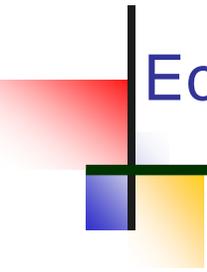


Lecture 10

Public Revenues: Theory and Practice – PART 4



Economics and Public Finance – This session outline

Chapter 3: Public revenues: theory and practice

3.4 The tax system in Portugal and other EU countries

- 3.4.1. A brief characterisation of the more important taxes in EU countries.
- 3.4.2. Social security contributions.
- 3.4.3. The personal income tax (“IRS”)

Economics and Public Finance – Readings

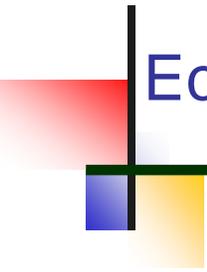
Readings English:

Summary Book Chapter 9 (translation) of Pereira and Nunes ***Economia e Finanças Públicas: da teoria à pratica***. Edições Almedina

Additional info on IRS: [Personal income tax \(IRS\) in Portugal](#)

Readings Portuguese:

Chapter 9 Pereira, Afonso et al. (2022) Economia e Finanças Públicas, 6^a edição, p. 287-317 (relevant pages).



Economics and Public Finance – Core topics

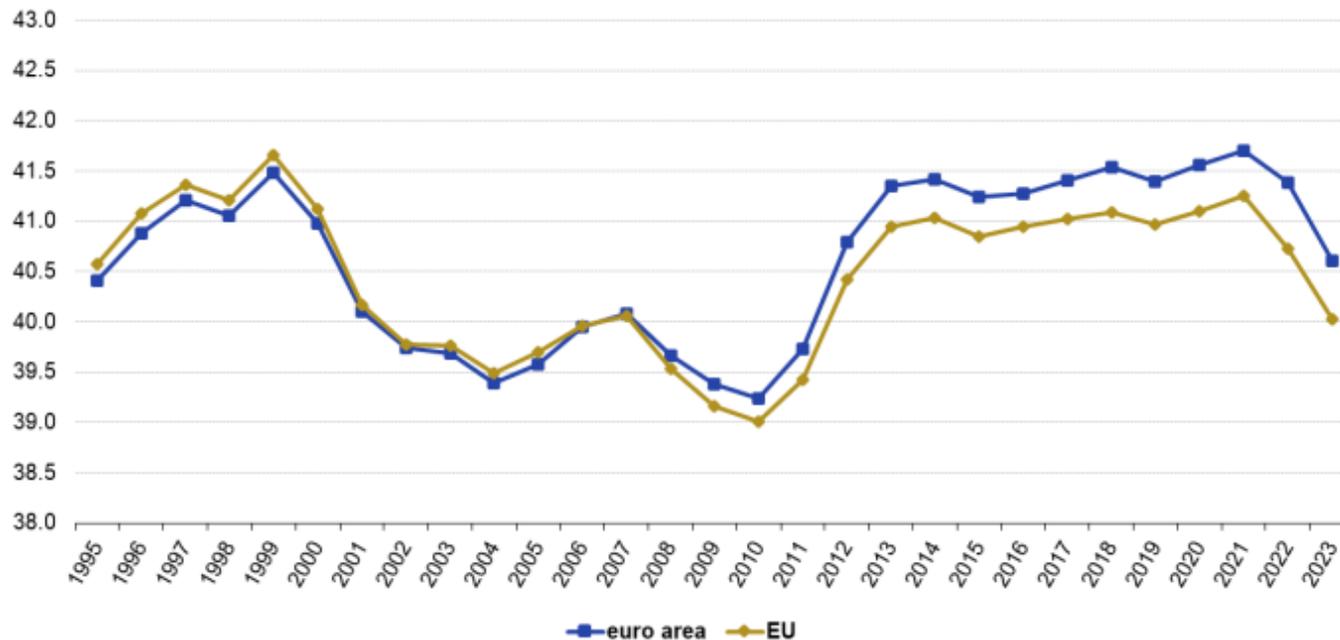
- The major types of taxes.
- Tax burden
- The characteristics and calculation of personal income tax (IRS)
 - Marginal and average tax rates
- Social security contributions

- **Objectives** of the next two lectures: learn the main features of the more important taxes and understand how they pursue objectives of either efficiency or equity.

EPF – General trends in taxation: European Union

- **Tax burden** (“nível de fiscalidade”) is usually measured as the **sum of tax revenues and social security contributions** as a percentage of GDP.

