PORTUGAL: A RACE TOWARDS TAX COMPETITIVENESS – THE NON-HABITUAL TAX RESIDENT REGIME

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INTRODUCTION

In recent years, Portugal has introduced several measures that aim to promote foreign investment and the relocation of wealthy or highly-qualified individuals to Portugal. In this context, two new programs entered into force: (i) the Golden Visa, which is a temporary residence permit granted to foreign individuals who make an eligible investment in Portugal, and (ii) the Non-Habitual Tax Resident ("N.H.T.R.") regime, which is a more favorable tax regime granted to individuals moving to Portugal.

The purpose of this article is to address the main features of the new programs and to highlight the main planning opportunities that may arise for an individual wishing to become an N.H.T.R.

THE GOLDEN VISA AND THE NON-HABITUAL TAX RESIDENT REGIME

The Golden Visa

A non-E.U. citizen may only change residence to Portugal if a residence permit (or visa) is obtained. There are several types of available visas, such as student visas, entrepreneurs' visas, or work visas. In many instances, a non-E.U. citizen may encounter difficulty in obtaining a proper visa or may not meet the underlying requirements to obtain a visa.

To remedy this perceived issue, the Portuguese government introduced the Golden Visa[1] program, which grants a temporary residence permit to non-E.U. citizens making investments in eligible activity in Portugal. The law provides for several types of investment activities:

- Transference of capital into Portugal, in an amount equal to or higher than €1 million
- Creation of at least ten jobs
- Acquisition of real estate property in a minimum amount of €500,000.00

Recently, the list of investment activities was extended to include the following situations:

[1] Pursuant to article 90.º-A of Law No. 23/2007, of July 4 (Immigration Law).

- Transference of capital in an amount that is at least €350,000.00 to be used in scientific research activities conducted by public or private institutions that are part of the national scientific system

- Transference of capital in an amount that is at least €350,000.00 to be invested in or to support artistic productions or to maintain Portuguese cultural heritage

- Transference of capital in an amount that is at least €500,000.00 to be used in the purchase of real estate that is part of urban reconstruction

If the investment is conducted in places considered to be low-density areas, the minimum amount of required investment is reduced by 20%. Investments may be made directly by an individual or through a single-person limited company wholly-owned by the individual.

The Golden Visa is granted for five years and gives its holder the right to enter, live, and work in Portugal, provided that the stay in Portugal equals or exceeds seven days in the first year and 14 days in subsequent years. It also allows the holder to move freely within the Schengen area. Once granted, a Golden Visa gives its holder's family the right to obtain a residence permit without making any further investment, provided that certain conditions are met. Family members include: (i) the spouse, (ii) minor or disabled children, (iii) economically dependent adults, and (iv) parents. In addition, the holder of a Golden Visa may obtain a permanent residence permit and may apply for Portuguese citizenship, provided that certain conditions are met.

"Once granted, a Golden Visa gives its holder's family the right to obtain a residence permit without making any further investment, provided that certain conditions are met."

To apply for a Golden Visa, a non-E.U. citizen must file a request together with all the relevant documentation, such as a passport, evidence of legal entry into Portugal, health insurance, authorization allowing the Portuguese authorities to seek information regarding a possible criminal record, and proof of the eligible investment made.

The Non-Habitual Tax Resident Regime

E.U. residents wishing to move to Portugal and non-E.U. residents that have obtained a visa can apply for the N.H.T.R. regime. The N.H.T.R. regime establishes favorable tax treatment for individuals wishing to move to Portugal. It provides an exemption for foreign-source income and lower flat tax rates on Portuguese-source employment and self-employment income, provided the income arises from high value added activities.

To qualify for the N.H.T.R. status, an individual must meet the following tests:

- *Residence Criteria*: The individual must spend more than 183 days in Portugal in a 12-month period, beginning or ending in a given year. Alternatively, the individual must have a house available with regard to which the individual maintains an intent to occupy as a habitual abode on all days of presence in the 12-month period.

- *No Prior Residence Criteria*: The individual must not have been deemed a Portuguese tax resident under Portuguese domestic law and a double taxation treaty, if applicable, or must not have been taxed as a Portuguese tax resident in the preceding five years.

