

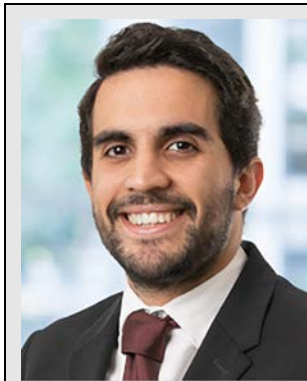
Selective BEPS in the New Portugal-U.K. Tax Treaty

by Diogo Ferreira Gomes

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In this article, Gomes examines changes to the recent Portugal-U.K. tax treaty and argues that it selectively implements base erosion and profit-shifting measures.

This article examines the design of the new Portugal-United Kingdom tax treaty, which took effect in December 2025 and will begin to apply in 2026. The convention introduces several features inspired by base erosion and profit shifting, including a principal purpose test (PPT) governing access to treaty benefits and a modern rule allowing source-state taxation of gains derived from real estate-rich entities. While these provisions strengthen antiavoidance safeguards and expand source-state taxing rights, the treaty's dispute-resolution architecture evolves more cautiously. Mandatory arbitration is confined to disputes arising under articles 5, 7, and 9 of the treaty, leaving controversies involving the PPT and real estate-rich rules outside the arbitration framework. This article argues that the treaty reflects a selective implementation of BEPS priorities: Enforcement mechanisms expand more rapidly than the institutional safeguards designed to manage the disputes they generate. In that sense, the Portugal-U.K. convention provides a useful case study of how modern tax treaties incorporate BEPS standards while maintaining a cautious approach to taxpayer certainty.

Introduction

After nearly six decades, the new Portugal-U.K. double tax convention¹ replaces a 1968 treaty² and emerges as a post-Brexit instrument that embeds several BEPS-inspired features within a modern bilateral framework. The convention entered into force on December 29, 2025. Its provisions generally apply to taxes withheld at source from January 1, 2026. Regarding other taxes in the United Kingdom, corporation tax applies from April 1, 2026, and the income tax and capital gains tax from April 6, 2026.³ For cross-border investors and multinational groups operating between the two countries, the treaty does not represent a distant reform but an immediate shift in the allocation of taxing rights and the availability of treaty relief.

The agreement does not merely incorporate BEPS standards,⁴ it rebalances authority within the treaty architecture, strengthening antiavoidance and source-state taxation tools while leaving dispute resolution guarantees comparatively narrow. This selective recalibration is the central lens through which the new convention should be understood.

The core thesis of this article is that the treaty reflects a selective implementation of BEPS priorities. It expands antiabuse architecture — most notably through a PPT that serves as a gatekeeper to treaty benefits — and reinforces

¹ Convention Between the United Kingdom of Great Britain and Northern Ireland and the Portuguese Republic for the Elimination of Double Taxation with Respect to Taxes on Income and on Capital Gains and the Prevention of Tax Evasion and Avoidance (Dec. 29, 2025).

² Convention for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (Mar. 27, 1968).

³ HM Revenue & Customs, "Portugal: Tax Treaties" (last updated Jan. 8, 2026) (into force Dec. 29, 2025, and effective from Jan. 1, 2026, for taxes withheld at source; Apr. 1, 2026, for U.K. corporation tax; and Apr. 6, 2026, for U.K. income tax and capital gains tax).

⁴ OECD, "Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 — 2015 Final Report" (Oct. 5, 2015).

source-state taxation by adopting a modern real estate-rich entity rule. At the same time, the agreement does not provide symmetrical reinforcement of dispute resolution mechanisms. Mandatory arbitration remains confined to articles 5, 7, and 9, leaving disputes involving the PPT and the real estate-rich rule outside the arbitration framework.⁵ The result is a treaty architecture in which enforcement tools expand more rapidly than the institutional safeguards designed to resolve the disputes they may generate.

