

# Hotel Activities' Development by Non-Residents: Portuguese Taxation and Accounting Framework

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**Abstract:** Purpose: Portugal has been recognized as an election destination in the tourism dimension. Several awards have been assigned to Portugal and Portuguese cities as the best places to have holidays worldwide. On the other hand, like other countries, Portugal has developed tax policies to catch foreign investment, and the tourism area is not an exception. The paper's primary goal is to understand the tax framework for the local lodging activities developed by non-residents in Portugal. Method: The research uses the legal research method to evaluate Portuguese legal data sources, in particular, it studies the personal income tax law and accounting standards. Results: The results show that the activity's development is framed in the Portuguese personal income tax category B scope. As a non-resident, the local housing income beneficiary is taxed to the income obtained in Portuguese jurisdiction through the hotel unit. The building is recognized as a fixed installation that will be recognized as a permanent establishment where the activity is developed. The gross income will be taxed under the simplified regime of the personal income tax, and it is applied a coefficient of 0.35 to determine the taxable base of the personal tax. Over the taxable base, the non-resident pays an effective tax of 25% of personal tax. All the expenses supported by the investor are not recognized in this process. The procedure is different whether the non-resident opts to be taxed under the organized accounting regime.

**Keywords:** Local lodging, Non-resident, Portugal, Personal income tax

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## 1. Introduction

Turismo de Portugal has been recognised nationally and internationally for the organisation and its activity. In recent years it has received several awards and distinctions, highlighting the quality of the Portuguese service. For instance, in 2022, it received the ISTO 2022 - International Social Tourism Organisation award, EEPA 2022 - European Enterprise Promotion Awards, World Travel Awards 2022, Medals of Tourist Merit 2022, and the Marketing Meios & Publicidade 2021 Awards. Alongside this, the Portuguese legislator has been adopting a fiscal policy promoting foreign investment in the country. The corporate income tax rate reduction is an example of a tax measure adopted or tax benefits to promote entrepreneurship (S. Aldeia, Mota, & Monteiro, 2021; Wołowiec & Skica, 2013). On the other hand, the perception that non-residents have of the Portuguese tax system is relevant in the decision-making process when considering investing in Portugal (Lestegás, Lois-González, & Seixas, 2018). Foreign people can invest in Portugal, or they can invest in Portugal and develop an activity, which is the case of non-residents who choose to buy property in Portugal to develop the activity of local accommodation. Therefore, studying the tax framework of the hotel business developed by non-residents in Portugal is essential.

In recent decades, many developing countries have researched tourism taxation (Bird, 1992) and have been implementing tax incentive programs for the tourism sector as part of their regional development policies. The primary objective of these programs is to increase local investment and employment since tourism activities are labour-intensive (Garsous, Corderi, Velasco, & Colombo, 2017).

The paper's primary objective is to develop the tax framework for the hospitality activities developed by non-residents in Portugal. In particular, it seeks to analyse the accounting and tax context of the non-resident person who develops local accommodation activity. To achieve this goal, the study researches Portuguese legislation, especially accounting standards and personal income tax law. Four sessions compose this work, firstly, the introduction explains the reasons and objective for the research; second literature review and methodology; third, the research's results; after that, the discussion and concluding remarks.

## 2. Literature Review and Methodology

In the last decades, literature has been studying the tourism phenomenon and its relationship with the foreign investment. Wang, Wan, and Dong (2014) investigate the crowding-out effect of tourism and regional differences in China. The authors provide evidence that the effect of crowdfunding varies in the case of an established local tax revenue due to differences in local infrastructure under the influence of different levels of investment and tourism-oriented entry and exit. Şengel, Işkın, Çevrimkaya, and Genç (2022) studied the

Monetary and fiscal Policies supporting the tourism industry during the COVID-19. In particular, the study highlights the financial policies implemented by countries to support the tourism industry during the pandemic period. The research concludes that countries financially support the tourism industry in terms of credit and liquidity. In addition, tourism investments are encouraged by tax breaks and low-interest rates.

Susana Aldeia, Macedo, Mota, and Pereira (2022) study the evolution of taxation in the hotel and restaurant sector in Portugal. The authors conclude that the Portuguese tax legislator needs to pay attention to the hotel and restaurant sector. There have been some changes in the income and consumption tax field in the last ten years, sustained by the desire to increase investment and control tax evasion. However, tax measures have yet to be introduced to help this business area during the pandemic of COVID-19. In addition, and regarding to Brazil's SUDENE Zone, Garsous et al. (2017) analyse Tax Incentives and Job Creation in the Tourism Industry. The study analyses a tax incentive program implemented by the federal government of Brazil in the SUDENE area in 2002 in which tourism businesses were eligible to participate. It provides evidence that tax incentives have substantially increased tourism employment in the SUDENE area. We find that during 2002-09, municipal tourism employment was, 30% higher than in the absence of the intervention, on average.

