# THE PRIVATE WEALTH AND PRIVATE CLIENT REVIEW

ELEVENTH EDITION

**Editor**
John Riches

THE LAWREVIEWS

# THE PRIVATE WEALTH AND PRIVATE CLIENT REVIEW

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# PREFACE

*It is not so long ago that a member of the Diplomatic Body in London, who had spent some years of his service in China, told me that there was a Chinese curse which took the form of saying, 'May you live in interesting times.' There is no doubt that the curse has fallen on us.*
Austen Chamberlain, March 1936

Undoubtedly, many periods in history may lay claim to be 'interesting times', and 2022 is one of them. A confluence of factors has changed the global landscape, not least the aftermath of the covid-19 pandemic, global supply chain disruption, the invasion of Ukraine and the global economy's transition to a post-covid world. There is also the looming prospect of climate change, which will only become more pressing. While there have been periods of high inflationary pressure before, never before have individuals, companies and jurisdictions been so globalised and interconnected. While good advisers should always ensure they are au fait with changes that may impact their clients, never before has it been as important for advisers to be scanning the horizon for upcoming legislative, tax, political and economic factors.

One interesting trend that has emerged over recent months is the migration of high net worth individuals (HNWIs) in response to economic and political uncertainty. Visual Capitalist have drawn up a global map showing predicted net emigration and immigration of individuals having wealth of over US$1 million.[1] While there are some foreseeable emigrations, with 2,800 HNWIs estimated to emigrate from Ukraine in 2022, 3,500 HNWIs to emigrate from Hong Kong and 15,000 HNWIs to emigrate from Russia, there are also some surprises. Eight hundred HNWIs are predicted to emigrate from Mexico, 2,500 from Brazil, 8,000 from India, 600 from Saudi Arabia, 1,500 from the UK, 10,000 from China and 600 from Indonesia.

On the immigration side, 800 HNWIs are projected to move to New Zealand in 2022, with 3,500 HNWIs to Australia in 2022, and Visual Capitalist report that approximately 80,000 millionaires have moved to Australia since the turn of the millennium. Meanwhile, Singapore is likely to attract 2,800 HNWIs, 4,000 to the United Arab Emirates, 2,500 to Israel and 2,200 to Switzerland. The US will likely attract 1,500 HNWIs, with Canada close behind in attracting 1,000 HNWIs. Finally, jurisdictions in Western Europe, which are maturing their limited tax regimes (Portugal, Italy and Greece), appear to be attracting HNWIs. Portugal is estimated to attract 1,300 HNWIs in 2022, with Greece not far behind

1 https://www.visualcapitalist.com/migration-of-millionaires-worldwide-2022/.

in attracting 1,200 HNWIs. Such a diverse diaspora shows that in 2022, HNWIs are still prepared to move to more attractive and favourable jurisdictions, and even to pay higher tax rates, in search of political and economic stability.

Meanwhile, other HNWIs are not necessarily emigrating, but instead taking advantage of remote working practices to split their time between jurisdictions, potentially becoming tax resident in a second or third country. This leads to increasing regulation and complexity, in both the tax and the automatic exchange of information spheres. The year 2021 saw the groundbreaking multinational agreement between 136 countries for a global minimum tax rate of 15 per cent for corporate entities to counteract tax avoidance and base erosion profit shifting. The intention is for this to commence in 2023, and it will apply to multi-national entities with an annual revenue exceeding €750 million. While the focus of this new regime is large corporate entities, the current drafting of the OECD's Global Anti-Base Erosion Model Rules (the 'Globe Rules') does in principle apply to trusts where they act as the ultimate holding entity of a multi-national group. The qualifying annual revenue threshold of €750 million under the Globe Rules will preclude their application to virtually all trusts owning businesses. However, it is conceivable that, in future, this threshold may be materially reduced – if so, it would not be the first time that trusts are caught up within reporting and regulatory regimes designed to apply primarily to corporate groups.

As expected, the global transparency agenda shows no signs of slowing down, and is instead evolving into ever-increasing areas. In such an arena, does asset protection for HNWIs become more important? While sanctions against targeted individuals are a useful tool against money laundering, terrorist financing and humanitarian crimes, indiscriminate blanket sanctions can harm innocent individuals. Individuals and families holding Russian passports, who did not hold an EU passport, and who were critical of the invasion of Ukraine, found themselves having to search for new trustees and trust management services after the EU brought in a blanket ban against Russian passport holders who did not also have an EU passport. Meanwhile, less than a year on from the Pandora Papers leak in October 2021, HNWIs looking for privacy are increasingly looking to 'mid-shore' as opposed to 'off-shore' jurisdictions for asset protection. Jurisdictions such as the United States and Singapore seem to feature increasingly as locations where families are looking to establish holding structures.

