Doing Business in Portugal

This document describes some of the key commercial and taxation factors that are relevant on setting up a business in Portugal.

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Background

Country overview

Portugal is the most western European country with a land border with Spain. Having been a full member of the European Union (EU) since 1986, Portugal **is now one of the fully-fledged members of** the European Monetary Union (EMU).

Its population is now approximately 10.5 **million people and the official language is** Portuguese. However, English is spoken by most of the people and is also widely used in business.

Portugal is an independent and sovereign republic. The legislative power lies with the Parliament and its members serve a four-year term.

The country has historical and close relations with old colonies, especially Brazil, Angola and Mozambique.

Economic overview

Portugal's open economy, strong ties with the European Union, and strategic geographic location, make it an excellent country for foreign investors.

Small and medium size companies employ most of the Portuguese workforce and they have a strong weight in economy. The most important industries are fabrication of transport equipment, textiles and clothing, footwear, electrical equipment, manufacturing, and mechanical engineering. The key sector of the economy is tourism; major tourist centres are Lisbon, Algarve and Madeira.

Portugal has a considerably skilled labour force, with an unemployment rate of around 11%, and low labour costs compared with other European Union countries.

Transport infrastructure

Portugal has invested in modernizing its communications infrastructure. The result is an impressive network of modern roads and highways, crossing all major cities in the country, with rapid access to Spain, and air and maritime route facilities.

Choice of Legal Form

Limited liability company

The Limited Liability Company is the form most frequently adopted by small and medium sized businesses. Share capital is divided into shares (quotas) whose holders are jointly liable for paying the company capital and liable for the total amount of share equity. The word 'Limitada' or 'Lda' must be in the name of the company.

The company needs a minimum of two shareholders, a minimum capital of 1.00 (one) Euro per quota, and the management is attributed to one or more directors, who must be private individuals. Creditors can claim only against the company share capital.

Limited Liability Companies can be transformed into Individual Stakeholder Companies ("Unipessoal") by concentrating all the capital shares in a single shareholder.

Holding company ("SGPS")

Holding Company activities are confined to owning stock in, and supervising management of, other companies. A Holding Company is also allowed to render management services to controlled companies (representing more than 10% of their capital).

Holding companies must be audited by a statutory/external auditor.

General partnership

General Partnership companies are rare in Portugal. These companies bear unlimited liability for company debt.

Branch / Representative office

A branch is not a separate legal entity distinct from its parent. A non-resident company that intends to carry on an activity in Portugal for more than six months must register a permanent **representative office; there are no formal** restrictions on operating a branch of a foreign company in Portugal. The formalities for establishing a branch requires the appointment of a local manager with the power to represent the **company, the filing of an application for a name, and the verification of the parent** company's incorporation documents.

Offshore legal entities

The Madeira Government has a degree of autonomy from Portugal, yet obeys Portuguese legislation. As a Free Trade Zone, Madeira has a special corporate tax regime, applicable to industrial, **commercial and financial activities.**

Companies are subject to a Corporate Tax rate of 5%, on operations with non- residents in Portugal, under certain conditions.

The offshore regime follows EU rules and may take advantage of EU directives and Tax Treaties honoured by the Portuguese Republic.

Subsidiary

A subsidiary depends upon another company, either in terms of that company being the holder of shares in the subsidiary, or through any contractual **links. A subsidiary is a different legal** entity from the parent company with all the implications of having a true and separated liability from the parent. Usually, it is established under the format of a Limited Liability Company or a Public Limited Company.

Public limited company

In a Public Limited Company ("S.A.") the capital is divided into shares; each shareholder's liability is limited to value of shares to which they subscribe.

The main characteristics of this kind of company are:

- The existence of at least 5 shareholders;
- A minimum amount of capital share of 50,000 Euros, divided into shares with a minimum value of 0.01 Euro per share;
- Up to a maximum 70% of share capital **is payable within five years and the** remaining 30% must be paid up when the company is incorporated.

Public limited companies must be audited by a statutory/external auditor.

Joint venture

The most common form of joint venture is the jointly owned company or equity- joint venture. This requires two or more partners to participate in the share capital of a new company to be incorporated, or, in a pre-existing company, the setting up of local holding company.

The contractual joint venture or consortium is a form of joint venture without the need for incorporating a company. This may entail tax advantages, as the tax authorities exert less control over this type of venture than an equity- joint venture.

Another contractual joint venture is "Agrupamento Complementar de Empresas - ACE" which is popular among civil construction consortia for large projects, and the investors are not required to be European Union residents.

