POTENTIAL PENSION EXCLUSION

I have heard that a portion of my pension might be excluded from assessment. Why is this so?

Contributions to pension plans normally have satisfied tax obligations in the fiscal year that they were made. Therefore, they can be protected from further assessment. According to Portuguese tax law, when made by the individual, they are assumed to be on an *after-tax* basis. When from the employer, certain basic criteria must be satisfied in order to qualify for a partial exclusion from taxation.

How does Portugal avoid potential double taxation?

Portuguese legislation defines a percentage of the pension to be excluded when formal criteria have been met. Originally 65%, this exception increased to 80% in 2007 and to 85% as of 2008.

How do other countries deal with this double taxation issue?

Internationally, in order to avoid double taxation, pensions are taxed in one of several ways:

a) on contributions going into the pension fund;
b) on cumulative growth of the fund;
c) upon payment of the pension;
d) a combination of the above.

For example, some countries explicitly exempt contributions in each year in which they are realised. Thus tax relief is granted up front. In others, retirees are entitled to a tax free "lump sum" on retirement. This constitutes a one-off settlement to eliminate double taxation. Subsequent pension disbursements are made on a normal tax basis. There are many other variants around the world.

How are pensions taxed under Non-Habitual Residency in Portugal?

Under the Non-Habitual Residency regime, Category H income (pensions) received abroad by non-habitual residents is exempt from tax in Portugal when:

1) for the part in which that income, where it arises from contributions, did not give rise to deduction (*for Social Security*) for the purposes of article 25º (2) of the Personal Income Tax Code;

2) or where:
   a) it is taxed in the State of origin in accordance with a Double Taxation Convention signed entered into by Portugal and that State; or
   b) in accordance with article 18º of the Personal Income Tax Code, it cannot be considered that this income was obtained in Portugal.

Despite being tax exempt under the conditions described above, this income must be aggregated in order to determine the tax rate applicable to the remaining taxable income.

Finally, because this status does not allow for a double exemption, it should be mentioned that the Decree-Law gives non-habitual residents the possibility to waive the right to exemption in favour of the method of tax credit.

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