Furthermore, in recognition of the increasing trend for transparency in real estate holdings, the UK has introduced 'The Register of Overseas Entities'. While the UK has a Land Registry that is a public register of the owners of all registered land in the country, it only requires information on the legal owner, which can be a nominee, trustee, company or another corporate entity. This new register will require any non-UK entity (e.g., a non-UK company that owns UK land) to register the beneficial owner of the land at UK Companies House. This law will have retrospective effect in England and Wales for any property bought since January 1999 and in Scotland from 2014; the anticipated commencement date is likely to be in early 2023. This latest transparency initiative uses the principles that apply to beneficial ownership of UK companies, which have been obliged to register their beneficial owners since April 2016. There are limited exemptions from registering, namely (1) the interests of national security; (2) the interest of the economic wellbeing of the UK; and (3) to prevent or detect serious crime. The way in which trustee owners of UK property register is far from straightforward; there will be an obligation to update the register annually where changes in ownership occur.

Meanwhile, the UK's trust register legislation has been updated to extend the reporting period from 30 to 90 days, and to exclude some low-risk trusts from registration, including life insurance trusts with death-only benefits, and bank accounts for those who are not sui iuris, (i.e., minors or those who do not have mental capacity). However, despite the removal of these low-risk trusts from the requirement to register, bare trusts and nomineeships will now be required to register by September 2022, which will affect a number of clients. The minister responsible for the amendments to the trust register, Baroness Penn of the House of Lords, explained that they had been implemented to ensure that the trust register 'strikes the right balance between the public interest in tackling money laundering and the right to privacy for those who use trusts for legitimate purposes'.[2]

The UK trust register information is currently only available to law enforcement agencies upon request. However, under the new amendments, which will take effect from 1 September 2022, any third party who can demonstrate a 'legitimate interest' will be able to request information on the register. Such a 'legitimate interest' requires the requester to be investigating a 'specified specific instance of money laundering or terrorist financing', and it must be 'reasonable for the requester to have that suspicion, among other requirements'.[3] In an encouraging understanding of the use of trusts for legitimate purposes, Baroness Penn further added that:

> *We believe that placing the information held on the trust register in the public domain would infringe the privacy rights of individual beneficial owners, the vast majority of whom are not involved in money laundering activities. However, we recognise that, for the register to be an effective anti-money laundering tool, the information must be made available to those who are at the forefront of anti-money laundering investigations.*[4]

The transparency regime is now slowly turning its gaze on cryptocurrency, with reports that some sanctioned individuals are using cryptocurrency to obscure their identity. Under the French implementation of the EU's Fifth Anti-Money Laundering Directive (5AMLD) in early 2020, any cryptocurrency firm with French clients or which operates in France must register with the French regulator, the Autorité des Marchés Financiers (the AMF) and the KYC limit for cryptocurrency transactions was reduced from €1000 to €0. It will be interesting to see whether 5AMLD will be extended or updated to require a public or semi-public register in relation to the beneficial owners of cryptocurrency in the future. Across the Atlantic in the US, the new Corporate Transparency Act comes into effect later in 2022 or latest in early 2023. This will require all domestic and non-US corporate entities to register their information and that of their legal and beneficial owners with the US Treasury Department and it is estimated that it will affect over 20 million businesses. There are currently no plans for the registers (which will be maintained at state level) to be made public.

2 *Hansard*. HL. Deb. Vol. 818, col. 388GC, 8 February 2022.

3 HMRC Internal Manual Trust Registration Service Manual, TRSM60020 – Third party access requests: contents: legitimate interest requests.

4 *Hansard*. HL. Deb. Vol. 818, col. 391GC, 8 February 2022.

What seems clear is that the plethora of initiatives that impact the private wealth arena continues to increase exponentially. These are interesting times and advisers need to remain alert to ensure they can give rounded advice that affects clients of all shapes and sizes.

