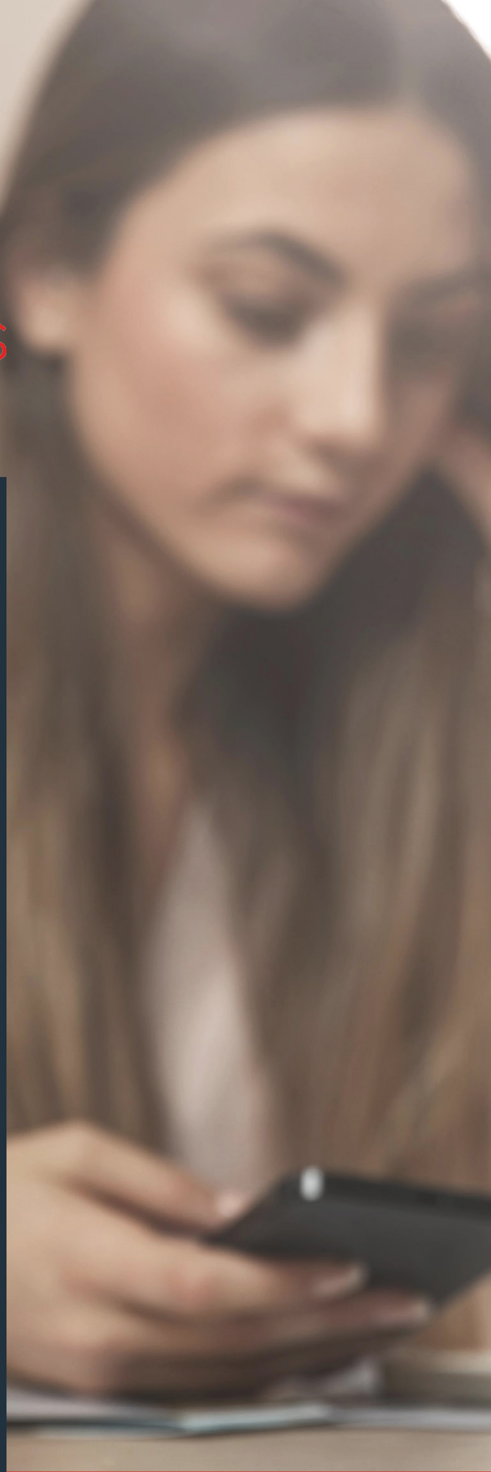

TAX TREATMENT OF PENSION INCOME IN PORTUGAL – THE 85/15 RULE AND NHR CONSIDERATIONS

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As Chartered Accountants, we frequently assist clients navigating the complexities of pension income taxation in Portugal. Below is an overview of how Portugal treats foreign pension income, including lump-sum distributions, and how specific rules such as the 85/15 rule may apply.

1. Taxable Basis – The 85/15 Rule

Under Article 54 of the Portuguese Personal Income Tax Code (CIRS), individuals receiving pension income may benefit from partial tax relief if the pension qualifies as a self-funded or contributory scheme, and it is not possible to precisely quantify the capital portion contributed by the beneficiary.

The key points are:

1 – When temporary and life annuities, as well as benefits paid under supplementary social security schemes classified as pensions, comprise amounts paid as capital reimbursement, the amount corresponding to capital is deducted.

2 – When the part corresponding to the capital cannot be broken down, to the totality of the rent, for the purposes of determining the taxable amount, an amount equal to 85% is written off.

3 – The provisions of the preceding paragraphs shall not apply to benefits due under supplementary social security schemes, whatever the debtor entity or its designation, if the contributions constituting the right deriving therefrom were borne by a person or entity beneficiary and have not been proven to be subject to taxation.

Therefore, where it is not possible to break down the pension into capital and income components, only 15% of the gross amount is subject to tax in Portugal, which leads to an effective tax rate of only 7.2%.

Important: We recommend obtaining a certificate from the tax authorities in the country of origin or from the pension provider, confirming the pension is of a contributory nature and eligible for this treatment, or other evidence of the personal contributions to the pension scheme. This documentation will be essential in the event of a tax audit to substantiate application of the 85/15 rule.

