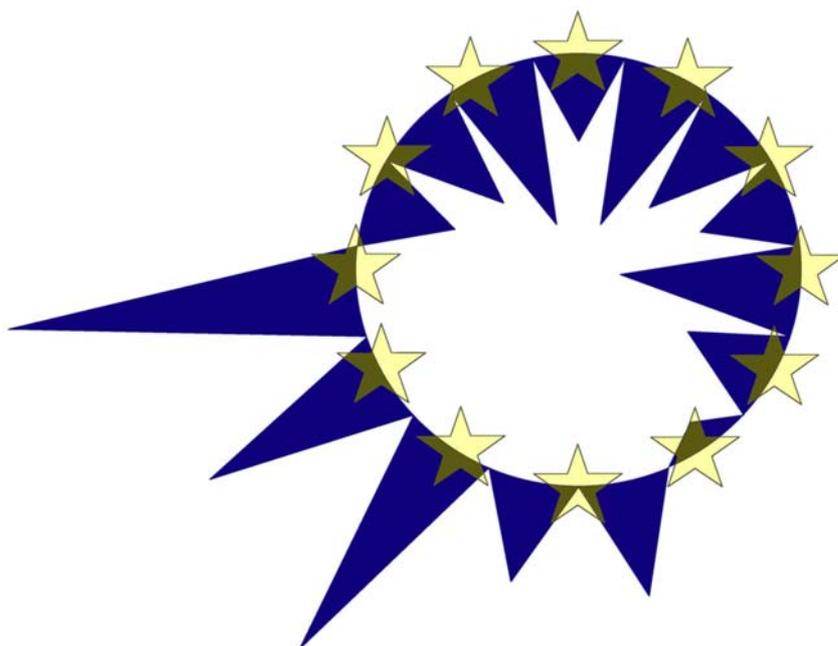


EUROMOD

COUNTRY REPORT



EUROMOD Country Report

PORTUGAL

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Euromod Country report – Portugal

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1. Tax benefit system – outline

The purpose of this report is to document the tax-benefit model Euromod as it has been developed to model the tax-benefit system of Portugal, using as data the income components, adds simulated benefits and deducts social insurance contributions and income tax to compute disposable income.

In this chapter we summarise the Portuguese tax-benefit system in a few paragraphs, like Euromod has modelled it.

1.1. Income components and benefits

The input components of the model regarding the incomes of individuals and families are primarily net incomes.

The basic components from incomes of dependent employment (COEMPY, employment income) or from self employment (COSLFEMY, self employment income) regard the individual, as one person can develop one or more activities and by so doing can earn incomes that result from both employment situations.

Investment incomes or property incomes (COINVY, investment income, e COPROPY, property income), also net incomes, and other primary incomes of individuals (COMAINTY, maintenance payments received, e COLUMPY, lumps sum income), are also referred to an individual level.

As it will be described in a further chapter, the ‘net-to-gross’ income conversion will include the individual contributions to social security and the estimated tax for gross level income, estimated at a first stage in terms of a fiscal unit and then adjusted regarding the effective charge to the individual.

Table 1.1a. Number of persons and total amounts of income to be simulated in Euromod (1998)

| Type of income | persons | source | amounts | source |
|------------------------|---------|--------|---------|--------|
| employment income | 3386 | 1 | 8463,5 | 2 |
| self employment income | 1353 | 1 | | |
| investment income | | | 5324,7 | 2 |
| property income | | | | |

Sources:

- 1) INE – Estatísticas do Emprego
- 2) Banco de Portugal – Relatório do Conselho de Administração

Notes:

- i) persons: thousands
- ii) amounts: 10⁹ Portuguese Escudos

The benefits in the Euromod model, simulated in relation to its attribution at the pattern (?) year (1995) and to the conditions of resources that occur in the simulation year (1998), regard the individuals or the families.

Unemployment benefits (PTBEN01A, unemployment related benefits) and pensions (PTBEN02A, PTBEN02B, PTBEN03A, PTBEN04A) regard individuals; the existence of several characteristics in the family determines certain “family” benefits, depending on if there are children (PTBEN05A, child benefits, PTBEN05B, family benefits) or if the family has a low income (PTBEN06A, minimum income, PTBEN07A, social assistance).

Other benefits are given to the individuals or the families, as housing benefits (COHB, housing benefits), scholarships (COEDY, student payments) and transfers (COREGY, other regular cash payments).

Table 1.1b. Number of recipients and total amounts of benefits to be simulated in Euromod (1998)

| Type of benefit | persons | source | Amounts | source |
|----------------------------------|---------|--------|---------|--------|
| unemployment related benefits | 167 | 1 | 133,1 | 2 |
| old-age insurance | 1685 | 1,3 | 1362,7 | 2,3 |
| old-age social pension | 69 | 1 | 54,9 | 2 |
| survivors related benefits | 796 | 1,3 | 274,9 | 2,3 |
| sickness and invalidity benefits | 1047 | 1 | 306,2 | 2 |
| child benefits | 1261 | 1 | 83,4 | 2 |
| family benefits | | | 25,5 | 2 |
| minimum income | 110 | 4 | 39,5 | 4 |

Sources:

- 1) MTS/IGFSS – Estatísticas da Segurança Social, I Volume – Regimes de Segurança Social, Dados Físicos
- 2) MTS/IGFSS – Conta da Segurança Social
- 3) CGA (Caixa Geral de Aposentações) – Relatório e Contas
- 4) MTS/IDS – o Rendimento Mínimo Garantido em Portugal (Janeiro 2000)

Notes:

- i) persons: thousands
- ii) amounts: 10⁹ Portuguese Escudos
- iii) child benefits received by the parents
- iv) minimum income: households and not persons

1.2. Taxes and contributions

The benefits that come from work and pensions are submitted to the Personal Income Tax (IRS) that is progressively reduced in function of higher income levels (?).

The estimated tax for a certain gross income level is estimated at a first stage in terms of a fiscal unit and then adjusted regarding the effective charge to the individual (TAX1, income taxes on work and pensions).

Incomes that come from investment or property are usually submitted to liberatory (??) taxes, regardless their level, and are kept in the source (TAX2, income taxes on capital).

Law allows taxpayers to sum all one's incomes, applying a tax over all the incomes of the individual, but few persons choose this situation (COINCTAX=TAX1+TAX2, income taxes).