**John Riches**
RMW Law LLP
London
July 2022

**Chapter 22**

# PORTUGAL

*Tiago Marreiros Moreira and João Riscado Rapoula*[1]

## I INTRODUCTION

Portugal has cemented its status as one of the most interesting jurisdictions for high net worth individuals (HNWI) in recent years.

The flexibility of the residence permit regimes for non-EU citizens (in particular the Residence Permit for Investment Activity, commonly known as the Golden Visa programme), together with the non-habitual tax resident regime (NHR) provided for a significant push to foster the attractiveness of Portugal. Moreover, the fact that Portugal (1) remains a jurisdiction that does not levy wealth taxes; (2) imposes taxes on donations on a territorial basis (e.g., only assets located in Portugal may trigger tax), although an exemption applies for free transfers between spouses, ascendants and descendants; and (3) does not levy succession taxes still contributes decisively for the significant flow of HNWI who see Portugal as the perfect jurisdiction to relocate to.

In addition, from the perspective of new trends in investment, such as cryptocurrencies and NFTs, Portugal is a top choice for investors as currently, as a general rule, it does not levy any taxes on gains resulting from these assets, unless such gains result from a business activity, as explained below.

In addition to the above, perhaps one of the most interesting – and less known – features of the Portuguese legal system is the legal certainty on which it relies. Indeed, with regard, for instance, to the NHR, there was a relevant change to the rules which went from providing for an exemption to foreign-source pension income to establishing a flat tax rate of 10 per cent. However, the law that amended this rule (the Portuguese Budget Law for 2020) has expressly safeguarded the situation of the individuals who were already under the NHR, by establishing that this amendment would only be applicable to those who would relocate to Portugal upon the enactment of the new law. This example aims at illustrating how stable the Portuguese tax law has been in recent years, which is undoubtedly an invaluable feature of a jurisdiction that needs to attract foreign investment and, in particular, HNWI.

The uncertain international setting triggered by the covid-19 pandemic and aggravated by the conflict in Ukraine, along with the safety and quality of living in Portugal, its geographical location, the opportunities that the Portuguese real estate market still offers and the openness of the country to investors on the agricultural sector and clean energies, keep our jurisdiction as one of the top-ranked places to live and to invest in a sustainable way, allowing us to look at the future of Portugal as a top destination for HWNI with clear optimism.

1 Tiago Marreiros Moreira is a partner and João Riscado Rapoula is a managing associate at Vieira de Almeida.

## II TAX

### i Overview

The Portuguese personal income tax (PIT) relies on tax residence as the most relevant criterion. Portuguese tax resident individuals are subject to PIT on a worldwide basis, whereas Portuguese non-resident individuals are only subject to tax on Portuguese sourced income.

An individual is deemed to be resident in Portugal if they can satisfy one of the following conditions:

*a* the individual remains in Portuguese territory for more than 183 days, consecutive or not, in any 12-month period commencing or ending in the relevant calendar year;

*b* though remaining for less than 183 days, the individual has, in any 12-month period of the relevant year, accommodation under circumstances that indicate an intention to keep and occupy it as a habitual residence;

*c* on 31 December of any given year, the individual is a crew member of vessels or aircrafts operated by entities with residence, head office or place of effective management in Portuguese territory; and

*d* the individual performs public duties for the Portuguese state abroad.

The NHR applies to any individual taxpayer who transfers the tax residence to Portugal, on the sole condition that such taxpayer did not qualify as a Portuguese tax resident in any of the five years prior to the application to this regime. The NHR does not require the individual to be professionally active, nor does it require minimum personal wealth or income thresholds. Moreover, this regime applies for a 10-year period counted from the year of arrival to Portugal (included).

PIT applies to specific items of income that are expressly set forth under the PIT Code: employment income, business and professional income, capital income (e.g., dividends, interest, royalties), real estate income, net worth increases (e.g., gains from the sale of real estate property or securities, proceeds from the liquidation of companies, non-compete compensations) and pensions.

For 2022, for regular tax residents, income will be taxed at the general progressive tax rates ranging from 14.5 per cent to 48 per cent, depending on the amount of income obtained by the taxpayer in the given tax year. For individuals whose income exceeds €80,000 but remains below €250,000, a solidarity surcharge of 2.5 per cent will also be due on income that exceeds the mentioned, threshold. Income in excess of €250,000 will also be subject to the solidarity surcharge at 5 per cent.

