

To Crypto or not to Crypto: Insights into the Portuguese Tax Proposals

By Kore Partners

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Portuguese [Budget Proposal for 2023](#) includes several rules for taxing income from crypto-assets and we outline below our insights into the background, proposals and practical issues. This is still a proposal, and the legislative process will be ongoing until the end of November. In any case, as the party supporting the Government holds a majority one should expect, besides possible technical adjustments, that the proposed measures will be approved and become effective as from 1st January 2023.

What is the current crypto tax regime in Portugal?

Despite Portugal being tagged as a friendly crypto tax regime, the tag did not arise from a specific favorable tax regime but instead from the lack of specific tax rules combined with a Tax Ruling released in 2016.

The Tax Ruling merely took the position that the disposals of cryptocurrencies were not taxed under capital gains category (because such assets could not be considered shares or financial assets) or within the investment income category (because the income would arise from the disposal of an asset). The Ruling provided that only if income would fall under business income this would constitute a taxable business activity.

The outcome of the 2016 Tax Ruling (even if not expressed in law until now) became a magnet in the crypto industry pushing investors to Portugal lured by the possibility to have a non-taxation of the gains arising from crypto related assets. Portugal was placed in the map for highly mobile crypto investors on a moment when other countries were issuing positions where income from crypto-assets was taxable.

Why is Portugal moving away from the 2016 tax ruling?

Countries have been worried with the fact that blockchain technology enables transfers of “value” (or income) from one user to another without any user having to trust or know the true identity of other user.

Despite Portugal being tagged as a friendly crypto tax regime, the tag did not arise from a specific favorable tax regime

The international trend in the last couple years has been to legislate trying to capture within the tax net income from crypto-assets and address enforcement challenges. At the OECD/EU level, projects are being rolled out for an appropriate exchange of information architecture that will require crypto service providers operating within one jurisdiction to report information about users and then have exchange information mechanism that identify beneficial owners to other participating jurisdictions. Faced with these global trends and with a tax regime merely based on a tax ruling, Portugal was becoming isolated as regards the non-taxation of gains from crypto-assets.

Pressure mounted to include specific tax rules and the finance minister announced 6 months ago that it would propose taxation of crypto-assets by October Budget proposals, requesting the Portuguese Tax Authorities to study and suggest tax rules for crypto. Close to the budget release date, new outlets reported that such study undertaken without any formal public participation had concluded that the suitable income tax regime was to mirror crypto-assets to the current tax regime of shares and tax at progressive rates the short-term gains (held less than 1 year) and at 28% rate gains held for more than 1 year. That study was never made public but news reported that the Government planned instead to follow the German tax regime by allowing tax investors to sell crypto-assets tax-free if a 1 year holding period is met.

Portugal was slowly becoming isolated with regards to the non-taxation of gains from crypto-assets

What are the measures in the Budget that affect individual investors?

We highlight 3 measures affecting individual investors, namely how gains will be taxed, how mining activity will be taxed and finally changes affecting inheritance and donations of crypto-assets.

1. Gains from the disposal of crypto-assets will be expressly qualified as capital gains but with a special tax regime linked to the holding period of such assets, as follows:
 - Exemption or 0% tax for crypto-assets not classified as securities held for more than 365 days.
 - 28% final taxation on the balance between gains and losses for disposal of crypto-assets held for less than 365 days. Losses can be carried-forward for 5 years but the use of such losses in a different tax year obliges the taxpayer to choose for progressive taxation (up to 48% plus surtaxes) if investor wants to use such losses.
 - Holding period takes into account assets acquired before 1st January 2023.