Total revenue from taxes and social contributions, EU and euro area
(% of GDP, 1995-2023)

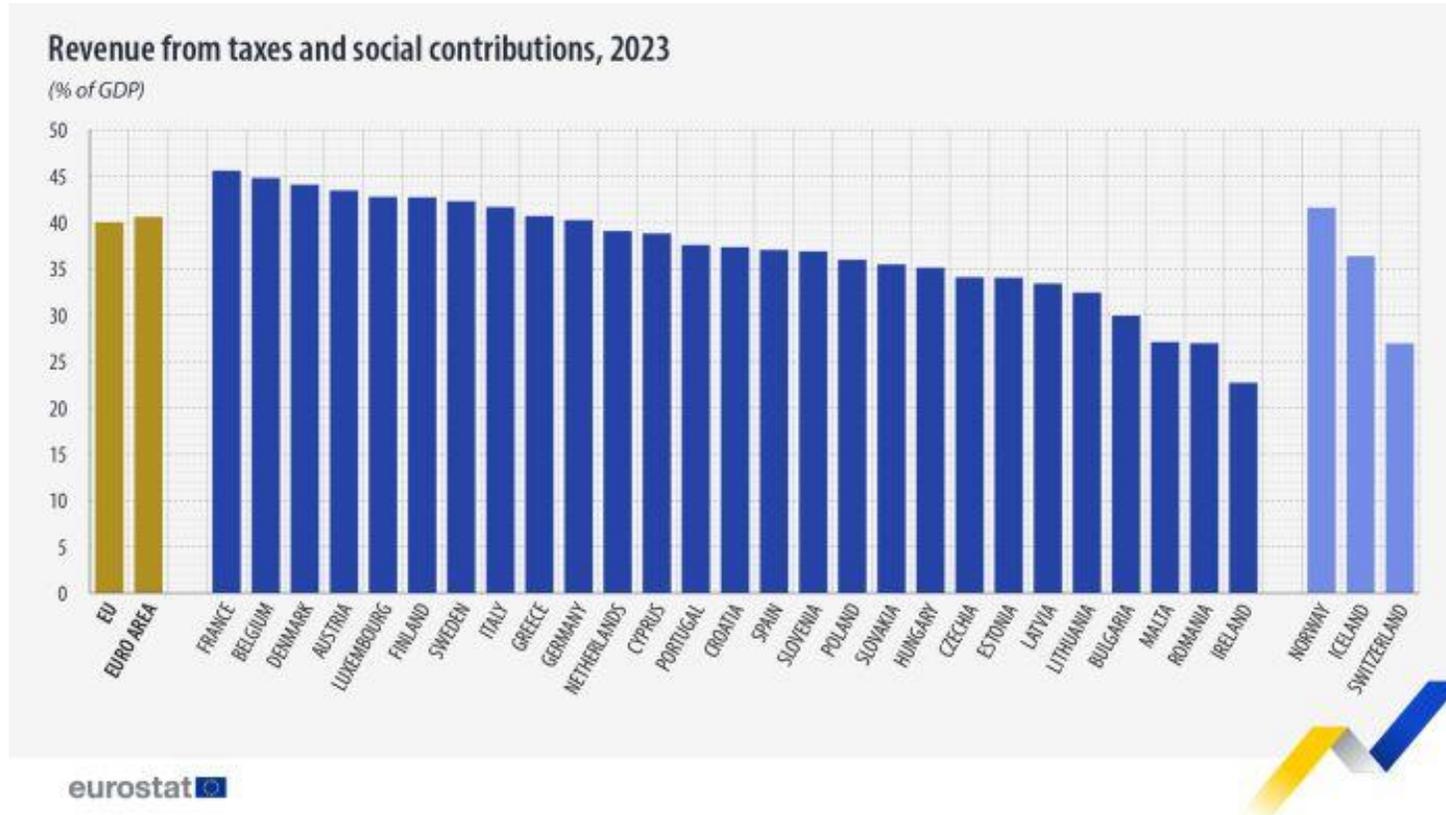


y-axis is cut

Source: Eurostat (gov_10a_taxag)

eurostat 

EPF – General trends in taxation: European Union



Portugal occupies a middle position in terms of tax burden within the EU member states.

EPF – The Portuguese tax system – Main types of taxes

- **1. Income taxes**

- Personal income tax (IRS), Corporate income tax (IRC)

- **2. Social Security contributions**

- **3. Taxes on consumption**

- General tax: Value Added Tax (VAT/IVA)
- Specific or Excise taxes: (ISP, IUC, IT, IABA, IA)

- **4. Local taxes on property**

- a) Municipal tax on real property (IMI)
- b) Municipal tax on real estate transfer (IMT)

- **Other taxes:**

- Stamp duty (*selo*)
- Municipal surcharge (local tax, “derrama”, may be levied on IRC)

Note: 1), 2), 3) and 4 a) are common taxes in most European Union states.

