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Source and residence: new configuration of their principles

sos extranjeros sobre una base eficaz y equitativa. Además, desde el decenio de 1980 y hasta 2000 se ha producido una repatriación de fondos procedentes de países extranjeros exentos del impuesto sobre los ingresos y sin ninguna necesidad de proporcionar explicaciones respecto a la fuente, siempre que estos fondos entren en el sistema financiero local.

En el presente siglo, tal situación está cambiando con rapidez gracias a la creciente realización y negociación de tratados para evitar la doble imposición, así como a la introducción de cambios legislativos que aplican convenientemente impuestos a los ingresos de fuente extranjera, aunque haya huecos legales. En términos generales, la conclusión de los últimos 15 años de política tributaria es que Perú está tratando de imponer más impuestos a los ingresos de fuente peruana. Sin embargo, mientras Perú no tenga varios tratados que mejoren la compilación de información sobre la fuente de los ingresos obtenidos por un residente, será conveniente continuar aplicando el principio jurisdiccional de los ingresos mundiales, evitando la evasión respecto a los impuestos sobre los ingresos peruanos. En 2003 se introdujeron cambios respecto a las normas relativas al principio de la fuente (ingresos de fuente peruana), que trataron de ampliar el alcance de la tributación y de actualizar las normas aplicables en vigor respecto a las nuevas tendencias internacionales de la tributación directa.

En relación con los métodos para evitar la doble imposición internacional, nuestras normas nacionales proporcionan el método del crédito como método unilateral. Como medida bilateral, la propuesta peruana de establecer acuerdos para evitar la doble imposición internacional establece el uso de cualquiera de los dos métodos existentes (método de la exención o el crédito), especificando que el método debe seleccionarse basándose en un análisis de nuestra legislación en relación con las leyes del país con las que se negocia. Si se negocia un crédito directo existe la posibilidad de conceder adicionalmente un crédito indirecto de primer grado, que permite evidenciar los impuestos cobrados a la sociedad que distribuye el dividendo al residente peruano.

Por último, los ingresos de fuente extranjera y los créditos por los impuestos pagados en el extranjero por la producción de tales ingresos son aplicados globalmente al residente, cualquiera que sea el tipo de inversión o actividad y/o el país de la fuente de dichos ingresos permitiendo arrastrar pérdidas de fuente extranjera durante un período indefinido de tiempo.

Portugal

Branch Reporter
Rogério Manuel Fernandes Ferreira*

1. Policy

So far Portugal has favoured entering into bilateral double taxation conventions with those states with which its economic relations are closer either by reason of commercial relations or migratory movements. Of particular significance are those concluded with European Union and OECD Member States, as well as those states having Portuguese as their official language. Within the scope of negotiations already initiated with a view to the conclusion of new conventions or the renegotiation of conventions already entered into, the criteria followed take into consideration the relative position of the contracting states, as far as economic development ratios are concerned, aiming at the elimination of double taxation of distributed profits, the limitation of benefits granted, and the exclusion of certain taxpayers from the scope of the conventions.

Considering the aims of this report, our analysis will focus on those income categories deemed to be more relevant in the Portuguese economic context (income from immovable property, business profits, dividends, interest and royalties).

In relation to income from immovable property, the applicable rule is taxation by the state where the property in question is located (*locus rei sitae*). In this case, we can therefore see that the solution adopted by Portugal does not deviate from that provided by the model convention. Nevertheless, we may find some variations, although some of them are in conformity with the provisions of the model convention as regards some items susceptible of being included in the category of income from immovable property. Thus, for instance, the convention concluded with Romania establishes that comprised in this concept are "property accessory to immovable property, livestock and equipment used in agriculture and forestry". Conventions concluded with Finland, France or Switzerland also establish that, irrespective of the concept of immovable property adopted by the domestic law, it shall include "rights to variable or fixed payments as a consideration for the working of, or the right to work, mineral deposits, sources and other natural resources". On the other hand, in the conventions concluded with Italy and Spain it was agreed upon, under a protocol, that the regime shall apply to "income from movable property in connection with immovable property and

* Lawyer; Expert in Tax Law

services designed for the maintenance and working thereof". In short, we can say that the concept of "immovable property" is coincident with that in force within the scope of the domestic law of each contracting state and the concept becomes broader so that it may cover some situations not directly provided for by the domestic law, which are relevant in the area of international relations, in order to allow for taxation in the state where the property is sourced.

In relation to business profits, the applicable rule is that included in the model convention, i.e. taxation by the state of residence, except in those cases where the activity is carried on in the other contracting state through a permanent establishment (PE), and insofar as profits are attributable thereto. Profits attributable to a PE are computed as if the establishment were a distinct and separate enterprise. However, while in the conventions concluded with Germany, Ireland, Morocco, Poland, the Czech Republic, Romania and Switzerland, that computation is made in accordance with domestic general rules and costs may be deducted irrespective of the place where they are incurred, in other conventions, such as that entered into with Austria, it is set down that there shall be allowed as costs only those duly substantiated. Also excluded is the deductibility of any costs which would not be deductible if the PE were an enterprise of the source country. A protocol was concluded with Italy establishing that there shall be allowed as deductions only "expenses duly substantiated which were incurred for the realisation of the purposes of that permanent establishment". Likewise, in the convention concluded with the United Kingdom it is said that the term "industrial or commercial profits" shall

> "include income derived by an enterprise from the conduct of a trade or business, including income derived from the furnishing of services of employees or other personnel[1] and dividends, interest or royalties effectively connected with a trade or business carried on through a permanent establishment which an enterprise of a Contracting State has in the other Contracting State..."