For certain items of income, as it is the case of capital income (such as dividends, interest and royalties) and capital gains derived from the sale of financial assets, will be subject to PIT at a flat rate of 28 per cent, except if the taxpayer opts to include these items of income in their general income that will be subject to PIT under the progressive rates (such option would only make sense, of course, if the effective progressive tax rate of the individual would be lower than 28 per cent).

With regard to resident individuals under the NHR, the applicable benefits range from a full exemption on certain types of foreign-sourced income and a reduced flat tax rate of 20 per cent to other types of Portuguese-sourced income.

In particular, passive income derived outside Portugal (e.g., dividends, interest and rental income) from non blacklisted jurisdictions is fully exempt in Portugal. This exemption applies irrespective of the taxation applicable at source. Capital gains resulting from the sale or redemption of securities remain, as a general rule, taxable at a rate of 28 per cent and pension income is taxable at a rate of 10 per cent.

Active income (e.g., income from employment and also from self-employment derived in connection with 'high value-added activities') may also be fully exempt provided specific conditions are met. The activities qualified as high value-added are identified in a statutory shortlist (published in the Ministerial Order No. 230/2019) that includes certain teachers, science and engineering technicians and professionals, general directors and executive managers of companies and IT professionals, among others. Portuguese-sourced active income derived in connection with high value-added activities will be subject to a flat rate of 20 per cent (instead of the general progressive tax rates).

In the specific case of fiduciary structures (e.g., trusts), we note that regular distributions qualify as capital income whereas proceeds resulting from the liquidation of foreign structures whose settlor is a third party are not subject to personal income tax.

It is also relevant to consider that Portugal does not impose an exit tax when a tax resident individual leaves. However, Portuguese tax residents who exchange shares or own shares in a company, which was subject to a merger or a division, and subsequently transfer their place of residence abroad, must include any capital gain or loss arising from the share exchange, merger or division in their taxable income for the year in which they cease to be resident in Portugal, and, consequently, be subject to tax.

The extensive network of double tax treaties (DTT) concluded by Portugal with other jurisdictions ensures that in the vast majority of cross-border transactions and income flows, an individual's income will not be subject to double taxation either through a tax exemption or a tax credit conferred by Portugal or the other relevant jurisdiction.

### ii The current status of new investment trends

#### *Cryptocurrency*

Cryptocurrency transactions are not yet subject to a clear tax regime in Portugal as the PIT Code does not provide for specific rules on this matter. However, we understand that the taxation of cryptocurrency transactions could potentially fall under two main categories: capital income or net worth increases as capital gains. While the former is typically associated with a return on invested capital, the latter corresponds to the (taxable) difference on the trading of securities.

The trading of cryptocurrency should not be qualified as investment income, because the revenues derived by the investor are not a return on capital, but are rather the net proceeds from the disposal of cryptocurrency. Therefore, the most adequate framework would be the taxation of cryptocurrency trading under the category of capital gains.

Given that under Portuguese law, taxation depends on the qualification of an item of income under a specific category of taxable income, it should be noted, as a starting point, that currency gains are generally not taxable transactions, which could lead to the conclusion that cryptocurrency gains should also fall outside the scope of PIT. It should be pointed out, in any event, that gains resulting from currency-related transactions covering financial derivatives may be taxable. Nevertheless, cryptocurrency should better fall under the qualification of a true means of payment, pursuant to European Court of Justice case law, and therefore should be treated as currency and not a financial derivative.

Therefore, under the current Portuguese tax law, gains with cryptocurrency trading should not be taxable in Portugal.

Despite that cryptocurrency trading is an innovative type of investment and is not yet subject to a specific tax regime, we underline that the Portuguese tax authorities (PTA) have already issued guidance on the matter,[2] confirming that gains arising from the trading of cryptocurrency do not fall under any of the PIT categories of income and are not subject to taxation. However, the PTA raised an additional option, in case the cryptocurrency trading is carried out on a recurrent manner (literally, with a 'habitual nature' and a 'profit-oriented manner'). The PTA consider that gains arising from the trading of cryptocurrency may qualify as business income if the taxpayer actively and habitually trades cryptocurrency.

This setting proposed by the PTA is not adequately supported from a technical standpoint. Indeed, the PTA argue that the habitual trading of cryptocurrency should be assimilated to a professional activity, such as the provision of services or the sale of goods. Such assimilation results from the 'habitual nature' and the 'profit-oriented manner' of the activity, although there is no further clarification on the characterisation of cryptocurrency trading as a business.