2. Lump Sum Payments – Classification and Risk

The Portuguese Government has introduced rules distinguishing between regular pension payments and capital income based on the duration and structure of the pension withdrawals.

Under Article 21 of the Tax Benefits Code:

- If pension benefits are paid regularly over more than 10 years, they will be taxed as Category H income (Pension Income).
- If payments (even in instalments) are made within 10 years or fewer, the income may be reclassified as Category E income (Capital Income), taxed autonomously at 28% under general capital income rules.

This affect individuals who wish to extract their entire pension in ten or fewer lump sums. However, the individual can take regular, smaller lump sums if they are made during ten years and one day, or more.

3. NHR Regime – Taxation of Foreign Pensions

For clients under the NHR regime, the standard flat rate of 10% applies to foreign pension income, provided they became Portuguese tax residents on or after 1 April 2020.

Whether the pension is paid monthly or as a lump sum does not, in itself, affect the tax treatment as long as the income is classified as 'pension income' by the country of origin.

However, recent amendments to Portuguese tax law have clarified the treatment of lump sums and the timeframe over which pension benefits are received.

Recommendations to Mitigate Tax Risk

To ensure pension income remains eligible for the 10% NHR tax rate, we recommend:

- Receiving pension payments over a period exceeding 10 years (e.g. annual or biannual lump sums).
- Avoiding a single large payment or a compressed series of lump sums that could trigger reclassification to Category E income.

This strategy enhances the consistency of the income stream and demonstrates alignment with the treatment of the income as a pension rather than capital.

4. Double Tax agreement Interpretation (DTA)

Under the applicable Double Tax agreement (DTA) between Portugal and the country of pension origin, Portugal typically retains the exclusive right to tax pension income if the recipient is a Portuguese tax resident at the time of payment.

If the centre of vital interests (habitual residence, family ties, and economic interests) lies in Portugal, Portugal is the state of residence for DTA purposes, and taxation should occur here—subject to local rules, including those outlined above.

5. Life Insurance Wrappers – Tax-Efficient Investment Alternative

Portugal offers very favourable tax treatment for unit-linked life insurance bonds, available to residents and non-residents.

Key advantages:

- Only capital growth is taxed (not the full redemption value).
- If the contract runs longer than 8 years and 1 day, effective tax is only 11.2%.

Redemption Period	Effective Tax Rate
First 5 years	28%
Between 5 and 8 years	22.4%
After 8 years + 1 day	11.2%

These products are regulated, considered complex financial instruments, and require prudent evaluation.

If you would like to explore insurance options or request a quote, you may contact our trusted insurance partner directly at tavira@allinsurance.pt.

Additional notes:

- Assets can be transferred in cash or in kind (note that in-kind transfers may trigger capital gains tax at 28%).
- In the event of the policyholder's death, indemnity payments are excluded from PIT.
- Premiums and commissions are exempt from Stamp Duty in Portugal.
- Minimum investment: Green Investment – €2,000, PPR – €100.

Conclusion

To summarise:

- The 85/15 rule may apply to contributory pensions with pre-taxed capital contributions made by the beneficiary.
- NHR pension income is taxed at a flat 10%, provided the income is correctly classified and structured.

- Lump-sum payments over 10 years are advisable to maintain eligibility for favorable tax treatment.
- Supporting documentation from foreign tax authorities is critical to defend your tax position in the event of an audit.

Life insurance wrappers can be a tax-efficient alternative for long-term investment.
If you're considering how best to structure your pension withdrawals or need clarity on how the rules apply to your specific case, our team of experienced professionals is here to help. We provide expert, personalised guidance to ensure your pension income is optimally managed and fully compliant with Portuguese tax regulations.

For any inquiries or support, our team can guide you through the whole moving process. Feel free to reach out to us at **info@afm.tax** or visit **www.afm.tax**.

"YOU MUST PAY TAXES, BUT THERE'S NO LAW THAT SAYS YOU NEED TO LEAVE A TIP."