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Ana Gomes

Madeira - a preferential tax regime

Autonomy

1. Madeira is a Portuguese archipelago situated in the North Atlantic Ocean, southwest of Portugal. In 2011 its total population was estimated at 267,785;
2. Madeira is one of the two Autonomous regions of Portugal (the other being the archipelago of the Azores). The archipelago is ruled by an autonomous Regional Government, and a Regional Assembly, elected by universal suffrage;
3. Article 227 of the Portuguese Constitution determines the legislative and executive powers of the regional authorities, which include ample legislative powers in fields not reserved to the national sovereign institutions, such as foreign policy, national defence and internal security. Madeira can, as such, define its taxation policy, under the law, and adapt the national tax system to regional circumstances. The archipelago can also benefit from the tax revenue levied or generated, as well as a share of the State tax revenue;
4. All European legislation, namely in the field of exchange of information, transparency and anti-money laundering is fully applicable to Madeira;

Governance

5. In Madeira, the same party has been in power since the first elections after the Portuguese Revolution, which re-instated democracy in Portugal, in 1974. Moreover, since 1978 until as recently as 2015, the President of the Regional Government was the same man, Alberto João Jardim¹, from PSD - Partido Social Democrata (EPP);
6. In the summer of 2011, months after the memorandum of understanding was signed between the Troika and the Portuguese government, Banco de Portugal and the National Institute of Statistics reported that there were financial liabilities of the Autonomous Region of Madeira that had not been reported to those two entities, as required by law. There was an undeclared sum of more than 1,1EUR billion, accumulated between 2003 and 2010. Most of the hidden debt related to 2010²;
7. The Portuguese Attorney General initiated a criminal inquiry over the occultation of the debt. In 2014, after three years, the Attorney General closed the case, declaring that the facts under investigation "could integrate crimes of prevarication and breach

¹ https://pt.wikipedia.org/wiki/Lista_de_presidentes_do_Governo_Regional_da_Madeira

² <http://expresso.sapo.pt/sociedade/ministerio-publico-arquiva-investigacao-a-divida-oculta-da-madeira=f892846>



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of budget execution rules for accused persons holding political office", but no evidence of such crimes was found;

Sociedade de Desenvolvimento da Madeira (SDM)

8. Sociedade de Desenvolvimento da Madeira, S.G.P.S., S.A. administers, promotes, and manages the international business centre (CINM - Centro Internacional de Negócios da Madeira/ZFM - Zona Franca da Madeira) in Madeira. It issues necessary licenses to incorporate a company within the legal framework of the international business centre of Madeira, and builds infrastructure for the industrial free trade zone³. The company was founded in 1984 and was awarded the concession contract to administer the CINM in 1987 for a period of 30 years;⁴
9. SDM has a hybrid structure. Its two shareholders are the Pestana Group (private entity) with 75% and the Regional government (25%). The current concession period (30 years) ends in 2017. The regional government was confronted with three scenarios: extending the concession to the SDM, opening a new international public tender for private companies to manage the FZM or bring its management (and proceeds) completely under the public sphere. It is expected that the Regional government will extend the current concession with a capital increase by the Regional government, to achieve a holding of 49% of the SDM⁵. The Regional government has never launched an international competition to grant the concession rights to the private shareholder;
10. The current Regional Director of Tax Affairs, Mr. João Machado, was recently appointed representative of the Regional Government in the administration of SDM⁶, which indicates alarming revolving doors between public authorities and the SDM;

Zona Franca da Madeira - Centro Internacional de Negócios da Madeira (CINM)

11. The CINM started its activities in 1987, thereby establishing Madeira's Zona Franca (Free Zone of Madeira - FZM) as an instrument for economic growth and development, to attract foreign investment and capitals. In a letter signed by P. Sutherland on behalf of the European Commission concerning the establishment of the FZM, he does not object to the creation of the FZM, **but it is clearly stated that under no circumstance he authorises it to be set up as an "offshore"** and that the job creation criteria is crucial for the authorisation (Annex 1). Since 1987, the European Commission has authorised four different regimes for the operation of

³ <http://www.bloomberg.com/research/stocks/private/snapshot.asp?privcapid=417024>

⁴ <https://sol.sapo.pt/artigo/126687/bruxelas-mantem-regime-fiscal-na-zona-franca-da-madeira>

⁵ <http://observador.pt/2016/11/22/zona-franca-da-madeira-vai-gerar-191-milhoes-de-euros-de-receitas-este-ano/>

⁶ <http://www.dnoticias.pt/imprensa/hemeroteca/diario-de-noticias/joao-machado-na-sdm-FX743430#>



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CINM/ZFM. The current regime is in place until 2020, producing effects until 2027. In the 3rd regime, the European Commission ordered the exclusion of financial activities from the FZM;