It therefore becomes evident that, insofar as the taxation rights are shared between the state of source and the state of residence where there is a PE, in accordance with the above-mentioned provisions, the state of source has its powers enlarged not only by reason of limitation of deductible costs for the purpose of determining the taxable income, but also owing to the broadening of the concepts used.

It should finally be noted that Portugal made some reservations in order to be able to tax any person who performs independent services, if such a person is present in the domestic territory for more than 183 days in any 12-month period, even if no PE is available to him. In short, the situations taken into consideration would point to a clear increase of taxing powers for the state of source, which seems to be more favourable for Portugal, considering the fact that it is an "importer of business and investment".

1 In this respect, our domestic law no longer considers the existence of a PE where the activity is performed in Portuguese territory (through employees or other personnel contracted for that purpose for an uninterrupted or interpolated period of time of at least 120 days in any 12-month period); this being so, currently there is no domestic provision identical to the provision of the convention allowing for taxation.

As far as taxation of dividends, interest and royalties is concerned, we will present a single analysis given the similarity of regimes in the conventions concluded by Portugal. The general rule is taxation in the state of residence. However, this is not an exclusive right to the extent that the state of source may also tax such income, although at a reduced rate varying between 5 per cent and 15 per cent.

With regard to the formulation of reservations, Portugal usually wishes to adopt an interest tax rate higher than that provided for in the model convention for taxation in the state of source, having therefore reserved the right to extend the concept of dividends, interest and royalties so as to cover, *inter alia*, some situations such as the partial transfer of rights attached to software, income from leasing of industrial, commercial or scientific equipment, and of containers, as well as income arising from technical assistance connected thereto, thereby increasing the taxation power allocated to the state of source.

Considering the treatment of these issues in the light of domestic law provisions, we may conclude for the existence of a mixed system. Resident persons, both individuals and companies, are subject to tax on a worldwide base, and non-residents are taxed only on income derived in the domestic territory.[2] Reference should be made here to the facts that (i) Portugal adopts the principle of absorption or limited attractive force,[3] according to which there shall be considered as part of the income attributable to the PE of a non-resident entity, in addition to "income of whatever nature derived by way of it", also "any other income derived in the Portuguese territory from an identical or similar activity as the activity carried on through that permanent establishment" belonging to a non-resident entity, and (ii) that the concept of PE laid down in Portuguese domestic law[4] is more comprehensive than that adopted in the model convention. For instance, in the model convention a building site is deemed to constitute a PE only if it lasts more than 12 months, whereas in domestic law the time limit is reduced to 6 months, starting from the preparatory works without any interruption for any reason. It should finally be noted that the concept of residence, of particular relevance for individuals, may be based on different connections with the domestic territory, including the mere intention to occupy a dwelling house under such conditions that it may be supposed to be an habitual abode.

In recent years, there has been no significant change in the policy followed by Portugal; furthermore, in both Community directives of major impact on this area – the Parent–Subsidiary and Interest–Royalties Directives – which are mainly designed to grant taxation rights to the state of residence, Portugal has benefited in both cases from a transitional period during which it maintains its taxation rights as state of source.

In Portugal, in recent years, no studies either at an institutional level or at an individual level have been made concerning the cost–benefit ratio of international convention rules, or in respect of the allocation of taxing powers between the state of source and the state of residence. In this field, an important academic

2 In relation to individuals, art. 15 of the IRS Code (personal income tax code); in the case of companies, art. 4, §§1 and 2 of the IRC Code (corporate income tax code).

3 See art. 3, §3 (2nd part) of the IRC Code.

4 See art. 5 of the IRC Code.

work was recently published that makes an approach to the subject matters dealt with in this report. It is an MA study that analyses the issues involving corporate taxation in the Community area, starting with the description of the three systems under discussion (taxation in the source country; the European tax on corporate income; and taxation on a common consolidated base), pointing out their respective advantages and disadvantages, and concluding with a critical appraisal of each one. In an abridged form, we may say that its author considers that none of the models is able to overcome the obstacles which in the present context are a hindrance to Community tax harmonisation. In any case, no answer is given to the issues under consideration.[5]

In the course of most recent years, unfortunately there have been no studies on the costs–benefits of tax treaties, on certain treaty provisions concerning the taxation of items of income or any shift between source/residence taxation.

2. Portuguese income taxation of residents and non-residents

As referred to above, taxable persons subject to income taxation (personal income tax – IRS and corporate income tax – IRC) are any individual or company resident in the Portuguese territory, in which case the principle of worldwide income taxation applies. There shall be considered as resident in Portugal any individual who, in the year to which the income relates, is present there for more than 183 days, uninterrupted or interpolated, or, having been present for a lesser period of time, has, on 31 December, a permanent home available to him under such conditions as to indicate an intention to maintain and occupy it as an habitual abode. Moreover, the Portuguese legislator considered as resident in Portugal those persons who are part of a household insofar as any of the persons (spouses) who are the head of the family are resident there. With regard to companies, there shall be considered as resident those with their head office or place of effective management situated in Portuguese territory. These rules are set down in the personal income tax and corporate income tax codes, in force as from 1 January 1989, with no substantial change thenceforth.

