



SOCIEDADE DE ADVOGADOS, SP,RL
ROGÉRIO FERNANDES FERREIRA
& ASSOCIADOS



Nº 08/22

NEWSLETTER

TERMINATION OF THE PORTUGAL-SWEDEN DTT AND THE NHR REGIME: PRACTICAL IMPLICATIONS

This Information is intended for general distribution to clients and colleagues and the information contained herein is provided as a general and abstract overview. It should not be used as a basis on which to make decisions and professional legal advice should be sought for specific cases. The contents of this Information may not be reproduced, in whole or in part, without the express consent of the author. If you should require further information on this topic, please contact contact@rfflawyers.com.

*

This Information is sent in compliance with articles 22 and 23 of Decree-Law no. 7/2004, of 7 January, regarding unsolicited e-mails. If you wish to be removed from our mailing list and avoid similar future communications, please send an email with "Remove" to the email address newsletter@rffadvogados.com.

Legal 500 – Band 1 Tax "Portuguese Law Firm" / Band 1 Tax "RFF Leading Individual" and highlighted in "Hall of Fame", 2013, 2014, 2015, 2016, 2017, 2018, 2019
Chambers & Partners – Band 1 Tax "RFF Ranked Lawyer", 2013, 2014, 2015, 2016, 2017, 2018, 2019 and Band 1 "Private Wealth Law" - HNW "RFF Ranked Lawyer", 2018
International Tax Review – "Best European Newcomer" (shortlisted) 2013 / "Tax Controversy Leaders", 2014, 2015, 2016, 2017, 2018, 2019 / "Indirect Tax Leaders", 2015, 2016, 2017, 2018, 2019 / "Women in Tax Leaders Guide", 2015, 2016, 2017, 2018, 2019 / "European Best Newcomer", 2016 / "Tax Firm of the Year", "European Tax Disputes of the Year" and "European Indirect Tax Firm of the Year", (shortlisted) 2017
Best Lawyers – "RFF Tax Lawyer of the Year", 2014 / "Recommended Lawyers", 2015, 2016, 2017, 2018
Who's Who Legal – "RFF Corporate Tax Adviser of the Year", 2013, 2015, 2016 / "RFF Corporate Tax Controversy Thought Leader", 2017 "Corporate Tax: Advisory and Controversy", 2017, 2018, 2019
Legal Week – RFF was the only Portuguese in the "250 Private Client Global Elite Lawyers" 2018
STEP Private Clients Awards - RFF "Advocate of the Year 2019" (shortlisted)
IBFD Tax Correspondent Angola, Mozambique and East-Timor, 2013, 2014, 2015, 2016, 2017, 2018, 2019

SUMMARY

Approved by the Parliament resolution n.º 20/2003 of March 11, the Double Tax Treaty (DTT) entered into between Portugal and Sweden ceased to apply to tax residents of one of these States on January 1, 2022, as a result of the termination made by Sweden, after approval by the Swedish Parliament of the proposal submitted by the Government of that country and under Article 30 of the Convention, as informed by the official notification n.º 2/2022, published by the Official Gazette.



www.rfflawyers.com
Avenida da Liberdade, 136, 3.º/ 4.º (Reception)
1250-146 Lisboa • Portugal
T: +351 215 915 220 • F: +351 215 915 244
contact@rfflawyers.com



FRAMEWORK

Approved by Parliament resolution n.º 20/2003 of March 11, the Double Tax Treaty (DTT) between Portugal and Sweden ceased to apply to tax residents of one of those States on January 1, 2022, as a result of the termination made by Sweden, after approval by the Swedish Parliament of the proposal submitted by the government of that country and under Article 30 of the Convention, as informed by the official notification n.º 2/2022, published by the Official Gazette on February 1, 2022.

The reasons that led to Sweden's termination are mainly related to the fact that, according to the DTT, only the State of residence would be competent to tax pension income. This in practice meant that Swedish pensioners who came to live in Portugal and registered under the special regime foreseen for Non-Habitual Residents (NHR) could benefit from double non-taxation of Swedish-sourced pensions, since they would not be taxed either in the source State (Sweden) or in the State of residence (Portugal).

To appease this concern, an Additional Protocol was signed in May 2019,

amending the DTT entered into between the two countries, namely the rule on taxation of pensions, by providing for a cumulative taxation competence between the two countries, as opposed to the exclusive taxation competence attributed to the State of residence, as it had been foreseen.

This protocol would allow Sweden to tax, from 2023 onwards, Swedish-sourced pensions paid to a tax resident in Portugal, if the latter country provided for the taxation of foreign-sourced pensions received by an NHR in its internal legislation, or from 2022 onwards, if this did not occur.

Despite this intention and the fact that the State Budget Law for 2020 introduced taxation at a flat tax rate of 10% on foreign-sourced pensions received by an NHR in Portugal, the Protocol was not ratified by the Portuguese government and, as such, did not produce any changes to the DTT entered into.

As a result of the lack of agreement between the two countries, Sweden proceeded to terminate the existing DTT, which ceased to have effect on January 1, 2022.

FORMERLY APPLICABLE SITUATION

The combination of the previously applicable DTT with the Portuguese domestic legislation in force until March 2020 (i.e., the entry into force of the 2020 State Budget Law, Law 2/2020), NHRs in Portugal were able to opt for the exemption method on almost all their foreign-sourced income, namely, pension income, capital income (i.e., interest, dividends, and royalties), property capital gains, income from self-employment and employment, provided certain conditions were met.

