



# UNDERSTANDING PROGRESSIVE TAX RATES IN PERSONAL INCOME TAX

## ALL FINANCE MATTERS

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Progressive tax rates are a fundamental aspect of Portugal's personal income tax system, aiming to ensure that taxpayers contribute to public finances in proportion to their earnings.

The higher your income, the higher the rate you pay, making the tax system more equitable for everyone.

In this guide, we'll walk you through how these rates work and how they affect your taxable income. You'll learn how the tax brackets are structured, how tax liability is calculated, and how different types of income are treated under the progressive tax system. Whether you're an individual taxpayer or self-employed, understanding these rates is crucial for managing your finances and ensuring you meet your tax obligations.

### **Explaining Progressive Tax Rates:**

Progressive tax rates are designed to apply specific tax rates to different ranges of taxable income. In simple terms, the more you earn, the higher the tax rate you pay.

Each tax bracket is associated with a range of taxable income, and within each bracket, there are two key rates: the normal rate and the average rate.

Currently, Portugal uses a system with nine distinct IRS tax brackets, which we will outline below.

### **Progressive Tax rates for 2025:**

<b>Bracket</b>	<b>Taxable Income</b>	<b>Normal Rate</b>	<b>Average Rate</b>
1st	Up to 8,059€	13%	13%
2nd	8,059€ – 12,160€	16.5%	14.180%
3rd	12,160€ – 17,233€	22%	16.482%
4th	17,233€ – 22,306€	25%	18.419%
5th	22,306€ – 28,400€	32%	21.334%
6th	28,400€ – 41,629€	35%	25.835%
7th	41,629€ – 44,987€	43.5%	27.154%
8th	44,987€ – 83,696€	45%	35.408%
9th	Above 83,696€	48%	–

## How Do Progressive Tax Rates Work?

When filing your tax return, the Tax Authority (AT) first calculates your total gross income for the previous year, then applies any relevant deductions to determine your taxable income.

This taxable income is then assigned to the appropriate tax bracket, which sets the rate that will be applied to your income.

It's important to note that not all of your income will be taxed at the same rate. Each tax bracket has both a normal rate and an average rate. Taxpayers with taxable income above 8.059€ (the threshold of the first bracket) will be subject to both rates.

**To better understand the calculation method, your taxable income is divided into two parts:**

1. **First Part:** This is the portion of your income that falls within the highest tax bracket in which your total income is fully included. The average rate of that bracket applies to this portion.
2. **Second Part:** Any income that exceeds the upper limit of the first bracket. This excess amount is taxed at the normal rate of the next higher bracket.

Let's break it down with an example:

### **Example: Step-by-Step Calculation of IRS Tax:**

Imagine that Maria has a taxable income of 25.500€. Here's how we calculate her tax liability:

1. **First part of income** (within the limit of the 5th tax bracket): Maria's income up to 22.306€ falls within the 4th tax bracket, with an average rate of 18,419%.

$$22.306\text{€} \times 18.419\% = 4.104,56\text{€}$$

2. **Second part of income** (excess falling into the 5th tax bracket): Now, we calculate the income above the 22.306€ limit, which is  $25.500\text{€} - 22.306\text{€} = 3.194\text{€}$ .

The next bracket (5th bracket) applies a normal rate of 21,334%.

$$3.194\text{€} \times 21,334\% = 681,44\text{€}$$

**3. Total Tax Due:** To find the total tax, we add up both parts:

4.104,56€ (from the first part) + 681,44€ (from the second part) = 4.786,00€

Therefore, Maria's total tax liability will be 4.786,00€, before any deductions, such as health or family-related expenses.

Based on any tax withholding Maria has already paid, she might either owe more or receive a refund depending on what was already deducted during the year.

### **Tax Withholding vs. IRS Tax Brackets:**

Tax withholding is the process where a portion of an employee's income is deducted and sent directly to the government by the employer. This amount depends on various factors, including the employee's income level, marital status, and number of dependents. Withholding helps employees pay their taxes throughout the year, so they don't need to pay a lump sum at the time of filing the tax return.

While the amount withheld is meant to be an estimate, it doesn't always match the final tax liability, since numerous factors such as changes in income or expenses can affect the amount due.

Once the IRS return is filed, the tax authority will calculate the total gross income, apply the appropriate tax rates based on the income brackets, deduct any eligible expenses, and compare it with the tax already withheld.

This process determines if the individual owes additional tax or qualifies for a refund.

### **Non-Habitual Residents Tax Regime:**

The Non-Habitual Resident (NHR) status in Portugal was a special tax regime designed to attract foreign residents and returning Portuguese citizens who have lived abroad for more than five years.

This regime offers substantial tax advantages on income from qualified work, pensions, and passive income.

Under the NHR regime, certain types of income are taxed at a flat rate of just 20%, providing a notable benefit compared to Portugal's progressive tax brackets, as well as tax exemptions or reductions on foreign-sourced income such as pensions, divi-

dends, and interest. This means that those with NHR status do not have to adhere to the standard progressive tax rates applied to other residents.

**Important Note:** While the NHR regime is no longer available to new applicants, individuals who have already registered under this regime will continue to enjoy its tax benefits for the full duration of the 10-year period, ensuring continued tax exemptions and reductions.

Understanding progressive tax rates is essential for anyone navigating the personal income tax system in Portugal. By applying different tax rates to varying income levels, the progressive tax structure ensures fairness and a gradual increase in tax liability as your earnings grow. It's important to know how these rates work, how to calculate your tax due, and how your taxable income fits within the different tax brackets.

At AFM, we are committed to helping you understand and manage your taxes more effectively. If you have any questions or need assistance with your tax return, we are here to support you. Our team of experts can guide you through the process, ensuring you comply with the current tax laws and make the most of any eligible deductions.





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