

*euro*FINESCO

eBook nº 8

# Tax-Efficient Investing in Portuguese Property

by  
Dennis Swing Greene

PORTUGAL

**Ficha Técnica:**

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Autor: Dennis Swing Greene  
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***euroFINESCO s.a.***

**HEADQUARTERS**

Rua do Sol, 4  
8200-448 GUIA (Algarve)  
*tel:* +351 289 561 333  
*fax:* +351 289 562 061

**Lisbon Branch**

Rua A.M. Cardoso, 15, 4ºD  
1200-273 LISBOA (Chiado)  
*tel:* +351 21 342 4210  
*fax:* +351 21 342 4212

**Madeira Branch**

Rua do Aljube, 61, 2º Dtº  
9000-067 FUNCHAL (Sé)  
*tel:* +351 291 221095  
*fax:* +351 291 221103

**Internet**

e-mail: [info@eurofinesco.com](mailto:info@eurofinesco.com)  
**[www.eurofinesco.com](http://www.eurofinesco.com)**  
Portugal  
*mobile:* +351 96 910 2813



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Let's be frank. This booklet has two purposes. One is to inform you, the potential investor in Portuguese property. The other is to promote our services at *euroFINESCO*. Over the following pages, we'll give you clear, accurate information in plain English about the key issues surrounding property investment in Portugal. That's our business. We have been the leaders in Fiscal and Expatriate Services in Portugal since 1991.

### **A “Win-Win” Solution**

Perhaps that is also why we start with the conclusion - that you should use a *Portuguese Nominee Company* to hold your investment property in Portugal. We believe this to be a genuine “*win-win*” situation. You, as the investor, whether buying or selling, have an excellent opportunity in Portugal, driven by climate and demographics in Europe. Portugal, in affording you an alluring framework that is squarely within legislation, both attracts foreign investment while gaining a competitive edge on other countries in Southern Europe.

### **A Compliant Solution**

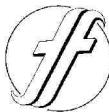
We believe in compliant solutions. Of course, we all dislike paying our taxes. That's only human. But most of us, in our hearts, are conscientious citizens, cognisant of the fact that we need to contribute our fair share. But while we have compliance obligations to meet, it is our *right* to be taxed at the *legal minimum*. There is nothing wrong about paying as little as possible, as long as you remain within the bounds of legislation. That is at the core of our purpose: to explain to you what your rights are under Portuguese Law and how to implement these goals in the minefield of Portuguese bureaucracy.

## **An Affordable Solution**

The solutions that we offer are not expensive. In fact, our services are competitively priced so there should be no significant difference in costs to you as compared with buying in your own name. As we will show, over the course of ownership and eventual sale, you can achieve significant tax advantages by using a *Portuguese Nominee Company*.

The issue is not merely how much you are going to pay. The key is how *wisely* you spend to assure that you get your money's worth. We sincerely believe that we can deliver excellent value for what you spend. We will be successful if you are.

In other words, we are on the same team.



Why invest in Property? Why invest in Portugal? These are two essential questions that require solid answers before you launch into a substantial commitment in a new country. Choosing residential property has different connotations than many other forms of investment. The risks and rewards are distinct from stocks and shares or gilts.

The potential on-going rewards, whether through direct use from owner occupancy or diverse forms of rentals, can bring in an excellent return with potentially promising tax treatment in Portugal. Renting in the Portuguese market can take any of several forms: high yielding seasonal lets, usually concentrated in popular resort regions; long-term stable lets to elderly retirees who wish to free up capital formerly locked up in their homes, or the traditional rental market to Portuguese nationals, working expats as well as others.

## **Demographics**

The heart of the answer lies in the demographic reality of an aging Europe. We have all heard about the “greying of Europe”. A recent report in the journal *Science* revealed a picture of a fast-ageing population. Life expectancy for British women, for example, has risen from just 50 a century ago to nearly 80 now. And by 2080 it is expected to rise to 100.

The consequences for Society are startling. As it impacts on our youth-dominated culture, the ageing population will spark a seismic change in the landscape, making all the familiar features unrecognisable. In all areas of life - pensionable age, crime patterns, popular culture, politics and family relationships - nothing will be left untouched.

Over the coming years, as the “baby-boom” generation retires, there will be a tide of seniors migrating south to the warmer, more hospitable climates. In neighbouring Spain, demographers predict that the number of foreign property owners will increase by *five fold* in the next decade alone. For a tiny country like Portugal, this wave of retirees translates into a huge influx of new home owners looking for their place in the sun. Not only will traditional destinations such as the Algarve or the Estoril-Cascais area remain popular, whole new regions of the interior will be discovered by this coming invasion of greying Northern Europeans.

### **Capital Appreciation**

For over 50 years property has proved to be the most consistent vehicle for investment, with property prices doubling every 7-10 years. Since the inception of statistical surveys property has proven to be a great medium to long-term investment, regardless of short-term market fluctuations.

Unlike almost any other asset, you have a wide range of long-term, low-interest finance available to help purchase your property.

You also have the added benefit of being able to obtain income throughout your ownership of the property.

### **Spain vs. Portugal**

Unless you have specific links to Portugal, you may be considering other countries for investment property options. While there are innumerable criteria to take into consideration, a head-to-head comparison of eventual forms of taxation will prove to be one of the key factors in making an informed decision. The following chart lists the principal taxes in Spain and Portugal and the respective marginal rates. While neither country would be normally classified as a “low-tax jurisdiction”, it is quite transparent that of the two countries, Portugal is the more benign.

TAXES	SPAIN	PORTUGAL
Personal Income Tax ( <i>IRPF / IRS</i> )	24% - 43% (>€46k)	14.5% - 48% (>€60k)
Tax on Non-Residents ( <i>IRNR</i> )	25%	25% (28% on lets)
Non-Resident Property Tax	3% pa on Property value	none
Real Estate Tax ( <i>Plusvalia/IMI</i> )	0.5% - 1%	0.5% - 0.8% / 0.3% - 0.5%
Capital Gains Tax on Property	flat 15% non-resident 5% withholding	50% exemption; balance at marginal rates
Wealth Tax ( <i>IP</i> )	0.2 % - 2.5% p.a.	none
VAT ( <i>IVA</i> )	8% / 18%	6% / 13% / 23%
Inheritance Tax ( <i>ISD</i> )	7.65% - 34%	Immediate Family exempt Others: 10% Stamp Duty
Property Transfer Tax	7% (Stamp Duty)	up to 6% ( <i>IMT</i> )

***Local Lodging Plan***  
**from**  
***euroFINESCO***



Our Plan is a full service package sorting out bureaucratic as well as fiscal requirements. We provide you with up-to-date, accurate information in plain English. While the plethora of prerequisites may seem a bit overwhelming at first, our friendly and knowledgeable staff will work with you to keep you compliant and help you to avoid pitfalls. When it comes time to pay tax, we strive to assure that you to pay only the legal minimum.