Table 1.2a. Number of persons and total amounts of taxes paid to be simulated in Euromod (1998)

| Taxes | persons | source | amounts | source |
|-----------------------------------|---------|--------|---------|--------|
| income taxes on work and pensions | | | 652,2 | 1 |
| income taxes on capital | | | | |

Source:

1) Banco de Portugal – Relatório do Conselho de Administração

Notes:

i) amounts: 10⁹ Portuguese Escudos

ii) taxes on the families

The workers contributions to social security (COEESIC, employee social insurance contributions: SSC1, from wages, SSC2, from self-employment) are a percentage of their gross wages; in the case of employees, in broad terms, is applied a fixed rate over the individual wage; in the case of the self employees the contribution is usually a fixed percentage of the national minimum wage.

Some of the workers' contributions to social security are taken from the taxable income of the individual or the fiscal unit.

The employers also contribute to social security, supporting their contributions on a percentage of their employees' wages (COERSIC, employer social insurance contributions).

Table 1.2b. Number of persons and total amounts of contributions paid to be simulated in Euromod (1998)

| Contributions | Persons | source | amounts | source |
|--|---------|--------|---------|--------|
| employee social insurance contributions from wages | 3418 | 1 | 469,9 | 2 |
| employee social insurance contributions from self-employment | 618 | 1 | | |
| employer's social insurance contributions | | | 1014,7 | 2 |

Sources:

1) MTS/IGFSS – Estatísticas da Segurança Social, I Volume – Regimes de Segurança Social, Dados Físicos

2) MTS/IGFSS – Conta da Segurança Social

Notes:

i) persons: thousands

ii) amounts: 10⁹ Portuguese Escudos

iii) the number of individuals who contribute to social security do not coincide, naturally, with the number of workers

2. Tax benefit system – detailed description

In this chapter, we provide a briefly description of relevant details of the tax-benefit system in Portugal, focusing on the way it has been modelled by Euromod.

We refer the names of policy modules, parameters and conditions in the relevant Euromod parameters' sheets, in particular pol_PT.xls.

In a number of instances, we mention where we make simplifying assumptions for Euromod. All amounts pertain to the system valid on January/November 1998 and are monthly unless otherwise noted.

The next table lists the policy sheets in pol_PT.xls, and refers to the sections in which the various policies are described.

Table 2. Policies included in pol_PT.xls

| section | Policy | description |
|----------|----------------|---|
| 2.1.1.a) | ptben01a (*) | unemployment related benefits |
| 2.1.1.b) | PTBEN02A | old-age insurance |
| 2.1.1.b) | ptben02b (**) | old-age social pension |
| 2.1.1.c) | PTBEN03A | survivors related benefits |
| 2.1.1.d) | ptben04a (*) | sickness and invalidity benefits |
| 2.1.2. | ptben05a (***) | child benefits |
| 2.1.3. | ptben06a (***) | minimum income |
| 2.3. | tax1 (****) | income taxes on work and pensions |
| 2.3. | tax2 (****) | income taxes on capital |
| 2.2.1. | ssc1 (***) | employee social insurance contributions (from wages) |
| 2.2.3. | ssc2 (***) | employee self-employed social insurance contributions |
| 2.2.2. | coersic (***) | employer social insurance contributions |

(*) it is not in the file pol_PT, sheet 'spine'

(**) it is associated to another variable in the file pol_PT, sheet 'spine' (old-age insurance agriculture)

(***) it has another name in the file pol_PT, sheet 'spine'

(****) it has another name and it is less disintegrated in the file pol_PT, sheet 'spine'

2.1. Benefits simulated by Euromod – description

2.1.1. social insurance benefits

a) unemployment related benefits

Unemployment benefits aim to compensate the loss of work payments, due to unintentional unemployment, in the case of dependent employees (independent workers are not covered by this benefit).

The individual must have ability and be disposable for work and must be enrolled as a candidate for a job at the employment agency (employment public service) in the area of residence.

The attribution of the benefit depends on a guarantee deadline: the individual must have a certain number of working days with the register of wages and paid contributions in a period of a certain number of months immediately before the date of unemployment (for example, 540 days and 24 months, respectively, for the attribution of unemployment benefits).

The duration of the attribution is determined by the age of the beneficiary at the time of the application (for example, 12 months if the beneficiary is less than 30 years old).

The amount of the attribution is 65% of the registered wage (related with the total of wages in the last 12 calendar months before the previous second month in relation with the date of unemployment) and it cannot overcome the limit of 3 minimum wages.

In Euromod simulation, the confirmation that the individual receives an unemployment benefit is enough to justify the simulation of the maximum limit of the benefit (3 x 58.900\$00, the national minimum wage in 1998; the variables of ECHP in Euromod do not give enough data for demanding the other conditions).

b) old-age

Old age benefits aim to protect the beneficiary in oldness situation, being a substitute of the work payments.

The attribution of old age benefits depends on the existence of 15 calendar years with the register of wages and paid contributions and on the fact that the individual is 65 years old. However, the individual can apply for the benefit in advance, after being 55 years old, if he/she has completed 30 calendar years of contributions paid, being the benefit reduced. One can also apply for the benefit after 65 years old, having the beneficiary the right to a bonus if he/she has registered the wages and paid the contributions, at least, for 40 calendar years.

The amount for old age benefits is 2% of the average wage, for each calendar year with register of wages, and it cannot be less than 30% nor more than 80% of the average wage, being guaranteed a minimum benefit value. The average wage is calculated in relation to the total amount of wages from the 10 calendar years with higher wages, in the last 15 years.

In July and December of every year, the beneficiaries receive, besides the old age benefit, an added amount of equal value.

Portuguese citizens living in national territory (exceptionally, when they live abroad) who are 65 years old and who are not covered by any compulsory contribution regime and who do not receive any monthly gross incomes over 30% of the guaranteed minimum wage, for the general workers, or 50% of that wage whenever there is a couple, have the right to an old age benefit in the frame of the Regime não Contributivo e Equiparado (RNCE) (??).

In Euromod simulation, the confirmation that the individual is beneficiary of the Regime Geral de Segurança Social (RGSS) (??) or of the Regime Especial de Segurança Social de Actividades Agrícolas (RESSAA) (??) is enough to justify the attribution of the benefit (the variables of ECHP in Euromod do not give enough data for demanding the other conditions), and the simulation regards only the minimum limit of the benefit in relation to the value of the benefits of January and November of 1998 (31.300\$00, benefit of the RGSS).