This was possible because the DTT recognized the cumulative competence of the two countries to tax, which was a necessary condition for attributing tax exemption under the NHR regime.

In other words, it was sufficient that the pension income paid to an NHR in Portugal were attributed to an entity with effective management or permanent establishment in Sweden for them to be considered as foreign-sourced and, therefore, benefit from a tax exemption in Portugal.

Moreover, as in the DTT between the two countries, only the State of residence was competent to tax these pensions, Sweden could not collect any tax on these the referred source of income, even if in Portugal there had been no taxation, leading to a situation of double non-taxation.

This scenario changed, however, as of 2020, when Portuguese domestic legislation no longer recognizes the possibility of foreign-sourced pensions, earned by an NHR, benefiting from an exemption from taxation, and started to subject pensions to a flat tax rate of 10%, although the possibility of the respective taxpayers being able to opt for the aggregation of such income (“englobamento”) and subject it to the marginal and progressive PIT rates.

With the termination of the exemption method for foreign-sourced pensions, the progressive nature of the exemption has also been removed, i.e. the aggregation of this income only for the purposes of determining the marginal and progressive tax rates applicable to other and possible income subject to these rates.

As for tax residents who did not benefit from the special regime for NHR in Portugal, they could also trigger the DTT previously applicable between the two states for the purpose of eliminating double taxation, by granting a credit in the State of residence for the tax paid in the source State, once the cumulative competence of taxation of the two countries on the income in question and respective limits (10% in the case of dividends, interest and royalties) had been verified.

TRANSITIONAL SITUATION

It should also be noted that with the entry into force of the Law 2/2020, a transitory regime was also foreseen which allowed:

- i) RNH registered before April 1, 2020,
- ii) or who had already requested registration but had not yet been granted it
- iii) or who were already registered as tax residents by that date, but had not yet applied for NHR registration,
- iv) to continue to benefit from the exemption previously foreseen until the end of the period of validity of that special regime (10 years),

without prejudice to the possibility of opting for autonomous taxation at the rate of 10% under the new regime.

Thus, we will have, at most, situations of NHRs in Portugal which may benefit from the above-mentioned exemption until the year 2029, under this transitory regime.

CURRENTLY APPLICABLE SITUATION

In respect of the current scenario, where there is no DTT in force between the two countries, the main changes in terms of taxation in the personal sphere of taxpayers, namely NHRs in Portugal, will occur in the source State, i.e. in Sweden.

Swedish citizens who have come to Portugal to reside here and benefit from the special regime for NHR will continue to be able to see almost all their foreign-sourced income (except for capital gains on movable assets) exempt from taxation in Portugal, no longer under the formerly applicable DTT, but under the OECD Model Tax Convention, combining with the applicable domestic legislation, or to opt for the tax credit method under the latter.

In the case of pension income, the situation will also be similar, i.e. NHR in Portugal will continue to be subject to the autonomous rate of 10%, unless they are under the transitional regime, as mentioned above.

However, because there is no longer a DTT in force between the two countries, Sweden will no longer encounter any obstacle or limitation to the taxation of the income at source of its non-tax residents who, in the meantime, have gone to Portugal to take up residence.

PRATICAL IMPLICATIONS

This effectively means that, in practice, capital income (dividends, interest and royalties) earned in Sweden by an NHR in Portugal will be subject to taxation in Sweden, according to the respective domestic legislation, without the possibility to oppose the 10% limitation on taxation in the source State, as provided for in the DTT formerly in force between the two countries, or, in the case of pension income, that Sweden may subject to taxation at a rate of 25%, as provided for in its domestic law, contrary to what happened previously, in which Sweden was prohibited from taxing pensions for lack of jurisdiction.

In the latter case, considering that Portugal no longer provides for the exemption method on foreign-source pensions received by a NHR, it should, as the State of residence, grant a credit for the tax paid in Sweden up to the limit of the applicable special rate, i.e. from the amount of tax paid at source, corresponding to the 25% rate applied in Sweden, 10% of the tax paid at the special 10% rate applied in Portugal may be deducted, resulting in 0% tax payable in Portugal and an overall effective tax of 15% on the pensions paid.

In the case of a Portuguese tax resident, who receives pension income from a Swedish source, the difference will reside in the possibility of deducting the tax paid in Sweden from the tax determined in Portugal, when previously, this was not possible due to the lack of competence of the source State (i.e. Sweden) to tax this income according to the DTT formerly in force between these two countries.

CONCLUSIONS

As a result, we believe that the specific situation of NHRs in Portugal who receive pensions or other income from Swedish source changes little with the termination by Sweden of the DTT which

was in force between these two countries.

Thus, we also believe that this may have been the reason why Portugal, which had signed the amending Protocol to the Portugal-Sweden DTT and which provided for the cumulative competence of taxation on pensions, has subsequently set aside its ratification, anticipating that its termination by Sweden would not change the current framework of relocation of Swedish citizens, including pensioners, to Portugal.

Lisbon, March 8th 2022

Rogério M. Fernandes Ferreira
 Duarte Ornelas Monteiro
 Joana Marques Alves
 Gonçalo Brites da Silva
 Ricardo Miguel Martins
 Vanessa Lopes Rodrigues
 Teresa Salgueiro Verdasca
 Marta Cabugueira Leal
 João Rebelo Maltez

(Private Clients Team)

www.taxandlegalbyrff.com