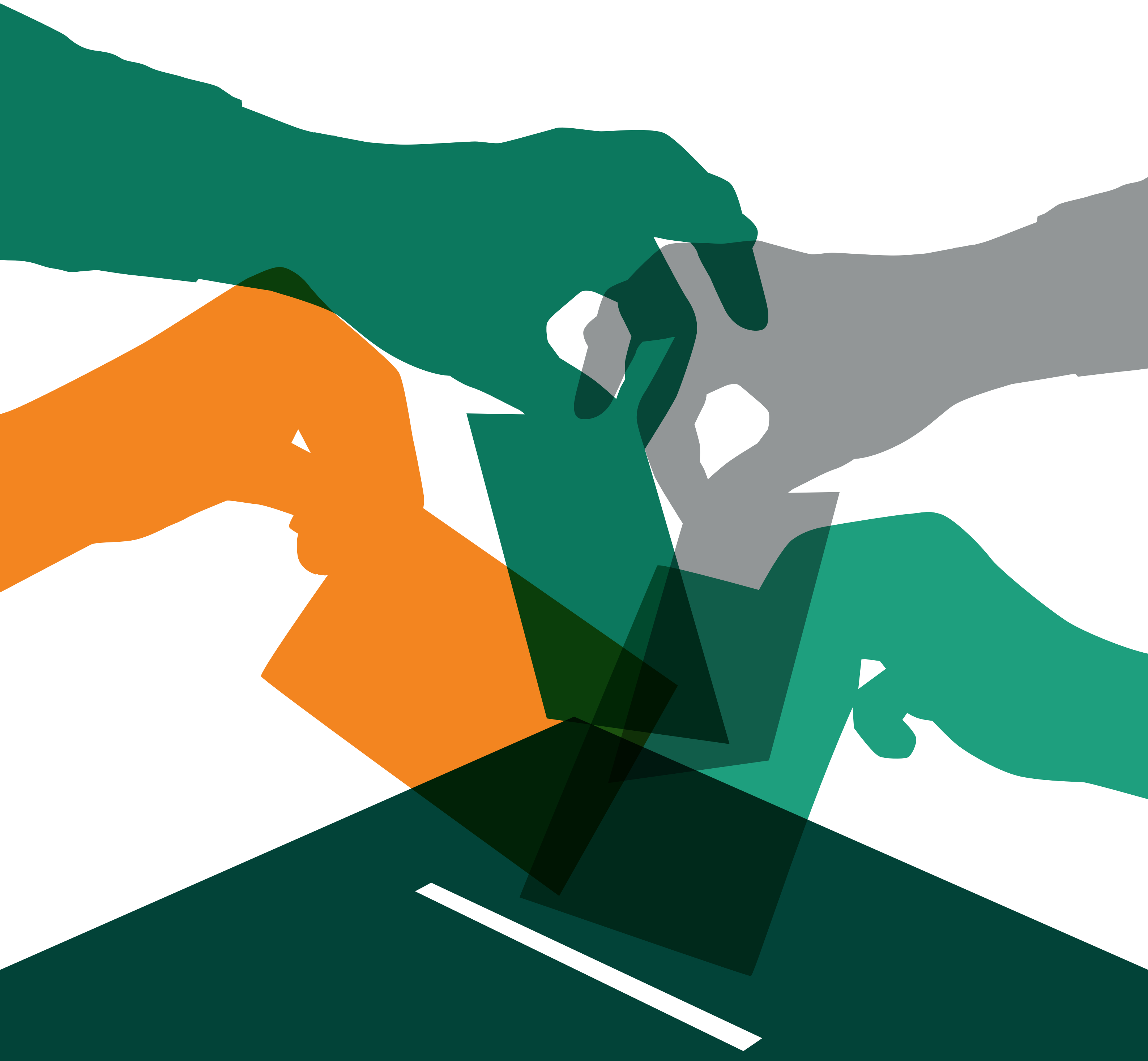
POLL MODE

BUDGET PROPOSALS 19



GARRIGUES

Portuguese Budget Proposals for 2019 – Selection of Tax Measures

The Portuguese Budget Bill for 2019 was presented to the Parliament on 15 of October 2018. The Budget Bill includes several tax measures impacting on areas that range from corporate tax, personal income tax, indirect taxes and property taxes.

