CAPITAL GAINS TAX
"Permutas"

Tax Implications

As with any property transaction in Portugal, the legal minimum transaction price for "*permutas*" is the rateable value ("*VPT*"). This fiscal evaluation is also the basis for annual "*IMI*" Property Rates. A "*permuta*" will trigger a update of the "*VPT*" which will be used to calculate any tax due. This may occur at the point of sale or, more likely, several months later. Beyond these restrictions, the buyer and the seller are free to negotiate the final value of the exchange.

Low or no "IMT"

The final transaction value is based on the formula "**A - B**", not "**A + B**". "*IMT*" (Property Transfer Tax) will only be calculated on the *difference*. Since Property Transfer Tax is progressive in nature, the tax savings will be even greater. When "**A = B**" (properties declared at equal value), there is no "*IMT*"due.

Low or no Stamp Duty

Stamp Duty on the deed is assessed at the rate of 0.8%, also based on the difference between the two values, with the owner with the larger amount paying the tax. If the amounts are equal, there is no tax to pay.

Partial or full CGT Exemption

As in any property transfer, the Capital Gain is calculated on the difference between the original price in the deed of acquisition, adjusted for inflation, and the net sales price, reduced by necessary expenditures, capital improvements within the previous 12 years and any outstanding shareholders' loans and/or bank mortgages.

Rollover Relief is achieved when there is a full re-investment of the proceeds of the sale of the *principal residence*. In the case of a "*permuta*", the "sales price" will be of equal value to both: either a) the higher property value or b) the lower property value plus the cash difference.

The swap simultaneously accomplishes both the sale (*"alienação"*) of the former *principal residence* and the purchase (*"aquisição"*) of the new one. Since both are of equal value ("**A = B**"), there is a full re-investment of the proceeds, achieving a full exemption from Capital Gains Tax for both parties.

If one of the parties receives a cash balance to compensate any divergence in underlying property values, this difference will be seen as a gain and will be taxable on a *pro rata* basis.

Swaps between spouses

When a couple is married under the Separate Assets Regime *(Separação de Bens)*, property can also be exchanged between the two. If each is registered with Finanças living in independent principal residences, these abodes can be swapped with little of no capital gains, based on the automatic reinvestment achieved under a swap as described above.

For couples registered under the Community Property Regime (*"Comunião de Adqueridos"*), they can follow the same procedure if they previously register with a notary a Declaration of Separate Persons and Assets ("*Separação de Bens e Pessoas"*). While this declaration is normally a precursor to a divorce settlement, the law allows couples to "kiss and make up" and get back together after the swap is in place.

Short-term Swaps

Even if your interest in an exchange may not be permanent, you may find the rewards to be worthwhile on a temporary basis to resolve certain problems associated with property ownership. By applying the swap principle, ***a short-term swap*** - a form of double exchange - both anticipates and eliminates Capital Gains Tax for an eventual sale.

An Illustration

John and Mary bought their home in the hills of the Algarve in 1990. Old farmhouses were inexpensive in those days as were labour and materials. After a few plans, a couple of years and almost no records of expenses, they had their dream home.

Twenty years later, their modest investment had a market value of almost a million euros, most of which was capital gain, even had they managed to save their invoices.

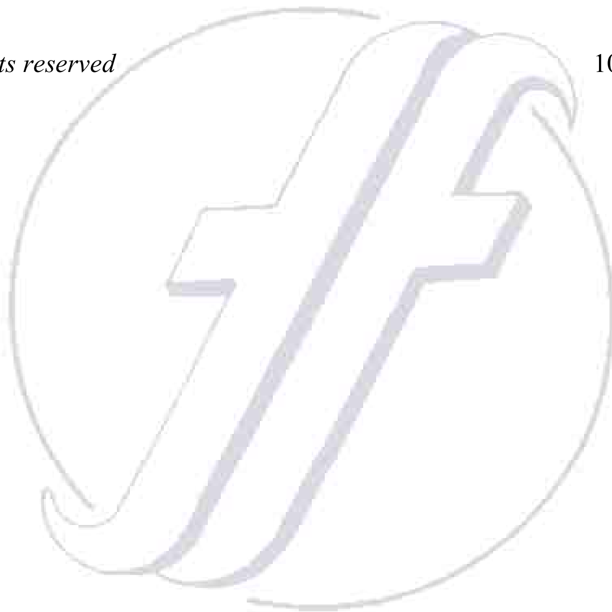
As they were getting on in years, they began planning for a "*downsize*" to a simple bungalow with a small garden. But the prospect of paying a huge CGT bill left them both with sleepless nights.

"Then came the idea of the Short-term Swap"

1) First, they made an agreement to swap properties of similar value;
2) Next, they swapped homes - on paper only - at an identical value. Because the swap involves properties of equal worth, there was no "*IMT*" and no Stamp Duty - only due on any difference in values. Because both were trading their principal residence, they were still eligible for *Rollover Relief* on Capital Gains. The "*permuta*" means that they both achieved an immediate reinvestment of the proceeds, so the transaction was exempt from Capital Gains Tax.
3) Finally, a few months later, they swapped back, also for equal values. Once again, no IMT, no Stamp Duty, no Capital Gains Tax.

4) Now both owners have as the base of acquisition of their respective properties the new uplifted value rather than their respective historical purchase prices.

With no outstanding CGT liability, they can now sell, buy their little bungalow and invest the balance to supplement their retirement income. *A happy ending!*



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