CGT REINVESTMENT
Strict Interpretation

After a few years of stability during the real estate meltdown, *Finanças* has tightened its interpretation of *Capital Gains Tax* law under *"IRS",* limiting CGT deductions. In question is the concept of reinvestment of the proceeds of the sale of one's principle residence.

Let's suppose that you sell your home this year. The calculation of capital gains is done by following these steps:

Step nº 1: Based on the year of purchase, multiply the original deed price by the Inflation Adjustment Coefficient. This gives the *adjusted purchase price.*

Step nº 2: Subtract the adjusted purchase price from the *sales price* as declared on the Deed of Sale.

Step nº 3: In the event of a profit, subtract any qualifying buying or selling costs (real estate commissions, notary fees, transfer tax, etc.) as well as documented capital improvements to the property over the past 12 years. This is your *net taxable gain*.

Step nº 4: As a resident, 50% of the *net profit* is taxed unless the gain is rolled over into another principal residence. Either way, always report the sale on your annual *IRS* declaration.

It is Step nº 4 where things begin to become complicated. Legislation provides an extended period to make the reinvestment:

a) Up to 24 months prior to the sale of your principal residence, you can pre-purchase either an existing dwelling or a building plot as your replacement property;

b) In the 36 months after the sale, you can re-invest in a dwelling or a building plot including construction costs.

We draw attention to the difference now being enforced between the two options. When the reinvestment occurs within the 3 years following the sale of the old residence, legislation envisages several situations for replacement, including construction. But when the rollover occurs within 2 year prior to sale, relief can only be achieved in the acquisition of new housing or a building plot, not construction or capital improvements. In a nutshell, if you pre-purchase a building plot, only the land is deductible, not the construction costs.

Note that, in order to achieve partial or full exclusion from capital gains taxation, the following conditions must be met:

1. To achieve full Capital Gains Tax exemption, the full proceeds of the sale must be reinvested. Otherwise, relief is granted on a *pro rata* basis;
2. When reinvesting in another property, the purchaser must formally establish residence within six months following the completion of the reinvestment period;
3. In the case of reinvestment through the acquisition of a building plot, the purchaser must begin the build within six months after the reinvestment period or request registration of property within 2 years of the date of commencement of construction. In any case, reinvestment must be completed by the end of the fifth year following the sale of the property to be replaced;
4. In the event that restoration or major construction occurs as part of the reinvestment, planning permission is required. Following completion of the approved project, the old registration number will struck off and a new registration issued. For this "new" property to qualify for CGT relief, reinvestment must be completed by the end of the fifth year following the sale of the replaced property.

As you can see, understanding the fine print is essential. Whatever your plans, it is always wise to seek experienced, professional advise when mitigating Capital Gains Tax. Potentially, there are many thousands of Euros at stake. With strict rules and rigid deadlines, careful planning is in order if your want to take full advantage of the opportunities at hand.

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