Trust

Trusts do not exist in Portuguese law. Nonetheless, the Madeira Free Trade **Zone allows the establishment of offshore** trust companies, if the proprietary is non- resident in Portugal and their income is derived from outside the country.

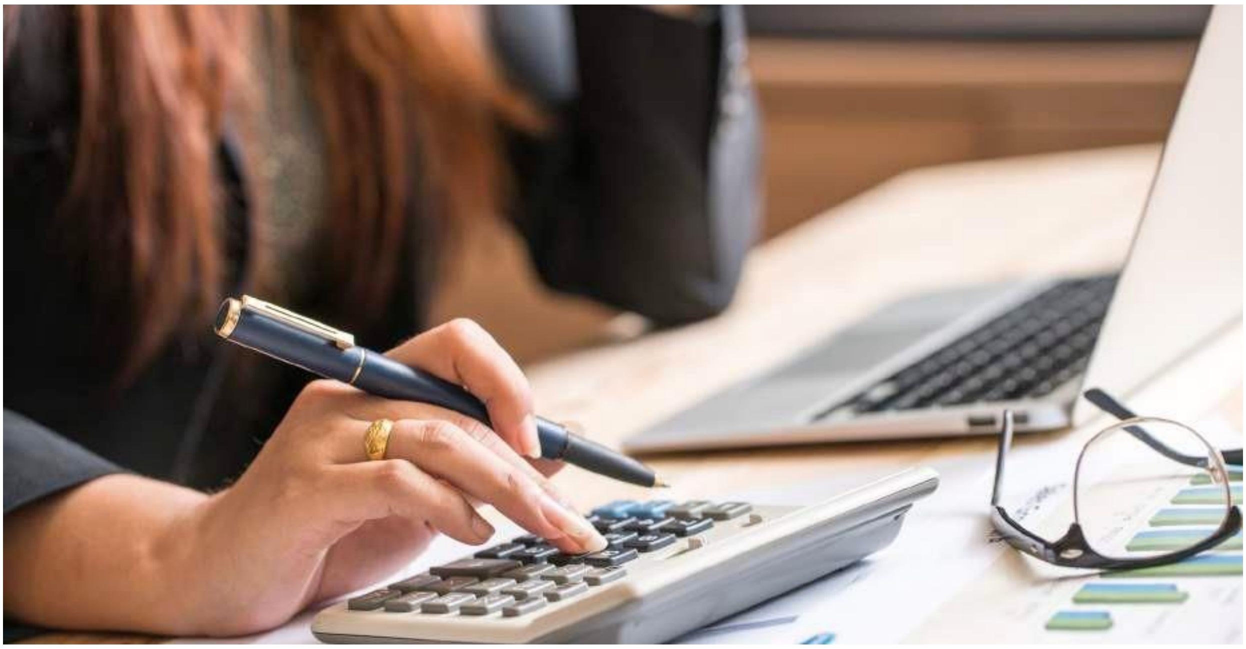
Audit Requirements

Requirement and thresholds

The following companies are required to have a statutory annual audit:

- Holding Companies (SGPS);
- Public Limited Companies (S.A.)
- Limited Liability Companies (Lda.) if exceeding 2 of the following 3 limits in 2 successive years:
  - Total assets of 1.5 million Euros
  - Total turnover of 3 million Euros
  - Average of 50 employees/year

Taxation



Corporate income tax (IRC)

The taxable profits of most small companies are charged as follows:

- **The first 15.000 Euros of profits are** charged at 17%
- **Profits over 15.000 Euros are charged** at 21%
- **Profits over 1.500.000 Euros and not** exceeding 7.500.000 Euros are charged at a marginal rate of 3% (“Derrama Estadual”).
- **Profits over 7.500.000 Euros and** not exceeding 35.000.000 Euros are charged at a marginal rate of 5% (“Derrama Estadual”).
- **Profits over 35.000.000 Euros are** charged at a marginal rate of 7% (“Derrama Estadual”).
- A Municipal surcharge (“Derrama”) may be levied on corporate tax (IRC), at a **maximal rate of 1.5% of taxable profit.**

Companies licensed to operate in Madeira Free Trade Zone are subject to a 5% rate **of taxation on profits (as explained under Offshore Legal Entities).**

Tax losses generated from 1 January 2017 onwards can be carried forward for a 5-year period. Companies that are considered as micro, small or medium companies (so called “PME”) and are agricultural, commercial or industrial, may carry forward their tax losses for 12 years. Deduction of carry forward tax losses is **capped at 70% of the taxable profit.**

Companies with head offices or effective management located in Portugal are subject to pay tax on income.

