VIEIRA DE ALMEIDA
& Associados Sociedade de Advogados, R.L.

Vieira de Almeida & Associados
Sociedade de Advogados
Mouzinho da Silveira, 10
P – 1250-167
Lisboa
Portugal

Tel: +351 21 311 3400
Fax: +351 21 353 2472
E-mail: lisboa@vieiradealmeida.pt

TAX

Regime change

The Special Debt Securities Tax Regime, due to come into effect in Portugal in the new year, will introduce a number of important developments relating to taxes incurred by non-resident entities. **Ricardo Seabra Moura** explains the key issues to consider

On 7 November, 2005, the Decree Law 193 approved the Special Debt Securities Tax Regime, which will take effect from 1 January, 2006.

The regime will introduce relevant amendments to the Portuguese debt securities tax regime applicable to bondholders (both individuals and companies) which are non-resident in Portuguese territory for tax purposes.

Tax on interest payments

The purpose of the new regime is to extend the existing tax exemption applicable to interest payments arising from Portuguese government bonds to interest payments in respect of debt securities issued by Portuguese corporate entities, and also to capital gains arising from both public and private debt.

Under the current regime, interest payments deriving from debt securities issued by Portuguese corporate entities which are held by resident or non-resident entities are subject to Portuguese withholding tax at a final rate of 20% (but this may be reduced in respect of non-resident entities by means of an applicable double tax treaty).

Under the Special Debt Securities Tax Regime, interest payments arising from Portuguese public or private debt securities held by non-resident entities (provided such payments are not attributable to a permanent establishment in Portuguese territory) which are not resident for tax purposes in the blacklisted jurisdictions approved by the Portuguese Ministry of State and Finance will be exempt from Portuguese withholding tax.

Further exemptions

In addition, the objective scope of the exemption has been widened in order to extend its applicability to:

- income obtained on coupon maturity;
- income obtained in the context of repo transactions; and
- debt security loan agreements or equivalent deals.

It should, however, be noted that private short-term securities issued for a period of less than one year (such as commercial paper) are excluded from the above regime.

Under the Special Debt Securities Tax Regime, any capital gains obtained in Portuguese territory from the sale or disposal of debt securities received by the above mentioned non-resident entities will be tax exempt.

However, it should be noted that the Portuguese State Budget for 2006 is already predicting a legislative authorisation that will allow the Portuguese Government to exclude from the scope of the exemption securities which are owned by non-resident entities held, directly or indirectly, in more than 20% by Portuguese resident entities, but including within such scope central banks and governmental agencies resident for tax purposes in blacklisted jurisdictions.

Transitory measures

The Special Debt Securities Tax Regime establishes a transitory provision (which applies to bond transactions prior to 1 January, 2006) clarifying that it will only be applicable to income obtained after the first coupon date after 1 January, 2006.

As a general rule, the direct custodian/register entity of the debt securities will have the obligation to obtain and provide evidence that the effective beneficiary is a non-resident entity.

The non-attendance of non-residence evidence in relation to any non-resident entities which qualify for the tax exemption described above shall carry the consequences of the income's liability to Portuguese tax.

Issuance of bonds

With this new tax regime, the Portuguese Government has now established the necessary conditions to strongly stimulate the bond market in Portugal. In fact, the issuance of bonds should, from now on, be considered a much more tax-efficient way of financing (since, as a general rule, it does not trigger Portuguese stamp duty on the issuance of notes and on interest payments).

In addition to this amendment, it is also expected that the legal limit presently applicable to the issuance of bonds will be increased in the very near future, which should make the debt issuance an even more attractive financing tool available to Portuguese companies — as currently, according to the Portuguese commercial law, the issuance of bonds can not exceed the existing and achieved share capital in the last balance sheet approved by the issuing company.

Ricardo Seabra Moura is an associate at Vieira de Almeida & Associados.