Economics and Public Finance – Social Security contributions (or payroll taxes)

- **Social Security contributions** are paid by **workers** and **employers**.
 - Social Security contributions can also be seen as “**earmarked taxes**”, **a sort of income tax and labour tax** (labour costs cover all costs incurred by employers when employing workers, hence including Social Security contributions). They are earmarked to the Social Security expenditures.
 - **although** Social Security contributions are somewhat different in nature from “normal taxes”, given that Social Security aims at supporting social benefits and coverage of risks of occupational disability and unemployment.

Economics and Public Finance – Social Security contributions (or payroll taxes)

- **Social Security contributions** are legally paid with flat rates on wage income by **workers** (11%) and **employers** (23,75%). It is an amount that employers subtract from employees wage.
- Does not apply to **fringe benefits** (meal tickets, regular subsidies to compensate work expenditures (“ajudas de custo”), work premia)
- Some benefits (e.g. pensions) from social security are somewhat associated with contributions during all working life (it has advantages and disadvantages...!)

Economics and Public Finance – Social Security contributions (or payroll taxes)

- The **economic incidence** of social contributions is a function of the characteristics of the labor market, in particular the elasticities of demand (by firms) and supply of labor (by workers). If supply is more rigid the economic incidence is mainly on workers (as can be illustrated graphically).
- If the elasticity of labor supply is smaller than the elasticity of demand, the economic incidence of the social security contributions falls mainly on workers.

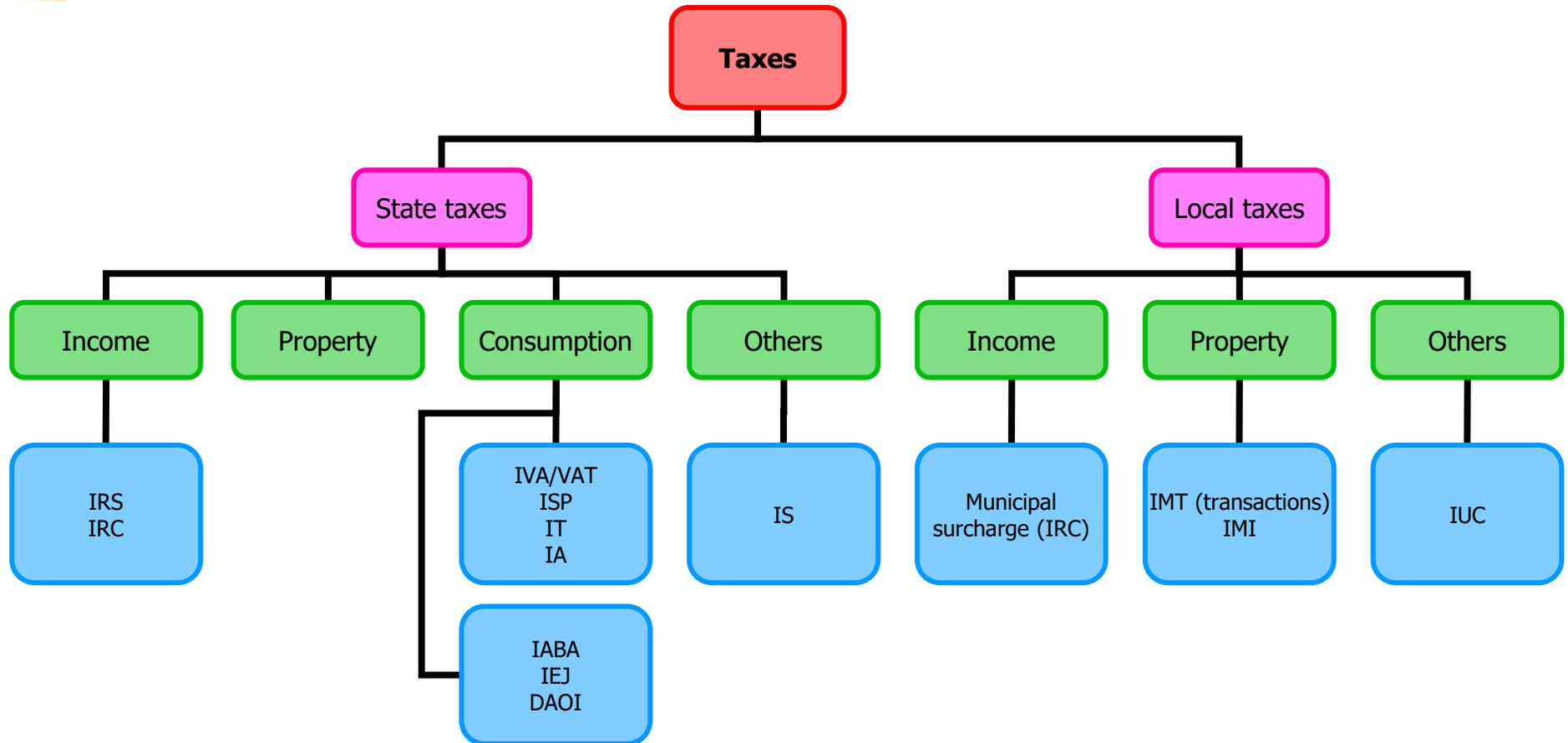
Economics and Public Finance – The Portuguese tax system