12. Since 2015 the FZM has a preferential tax regime with a nominal corporate tax rate (IRC) of 5%, which, however, is subject to maximum limits of taxable profit in each company (*plafonds*), according to a table established by the number of jobs created by the company. Thus, the effective tax rate on IRC in each company varies between 5% and 21%, the higher the higher the taxable profits and the lower the number of jobs created;
13. The activities currently accepted and licensed under the FZM fall into three main areas:
 - a. The Industrial Free Zone, comprising industrial or warehousing processing activities, with physical movement of products;
 - b. The International Ship Registry of Madeira (MAR) which permits the registration of yachts or commercial vessels, and constitutes a Portuguese maritime registry of an international and open nature;
 - c. International Services, which includes predominantly international business services with a broad spectrum of activities, excluding those of a financial or intra-group nature;
14. At the end of 2015, according to the CINM, there were 2.016 corporate entities operating in the FZM, the large majority of which under International Services firms. According to the CINM, the ZFM generated more than 151 million euros in 2015 of effective tax revenue for the Autonomous Region of Madeira, that is, more than 17% of all tax revenue of the Region⁷;
15. The Regional authorities have informed me that there are not secret tax rulings granted to companies based in the FZM. Upon compliance with the conditions, the authorities merely grant the applicable reduced tax rate;

Law and Scrutiny

16. The Regional Tax Authority AT-RAM⁸ (Autoridade Tributária e de Assuntos Fiscais da Região Autónoma da Madeira) is an executive unit of the Regional Finance Department and Public Administration of Madeira that is responsible for ensuring the collection and managing the various legally prescribed taxes in the Region and run policies and fiscal guidelines set by the Regional Government of Madeira. The AT-RAM is organically independent from Autoridade Tributária (AT), the central

⁷ <http://www.ibr-madeira.com/pt/noticias/noticias/462-receita-fiscal-do-cinm-ultrapassa-os-150-milh%C3%B5es-em-2015.html>

⁸ http://info.portaldasfinancas.gov.pt/NR/rdonlyres/EE09967A-A443-4C4C-AC6B-39D62623DC63/0/Decreto_Regulamentar_Regional_14_2015_M.pdf



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Portuguese Tax Authority, however, large taxpayers are under the umbrella of the “large taxpayers unit” in the central AT, including large corporations. But the “large taxpayer unit” in the central AT was deactivated and, though formally re-established in 2016, has yet to be adequately staffed. The AT has, in any case, full access to the database of AT-RAM, and can carry out inspections and investigations concerning all corporate entities registered in the FZM⁹. Yet in practice this does not happen. Differently from what happens with the Autonomous Region of the Azores, the AT has no control over the AT-RAM. This was confirmed by me directly, at top level of the AT;

17. Law No. 118/2015 of 31 August 2015 was adopted by Portuguese Parliament, transposing into Portuguese law the only part of the text of the 2015 Anti-Money Laundering Directive (IV ALMD) which allows a top manager to be registered as the beneficial owner, should it prove difficult for obliged entities to identify the actual beneficial owner.¹⁰ The transposition of this clause introduced in the IV AMLD (and the sole IV AMLD provision transposed into Portuguese law so far) might be abused in Madeira, to shield certain beneficial owners of corporate entities associated with money laundering, tax fraud and aggressive tax planning;
18. This transposition will also affect the utility of the forthcoming business register of beneficial owners of legal entities established in Madeira as foreseen by the AMLD IV, since it might be fed with information solely concerning top managers, and not the beneficial owners.

Several suspicious cases

19. In Spain, famous football players were charged with tax fraud, involving entities established in Madeira. Javier Mascherano from Futbol Club Barcelona was also accused of tax fraud by Spanish authorities, amounting to 1 500 000€, on earnings linked to his image rights from 2007 to 2009. He was accused of fictitiously selling the rights to Anadyr Overseas, a shell company in Madeira, when transferring from Liverpool.¹¹ Adriano Correia, also from Barcelona at the time, is still being charged with tax fraud by Spain, amounting to 700 000 € due on earnings linked to his image rights from 2011-2012. He is accused of fictitiously selling the rights to Chacun à sa Place, a corporate entity in Madeira, when he was transferred from Sevilla. The Spanish Tax Authority is seeking a 1 000 000€ fine in addition to the payment of the

⁹ https://info.portaldasfinancas.gov.pt/NR/rdonlyres/01D66ED3-05C1-44E7-A3B2-1E096142D3FE/0/Lei_64_2015.pdf; art 7

¹⁰ http://www.pgdlisboa.pt/leis/lei_mostra_articulado.php?nid=2400&tabela=leis&nverso=

