

TAX GROUP

TAXATION OF SOLAR PLANTS IN PORTUGAL

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ABOUT US

MACEDO VITORINO WAS ESTABLISHED IN 1996, FOCUSING ITS ACTIVITY ON ADVISING DOMESTIC AND FOREIGN CLIENTS IN SPECIFIC ACTIVITY SECTORS, INCLUDING BANKING, TELECOMMUNICATIONS, ENERGY AND REAL ESTATE AND INFRASTRUCTURE.

Since the incorporation of the firm we have been involved in several high profile transactions in all of the firm's fields of practice, including banking and finance, capital markets, real estate, M&A, complex disputes and corporate restructurings.

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We are mentioned by The European Legal 500 in most of its practice areas, including Banking and Finance, Capital Markets, Project Finance, Corporate and M&A, Tax, Telecoms and Litigation. Our firm is also mentioned by IFLR 1000 in Project Finance, Corporate Finance and Mergers and Acquisitions and by Chambers and Partners in Banking and Finance, Corporate and M&A, TMT, Dispute Resolution and Restructuring and Insolvency.

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- Corporate and acquisition finance
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- Employment
- Foreign investment, mergers & acquisitions and privatisations
- Real estate acquisition and disposal
- Tax

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INTRODUCTION

It is often said that Portugal is the country with the largest number of sunny days in Europe, with more than 300 days of sunshine in a year.

These weather conditions give Portugal the perfect recipe to use solar energy at its full potential. As such, the Portuguese photovoltaic market is experiencing an all-time high at the present moment, thanks to various successful small and large-scale projects.

In addition, the Portuguese Government is committed to a long-term strategy for carbon neutrality by 2050, with the most recent data (January 2021) showing that 71,2 % of the electricity generated in Continental Portugal came from renewable sources.

Solar power currently represents 3.8% of the electricity generated in Portugal mainland, but it is expected that this figure will grow, particularly, thanks to the competitive solar auctions conducted in 2020 and in 2021, with more expected to be launched in the following years.

This study's goal was to determine which taxes are applicable during the construction and the operation phase of solar power plants in Portugal, including national and municipal taxes and fees.

As such, this analysis is focused on Real Estate Taxes, Corporate Income Tax, Value Added Tax and other taxes applicable in the energy sector.

I. REAL ESTATE TAXES

I.1. CONSTRUCTION PHASE

Solar plants may be built over land acquired or leased by the solar plant owner.

The acquisition of the ownership (*direito de propriedade*) or a surface right (*direito de superfície*) over the land will be subject to municipal real estate transfer tax (“**RETT**”) and stamp duty.

RETT rates vary depending on the type of asset:

- Land: 5%; and
- Urban buildings (other than housing) and other onerous acquisitions: 6.5%.

The stamp duty is charged at a rate of 0.8%.

As a rule, RETT and stamp duty will be levied on the acquisition price or the asset tax value, if higher.

The lease of the land is not subject to RETT and is only subject to stamp duty at a rate of 10% over the lease rent.

I.2. OPERATION PHASE

The ownership and surface rights are subject to municipal real estate tax (“**RET**”).

RET is levied on the asset tax value.

RET rates are different depending to the type of real estate asset:

- Urban buildings: 0,3% to 0.45%; and
- Land: 0.8%.

As a rule, the owner or surface right holder must pay RET in May of every year, although it may also be paid in instalments under certain conditions.

If the land is leased, RET will be paid by the owner unless the parties agree otherwise.

2. CORPORATE INCOME TAX

2.1. CONSTRUCTION PHASE

2.1.1. DEDUCTION OF COSTS AND LOSSES

The costs and losses necessary for the generation of the income or gains subject to Corporate Income Tax (“**CIT**”) or for the maintenance of the producing source may be deducted for tax purposes. These include:

- Production or acquisition cost of any goods or services, such as materials used, labour, energy and other general manufacturing, maintenance and repair costs; and
- Distribution and sale charges, covering transport, advertising and placement of goods.

However, some expenses incurred during the construction phase are not accounted as costs, but rather as tangible fixed assets. Capitalised costs will not be deductible as tax costs but may be amortized according to Portuguese tax rules.