With ***euroFINESCO*** at your side, you can focus your time and effort on what's key to making your business a success: *maximising bookings*.



One misconception that many people have about the climate of Portugal is that it is Mediterranean. No Mediterranean wave laps Portugal's shores. The Atlantic, however, has considerable influence on the weather, bearing humidity and welcome rains, reducing the length of the summer drought and moderating the temperature.

Most books about Portugal mention that Continental Portugal can be broken up into two different climactic regions: a temperate climate in the north and a Mediterranean-like climate as you move further south. Of course this is very simplistic as there are many micro-climates and variations based on elevation and distance from the coast. As in Spain, three sets of influences are involved in forming the climate: the Atlantic, the continental (Mesetan, referring to the Spanish Mesa), and Mediterranean.

## **The North**

The Atlantic influence predominates overall, putting most of the country into the humid zone, but this is especially true in the northeast, where it gives a mild, rainy climate. Temperatures in the dead of winter in *Viana do Castelo* are very mild. The big problem is the rain, more than 1,000 millimetres, but that is also why the region is so green.

A select group of foreigners has retired to country homes inland from *Viana*, especially along the *Minho* River in *Caminha*, *Valença do Minho*, or *Monção*. The lush vegetation and the proximity to Spain make this a sought after area, but thus far by wealthy city dwellers from Portugal.

The farther inland you go the more the temperature drops in winter and increases in summer, although hot spells, with temperatures rarely passing 35°, usually don't last more than a day or two.

The coastal climate continues mild as you head south. *Porto* has a similar climate to *Viana do Castelo*. In fact, the coastline enjoys a uniform climate. The temperature at *Viana do Castelo* is almost the same as that at Cape St Vincent, in the extreme south, and if there is slightly more rain, it is offset by there being more humidity in the south. *Porto*, like *Viana*, gets a lot of rain and the winters can be quite humid. The summer is mild with a constant sea breeze that lowers the daytime temperatures but makes staying on the beach often uncomfortable. The water all along the coast is chilly and few people swim for long periods of time. Water temperatures for *Porto* in July are 16 degrees centigrade. Few foreigners choose the *Porto* region for retirement because pollution, industrial blight, horrendous traffic problems and a growing crime rate make the city unattractive for living. Inland from *Porto*, the *Douro* valley has a micro-climate that makes summers hotter and winters slightly more mild.

## **The Centre**

South of the *Douro* River, the mountainous terrain makes winter temperature extremes more pronounced. The winter chill only starts to fade when we arrive in the centre of the country near *Coimbra*. From *Coimbra* south to *Lisbon* there is an excellent area from a retirement point of view. This area includes *Leiria* and *Caldas da Rainha*. The land is fertile, the cities are small and prosperous, the ocean is near, and *Lisbon* and *Porto* are both within train, bus, or car driving distance. *Coimbra*, with its excellent medical facilities and busy cultural life because of the university, is also close by.

Lisbon is warmer than *Porto* in the summer and in the winter, although differences are slight. During the summer months of July and August the temperature can reach 33 degrees centigrade and in winter the temperature can fall to 12 degrees centigrade, but this would be an exceptionally cold day. It is uncommon in the winter for temperature to drop below 15 degrees centigrade.

## **The South**

South of Lisbon the coastal temperatures remain moderate with water temperature still cold, although warmer than in the north. The frigid waters of the Atlantic only really heat up a little in the summer when they go past Cape St Vincent and head for the Mediterranean.

Inland from the southern coast is the *Alentejo*, with mild winters (daytime temperatures rarely dropping below 10 degrees centigrade), but can be very hot in summer, with daytime temperatures in *Beja* or *Évora* often passing 35 degrees centigrade. Air conditioning would be a recommended investment here.

## **Algarve**

The place where most foreigners end up when they visit or when they retire to Portugal is the Algarve, and for one reason: *climate*. Although the Algarve is not on the Mediterranean, it has a Mediterranean climate with mild, wet winters and dry summers.

Basking in sunshine at the southernmost tip of Portugal, the Algarve has become one of the most sought after locations for those wanting a home, or second home, where there is a guarantee of a less hurried yet fairly sophisticated way of life. All year round, the Algarve enjoys perhaps the best climate in Europe. With only a short period of rainfall (it normally rains between November and March) and long hours of sunshine (the highest in Europe), the Algarve region is truly blessed.

Due to its relief and geographical position, the Algarve is influenced climatically by the European continent, North Africa, the Atlantic Ocean and the Mediterranean. The maximum temperatures in the Algarve vary, throughout the year, between 15°C and 31°C and the temperature never falls below zero in the winter.

Average Temperatures in the Algarve	
Air temperature in Summer:	24°C to 29 °C
Air temperature in Winter:	15°C to 18°C
Seawater temperature in	21°C to 24°C
Seawater temperature in	15°C to 19 °C

## Madeira

The island of Madeira is lapped by the waters of the gulf stream with warm comfortable summers and mild winters. An unusually mild climate, summer temperatures range from a high of 25° to a low of 20°. January temperatures range from 19° to 14° which explains why the winter is the high season for tourists fleeing the cold, dark reaches of Northern Europe.

The island is full of small microclimates. The bay of *Funchal*, protected by the highest peaks, enjoys the best of sunshine. Further down the west coast at *Ponta do Sol* and *Calheta*, backed by the lower hills of the *Paúl da Serra*, the sun shines brighter during these months, but they are less protected from the sea winds.

The prevailing wind is the North Easterly Trade that gathers off the Portuguese coast and runs down to the Cape Verde Islands. It brings moisture and large sea swells to the north coast, and often, particularly in the morning, adversely affects the weather on the eastern end of the island between *Caniço* and *Caniçal*. However in a westerly wind these areas can be surprisingly dry and sunny whereas the south and west coasts are duly soaked.