¹¹ <http://www.jornaleconomico.sapo.pt/noticias/justica-espanhola-arquivou-processo-xabi-alonso-envolvia-empresas-sede-na-madeira-110269>



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due taxes¹². The intermediary company in all these cases was Igmasa Management, established in the principality of Andorra.¹³

20. The Panama Papers revealed that Mexican shipping company Grupo R, a giant conglomerate, used companies created by Mossack Fonsenca in four continents to obtain loans with banks of at least \$14 billion to buy machinery that was leased to state oil company Petróleos Mexicanos (Pemex).¹⁴ Three of them, Laforta, Utiledulci and Rubicon, were based in the FZM. These companies are active and managed by the intermediary firms Mossack Fonseca and Igmasa Management. The local manager in Madeira for the three firms is Mr. Samuel de Araújo and they are all owned by other shell companies in other jurisdictions like The Seychelles and Luxembourg. Laforta alone was able to obtain loans in the amount of 660 million dollars to build oil platforms. The three firms declared profits of 353 Million EUR in 2014, while declaring merely 9 employees in Madeira, and each one costs to the companies from 300 to 340 EUR per month (which does not even cover for minimum wage), as revealed by an investigation by the Portuguese Public TV Channel RTP.¹⁵

Unverified job creation by the FZM

21. Unverified numbers are reported to the European Commission to grant eligibility of Madeira for regional investment aid under EU state aid rules, thereby allowing the Portuguese State to grant state aid to FZM companies. According to the Regional government, the AT-RAM is the entity that supplies the number of jobs created by the FZM. However, many sources do not see a correspondence between the numbers reported and the jobs effectively created in the region. These numbers aim to sustain the idea that the FZM can foster job creation and the regional development in the islands;
22. With regard to actual job creation, a study by researcher João Pedro Martins estimated that about 2800 workers in the FZM are fictional.¹⁶ He points out that the entity actually responsible for the data provided is neither the Portuguese Tax Authority (Autoridade Tributária) nor the Regional or Central Government. It is, rather, the SDM, the entity running the FZM;
23. The data reported to the European Commission is gathered through a questionnaire filled by companies present in the FZM. According to Mr. Martins, each of these

¹²http://www.cmjornal.pt/desporto/futebol/detalhe/adriano_acusado_de_fraude_fiscal_pelo_fisco_espanhol

¹³ <http://www.diariorc.com/2012/11/07/xabi-alonso-y-mascherano-no-son-los-unicos-los-deportistas-defraudadores-siguen-siendo-idolos-en-espana/>

¹⁴ <http://www.univision.com/noticias/papeles-de-panama/naviera-mexicana-financio-compra-de-barcos-para-pemex-con-empresas-creadas-por-mossack-fonseca>

¹⁵ http://www.rtp.pt/noticias/panama-papers/escandalo-panama-papers-chegou-a-madeira_v913474

¹⁶ *Suite 605*, João Pedro Martins, Nexo Editorial, 2011.



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companies signals it has 1 employee, but his research found, for instance, 2 workers which managed, simultaneously, 870 companies¹⁷;

24. According to his research, the 2000 offshore companies in Madeira are managed by 20 CSP (Corporate Service Providers).¹⁸ These are companies associated with law firms, which offer package solutions to clients such as shell companies, including registration, bank accounts, and even frontmen (also known as nominees) to serve as “managers”. Their headquarters combined cannot host more than 200 jobs/employees in Madeira;
25. According to Mr. Martins, most of these companies do not create jobs, do not produce real economic activity and do not add significant value to the business community. These entities are mostly integrated in opaque corporate structures used for transfer pricing mechanisms by multinationals and aggressive tax planning. These fictional operations, with the sole purpose of tax optimisation, violate National Anti-Abuse Laws such as Article 38 (2) of the Portuguese Tax Code¹⁹;
26. Under current EU state aid rules, an investigation by either the Portuguese State or the European Commission into the veracity of the data provided (namely on the number of jobs created) would allow for the Portuguese State to be reimbursed by the companies registered in the FZM in the amount of state aid received (under reduced corporate tax rates) if they were found not to comply with the conditions laid out by the European Commission;
27. Finally, the financial transactions reported under the FZM artificially inflate Madeira’s regional GDP, thus preventing eligibility of the island to receive large sums in European structural and regional funds allocated to EU’s outermost regions.²⁰ Moreover, this *status quo* establishes a disadvantage in competition between Madeira’s small and medium enterprises as they pay a larger share of taxes than multinationals.

¹⁷ *Suite 605*, João Pedro Martins, Nexo Editorial, 2011.