2.1.2. TAX LOSS CARRY FORWARD

As a rule, losses may be deducted from taxable profits within the following 5 tax years. Nevertheless, companies that qualify as micro, small and medium-sized enterprises (“**SMEs**”) may carry forward tax losses in the following 12 tax years with an annual limit equal to 70% of the taxable income.

In view of the current pandemic crisis caused by Covid-19, the 2020 Supplementary Budget approved a set of special rules for the years 2020 and 2021:

- Tax losses generated in 2020 and 2021 may be carried forward in the following 12 years;
- The annual limit of the deduction is extended from 70% to 80%; and
- The years 2020 and 2021 will be disregarded when counting the period for carrying forward tax losses (of 5 or 12 years).

2.2. OPERATION PHASE

2.2.1. TAXATION OF INCOME

The general CIT rate applicable to taxable profit is 21%.

Companies that qualify as SMEs benefit from a 17% rate on the first €25,000.

The amount of CIT due in each tax period can be increased by the Municipality Surcharge (*Derrama Municipal*), which varies according to the municipality where the company's head office is located and eventually the company's turnover.

The Municipal Surcharge rate is fixed annually by each municipality up to a maximum of 1.5%. However, municipalities may approve exemptions for:

- Companies with a turnover of less than €150,000 in the previous financial year;
- Companies operating under a certain Code of Economic Activity (the so-called “CAE”); and
- Companies that have been recently incorporated and create jobs.

As a rule, the income is deemed to be generated in the municipality where the taxpayer has its head office or effective management.

If the taxable profit exceeds €1,500,000, a State Surcharge (*Derrama Estadual*) will be applicable at the following rates:

- On the taxable profit between €1,500,000 and €7,500,000: 3%;
- On the taxable profit between €7,500,000 and €35,000,000: 5%; and
- On the taxable profit exceeding €35,000,000: 9%.

As a rule, CIT and municipal taxes must be self-assessed and paid by the companies after submission of the annual tax returns (Form 22) by 31 May of each year.

Companies will be entitled to deduct to the CIT any advance tax payments, special advance payments and additional advance payments that may be made by them during each tax year.

1.2.2. AMORTIZATION OF TANGIBLE ASSETS

The expenses incurred during the construction phase of the solar plants which are recorded as tangible fixed assets are subject to impairment due to their loss of value because of their use, the passage of time, technical progress, or other causes.

Portuguese tax laws determine that these assets may be subject to depreciation as from their entry into operation and the relevant amortization periods.

As a rule, the amortization must be carried out during the maximum period of useful life, which implies that at least the minimum quota of depreciation is accounted as a cost. As a result, depreciations made beyond the maximum life span are not accepted as tax costs.

According to the depreciation regime, the life span may vary between a minimum of 12.5 years and a maximum of 25 years.

As a rule, the calculation of the depreciation and amortization of the assets is made in accordance with the straight-line method. However, companies may choose the declining-line method under certain conditions.

The adoption by the taxpayer of other amortisation methods, which result in the application of depreciation or amortisation quotas higher than those provided in the law, is subject to the Tax and Customs Authority's authorisation.

2.3. LIMITS ON DEDUCTIBILITY OF FINANCING EXPENSES

Net financing expenses can contribute to the determination of taxable profit up to the higher of the following limits:

- €1,000,000; or
- 30% of the earnings before taxes, net finance costs, depreciation and amortization.

However, there are two exceptions:

- Net financing costs that may not be deductible in a given year may be considered in one or more of the five subsequent tax periods, after the deduction of the net financing costs of that period, subject to the above-mentioned limitations; and
- If the amount of financing costs deducted is less than 30% of the earnings before taxes, net finance costs, depreciation and amortization, the unused portion is added to the maximum amount deductible in the five subsequent tax periods.

The right to carry forward the financing costs ceases to apply when it is verified, at the end of the tax period in which the deduction is made or the limit is increased, that there is a change in the ownership of more than 50% of the share capital or majority voting rights of the taxpayer, except in cases provided in the law or if authorization is obtained from the member of the Government responsible for the area of finance in cases of recognized economic interest, by means of an application to be filed with the Tax and Customs Authority under the terms of the law.