Thus, we may conclude from the analysis of the present regime that Portugal has opted for a taxation regime on residents that is based on their worldwide income; in this case, any income derived abroad is taxed in Portugal as if it were derived from a domestic source. As a matter of fact, considering the principle underlying taxation of residents, their localisation at source is not, as a general rule, relevant insofar as the connection element that enables the Portuguese state to exercise its taxing powers is the domicile, head office or the place of effective management of taxable persons. Then, as a general rule, the juridical nature of the income payer will be of no consequence, as well as the fact that income is transferred or not to Portugal.

[5] See Paula Rosado Pereira, *A Tributação das Sociedades na União Europeia: Entraves Fiscais ao Mercado Interno e Estratégias de Actuação Comunitária*, Almedina, Coimbra, 2004.

Even if income never enters into Portuguese territory – by a banking route or any other – the Portuguese state maintains full taxing powers, and the taxable person is required to give evidence thereof in his yearly tax return. In analysing this regime, no significant discrepancy appears at the level of taxation on companies or individuals.

Within the scope of personal income tax (IRS) relief of international double taxation is achieved by granting to the income owner a tax credit up to the amount of the taxable basis corresponding to such income. The limit is the equivalent of the following amounts, whichever is the lesser: (i) income tax borne abroad, and (ii) that fraction of the taxable basis as computed before the deduction is given, corresponding to that income that may be taxed in the state in question. Where there is a double taxation convention, the deduction to be made shall not be higher than the amount of tax that would be paid abroad in accordance with the limits of the convention. If the taxable base in the year during which such income is obtained is not sufficient, the remaining credit may be deducted up to the end of the five subsequent years from that part of the taxable base pro rata to the net income of the corresponding category. However, income derived by residents abroad, under cooperation agreements, or enrolled in peace forces in the service of the United Nations, is tax exempt. It should be noted that, in spite of this exemption, income derived as such must be aggregated for the purpose of determining the applicable tax rate.

Within the scope of corporate income tax (IRC) the method adopted under Portuguese domestic law is also the tax credit, its regime being identical to that applying to individuals. Excluded are situations of distribution of dividends by the subsidiary resident in another EU Member State, in which case income included in the taxable base corresponding to distributed profits shall be deducted. For such a regime to be applied, it is necessary that: (i) the company paying income is subject to tax and not exempt therefrom; (ii) the beneficiary entity is not covered by the tax transparency regime; and (iii) the participation is higher than 10 per cent of the capital stock or, if less, has an acquisition value of no less than 20,000,000 euro, and is held during the year prior to profits being made available, or, if held for less than one year, the participation is held for a period of time necessary to complete that period.

In the conventions concluded by Portugal different criteria have been adopted with a view to eliminating double taxation situations. In the conventions with Germany, Austria and Mozambique, the adopted method is the exemption method with progressivity – income is not taxed but its aggregation for the purpose of determining the tax rate is obligatory; however, in these conventions the ordinary imputation method is also provided for – income is taxed according to the general terms, and the state of residence "credits" the tax borne in the state of source. As a rule, we may say that the adopted methods are the ordinary credit method for non-exempt income, and in relation to exempt income, the exemption method with progressivity.

For the purposes of determining the taxing powers of the Portuguese state in connection with income derived by non-residents, Portuguese domestic tax law expressly enunciates income deemed to be obtained in the domestic territory. As a general rule, this is the case with activities carried on in the domestic territory,

or in connection with immovable property situated therein, or income payable by entities resident in Portugal.

With a view to the application of those regimes aiming at the elimination/alleviation of double taxation, the taxable person is required to give evidence that his activity was subject to income tax abroad. That is to say, the substantiated existence of tax abroad, in accordance with the laws of the other state, is a condition for the application of those regimes aimed at the elimination/alleviation of international double taxation. Should Portugal limit the category of "income from abroad", it would be perverting its own regime of elimination/alleviation of double taxation to the extent that it would simultaneously limit its scope by restricting the notion of "foreign income": if the entirety of income derived by residents were taxed (worldwide taxation), double taxation would then be promoted, thereby counteracting the purposes of the regimes under consideration. Where a non-resident entity derives income that is not considered to be obtained within the domestic territory, it is not taxed in Portugal.

Income from foreign source derived by a PE situated in Portugal is subject to personal income tax, taking into account income obtained in Portuguese territory. As a matter of fact, if such income (either of internal or international source) is attributable to the PE it is taxable in Portugal. On the other hand, corporate income tax, insofar as it is levied on profits attributable to a PE situated in Portuguese territory and belonging to an entity without its head office or place of effective management therein, is also levied on those profits.

In relation to non-resident entities with a PE in Portugal, there shall be allowed a tax credit in favour of the PE where it derives income taxed in a foreign state, in accordance with the provisions of the model convention.

Under the terms of Portuguese domestic law, profits derived by a non-resident company subject to a clearly more favourable taxation regime shall be attributable to its resident members pro rata to their respective corporate rights. This rule was introduced in the Portuguese legal system by Decree Law no. 37/95, of 14 February.