¹⁸ <http://www.ibr-madeira.com/pt/supporting-services.html>

¹⁹ <https://info.portaldasfinancas.gov.pt/NR/rdonlyres/87CAB3CA-4ED1-411A-9BDE-3E9725C24F21/0/LGT.pdf>

²⁰ *Suite 605*, João Pedro Martins, Nexo Editorial, 2011.



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Conclusion

In conclusion, the FZM is an extremely low taxation jurisdiction which, combined with lax anti-money laundering enforcement and supervision, is extremely vulnerable to the use by international corporations and criminal organisations for aggressive tax planning, tax fraud, tax avoidance and money laundering.

The European Commission allowed this special jurisdiction to be established in 1987 determining it could not be an “offshore fiscal centre”, based on the special needs of support from an ultra-peripheral region and demanding that “job creation” be a crucial criteria to maintain its activities. However, the jobs actually created, the reliability of any regional or national controls, including the performance of anti-money laundering duties, have not been independently verified - neither by the Portuguese State nor by the European Commission.

There was an attempt of fact finding by the Portuguese Ministry of Finance in 2011²¹, but this was fiercely opposed by the Regional authorities and never more pursued despite the huge financial fraud and deficit uncovered in the Regional budget when Portugal was under the Troika’s adjustment programme.

Ana Gomes MEP
February 2017

²¹ <http://www.dnoticias.pt/imprensa/hemeroteca/diario-de-noticias/269961-zona-franca-em-cheque-por-auditoria-nacional-HODN269961>; <https://info.portaldasfinancas.gov.pt/NR/rdonlyres/2B68EBF3-2301-48C0-818A-6D0E3CCA8CC/0/relatoriodecombateafraudeeevasaofiscaisde2010.pdf>



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Excelência,

Em carta nº 2414 de 18 de Novembro de 1986 enviada pela Vossa Representação Permanente, V. Exa. comunicou à Comissão, e em conformidade com as disposições do parágrafo 3º do artigo 93º do Tratado CEE, um projecto de um regime de auxílios tendo por objecto a concessão de auxílios financeiros e fiscais às empresas industriais, financeiras e comerciais que se instalaram na Zona Franca da Madeira.

Foram enviadas à Comissão informações complementares pelas cartas de 6 de Janeiro e 6 de Março de 1987.

De acordo com as diferentes informações chegadas à Comissão, o regime proposto pode ser descrito da seguinte maneira :

- as empresas de natureza industrial, comercial e financeira que se instalaram na Zona Franca poderão beneficiar de auxílios financeiros e fiscais;
- os auxílios financeiros consistem em co-financiamento, até 50% dos custos de formação do pessoal e dos custos resultantes dos investimentos nos processos de fabrico que permitam economias de energia;
- determinados auxílios fiscais beneficiam os fornecedores de capital, crédito e tecnologia (propriedade industrial) às empresas da Zona Franca;
- os auxílios fiscais de que beneficiam directamente as empresas da Zona Franca consistem na isenção, até ao ano 2011, da contribuição industrial, imposto extraordinário e contribuição predial, e na isenção, sem limite temporal da sisa e do imposto sobre as sucessões e doações

Sua Excelência,
Eng. Pedro PIRES DE MIRANDA
Ministro dos Negócios Estrangeiros
Ministério dos Negócios Estrangeiros
Largo do Rilvas
P - 1354 LISBOA CODEX

directas pelas aquisições de bens imóveis, do imposto complementar, do imposto de mais-valias relativamente às transmissões onerosas de terrenos ou de valores do activo immobilizado e das taxas e impostos locais.

Após ter examinado os objectivos, as modalidades de aplicação e as consequências sobre a concorrência intracomunitária deste regime de auxílios, e tendo em conta a "Declaração Comum relativa ao desenvolvimento económico e social das regiões autónomas dos Açores e da Madeira", anexo ao Tratado de Adesão, a Comissão decidiu não levantar objecções à sua aplicação por um período de três anos a contar do primeiro caso concreto de aplicação. A Comissão reexaminará o regime em questão no fim deste período. Além disso, ela pede ao Vosso Governo que lhe envie um relatório anual sobre a aplicação dos auxílios mencionados.

A Comissão chama a atenção do Vosso Governo para o facto de a aplicação deste regime estar sujeito às regulamentações e disposições diversas do direito comunitário relativas a certos sectores industriais e agrícolas. Ela recorda-vos ainda que a presente autorização não significa em caso algum a aprovação da zona financeira "off shore" que o Governo Autónomo da Madeira terá a intenção de instaurar na Zona Franca.

É enviada uma cópia da presente carta aos governos dos outros Estados-membros para os informar desta tomada de posição da Comissão.

Com os melhores cumprimentos.

Pela Comissão

Portugal


P. SUTHERLAND

Membro da Comissão