3. VALUE ADDED TAX

3.1. CONSTRUCTION PHASE

3.1.1. ACQUISITION OF EQUIPMENT IN PORTUGAL

Acquisitions of appliances, machinery and other equipment used exclusively or mainly for capturing and using solar energy are subject to Value Added tax (“**VAT**”) at a rate of 13%. Acquisitions of other goods and services are subject to the general rate of 23%.

In the case of acquisition of equipment where the vendor is based in Portugal, VAT is assessed by the seller of the goods.

There may be an inversion of the taxable person in case the supplier performs the installation, and this installation involves civil construction work, as explained below.

3.1.2. ACQUISITION OF EQUIPMENT IN ANOTHER MEMBER STATE

Where the supplier of the equipment is resident in another Member State and the equipment is dispatched from that Member State, the supply will constitute an intra-community supply.

Intra-community transfers will give rise to two operations:

- An intra-community supply of goods which is VAT exempt in the Member State of origin; and
- An intra-community acquisition of goods which is subject to VAT in the Member State of destination.

In intra-community acquisitions, there is a reverse charge, since it is the purchaser - and not the supplier - who must pay VAT.

In the case of transfers of goods dispatched or transported from another Member State in which the installation or assembly in Portuguese territory is made by or on behalf of the supplier, the transaction is also considered located in Portuguese territory and, consequently, will be subject to VAT in Portugal.

3.1.3. VAT DEDUCTION, VAT CREDIT AND VAT REFUND

As a rule, the VAT will be deducted at the moment the tax becomes chargeable, *i.e.*:

- In transfers of goods, when they are placed at the disposal of the purchaser; and

- In the provision of services, at the time of their performance.

Whenever the VAT deduction exceeds the amount due for taxable transactions, in the corresponding period, the excess is deducted in the following tax periods, which translates into a VAT credit.

If the value of the VAT credit continues for 12 months in relation to the period when the excess began, a refund can be requested, provided the value is greater than €250.

The company may also apply for a refund before the end of the 12th month period in cases where a VAT credit exists at the time of end of activity, change of the VAT taxation regime, or if the credit in favour of the taxpayer is higher than €3,000.

The reimbursement of the VAT shall be made by the Directorate-General for Taxation (“*Direção-Geral dos Impostos*”) until the end of the second month following the month in which the request was presented, at the end of which the payment of compensatory interest may be requested, provided that certain conditions are met, namely:

- Submission of the VAT returns in which the refund request was made within the deadline; and
- Delivery of a guarantee (usually in the form of a cash bond or bank guarantee) that may be required by the Directorate-General of Taxation whenever the amount to be reimbursed exceeds €30,000.

3.1.4. CONSTRUCTION SERVICES: REVERSE CHARGE RULE

Generally, VAT is assessed by the companies that provide the services. In the case of construction services, there is a reverse charge.

The reverse charge will apply when the following (cumulative) requirements are met:

- There is a purchase of “construction services”; and
- The purchaser is a VAT taxpayer in Portugal and carries out transactions that confer, in whole or in part, the right to deduct VAT.

As a result of the reverse charge, the purchaser of the construction services is responsible for assessing and paying the VAT due, without prejudice to the right to deduct it under the general rules.

It should be noted that in cases where the obligation to assess and pay the VAT falls in the purchaser of the goods and services, only the tax assessed by virtue of that obligation confers the right to deduct.

Regarding the supply of movable assets in connection with the construction services, the Tax and Customs Authority has published several opinions that clarify the application of the reverse charge rules.

3.2. OPERATION PHASE

3.2.1. SALE OF ENERGY IN PORTUGAL

A supply of goods carried out for consideration within the Portuguese territory by a VAT taxpayer is subject to VAT.

Electricity, gas, heat, refrigeration and the like are considered tangible goods for VAT purposes.

Thus, the sale of energy by a photovoltaic power plant will be considered a transfer of goods and is subject to the general VAT rate of 23% and the seller must pay VAT.

