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Portuguese Companies **Corporate Taxation**

Synopsis

Investment and business in Portugal are usually conducted through the incorporation of a company, in order to benefit from limited liability.

Company Law is the backbone of modern business and is still a fast-moving field. In Portugal, new legislation is spurred by E.U's policy harmonization agenda and the private sector's pressure for company law to be consistent with the realities of business.

Basic understanding of Corporate Law is an unavoidable reality for every business, regardless of the industry specificities.

This document provides an overview of the different types of Portuguese companies and the Corporate Income Tax system.

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Introduction

In Portugal, a comprehensive set of legal provisions governs all aspects of corporate activity, providing for matters such as how companies are formed and governed, how the limitation of members' liability is to be regulated, how a company's directors are expected to act and report to shareholders, and how companies should record their performance in accounting terms.

Portugal has made significant efforts to re-think and adjust its company law framework considering the internationalisation of business and is up to date with modern business practices.

Portuguese companies have direct access to all European Union laws and regulations, such as Directives and Regulations.

Both resident and non-resident individuals or companies can incorporate a company in Portugal. There are no restrictions on the entry or repatriation of foreign capital.

A local partner is not required for any purposes and special registration or notification of Authorities is not required in relation to foreign investment. However, mandatory registration or licensing is required for specific activities.

There are no restrictions on commercial or business relations with certain countries or jurisdictions, but Portugal has strict regulations to combat Money Laundering and Terrorism Financing.

Portuguese companies have access to an extensive Tax Treaty network and Tax and Social Security benefits such as:

- Participation Exemption Regime: Tax exemption on inbound and outbound dividends and capital gains derived from qualifying shareholdings
- IP Box: Partial tax exemption on income derived from the sale or temporary licensing of industrial property rights such as industrial drawings, models, or patents
- Contractual regime benefits for investment projects: Tax credit applicable to projects considered strategic for the national economy, projects that reduce regional asymmetries, or technological and scientific research projects
- Municipal tax benefits for the refurbishment of real estate
- Job creation benefits and grants
- Credits to avoid international double taxation
- Tax benefits applicable to reinvested earnings
- Benefits applicable to shipping companies of the merchant navy

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Portuguese Companies

Companies with head office in Portugal will be regulated by Portuguese Law.

In some instances, companies with their head office abroad but carrying out business activities in Portugal on a permanent basis must establish a permanent establishment in Portugal.

Types of companies

The types of companies most frequently adopted in Portugal are Private Limited Quota Companies, Sole Quotaholder Companies, and Joint-Stock Companies.

Private Limited Quota Company (“Sociedade por Quotas”) is the most common, simple and financially-sound solution for small to medium enterprises, since they are not subject to any minimum share capital requirement. It requires two quotaholders to be incorporated. Share capital is represented by and divided into quotas.

A Sole Quota Holder Company (“Sociedade Unipessoal por Quotas”) is incorporated at the outset by a single quotaholder and for that reason is not suitable for joint ventures.

The incorporation of a Joint-Stock Company (“Sociedade Anónima”) requires five shareholders or, in certain cases, one corporate shareholder. The minimum share capital of EUR 50.000 is divided into shares and makes it a suitable equity vehicle for larger investments. Bearer shares are not allowed in Portugal.

Usually, the choice between corporate vehicles will depend on the complexity of the project, on the investments involved, and on mandatory legal requirements for particular sectors. Corporate governance aspects may significantly influence business operations.

Private limited quota companies benefit from a lighter governance structure, hence being appropriated for short-term or smaller investments. On the other hand, Joint-stock companies are usually recommended for enduring investments, especially where a large number of investors is foreseen.

Other types of companies available, seldom used, include the General Partnership Company (“Sociedade em Nome Colectivo”) and Limited Co-Partnership Company (“Sociedade em Comandita”). A European Company (*Societas Europaea*) may also be incorporated in Portugal. It requires a registered office or head office in Portugal and operations in other E.U. countries. The minimum share capital is EUR 120.000.

Partnerships

Portuguese legal provisions do not foresee the possibility of Partnerships, except for professional partnerships such as law firms.

Branches

Non-Portuguese companies may set up a branch in Portugal. A branch is a permanent representation (and a permanent establishment) of a foreign company.

A branch is not legally independent from its head office. There are no share capital requirements, but the head office may allocate capital to the branch for operational purposes. Being unincorporated, a branch is not a limited liability entity.

Portuguese branches are a type of permanent establishment. According to Portuguese Corporate Tax rules, permanent establishments are liable to Corporate Tax on worldwide profits and must have organized accounts under Portuguese rules.

Passporting

Passporting applies to Portuguese companies.

Companies established in any European Economic Area (EEA) Member State have access to the single market for financial services under single passport rights. A Portuguese company licensed in Portugal is therefore authorized to provide financial services across the EEA without the need for further licensing.

Other aspects

The company name must reflect the company's activities and should not be misleading as regards the identification of shareholders, nor should it be subject to confusion with another previously registered name. A corporate name must not include forbidden expressions or expressions contrary to the principle of good morals. The principle of exclusivity will protect the corporate name in Portugal.

The disposal of shares is not subject to restrictions unless provided for in the by-laws. The disposal of quotas is generally subject to the company's approval unless otherwise established in the articles of incorporation. Further limitations may be included in the by-laws for Private Limited Quota Companies.

For a company to commence business activities, registration with the Tax Authorities and Social Security Authorities, and the appointment of a Portuguese accountant are required.

Corporate Income Tax

Joint-Stock Companies and Private Limited Quota Companies are taxed according to similar rules. Both types of companies are treated as separate entities from their shareholders and quotaholders unless they are transparent entities (pass-through) for tax purposes.

