Blacktower Group – Tax in Portugal 2019

Our advice, your advantage

SINCE 1986

BLACKTOWER

FINANCIAL MANAGEMENT GROUP

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Introduction

If you are thinking of moving abroad to settle in Portugal, there are a number of financial considerations to contemplate. Ideally, you should plan ahead with a view to optimising your wealth and reducing your tax liability.

Professional advice is essential if you are to understand the tax ramifications of a move to Portugal. Tax laws between the UK and Portugal differ significantly and if you are going to protect your wealth successfully, having the support and guidance of a professional who understands all the relevant cross-jurisdictional issues is an invaluable asset.

However, the process should not simply be about protecting what you already have; it should also be directed towards recognising and capitalising on the many opportunities that exist for an expat of your generation and position. Of course, although these opportunities will depend on your individual circumstances, there is value to be gained in understanding the general tax situation in Portugal and this is what we hope this document will help you achieve.

The contents of this Tax Guide are believed to be correct at the date of publication. Every care has been taken that the information in this Guide is accurate at the time of release. However, all information and tax figures are subject to change and you should always make enquiries, check details and, where necessary, seek legal advice before entering into any transaction. The information is for guidance only and does not constitute advice. You should seek professional tax advice tailored to your needs and circumstances before making any decision.

Your Residency Status and Tax

Typically, your country of residence will tax you on income, capital gains, dividends and so on, so it is crucial to understand which jurisdiction you are a resident of.

Portuguese Residency

To qualify for Portuguese tax residency, you must spend at least 183 days of every tax year (January to December) in the country, with your eligibility for Portuguese tax counted from your day of arrival if the move is permanent.

UK Residency

In terms of UK tax residency, your status is determined under the UK Statutory Residence Test. There are several possible statuses under this test:

- Automatic overseas resident
- Automatic UK resident
- Sufficient ties

In the event you do not meet the respective criteria for either of the 'automatic' residence tests, the third status is assessed based on the number of days you are resident in the UK together with an assessment of your applicable 'ties' to the UK. Qualifying ties include:

- having 'substantive' work in the UK
- having family in the UK
- having housing or accommodation in the UK
- spending more time in the UK than any other country together with at least 91 days in the UK over the preceding two years.

Whatever the case, you should seek advice as how to best define and process your status and application.

Portugal's NHR Regime

Portugal's Non Habitual Resident (NHR) regime provides numerous immediate tax advantages for first-time residents in the country, or, alternatively, for those who have not been resident for any of the five preceding tax years.

NHR confers tax benefits for 10 years, including a 20% tax rate on 'high added value' activities (employment and self-employment-related). It also provides opportunities for tax exemption on UK pension income and many other sources of foreign income.

NHR and Pensions

The rules of the Non-Habitual Resident regime allow expats in Portugal to receive some forms of UK pension income tax-free in both countries. In fact, there are rules in place that may enable you to take your entire fund tax-free.

However, this does not mean that all is straightforward when dealing with UK-Portugal cross-jurisdictional pension issues. For example, some pensions automatically attract UK tax. Furthermore, if you are domiciled in the UK when you die, any pension you have withdrawn tax-free will be subject to inheritance tax.

Double Tax Treaties

The terms of the UK/Portugal Double Tax Treaty mean it is only possible to be a tax resident in one of the two countries at any given time. The treaty includes rules that can help you establish your tax residency.

However, if your circumstances change, it is important to take regular advice to ensure that your personal situation continues to align with the rules necessary for your tax status. Any oversights in this regard can prove costly as you could end up paying more tax than necessary.

Establishing Tax Efficiency

The UK/Portugal Double Tax Treaty prevents income from being taxed in both countries. However, in some cases it may be possible to pay tax in the wrong country and to consequently pay more than you need to.

Although it is possible to offset tax paid in one country against the tax due in the other, this does not always provide advantages. It is better to avoid the higher liability in the first place. Finding the arrangement that is most suited to your individual circumstances is rarely straightforward, so it is important to take advice regarding the most tax-efficient arrangement for your personal situation.

Your Tax Residency

When you move to Portugal it is essential that you contact the authorities to declare your residency and tax status. This is true even if all your income, savings and pensions are UK-based.

Failure to declare and disclose tax and residency status may result in you breaking the law and incurring some form of penalty. For example, if you pay UK tax but have not declared some or all of your income to the Portuguese authorities, you could be penalised for tax evasion and become liable for interest on underpaid tax.

By taking early advice, you can ensure your tax and residency statuses are structured in a way so that your affairs are both legal and optimised towards reaching your financial goals.

Social Security and Healthcare

It is important that you are clear about where you should be paying social security. If you get this wrong you could lose out on entitlement to state healthcare and other protections. Ultimately, errors in this regard may also lead to financial penalty and loss of pension rights.