Branches and permanent establishments are only liable to pay tax on income and capital gains attributed to that branch or permanent establishment.

Companies that do not have their head **offices, effective place of management, or** permanent establishment in Portugal are only subject to pay tax on income earned in Portugal.

Personal income tax (IRS)

Personal Income Tax is levied on income earned by individuals residing in Portugal as well on the income obtained in Portugal by non-resident individuals.

The resident individuals in Portugal are taxed by progressive tax rates, according to table below:

Mainland - Portugal		Madeira		Azores	
Income (€)	Tax Rate	Income (€)	Tax Rate	Income (€)	Tax Rate
0 – 7,091	14.5%	0 – 7,091	12.41%	0 – 7,091	10.15%
7,091 – 20,261	28.5%	7,091 – 20,261	28.5%	7,091 – 20,261	21.38%
20,261 – 40,552	37%	20,261 – 40,552	37%	20,261 – 40,552	29.60%
40,552 – 80,640	45%	40,552 – 80,640	45%	40,552 – 80,640	36%
Above 80.640	48%	Above 80.640	48%	Above 80.640	38.4%

An extraordinary surtax will be applicable to income earned in 2017, according to the following table:

Taxable Income	Tax Rate
More than Eur 20.261 and up to Eur 40.522	0,88%
More than Eur 40.522 and up to Eur 80.640	2,75%
More than Eur 80.640	3%

Additionally, solidarity rate is applicable on income exceeding Euros 80,000, subject to the marginal tax rates. A rate of 2.5% is applicable to taxpayers with a taxable income exceeding €80,000 up to €250,000 and a rate of 5% is applicable to taxable income exceeding €250,000.

There is a special regime for Non-Habitual Residents:

The regime will apply to individual taxpayers who become Portuguese tax residents, under Portuguese domestic law, provided they have not been taxed as tax residents in Portugal in any of the previous **five years. In these circumstances,** individuals will be considered as non- habitual residents upon their registration as such with the tax authorities.

The employment and self-employment income (net of expenses) obtained in "high **value-added activities" is taxed at a flat** rate of 20%.

Foreign-source income (e.g. pensions) may be exempt, under certain conditions.

The regime is applicable for a period of ten consecutive years.

Capital gains tax

The capital gains arising from the disposal of shares are tax free if obtained by non-residents.

This exemption is not valid if:

- The assets of the company whose shares are being disposed are composed more than 50% by real estate located in Portugal;
- The seller is resident in a tax heaven.

If the above-mentioned exemption is not applicable, the capital gains from the disposal of shares are charged at the rate of:

- 14% for shares of micro and small companies;
- 28% for shares of other companies.

The gains arising from the disposal of property are charged at the rate of 25% for non-residents.

Value added tax (VAT)

VAT is an indirect tax, payable by suppliers of goods and services, who charge it in every supply they make within their respective activities, and afterwards pay the respective amount to the Tax Authorities.

Rate	Portugal (Mainland)	Azores	Madeira
Reduced	6%	4%	5%
Intermediate	13%	9%	12%
Standard	23%	18%	22%

The taxpayer has the right to deduct the value of the VAT payment when acquiring a product for which the seller has already paid VAT.

Local taxes

Municipal surcharge

The municipal surcharge ("Derrama") is a municipal tax, the revenue goes to the local municipality. The municipal surcharge may amount to up to 1,5% of **taxable profit.**

Property transfer tax (IMT - Imposto Municipal sobre a Transmissão Onerosa de Imóveis)

The Property Transfer Tax is a municipal tax which relates to the transmission of real property on Portuguese territory. Please note that these transmissions can be subject to stamp tax.

The acquisition of more than 75% of the share capital ("sociedades por quotas") which owns real estate located in Portugal, is also subject to IMT (as well as of a privately placed closed-end Real Estate Investment Funds).

Description	Tax Rate
Other urban properties and other acquisitions	6.5%
Acquirer is a tax resident **offshore (except individuals)**	10%

Property tax (IMI – Imposto Municipal de Imóveis)

The Property Tax is a tax calculated based on registration value of urban and rural properties located in Portuguese territory.

This tax is due with on the 31st December of the year that it concerns.

The registration value is determined by valuation, based on the type of property.

Property	Tax Rate
Urban property	0.3% to 0.45%
Rural property	0.8%
Property owned by residents **offshore (except individuals)**	7.5%

Taxes additional to the IMI (AIMI)

The AIMI is due by individuals and companies, as well as by structures or collective bodies without autonomous legal personality and undivided inheritances, that are owners, usufructuaries, or have the surface right of urban properties located in Portugal.

