

A Guide to Portuguese Taxation

Overview

Although Portugal is far from a low tax country, with the State spending and raising, nearly 50% of GDP, a relatively high rate of social security contribution (34.75% on employees) permits taxes below EU average. Many UK taxpayers are pleasantly surprised.

Portugal has neither wealth nor inheritance tax. Investment income is generally taxed at a flat rate of 20%. There is no capital gains tax on shares held over 12 months. An extensive range of double tax treaties allows tax deducted in the source country to be recovered or given as a credit against Portugal tax. Foreign employees are also exempt from tax on income arising outside Portugal, providing the income is there assessed.

Tax rates are graduated up to a maximum of 42% on taxable incomes over €64,000. However an extensive range of deductions for social security and maintenance payments and personal and expenditure tax credits on health, education, property, insurance, renewable energy, pension plans and donations further help to reduce the final bill. Local authorities have limited scope to reduce tax rates for their residents.

Income Tax

Business and Professional

Self-employed and businesses with annual sales under €149,739 and fees under €99,760 are normally taxed on the simplified regime. This assumes business expenses of 80% of sales and 30% of fees without the need of proof, so that taxed income is just 20% of sales and 70% of fees.

Pensions

- Attract an income allowance of €6,000 (pensions under €30,000, net of the deduction) per person. The handicapped are allowed additional pension income tax free, up to a limit of the lower of €2,500 or 10% of the income.

- Only the income portion of annuity and other pensions purchased by the taxpayer out of taxed income should be declared. Where the fund manager cannot provide the split between the capital and interest portions, then a ratio of 85% capital/15% income may be used.

Investment Income

- Dividends: Are generally taxed at a flat rate of 20%. At the (lower income) taxpayer's option, they may be assessed jointly with other income in which case just 50% of dividends from EU companies (as defined in 90/435/CEE) are assessed.

- Interest: Portugal source income is generally taxed at a final "liberating" tax rate of 20% and the taxpayer is not required to report the income on his tax return. Foreign source income must be reported, but the taxpayer may opt for a flat 20% "autonomous tax". Interest may, at the (lower income) taxpayer's option be assessed jointly with other income.

- Life insurance income is defined as the excess of benefits received over premiums paid. Where at least 35% of premiums are paid in the first half of the contract life, then 20% of income is tax free on contracts over 5 years, increasing to 60% of income tax free on contracts over 8 years.



Photo: Mauricio Abreu

Image: www.pacdd.com



- Investment Funds and Unit trusts: Income does not have to be declared since the responsibility to deduct tax is with the fund managers. Income may be declared and assessed at the (lower income) taxpayer's option.
- Interest on the first €10,500 capital in retirement savings accounts is entirely exempt from tax.
- Fixed term deposits over 5 years are taxed on just 80% of the interest and those over 8 years on 40% of the interest.
- Income received on capital reimbursement of "PPR" pensions are 80% exempted if subscribed before 31st December 2005 and 60% if subscribed later.

Capital Gains

- 50% of the gains on the sale of personal private residence are exempt and roll-over relief is available on reinvestment in another residence. This reinvestment has to be made in the 24 months prior or in the 36 months after the sale, in a principal private residence in the EEA.
- A gain on sale of company capital is taxed at a flat rate of 10%. Gains on sale of shares (SA company) held over 12 months are exempt (except for property companies).

Image: www.pacdd.com



Property taxes

Caution about property taxes. Since 2004, tax office valuations of properties are close to, and in some cases even exceed, market prices. Purchase tax (IMT) is graduated up to a maximum of 6% of the higher of the contract price or tax office valuation. Stamp tax is a flat 0.8%. Annual property tax (IMI) is a maximum 0.5% of tax value. The sale of property, including a principal private residence, is subject to capital gains tax (though roll-over relief into the purchase of another principal private residence in the EEA is possible). Non resident owners must appoint a tax representative and are liable to a flat 25% CGT on sale with no rollover possibility. It is an area where professional advice is essential.

STOP PRESS!!!!

Portugal changes income tax to attract foreigners

For once the legislator has realised that reducing tax rates may increase rather than reduce tax revenue. The potential beneficiaries of this enlightenment are foreigners and returning Portuguese emigrants who settle in Portugal after 1st January 2009.

A decree law of September 2009 introduces a new classification of "non-habitual tax resident", a status initially granted for 10 years. This has similarities to the non-domicile status under UK and Swiss tax laws.

The non-habitual resident is not taxed on employment, approved self employment, investment, property or private pension scheme income or capital gains originating outside Portugal, providing these are subject to tax (though not necessarily taxed) in the source country under the terms of a double tax treaty and do not arise from a location on the Portuguese offshore blacklist.

He or she may also be permitted a flat 20% tax rate on Portugal and foreign source employment and self employment income. To qualify, this income must be of high added value arising from scientific, artistic or technical activity to be defined by the Finance Ministry.

Exempt income must however be declared for purpose of establishing the tax rate to apply to the income, if any, taxed under the normal "progressive" rate method.

The economic benefits foreseen for Portugal include the extra spending and entrepreneurial activity of well off immigrants as well as the indirect and property taxes they support.



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