Tax Efficiency of Investments Depends on Residency

What is tax efficient in the UK may not be tax efficient in Portugal, and vice-versa. For example, both Premium Bond winnings and Individual Savings Accounts (ISAs) are tax-free in the UK. However, they may attract considerable tax liability in Portugal so you may want to restructure any investments of this type before you begin residency in the country.

Furthermore, you may wish to consider the tax efficiency of the following investments when moving from the UK to Portugal:

- Equities
- Unit trusts
- Open Ended Investment Companies
- Investment bonds

It is worthwhile talking to your adviser about the various tax-efficient investment vehicles accessible to you as a resident of Portugal and how these may ultimately reduce your tax liability.

Offshore Bank Interest

The worldwide bank interest income of residents in Portugal is subject to a flat rate tax of 28%, regardless of the location and whether the account is used or not. However, it may be possible to add accrued interest to your other income and for it to be taxed accordingly.

The exception is if the account is held in a jurisdiction listed by Portugal as a 'tax haven'. Blacklisted locations include Gibraltar and Guernsey, despite the Organisation for Economic Co-operation and Development (OECD) Global Forum Rating categorising these jurisdictions as "largely compliant". These countries attract a higher tax rate of 35%.

You should declare all your assets and accounts. Portugal is a signatory to the Common Reporting Standard, under which almost 100 jurisdictions automatically exchange tax and financial information on a global level. Failure to declare could result in significant fines and penalties.

Rental Income

Rental Income from UK Property

There are more than 1.75 million landlords in the UK and many of these are expats who have multiple properties in the UK. Often these serve as a kind of proxy pension fund. Owners may have one or more UK properties which they may no longer live in but do not wish to sell because of personal or familial attachments.

Rental income from UK properties remains taxable in the UK, regardless of residence status, and must be appropriately reported in both the UK and Portugal. Tax paid in the UK can be offset against Portuguese tax on the same income. However, if you are a Non-Habitual Resident the income is not liable for any tax in Portugal.

Unless you have particular reasons for owning UK property while resident in Portugal, it may be worth talking to your adviser about the potential benefits of alternative investments.

Rental Income from Portuguese Property

All income derived from property owned in Portugal is subject to tax. For non-residents of Portugal this is a flat rate of 28% (although some specific deductions are allowed, not including mortgage interest).

Portugal's Property Wealth Tax

An annual wealth tax on property assets in the country has been levied since 2017. AIMI - Adicional Imposto Municipal Sobre Imóveis is seen as Portugal's version of a wealth tax, which affects owners with a share in Portuguese property worth in excess of €600,000. This threshold is for individuals. Spouses and civil partners have a combined allowance of €1,200,000. Regardless of residency status, rates applied are 0.4% on the total amount for properties held by companies, 0.7% to 1.5% for Individuals – the higher rate being applied to properties valued in excess of €2,000,000.

Property Tax in Portugal

Every owner of a property in Portugal is subject to IMI – Imposto Municipal Sobre Imóveis. According to the IMI rules, you are considered an owner if you are in possession of the property or land, at 31st December of each year.

A few full IMI exemptions do apply. If you have a gross annual income of less than €15,295 and the total property value is less than €66,500, you will be exempt from paying IMI. If you buy a property for primary residency purposes, you can also benefit from a three-year exemption. Providing the value of property is €125,000 or less and your annual gross income is less than €153,000.

Capital Gains on Property

Capital gains tax (CGT) is payable on proceeds from the sale of a property in Portugal at a rate of 28% for individuals and 25% for companies (non-residents). The CGT is only applicable on 50% of the gain.

The exceptions to CGT in Portugal are:

- If the full proceeds from the sales (capital gains included) are reinvested in the purchase of another property (primary residence) in Portugal within a period of three years.
- If the full proceeds from the sales (capital gains included) are reinvested in the purchase of another property (primary residence) within the EU or EEA in a maximum period of three years.
- If the property was purchased prior to January 1989.

For property in the UK, only 50% of capital gains are added to your other income and taxed at the relevant Portuguese rate; the remaining 50% is exempt.

However, it is worth bearing in mind that you will also be liable for UK capital gains tax for amounts accrued after 6 April 2015, even if you are resident in Portugal.

Undeclared Income or 'Black Money'

Not that long ago in Portugal many property sales were borderline in their legitimacy as neither vendor nor buyer always disclosed the full value of the transaction. Not only is this practice of under-declaring purchase price illegal, it can also result in a much larger capital gains liability than would otherwise apply when you sell the property further down the line. Such 'black money' transactions should be avoided.

Succession Laws

In August 2015 Portugal implemented an EU regulation known as 'Brussels IV'. Under the terms of Brussels IV, if you reside in Portugal you can choose to have UK succession law apply to your estate, otherwise Portuguese succession law will apply automatically upon your death.

There may be significant advantages to electing UK succession law: Portugal's forced heirship rules do not allow you to choose certain beneficiaries – for example, step-children – while simultaneously forcing you to hand on as much as half of your estate to your 'bloodline' – this includes children (biological and adopted), spouse, parents and grandparents – regardless of whether you want this.