Antiabuse Architecture: PPT as Gatekeeper

One of the most consequential structural features of the new convention is the adoption of a PPT as a central condition for access to treaty benefits. The PPT reflects the post-BEPS consensus that treaty relief should not be granted when obtaining that relief was one of the principal purposes of an arrangement, unless granting the benefit would be consistent with the object and purpose of the relevant treaty provisions.⁶

As a result, the logic of treaty entitlement is fundamentally altered. Under earlier treaty practice, access to reduced withholding rates typically depended on formal criteria such as residence, legal ownership, or shareholding thresholds.⁷ While those requirements remain relevant, they are now filtered through a purposive assessment. A taxpayer may satisfy the mechanical conditions for treaty relief and still face denial of benefits if tax authorities conclude that the arrangement lacks sufficient economic rationale.

The treaty establishes reduced rates — including a general 10 percent rate on dividends and the possibility of exemption for qualifying parent-subsidiary relationships — but those benefits are implicitly conditioned on the absence of abusive intent.⁸ The PPT therefore operates less as a narrowly targeted antiavoidance rule and more as a structural entitlement test governing access to treaty relief.

By requiring an assessment of principal purposes and economic substance, the PPT reallocates interpretative discretion to tax authorities and introduces a degree of ex ante uncertainty for taxpayers. This shift aligns with the broader BEPS objective of preventing treaty shopping and artificial arrangements, but it also increases the likelihood of disputes over the interpretation of purpose and economic rationale — a development that becomes particularly relevant when considering the treaty's dispute resolution architecture.

Real Estate-Rich Entities and Expanded Taxation

The convention's real estate-rich rule marks a structural policy shift: Indirect transfers of immovable property are treated as economically equivalent to direct disposals for source-state taxation purposes.⁹ Unlike the 1968 treaty, the new agreement adopts a modern approach broadly aligned with article 13(4) of the OECD model convention.¹⁰

Under article 13(4) of the new convention, gains derived from the alienation of shares or comparable interests may be taxed in the jurisdiction where the underlying immovable property is located if more than 50 percent of the value of those interests is derived directly or indirectly from such property. The rule is reinforced by a 365-day lookback period, meaning that the threshold is satisfied if the condition was met at any point during the year preceding the disposal.

This temporal extension significantly reduces the scope for pretransaction restructuring designed to circumvent source-state taxation. Attempts to rebalance assets shortly before an exit may no longer affect the outcome if the property value threshold was exceeded during the preceding twelve months.

The protocol to the treaty further clarifies the scope of the provision by specifying that “comparable interests” include interests in

⁵ Portugal-U.K. Income Tax Treaty, *supra* note 1, at arts. 5, 7, and 9.

⁶ OECD, *supra* note 4.

⁷ OECD, “Model Tax Convention on Income and on Capital 2014,” Commentary on Article 1, paras. 8-26 (Oct. 30, 2015) (reflecting the pre-BEPS approach to treaty shopping, based on specific antiabuse provisions, particularly in articles 10, 11, and 12).

⁸ Portugal-U.K. Income Tax Treaty, *supra* note 1, at art. 13.

⁹ OECD, “Model Tax Convention on Income and on Capital 2017,” art. 13(4); and OECD, Commentary on Article 13, paras. 28.4-28.7 (Apr. 25, 2019) (explaining the treatment of gains from shares deriving their value from immovable property as comparable to direct disposals for source-state taxation purposes).

¹⁰ *Id.* at art. 13(4).

collective investment vehicles and similar pooled investment arrangements.¹¹ This clarification materially expands the practical reach of the rule and brings within its scope transactions involving investment funds and other structures whose underlying assets consist primarily of real estate.

Illustration

Consider a fund vehicle holding a Portuguese real estate portfolio through tiered entities. If more than 50 percent of the value derives from immovable property at any time in the prior 365 days, gains on a share disposal may be taxed in the source state, even when the exit occurs offshore. Rebalancing assets shortly before signing may not change that outcome, and any claim to treaty relief then faces the PPT on top.