Urban Properties classified as "Housing" and "Construction Land" are subject to AIMI (except those which are exempt or have not been subject to IMI taxation in previous years).

Urban properties classified as "trade, industry, or services", "others" and "Rustic properties" are not subject to AIMI.

The taxable amount corresponds to the sum of the Tax Registration Value (TRV) of all the urban properties held by each taxpayer, as reported on 1st of January each year.

For individuals and undivided inheritances, a deduction of EUR 600,000 is available from the taxable amount on the sum of the TRV of the buildings owned by them (or EUR 1,200,000 in the case of taxable persons who are married or in a joint-stock association who opt for joint taxation). For the properties exceeding this TRV, the rates to be applied will be 0.7% for TRV between 600,000 euros and 1,000,000 euros and 1.0% for what exceeds a TRV of 1,000,000 euros.

For companies, the rate to be applied is 0.4% on the TRV of real estate not related to the productive activity to which they are devoted. However, it should be noted that the value of buildings held by companies for the personal use of the owners of their capital, of the members of the governing bodies, or of any administrative, management, or supervisory bodies, or their spouses, ascendants and descendants, is subject to the rate of 0.7%, and is subject to the additional rate of 1.0% for the part of the value that exceeds 1,000,000 euros.

For buildings owned by entities subject to a more favourable tax regime, the rate is 7.5%.

Stamp duty

Stamp duty is due on acts, contracts, documents, titles, books, papers and other facts foreseen in the General Table, which occur in Portugal and are not subject or exempt from VAT.

Transactions subject to VAT are exempt from Stamp Duty, but in the documents involved in the transaction, the duty is paid.

Tax treaties

Portugal has signed double taxation agreements with 79 jurisdictions (until 24th April 2017), 76 in force and 3 signed but not yet in force. In addition, double tax treaties grant an exemption or a reduced rate of tax on certain receipts, such as interest, royalties, dividends, capital gains, and others in transactions carried out between parties associated. See Appendix I.

Transfer pricing

Commercial transactions between associated enterprises should be subject to identical terms and conditions to those that would be accepted and agreed between independent entities (arm's length principle).

Taxpayers whose net sales and other operating incomes exceed EUR 3.000.000,00 in the previous year must prepare and maintain an annual transfer **pricing documentation file, which must be** prepared by the 15th day of the seventh month following the end of the tax year. **The transfer pricing documentation file** must be submitted upon request.

According to the Portuguese legislation, the documentation must be provided in Portuguese.

Allowances

Depreciation

Depreciation is provided on all fixed assets except land to write off the value of the asset over its useful life.

The rates of depreciation are defined by legislation for each category of asset and are tax deductible.

Employment

Social security contributions

Contributions to Social Security are compulsory for both employees (11%) and employers (23.75%) as well as for self-employed individuals (34.75%).

Members of the management of Portuguese companies are automatically liable to pay Social Security based on the income received, regardless of whether they are resident in Portugal.

Members of the management of Portuguese companies may be resident anywhere in the world; they may avoid the Social Security liability in Portugal by providing proof of their registration to, and payment of, social security in their country of residence.

Employment of foreign personnel

Non-EU personnel intending to work in Portugal must apply for a work visa before entering in national territory. Foreign workers provided with all authorizations to work in national territory, have the same rights as domestic workers in Portuguese labour laws.

Medical

The contributions for the health/medical system are, like social security, deducted from employee income.

Withholding Taxes

The main corporate withholding tax rates are in table below:

Income	Tax Rates	
	Resident	Non-Residents
Royalties	25%	25%
Technical Assistance	-	25%
Interests of bank deposits	25%	25%
Dividends	25%	25%
Agency fees and other services	-	25%
Rental income	25%	25%

Please see appendix 1 for a table of Withholding tax rates for income paid from Portugal to countries that have Double Taxation Agreements.

