpayers and tax authorities' positions, the draft Law aims, overall, to stimulate tax justice efficiency.

2 November

Real Estate capital gains reinvestment

Decree-Law 361/2007 came into force introducing amendments to the real estate capital gains regime of the Personal Income Tax Code (PITC). In line with the European Court of Justice decision (process C-345/05), the new regime establishes that real estate capital gains reinvested in real estate located within the Member State territory or the European Economic Area are exempted from personal income taxation (extending the previous regime which exempted only reinvestments within the Portuguese territory). Once the real estate capital gains are obtained it should be reinvested within two years.

2 November

Filipa Correia Pinto joins VdA Tax Practice

Filipa Correia Pinto, a Lawyer previously working with MLGTS Tax Practice in Oporto, joined Vieira de Almeida Tax Practice. Filipa Correia Pinto has extensive knowledge in tax practice, mostly on tax analysis of operations and on tax litigation and integrates VdA Oporto office, which reinforces an integrated and global response to its clients, in accordance with VdA service policies.

7 November

Informative Morning – Draft State Budget Law for 2008

Vieira de Almeida organised an Informative Morning regarding the draft State Budget Law for 2008, in which were highlighted the most relevant amendments contained in this draft Law, as well as their repercussions on taxpayers.

12 and 13 November

Real Estate Investment Funds Seminar

Pedro Simões Coelho and Tiago Marreiros Moreira participated, on the 12th and 13th November, as speakers in a seminar dedicated to Real Estate Investment Funds (REIF), organised by IFE – International Faculty for Executives, with the main purpose of explain the REIF legal framework and the respective tax issues that may rise.

13 November

Electronic commerce and invoicing seminar

Conceição Gamito participated as speaker at the electronic commerce and invoicing seminar organised by the Institute for International Research, analysing the main tax issues related to electronic invoicing.

15 November

New Official Tax Form - Form 10

Pursuant to the amendments introduced by Decree Law 361/2007, a new Official Tax form - Form 10 - is now available. Under this new form, companies must report the deductions related to social security regimes, health care systems or union contributions. These elements should be reported in 2008, concerning 2007 income.

15 November

Seize of bank account

Following an inspection promoted in several local tax authorities' offices, regarding some foreclosure processes, the Ombudsman office issued a recommendation to Banco de Portugal Governor in order to this entity recommend to credit institutions the end of foreclosure processes orders issued by the Tax Office, which lead to the freezing of all bank accounts, and by so, violating legal rules regarding this matter.

26 to 30 November

Institute for Construction and Real Estate

Conceição Gamito, Rita Magalhães, Joaquim Pedro Lampreia, Catarina Belim and Pedro Manuel participated as speakers in a qualifying course for companies, organised by the Institute for Construction and Real Estate (Instituto da Construção e do Imobiliário, I.P.) in which were analysed real estate taxes, VAT and accessory declarations related to real estate. It was also presented in brief the Portuguese tax infringement regime.

29 November

Madeira Free Trade Zone – Special tax regime

The Council of Ministers has approved the extension of the special tax regime in Madeira Free Trade Zone (MFTZ) applicable to companies licensed (or those that would be licensed until 2013) in MFTZ.

The special regime extends the reduced Corporate Income Tax rate presently applicable until 2020 (2007/2009 – 3%; 2010/2012 – 4%; 2013-2020 – 5%). To companies already licensed this regime is applicable from 1 January 2012.

Tax Calendar - December 2007

Day	Tax	Obligation
10	VAT	Monthly VAT returns - submission of October 2007 VAT return (and its annexes) and payment of the tax due.
15	Social Security	Payment of the previous months' contributions.
20	PIT/CIT	Payment of the tax withheld in the previous month.
20	Stamp Tax	Payment of the tax assessed for transactions performed in previous month.
31	CIT	Payment in advance of CIT due by a tax resident entity in which an activity of commercial, industrial or agricultural character is carried on and also by non resident entities with a permanent establishment in Portugal.

Vieira de Almeida & Associados - Sociedade de Advogados, RL | www.vda.pt

Av. Duarte Pacheco, 26 - 1070-110 Lisboa - Portugal | lisboa@vda.pt

Av. da Boavista, 3433 - 8º - 4100-138 Porto - Portugal | porto@vda.pt

Calçada de S. Lourenço, 3 - 2º C - 9000-061 Funchal - Portugal | madeira@vda.pt

This is a limited distribution newsletter and should not be considered to constitute any kind of advertising. The reproduction or circulation thereof is prohibited. All information contained herein and all opinions expressed are of a general nature and are not intended to substitute recourse to expert legal advice for the resolution of real cases.