At the same time, the changes in the vat rate in the hotel sector aroused the curiosity of researchers. Skare and Kukurin (2020) assess the effects of vat legislative changes on the tourism sector in Croatia. The authors explain that changes in value-added tax (VAT) significantly impact the tourism industry's competitiveness level. In the European Union, a reduced VAT rate for tourist accommodation and restaurant services is recognised as a tool to boost competitiveness. Most E.U. countries apply reduced VAT rates for both accommodation and restaurant services. Manente and Zanette (2010) analyse the macroeconomic effects of a legislative measure to reduce VAT on the Italian restaurant and hotel industry. In particular, the study tests the effects on the Italian economy of a fiscal measure aimed at lowering the VAT rate from 10% to 5% in the Italian "Hotels and Restaurants" sector. The authors explain that such a measure would increase tourist nights would increase by a maximum of 3.15% and total tourist consumption by 4.4%. From an investment perspective, they concluded that the sector's gross fixed investments would increase by 2.17%. Regarding the budget constraint, the final 'cost' of the tax measure to the Treasury was identified. At the macroeconomic level regarding employment, the tax measure would produce a total increase of almost 100,000 jobs.

In this conceptual background, this research aims to address two questions: what is the tax framework in terms of PIT of local accommodation income obtained by non-residents in Portugal? What is the role of accounting in this process? In order to answer them, an analysis of the legal structures of Portugal was presented. Portuguese data sources were included: the personal income tax – imposto sobre o rendimento das pessoas singulares, and the Accounting law – Sistema de Normalização Contabilística.

### **3. Results: Development of Activity as a Self-Employed Person**

#### **3.1 Legal Framework**

The investor is considered a non-resident in Portugal when he/she does not fulfil the conditions foreseen in article 16 of PIT (Pereira, 2019). Generally, this concept implies the observation of criteria such as the number of days of permanence in Portugal and the fact of having a dwelling in such conditions that make the current intention to maintain and occupy it as habitual residence be assumed (Comissão para a reforma do imposto sobre o rendimento das pessoas singulares - 2014, 2014). When a taxpayer is considered a non-resident, he is only subject to PIT if he obtained income in Portugal and must file a PIT return as a non-resident (Abreu, 2012). If a person is considered a non-resident and did not obtain income in Portugal, the person does not have to file a PIT return.

Article 19 of the General Tax Law (GTL) required the appointment of a legal representative for tax purposes, with only citizens of member states of the European Union (E.U.) or the European Economic Area (EEA) would be exempt from doing so. This option had the objective of compliance with tax obligations and enabling the exercise of rights before the Tax Authority (AT) by non-resident taxpayers as a result of residence outside Portugal. This previous understanding of the Law had limitations in that it did not consider electronic means as a form of communication at the taxpayer's disposal. The recent change introduced by Decree-Law 44/2022 of July 8 has allowed the "debureaucratization" of the obligation to appoint a tax representative. This legal rule recognises that alternative means may be sufficient and appropriate to ensure compliance with tax obligations and enable the exercise of rights as a taxpayer. Thus, currently, the non-resident does not need to appoint a legal representative in Portugal. However, outside this exemption are the cases in which the taxpayer exercises an activity as a self-employed person in Portuguese territory, in these situations, and when applicable, the

obligation to appoint a tax representative a tax representative, who must cumulatively be a VAT taxpayer and be resident for tax purposes in Portugal.

### 3.2 Personal Income tax law

Exploring furnished lodging fits in the rendering of hotel activity services. In this sense, the income obtained is considered taxable under personal income tax, particularly the type of business and professional income (category B). In normative terms, it is article 3 that regulates category B income, in particular, article 4.1.h) provides explicitly for local housing activities (AT, 2020). Individuals are taxed under the personal income tax. Residents are subjectively and objectively taxed, while non-residents in Portuguese territory are taxed under PIT on an objective basis. It means that the tax is levied only on income obtained in Portuguese territory regarding income obtained from business activities imputable to a permanent establishment located in Portugal (Catarino & Guimarães, 2021). Article 18 of the PIT clarifies the concept of permanent establishment, which defines a permanent establishment as any fixed installation through which one of the activities listed in article 3 of the PIT law is carried out. Thus, purchasing a property in Portugal and the consequent exploitation as furnished accommodation is considered a permanent establishment, and the income obtained is attributable to the establishment. Thus, the conditions are met for this income to be earned in Portuguese territory and, therefore, subject to taxation in the PIT sphere. The personal income tax law foresees two tax regimes: the simplified regime (SR) and the organised accounting regime (OAR).