Despite certain expectation that there could be significant tax changes, the final proposal has not included any major structural amendment but rather simple adjustments/clarifications and, therefore, may be framed as a consolidation Budget with focus on stability and continuation of the tax/economic policy of the last years. Having said this, the Budget Bill may be divided in two main structural ideas: stability and reinforcement. As for stability, all the suggestions for reduction of the personal income tax rates and progression, as well as possible changes to the so-called non-habitual regime for inward expatriates were not incorporate in the final text. To the contrary, the key Budget highlights indicate government tax policy directed to reinforcement of anti-abusive and transfer pricing orientated measures and the creation of a new tax regime for "ex-residents" to curb the brain-drain. This Budget still continues to push the level of tax incentives connected with productive investment and a special focus on preservation and enhancement of forestry resources. Absent from the Budget Bill are measures for the transposition of the EU Anti-avoidance Directive (ATAD), which the Government opted apparently to cover in a separate piece of legislation.

The Budget Bill will now enter a phase of parliamentary discussion during a period of at least 6 weeks to arrive to a final text. Garrigues tax team provides a first insight into the 20 most relevant tax measures, which if approved are expected to apply as from 1 January 2019.

Corporate Income Tax (CIT)

- Impairment losses on receivables of doubtful of recovery are no longer recognized for tax purposes if the credit is linked to a company held, directly or indirectly, in more than 10% of its share capital by the same shareholder (company or individual). This is not applicable if the debtor is under an insolvency or revitalization type procedures (judicial or of-court) or if the credits have been claimed judicially or through arbitration courts.

- Since 2014, amortization costs of intangible assets (such as (e.g. goodwill acquired in a business combination, trademark and licenses) (i) acquired for consideration; and (ii) with no defined life span, are tax deductible, during 20 years after their initial recognition (in equal parts each year). The Budget includes a provision that such costs will no longer be deductible if the intangible assets are acquired from a related party entity, as provided by the transfer pricing rules.

- The Budget for 2019 aligns the Portuguese capital gains rules applicable to non-residents on the transfer of real estate rich companies with other provisions, such as the recently implemented taxation of foreign indirect shareholdings. It is now proposed a clarification to the domestic capital gains exemption providing that indirect transfers of real estate rich companies should not benefit from the domestic capital gain exemption, when realized by non-residents. An asymmetry between the taxation of residents and non-residents remains in place.

- Under the current tax regime for investment support (RFAI), companies may benefit from a tax credit against tax due for certain qualifying investments. The Budget proposes to increase the maximum limit for eligible investments from €10 million to €15 million that benefit from the application of a 25% tax credit. The 10% tax credit continues to apply for investments above €15 million.

- The current deduction for retained earnings and reinvested earnings (DLRR) is essentially an incentive that provides the ability for micro, small and medium-sized companies to apply a CIT deduction of 10% of their retained and reinvested earnings used for the acquisition of relevant expenditure. The Budget proposes to increase the maximum amount of retained and reinvested profits which may apply for tax deduction from €7.5 million to €10 million.

- There are also a number of additional adjustments and extensions of the tax incentives, with particular mention the contractual tax incentives and to the special regimes applicable to forestry activities (either via investment funds or entities that undertake forestry management activities). Following the recent abolition during 2018 of the important job creation tax incentive, the Portuguese Government anticipates (subject to approval under EU State Aid rules) of the intention to put forward a job creation incentive targeted to Portuguese inland regions allowing deduction of additional 20% of labor related costs (with a limit of the CIT payable in each period).

- The autonomous tax (CIT charge over certain expenses) is a special feature of the Portuguese tax regime ultimately designed to disincentive certain corporate expenses. The Budget widens the scope of this autonomous tax by increasing the rates for costs linked with light passenger vehicles and motorcycles from 10% to 15% (vehicles with acquisition cost lower than € 25.000) and from 35% to 37,5% (vehicles with an acquisition cost equal or higher to € 35.000).

- The deadline for submission of CIT tax return in case of cessation of activity changes from thirty days counting from the cessation date to the end of the third month following the date of the termination of the activity. This new three month deadline applies equally to any CIT tax return of the prior fiscal year to the termination of the activity if and when the deadline has not yet elapsed.