There are no specific provisions on foreign income fund rules in Portuguese law.

Portuguese tax law provides for an objective exemption in respect of income from capital gains realised from the transfer against payment of corporate rights, other marketable securities, autonomous warrants issued by resident entities and negotiated in controlled markets by non-resident individuals or companies without a PE. This exemption does not apply where the non-resident entity is, directly or indirectly, owned by more than 25 per cent by resident entities. This regime was enacted by Law no. 87-B/98, of 31 December (1999 State Budget Bill). Likewise, this exemption does not apply to non-resident entities without a PE and with their domicile in a territory with a clearly more favourable tax regime included in the list approved by a ministerial order (*portaria*) from the Minister of Finance. Nor does it apply to capital gains realised by non-resident entities from the transfer against payment of corporate rights in companies resident in Portuguese territory, the assets of which are constituted more than 50 per cent by immovable property located in Portugal or, in the case of holding companies, those which have a controlling position. This regime results from the wording given to the Tax Incentives Statute (*Estatuto dos Benefícios Fiscais*) by Law no. 109-B/2001, of 27 December.

As a rule, no subjective exemptions (on a case-by-case basis or not) are allowed. The tax regime of the Free Zone of Madeira provides for an objective exemption, which means that income derived by (i) entities established in the respective delimited industrial area, (ii) licensed entities carrying on a shipping industry, (iii) credit institutions and (iv) other kinds of companies will benefit, provided some special requirements are met, from an income tax exemption (personal income tax or corporate income tax) until 31 December 2011. However, entities licensed as from 1 January 2003 are subject to corporate income tax at a rate of 1 per cent between 2003 and 2004, 2 per cent in 2005 and 2006, and 3 per cent from 2007 to 2011.

The situation described above has not been the object of any substantial change in recent years, except as concerns this last-mentioned taxation at reduced rates.

In accordance with Community law, binding on Portugal, Member States are not allowed to discriminate against corporate persons on the basis of their nationality or the nationality of owners of capital stock. In Portuguese tax law there is no separate treatment, even for residents in third states (non-EU), for companies owned by resident or non-resident entities/individuals. Nevertheless, there subsist in Portuguese law some special situations that are not in compliance with the non-discrimination principle. Thus, some changes are likely to occur in this area in the short term. The thin capitalisation regime is only applicable in respect of excessive indebtedness of a national enterprise towards a non-resident entity with which it has special relations. The deduction as costs of social utility of expenses incurred with health, life or personal accident insurance is only allowed where the insurance contract is concluded with an entity having its head office or place of effective management in the domestic territory. Reinvestment of realisation amounts in order to prevent taxation on capital gains is also not allowed with non-resident entities located in a territory with a clearly more favourable tax regime, or with non-residents with which special relations exist, except, as regards the last-mentioned case, if designed at the realisation of capital stock. There shall not be deductible for the purpose of determining the taxable income any amounts paid or payable, irrespective of the way they are paid, to individuals or companies resident outside the Portuguese territory and subject therein to a clearly more favourable tax regime, unless evidence is given that such charges correspond to operations effectively realised and they are not of an anomalous nature or an excessive amount. Profits derived by non-resident companies subject to a clearly more favourable tax regime (if owned by a resident with a direct or indirect participation of at least 25 per cent, or 10 per cent where the company is owned more than 50 per cent by resident members) are attributable to the company member pro rata to the respective corporate rights.

The preceding situation has not been the object of any substantial change in recent years.

Domestic law provides for taxation of residents on their whole income, i.e. irrespective of whether it is derived in Portugal or abroad. In this sense, taxation on income derived by residents is not dependent upon the taxation regime applying thereto in the state of source. In any case, as already mentioned, in the sphere of those measures designed to combat tax avoidance and evasion, a list of countries with a tax regime considered to be clearly more favourable has been published, by way of a ministerial order from the Minister of Finance. Where

resident persons, both companies and individuals, participate in the capital of a company with its head office in a territory covered by the above-mentioned ministerial order, or where it is not taxed on income in the state of residence, or the tax paid therein is equal to or less than 60 per cent of the tax that would be paid in Portugal, the profit of such a company is assigned to its members pro rata to the capital owned by them. For this purpose, it is necessary that such a member owns, directly or indirectly, a corporate right more than 25 per cent, or, if the company is held by residents more than 50 per cent, a participation of at least 10 per cent. This regime was introduced by Decree Law no. 37/95, of 14 February.

3. Portugal's taxation as a source country

Table 1 shows the taxation of Portuguese source income earned by non-residents.

In Portugal a general approach to determining the geographical source of income has not been developed so far. We may infer from the analysis of the Portuguese tax regime that, depending on the nature of income, the adopted criterion varies between the source of payment, the source of production, or fictions.

Under corporate income tax, the basic rule is the taxation of profits attributable to a PE situated in the domestic territory. The principle of effective connection is in force, together with the principle of limited attractive force. As far as it concerns personal income tax, the rule is the same, such income being taxed in Portugal.