The confirmation that the individual is beneficiary of RNCE and for individuals who are 65 or more years old, being without incomes resulting from benefits and having monthly gross incomes under 30% of the national minimum wage (the variables of ECHP do not give enough data for demanding the other conditions), the Euromod simulation attributes a minimum social benefit (22.100\$00, in relation to the value of the benefits between January and November of 1998).

c) survivors

The protection by death, by the attribution of survival benefit or death grant, aims to protect the beneficiary family due to his/her death.

The survival benefit occurs if the deceased beneficiary had fulfilled the guaranteed deadline of 36 months with register of wages. It is given to the spouse, divorced former spouse entitled to alimony, descents until the age of 18 or over in certain situations (for example, if

they are not covered by any compulsory regime of social protection or if they are invalid individuals entitled to benefits due to family charges) and ascendants dependant on the deceased in certain circumstances (if there is no spouse, nor divorced former spouse, nor descents entitled to the same benefit).

The amount is a percentage of the value of the benefit or of the one that the deceased beneficiary would have been entitled at the time of the death, in relation to the person to whom is given; the duration of its attribution also varies according those characteristics.

In Euromod simulation, the confirmation that the individual receives a survival benefit is enough to justify the attribution of the benefits (the variables of ECHP in Euromod do not give enough data for demanding the other conditions) and it only simulates the minimum limit of the benefit, in relation to the value of the benefits between January and November of 1998 (31.300\$00).

d) sickness and invalidity benefits

The benefits to protect sickness aim to compensate the loss of work payments, caused by non occupational diseases.

The attribution of sickness benefit depends on the situation of temporary incapacity for work certified by the responsible health services, when there is the register of wages during 6 calendar months and when during 12 days there is the register of wages for effectively work done in the 4 months immediately before the month previous to the date of the beginning of disability.

The period of attribution has a limit and the amount depends on several situations.

The invalidity benefits aim to protect the beneficiary who is completely invalid for work before reaching the age limit for receiving old age benefits.

When the permanent incapacity for work, for non occupational reasons, occurs after the enrolment in Social security, confirmed by the Sistema de Verificação de Incapacidades (SVI) (??) and there is a guarantee deadline regarding 5 calendar years, continuous or discontinuous, with the register of wages, there are conditions for the attribution of the benefit.

The attribution of the benefits occurs while the incapacity for work lasts and until the individual reaches the age limit for receiving old age benefits.

The invalidity benefit amount is 2% of the average wage, for each of the calendar years with register of wages, and it cannot be under 30% nor above 80% of the average wage, being guaranteed a minimum value of the benefit. The average wage is calculated in relation to the total amount of the 10 calendar years with higher wages, in the last 15 years.

In Euromod simulation, the confirmation that the individual receives sickness or invalidity benefits is enough to justify the attribution of the benefits (the variables of ECHP in Euromod do not give enough data for demanding the other conditions) and it only simulates the minimum limit of the benefit, in relation to the value of the benefits between January and November of 1998 (31.300\$00).

2.1.2. child benefits

The protection on family benefits aims to protect families by compensating them in the common expenses of family duties.

The general conditions regarding the beneficiary for receiving these benefits are: the existence of a register of wages, in the name of the beneficiary, in the 12 months before the second month previous to the date of the application or the confirmation of the attribution.

The general conditions regarding families for receiving these benefits are: being dependent on the beneficiary, not having any professional activity covered by a compulsory social protection regime (the inclusion of relatives dependent on the beneficiary is determined).

The family benefit to child and young people (Subsídio Familiar a Crianças e Jovens – SFCJ) is given to the descents until they are 16 years old, or from 16 to 18 if they attend compulsory school, or from 18 to 21 since they attend secondary school, or from 21 to 24 if they attend university, without benefiting of any scholarships, training grants or traineeship payments in a value over 2/3 of the national minimum wage.

Age limits can be broadened up by a medical declaration in the case of diseases or accidents that interfere with regular school attendance and success and it is broadened up until 24 years old to handicapped descents who are under the conditions of bonus attribution because handicap (handicapped young people, under 24, if they attend or are interns in a specialised institution in rehabilitation or if they are in such conditions, or if they need specific pedagogical and/or health support adequate to their invalidity).

The amount is calculated in relation to three grades of income, determined in relation to the national minimum wage (until 1,5 times the national minimum wage; over 1,5 times and under 8 times the national minimum wage; and over 8 times the national minimum wage) and it is given according the annual gross incomes of the household in which the descent is dependent on; it is higher in the first 12 months of life and it is re-valued after the third descent entitled to the benefit.

Introduced in the 1st of July of 1997, the family benefit to children and young people regarded, until that time, a set of benefits which disappeared meanwhile and that in 1995 would be considered family benefits (PTBEN05B) by the ECHP: child benefit (whose philosophy is present in the SFCJ, but without a positive differentiation and with lower monthly amounts), birth benefit (given just once at the occasion of the child giving) and nursing benefit (given during the first 10 months of the born child).

In Euromod simulation, the attribution of the child benefit to the household with children and young people in the defined age limits and with school attendance in the defined conditions, depending the amount on the household income, the age and number of the descents, is made, on principle, to the mother (the variables of ECHP in Euromod do not give enough data for demanding the other conditions). The amount of the attribution in relation to the annual gross incomes of the household in which the descent is dependent on, to the age and to the number of descents, is (values for 1998):

| Descents age | n° of descents | |
|-------------------|----------------|---------|
| | <= 2 | >= 3 |
| <= 12 months | | |
| income <= 1,5 SMN | 14000\$ | 21000\$ |
| income <= 8 SMN | 11000\$ | 14800\$ |
| income > 8 SMN | 7270\$ | 9450\$ |
| > 1 year | | |
| income <= 1,5 SMN | 4200\$ | 6300\$ |
| income <= 8 SMN | 2950\$ | 4000\$ |
| income > 8 SMN | 2770\$ | 3600\$ |

To simplify, Euromod simulation considers a 12 months or under years old' child as the one who is 0 years old in the age variable of the ECHP in Euromod.