- Allocation of tax revenues by tier of government depends on the nature of government (unitary or federal countries):

	VAT/ IVA	Personal Income Tax (IRS (individuals))	Corporate Income Tax (IRC)	Property Tax and Transaction T	Excise Taxes
1. Central/Federal Government	V	V	V		V
2- State (in Federal Countries)	V	V	V		V
3a. Regions (Madeira & Azores)	V	V	V		V
3b Municipalities		up to 5%	Surcharge	V	

- Taxes on income and spending are considered as revenues of the State and the Autonomous Regions of Madeira and Azores (the portion of tax revenues therein generated).
- Portuguese municipalities tax property which is an immovable tax base.

EPF – A summary table of the Portuguese tax system (*)



(*) Please refer to the Portuguese Glossary in last page.

Economics and Public Finance – Personal income tax (“IRS”)

- **Key features of the Personal Income Tax (IRS)**

- It is a **customized** tax (it considers the entire household).
- It is a **unitary** tax (it considers all types of income).
- It is a **progressive** tax (it has increasing marginal rates).
- Personal income tax (“IRS”) taxes:
 - Total income (in Portugal or abroad) from **resident taxpayers**.
 - Income earned in Portugal from **non-residents taxpayers**.

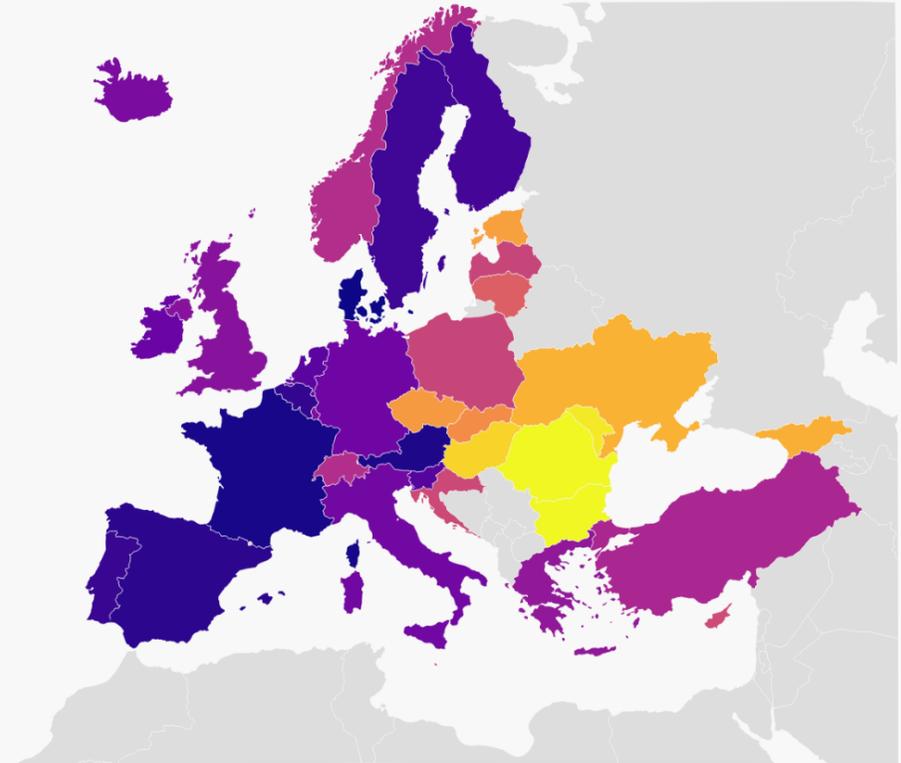
Top income tax rates

Portugal is among the countries with highest top marginal income tax rates in European OECD countries

Top Personal Income Tax Rates in Europe

Top Statutory Personal Income Tax Rates in 35 Major European Countries, 2025

10% 55.9%



Note: Combined central and sub-central top personal income tax rates and surtaxes are shown. Social security contributions are not captured.
Source: European Commission, "Taxes in Europe Database v4," PwC, "Worldwide Tax Summaries - Personal Income Tax (PIT) rates," and Bloomberg, "Country Profiles."