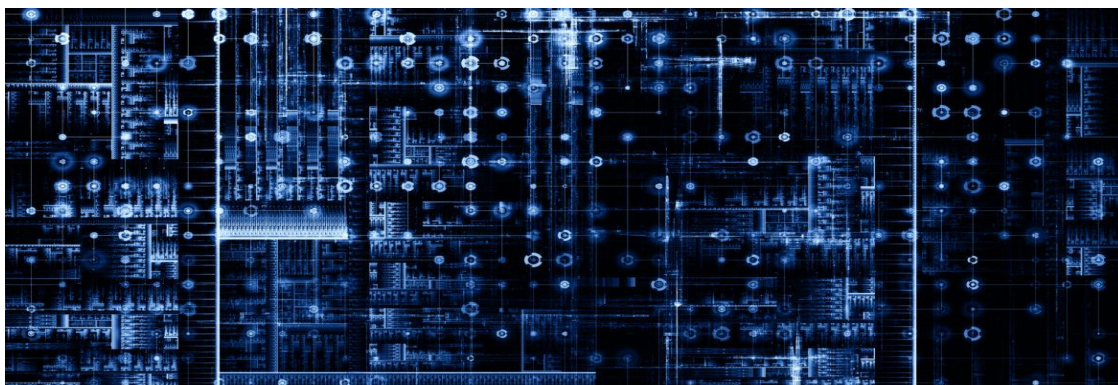
2. Operations related to issuance of crypto-assets, including mining or validation of crypto transactions through blockchain consensus mechanisms will be expressly qualified as commercial activities taxed as business income, as follows:
 - 15% of the income from such operations are taxable at progressive rates (without accounting any other deductions/expenses) to the extent that taxpayers have not exceeded in the previous fiscal year €200,000 of gross annual amount of business income. Effective tax rate ranges up to 7% of gross proceeds.
 - For taxpayers above €200,000 threshold, the taxable base is determined in a similar way to a company, accounting for deductible expenses. Net income will then be taxed at progressive marginal tax rate up to 48% plus additional solidarity surtax of 2.5% on income between €80,000 and €250,000 and 5% on income exceeding €250,000.
 - The simplified regime may apply for Portuguese companies generating income below the €200,000 threshold. Outside the simplified regime, 21% standard tax rate plus local/state surtaxes may apply for crypto trading via company.
3. In Portugal, generally no inheritance or donation tax arises unless such event (donation or inheritance) occurs outside direct family beneficiaries and specifically concerns assets deemed located in Portugal. In this latter case, a stamp tax of 10% may arise. Proposed rules cover crypto-assets within stamp tax rules, as follows:
 - Crypto-assets deposited with Portuguese-based entities are deemed to be Portuguese assets to which a 10% stamp tax may apply if gifts/inheritance occur outside direct family.
 - Foreign-held crypto-assets may also fall under the 10% stamp tax when the deceased (in case of inheritance) or beneficiary (in case of donation) are resident in Portugal and the direct family exemption would not apply.

Simplified regime (below €200k threshold) allows to apply progressive rates only to 15% of the income from crypto-asset mining

What are the other measures that affect stakeholders and investors?

We highlight 3 additional measures that affect stakeholders/investors, namely how crypto-related commissions will be taxed, how reporting information will flow to the tax authorities and finally how crypto-assets may be valued in real estate transactions.

1. Stamp tax to be levied on commissions and consideration charged by crypto-service providers at 4% rate (same rate for financial services commissions). This tax is due whenever the service providers or the final recipients are resident in Portugal. The crypto assets providers resident in Portugal will be responsible to deliver that tax and non-residents should appoint tax representative for operations not intermediated by entities domiciled in Portugal.



2. Entities providing custody/administration services for crypto-assets on behalf of third parties or managing crypto trading platforms are required to submit an official form to the Portuguese tax authorities, until the end of January of each year, communicating the operations carried out with its intervention relating to crypto-assets.
3. Finally, for real estate transfer tax purposes due on property acquisition and when crypto-assets are used for a purchase of a property there are new rules to set the market value of the crypto-assets given in exchange.

Is there a definition of Crypto and are NFTs included?