3.2.2. SALE OF ENERGY TO A MEMBER-STATE

The sale of energy to a buyer based in another Member State constitutes an intra-community transfer. As such, the following rules are applicable:

- The intra-community supply made by the seller is VAT exempt in Portugal; and
- The intra-community acquisition by the buyer is subject to VAT in the Member State of destination.

In this way, the seller does not have to account for VAT and it is up to the buyer to do so, provided this does not affect the right to deduct input VAT.

4. OTHER TAXES AND TARIFFS

4.1. SOCIAL ELECTRICITY TARIFF

The social electricity tariff was created with the purpose of guaranteeing access by all consumers to the essential electricity supply service, namely economically vulnerable customers.

The payment of this tariff is ensured by the owners of electricity generating centers under the ordinary regime, in proportion to the installed capacity of each electricity generating center.

The amount of income obtained with the financing of the costs of the social tariff by the owners of the generating power plants, as well as its allocation to the operators intervening in the electricity sector value chain until the attribution of the social tariff by the distribution network operator are determined in accordance with that established in the tariff regulations applicable to the electricity sector.

Nevertheless, in accordance with the Clarification of 17 June 2020 of the Directorate-General for Energy and Geology (“**DGEG**”), the holders of the rights arising from the auction procedures of July 2019 and August 2020 for the allocation of reception capacity in the Public Service Electricity Network (“**RESP**”) of electricity produced at solar power plants (“**Rights Holders**”) are exempt from the social tariff for electricity.

4.2. EXTRAORDINARY CONTRIBUTION OVER THE ENERGY SECTOR

The State Budget Law for 2014 created an extraordinary contribution over the energy sector. This contribution is imposed on natural or legal persons that make part of the national energy sector and that are VAT taxpayers.

This contribution is levied on the value of the following assets:

- Tangible fixed assets;
- Intangible assets, with the exception of industrial property; and
- Financial assets allocated to concessions or to activities licensed under the terms of the previous article.

The rate of the extraordinary contribution on the energy sector is 0.85%.

According to the DGEG clarification, the Rights Holders are exempted from this extraordinary contribution.

4.3. CLAWBACK MECHANISM

Under Decree-Law no. 74/2013 (“**Clawback Law**”), the Portuguese Government approved a regulatory mechanism aimed at compensating the distortions that the extra-market measures and events registered within the European Union cause in the formation of the average electricity prices in the wholesale market in Portugal.

This way, whenever the abovementioned extra-market events give rise to benefits not expected for domestic producers, the corresponding compensation is made, within the scope of the distribution of costs of general economic interest, ensuring the balance of competition in the wholesale electricity market in Portugal.

In this sense, Decree-Law no. 104/2019 amended the Clawback Law introduced the possibility of a payment on account which mitigates the time lag occurring between the verification of the extra-market event and the respective compensation. It also allowed to adjust the external event to the electricity production technology on which it is focused, to avoid distortions of undifferentiated application to different energy production sources. Important to note that with this amendment, the Clawback Law has now expressly established that the clawback charges apply to all electricity producers that sell electricity at a price by reference to OMIE (the Iberian electricity daily market).

The value of the payment on account to be applied in 2021 to electricity producers covered by the clawback mechanism is €2,24/MWh, per unit of energy injected in the public service electricity grid, which already takes into account and internalises local events that affected the Electric National System (“SEN”) such as the taxation of petroleum products and energy, the extraordinary contribution on the energy sector and the social tariff for electricity.

Nevertheless, although Clawback Law only established that this charge is to be applied to electricity producers, the Portuguese Energy Secretary of State determined that in the case the supplier acquires electricity from a producer under a power purchase agreement (“PPA”) with a fixed price to sell it at OMIE, receiving the respective marginal price as return, there will be an increase in gain with the nature of a windfall profit at the level of the supplier, which must be subject to the Clawback Law mechanism.

Between 1 July and 30 September 2021, by Order no. 6398-A/2021, the Portuguese government decided to suspend the application of this rate, which corresponds to the suspension of tax measures in Spain, identified by Energy Services Regulatory Authority (“Entidade Reguladora dos Serviços

Energéticos – ERSE”) as having an impact on the formation of average electricity prices in the wholesale market in Portugal.

According to the DGEG Clarification, the Rights Holders are exempt from the clawback mechanism.

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