Under personal income tax, income derived by a non-resident that is not attributable to a PE in Portuguese territory is taxed if in connection with the exercise of professional or independent activities, or other services, including services of a scientific, artistic or technical nature, and agency services in the celebration of a contract of whatever nature, realised or used in the Portuguese territory, other than those activities concerning transport, telecommunications and financing activities, insofar as they are payable by entities having therein their residence, head office, place of effective management or a PE to which such payment is attributable. Likewise, income derived from a single act performed in Portuguese territory is also taxed in Portugal. Under corporate income tax, the profits of a non-resident enterprise not attributable to a PE located in Portugal are determined in accordance with the rules set down for the corresponding categories of personal income tax, and also the object of taxation, as for the purposes of this latter tax, in the case of income related to immovable property located in Portuguese territory, including capital gains resulting from its transfer, or gains resulting from the trasnfer of parts of capital stock in entities with their head office or place of effective management in Portuguese territory.

The basic rule is taxation at source of any payment in connection with dividends distributed by a domestic subsidiary, as well as portfolio investments in Portugal.

Income earned from services performed by independent professionals and consultants, if payable by resident entities in Portuguese territory, or the payment of which is attributable to a PE situated therein, provided it is realised or used in

Table 1. Portugal's domestic law treatment of income earned by a non-resident

Type of income	A. Does Portugal tax this income when earned by a non-resident?	B. Is the non-resident taxed on a net or gross basis (i.e. can he deduct relevant expenses)?	C. At what rate is the non-resident taxed?
Business profits (excluding services) attributable to a local PE	Yes (but Portugal also adopts the principle of limited attractive force)	Net basis	25% – IRC; 30% – IRS
Business profits (excluding services) not attributable to a local PE	No (however, it is taxed if it is a single act performed in Portuguese territory)	NA	NA
Dividends paid to a foreign parent	Yes	Gross basis	25% (except Parent–Subsidiary Directive
Dividends paid to a foreign portfolio shareholder	Yes	Gross basis	25%
Independent services rendered by professionals and consultants	Yes	Gross basis	25%
Independent services by artistes and athletes	Yes	Gross basis	25%
Other types of independent services	Yes	Gross basis	15% – agency commissions in the celebration of any contract/other services rendered (non-territoriality of transports, telecommunications and financing activities)
Employment income	Yes	Gross basis	25%
Shipping and air transport income	No	NA	NA
Rental payments for immovable property	Yes	Net basis	25%
Interest	Yes	Gross basis	20% (exemption for certain incomes of public debt;

Table 1. (cont.)

Type of income	A. Does Portugal tax this income when earned by a non-resident?	B. Is the non-resident taxed on a net or gross basis (i.e. can he deduct relevant expenses)?	C. At what rate is the non-resident taxed?
Interest (cont.)			exemption for private debt under consideration[a]
Rental payments for equipment (not a financial lease)	Yes	Gross basis	15%
Royalties	Yes	Gross basis	15%
Capital gains on shares	Yes	Net basis	10% – IRS (except shares owned for more than 12 months) 25% – IRC In both cases possibility of exemption of article 26 of EBF
Other capital gains	Yes	Net basis	25%
Pensions	Yes	Gross basis	25%
Other important categories of income	Yes		

[a] Under the terms of Law no. 107-B/2003, of 31 December (2004 State Budget), the government was authorised to "create a regime of exemption from personal income tax and corporate income tax for income from marketable securities representative of non-public debt derived by non-residents in the Portuguese territory and having not a permanent establishment available in this territory to which such income is attributable". Such income concerning marketable securities of non-public debt covers those realities qualified as income from capital and capital gains for the purposes of income taxation.

Portuguese territory (other than services in connection with transport, communications and financing activities) is taxable under personal income tax or corporate income tax, as the case may be.

Income derived by artistes and sportsmen, under the terms of personal income tax, is subject to the basic rule of taxation at the source of production (the place where the services are rendered). Under corporate income tax, the basic rule is the source of payment.

As to income derived from other kinds of independent services, under personal income tax the basic rule is taxation at source of production/utilisation of services,

and under corporate income tax, the basic rule of liability is to tax at the source of payment.

Income derived from the exercise, within the domestic territory, of dependent services (employment), or where the paying entity has therein its residence, head office, place of effective management, or a PE to which such payment is attributable, is taxed in Portugal.

Income from shipping and air transport is taxed in Portugal where the beneficiary entity is a resident in the domestic territory. Where the beneficiary thereof is a resident of another state, income derived in the domestic territory shall not be taxed insofar as an equivalent benefit is granted to resident companies of the same nature and such reciprocity is recognised by the Minister of Finance.

Income from immovable property is taxable in Portugal under personal income tax or corporate income tax, if such property is located there (*locus rei sitae*).

Income from rental payments for equipment is subject to tax if the payer has his residence, head office or place of effective management in Portuguese territory, or if such payment is attributable to a PE situated there.

With regard to taxation of interest and royalties the rule adopted by the Portuguese tax law follows the source of payment criterion.

The Portuguese legal system establishes liability to tax – personal income tax or corporate income tax – of capital gains on shares if the representative of the capital of entities has its head office or place of effective management in Portuguese territory.

