



SIMPLIFIED REGIME SUMMARY
a programme that lives up to its name

The Simplified Regime, established in 2001, has had massive adherence by freelancers over the years. Currently, 99% of Freelancers in Portugal pay their IRS through this scheme. The Simplified Regime offers Sole traders a simple, cost-effective alternative to traditional profit/loss methods of accounting. With assessment based on a fixed percentage of gross invoicing, small independent businesses simplify record keeping, reduce taxes and increase productivity. Individual entrepreneurs whose annual turnover does not exceed €200,000 qualify for the Simplified Regime.

As the following chart illustrates, the Simplified Regime is not quite as simple as it used to be. Formerly with just two categories, the scheme has recently expanded to six. Under this method of assessment, taxpayers do not deduct professional and business expenses against their annual income with the exception of rental income which is reported net. Instead, taxable income is computed by applying the following coefficients to gross turnover:

Category B: Expanded Simplified Regime	Base
Sales of goods and services;	15%
Liberal Profession business activities (<i>profissões liberais</i>)	75%
Other income from services; Activities related to tourism	35%
Royalties, know-how, other income in connection with activity; Rental income not declared in Category F.	95%
Non-business related subsidies	30%
Business related subsidies; sources of income not listed	10%
Income taxed under Fiscal Transparency	100%



Clearly, a major innovation is in the sector of *Service Activities* with the distinction of “*Other Income from Services*”. Unlike most professional services (*profissões liberais*) that remain with an exclusion limited to 25% (professions usually requiring advanced degree qualifications as opposed to support services and vocational careers in non-academic skills and technical trades), *vocational services* are allowed to exclude up to 65% of their invoiced income. This means that final taxable income can be just 35% of gross turnover, taxed at marginal rates for residents and 25% for non-residents.

Filing your Income Tax Return

Having first opened your business activity (“*Início de Actividade*”), it will come time to settle up with the taxman after completing your first year. The fiscal year in Portugal corresponds to the calendar year. Business activity falls into Category B and is reported on “*Anexo B*” in April/May. Although many expenses do not enter into these calculations, you need to keep records of your expenses for reporting Value Added Tax (“*IVA*”). In year one, freelancers enjoy 50% “entrepreneur” reduction on their assessment. This tax relief reduces to 25% in the second year of business before normalising in the third year and beyond.

Starting in the third year of operation, you will need to pay estimated taxes in instalments. These Payments on Account are made in July, September and November with the final balance settled through the annual Income Tax declaration (“*IRS*”).

Example: A freelancer providing support services to businesses can qualify for a 65% exclusion on their invoiced income. A gross €30,000 annual income would be assessed ± €1,500 in “*IRS*” individual income tax. Compared to previous practices, based on the former prevailing 75% coefficient, the same income, would have paid over €4,500 in tax.



Those in *Sales* also enjoy a reduction with taxable income fixed at 15%. Taxation on €30,000 falls to €625, a net of just 2% of total turnover. Non-residents are levied at a flat rate of tax of 25% (a net of 3.75% of turnover).

“Holiday Lets” as a Tourist Business

If you let out furnished accommodations to holidaymakers on a short term basis, this type of activity is also taxed on 35% of invoiced income. For non-residents, this equates to an effective tax rate of less than 9% of gross income versus the existing 28% rate for long-term rental income. Residents aggregate with other forms of declared income and are assessed at marginal rates.

Also important for non-residents, according to Double Taxation Treaties throughout the EU, there should be no further assessment in your home jurisdiction as this income should be exclusively taxable in Portugal, classified as “business profits”.

Valued Added Tax (“IVA”)

When your income exceeds €10,000, you will automatically be included in the VAT regime in the following year. The percentage that you charge your clients (23%, 13% or 6%) depends on the nature of your business activity. On a quarterly basis, you report the VAT that you have collected as well as the “IVA” that you paid on your business expenses, reporting the balance. If in favour of the State, you pay the difference to *Finanças*. If you paid more than you received, you will be entitled to a refund. When invoicing clients in the EU, the “Reverse Charge” principle normally applies. This means that you don’t charge VAT and can reclaim the VAT charged on your business expenses.

Social Security

Monthly Social Security contributions normally begin the second year of business activity unless an exemption applies. Deductions are according to the amount of income actually received, based on IRS declarations in the preceding quarter. Workers will automatically be placed into a deduction category by Social Security: 70% of income from services and 20% for Sales



serve as the contributory base. As of 2019, most freelancers make Social Security contributions at the rate of 21.4%. For services, that's a net rate of 15%. Also in 2019, Local Lodging activities are exempt from Social Security contributions. Freelancers with small incomes may also claim an exemption. Self-employed individuals must declare their income to Social Security each quarter. The 2019 regime also creates a minimum monthly contribution of €20 to guarantee stability and continuity over the course of one's contributory career to assure future pension entitlements as well as other social benefits associated with occurrences of unemployment or illness.

NHR and the Simplified Regime

The Non-Habitual Residency (NHR) programme has been successful in attracting freelancers to Portugal from around the world. While NHR offers pensioners a 10-year tax-free holiday and wealthy executives a modest 20% flat assessment on six-figure salaries, this solution can leave much to be desired for freelancers. In fact, a better option already exists for “gig economy” freelancers in the Simplified Regime, the standard means of assessment used by the vast majority of entrepreneurs in Portugal.

Conclusion

Many will applaud these incentives. Not just because they will pay less tax but, equally important, these measures promote growth and reward compliance, fundamental values at the heart of any sustainable tax system. There is probably no faster or better way to promote employment. Entrepreneurial spirit is fostered, self-reliance encouraged, two more essential values at the heart of any healthy economy.

*With **euroFINESCO** at your side to meet your business compliance obligations, not only will you be off to a good start, you can find opportunities to mitigate tax while better serving your clients throughout the EU and around the world.*

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