Despite the many virtues of Portugal, the Portuguese are plagued by a unmistakable malady: Bureaucracy. In acquiring a property, it is crucial to understand the red tape and legal instruments involved. Otherwise, you may be in for a rude surprise. The following highlights refer to key points when contemplating buying any property. It is always recommended that you seek legal as well as qualified professional advice in any property purchase.

### **Basic Documentation**

It is important to insure that any plans registered with the “*Câmara*” (Council) referring specifically to the property agree with the existing construction as the current owner will be held responsible for any variations or unauthorised constructions. A property for living purposes must have the following documentation:

- a) Habitation License with the local Council (“*Câmara*”).
- b) A certified amendment (“*Averbamento*”) in the records of the Land Registry (“*Conservatória*”);
- c) A detailed Property Book (“*Caderneta Predial*”) from the Tax Office (“*Finanças*”).

Commercial and Industrial properties require both points b). and c).

### **Promissory Contract**

It is normal for both Parties to enter into a Promissory Contract detailing the conditions of Sale – “*Contrato de Promessa de Compra e Venda*”. This Contract is then legalized by registering it in the Notary Office. This Contract is legally binding on both sides and the law requires the sellers to repay twice the deposit should they withdraw from the sale. Likewise, if the buyer fails to complete, he forfeits the total of his deposit.

It is often found practical for the buyer to appoint a third party, such as a lawyer, to represent them in any formal legal acts. A Power of Attorney (“*Procuração*”) is prepared with the necessary details and then signed and registered at the Notary.

You are required to obtain a Fiscal Number (“*Número de Contribuinte*”) from the local Tax Office (“*Finanças*”).

Prior to completing the deed, the purchase will usually be subject to a Transfer Tax (“*IMT*”, formerly called “*Sisa*”) that is paid at the local Tax Office. The amount charged is dependent upon the nature of the purchase and does vary (see chapter 4). In certain cases the buyer may be exempt from paying this Tax.

### **Deed of Sale**

When all the above requirements have been completed, the act of sale can proceed in any Notary Office. This act is known as the “*Escritura de Compra e Venda*”. Prior to the closing, the Notary will check that all the necessary documents are correct to ensure that the sale can proceed according to the facts provided. Payment is normally made separately from buyer to seller prior to the formal closing. After the act is recorded, the Notary Office will issue a certified photocopy of the entry, which is the proof to the buyer that the act has officially taken place.

### **Registration**

With the Deed complete, the property must be registered in the name of the new owners at the Land Registry (“*Conservatória do Registo Predial*”). Likewise, there is a parallel registration process at *Finanças* where technical drawings must be submitted and a new Rateable Value determined (“*Valor Patrimonial Tributável*”) that will serve as the base for future Rates assessment (“*Imposto Municipal Imobiliário*”).



Portugal, like any other country in Europe, has an array of taxes that relate to Property. Some are connected to possession of the Property, others to different forms of related income, while still others to its transmission. What was that proverb about Death and Taxes?

### **INHERITANCE TAX**

Let's start with the good news. Portugal abolished Inheritance Tax as of 1 January 2004. All family members (spouse, children, grandchildren, parents and grandparents) are exempt from tax on gratuitous transfers due to either Gift and Inheritance. All others assessed Stamp Duty at a flat rate of 10%.

### **MUNICIPAL PROPERTY TRANSFER TAX**

"IMT, formerly called "Sisa", is levied on the *transfer for consideration* of ownership rights or of partial ownership on real estate (immovable property). The taxable person is the one who acquires the property. For buildings intended exclusively for housing purposes

### **Portuguese Mainland - primary residence**

Amount liable to Transfer Tax (in Euros)	Percentage Rates - 2018	
	Marginal Rate	Adjustment
Up to 92 407	0%	0
Over 92 407 - 126 403	2%	1 848,14
Over 126 403 - 172 348	5%	5 640,23
Over 172 348 - 287 213	7%	11 358,99
Over 287 213 - 574 323	8%	11 959,32
over €574 323	single rate of 6%	-

### Portuguese Mainland - *secondary residence*

Amount liable to Transfer Tax (in Euros)	Percentage Rates - 2018	
	Marginal Rate	Adjustment
Up to 92 407	0%	0
Over 92 407 - 126 403	2%	1 268.90
Over 126 403 - 172 348	5%	2 263.60
Over 172 348 - 287 213	7%	4 157.80
Over 287 213 - 550 836	8%	-
over €550 836	single rate of 6%	-

### Madeira and Azores - *primary residence*

Amount liable to Transfer Tax (in Euros)	Percentage Rates - 2018	
	Marginal Rate	Adjustment
Up to 115 509		0
Over 115 509 - 158,004	2%	2 310.18
Over 158 004 - 215,435	5%	7 050.29
Over 215 435 - 359,016	7%	11 358.99
Over 359 016 - 717,904	8%	14 949.15
over €717,904	single rate of 6%	-

### Madeira and Azores - *secondary residence*

Amount liable to Transfer Tax (in Euros)	Percentage Rates - 2018	
	Marginal Rate	Adjustment
Up to 115 509		0
Over 115 509 - 158 004	2%	1 155.09
Over 158 004 - 215 435	5%	5 895.20
Over 215 435 - 359 016	7%	10 203.90
Over 359 016 - 688 545	8%	13 794.06
over €688,545	single rate of 6%	-

Rural property	5%
Building plots	6.5%
Offshore Companies	10%

## **Assessment and Collection**

Payment must be made prior to the Deed of transfer at the local tax office or online via Internet. Even if the transaction is exempt, a completed declaration is still required.

## **INDIVIDUAL INCOME TAX - “IRS”**

### **Category B - “Letting” as a Business**

If you are engaged in tourist related services, these receive special treatment under the Simplified Regime (*see below*). If you let out furnished accommodations to tourists on a short term basis, this type of activity is treated in a similar same way to “Sales”. In other words, you are only taxable on 20% of your invoiced income.

Since 2001, all forms of self-employment are taxed under Category B (commercial, industrial & agricultural business activities). For tax purposes, reporting will follow the rules of either the *Simplified Regime* or *Standard Accounting*, depending on which option was chosen at the time of registering one’s business activity. If no option was specified, then the Simplified Regime applies.