The rule adopted in Portugal, in respect of capital gains concerning immovable property, is, as mentioned above, the location of the good (*locus rei sitae*). In the case of capital gains from marketable securities, the relevant element of connection is the head office, or the place of effective management of the issuing entity in Portuguese territory, or the allocation of payment to a PE situated there. In the case of alienation against payment of intellectual or industrial property, or experience acquired in the commercial, industrial or scientific sector, where the transferor is not the original owner, taxing powers are determined on the base of a fiction that the effects are to be produced in the place where the registration or any equivalent formality is performed.

In relation to pensions, the basic rule adopted is taxation according to the source of payment criterion.

Where any good, right or a juridical situation to which other property accretion is related is deemed to be located in Portugal, a mixed cumulative criterion of *locus rei sitae* and source of payment applies.

As we have seen, income attributable to a PE of a non-resident entity is subject to the same regime as applies to resident entities.

For income obtained by a non-resident entity to be computed on a net basis it must be attributable to a PE situated in Portugal. In such case, there may be allowed as costs, in determining the taxable profit of the PE, general administrative expenses in conformity with allocation criteria accepted and according to limits deemed reasonable by the Portuguese tax administration which are attributable to the PE. The criteria underlying the allocation of costs must be justified in the respective tax return and show consistency in successive exercises.

Payments made to non-resident persons, individuals or companies, subject to a clearly more favourable tax regime (domiciled in

in the list approved by a ministerial order from the Minister of Finance, or where the amount of tax paid is equal to or less than 60 per cent of the amount that would be payable if the entity were located in Portugal) is not deductible in determining the taxable profits, unless the person concerned gives evidence that the charges are effectively related to an economic operation, and their amount is not deemed to be excessive. Taxable persons making such payments are required to produce, after notification for that purpose, and within 30 days at least, any supporting evidence of tax paid by the non-resident entity, as well as any computation made for the assessment of tax that would be due if the entity were considered to be resident in Portuguese territory. This regime was laid down by Decree Law no. 37/95, of 14 February.

Likewise, such payments made to a beneficiary in the above-mentioned situation give rise to payment of tax, as an autonomous taxation, at a rate of 35 per cent or 55 per cent depending on the paying entity being subject to the general taxation regime, or being wholly or partly exempt therefrom, or not performing as its main activity a commercial, industrial or agricultural activity. This regime was introduced by Law no. 30-G/2000, of 29 December.

On the other hand, where a non-resident entity that is subject to a clearly more favourable tax regime, as mentioned above, derives capital gains from the transfer against payment of corporate rights, other marketable securities, autonomous warrants, and derivative financial instruments, there shall not apply the tax relief consisting of exemption of such capital gains, which will be taxed according to the general regime. This regime was introduced by Law no. 30-G/2000, of 29 December.

With regard to income derived by a resident having its source located in a state with a clearly more favourable tax regime, the corporate income tax code sets down that any charges arising from the transfer against payment of corporate rights, irrespective of the manner in which it takes place, if held by the alienator for less than three years, shall not be allowed as costs or losses of the exercise.

Where a company resident in a clearly more favourable tax regime is owned, directly or indirectly, more than 25 per cent by a resident, or such a company is owned more than 50 per cent by resident shareholders with a participation of at least 10 per cent in its capital stock, profits shall be assigned to resident shareholders pro rata to their participation in the equity capital. In such cases, only the income tax levied on such profits in the state where the company is a resident will be allowed as a deduction. In addition to tax liability, there are also some duties of a formal nature insofar as the resident is required to keep his accounting, to be produced if so requested, as approved by the competent corporate bodies of the non-resident company; the chain of direct and indirect participations between the non-resident entity and resident entities; and evidence of tax paid by the non-resident company together with an estimate of tax that would be due if the company giving rise to such income were a resident of Portugal.

In respect of personal income tax, and for the purpose of determining the balance between capital gains and losses realised in a given tax year, with regard to (i) onerous alienation of corporate rights, including the redemption and amortisation by way of capital decrease, and other marketable securities; (ii) operations concerning derivative financial instruments; (iii) operations concerning

autonomous warrants; and (iv) operations concerning certificates granting to their holders the right to receive the value of a given underlying asset, any losses incurred shall not be taken into account where the counterpart is domiciled in a territory with a clearly more favourable tax regime.

Under personal income tax, only residents are entitled to personal allowances according to Portuguese domestic law. On the other hand, no relief of a personal nature is allowed under income taxation. However, there are some exceptional situations in this regard, in which public interest overrides general principles and the law provides for the granting of special (contractual) benefits to certain entities, deemed to be relevant from a socio-economic point of view. Thus, investment projects in production units carried out before 31 December 2010, of an amount equal or higher than 4,987,978.97 euro, which are relevant for the development of a sector considered to be of strategic interest for the national economy and the reduction of regional asymmetries, leading to the creation of jobs and contributing to stimulate technological innovation and domestic scientific research, may benefit from tax incentives for a maximum period of ten years. In addition to an exemption or reduction of capital taxation, such incentives are granted, as far as income taxation is concerned, by way of a tax credit to be determined on the base of a percentage to be applied, ranging from 5 per cent to 20 per cent, of the relevant project investments effectively carried out. The investment project is, therefore, required to comply with some quantitative limits and qualitative requirements.

4. Coordination of residence and source country taxation

Portugal's tax treaty policy with regard to income is given in Table 2.