In addition, the Portuguese case law has recognised several times that the classification as commercial or business activity implies the existence of an increase in the value of the asset by virtue of the exercise of the activity, resulting in the creation of economic utility and also the existence of a relationship between the business agent and a third party. It is clear that the cryptocurrency trading neither implies any added value by the economic agent, nor a relationship between the holders and third parties (i.e., there is no act of commerce). In fact, the gains or losses result from the fluctuations on the value of the cryptocurrency.

Therefore, we take the view that cryptocurrency trading (like the management of a portfolio of financial assets for the personal benefit of the investor) should not qualify as business income as it is not a commercial activity.

***Gains with non-fungible tokens***

According to the Portuguese tax law, income is only subject to PIT provided that it falls under one of the categories of income. Hence, no taxation will be levied on income that is not qualified as taxable income pursuant to the PIT Code.

To date, non-fungible token (NFT) transactions are not subject to a clear tax regime, as the PIT Code does not provide for specific rules on this matter. Given that taxation depends on the qualification of an item of income under a specific category, we note that, as a starting point, it is important to define if NFTs may be deemed as a financial investment or if their sale shall be considered a regular sale of goods.

Taking the above into consideration, the PTA may only consider NFTs a financial asset if the investment is made typically via an exchanged-traded fund (ETF) (or investment fund oriented to invest in NFTs). Being that the case, any gains resulting from the sale of the ETF or the units of the investment fund would qualify as capital gains.

On the other hand, the sale of NFTs as a regular sale of goods will not be subject to tax in Portugal because of the absence of a specific rule governing this type of gain.

However, if the sale of NFTs is carried out on a recurrent manner (i.e., with a habitual nature and a profit-oriented manner) the PTA's aforementioned position on the ruling of

2 Tax Ruling of 27 December 2016, DSIRS Proc.: 5717/2015, published on the PTA website at https://info.portaldasfinancas.gov.pt/pt/informacao_fiscal/informacoes_vinculativas/rendimento/cirs/Documents/PIV_09541.pdf.

cryptocurrencies may lead to the qualification of this type of income as a business income derived from a commercial activity, even though, for the reasons explained above, the authors do not follow the position of the PTA.

With regard to NFTs., it is also worth mentioning that the Portuguese domestic tax law does not include any specific rules to address taxation of artworks. Indeed, as a general rule, capital gains derived from the sale of artworks are not subject to PIT and there is no obligation of declaring or disclosing private artworks to any Portuguese authority.

However, should an individual engage in a professional activity related to the sale of artworks, any capital gains derived from the sales will be qualified as business income.

### iii Amendments to tax law for 2022

#### *Capital gains*

In what concerns relevant developments of the Portuguese tax system, the recently approved State Budget Law for 2022, which entered into force on 1 July, has introduced relevant amendments regarding the taxation of capital gains derived from the sale of assets, other than real estate.

As referred above, currently, capital gains with the sale of securities are subject to tax in Portugal, at a flat rate of 28 per cent levied on the year-end net capital gain (i.e., after offsetting losses). However, the State Budget Law for 2022 foresees that, from 1 January 2023 onwards, the positive balance between capital gains and capital losses arising from the transfer for consideration of shares and other securities, is mandatorily aggregated and taxed at progressive rates if the assets have been held for less than 365 days and the taxable income of the taxpayer, including the balance of the capital gains and capital losses, amounts to or exceeds €75,009.

The said amendment raises some questions regarding whether it is in breach of the Portuguese Constitution. Indeed, the Portuguese Constitution establishes that individuals should be taxed in accordance with their ability to pay taxes. Because the regime approved by the State Budget Law for 2022 allows individuals to be taxed under significantly different tax rates (28 per cent versus the progressive tax rates, which may go up to 48 per cent, accrued with solidarity surcharge), for the same item of income, solely on the basis of the period for which the asset has been held, it will not be surprising if the constitutionality of this amendment is challenged in the Portuguese courts.

Moreover, this amendment also reflects to some extent an incoherence regarding how the disposal of assets may lead to different outcomes: on the one hand, traditional financial assets (such as bonds or shares) lead necessarily to taxation, whereas gains from trading cryptocurrency or NFTs are yet to be subject to a clear tax regime and currently are left outside the scope of PIT.