2.1.3. guaranteed minimum income

The guaranteed minimum income (Rendimento Mínimo Garantido - RMG) is a cash benefit with temporary character, associated to a program of social insertion, which aims to ensure that individuals and their households have the resources that contribute to satisfy their minimum needs and to create conditions for a progressive social and professional insertion. The beneficiaries of the RMG are individuals and families facing deep economical needs, under the following situations: i) individuals with incomes lower 100% of the social benefit and ii) households with incomes lower the sum of 100% of the value of the social benefit, by each adult until two, 70% of the value of the social pension, by each adult and from the third, and 50% of the value of the social pension, by each minor. The incomes of the household resulting from work or from training actions are considered only in 80% and the rent grants, family allowances or scholarships are not considered as incomes.

Other attribution conditions are related to the age of the individual (one must be 18 or more years old, or if one is under 18 must be autonomous economically or having been emancipated by marriage, must have the exclusive economical charge of minors or the minors must be dependent exclusively on his/her household, or one must be pregnant). Other conditions are: the individual must live legally in Portugal; he/she must agree to enrol and follow a social insertion program; he/she must apply for social security benefits whenever he/she has the right to them and must exercise the right of collection of eventual credits or the recognition of the right to nourishment.

The cash benefit is given to the household and it is indexed to the value of the social pension resulting the benefit of the RMG from the difference between the value of the minimum income of the household and the value of its actual income. The first is calculated as follows: 100% of the value of the social pension, by each adult until two, 70% of the value of the social pension, by each adult and from the third, and 50% of the value of the social pension, by each minor. The incomes of the household resulting from work or from training actions are considered only in 80%.

In Euromod simulation, the attribution of the guaranteed minimum income (RMG) respects the constitution of the household and the value of the household income calculated in the

described conditions (the variables of ECHP in Euromod do not give enough data for demanding the other conditions); the value of the cash benefit of the RMG is indexed to the value of the social pension (22.100\$00, in relation to the value of the pensions between January and November 1998).

2.2. Social insurance contributions

The workers' level of contributions from real income or conventional income depends on the sort of the income resulting from work (employee, employer), on the sort of the workers' occupation or job and on the activity sector in which he/she is included, as well as on other characteristics. In spite of this diversity, Euromod simulation has considered the most common situations.

2.2.1. employee

Among the contribution regimes, there is the Regime Geral de Segurança Social dos Trabalhadores por Conta de Outrem (?) which covers as beneficiaries the employees attached to an employer agency with a work contract or any other legally compared.

The contributions regarding employees are calculated through the taxation of a global rate over the wages paid to workers. The rate in charge of the beneficiary, the employee, is 11%.

Other contribution rates (?) are also taxed over real wages or conventional wages for certain sorts of workers or in certain activities, such as undifferentiated farmers, professional football and basketball players, church members, associations and religious confessions members.

The incomes of civil servants resulting from their labor relation with the State are also covered by the contributions for a specific regime of social security, at the rate of 11%.

In Euromod simulation, the contributions for social security from the dependent workers (employees) is 11% of the income resulting from their work (the variables of ECHP in Euromod do not give enough data for demanding the other conditions).

2.2.2. employer

Among the contribution regimes, there is the Regime Geral de Segurança Social dos Trabalhadores por Conta de Outrem (?) which covers as beneficiaries the employees attached to an employer agency with a work contract or any other legally compared.

The contributions regarding employees are calculated through the taxation of a global rate over the wages paid to workers. The rate in charge of the taxpayer, the employer, is 23,75%.

Other contribution rates are also taxed over real wages or conventional wages for employer agencies that employ certain type of workers or that operate in certain activities, such as undifferentiated farmers, professional football and basketball players, church members,

associations and religious confessions members, or to certain types of employer agencies such as non profit organizations.

The incomes of civil servants resulting from their labor relation with the State are not included as contributions of the employer agency for a specific regime of social security. The occurrences of those employees are financed by a transfer from the State Budget to a specific regime of the employees and agents of Public Administration (ADSE e CGA).

In Euromod simulation, the contributions for social security from employer agencies, even that the workers of these agencies are civil servants, is 23,75% of the income of the worker resulting from his/her dependent work (the variables of ECHP in Euromod do not give enough data for demanding the other conditions).

2.2.3. self-employer

Among the contribution regimes, there is the Regime Geral de Segurança Social dos Trabalhadores Independentes (?) which covers as beneficiaries the self-employees who are not attached to an employer agency with a work contract or any other legally compared, namely traders, liberal professionals, independent managers (?) or spouses of independent workers with whom they work in regular and permanent terms.

For the workers who are developing for the first time activities as self-employers, the inclusion in this regime is not compulsory in the first 12 months of activity; self-employers with annual gross incomes like, or under, 6 times the national minimum wage are optionally included in this regime.

It is the independent worker the responsible to fulfil the contribution obligation. It implies the option, from 11 grades indexed to the national minimum wage, for a conventional wage as a base for the contributions, even the worker develops more than one activity on his/her own:

| | |
|------------------------|-----------|
| 1st grade | 1 x SMN |
| 2 nd grade | 1,5 x SMN |
| 3 rd grade | 2 x SMN |
| 4 th grade | 2,5 x SMN |
| 5 th grade | 3 x SMN |
| 6 th grade | 4 x SMN |
| | (...) |
| 11 th grade | 12 x SMN |

Whenever there are low incomes, lower wages can be defined: 50% of the national minimum wage when independent workers, with incomes like or lower 6 times of the national minimum wage, apply for their optional inclusion in the regime; or the twelfth of the annual gross income with a minimum limit of 50% of the national minimum wage (rounded off to the above one thousand escudos) (?), when workers of the compulsory inclusion in the regime have incomes lower than 12 times the national minimum wage, in a given calendar year.

The amount of the contributions is related to the social protection scheme of the worker, once that the Regime Geral da Segurança Social dos Trabalhadores Independentes (?)

includes the compulsory protection scheme, more restricted, and a wider protection scheme that the worker can choose. The rate applied to the wage chosen, as the basis of the contribution is 25,4% in the compulsory scheme and 32% in the wider scheme.

Self-employers, when they are at the same time employees, can contribute to both of the social security regimes.

In Euromod simulation, the contributions for social security from self employers, when they are not also employees (dependent workers), are 25,4% of the national minimum wage (25,4% x 58.900\$00, the national minimum wage in 1998; the variables of ECHP in Euromod do not give enough data for demanding the other conditions).