Yes, the proposal replicates the crypto-asset definition found in the latest EU Commission's legislative proposal on crypto-assets, the so-called [Markets in Crypto-Assets Regulation \("MiCA"\)](#). Under the proposed definition, crypto-asset means "a digital representation of value or rights which may be transferred and stored electronically, using distributed ledger technology or similar technology". Under this definition, non-fungible tokens (NFTs) can be considered as crypto-assets as they match each component of the definition. It should be noted that crypto-assets that are unique and not fungible with other crypto-assets fall outside the MiCA rules (with only fractionalized NFTs not being considered unique and not fungible). Further clarification from the tax authorities may be required if the interpretation of the MiCA regulation has any relevance for tax purposes.

What is then considered taxable event for purposes of capital gains?

The law uses the word "disposal" and therefore one would expect that the following crypto taxable events arise when: (I) disposing crypto for fiat; (II) trading a token for a different token; (iii) using crypto to buy goods or services.

For the calculation of the one-year period, the acquisition and disposal date resulting from the wallet will be decisive and there is no express reference to the rule that exists for securities to apply the so-called first in first out (FiFo) method. No rules exist that staked or lent tokens do not interrupt the holding period (as in Germany). The disposal value is presumed to be the market value at the disposal date. No rules are set on when acquiring and selling crypto-assets can be considered a business activity and therefore general principles should apply for cases where the taxpayer behaves like a trader or acts in a typical banking manner and uses a business set up in a commercial driven manner.

When is there a mining activity taxable under business income?

The business income category includes all income arising from the carrying on of any commercial and industrial activity and the proposal is for the "mining or validation of crypto assets transactions through blockchain consensus mechanisms" to be deemed to be a commercial activity and taxed - either via proof of work (PoW) or proof of stake (PoS).

The Portuguese tax proposal replicates the MiCA regulation definition of crypto-asset



As the proposal is drafted, it remains unclear if all proof of stake (PoS) staking activity should be deemed commercial activity leading to the business activity taxed at either the 15% presumed tax base or 100% tax base (depending on simplified regime or organized accounts regime applying).

Guidance may be necessary to determine if certain staking activities that do not require the participant to actively participate on the validation process (such as staking pools) should not be considered business income and instead capital gains when the crypto-assets are later disposed. Taxing those passive staking rewards at sale moment would be the most sensible. A similar question may be raised for governance tokens that provide decentralized decision-making mechanism for DAO members to interact with the governance protocols and control the smart contracts underlying the DAO protocol.

How are DeFi transactions framed under the proposed Portuguese rules?

There is no express reference or guidance yet as to how the principles of the Budget would apply to DeFi transactions. Applying the categorization as capital gains, business income or eventually gift taxation, we may outline tentatively in a table ([click here](#)) what could be considered as a potential outcome of the several DeFi & other related transactions.

What are issues that require amendment or clarification?

In terms of income tax, it would be preferable for an authorization to legislate during 2023. This would allow the stakeholders to actively participate on guidance and obtain clarifications on key points such as: (i) timing of recognition of gain on transfers/exchanges; (ii) taxation of periodic income; (iii) character of income for staking; and (iv) determining holding period and amount of gain. The tax authorities should further clarify the distinction between commercial activity and private management within NFTs and DeFi. Finally on the other areas, we suggest the Government to consider:

- Eliminate the proposed stamp tax rules on commissions as they are an inadequate means to tax intermediation within crypto-asset industry and such rules likely put in a worst position the local Portuguese players.
- Eliminate the inclusion of non-Portuguese custodied crypto-asset from the scope of gift and inheritance taxation because such extension of the territoriality principle raises unnecessary complexity.

- Postpone the information reporting for Portuguese entities providing custody and administration services for crypto-assets or crypto-asset trading platforms until the OECD Crypto-Asset Reporting Framework or CARF is approved or providing sufficient time to prepare internal reporting systems.

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Rua Garrett 19, 2C, Lisbon, 1200-203, Portugal