The SR assumes the net income and, consequently, the activity's expenses. It means that the profit made is not considered but a presumed profit (Aguiar & Lopes, 2007). Being the non-resident falls under this regime, it is considered that 35% of the income obtained from the accommodation constitutes taxable income, consequently, it is assumed that the activity had 65% of expenses (Nabais, 2021). This method of calculating the taxable base is suitable for small businesses since it does not entail high overhead costs, such as having to use the services of a certified accountant. The OAR regime implies more tax scrutiny because the entrepreneur is obliged to some additional obligations that represent additional context costs. In particular, the non-resident must have a bank account through which all activities' financial movements pass and use a certified accountant's services to certify the accounts (PWC, 2018). In this regime, the tax base is determined based on the accounting profit, which justifies the second requirement. This regime highlights the role of accounting for tax purposes, so it is necessary to keep in mind the application of the accounting standards in force in Portugal (Oliveira, 2011). In Portugal, personal income tax is based on the principle of progressivity, which means that residents are taxed by progressive rates, which are foreseen in article 68 of the PIT. The same does not happen with income obtained by non-residents to which a special rate is applied. Thus, in the case of category B income obtained by non-residents in Portuguese territory through a permanent establishment, the taxable income will be taxed at a special rate of 25%. The special rates are foreseen in article 72 of the PIT, in this specific case, what is stated in number 2, paragraph a) should be considered.

### 3.3 Accounting Standards

Currently, many countries have taxed the income of larger companies based on the profit determined according to accounting rules (DGI, 2008). Since 2010 Portugal has in place a new accounting standard based on the international accounting standards of the International Accounting Standards Board (IASB) (Rodrigues, 2021). The Accounting system began by distinguishing small entities (S.P.) from other entities subject to the complete application of the accounting and financial reporting standards (NCRF), allowing them the option to apply the accounting standard for financial reporting for small entities (NCRF-PE). Additionally, a special simplified regime of accounting standards, information standards, and accounting information is applicable to the so-called micro-entities (NCRF-ME). According to the characteristics of the business, namely the volume of income, the balance sheet total, and the number of employees, the entrepreneur must apply the rule in the business category falls. Following article 9 of Decree-Law no. 158/2009, micro-entities are considered to be those entities that do not exceed two of the following three limits (1) a balance sheet total of € 350 000, (2) net turnover of € 700 000, and (3) an average number of employees during the period of 10. In the same way that small entities are those entities that, on the balance sheet date, do not exceed two of the following three limits (i) balance sheet total of € 4,000,000, (ii) net turnover of € 8 000 000, and (iii) an average number of employees during the period of 50. For example, suppose the non-resident invoices about 200,000 euros a year, its balance sheet totalling 300,000 euros, and it has two employees. In that case, it applies the NCRF-ME standard mandatorily, optionally, the NCRF-PE standard or the set of 28 standards. In determining the net result for the period, income is deducted from expenses, and income tax is levied on the profit. The result obtained in the accounting is relevant for income tax purposes.

#### 4. Discussion and Conclusions

The main goal of this paper is to realise the legal framework of local accommodation activity developed by non-residents in Portugal. The development of this activity by non-residents in Portugal requires some attention because it involves significant tax obligations. In income tax, the non-resident has to pay tax on income obtained in Portugal from activities. The tax base calculation depends on the regime in which the non-resident is framed under the PIT, whether it is a simplified regime or an organised accounting regime. The simplified regime implies the base calculation according to coefficients previously established in the Law, which in this case is 0.35, in particular, in 1 euro income, 0.35 euros are considered taxable base. In the organised accounting regime, the determination of the base is calculated from the profit calculated in the accounts and corrected under the Law. In the second case, and considering the relevance of the correct application of accounting standards, the entrepreneur needs to hire a certified accountant. Once the tax base has been determined, on that amount, the non-resident is subject to a special PIT rate of 25%.

The research evidence the fact that the current legal dispositions of SR discourage non-resident investors do not develop hospitality activity in Portugal due to all the expenses related to the activity are not recognised as such, and it is considered investor has a net taxable profit of 35%. The fact that the research only analyses the legal framework of the Portuguese jurisdiction constitutes a limitation, and it will be important to compare other jurisdictions that traditionally have different rules in the income taxation domain.

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