The State Budget Law for 2022 includes another amendment related to the taxation of capital gains derived from the sale of assets other than real estate property (e.g., shares or any other financial assets), in a scenario where the taxpayer has acquired such assets by donation.

Under the regime in force previously to the approval of the State Budget Law for 2022, the taxable income derived from the sale of assets different than real estate, that had been acquired by the taxpayer through a donation made by a spouse, ascendant or descendant, was determined by offsetting the value of the asset in question (ascertained in the moment of the donation under the rules of the stamp duty code, applicable to gifts) to the proceeds obtained with the sale of the asset.

The State Budget Law for 2022 now determines that, in the above-mentioned scenario, the acquisition value of the donated assets should be the value that would be considered for stamp duty purposes until the two years prior to the donation. Such amendment can have a significant impact on the determination of the taxable income resulting from the sale of the assets and is intended to tackle situations where a latent gain is eliminated through a donation that would allow for a step-up in the acquisition value of the asset at the level of the beneficiary, in particular in those cases where a sudden appreciation in the value of the asset occurs.

However, again the ability to pay taxes principle seems somewhat to be jeopardised by a rule which establishes as the purchase price – key to the determination of the taxable capital gain – the value of the shares (as determined by the Portuguese Stamp Duty Code) by reference to a period of two years prior to the donation, which may lead to situations where the taxable gain will overcome the real gain of the individual. This rule also raises challenges as to its constitutionality.

One final note regarding the Portuguese Budget Law for 2022, as it includes a rule according to which any gains with the assignment of a contractual position in fiduciary structures (including the status of beneficiary) shall also qualify as capital gains. The authors find this rule quite peculiar, especially if we consider a situation of a trust, where, for instance, the position of beneficiary is not 'an asset' that may be subject to a transaction as it is usually defined by third parties, such as the settlor or the trustees.

## III SUCCESSION

There has been no inheritance and gift tax regime in Portugal since 1 January 2004. However, the transfer of assets by way of inheritance or gift may be subject to stamp duty, if the assets are located in Portugal. In particular, the free transfer of assets (inheritance and gifts) may be subject to a 10 per cent tax rate (if the transfer refers to real estate, an additional stamp duty at 0.8 per cent will also be due (Stamp Duty Code)). There is an exemption applicable to free transfer of assets made between spouses or unmarried partners, descendants and ascendants.

Successions are governed by the law of the last residence of the deceased (Regulation (EU) 650/2012 on jurisdiction, applicable law, recognition and enforcement of decisions and acceptance and enforcement of authentic instruments in matters of succession and on the creation of a European Certificate of Succession (Succession Regulation)). However, resident individuals can choose to regulate their succession in accordance with the law of the state of where they are nationals.

When the Succession Regulation is not applicable, the Portuguese domestic conflict rule determines that the applicable law on succession matters is the personal law of the deceased (which is usually the nationality law).

The Portuguese succession regime remained unchanged for the past few years. Under Portuguese law, succession may qualify as:

*a* mandatory;
*b* testamentary (i.e., through a will); and
*c* legal (residual succession, which applies when there is no mandatory legal succession and the testamentary succession does not deal with all the assets of the deceased).

Under a mandatory legal succession, half or two-thirds of the inheritance must be granted to the spouse and the direct descendants and ascendants. The remaining assets can be disposed by means of testamentary succession or will be distributed to the following heirs entitled to the legal succession:

*a* spouse and descendants;
*b* spouse and ascendants;
*c* siblings and their descendants;
*d* other relatives; and
*e* the Portuguese state.

Portuguese domestic civil law allows for the recognition of foreign wills, under the general rule in the Portuguese Civil Code, which states that legal documents or transactions taking place in other countries may be recognised in Portugal if they are legal in the country in which occurred. However, the Portuguese Civil Code requires foreign wills to have a minimum solemn form (for example, if it is made before a notary). According to Portuguese case law, if the will complies with the formal rules in force in the foreign country in which it was made, it should in principle be accepted in Portugal.

The key takeaway is that because of the mandatory rules established by the Portuguese legislation on the distribution of assets (e.g., only half or one-third of the estate can be available to other individuals or entities, because the remaining is reserved to the legal heirs of the deceased), whenever the Portuguese law applies to a succession there might by incompatibilities between a given structure that ought to manage a given estate for the benefit of a group of individuals and the entitlement to such assets of the mandatory legal heirs.

