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PORTUGAL

RATIFICATION OF ARBITRATION EEC/90/436 CONVENTION

The Convention regarding the elimination of double taxation in case of correction of profits between associated companies was ratified on 28 October 1994. This was notified in the *Diário da República* on 17 January 1995 and came into effect on 1 January.

1. *Anti-abuse clauses*

Concern about the increase in tax avoidance and tax fraud arising from the internationalization of companies and the greater mobility of factors led to Portugal introducing some special anti-abuse clauses this year. These already exist in other Member States such as Germany and are also reflected in community fiscal law. Thus, the deduction of sums paid or owned by companies, (subject to tax on income - IRC) to individuals or companies resident outside Portuguese territory, but resident within the territory of a Member State and subject in that state to a 'clearly more favourable system' (one in which the tax on income is under 20 per cent), for the determination of taxable profits can only be achieved through proof by the company liable to tax that these sums are for 'genuine operations carried out' and that 'are not of an abnormal nature nor for an excessive amount.'

In the absence of a harmonized community system on this matter, the norm applies to sums paid to individuals or companies resident in Member States whose level of tax on income is under 20 per cent.

Another clause establishes that the profits of companies based in states with a 'clearly more favourable system' (one in which the tax on income is under 20 per cent) are directly attributed to partners resident in Portugal, provided that the partner directly or indirectly has a minimum holding of 25 per cent or of at least 10 per cent if over 50 per cent of the non-resident company is directly or indirectly held by resident partners.

This attribution to the partners is, however, waived when, due to the nature of the activity in question, it is assumed that there is a genuine link to the source state which justifies taxation in that country, without any

direct effect on the territory where the partners are resident. That is to say, when due to the nature of the activity in question, it is assumed there is no tax avoidance:

- (a) When at least 75 per cent of the profits in question derive from agriculture or industry in the territory where they are located or from commercial activity which does not involve residents in Portugal, or which, if it does involve them, is oriented towards the market in the territory where they are located; and
- (b) the main activity of the non-resident company does not involve banking operations, nor certain operations in insurance (when the income derives mainly from insurance of goods located outside the land of residence of the company or from insurance of people who are not resident in that territory), nor operations in financial assets, intellectual or industrial property rights, the supply of information on experience acquired in industry, commerce or science or supplying technical assistance, nor the leasing of real estate provided it is not located in the territory in question.

The relevance of these clauses for community law related to cases where income tax of a Member State of the European Union is lower than 20 per cent. This raises the question of relations between internal law and the directives which have been approved.

Although no aspect regarding the tax system for individuals resident in Member States has been harmonized as yet, the question is whether the harmonization deriving from EEC/90/435 Directive does not preclude the possibility of a direct attribution to partners resident in one Member State of the taxable profits of a company resident in another Member State. According to Parent/subsidiary Directive, in effect in Portugal since 1 January 1992 (Article 45, Nos. 1 and 3 CIRC) profits from an affiliated company resident in another Member State and whose parent company resides in Portugal will only be taxed when the source state pays them to the parent-company (this deferred taxation already was the result of the unilateral system). These profits benefit from credit related to the tax already paid at source: deduction of 95% of the income included in the tax base.

As the state where the parent company resides can only tax the profits of the affiliate when they have been paid, the partners of the parent company can only be taxed when dividends are paid. This arises as the deferred taxation system has the same basis for companies (such as parent companies or associated companies) which are resident or not in the same state as for individuals (partners): due to the legal status of the company, the payment of profits to the parent company or the partners for the purposes of taxation is only valid once the profits are paid.

Consequently, as the norms introduced into Portuguese legislation were aimed at reducing abuse, it must be asked whether they go against harmonized community law. If the profits of the affiliate are immediately attributed to the partners, they cannot be attributed to the parent company only at the moment of payment, nor the subject to the credit system as established by the Directive. In contrast, they will be liable to economic double taxation. Even if the source state (or state where the affiliate is resident) has a low taxation rate.

Clearly, EEC/90/435 Directive does contain conditions for the introduction of the harmonized system which also act as anti-abuse measures: these state that the parent company should have a minimum holding in the capital of the affiliate (it should not be under 25 per cent), that this should be a direct holding and that it should be held by the parent company for two consecutive years or for two years from the founding of the held company. These premises for the introduction of the community system simultaneously act as anti-abuse measures. Other than this, the directive merely repeats, in another clause, the possible non-application of any norm relating to the harmonized system when the parent company's share in the affiliate is not held for an uninterrupted period of at least two years.

However, there is no general clause which provides for the non-application of the harmonized system in the event of tax avoidance (*abus de droit, fraude alla lege*, substances over form, etc.)

Thus, bearing in mind that there are Member States whose level of taxation on company income are under 20 per cent, and that Member States may, at any time, opt for tax levels under the aforementioned 20 per cent, the question is raised as to whether these special anti-abuse clauses go against community law.

The main aim here is to note the legal changes, rather than to provide a complete answer to questions which might raise doubts about compatibility between internal nation-

al and community law. Suffice it to say that, disregarding the fact that the laws in the different Member States contain similar clauses, if community law in this matter and Directive 90/435/CEE are taken into account, the Court of Justice allows substantial space for the internal control of tax evasion (see, for instance, decision *Daily Mail*, 27 September 1988, Case NO. 81/87, 1988, 5483 ff).

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SPAIN

NEW REGULATIONS ON EXCISE TAXES

In July 1995 a new and complete set of Regulations concerning Excise Taxes has been introduced. The Act 38/1992, 28 December 1992 on Excise Taxes, introduced in Spain a new set of rules concerning these duties in order to comply with EC Directives in this area in relation with the introduction of the internal market. Provisional Excise Duties Regulations were issued by means of the Royal Decree 258/1993, 19 February 1993. These Regulations were uncomplete, (for example, they didn't cover rules covering the Registration Car Tax), they were provisional and insufficient to interpret the complexities and intricacies of the new Excise Taxation area. Also, as a result of several legal changes introduced in the Act 38/1992 from the 1 January 1993, they became outdated. Therefore a new and complete set of Excise Tax Regulations became necessary.

The Royal Decree 1165/1995, 7 July ('Official Gazette' of 28 July), has fortunately achieved this target. Now, the Spanish Tax Administration and taxpayers have a perfect, complete, broad¹ and clear set of Regulations, including the Registration Car Tax. Therefore, the principle of legal security has been achieved.²

IMPLEMENTATION OF SEVENTH VAT DIRECTIVE

Spain has introduced new rules on the special VAT regime for second-hand goods (works of art, collectors' items and antiques), implementing the Seventh VAT Directive, Directive 94/5/EC, 14 February

¹ As an example of this complete and broad picture of the matters covered by the new Regulations, it is worth noting that they have 13 articles.

² The Spanish Constitution puts forth this principle as a general objective for the whole legal structure in its Article 9.3.