2.3. Income taxation

Euromod model builds the fiscal unit based on the rules of 1995 and 1998, after having converted the net incomes in gross incomes (see 3.4.). The conversion process 'net-to-gross', after the calculation of the income amount for the fiscal unit and the taxation of the individual income with the tax rate of the fiscal unit, determines the effective rate over the individual income.

In general, the tax unit for income taxation is the family in a household. The model define the family with the nuclear members (usually father and mother married, or similar) and all the dependent members (usually children and grandparents in some conditions); the income of the family is the sum of all the components of income of all the members of the family.

In the case of a resident and his household, if any, the tax is payable on the whole amount of incomes derived by the persons who are part thereof, being considered as taxable persons those in charge of its direction. The family unit is composed of: both spouses not judicially separated from bed and board and their dependants; each spouse or ex-spouse, respectively, in case of a judicial separation from bed and board or of decree of nullity, annulment or dissolution of a marriage, and any dependant in charge; unmarried father or mother and dependants in charge; unmarried adopting father or mother and dependants in charge.

For such purpose, the following are considered as dependants: adopted children and stepchildren, minor of age and not emancipated; adopted children and stepchildren, major of age, who are not more than 25 years old, not deriving an yearly income higher than the domestic minimum wage and having attended in the year to which the tax relates the 11th or 12th year of schooling in a middle or higher educational establishment or concluded their obligatory military service or civil service; adopted children or stepchildren, major of age, who are unable to work and to provided for their own maintenance, provided that they do not derive income higher than the maximum domestic minimum wage; minors in wardship provided that they are not deriving any income.

Dependants may however be taxed separately unless, as in the case of minor and not emancipated adopted children or stepchildren, the administration of incomes derived by them is not fully carried out by them.

In the case of a resident within the Portuguese territory, IRS (Imposto sobre o Rendimento das Pessoas Singulares, Personal Income Tax) is levied on the overall income, including income from outside that territory.

Personal Income Tax (IRS) is levied on the yearly amount of incomes in the categories enumerated below, after the appropriate deductions and allowances.

Category A - Earned income from dependent employment

The IRS Code (CIRS) adopts a considerably broad notion for employment income. Thus, there shall be liable to tax any remuneration paid or made available to the employee derived from an employment on somebody else's account under an individual labour agreement or a similar one, from services rendered under a contract for purchasing of services or of a similar nature under the authority or direction of another person, from the performance of a public job, service or duty, or from a remuneration received by reason of pre-retirement or reserve with or without the rendering of services, including, in particular, wages, salaries, fees, commissions and subsidies, either periodical or non periodical, fixed or variable, of a contracting nature or not. Any advantages or benefits resulting from, or by reason of, a service rendered (as, for instance, benefits in kind) are also subject to tax.

Category B - Income from self-employment

This category covers income derived on one's own account from the exercise of a scientific, artistic or technical activity, within the scope of the professional activities shown in a list annexed to the Code as well as income from intellectual (copy-rights and related rights) or industrial property or from information concerning an industrial, commercial or scientific experience if derived by their original holder.

This category also covers income from the exercise on one's own account of an activity consisting exclusively of services not comprised in other categories, whenever the taxable person has no employee or collaborator at his service, as well as any amount payable as an indemnity in connection with the activity performed or the change of the place where it is performed, the amounts derived from the exercise of a fortuitous act of a scientific, artistic or technical nature or from the performance of services not comprised in other categories, under the conditions already referred to, and any subsidies or allowances designed for exploitation within the scope of eligible activities in the same terms as for the recipient of income in category C.

There shall be deemed to constitute income derived by the members of professionals companies (subject to the fiscal transparency regime) to be included in this category income resulting from the allocation made according to provisions and under the conditions of Corporate Income Tax Code (CIRC).

Category C - Business income

Included in this category are profits attributable to the exercise of any commercial or industrial activity as, for instance, profits from fishing, transport, hotel and tourism activities, profits from agricultural or cattle-breeding activities not connected with the exploitation of land or where such exploitation is of a mere ancillary nature, profits from such activities if embodied in others of a commercial or industrial nature, as well as profits arising from any fortuitous act of a commercial or industrial nature not comprised in other categories.

There shall be deemed to constitute income of members of companies subject to the fiscal transparency regime, other than professional companies to be integrated in this category or in category D, as the case may be, income resulting from the allocation made according to the provisions and under the conditions of Corporate Income Tax Code (CIRC).

Category D - Agricultural income

The tax is also levied on income from agriculture, being considered as such profits derived from agricultural, forestry or cattle-breeding activities.

Category E - Investment income

Income from capital investment is equally subject to IRS. This category comprises, namely, interest from loan contracts and opening of credit, interest and other income from bank deposits, interest and other income from securities including government bills, profits from entities liable to corporate income tax placed at the disposal of respective members or owners, and income from contracts having as their object the alienation or temporary use of rights on intellectual or industrial property or information concerning an industrial, commercial or scientific experience, when not derived by the respective author or beneficial owner, as well as profits from technical assistance and from the use or the right to use an agricultural, industrial, commercial or scientific equipment, that are not income from real estate.

Category F - Income from real estate

For IRS purposes, income from real estate consists of the rents from rural, urban and mixed property paid or placed at the disposal of the respective owners.

The Code provides for a concept of both rent and real estate for this purpose.

Category G - Capital gains

IRS is levied on the following capital gains to the extent they are not considered to be commercial, industrial, agricultural or capital income: gains from the disposal for consideration of rights in rem on immovable property, the appropriation of immovable property belonging to private assets to a commercial, industrial, agricultural, forestry or cattle-breeding activity exercised on his own name by the owner thereof, as well as from the appropriation of rural property connected with the exercise of an agricultural, forestry or cattle-breeding activity to a business activity performed by the same person; gains from the disposal for consideration of corporate rights, including the remission and depreciation thereof through capital decrease, and other marketable securities; gains from the transfer for consideration of intellectual or industrial property or of a commercial, industrial or scientific experience, where the transferor is not the beneficial owner thereof; gains from the transfer for consideration of lease or other rights or assets allocated in a permanent way to the exercise of an independent professional activity, including the permanent allocation thereof to any other purpose not connected with such activity.

There shall not be liable to tax capital gains as derived from the transfer of: bonds and debentures; shares owned by the respective owner for more than 12 months.

