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WHT applicable to dividends obtained in Portugal by EU investment funds

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According to the Portuguese tax system, dividends distributed by Portuguese companies to non-resident investment funds are generally subject to withholding tax (WHT) at a 25% rate. The WHT may be reduced pursuant to a double tax treaty, insofar as the non-resident investment fund is eligible to claim double tax treaty benefits. However, no WHT is applied to dividends paid to Portuguese investment funds.

This difference in treatment between resident and non-resident investment funds has been seen as incompatible with EU law – namely, a breach of the free movement of capital. Therefore, a considerable number of cases have already been brought before the Portuguese tax courts by foreign investment funds that have claimed for the application of a full exemption (*pari passu* with Portuguese investment funds), which leads to a WHT refund.

One of these cases has reached the European Court of Justice (ECJ) and is currently awaiting a decision, which is expected shortly as the parties have already submitted their final written pleadings and the advocate general has already delivered her opinion (case C-545/19).

While most of the cases brought before national courts are pending the ECJ's position in case C-545/19, the Portuguese courts did not find it necessary to wait for the ECJ ruling in some cases. Taking the view that there are already sufficient grounds for the assessment of a breach of EU law, several national courts have considered the extensive ECJ case law that deals with WHT that has been levied on dividends distributed by resident entities to non-resident entities, and concluded that there was indeed a breach that renders Portuguese domestic withholding tax provisions incompatible with the free movement of capital. Therefore, there are a growing number of decisions in the tax arbitration courts

that are favourable to non-resident investment funds. These cases are becoming common in Portugal and have already led to several effective refunds.

For the purposes of claiming WHT refunds on these grounds, taxpayers should file an administrative claim (which is the mandatory first step) within two years from the legal deadline to deliver the WHT to the Portuguese tax authorities. This means that the recent trend will likely evoke a change in the Portuguese legislation to end the discriminatory treatment, as it is already creating leeway for foreign investment funds to claim back the WHT suffered in the past two years.

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