Taken together, the 50 percent threshold, the 365-day lookback period, and the protocol clarification significantly strengthen the source state's ability to tax gains connected with immovable property. The provision therefore reflects a broader trend in international tax policy: reinforcing source-state taxation in which economic value is closely tied to immovable assets located within a jurisdiction.¹²

The Arbitration Gap

While the convention modernizes antiabuse standards and strengthens source-state taxation, its approach to dispute resolution remains comparatively restrained.

The treaty provides for mandatory arbitration, but only regarding disputes arising under articles 5, 7, and 9; namely, those concerning permanent establishments, business profits, and associated enterprises.¹³ This design choice highlights the selective nature of the treaty's implementation of BEPS-inspired reforms.

Disputes involving the application of the PPT or the real estate-rich entity rule are not subject to mandatory arbitration. These exclusions are

significant because they concern precisely the areas where interpretative disagreements are most likely to arise. The PPT requires an inherently subjective assessment of principal purposes and economic substance, while the real estate-rich rule involves complex valuation and factual determinations.

In such cases, the mutual agreement procedure remains the primary avenue for dispute resolution. Although the MAP has evolved significantly and continues to serve as a central mechanism for resolving international tax disputes, it does not necessarily provide the same degree of certainty or finality as mandatory arbitration.¹⁴

As a result, the treaty's architecture creates a notable asymmetry. Antiavoidance standards and source-state taxing rights are strengthened, yet the mechanisms designed to resolve disputes arising from those standards remain comparatively limited. This imbalance may place additional pressure on the MAP process, particularly if disputes involving the interpretation of antiabuse provisions become more frequent.

Treaty Design Implications: A Selective BEPS Model?

The architecture of the Portugal-U.K. convention illustrates the policy trade-offs that characterize the post-BEPS treaty landscape. Modern tax treaties increasingly attempt to reconcile two competing objectives: preventing abusive cross-border arrangements and preserving legal certainty for international investment.¹⁵

The convention clearly advances the first objective. The adoption of the PPT strengthens the antiabuse framework governing access to treaty benefits, while the real estate-rich entity rule expands source states' ability to tax gains connected with immovable property.

At the same time, the evolution of dispute resolution guarantees appears more cautious. By confining mandatory arbitration to disputes

¹¹ Portugal-U.K. Income Tax Treaty, *supra* note 1, at Protocol (clarifying comparable interests, including collective investment vehicles).

¹² OECD, *supra* note 4; and OECD, "Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting," at art. 9 (Nov. 24, 2016).

¹³ Portugal-U.K. Income Tax Treaty, *supra* note 1, at art. 25 (including its arbitration provisions, as limited to disputes arising from the application of articles 5, 7, and 9).

¹⁴ OECD, "Making Dispute Resolution Mechanisms More Effective, Action 14 — 2015 Final Report" (Oct. 5, 2015).

¹⁵ OECD, *supra* note 4; *id.* (reflecting the balance between antiabuse measures and the need to ensure taxpayer certainty through effective dispute resolution).

concerning permanent establishments, business profits, and associated enterprises, the treaty leaves the interpretation of key antiabuse provisions largely within the sphere of administrative negotiation.

In short, the treaty is a case study in selective BEPS architecture: Enforcement tools expand faster than the institutional safeguards designed to manage the disputes they generate. That asymmetry may not be accidental — it reflects a policy choice to prioritize antiavoidance and source-state taxing rights while relying on a more traditional MAP framework for the most contentious interpretative disputes.

Conclusion

The new Portugal-U.K. tax treaty represents a substantial modernization of the bilateral

framework, notably through the adoption of a principal purpose test and a robust real estate-rich entity rule. These features align the convention with post-BEPS standards, strengthening antiavoidance safeguards and expanding source-state taxing rights. However, as demonstrated, the treaty's architecture remains structurally selective. Mandatory arbitration is confined to a limited set of provisions, leaving the most complex areas — particularly the PPT — outside its scope. This asymmetry reflects a broader feature of post-BEPS treaty design: enforcement has advanced more rapidly than certainty. Whether taxpayers will ultimately benefit from a corresponding level of legal certainty will depend on how these standards are applied in practice and how effectively the mutual agreement procedure absorbs the resulting disputes. ■