Excluded from tax are gains from the transfer for consideration of buildings designed to the dwelling house of the taxpayer or of his household, provided that the result from such disposal is reinvested within 24 months counting from the realisation date in the acquisition of another building, building land or in the construction, enlargement or improvement of another building exclusively for the same purpose.

Category H - Pensions

Retirement, old-age, disability pensions or survivor's annuity as well as any similar pension and respective supplements, alimony, temporary or life annuity and any other pension or subsidy not expressly mentioned are liable to tax provided they are paid or made available to the beneficiary thereof.

Category I - Other income

Finally, IRS is levied on winnings from lotteries, raffles, betting, lotto and bingo paid or placed at disposal as well as on sums or prizes won in draws or competitions.

The taxable income under IRS is income resulting from the aggregation of incomes of different categories derived each year, after deductions applying to each income category and allowances also provided for under the Code.

In relation to deductions, there are some specific rules applying to each income category, but the model Euromod only developed some of them.

If the beneficiary has a degree of permanent disability equal or higher than some percentage, there are some additional rules too.

In determining the taxable income of a taxable person who is a resident in the Portuguese territory, there shall be granted as a deduction from the overall net income the following allowances if duly substantiated:

- a) Amounts paid and not reimbursed in relation to health expenses incurred by the taxpayer and his household, as well as interest on loans for payment thereof;
- b) Amounts paid and not reimbursed concerning health expenses of the taxpayer's ascendants and collateral to the third degree, where disabled and receiving income no higher than the minimum national wage, provided they live in common economy with the taxable person;
- c) Education expenses of the taxpayer and his dependants;
- d) Costs incurred with nursing homes or other institutions for old-age care in respect of the taxpayer's ascendants or collateral to the third degree, receiving income no higher than the minimum national wage;
- e) Debt interest and redemption incurred in connection with the acquisition, construction or improvement of a permanent owner-occupied dwelling-house or with the lease of a permanent home of the tenant if duly substantiated, other than redemption related to the discounting of a housing-savings account balance; payments due on contracts entered into with housing co-operative companies or within the scope of a group acquisition regime, for the purpose of acquiring a permanent owner-occupied dwelling-house or for the lease of a permanent home of the tenant, if duly substantiated, for that part in respect of interest on, and redemption of, the corresponding liabilities; the amounts net of any official grant or subsidy paid as rents by the lessee of a building or part thereof for his own and permanent home, if relating to lease contracts concluded under the Urban Rental System, as approved by Decree Law nr. 321-B/90 of 15 October, or as rents under a leasing agreement in respect of a permanent owner-occupied dwelling house subject to this regime, for that part which does not represent a capital depreciation, provided that such immovable property is situated within the Portuguese territory;
- f) Life insurance premiums covering exclusively death, disability or old-age retirement risks, provided that in the last-mentioned case the beneficiary thereof is covered after 55 years of age and for a period of five years, as well as health or personal accident insurance, any contributions for pension funds or any other complementary social security scheme under the terms laid down in the Code in respect of the taxable person or his dependants, paid by him or by third persons, provided that in such case they have been subject to tax as income in accordance to the provisions of the Code (these allowances shall not be granted unless the entity that is the beneficiary of such premiums or contributions has its head-office, the effective management or a permanent establishment through which its activity is exercised in the Portuguese territory);

- g) Compulsory alimony payments made by the taxpayer under a court decision or legal obligation;
- h) Any indemnity payable under a court order or legal obligation, by the employee to his employer on the unilateral cancellation of a personal labour contract without previous notice or, in all other cases, any indemnity the amount of which does not exceed the basic remuneration corresponding to the prior notice;
- i) Contributions to professional unions for that part not representing a counterpart to health, education, third age support, housing, insurance or social security benefits.

2.3.1. Taxable income

The taxes on the incomes resulting from work and pensions are estimated by Euromod model in a different way from those resulting from investments and properties: after specific reductions (see 2.3.2.) to incomes resulting from work (COEMPY, COSLFEMY, COLUMPY) and from pensions of the fiscal unit (PTBEN02A, PTBEN02B, PTBEN03A, PTBEN04A), is applied the following tax rate (annual values for 1998):

| Taxable income | Rate percentage | Item to deduce |
|--|-----------------|----------------|
| Up to 1.080.000\$00 | 15,0 | - |
| Over 1.080.000\$00 up to 2.500.000\$00 | 25,0 | 108.000\$00 |
| Over 2.500.000\$00 up to 6.280.000\$00 | 35,0 | 358.000\$00 |
| Over 6.280.000\$00 | 40,0 | 672.000\$00 |

In relation to taxable persons who are married and not legally separated from bed and board, the applicable rates are those corresponding to the taxable income divided by 2. The tax rates shall apply to the quotient of taxable income, and the obtained result is multiplied by 2 to determine the IRS taxable amount.

Euromod applies a liberatory (?) rate of 20% on the source to the income resulting from investments and properties (COINVY, COPROPY), which is the regular situation of taxation of these kind of incomes, regardless their amount.

2.3.2. deductions and reductions to considered incomes

From gross income derived from dependent personal services there shall be deducted for each income earner 70% of its amount up to a limit of 498.000\$00 (in 1998, annual values) or, if higher, 71% of twelve times the maximum domestic minimum wage (in 1998, 501.828\$00, annual values). If, however, any compulsory social security contributions (SSC1) are in excess of this threshold, the whole amount of such contributions shall be allowed as a deduction.

In relation to incomes resulting from self-employment, Euromod model does not deduce the worker's contributions to the social security.

In relation to pension incomes, those incomes whose yearly amount is equal or lower than 1.415.000\$00 (in 1998, annual values) for each beneficiary shall be fully deducted.

However, if the annual income for each beneficiary exceeds that amount, the deduction shall be equal to the amount mentioned above.

Euromod model also considers as a deduction to the considered incomes of the fiscal unit the amount spent with the payment of interest taxes and debt amortisation (COMORINT) regarding debts for one's housing or rent's payment (CORENT) due to housing rent according specific legislation (Regime de Arrendamento Urbano), at the maximum of 308.000\$00 (in 1998, annual values).

2.3.3. deductions to the assessment (?)

The variables of ECHP in Euromod do not offer enough data in order to demand all the conditions in the definition of the exact amount of the deduction to the assessment (?) as, for example, the disability of members of the fiscal unit.