The main goal of this regime, introduced in 2009,[2] is to attract highly-qualified individuals and wealthy individuals to Portugal. In recent years, it has proven a success. When introduced, the N.H.T.R. regime required proof of residence outside of Portugal in the preceding five years. This required an individual to obtain residence certificates issued by tax authorities in other countries and proved to be cumbersome. For that reason, the procedures were simplified[3] and currently provide that an individual wishing to apply for the N.H.T.R. regime need only present a sworn statement evidencing that tax residence in Portugal did not exist during the preceding five years. Naturally, if the tax authorities question the veracity of the statement, the individual must demonstrate that taxes were paid as a tax resident in another jurisdiction during the entire five-year period.

The Portuguese government has published a list of the activities that qualify as "high value added activities of a scientific, artistic or technical nature."[4] Included are activities of

- auditors,
- medical doctors,
- engineers,
- teachers,
- investors,
- directors, and
- managers.

The employment or self-employment income derived from one of the listed activities can be taxed at a flat rate of 20%, if it is deemed to be of Portuguese source. It is exempt if it is of foreign source and is or may be taxed in its state of source in accordance with a double tax treaty entered into between Portugal and the state of source (or the O.E.C.D. Model Convention).[5] This exemption rule can represent attractive planning opportunities for individuals wishing to move to Portugal.

There are several instances where the exemption is allowed even though the income is not subject to tax abroad. One relates to pensions and the other relates to investment income:

- *Foreign Pensions*: Nonresident pensioners who move to Portugal may achieve a full exemption on foreign-source pensions because Portuguese law currently establishes an alternative to the subject-to-tax test. Under the alternative, foreign-source income that is deemed not to be obtained in Portugal can be exempt. When pension income is paid by an entity that does not have a head office or permanent establishment in Portugal, it is not obtained in Portugal.

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2 Decree-Law No. 249/2009, of September 23.

3 Following the publication of Order No. 9/2012.

4 Approved by Ministerial Order No. 12/2010, of January 7.

5 The exception is foreign-source employment income that needs to be effectively taxed in the state of source so as to benefit from an exemption in Portugal.

“The term ‘non-habitual resident’ can be misleading. To benefit from this regime, an individual must be deemed to be a tax resident in Portugal in each year.”

- <u>*Foreign Investment Income and Gains*</u>: Foreign-source investment income can be exempt if it may be taxed in the state of source, but the tax law in the country of source provides for no effective taxation of the income. Generally, this exemption applies to income from traditional investments generating interest and dividends. It does not apply to other forms of investment income. Portuguese domestic legislation contains a broad definition of the term “investment income.” Included, *inter alia*, are income items arising from

    - swaps,
    - life assurance products,
    - investment certificates, and
    - trust distributions.

    Regarding these latter investments, the understanding is that the exemption does not apply, so it is fundamental for an individual to evaluate and tailor an investment portfolio to become tax efficient under the N.H.T.R. regime or that an efficient ownership structure is put in place.

    The same concern over taxation exists for capital gains from the sale or exchange of movable assets. Most double tax treaties signed by Portugal provide that these gains can be taxed only in the state of residence, which in this case is Portugal. The logical conclusion is that such gains cannot be exempt in Portugal under the N.H.T.R. regime. Again, careful planning is required prior to the establishment of tax residence.

On a final point, an individual qualifying as an N.H.T.R. acquires the right to be taxed under that beneficial regime for a period of ten consecutive years. The term “non-habitual resident” can be misleading. To benefit from this regime, an individual must be deemed to be a tax resident in Portugal in each year.

CONCLUSION

The N.H.T.R. regime, together with the Golden Visa program, are excellent opportunities and incentives for nonresidents wishing to move to Portugal. In addition, Portugal does not have a wealth tax. While Portugal does not have an inheritance tax[6] on lifetime gifts and legacies at death, such transfers are subject to the Stamp Duty Code of 10% plus an additional tax of 0.8% for transfers of real estate.[7] Exemptions from the 10% tax are provided for lifetime transfers of property to a spouse, ascendants (*e.g.*, parents and grandparents), and descendants.

Finally, it should also be noted that Portugal offers other advantages that should not be disregarded, such as good weather, beautiful landscapes, great food, and welcoming people. For these reasons, coupled with the tax incentives described, Portugal has received in the recent years a significant number of N.H.T.R. applications. According to the data made available to the public, Portugal received 1,078 N.H.T.R. requests in 2013, and the number of requests is believed to have increased in 2014 and 2015.

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6 The newly appointed Portuguese government has disclosed plans to revisit the inheritance tax model, but it is uncertain to what extent it may change.

7 Stamp duty is a territorial tax, meaning that tax will only be levied on the assets deemed to be located in Portugal. Moreover, direct family benefits from a stamp duty exemption. The tax rate for donations and mortis causa transfers that are not exempt is 10%.