March - 2016

BUDGET LAW MEASURES FOR 2016

The Budget Law for 2016 (Law n.º 7-A/2016) was published on 30 of March 2016. The Budget Law provides for several tax measures impacting on areas that range from corporate tax, indirect taxes, real estate taxes and personal income tax. Garrigues tax team provides an insight into the most relevant tax measures.

1. Corporate Income Tax (IRC)

In terms of corporate income tax, we would highlight the following measures:

- Halt on lowering the CIT rate that was predetermined in the framework of the CIT reform of 2014. Portuguese CIT will continue for 2016 to be levied at a 21% standard rate, to which may be added a municipal surtax ("*derrama municipal*") and a state surtax ("*derrama estadual*") up to a combined maximum rate of 29.5% (depending on place of activities or level of profits).
- Revision of the participation exemption rules for outbound and inbound dividends and capital gains derived by resident companies which provide for the increase of the minimum shareholding percentage from 5% to 10% and lowering of the holding period from 2 years to 1 year. These rules are scheduled to apply already in 2016.
- Reduction of the loss carry-forward mechanism from 12 years (in place since 2014) to 5 years. This rule is scheduled to apply only as from 2017 onwards. The 12 years remain applicable to small and medium enterprises ("SME") as per the qualification provided in Decree-Law 372/2007, of 6 November.
- Introduction of country by country ("CBC") reporting for multinational groups with a net turnover exceeding EUR 750 million, which largely reflect the recommendations made by the OECD with respect to Action 13 of the OECD Base Erosion and Profit Shifting (BEPS) project.
- Authorization to amend Patent Box Regime which currently provides a 50% exemption for income derived from the licensing of certain qualifying intellectual property, which will imply the introduction of the "modified nexus approach" adopted under Action 5 of BEPS project. These amendments are expected to apply as from 2017 onwards.
- Authorization to establish an optional tax revaluation of fixed assets and investment properties applicable in 2016 with remaining useful life of 5 years or more. This tax revaluation will imply an upfront taxation at a rate of 14% (payable in three equal instalments in 2016, 2017 and 2018).

In the meantime, Law 5/2016 of 29 February also amended the CIT Code by implementing the Directive 2015/121 that establishes an anti-abuse rule for the purposes of transposition of the Parent Subsidiary Directive.

Under the said anti-abuse rule, the Portuguese domestic participation exemption regime for outbound and inbound dividends will not be applicable to profits and reserves distributed (or received) when there is "*an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose to eliminate double taxation on those profits and reserves, are not genuine having regard to all relevant facts and circumstances*".

For the purpose of the Portuguese implementation of the anti-abuse rule, it is understood that "*an arrangement or series of arrangements shall be regarded as not genuine to the extent that they are not put into place for valid commercial reasons and do not reflect economic substance*".

2. Personal Income Tax (IRS)

In terms of personal income tax, there are no major changes as there was a PIT reform enacted in 2015. It is nonetheless worth mentioning:

- Budget Law does not contain material changes to the personal income tax rates (progressive or flat rates).

- Budget Law withdraws the family quotient approved in the said reform and the revision of the tax credits against the tax due.

- No change is also included affecting non-habitual residents. Budget Law includes an authorization for the government to implement during 2016 an automatic procedure to register non-habitual residents.

- Budget Law includes an authorization for the government to transpose the Directive 2014/107/UE and Common Reporting Standard (CRS) regarding automatic exchange of information mechanisms to domestic law.

3. Other relevant measures

In terms of other taxes, we would highlight the following:

- Reduction as from 1 July 2016 of the VAT from 23% to 13% on certain restaurant and catering services.

- Increase of 50% on stamp tax on consumer credit and elimination of stamp tax exemption certain non-qualified shareholder loans (below 10% shareholding and 1 year holding period). Interbank guarantees and commissions will also no longer be exempt from stamp tax, with the exception of those connected with the effective granting of credit to clients. The Budget Law also provides for stamp tax at a rate of 4% on fees charged on credit/debit card-based payments.

- The Portuguese Bank Levy is extended for 2016 and will also payable by Portuguese branches of EU/EEA based credit institutions (excluded under the prior rules). The Bank Levy will also be increased for 2016 to a rate that can range between 0.01% and 0.11% over the institutions' liabilities, reduced by their core capital (tier 1) and complementary capital (tier 2). The remaining rates remain applicable. The contribution directed to the pharmaceutical industry will be maintained for 2016.

- Significant increase on excise duties (IEC) in particular affecting alcoholic beverages, oil and energy products and tobacco. The Budget Law also provides significant increases to Vehicle Tax (ISV) and to the road tax (IUC).

- Automatic increase of the tax value for property tax (IMI) on property allocated to commercial, industrial and services activities.

- Changes on the taxation for property tax (IMI) and real estate transfer tax (IMT) affecting real estate investment funds. This includes the termination of an existing tax exemption for open-ended investment funds for both property tax (IMI) and real estate transfer tax (IMT) purposes. In addition, the Budget Law considers taxable for transfer tax purposes (IMT) the transfer of more than 75% of the units of closed real estate investment funds to a single purchaser (similar to a provision currently applicable to the transfer of limited liability companies – Lda).

- Minor amendments to the tax regime applicable to Portuguese Collective Investments Vehicles (recently revised by Decree-Law 7/2015), namely:

  - For qualified non-resident unit holders/investors in a Portuguese CIV the current tax regime disqualifies from the tax regime: (i) non-residents resident in a blacklisted territory; or (ii) non-resident entities directly or indirectly held in more than 25% by Portuguese resident entities. The Budget Law provides that: income distributed by the CIV or derived from redemption of units accruing to individuals/corporate entities resident in a blacklisted territory are taxed at a 35% withholding tax rate. The 35% rate is also applicable when the income is paid or made available by a local paying agent to accounts held on behalf of undisclosed third parties (omnibus accounts), unless the beneficial owner is identified.

  - The carve-out for income paid to non-resident entities directly or indirectly held in more than 25% by Portuguese residents will no longer apply when such non-resident entity is: (i) resident in the European Union; or (ii) resident in European Economic Area (EEA), if the state of residence of the entity is bound to an administrative cooperation mechanism similar to the one established within the European Union; or (iii) resident in a country with a tax treaty in force with Portugal, which foresees for exchange of information mechanism.

- Reinforcing domestic exchange of information mechanisms that will allow the access by the tax authorities to payment made by credit and debit cards for entrepreneurs (category B taxpayers).

- Authorization for the establishment of a film production tax incentive for CIT purposes to be drafted during 2016.

For more information or if you wish discuss in detail any issues related to this alert, please contact your local Garrigues professionals.

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