Unless *Standard Accounting* is specifically requested, those in this category remain in the *Simplified Regime* for the determination of taxable income, if gross turnover did not exceed €150 000:

Until other activity specific means are established, the calculation for determining taxable income is as follows:

- sales of merchandise & products . . . . X . . . . 15%
- other services; local lodging. . . . . X . . . . 35%
- billings for services & others . . . . X . . . . 75%

Income under the Simplified Regime, with a minimum taxable level equal to €2 821, will be included with other sources from other categories for determining overall taxation.

### **Category F - Rental Income and Non-Residents**

If you rent out a house or an apartment on a long term basis in Portugal, you will need to declare the income on a Portuguese income tax return. Non-residents area assessed at the tax rate of 28% for this type of income

while Residents can elect the same flat rate or add this income to other sources and pay at marginal rates. For Non-Residents, the tax paid in Portugal should be eligible for a foreign tax credit in the home jurisdiction. Be sure to consult the appropriate Double Taxation Treaty to deal with potential conflicts.

Income in Category F results from economic benefit - either in cash or in kind - from rents or habitation rights. Any additional rental income from accompanying equipment, furnishing or services included with housing also needs to be declared in this category.

### **Category G - CGT for Individuals**

When you sell a property in Portugal, the notary who performs the deed is required to report the transaction to *Finanças*. Stated more bluntly, if you don't report the sale, he will and they will come after you. In one recent example, an apprehended taxpayer received notification of the missing transaction even before his tax assessment was issued. He was fortunate. He had only to pay a re-submission fine. Others are forced to pay penalties as well as accumulated interest that, on the larger amounts that are typical in many home sales, can prove quite costly.

### **How to calculate the gain for Residents**

Although it is *Finanças*, not you, who does the actual calculation, it may be worthwhile knowing what you will have to pay. Let's suppose that you sell your home that you had originally purchased in 1994. Calculate your Capital Gains as follows:

- Step 1: From the sales price, subtract any buying and selling costs (commissions, notary fees, etc.);
- Step 2: Multiply the purchase price by the Inflation Adjustment Coefficient for 1994;
- Step 3: Add to the adjusted purchase price any documented capital improvements in the past 12 years.
- Step 4: The taxable gain is one half of this result.

Conclusion: *The difference between the adjusted purchase and sales prices is your net taxable profit.*

Proper invoices can be a major problem. Many contractors will give only informal receipts that are not valid for tax purposes. If this dilemma reaches significant proportions in your instance, specific tax advice may be in order.

### **Taxation: *Resident* vs. *Non-Resident***

As with all aspects of taxation in most countries, tax breaks exist for residents (who are the voters) that do not exist for non-residents (who cannot vote). Therefore, those that make their principal abode outside of Portugal pay a flat tax of 25%, more than any resident higher rate taxpayer would pay.

Residents receive a 50% exemption before the gain is added to their other income and taxed at marginal rates. If the property is your principal residence, then you can roll over your profit into a new property. You have a 5 year window to do so: up to two years before the sale and as much as 3 years after. If you re-invest less than the full amount, the exemption will be on a *pro rata* basis. In the event that you do not fulfill your declared intentions, an assessment will be made on the entire non-reinvested balance plus interest.

### ***Non-Discrimination between Residents and Non-Residents***

As of 2011, the optional regime applied to EU and EEA citizens is now applicable to broader kinds of income. This regime provides for the possibility of a tax refund whenever taxation exceeds what *Residents* would pay under the domestic progressive tax rate system. In other words, you may be eligible for a partial refund on your already reduced commercial assessment.

### **Portuguese Nominee Company**

If you use a Portuguese Nominee Company to hold your property, the CGT rate on the sale of the Company drops to only 14%.

*(See Chapter 6)*

## **MUNICIPAL PROPERTY TAX (*Rates*) - “*IMI*”**

At the heart of the 2003 Property Tax Reform is the new “*VPT*” Evaluation System (“*Valor Patrimonial Tributário*”). Comprised of five basic components, this calculation is based on “market value” rather than “potential rental income” as in the previous system.

### **Factor nº1: *Constructed Area and Implantation***

The area is a function of cost. The 2010 value per m<sup>2</sup> is €603. Area coefficients are determined as follows:

Type of Area	Coefficient
Covered Habitation Area	1
Outbuildings	0.3
Garden and Patio areas (up to 2x implantation)	0.25
Surrounding land	0.005

To calculate this primary factor, add the areas, previously multiplied by the respective coefficients, then multiply by the cost per square metre. Next this base will be altered by the remaining coefficients.

### **Factor nº 2: *Type of Usage***

The Area Factor is adjusted by type of Usage, having been assigned coefficients as follows:

Type of Usage	Coefficient
Commercial	1.2
Services	1.1
Residential	1
Subsidized Housing	0.7
Industrial and Warehouse	0.6
Covered Parking	0.4
Degraded Housing	0.45
Open air Parking	0.08

### **Factor nº 3: Age**

The *Age* factor is adjusted by the year of construction or the property's last re-evaluation. The Age Coefficient is determined as follows:

Age in Years	Coefficient
Less than 3	1
3 to 5	0.98
6 to 10	0.95
11 to 15	0.9
16 to 20	0.85
21 to 30	0.8
31 to 40	0.75
41 to 50	0.65
51 to 60	0.55
60 to 80	0.45
More than 80	0.35

### **Factor nº 4: Location**

The following table illustrates the highs and lows in each Council in the Algarve, depending on how the property is used:

#### **Municipal Tax Rates (by council) - ALGARVE**

Albufeira	0.30 %
Alcoutim	0.30 %
Aljezur	0.35 %
Castro Marim	0.40 %
Faro	0.45 %
Lagoa	0.36 %
Lagos	0.38 %
Loule	0.30 %
Monchique	0.30 %
Olhão	0.40 %
Portimão	0.45 %
S. Bras de Alportel	0.42 %

Silves	0.30 %
Tavira	0.38 %
Vila do Bispo	0.40 %
Vila Real de Santo Antonio	0.45 %

### 2016 Municipal Tax Rates (*by council*) - MADEIRA

Calheta	0.32%
Câmara de Lobos	0.34%
Funchal	0.32%
Machico	0.30%
Ponta do Sol	0.30%
Porto Moniz	0.30%
Porto Santo	0.30%
Ribeira Brava	0.30%
Santa Cruz	0.30%
Santana	0.30%
São Vicente	0.30%

### 2016 Municipal Rates (*by council*) - GREATER LISBON

Amadora	0,36%
Cascais	0.39%
Lisboa	0.30%
Loures	0.39%
Mafra	0.50%
Odivelas	0.38%
Oeiras	0.34%
Sintra	0.37%
Vila Franca de Xira	0.30%

How these coefficients will play out in the marketplace still remains to be seen. Will a 3.0 be a sign of ultimate prestige and luxury? If so, *Quinta do Lago* and *Vale de Lobo* will have to demand an upgrade since both surprisingly fall short of this perfect mark. On the other end of the spectrum, will a lovely council on the banks of the *Guadiana* such as *Alcoutim*, or *São Brás de Alportel* nestled in the mountains, suddenly become in demand because of their low rates? Only one thing is certain. Perspective buyers have a new and important element in the equation when searching for a new home.