Economics and Public Finance – Personal income tax (“IRS”)

- IRS is a comprehensive tax.

It includes different types of personal income:

- earned income from dependent employment (Category A)
- business and professional activities’ income (Category B)
- income from capital and market investment gains (Category E)
- real estate (rental and property) income (Category F)
- pensions (Category H)
- net wealth increases (Category G)
 - capital gains on sales of property, gambling and lotteries winnings,...

EPF – Personal income tax (“IRS”): Tax rates (Budget 2026)

	Taxable income (TI)	Tax rates (%)	
	Tax Bracket (euro)	Marginal	Average
1	Up to 8342	12.5	12.5
2	8,342 < TI ≤ 12,587	15.7	13.579
3	12,587 < TI ≤ 17,838	21.2	15.823
4	17,838 < TI ≤ 23,089	24.1	17.705
5	23,089 < TI ≤ 29,397	31.1	20.579
6	29,397 < TI ≤ 43,090	34.9	25.130
7	43,090 < TI ≤ 46,566	43.1	26.472
8	46,566 < TI ≤ 86,634	44.6	34.856
9	TI > 86,634	48.0	-

The **marginal tax rate** is the one who applies to the range of incomes in that bracket.

The **average tax rate** is the ratio of the tax liability and income. In the table is calculated at the top of the bracket (e.g. 12587, 17838)

Tax bracket	Income	Marg. Tax	Tax Liability
1	8342	12.5%	1042.8
2	4245	15,7%	666.5
3	5251	21.2%	1113.2
4	2700	24.1%	650.7
Total	20538		3473.2

Example: Taxable income=20.538 (see slide 18)

Average tax rate = Tax liability/Total income=16.9%

EPF – Personal income tax (“IRS”): Tax calculation process

1. **Gross income**
2. Specific deductible amounts (e.g. Social security contributions)
3. Net income [(1) - (2)]
4. **Per capita income** Family/conjugal ratio/quotient [(3) / 2] (if there is a couple)
5. Tax yield per capita - applicable tax rates (individually)
6. **Tax yield per household [(5) * 2]**
7. Tax deductibles/benefits (household expenditures on health, education, etc.)
8. **Payable tax (“IRS”) [(7) - (8)]**

IRS – example* (a couple, with one son)

	2025
1. Gross income	50000
2. Specific deduction (4.462,15€ per capita)	8924,3
3. Net income [(1)-(2)]	41075,7
4. Income per taxpayer [(3)/2]	20537,85
5. Tax per capita (application of the tax rates)	3666,6075
6. Tax yield per household [(5)*2]	7333,215
7. Tax deductibles	1 405 €
•Personal deductions (600€ first dependent)	600 €
•Health (15%* 1500€)	225 €
•Education (30%*1.000€)	300 €
•Household general expenditures (0,35*800€)	280 €
8. Payable Income tax [(6)-(7)]	5 928 €

*Declaration in 2026 refers to income and tax rates of 2025

Cont.

Observations:

- **Income per taxable person (4):** application of the conjugal quotient (divide by 2) not to penalize couples.
- **Tax yield by taxable person (5):** the income per taxable person is less than €22,306 (upper limit of the 4th bracket in 2025); therefore, the respective **average rate of the lower bracket** (3rd bracket) - 16.48% - plus the remaining income times marginal rate of the 4th bracket (18.42%) is applied.
- Then we multiply by 2, since there are two income earners **(6)**
- **Tax deductions to implement the “equivalent income” (7):**
 - Personal deductions: €600 per dependent (e.g. child)
 - General family expenses, health and education

The amount of IRS paid is the tax due on the previous year's income.

Throughout the year there are withholding taxes (employer) that were levied on the remuneration earned.

Economics and Public Finance – Tax deductions (IRS)

- These are some of the **tax deductions*** applicable as tax benefits to IRS by taking into consideration the taxpayer's conjugal/family situation, avoiding or reducing double taxation on certain income items:
 - **Personal deductions:** for single and married taxpayers, with dependent children or parents living together.
 - **Household spending:** household general expenditures;
 - **Healthcare;**
 - **Education and training;**
 - **Financial investments:** in retirement savings plans, life and health insurances.
 - **Other** benefits and incentives.

* *Tax deductions usually have a maximum amount in each category.*