Personal Income Tax (PIT)

- A new tax regime planned to be applicable until 2023 is proposed for the so-called "ex-residents" who return to Portugal, providing that employment income (Category A) and business and professional income (Category B) will be taxed only at progressive rates on 50% of the income derived, when:

  - Taxpayers become tax resident within 1 January 2019 and 31 December 2020;
  - Taxpayers have been tax residents in Portugal in any given fiscal year prior to 31 December 2015 (and not been considered resident taxpayers in the 3 years prior to the start of the regime); and
  - Taxpayers have not requested for the application of the non-habitual tax regime (i.e. it is not cumulative with NHR status).

- The Budget provides that supplementary work income and income relative to prior years should be subject to advance withholding taxes, with specific withholding taxes being applicable to such income streams. In the same way as for holiday and Christmas subsidies, those income streams should not be added to the regular income for purposes of determining the general withholding tax applicable under the PAYE system.

- The PIT tax return deadline for submission will be changed from 31 May to 30 June of each calendar year.

- The Budget also includes an authorization for the government to review the capital gains rules applicable on the allocation of any personal assets to the conduct of a business or profession by the individual in order to deem the taxable event only the effective disposal of the asset.

Indirect Taxation (VAT and other taxes)

- The Budget transposes to domestic law the EU Directive 2016/1065 dealing with the VAT treatment of vouchers. Following this transposition, the VAT Code will include a definition for "voucher", "single-purpose voucher", "multi-purpose voucher" and establishes the chargeable event and the taxable value for these types of vouchers.

- In Portugal the VAT rates are as follows: (i) Reduced rate - 6% (4% for the Azores and 5% for Madeira) for goods and services included in List I annexed to the VAT Code; (ii) Intermediate rate - 13% (9% for the Azores and 12% for Madeira) for goods and services included in List II annexed to the Code; and (iii) Standard rate - 23% (18% for the Azores and 22% for Madeira) applying to all other goods and services. The Budget proposes several adjustments to the list of services and goods subject to the reduced and intermediate rates, with particular reference to certain cultural activities that may access as from 1 July 2019 the reduced rate.

- The Budget includes a proposal to reduce the scope of the exemption of the Energy Sector Extraordinary Contribution applicable to assets allocated to the generation of electricity through renewable energy sources, namely in the situations where the production of energy is covered by guaranteed remuneration schemes. Under the terms proposed, renewable energy companies which are covered by this kind of remuneration regimes are impacted unless qualifying as cogeneration or renewable energy with electric power installed below 20 MW.

Stamp Tax and property taxes

- Last year the Budget approved an increase of the stamp tax levied on regulated consumer credit based on the maturity of the loans. The new rates applicable during 2019 will be as follows: (i) consumer credit of less than one year (0.192% from 0.12% per month/fraction); consumer credit of one year or more (2.4% from 1.5%); (iii) consumer credit of term of five years or more (2.4% from 1.5%); (iv) consumer credit of period not determined (0.192% from 0.12% per month by the monthly average of the debt).

- A special tax incentive currently allows companies involved in a merger to qualify for exemption from RETT with respect to the transfer of real estate, as well as exemption from registration fees and stamp tax that normally would be due. This regime was revised in 2018 and the Budget proposes to make this exemption also automatic (no need for prior request) also for the case of demergers. The Budget on the other hand introduces a specific anti-abuse rule (SAAR) designed to allow the tax authorities to consider this exemption not applicable if "*it is concluded that the operations had as a principal purpose or has one of the principal purposes the obtainment of a tax advantage, which may be considered verified, namely, when the operations are not undertaken for valid economic reasons and do not reflect economic substance, such as the reinforcement on competitiveness and productive structure*". In cases where the tax authorities apply this SAAR, they are authorized to issue an assessment increased by 15 per cent.

- In cases of real estate financial leasing, the lessors will no longer be able to reflect on the financial lessees the Additional property tax (AIMI) if the cadastral tax value of the asset leased does not exceed € 600.000.

- There is an authorization for the Government to change the classification of urban buildings or autonomous units as vacant, as well as to set the definition of "urban pressured area", as well as to proceed with an aggravation of the tax rate of the annual property tax (IMI) applicable, up until six times its current rate, to urban buildings or autonomous units that are vacant for more than two years and located in urban pressured areas. The tax rate may be aggravated in each subsequent year in 10% up until 12 times.

Garrigues will monitor closely this phase of political debate and is available to discuss with you the potential impact of the proposed measures on your business or activities.

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

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