### **Factor nº 5: *Quality of Construction***

This component is a two-edged sword: features, such as a swimming pool or private garage, will push up the overall value of your home. Living on a dirt track, as opposed to a tarmac road, lowers the appraisal. Note that the single family dwelling coefficient is determined along with the location factor. Actual “Quality of Construction” and “Exceptional Location” will need to be determined by a *Finanças* assessor on a case-by-case basis so your calculation will not be wholly accurate. Nevertheless, you’ll still be close and you will have unveiled what, until now, has been cloaked in mystery.

The remaining sub-coefficients all have fixed values as follows:

<u>FIXED RATE COMPONENTS</u>			
<i>Increase:</i>	<i>%</i>	<i>Decrease:</i>	<i>%</i>
Closed Condominium	0.20	No kitchen	0.10
Single Garage	0.04	No bathroom	0.10
Collective Garage	0.03	No running water	0.08
Private Swimming Pool	0.06	No electricity	0.10
Collective Swimming Pool	0.03	No gas	0.02
Tennis Court	0.03	No sewage	0.05
Other Leisure Equipment	0.04	No paved road	0.03
Central Air Conditioning	0.03	Diminished living quarters	0.06
Elevator (< 4 stories)	0.02	No elevator (>3 stories)	0.02
		Building in poor repair up to	0.10
<u>VARIABLE COMPONENTS:</u>			
Single Family Dwelling (0,0 - 0.20 %)			
Construction Quality (0.0 - 0.15 %)			
Exceptional Location (0.0 - 0.10 %)			

With all of the pieces in place, you are ready to assemble your “*VPT*”. The simplest way to do this is to use the Finanças’ internet simulator.  
<http://www.e-financas.gov.pt/SIGIMI/default.jsp>

### **Final Property Registration with *Finanças***

Whenever a property is transacted, a “*Modelo 1*” must be completed. You will be asked to submit architectural drawings of the house and situation of the property. The outcome of this process will be the determination of the “*VPT*” and any tax owed will be based on this figure. If a preliminary assessment has been made on transitional values, then a second assessment will be levied based on the difference. Eventually, all properties will undergo the “*Modelo 1*” process so that eventually, over a 10 year period, all properties in Portugal will be brought up to the new norms.



There are many great reasons to seriously consider investing in property in Portugal, including:

- Creation of wealth;
- Opening up alternative life and work style choices;
- Managing investment risk by adding diversity to your investment strategy;
- Offsetting times of poor portfolio, endowment & pension funds performance;
- Supplementing pensions;
- Increasing retirement options;
- Excellent history of growth in value.

## **A Unique Investment**

Investing in property is truly a unique investment:

- The investor benefits 100% from any capital growth, even when mortgaged up to 85% of the value of the property;
- People are willing to pay to live in your investment, which can cover your costs of ownership and contributes to your income, particularly as rentals grow in time;
- Extremely tax efficient - rental income is also partially offset against mortgage interest, as are most costs in maintaining and running the investment property, before tax is assessed;
- Ability to extract cash from your investment at your discretion from time to time.

## **Financial Performance of Property**

The attraction of investing in property continues, and with good reason. Residential property has exhibited extraordinary growth in recent years, and even over the long term, has outperformed the stock market.

Over the last 30 years, property values have doubled every 7-10 years and rental income has also doubled every 9 - 12 years. Growth in recent years has been extraordinary, but is still forecasted to continue; even though at more modest levels.

## A) BUY TO LET

### Why Buy-to-Let

Buying a property to let can serve as a stand alone investment option or work in conjunction with long-term personal goals for eventual retirement. Since this practice has the potential to include many problems as part of the package, it is definitely not for everyone. But when well managed, there are promising rewards.

### Capital Growth

Over the long term property is almost always an appreciating asset. Unless you buy at an inflated price, let the place fall into disrepair, or some kind of disaster besets the structure, then you should eventually end up with a property worth considerably more than you paid for it.

Studies have shown gross property values on average have increased by a factor of 22 over the last 30 years. With foreseeable demographic pressures in Portugal over the coming years, demand for housing is set to boom. There is no reason to suggest that this long-term appreciation trend will change.

It is for this reason that many people invest in property purely for long term profit, hoping to make money on the rising value of a property. It can be a very successful vehicle if you know what you are doing, choose the right areas and properties and, most important, have a bit of good luck.

### Income

Some people manage to make a tidy income from renting out property. However, this is also the investment objective that has the highest failure rate. Choose the wrong property and you can find that much of your supposed income is eaten up by maintenance, repair costs, mortgage payments during void periods, refurbishment, financial products, lettings agent fees and various other expenses.

### Retirement Planning

Property is an increasingly popular choice people among people planning for retirement. This has in part been driven by falling annuity rates, that mean pensions may not provide the returns previously expected. Shrewd property acquisitions can remove much of the dependence on a pension. If approached correctly, a buy to let investment can be self financing over the life of the loan repayments. Once the mortgage has been repaid, the property can provide a useful and sometimes sizeable income.

With a personal pension, you cannot access your cash until you retire. When you do, you are then forced to buy an annuity, which are subject to variations in their rate, meaning that you cannot guarantee how much you will end up receiving. With property, you can access the cash at any time you wish, by selling up. As well as having an investment that could provide you with a regular long term income, you end up with a sizeable asset that you can pass to your children or other relatives.