In relation to the tax obtained by the fiscal unit, after the specific deductions to the taxable incomes, Euromod model considers the following deductions (annual values for 1998): 35.200\$00 for each taxable person, unmarried or legally separated from bed and board; 26.800\$00 for each taxable person, married and not legally separated from bed and board; 19.400\$00 for each dependant who is not liable for IRS (this amount is increased in respect of each dependant in the same conditions by 220\$00, 440\$00 or 560\$00, respectively, depending on the household being formed by two, three or more dependants); 19.400\$00 for each ascendant living under a regime of joint economy with the taxable person and not deriving income higher than the minimal social pension of the general scheme.

3. Data

3.1. General description

The data used are from the 1996 wave (3rd Wave) of the Eurostat's European Community Household Panel (ECHP) – Portuguese data-set.

The ECHP is a standardised survey in Member States of the European Union under auspices of the Statistical Office of the European Communities (Eurostat). The survey involves annual interviewing of a representative panel of households and individuals in each country (more in DRAE – Euromod Database Robustness Assessment Questionnaire).

3.2. Sample selection, weighting

The variables from ECHP included in the Euromod database are described in Annex A – Data Requirements Document. The data were collected in 1996, and the income data mostly pertain to 1995.

As has been documented in Annex A, from the original data households with unit missings (persons aged 16 or more who did not fill out a questionnaire) and households with persons with missing income information have been deleted. As a result, the dataset used contains 14468 persons in 4806 households, slightly different from the original dataset.

There is a standard set of weights developed at Eurostat and described in ECHP documentation (DOC. PAN. 36, 51, 87).

3.3. Variable adjustment

The income variables refer to 1995. However, the employment status variables refer to the situation in 1996. To improve consistency with the income variables, the employment status variables have been adjusted in accordance with income components received in 1995, as documented in the DRD (Annex A). If the adjusted employment status (coempst) differs from the original employment status, variables such as branch of industry (coindust), size of firm (cofirmsz), number of hours worked (cohours) have been adjusted as well, if relevant making use of information about previous or last employment.

3.4. 'Net-to-gross' conversion

The Euromod model builds the fiscal unit based on the rules of 1995 and 1998, after the conversion of net incomes in gross incomes (2.2 and 2.3 refer the deductive variables to the gross income of individuals).

An iterative (?) process of calculation of an estimation of the gross income in function of the contributions to social security and the taxes over the estimated incomes for the taxable incomes, after that taxation, as they are available at Euromod database, allows us to estimate values for gross incomes. In an iterative (?) way, the value of social security contributions and taxes over incomes, deductive from the gross income estimation, is equivalent to the net income of the original database.

The conversion process of 'net-to-gross' is originally elaborated regarding fiscal unit: first, it is calculated the amount of tax for the fiscal unit and the rate tax of the fiscal unit is deduced to the individual's income; only after this, the effective rate over the individual income is determined.

3.5. Summary statistics in data year

In the next tables, we compare summary statistics on region, sex and age in the data from Euromod with statistics from external data sources.

Table 3.5a. Number of persons (thousands) by region

| | Euromod | % | INE (1998) | % |
|-----------------------|---------|-----|------------|-----|
| Norte | 3516 | 35 | 3578 | 36 |
| Centro | 1672 | 17 | 1710 | 17 |
| Lisboa e Vale do Tejo | 3413 | 34 | 3326 | 33 |
| Alentejo | 534 | 5 | 510 | 5 |
| Algarve | 319 | 3 | 349 | 3 |
| Açores | 229 | 2 | 245 | 2 |
| Madeira | 239 | 2 | 260 | 3 |
| Portugal | 9922 | 100 | 9979 | 100 |

Sources: Euromod; INE – Estatísticas Demográficas

Table 3.5b. Number of persons (thousands) by sex of the individual

| | Euromod | % | INE (1998) | % |
|--------|---------|-----|------------|-----|
| Male | 4772 | 48 | 4805 | 48 |
| Female | 5150 | 52 | 5174 | 52 |
| Total | 9922 | 100 | 9979 | 100 |

Sources: Euromod; INE – Estatísticas Demográficas

Table 3.5c. Number of persons (thousands) by age

| | Euromod | % | INE (1998) | % |
|--------------|---------|-----|------------|-----|
| Less than 15 | 1759 | 18 | 1737 | 17 |
| 15 – 24 | 1639 | 17 | 1613 | 16 |
| 25 – 34 | 1484 | 15 | 1507 | 15 |
| 35 – 44 | 1345 | 14 | 1359 | 14 |
| 45 – 54 | 1172 | 12 | 1200 | 12 |
| 55 and more | 2522 | 25 | 2552 | 26 |
| Total | 9922 | 100 | 9968 | 100 |

Sources: Euromod; INE – Estatísticas do Emprego

3.6. Updating

To update the data from 1995 to the common base year 1998, the following updating factor have been used:

| Updating index | | Observations | Source |
|----------------|--------|---|---|
| e_ind | 1.1594 | Earning | MTS/DETEFP - Quadros de Pessoal (micro-data); MTS/DEPP (estimation based on micro-data) |
| slf_ind | 1.2307 | Incomes from work (incomes received by the resident families, includes employers' contributions to the Social Security) | Banco de Portugal - Relatório do Conselho de Administração, Gerência de 1998, (estimation based on Contas Nacionais from INE for the year 1995) |
| i_ind | 1.1429 | Incomes from enterprises and properties | |
| cpi_ind | 1.0843 | Inflation | INE – Índices de Preços no Consumidor, Toatl Geral Nacional |
| b2a_ind | | Updating of pensions depending on the amount or level of the pension | MTS/IGFSS – Estatísticas da Segurança Social, I Volume – Regimes de Segurança Social, Dados Físicos; MTS/IGFSS – Conta da Segurança Social |
| b3a_ind | | | |
| b4a_ind | 1.1789 | Weighed with the evolution of social protection expenses with sickness and invalidity | |
| b5b_ind | 0.7837 | Weighed with the evolution of social protection expenses with maternity, birth and nursing benefit, marriage benefit (the last ones, in 1998, included in family benefit to children and young people, substitute of the child benefit) | |
| hb_ind | 1.0986 | Inflation (1995: housing, water, electricity, gas; 1998: housing, water, electricity, gas and other fuel) | INE - Índices de Preços no Consumidor, Habitação |
| sp_ind | 1.1327 | National minimum wage (SMN) | Diários da República - I Série |
| mi_ind | 0.4597 | Interest rates of bank operations – weighed average – operations above 5 years –loans to private individuals and to emigrants (December) | Banco de Portugal - Boletim Estatístico |

4. Validation

In this chapter we compare some basic preliminary results from the Euromod baseline run with national statistics, in order to validate the aggregates produced by Euromod.