## IV WEALTH STRUCTURING AND REGULATION

Any foreign structure held by a Portuguese resident individual which is located outside the Portuguese territory may raise challenges, taking into account some specific provisions of the Portuguese domestic law.

The first set of rules to point out relates to controlled foreign company (CFC) legislation, which aims at avoiding the deferral (or even elimination) of taxation of income by means of the use of entities that are either located in low-tax jurisdictions or that are not subject to tax on their profits.

CFC rules apply to resident individuals that hold, directly or indirectly, a significant interest in non-resident entities subject to a more favourable tax regime. For this purpose, the non-resident entity is deemed to have a favourable tax regime not only when located in a black-listed jurisdiction, but also when such entity is either fully exempt or subject to an income tax rate lower than 10.5 per cent (i.e., less than 50 per cent of the Portuguese Corporate Income Tax (CIT), due if the company was Portuguese).

According to this set of rules, the income derived by the foreign entity is allocated to the Portuguese-resident shareholder irrespective of any distribution. In particular, the profits of the foreign company may not consist in more than 25 per cent of:

*a* royalties or any other income generated from intellectual property, image rights or similar;
*b* dividends and income from the disposal of shares;
*c* income from financial leasing;

*d* income from insurance, banking (even if not performed by credit institutions), insurance and other financial activities contracted with entities with special relationships;
*e* income from invoicing companies that earn sales and services income from goods and services purchased from and sold to associated enterprises, and add no or little economic value; and
*f* interests or any other income generated by financial assets.

Another rule to highlight relates to the presence of entrepreneurs who manage their international business from the Portuguese territory. Under the CIT Code, companies are taxed in Portugal on their worldwide profits in the event they are resident for tax purposes in Portugal. A company is deemed to be resident in Portugal if it has its corporate seat or (alternatively) its place of effective management in Portugal. Although there are no legal criteria to define where the place of effective management is located, according to Portuguese case law, 'place of effective management' might be defined as the place where the most relevant decisions are taken (e.g., where the board meetings take place) and where adequate substance (e.g., people and buildings) is present.

For instance, depending on the structure of the board of directors of the companies, if the sole shareholder and the CEO of a given company is the sole presence of that company in Portugal, while the relevant decisions are taken in board meetings which take place in abroad, we take the view that the 'place of effective management' rule should not apply. On the other hand, if no board of directors exist or if no relevant decisions are being executed from abroad, that company may indeed be deemed as Portuguese resident, which would lead to corporate taxation in Portugal based on the aforementioned rule.

Moreover, the presence of a CEO in Portugal may also raise questions as to whether the foreign company may have a permanent establishment (PE) in the Portuguese territory, which would also lead to corporate taxation of the companies in Portugal to the extent there were profits attributable to such PE.

Finally, it is also important to point out that the Portuguese tax law includes a general anti-abuse rule (GAAR) that allows PTA to disregard corporate entities without proper economic substance (i.e., that were created having as their sole or main purpose the obtaining of tax advantages).

The above-mentioned remarks regarding CFC legislation, place of effective management and the general anti-abuse clause aim at pointing out that any wealth structuring which includes a foreign corporate structure without proper substance or an economic rationale behind it may raise challenges.

In addition, the proposal for the implementation of the EU's Anti-Tax Avoidance Directive 3 will bring another layer of challenges to corporate or fiduciary structures, which may ultimately lead to situations where these entities are denied tax residence certificates, preventing them having access to DTTs.

At the internal level, the PTA have issued a recent ruling regarding the tax treatment of distributions made by any *société d'investissement à capital variable* (SICAV funds).[3]

The ruling in question analyses how distributions made by SICAV funds to Portuguese tax residents who benefit from the NHR should be taxed and considers the possibility of treating this type of income as a dividend for the purposes of application of DTTs. Should this type of income be treated as a dividend, then, in principle, it would be subject to taxation

3 Ruling No. 755/2018, published on 2 May 2022.

at the source state as determined by the DTT concluded between Portugal and Luxembourg, which would imply that this item of income should not be subject to PIT in Portugal under the NHR rules.

