"NHR" status suffers another setback

Amendment to the tax treaty with Sweden ends the exemption for Swedish pensioners

Sweden is one of the countries protesting against the so-called Non-Habitual Residency Regime, accusing Portugal of promoting unfair tax competition within the European Union. To change the situation, Stockholm requested a review of the bilateral tax agreement with Portugal, similar to what Finland had done previously.

The amendments were signed in Brussels by Mário Centeno and his counterpart, Magdalena Andersson. When formally ratified, the new agreement will allow Sweden to tax pensioners who had registered in Portugal under the "NHR" scheme.

What is special about the "NHR" regime?

Created in 2009, the "NHR" scheme was sold politically as a special programme to attract "high-valued professionals" to Portugal. In reality, "NHR" been proved to be much more, offering a menu of tax breaks over a 10-year period on earned income:

i) a flat tax rate of 20% on "IRS" for "high-value" income earned in Portugal;

ii) double exemption for retirees who bring pensions from abroad;

iii) a potential exemption from the "IRS" on diverse sources of other foreign earned income.

To be eligible (whether a foreigner migrant or a returning Portuguese national), a citizen must not have resided in Portugal during the previous five years. Buying a home can often an indicator of this unusual fiscal status.

Double tax exemption on pension income: ***How is it possible*****?**

In ordinary taxation, a retired individual migrating to Portugal must pay "IRS" on pensions paid from abroad. Under "NHR", there is a double benefit: foreign pensioners not only do not have to pay "IRS" on their pensions from Portugal. They also are entitled to full tax exemption on their pensions in the country of origin, according to the relevant Double Taxation Agreement. This is due to a 'loophole' in tax agreements, signed decades ago when tax planning was less prevalent. The simple adhesion to "NHR" in Portugal prevents the foreign State from demanding tax where the pension is paid. It is this double exemption that has attracted many EU nationals to Portugal while provoking open hostility from tax offices around Europe, such as has occurred with Finland and Sweden.

What will happen next**?**

The signing of this rectification to the accord with Sweden kick-starts change in the tax agreement, and this 'loophole' will close. The amendment follows the same rule of the new treaty with Finland. That is, it gives the Swedish State the right to tax all the pensions it pays, with a transitional period of three years. If Portugal taxes pensions in the three years following the entry into force of the DTA, nothing will happen; if, on the other hand, the exemption is maintained, the Swedes can proceed with taxation in Sweden. But for this to happen, the agreement must first be ratified and signed. The tax treaty with Helsinki has as yet to be ratified and, for the time being, has been suspended.

Conclusion

The 10-year tax holiday that Portugal offers under "NHR" may be of little or no real benefit if other EU countries follow the model set forth by Finland and Sweden.

In the aftermath of the 2008 credit crisis, the EU proved tolerant of programmes such "NHR" in struggling countries like Portugal. However, economic recovery will inevitably mean the eventual return to a "level playing field" and the end of this form of tax competition within the European Union between its member states.

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