You should be aware that if you are a resident of Portugal, Portuguese succession law will apply to all your worldwide assets (excluding non-Portuguese real estate). As such, careful planning in relation to succession laws and inheritance taxes is essential.

Inheritance Planning

Portugal levies a succession tax on property, but it may be possible to avoid this when gifting property to your children or other beneficiaries. However, taking this step may not prevent the property in question becoming liable for UK inheritance tax.

One way to protect your legacy and to structure your assets effectively is to use ownership via a company to mitigate succession and inheritance taxes. However, this can create new kinds of complexities and liabilities, including capital gains and corporation taxes, particularly if you are not classified as a habitual resident. Whatever the case, it is important to seek reliable advice in this regard – what is best for one person may be disadvantageous to the goals and circumstances of another.

Wills and Probate

UK Wills are valid in Portugal but can be complicated by cross-jurisdictional probate regulations. It can be a laborious and time-consuming process negotiating cross-border probate before assets can be distributed.

It is important to be careful and to take advice. Writing a Portuguese Will can potentially invalidate your UK Will and in some cases could even lead to disputes between your heirs.

Inheritance Tax

Parents, children and spouses in Portugal are exempt from inheritance tax (IHT) – known as stamp duty in Portugal. The rate for other beneficiaries is a globally favourable 10%. This tax applies to all Portuguese-situated assets, including property, as well as lifetime gifts.

Unlike the UK, in Portugal the tax is paid by the beneficiary rather than the estate. However, just as in the UK, the beneficiary cannot take legal ownership of the bequeathed asset until the tax has been paid. Inevitably, problems can arise in this regard as an asset cannot be sold until the stamp duty has been paid.

IHT for UK Domiciles with Strong Portuguese Links

UK domiciles are subject to UK inheritance tax on death even if they have previously lived for extended periods in Portugal. In theory, this can result in estates being liable for both Portuguese and British inheritance tax. However, although there is no double tax treaty between the two countries relating to inheritance tax, the UK provides unilateral relief to prevent double taxation.

Despite this relief, complicated situations can arise. Good advice and prudent planning are likely to prove invaluable in helping you pass on your estate in line with your wishes and with only the minimum level of tax.

Unmarried Couples and UK Civil Partners

Portuguese stamp duty of 10% applies to both lifetime gifts and Portuguese assets inherited by unmarried couples. This rate also applies to gifts and assets passed on to non-bloodline relatives – for example, step-relatives or close friends.

However, unmarried couples who have lived together for two or more years and have registered this fact with the Portuguese tax authorities can be treated as a married couple for tax purposes.

Portugal has a progressive approach to same-sex couples, and recognises both same-sex marriages and UK civil partnerships, ensuring that both categories of couple are treated as spouses under Portuguese tax law.

Taxation of Trusts

Trusts are an increasingly popular method of estate and succession planning. However, since 1 January 2015 Portugal has made distributions from trusts taxable at a rate of 28% or, for ‘blacklisted’ jurisdictions, such as Gibraltar or the British Virgin Islands, 35%. The same rates of tax apply to any gains made after a trust has been wound up.

Conclusion

Professional, expert advice is critical when attempting to plan and manage your finances, particularly if there are possible cross-jurisdictional and language issues to consider.

Portugal's taxation and succession laws differ markedly from those in the UK – sometimes they may work to your personal advantage, but at other times they may not. It is only by carrying out full analysis of your situation and with careful planning that you can feel confident of striking a balance that most closely aligns with the interests of you and your family.

At Blacktower, we understand that everyone is different and it is important that your adviser has an understanding of you, your circumstances, your long-term goals and your cash flow needs. We take the time to get to know you and will answer all your investing, saving and retirement planning questions so that we may provide a truly bespoke service.

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Tax Rates in Portugal

Not all capital gains are treated in the same way: some are added to income; others are taxed at a fixed rate, and others are exempt.

Income tax rates for 2019 income

INCOME	TAX RATES %	BAND €	TAX ON BAND €	CUMULATIVE TAX €
0 - 7,091	14.5%	7,091	1,028	1,028
7,092 - 10,700	23%	3,608	830	1,858
10,701 - 20,261	28.5%	9,561	2,725	4,583
20,262 - 25,000	35%	4,738	1,658	6,241
25,001 - 36,856	37%	11,655	4,386	10,627
36,857 - 80,640	45%	43,783	19,702	30,329
Over 80,641	48%	-	-	-

Interest earned from Portuguese bank accounts is paid subject to deduction of tax at 28%. However, habitual residents of the country can add this to other income for taxation at the standard scale rates.

For income derived from accounts outside Portugal either a 28% flat rate applies or the scale rates listed in the table above. Blacklisted 'tax havens' have interest taxed at a higher rate of 35%.

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