Conventions entered into by Portugal essentially follow the provisions of the OECD model convention, as already mentioned. However, since Portugal is an investment recipient country, there has been an attempt to amplify the spectrum of taxation in the state of source, considering the fact that there has been no significant change in the socio-economic context in which Portugal is inserted, its policy in this respect has undergone no substantial change.

In general terms, Portuguese domestic policy concerning negotiation of double taxation conventions does not comply with the requirement of tax-sparing clauses. In any case, from an analysis of the conventions so far concluded it may be inferred that such clauses in favour of Portugal have been included in the conventions with Austria, Belgium, Italy, Finland, Macao, Norway and the United Kingdom. In the convention with Malta there is a tax-sparing clause that benefits both contracting states, although with a time limit of the first seven years counting from its entry into force. Where in the course of a negotiation there is a proposal to include a clause of this kind and it is not adopted in the final wording, the existing tax incentives shall not suffer any change for residents of that other state deriving income subject to tax in Portugal.

According to the preceding paragraphs, the adoption of tax-sparing clauses by Portugal is not a common policy. Nevertheless, the conventions concluded with

Table 2. Portugal's tax treaty policy with regard to income

Type of income	A. Follows the OECD model convention	B. Tries to obtain more residence taxation rights than are provided in OECD model	C. Tries to obtain more source taxation rights than are provided in OECD model
Business profits (excluding services) attributable to a local PE	Yes	No	No
Business profits (excluding services) not attributable to a local PE	Yes	No	No
Dividends paid to a foreign parent	Yes	No	No
Dividends paid to a foreign portfolio shareholder	Yes	No	No
Independent services rendered by professionals and consultants	Yes	No	No
Independent services by artistes and athletes	Yes	No	No
Other types of independent services:	Yes	No	No
Employment income	Yes	No	No
Shipping and air transport income	Yes	No	No
Rental payments for immovable property	Yes	No	No
Interest	Yes	No	No
Rental payments for equipment (not a financial lease)	No	No	Yes[a]
Royalties	No	No	Yes[b]
Capital gains on shares	Yes	No	No
Other capital gains	Yes	No	No
Pensions	Yes	No	No
Other important categories of income	Yes	No	No

[a] As referred to throughout this text, Portugal imports more investment than it exports. Thus, Portuguese tax policy is centred on the reinforcement of powers of the state of source, the most common situation for Portugal. In this respect, Portugal has reserved the right to treat these realities as royalties – a situation in which the taxing power is shared between the state of source and the state of residence. Furthermore, technical assistance services connected with leasing of such goods, and containers, are equally covered by the concept of royalty for tax purposes, under the terms of conventions so far concluded.

[b] According to the preceding footnote, reservations made by Portugal in this context are intended to extend the concept of royalty in order to cover some realities that, as a rule, are analysed and taxed in accordance with regimes that grant to the state of source exclusive taxing powers. It should be noted, however, that Portuguese tax policy relies essentially upon the relative position of the contracting parties. Thus, in the tax conventions concluded with Cape Verde and Mozambique, the final wording is quite close to that of the model convention.

Mozambique, Macao and Cape Verde include a provision of this kind in favour of these states. As already mentioned, the convention with Malta contains a tax-sparing clause, although it is limited to the first seven years of its entry into force, in favour of this state (an identical benefit is established in favour of Portugal, as already mentioned).

Over the last few years there has been no significant change in Portuguese domestic policy as regards tax-sparing provisions being agreed upon or asked for.

As far as income taxation is concerned, we could not find any situation of financial compensation between states, by virtue of sharing rules of taxing powers.

In line with the OECD guidelines, the taxation levied on a PE of a company resident in another contracting state shall not be subject to a regime more burdensome than the regime applying to domestic companies. Accordingly, the conventions concluded by Portugal comply with this principle (non-discrimination), as expressly shown in the conventions with Malta, Macao and Mexico.

At the Community level, the Court of Justice (Case 270/83 *Avoir Fiscal*, judgment of the Court of 28 January 1986; and Case C-307/97 *Saint Gobain*, judgment of the Court of 21 September 1999) decided that discrimination against PEs of non-residents is against the provisions of the Treaty (freedom of establishment); therefore, Member States are required to tax the PE of a company resident in another Member State in accordance with the law applying to their own enterprises.

In the Portuguese legal system, in accordance with international doctrine, the principle of the negative effect of treaties is applied. In conformity with this, and as a general rule, conventions only regulate the sharing of taxing powers between

states in order to avoid or to alleviate double taxation of the same income derived by the same taxable person. This means that they are not a primary source of tax liability, and it is not usual to give a wider scope to the concepts underlying the tax events provided for in the domestic law. And where such widening occurs, it cannot give rise to any obligation that would not result from domestic law.

The rules included in the conventions concluded by Portugal are, generally speaking, more favourable or identical to similar provisions of the Portuguese domestic legal system.

Appendix

Resolution no. 6328/2002 (2nd Series), of 24 September 2001, from the Secretary of State for Fiscal Affairs, published in the official journal (*Diário da República, II Série*, of 22 March 2002) contains some recent decisions concerning Portuguese external tax policy.