### **Current Market Conditions**

Today there is much talk about melt down in the Buy-to-Let market place caused by escalating increases in property value and predicted increases in interest rates. However, many industry experts share the view that the buy to let market will continue to thrive whatever the external factors.

If you look at the housing market during recession, people are more likely to rent than buy, particularly first time buyers. If prices are static or even falling, investors will be able to buy at a more realistic price and with the higher demand for rental properties, yields will, if anything, increase over and above those we have seen in the buoyant market of the last few years. Likewise if interest rates increase, first time buyers in particular are more likely to stay in rented accommodation, producing the same result for the investor as above.

### **Future Trends**

It is our view that Buy-to-Let should continue to be a sound long term investment, especially as reports show rental yields at record levels as well as increasing numbers of new tenancies, together with the ongoing potential for capital appreciation. By comparison, in recent years we have seen huge stock market declines, pension and endowment mis-selling scandals and extremely poor returns on deposit based investments.

Another significant boost to this market seems likely from April 2006 following Gordon Brown's announced plans to permit pension funds to invest in residential property throughout the European Union. Many experts predict that this could lead to large amounts of money pouring from the stock market into buy to let property.

## RENTALS IN PORTUGAL

Over the past 30 years, it has been increasingly difficult to find properties to let or, conversely, landlords willing to rent in Portugal. This is not due to any fundamental shortfall in housing on a national level. To the contrary, Portugal has one of the largest housing stocks per capita in the European Union. Yet more often than not, these second and third homes stand empty while young couples, students, etc. find it nearly impossible to find rental accommodation under reasonable conditions.

### Background

Why such an imbalance? Historically, rental properties used to be quite abundant in Portugal. Years ago, it was common to see a small white paper square taped in each of the windows of an apartment or house that meant “For Rent”. In those days, prior to Social Security, it was common for middle class families to save and eventually purchase property to rent to create an income flow that would sustain them in retirement, just as you may be contemplating to do today.

When the Revolution came in 1974, all of this changed. Radical new laws were passed, giving tenants more rights than the landlords. Rents were frozen as well as the Rateable Value (“*Valor Patrimonial*”) for all practical purposes. As History has proven over and again, when time becomes artificially arrested, distortions set in that eventually grow to ludicrous proportions. On the eve of the 2003 Property Tax Reform, one half of the property owners in Portugal (those owning older housing) paid only 1% of the tax collected. At the other end of the spectrum, less than 1% of the owners (brand new housing) contributed over a third of property tax revenues. It is no wonder that the system needed a serious overhaul!

### Market Distortions

These generalised low Rates assessments have had a perverse effect on the Rental Market. With overhead so low on most older properties, there was no need to bring in income to offset costs. Likewise, with little or no income from the properties, many older buildings have gradually fallen into a sad state of disrepair and, in some cases, serious degradation. This artificial lack of supply has led distorted prices on the few flats available. Both major political parties have proposed sweeping changes in the legislation governing property rental. However, with the rapid turnover in governments in recent years, none of these proposals have as yet been enacted into law. As a consequence, we are still in the waning years of a warped system where landlords either are forced to subsidise sitting tenants

or else do not dare to rent out for fear of losing control over their property. But all the news is not bad. Change is inevitable and with it opportunity. The basic market conditions that regulate the Rental market elsewhere will come into place in Portugal as well. With decades of pent-up demand, this market promises to have significant potential, at least until a more normal equilibrium settles into place.

### **Local Agents vs. Self Administration**

One of the early decisions to make will be whether to rely on local agents to carry out your plan or putting in the time and energy yourself to make your project come to fruition. Not everyone is a “*do-it-yourselfer*”. Even if you are, taking matters into your own hands may be appropriate in one situation yet not in the next.

If you are non-resident in Portugal, than the choice may be an obvious one. You will have to find local agents to meet requirements. Even for residents, it is not simply a matter of having the time and presence. In a highly bureaucratic environment such a Portugal, knowledge of both the language and the systems can be essential.

### **Perspectives**

In the meantime, before the long-term perspectives come to fruition, what are the alternatives for a potential landlord?

- *Short-term Contracts*

One solution is to use short-term contracts. While these call for frequent renewals, they also reduce the risk of not being able to get rid of an unwanted tenant

- *Holiday Lets*

In popular tourist areas such as the Algarve, one or two week lets to tourists during the high season can prove a profitable enterprise. It is much more of a business - almost like running a Bed & Breakfast - and has different regulations as well as a specific tax regime.

- *Senior Lets*

Some foreign residents find that, as they get into their later years, the dream home they once bought when they first retired has become more of a burden than a blessing. By selling an appreciated property, they free up much needed capital that can enhance their standard of living in their twilight years and renting proves to be a viable option.

From a landlord's perspective only the latter provides a more dependable solution. As the distortions in the marketplace gradually work themselves

out, more stable opportunities should arise. Since most investors in the Property tend to have a more long-term perspective, we may be on the eve of “perfect timing”.

### **c) LEVERAGING OR GEARING**

A unique aspect of property investment is the phenomenon known as Leveraging or Gearing, where your investment benefits from the capital growth of both your equity and the mortgage you borrow. This is best explained with an example:

If property increases in value by 9% after one year, the value goes up to €168,000, an increase of €14,400.

By renting out the property (with income and costs being equal), the return on investment is not 9%, but €14,400/€24,000, or 60%.

In the above example, if the property then continues to increase in value by a modest 5% per year, after 7 years:

The value of the property will increase from €160,000 to €233,000, a

Property Purchase Price: €160,000

85% Mortgage: €136,000

15% Invested Equity: € 24,000

gain of €73,000, or 46%;

The equity you hold in the property will increase from €24,000 to €97,000 – an increase of 301%. If the same €24,000 had been invested in the stock market and grew at 5% per year, you would have seen your investment grow to just under €34,000. To achieve the same growth as our property example, the stock market would have to grow by almost 21% every year. How likely is that versus the conservative growth in the property market of 5%?

One huge benefit of property investment is the ability to remortgage properties, subject to adequate rental to mortgage interest cover (typically 125-130%), to release tax-free funds for any purpose – to accelerate property investment, fund life-style needs or work-style changes.

This is the main technique that allows investors to grow their portfolios without having to inject new money, and to continue to benefit from gearing. Extracting money from one property to invest in a number of others is the keystone to creating serious wealth from the property market.