In the ruling, the PTA resort to the Commentaries to the OECD's Model Convention to Avoid Double Taxation to determine if this type of distribution should be treated as a dividend for the purposes of applying the Portugal–Luxembourg DTT. Because the mentioned commentaries do not provide a closed definition of what types of income should be included in the concept of dividends, and considering that the commentaries also mentioned that such definition is impossible, considering the disparities in the internal legislations of OECD jurisdictions, the PTA concluded that distributions made by investment funds should not be comparable to profit distributions made by companies to shareholders and, therefore, should have a different tax treatment and not be regarded as dividends for the purposes of application of the DTT. As such, the PTA claimed that these distributions should be treated as 'other income' under the applicable DTT and be exclusively taxed on the jurisdiction where the taxpayer is resident. Therefore, the exemption under the NHR rules would not be applicable in Portugal and these distributions should be subject to PIT at a 28 per cent rate.

The conclusions expressed in the mentioned ruling are difficult to justify considering that it seems to ignore the broad concept of 'dividend' under the applicable DTT which includes income from shares, privileged shares or other rights, not being debt-claims, participating in profits, as well as income from other corporate rights which are subjected to the same taxation treatment as income from shares by the laws of the state of which the company making the distribution is a resident. Not only does the ruling fail to address the nature of the SICAV to assess whether or not the holder of the units has a corporate right but it also does not include any reference to the treatment in Luxembourg of distributions made by these entities and whether or not such distributions have a similar tax treatment as the one applicable to dividends.

The position expressed on this ruling by the PTA should probably trigger litigation as it is far from being well grounded and it seems not to be aligned with the correct application of the concept of dividends in DTTs.

This highlights that any individuals who relocate to Portugal and benefit from the NHR may enjoy an exemption of foreign-source dividend and interest provided the income is not sourced in a black-listed jurisdiction. These features of the NHR and the challenges raised by foreign corporate structures that may be used for wealth planning purposes seem to imply that for HNWI relocating to Portugal, holding assets at the personal level – at least for the 10-year period the NHR lasts – may not be a bad idea.

However, it is surprising that, in the context of US LLCs (tax transparent entities), the tax treatment of transparent entities has already been clarified by the PTA in (at least) two tax rulings.[4]

The PTA have considered that profit distributions from United States LLCs – to their shareholders who are resident for tax purposes in Portugal – should be qualified as investment income, even though the distributions are not an actual dividend for tax purposes (given the tax transparent treatment provided by US domestic law).

Regarding the income qualification for double tax convention (DTC) purposes, in both cases the PTA considered that the distribution of revenues accrued at the level of the US

4 For example, tax Ruling of 20 December 2017, DSIRS Proc.: 2360/2016.

LLC should fall within the 'other income' provision of the DTC celebrated between Portugal and the United States, which provides for shared taxing jurisdiction, hence triggering the exemption of tax for individuals under the NHR.

Also, no CFC rules were raised by the PTA on the LLC structure, which makes it attractive for HNWI who have their estate based in the United States, in view of a relocation to Portugal, despite all the reserves that may result from the anti-abuse provisions established by Portuguese domestic law.

## V OUTLOOK AND CONCLUSIONS

Considering the discussed topics and in spite of the internal and international tax landscape becoming more complex and aware of potentially abusive situations, Portugal remains an interesting jurisdiction to HNWI who intend to relocate or to structure their wealth. Mainly, the possibility of benefitting from the NHR regime and its consequences has benefits that outweigh any negative impacts that may result from the discussed legislative trends or tax authorities' positions.

While the future remains uncertain, especially with regard to the current international uncertainty and looming financial hardship (with increasing inflation and recession on the horizon), we anticipate that the features that make Portugal an attractive jurisdiction for the purposes of wealth planning and for HNWI should persist, even if undergoing some changes, such as the expected approval of a legal framework applicable to activities related to crypto assets, which should be a hot topic for the Budget Law for 2023, to be presented later this year.

**Appendix 1**

# ABOUT THE AUTHORS

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Tiago Marreiros Moreira joined VdA in 2001 where he is presently a member of the board, the head of international operations, the social and corporate advisory group executive partner and head of the tax practice.

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He also plays a key role assisting multinational groups and companies in the definition of their transfer pricing policies, as well as in the negotiation and settlement of relevant disputes with tax authorities in Portuguese-speaking countries.

Tiago is also very active within the private wealth sector, notably advising numerous family offices, HNWI and private bankers in the legal and tax structuring of investments and estates, as well as in succession planning.

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