REDOMICILIATION: White-Listed Companies
"The Triangulation Trap"

Those who redomiciled to Delaware or Malta are faced with the following dilemma: while they have managed to escape for the time being the immediate consequences of punitive taxation on blacklisted companies, they have failed to resolve one of the fundamental problems: *the Sovereignty Issue*. No government likes to lose control over a piece of sovereign territory, especially when it means giving up most taxation rights. Portugal is no exception. This is why the OECD introduced measures in the current version of the Model Double Tax Treaty to enable countries to assess Capital Gains on effective property transfers wrapped in foreign Company.

Tax Treaties

As an example, let us examine the case of a Delaware Company. In the USA - Portugal Tax Treaty, Article 14 (*Capital Gains*) states:

> *"1. Gains derived by a resident of a Contracting State from the alienation of immovable property (real property) situated in the other Contracting State may be taxed in that other State."*
>
> *"2. For the purposes of paragraph 1, immovable property situated in Portugal includes stock, participations, or other rights in a company or other legal person the property of which consists, directly or indirectly, principally of immovable property situated in Portugal..."*

To translate "*Treaty Speak*" into Plain English, this article states that the country where the property is located (Portugal) has taxation rights on the deemed transfer of the property upon the sale of the shares. It is important to note that these tax treaties take precedence over national legislation.

This provision mirrors the OECD Model Tax Treaty, giving countries the tools to combat fiscal fraud. With only minor variations, this condition is clearly defined in most other Portuguese bilateral tax treaties. Therefore, a white-listed Company normally offers little protection from CGT for Portuguese residents.

The most recent attack comes in the 2018 Portuguese State Budget which introduces an enhanced definition of Capital Gains on Immoveable Property mirroring provisions already in tax treaties. When shareholders' sell their shares in a non-resident company which derives more than 50% of its value from real estate located in Portugal, *Finanças* now has been given the right to tax the transfer as an immoveable property conveyance rather than the mere sale of shares in national legislation.

Non-Residents - *a potential Double Whammy*

But what if you are not resident in Portugal? Are you safe from liability to Portuguese assessment? The situation could be just as bad.

While you may not be resident in either jurisdiction, the Company still is. The Delaware Company, as a "*resident person*" embraced by the USA - Portugal Treaty, could be liable to CGT assessment, based on the effective transfer of rights to the property set off by the sale of the shares. However, in the case of a British or Irish tax resident, the respective treaty with the USA is oblivious to the Portuguese "*situs*" issue and is only concerned with the gain from the sale of shares as "Moveable Property", triggering a separate individual CGT assessment in the home jurisdiction based on worldwide income. Because of the triangulation between jurisdictions, the bilateral accords leave no means to eliminate double taxation.

Under current Portuguese legislation, new measures beefing up anti-avoidance practices were brought into place with *decree-law 39-A/2005 of 29 July* which states explicitly that any capital gains tax exemption is lost on the sale of shares when more than 50% of the company's assets is real estate in Portugal.

To exacerbate the potential problem even further, the same principal of deemed real estate conveyance could also apply to Property Transfer Tax (“*IMT”,* formerly called *Sisa*). Overall, as a non-resident, the sale of the shares of the white-listed Company could attract Portuguese Capital Gains Tax of 25% and an additional “*IMT*” assessment of up to 6%.

“the Triangulation Trap”

To restate the obvious, the taxpayer might be faced with being taxed twice: once, in the Company from the *de facto* transfer of rights to the Portuguese property, and also as an individual on the gain from the sale of US shares within a worldwide assessment in the home jurisdiction.

Under Portuguese law, as elsewhere throughout the European Union, it is your obligation to declare all of your taxable income. It is *Finanças'* job to evaluate and assess income or implement coercive measures if you do not fulfill your reporting requirements. If left undeclared, a liability could remain in the Company as an eventual charge against future shareholders.

Conclusion

Ever since the Bank of Portugal issued the edict to stop mortgage lending to Offshore jurisdictions, attitudes have begun to change.

One thing is quite clear: using a third-country jurisdiction to veil property transfers and fiscal obligations could be a risky proposition. Tax Authorities in Portugal and around the world now possess powerful “tools” to close loopholes that were once common practice. The option of a “*white-listed*” Company should be considered anything but “best” advice for professionals and probably not a sensible solution for the majority of property investors in Portugal. Using a third jurisdiction company to hold a Portuguese property most likely will not meet the objective of avoiding taxation but rather the contrary: compound the risk of being snared twice in one's own “*Triangulation Trap*”.

We believe that there is a safer, fully compliant alternative: using a *Portuguese Nominee Company.*

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