## D) DOWNSIZING

The decision to sell your home in retirement (and subsequently buy a small apartment or rent) is commonly influenced by a number of factors, both emotional and financial.

People choose to sell for one of several reasons:

- to help reduce expenses;
- to provide a capital base to generate retirement income;
- to simplify their lifestyle;
- because of change in circumstances (financial or health).

From a strictly financial perspective, the decision to sell a home is most often made when the income generated from the sale -- combined with the elimination of any housing-related expenses -- exceed rent costs. Here are some important points to consider:

To help reduce expenses:

- mortgage if not paid off
- property taxes and maintenance charges

One or more of these conditions may make it difficult to manage financially or reduce your lifestyle expectations beyond what you would want. Before making the final decision, investigate what type of living arrangements you would like and how much they would cost to make sure that the savings are really there to support you.

- To provide a capital base from which to generate income:

If you find that your retirement income doesn't quite meet your expenses, the capital you will free up selling your home can be invested in income-producing investments, providing you with the extra income you may need.

Again, look into what type of living arrangements you would choose and how much they would cost to make sure the extra income would cover those living expenses and more.

- To simplify your lifestyle or better meet your new lifestyle:

Would it be more convenient to live in a smaller place? Or a place that's closer to certain facilities - friends, family, activity centers you plan to use regularly, etc.?

Do you feel comfortable living in your current neighbourhood in the future? Especially if you should become less physically active? Are there facilities nearby? Is public transportation conveniently located? Is the neighbourhood relatively crime-free? Are there stores nearby, or delivery services?

Look closely at your current home: are there many stairs? Slippery floors? Do you believe you will be able to comfortably do all the chores your house requires as the years go by?

What about your retired lifestyle? How much traveling are you planning to do? If you're spending most of your time traveling, will your home be empty while you're away? Do you have a cottage where you're planning to spend much of your retirement years? Do you belong to a community club or church where you're planning to spend much of your time? These decisions will help you decide whether it makes better sense to sell your house and downsize or simply relocate.

- Change in circumstances:
  - If you're finding it difficult to keep up maintenance or repairs;
  - If you have mobility or strength problems - you're find it difficult to climb stairs, or are having problems preparing meals, for example; or
  - You're experiencing short-term memory loss, like forgetting to take medication, or key dates and commitments; or
  - You're experiencing a change in financial circumstances;
  - You may find that moving to a smaller place or a retirement community is right for you.

## **E) EQUITY RELEASE**

Many older homeowners are unaware it is possible to release the equity in their property. Two types of scheme are available. Homeowners generally need to be aged at least 70 to take advantage of either.

### **Home reversion scheme**

In this scheme the client sells their home, or a percentage of their home, to a plan provider. In return they receive a cash lump sum or a monthly income, or a combination of both. The amount available to borrow is normally dependent on age or gender - for example the younger you are, the less you receive; and it is taken into account that women are expected to live longer. The person can remain in the house rent free until the last remaining borrower (if a couple) dies or is transferred into long term care. When the property is sold, the plan provider reclaims their percentage with the remainder going towards specified beneficiaries. However, the same percentage of any future rise in the value of the home would also belong to the plan provider.

## **Cash release scheme**

With this scheme the homeowner takes out a fixed rate interest only mortgage on their property and uses the borrowed money to purchase a regular income. There are no monthly repayments to be made as the interest is accumulated over the life of the mortgage. When the borrower dies or is moved into long-term care, the original loan plus accumulated interest is repaid. The longer you live the larger the interest that will be due. It is important to consider taking out a fixed interest loan with a guarantee that the amount owed will not exceed the value of the house, therefore ensuring no risk of negative equity.

## **F) OFF PLAN - *Buying Property Off Plan***

Purchasing property from plans offers a solid investment opportunity and is a preferred property investment option for large and small property speculators.

In Portugal and Spain, Off Plan property purchasing continues to offer high return on investment. The additional benefit to the property buyer is the relatively small initial outlay - usually a 30% deposit with the balance due on completion of the complex, when property has already appreciated due to the strength of the property market.

Buying Off Plan Property can offer strong investment returns:

- It's possible to achieve returns of over 100% of your initial investment within 24 months;
- Profit can be free of capital gains tax;
- Long-term ownership of the property benefits from the property appreciation in the fastest growing market in Europe.

Why Buy Off Plan Properties-

- Developers offer lower more competitive prices to off-plan buyers, sometimes below market value, to secure immediate finance;
- Access to better investment opportunities; penthouses, layout, square footage which generate a better return at resale;
- Own a brand new property on completion.

Only pay 30% of property value as a deposit with no further payments until completion when the remaining 70% can be financed with a mortgage or the property sold at its increased market value.

Take advantage of future market appreciation at current market rates.

## **G) FRACTIONAL OWNERSHIP**

Usually offered in the form of a Private Residence Club, fractional ownership is title to real property or a share in a company owning the property, making it possible to own a holiday residence without worrying about maintenance, taxes, or property management. You pay for the weeks or months you use or rent with the costs shared between the owners of each residence.

Many fractional ownership purchasers chose a Private Residence Club for the lavish amenities and the limited time they have to spend at their holiday home. The added value is very appealing, especially when compared with timeshare or full ownership. Timeshare, no matter how luxurious, is a usage contract; and full ownership comes with full responsibility, including maintenance—a headache for owners living at a distance.

Fueling the growth of this active slice of the holiday home market is the fact that fractional ownership requires far less capital investment. And, because it is deeded ownership, you have a real asset, one you can will to heirs, sell, rent, or mortgage.



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nº 6: *The Portuguese Nominee Company*  
**“the better way to hold Portuguese property”**

At *euroFINESCO*, we continue to investigate options available to potential property owners in Portugal and can now recommend with confidence using a small Portuguese company structure that may well prove to be the most appropriate vehicle for purchasing property in Portugal: the **Portuguese Nominee Company**. This form of home ownership offers many of the advantages that property buyers once sought in Offshore Property Companies but achieves these objectives in a compliant, mainstream fashion. This type of non-trading company can provide stability as well as attractive benefits, meeting diverse potential needs:

- First-time Home Buyers in Portugal;
- Investment Properties → Buy-to-let;
- Property Subdivisions;
- Downsizing;
- Off-plan Investing;
- Capital Gains Tax Mitigation;
- Offshore Property Companies (both white & blacklisted).

