18 May 2020

Global Tax Alert

Portugal requested by European Commission to amend legislation transposing the Anti-Tax Avoidance Directive

Executive summary

On 14 May 2020, the European Commission (the Commission) sent a letter of formal notice to Portugal requesting Portugal to adjust its internal law to be in line with the interest limitation rule set forth under the European Union (EU) Anti-Tax Avoidance Directive (ATAD) – Article 4 of the Council Directive (EU) 2016/1164.

Detailed discussion

The ATAD was presented by the Commission as part of the Anti-Tax Avoidance package in January 2016, to provide a coordinated implementation across the EU of a specific set of anti-tax avoidance provisions, namely, interest deduction limitation rules, controlled foreign corporation rules, hybrid mismatches rules, exit taxation rules and the general anti-abuse rule.

With respect to interest deduction limitation rules, the Portuguese Corporate Income Tax (CIT) Code already provided a rule under which the deduction of net financing expenses is capped by the higher of either (i) 30% of the tax EBITDA; and (ii) €1 million.

To comply with the ATAD's text, Law n. 32/2019, of 3 May 2019 introduced some amendments and/or clarifications to the former provision mainly regarding the concepts of:

- "Financing expenses" in order to include, among other topics, the depreciation of the borrowing costs that are capitalized in the acquisition cost of assets.
- "Tax EBITDA," which now corresponds to the taxable profit (or tax loss) subject to and not exempt from CIT, adjusted by the net financing expenses, the depreciation and the amortization amounts that are tax deductible.

Furthermore, Portugal opted to exclude the entities under supervision of the Bank of Portugal and the Supervisory Authority for insurance and pension funds (*Autoridade de Supervisão de Seguros e Fundos de Pensões*), Portuguese branches of credit institutions and other financial institutions or insurance companies and securitization companies incorporated under Decree-Law 453/99, of 5 November 1999 (already included in the previous version).

Nevertheless, the ATAD's wording only allows for financial undertakings to be excluded from the interest deduction limitation rules and thus the Commission considers that the Portuguese tax law should be amended in order for this limitation to apply to entities that cannot be qualified as financial undertakings (namely, securitization entities).

According to the information made public, if Portugal does not act within the next four months, the Commission may send a reasoned opinion to the Portuguese authorities.

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