Appendix 1, Double Taxation Treaties

	Rate (%)		
Country	Dividends	Interest	Royalties
Algeria	15/10	15	10
Austria	15	10	10/5
Barbados*	15/5	10	5
Belgium (Aditional convention)	15	15	10
Brazil	15/10	15	15
Bulgaria	15/10	10	10
Canada	15/10	10	10
Cape Verde	10	10	10
Chile	15/10	15/10/5	10/5
China	10	10	10
Colombia	10	10	10
Croatia	10/5	10	10
Cuba	10/5	10	5
Cyprus	10	10	10
Czech Republic	15/10	10	10
Denmark	10	10	10
East Timor*	10/5	10	10
Estonia	10	10	10
Ethiopia*	10/5	10	5
Finland	15/10	15	10
France	15	12/10	5
Georgia	10/5	10	10
Germany	15	10	10
Greece	15	15	10
Guinea-Bissau	10	10	10
Holland	10	10	10
Hong Kong	10/5	10	5
Hungary	15/5	10	10

	Rate (%)		
Country	Dividends	Interest	Royalties
Iceland	15/10	10	10
India	15/10	10	10
Indonesia	10	10	10
Ireland (Protocol revising the Convention)	15	15	10
Israel	15/10/5	10	10
Italy	15	15	12
Ivory Coast*	10	10	5
Japan	10/5	10/5	5
Kingdom of Bahrain*	15/10	10	5
Korea	15/10	15	10
Kuwait	10/5	10	10
Latvia	10	10	10
Lithuania	10	10	10
Luxembourg (Additional convention)	15	15/10	10
Macau	10	10	10
Malta	15/10	10	10
Mexico	10	10	10
Moldova	10/5	10	8
Morocco	15/10	12	10
Mozambique (Protocol revising the Convention)	10	10	10
Norway	15/5	10	10
Pakistan	15/10	10	10
Panama	15/10	10	10
Peru	15/10	15/10	15/10
Poland	15/10	10	10
Qatar	10/5	10	10
Republic of San Marino*	15/10	10	10
Republic of Senegal	10/5	10	10

	Rate (%)		
Country	Dividends	Interest	Royalties
Romania	15/10	10	10
Russia	15/10	10	10
São Tomé and Príncipe*	15/10	10	10
Saudi Arabia	10/5	10	8
Singapore (Protocol revising the Convention)	10	10	10
Slovakia	15/10	10	10
Slovenia	15/5	10	5
South Africa	15/10	10	10
Spain	15/10	15	5
Sultanate of Oman*	15/10/5	10	8
Sweden	10	10	10
Switzerland (Protocol revising the Convention)	15/5	10	5
Tunisia	15	15	10
Turkey	15/5	15/10	10
United Arab Emirates	15/5	10	5
United States of America	15/5	10	10
United Kingdom	15/10	10	5
Ukraine	15/10	10	10
Uruguay	10/5	10	10
Venezuela	10	10	12/10
Viet Nam*	15/10/5	10	10 / 7.5

* Not yet enacted

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If you are setting up a business in Portugal, the members of DFK International can **help you to achieve this efficiently. You will** receive practical advice on businessissues, tailored to meet your objectives, from experienced business advisers.

For further information on the services **available from the DFK member firms in** Portugal please see overleaf.

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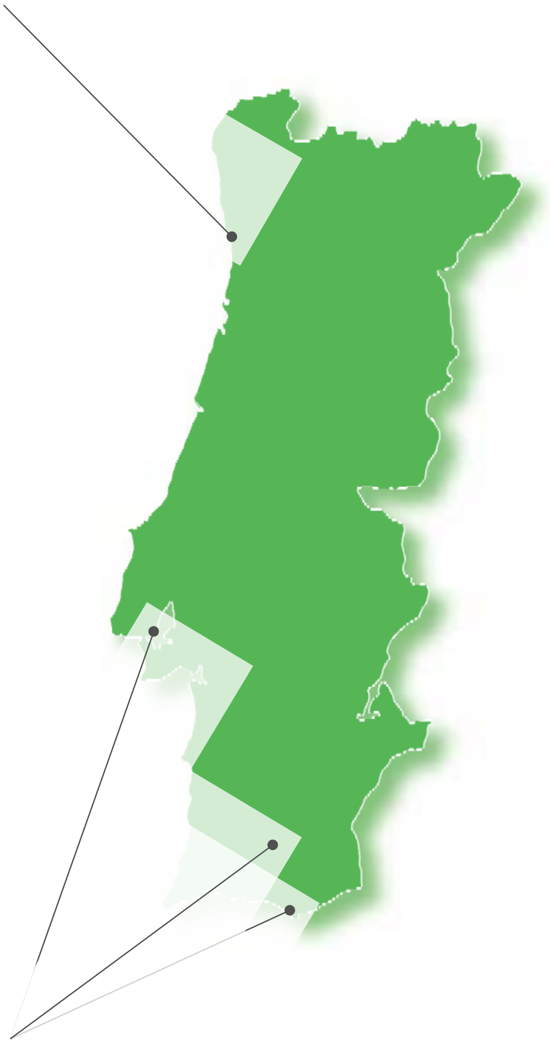

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