### **A Fully Compliant Structure**

In fact, although infrequently used in recent years, these small Nominee Companies have existed in Portuguese statute law since the 19<sup>th</sup> century and have been embraced in subsequent legislative reforms over the past 150 years. Therefore, they are fully compliant and are not subject to any of the punitive laws that have made Offshore Property Companies a pariah: no deemed income assessment, no 5% Rates bill. In fact, the simplicity of this form of company makes this structure easy and inexpensive to run.

### **Lower Taxation**

One of the big advantages of the Nominee Company is a substantial reduction in the Capital Gains rate on the sale of the Company when compared to non-resident entities. As a resident corporate structure, CGT assessment is only 10%, some two and a half fold less than the 25% rate that a non-resident company (Delaware, Malta and other Offshore) would be

required to pay. In addition, this assessment is flat-rated, so your profit will not push up the rest of your income into a higher tax bracket. While not as low as the eventual CGT exemption of an “*S.A.*” (*Sociedade Anónima* or PLC equivalent), the operating costs of a Nominee Company are a fraction of those of a “*S.A.*”, thereby making the structure much more attractive to both owners and to future buyers alike. In addition, there is a potential exemption from Property Transfer Tax (“*IMT*”) for the new buyer, something that would be impossible under direct property acquisition. If future shareholders avoid a 75% or greater concentration of shares in one individual, then the purchase of the Company’s shares will not trigger “*IMT*” (formerly called “*Sisa*”). Like other assets in Portugal, bequests upon death or gifts during one’s lifetime are tax exempt to immediate relatives: spouse, children, grandchildren, parents or grandparents. All others will be assessed Stamp Duty of 10%.

### **Ease of Transfer**

With the property secured safely within the Company, bureaucracy is significantly reduced at the time of sale, cutting costs and complications so often associated with property ownership in Portugal. A simple deed of transfer, declaring the sale of the shares, is all it takes, thereby avoiding the headaches related to licencing, registration and ever-changing rules related to property paperwork. This form of home ownership offers simplicity and full compliance while embracing many advantages that property buyers once sought in Offshore Property Companies.

### **No Benefit-in-Kind Assessment**

Within Portugal, Nominee Companies are not subject to benefit-in-kind nor deemed income assessment as was imposed on Offshore Companies. Under Fiscal Transparency rules, Nominee Companies are, in fact, tax-exempt.

While there has yet to be specific rulings from Tax Authorities in other EU jurisdictions regarding potential benefit-in-kind assessment for non-residents in Portugal, it is clear that the presumptions surrounding this type of taxation do not apply to Portuguese Nominee Companies and their owners:

- a) As a non-trading entity, the Nominee Company has the sole purpose of administering its assets to the benefit of the shareholders;
- b) The Company is bound to full Fiscal Transparency;
- c) The Company is required to have administrators with statutory compliance obligations.

Both under Legislation as well as Company Statutes, there is clearly no basis to conclude that the Shareholders could be construed as “*Shadow Directors*”, the underlying premise for any benefit-in-kind assessment.

## **Restrictions**

There are certain restrictions to such structures. Whether these limitations prove to be a negative or not depends upon your situation.

- 1) First of all, the company and shareholders must be declared in the Public Registry. There is no confidentiality as was typically the case in Offshore jurisdictions. Any assessment, although calculated by Company Code rules, is taxed directly to the shareholders, not to the Company under a regime referred to as “Fiscal Transparency”.
- 2) Shareholding is also constrained. These Nominee Companies must have a minimum of two shareholders but no more than five. These shareholders are normally individuals and members of the same family, although collective entities such as companies or trusts may be shareholders in certain circumstances.
- 3) The Company is required to have administrators in order to meet basic compliance obligations. However, these requirements are not extensive and annual operating costs are modest. Auxiliary overhead is also minimal. This type of company does not pay the minimum corporate income tax (“PEC”) as would a commercial Limited Liability company.

## **Domiciliary Services**

In addition to orchestrating the formation of your Company to Portugal, *euroFINESCO* is also prepared to provide all necessary on-going administrative services required in Portugal. As Company Administrators, our basic services include:

- Resourcing accurate and current information in Portugal to Beneficial Owners regarding Company obligations as well as relevant legislation;
- Clarification of pertinent procedures and interpretations with *Finanças*;
- Communications liaison between *Finanças* and the Nominee Company;
- Reporting to Beneficial Owners regarding requirements in Portugal;
- As your Administration, we are qualified & prepared to meet all compulsory company compliance commitments.

In fact, this administrative structure also provides an important support structure of knowledgeable, local professionals who are on your side if and when things go wrong (which is all too often!).

## eBooks from euroFINESCO

- 1) Offshore Companies: *Moving Onshore*
- 2) Self-Employed in Portugal
- 3) Requirements of the Common Reporting Standard
- 4) Setting Up Fiscal Residence
- 5) Capital Gains Tax on Portuguese Property
- 6) Portuguese Tax Code Summaries
- 7) “*VPT*” Unveiled
- 8) Tax-Efficient Investing in Portuguese Property
- 9) Income from Portuguese Property
- 10) Taxation on Portuguese Property
- 11) “*S.C.I.*”: *Sociedade Civil Imobiliária*
- 12) Property Companies: *White-List or Portugal*
- 13) Nominee Companies for Portuguese Property
- 14) Fiscal Representation in Portugal
- 15) “*Permutas*” or Property Swaps
- 16) Estate Planning & Nominee Companies
- 17) “*I.H.T.*” – Residence Rules & Determining Domicile
- 18) Moving to Portugal – *before, during & after*
- 19) Taxation of Pensions in Portugal
- 20) “*I.R.S.*” Tax Credits
- 21) CGT Mitigation: *14 Arrows in the Quiver*
- 22) Residence Rules: *in the EU, Portugal and the UK*

### Extracts from *Relocating to Portugal - Useful Information*

- 23) Acquiring Portuguese Citizenship
- 24) Visas and Legal Framework
- 25) Your Rights to Health Care
- 26) Access to Education
- 27) Recognition of Qualifications
- 28) Social Security Entitlements
- 29) Golden Residence Visa
- 30) Leaving Portugal - *Moving Back*
- 31) Non-Habitual Residence Status and the Alternatives
- 32) Trusts, Foundations and Fiduciary Structures