4.1. Benefits and benefit recipients

The next table compares total amounts of benefits and benefit recipients for the benefits simulated in Euromod.

Table 4.1. Benefits and benefit recipients – comparison of Euromod base line run with National Statistics (1998)

| | persons | | amounts | |
|--------------|---------|-------------------------------|---------|-------------------------------|
| | | representative of Euromod (%) | | representative of Euromod (%) |
| ptben01a | 223 | 133 | 123,5 | 93 |
| ptben02a | 1499 | 89 | 1166,5 | 86 |
| ptben02b | 138 | 94 | 22,3 | 41 |
| ptben03a | 467 | 59 | 197,9 | |
| ptben04a | 367 | 35 | 173,7 | |
| ptben05(a+b) | | | 128,3 | |
| ptben05a | 1573 | 127 | 114,2 | |
| ptben06a | 169 | 159 | 52,7 | |

Sources: Euromod; National Statistics

Notes:

i) persons: thousands

ii) amounts: 10⁹ Portuguese Escudos

iii) minimum income (ptben06a): households and not persons

4.2. Social insurance contributions and taxes

The next table compares total amounts of social insurance contributions and income taxation with the amounts produced by the Euromod baseline run.

Table 4.2. Social insurance contributions and income taxation – comparison of Euromod base line run with National Statistics (1998)

| | persons | | amounts | |
|----------|---------|-------------------------------|---------|-------------------------------|
| | | representative of Euromod (%) | | representative of Euromod (%) |
| coeesic | 4208 | 104 | 856,8 | 182 |
| ssc1 | 3535 | 103 | 736,1 | |
| ssc2 | 672 | 109 | 120,7 | |
| coersic | | | 1589,3 | 157 |
| coinctax | | | 1237,8 | |
| tax1 | | | 1174,9 | |
| tax2 | | | 62,9 | |

Sources: Euromod; National Statistics

Notes:

i) persons: thousands

ii) amounts: 10⁹ Portuguese Escudos

iii) the number of individuals who contribute to social security do not coincide, naturally, with the number of workers

4.3. Poverty incidence

Table 4.3a compares income inequality indicators and poverty rates of the Euromod baseline run with independent sources.

Table 4.3a. Income inequality indicators and poverty rates – comparison of Euromod base line run with independent sources

| | Euromod (1998) | ECHP (1996) | IOF (1994/95) |
|------------------|-------------------|----------------|------------------|
| Poverty rate | 21,9 | 22 | 20,4 |
| Gini coefficient | 0,36 | 0,37 | 0,357 |

Sources: Euromod; ECHP, 1996; Rodrigues (1999)

Note:

- i) IOF – estimation from Rodrigues, based in Inquérito aos Orçamentos Familiares do INE (considering only monetary income)
- ii) poverty rate – persons below poverty line (60% of median equivalent disposable income, using the modified OECD equivalence scale)

Table 4.3b presents additional information on the distribution of equivalent disposable income in the Euromod baseline run.

Table 4.3b. Deciles of equivalent income in Euromod

| Decile | Disposable income | Taxes | Simulated benefits |
|--------|----------------------|-------|-----------------------|
| 1 | 3,0 | 0,2 | 34,5 |
| 2 | 4,2 | 0,6 | 9,2 |
| 3 | 5,0 | 0,8 | 13,3 |
| 4 | 5,9 | 1,9 | 7,9 |
| 5 | 7,2 | 2,8 | 6,6 |
| 6 | 8,5 | 3,7 | 6,0 |
| 7 | 10,1 | 6,3 | 5,5 |
| 8 | 12,2 | 9,0 | 5,0 |
| 9 | 15,4 | 18,0 | 5,9 |
| 10 | 28,6 | 56,7 | 6,0 |

Source: Euromod

Table 4.3c compares average disposable income in every decile in the Euromod baseline run with independent source.

Table 4.3c. Disposable income in every decile

| Decile | Euromod (1998) | IOF (1994/95) |
|--------|-------------------|------------------|
| 1 | 3,0 | 2,8 |
| 2 | 4,2 | 4,2 |
| 3 | 5,0 | 5,3 |
| 4 | 5,9 | 6,4 |
| 5 | 7,2 | 7,4 |
| 6 | 8,5 | 8,6 |
| 7 | 10,1 | 10,0 |
| 8 | 12,2 | 11,9 |
| 9 | 15,4 | 15,3 |
| 10 | 28,6 | 28,0 |

Sources: Euromod; Rodrigues (1999)

Note: IOF – cálculos de Rodrigues, com base no Inquérito aos Orçamentos Familiares do INE (considerando apenas os rendimentos monetários)

4.4. Conclusion

The validation exercise on the Euromod baseline run for Portugal has shown that Euromod is not (yet) perfect for the simulation of the consequences of tax and/or benefit policy measures in Portugal.

The number of employees in Euromod database in 1995 was overestimated in 16% and in 1998 only in 4%, determining the representation of the incomes resulting from the work of employees and self-employers: 105% of the national macro statistics in 1995, 94% in 1998. To some extent, the lack of precision can be ascribed to simplifying assumptions made in Euromod. Obviously, the quality of the underlying data also plays a role here. A better understanding of Euromod pluses and minuses could possibly be gained by a more detailed comparison of distribution statistics of simulated instruments from the baseline run with external sources.

5. References

Banco de Portugal – Relatório do Conselho de Administração

CGA (Caixa Geral de Aposentações) – Relatório e Contas

Eurostat – ECHP, 1996

INE – Estatísticas Demográficas

INE – Estatísticas do Emprego

MTS/IDS – o Rendimento Mínimo Garantido em Portugal (Janeiro 2000)

MTS/IGFSS – Conta da Segurança Social

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Rodrigues, Carlos Farinha: “Repartição do Rendimento e Pobreza em Portugal (1994/95)”, in Revista de Estatística, INE, 1º Quadrimestre de 1999