

Tax Flash

Autonomous Taxation - Constitutional Court expressed for the non unconstitutionality

31 January 2011

In a Judgment of 12 January 2011 (Judgment 18/2011, Case 204/2010), the Constitutional Court (Court) has ruled that article 5 of Law no. 64/2008, of 5 December, which increased from 5% to 10% the rate of autonomous taxation applicable to representation expenses and expenses of light passenger vehicles, is not unconstitutional.

This Judgment results from a judicial appeal filed by a taxpayer in a first instance tax court (tax court), who argued the unconstitutionality of that provision based on the following arguments:

- Breach of the non-retroactivity principle of the tax law, as provided in paragraph 3 of Article 103 of the Portuguese Constitutional Law (Constitution), and
- Breach of the principle of protection of confidence, since the referred provision, included in a decree that entered into force on the 6 December 2008 (date of publication), was effective as from 1 January 2008 (an amended letter a, paragraph 3 of Article 81 of the Corporate Income Tax – CIT – Code).

The taxpayer obtained a favourable decision in the tax court, which decided on the material unconstitutionality of the provision, considering that it produced retroactive effects.

Consequently, the Public Prosecutor appealed to the Constitutional Court, which has reversed the earlier ruling.

Grounds for the Constitutional Court's decision

I – Breach of the non-retroactivity principle of the tax law

The Court referred to an earlier decision (Judgement 399/2010), according to which the constitutional legislator who introduced the current wording of paragraph 3 of article 103 of the Constitution (1997 review), intended only to establish the prohibition of the so called authentic retroactivity of the tax law.

Authentic retroactivity will only cover those cases where the taxable event that the new law seeks to regulate has already produced all its effects under the old law, excluding from its scope situations of incomplete retroactivity, i.e., those situations in which the law applies to past events but its effects still persist in the present – this happens when a law is approved before the end of the year to which the tax relates.

In a previous decision about a similar situation, the Court did not declare the unconstitutionality of tax rules that increased taxation for the taxpayer, in respect of tax facts that did not take place entirely within the scope of the previous law, and continued to take place within the same tax year, in the course of the new law. This situation was considered to be incomplete retroactivity, not covered by paragraph 3 of Article 103 of the Constitution. Based on the same arguments, the Court has ruled that the alleged material unconstitutionality due to a breach of the referred constitutional provision did not occur.



II – Breach of the principle of protection of confidence

Following a previous Judgement (399/2010), the Court stated that the enforcement of the principle of protection of confidence involves four tests, which are not met in the case at hand:

- The State/legislator behaved in way which is likely to create expectations of continuity of law;
- Those expectations are legitimate, justified and based on valid reasons;
- The individuals made plans in the expectation of consistency on the part of the State;
- There are no public interest reasons that justify the lack of continuity on the part of the State which has created such expectations.

The Court considered that there was no clear evidence leading to a conclusion that the legislator should not have amended the legal regime of autonomous taxation, and that, accordingly, any such changes, made for reasons of public interest, would be acceptable.

The Court also stated that the mere fact of a legal amendment which increases the taxpayer's taxation is not sufficient argument that such amendment should always occur before the beginning of each tax year and not during its course.

Moreover, the Court considered that, in the case of long-term juridical relations or complex facts that are not fully consummated, there is no obligation to comply with a principle of non-frustration of legal expectations or maintenance of a legal regime. Therefore, the legislator is not precluded from amending the legal regime and thus affect pre-existing juridical relations, which still exist at the time new provisions are implemented – indeed, this is a necessary consequence of the self-revision of laws.

The Court did not agree with the taxpayer's argument that he would not have incurred certain expenses subject to autonomous taxation if the increase of the applicable rate was expectable or known. The Court stated that the expenses in question, due their nature, are indispensable to generate taxable profits or gains, or to maintain the business of the company, so the taxpayer would always have incurred those expenses.

Dissenting vote

There was a dissenting vote in this Judgement, based on the following arguments:

- The rule under analysis is unconstitutional because it is retroactive; it is not possible to conclude otherwise based on the arguments used in previous Judgements;
- Although the autonomous taxation provision is included in the CIT Code, the tax at hand materially differs from the taxation under CIT; in fact, autonomous taxation does not have the object of taxing income at the end of the tax period, but, rather, of taxing a certain kind of expenses;
- Each expense is an autonomous taxable event, producing a liability of the taxpayer, irrespective of whether or not it has taxable income (for CIT purposes) at the end of the tax period;
- The increase of the autonomous taxation rate increases taxation for the taxpayer at a time when the taxable event has already occurred, even though the autonomous taxation is assessed and paid at a later time (payment is simultaneous with the payment of the CIT due);
- The assessment of the taxable basis for autonomous taxation purposes by the end of the tax year is a summation of individual expenses, to which the (now increased) autonomous taxation rate applies; the computation of that taxable basis is not a taxable event of successive formation, but a mere aggregation of amounts which are the basis for computation of the autonomous taxation;
- Paragraph 3 of Article 103 of the Constitution prohibits authentic retroactivity, which does not occur in the case of taxes on income when the increase of the tax rate takes place before the end of the tax period; in fact, the taxable event for CIT purposes is assessed with reference to the end of the tax year, while in case of autonomous taxation this does not happen, as the computation is not based on income but instead on individual expenses.

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