The tax transparency regime applies to certain family-owned personal asset management companies, to certain professional services firms, and to certain joint venture entities.

Scope of taxation

Corporate tax residency is enforced on entities with registered headquarters or place of effective management in Portugal.

Portuguese companies are taxed on profits generated worldwide.

For Portuguese Corporate Income Tax (“CIT”) purposes, taxable profits are determined according to accrual accounting rules governing Profits and Losses (“P&L”) in addition to the net variation in equity not reflected in the P&L statement. Portuguese GAAP financial statements must be prepared annually.

There are other adjustments introduced by the Tax Code, mainly regarding non-cash expenses, depreciation, losses, transfer pricing, undocumented expenses, bad debts, amongst others.

Corporate Income Tax is assessed over a period equal to one financial year, which generally matches the calendar year. However, a financial year other than the calendar year can be adopted.

Exceptions apply to certain types of income under specific tax incentives programs, and dividends or capital gains on the disposal of shareholdings under the participation exemption regime.

Portuguese companies are liable to CIT on profits, at a 21% rate. SMEs may benefit from a tax of 17% up to EUR 50.000 of taxable income.

Treaties to Avoid Double Taxation

Portuguese companies benefit from an extensive Tax Treaty network with the following countries:

Algeria, Andorra, Angola, Austria, Bahrain, Barbados, Belgium, Brazil, Bulgaria, Canada, Cape Verde, Chile, China, Colombia, Croatia, Cuba, Cyprus, Czech Republic, Denmark, East Timor, Estonia, Ethiopia, France, Georgia, Germany, Greece, Guinea Bissau, Hong Kong, Hungary, Iceland, India, Indonesia, Ireland, Israel, Italy, Ivory Coast, Japan, Korea, Kuwait, Latvia, Lithuania, Luxembourg, Macao, Malta, Mexico, Morocco, Mozambique, Netherlands, Norway, Pakistan, Panama, Peru, Poland, Qatar, Republic of Moldova, Republic of Uruguay, Romania, Russia, San Marino, São Tome and Principe, Saudi Arabia, Senegal, Singapore, Slovak Republic, Slovenia, South Africa, Spain, Sultanate of Oman, Switzerland, Tunisia, Turkey, Ukraine, United Arab Emirates, United Kingdom, United States of America, Venezuela, Vietnam.

Participation Exemption Regime

The Portuguese participation exemption regime allows international enterprises to avoid double taxation of dividends and capital gains arising from the disposal of both foreign and Portuguese shareholdings.

Portuguese companies are exempt from corporate income tax on inbound dividends and capital gains and foreign corporate shareholders are exempt from withholding tax on dividends provided certain conditions are met.

This regime puts Portugal on the map as a privileged jurisdiction for companies to do business and invest worldwide in a tax-efficient manner.

Inbound transactions

Dividends

Dividends derived from qualified shareholdings in companies located in non-blacklisted jurisdictions will not be liable to Corporate Income Tax in Portugal.

A qualified shareholding requires a 10% direct or indirect shareholding (or voting rights) by a Portuguese Parent Company in a foreign subsidiary held for a minimum 12-month period.

The foreign subsidiary's profits must be liable and not exempt from a type of Corporate Income Tax listed in Directive 2011/96/EU or taxed at a minimum rate of 12.6%.

If the participation exemption is not applicable due to the non-fulfillment of one of the aforesaid requirements, the Portuguese company may still be entitled to a tax credit for the underlying tax paid by eligible direct or indirect subsidiaries or a tax credit for double taxation due to tax being withheld on dividends. Intra community payment of dividends is also regulated by the Parent-Subsidiary Directive.

Domestic payments of dividends are tax-exempt provided a 5% shareholding is held for one year prior to the payment of dividends.

Permanent establishments

The exemption regime is also applicable (and optional) to profits and losses attributable to foreign permanent establishments of Portuguese companies. Therefore, Portuguese companies are entitled to exclude from taxation profits and losses in foreign PE. Some restrictions may apply.

Capital Gains

Capital gains derived from the sale of foreign qualified shareholdings are not taxable in Portugal. The applicability of the participation exemption regime to capital gains may be limited by anti-abuse provisions, namely where the subsidiary owns real estate.

Outbound transactions

Dividends

Dividends paid by Portuguese subsidiaries to foreign Parent companies will not be liable to withholding tax in Portugal if the qualified shareholding requirements are met.

A qualified shareholding requires a 10% direct or indirect shareholding (or voting rights) by a foreign Parent Company in a Portuguese foreign subsidiary. The qualified shareholding must also be held for a minimum 12-month period.

The Parent Company must be tax resident in an E.U. jurisdiction or in a country with which Portugal has entered into a Double Taxation Agreement.

The following additional requirements must also be met:

- The nonresident corporate shareholder must be liable and not exempt from a type of Corporate Income Tax as listed in Directive 2011/96/EU or taxed at a minimum rate of 12.6%; and
- The applicable Double Tax Treaty provides for an administrative cooperation mechanism regarding taxation similar to the E.U. system.

Intra community payment of dividends is also regulated by the Parent-Subsidiary Directive.

Domestic payments of dividends are tax-exempt provided a 5% shareholding is held for one year prior to the payment of dividends.

Permanent establishments

As a rule, after-tax repatriation of profits by Portuguese permanent establishments is not liable to withholding tax in Portugal.

Capital Gains

Capital gains derived from the sale of Portuguese shareholdings are not liable to corporate tax in Portugal, provided corporate shareholders are not located in a blacklisted jurisdiction.

The exemption does not apply if the participated company owns real estate properties in Portugal accounting for more than 50% of the total value of the company's assets. This exception does not apply in the event these properties are used in an agricultural, industrial, or commercial activity.

About GFDL

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