Résumé

Le Portugal est un "importateur" d'investissement dont le tissu économique est essentiellement constitué par de petites et moyennes entreprises qui, en raison de leur structure et de leur taille, ne visent pas l'internationalisation. Les principes ancrés dans le modèle de convention de l'OCDE ont été adoptés dans les conventions de double imposition afin de promouvoir jusqu'à un certain point les pouvoirs d'imposition accordés au pays de la source. Ce résultat est atteint essentiellement par l'élargissement des concepts. Le Portugal a accordé la préséance à la négociation de conventions avec les États membres de l'UE et de l'OCDE, ainsi qu'avec les États dont la langue officielle est le portugais, bien qu'aucune convention n'ait été conclue jusqu'ici avec l'Angola, Sao Tomé et Principe et la Guinée-Bissau.

Au Portugal, les résidents sont imposés sur leur revenu mondial – indépendamment de la source – tandis que les non-résidents sont imposés sur les revenus censés provenir du territoire national. La législation fiscale portugaise établit le principe de la non-discrimination, sauf dans le cas de règles spéciales visant à lutter contre les abus, en imposant les non-résidents par référence aux revenus générés sur le territoire portugais. En outre, la déductibilité des dépenses attribuables à un établissement stable ne dépend pas du fait que sa contrepartie est un résident. En règle générale, les résidents d'autres États membres de l'UE ne sont pas soumis à des dispositions moins favorables que celles qui s'appliquent aux résidents dans des conditions similaires. Le Portugal a éliminé progressivement un certain nombre de situations allant dans le sens contraire qui survivaient jusqu'ici.

Le système fiscal portugais est conforme aux directives de l'OCDE, est imprégné des principes du droit communautaire et accepte la règle de la non-discrimination.

Zusammenfassung

Portugal zählt zu den Investitions-"Importeuren", die Unternehmensstruktur des Landes setzt sich im Wesentlichen aus kleinen und mittleren Betrieben zusammen, die aufgrund ihrer Struktur und Grösse kein Interesse an Globalisierung haben. Die Grundsätze im

OECD-Musterabkommen wurden in Doppelbesteuerungsabkommen übernommen in dem Bemühen, darin die sozio-ökonomische Realität widerzuspiegeln und in gewisser Weise die Steuerbefugnis, die den Quellenländern zugestanden wurde, zu fördern. Dies wird vor allem durch die Erweiterung der Konzepte erreicht. Portugal hat der Verhandlung von Abkommen mit EU- und OECD-Mitgliedstaaten Vorrang eingeräumt sowie mit den Staaten, die Portugiesisch als Amtssprache pflegen, obwohl es bis heute noch kein Abkommen mit Angola, Sao Tome und Principe sowie Guinea-Bissau gibt.

In Portugal ansässige Personen werden mit ihrem Welteinkommen besteuert – unabhängig von der Quelle – und Nichtansässige werden mit dem Einkommen besteuert, das im Inland erworben wurde oder als solches betrachtet wird. Das portugiesische Steuerrecht begründet das Prinzip der Nichtdiskriminierung, es sei denn im Fall der besonderen Regeln gegen Missbrauch, durch Besteuerung von Nichtansässigen unter Bezugnahme auf den Teil des Einkommens, der auf portugiesischem Boden verdient wird. Ausserdem ist die Abzugsfähigkeit von Kosten, die einer ständigen Niederlassung zugeordnet werden können, nicht abhängig ist von der Ansässigkeit der zugehörigen Gesellschaft. In der Regel gelten für Ansässige eines anderen EU-Mitgliedstaats keine weniger günstigen Vorschriften als für Ansässige unter vergleichbaren Umständen. Portugal hat schrittweise eine Reihe von noch bestehenden Rechtslagen geregelt.

Das portugiesische Steuerrecht steht im Einklang mit den OECD-Richtlinien, integriert Gemeinschaftsrecht und achtet auf Nichtdiskriminierung.

Resumen

Portugal es "importador" de inversiones, con un tejido económico constituido por pequeñas y medianas empresas que, por su estructura o tamaño, no buscan la internacionalización. Los convenios de doble imposición siguen las directrices del modelo de convenio de la OCDE para reflejar la realidad socioeconómica y promover, en cierta medida, la potestad tributaria del país de la fuente, propósito que se alcanza fundamentalmente por la ampliación de los conceptos. Portugal ha dado preferencia a la negociación de convenios con los Estados miembros de la UE, de la OCDE y de habla portuguesa (aunque todavía no se han concluido los CDI con Angola, Santo Tomé y Príncipe y Guinea-Bissau).

Los residentes tributan en Portugal por su renta mundial – independientemente de la fuente – y los no residentes por su renta de fuente interna. La legislación fiscal portuguesa establece el principio de no discriminación – excepción hecha de las normas específicas de lucha contra los abusos – en la imposición sobre las rentas de no residentes generadas en territorio portugués. Además, la deducibilidad de los gastos imputables a un establecimiento permanente no depende de que su contraparte sea residente. Los residentes de otros Estados miembros de la UE no están sujetos, en general, a disposiciones menos favorables que las que se aplican a los residentes en condiciones similares. Portugal ha eliminado progresivamente algunas situaciones que iban en sentido contrario y que permanecían vigentes hasta ahora.

El sistema tributario portugués se conforma a las directrices de la OCDE, viene informado por los principios del derecho comunitario y acepta la norma de no discriminación.