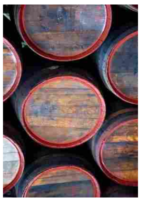
*euro*FINESCO *s.a.* FISCAL & EXPATRIATE SERVICES

an *ePublication* from *euro*FINESCO

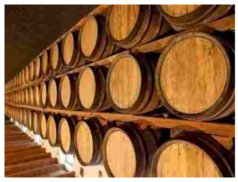
nº 14a - Summer 2012



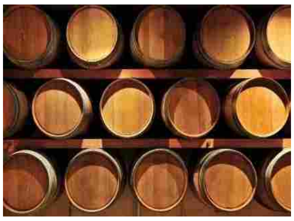
"Permutas" - Property Swaps

In Portuguese, a property barter exchange is called a "*permuta*". Rather than purchasing a property for money, two owners swap their respective homes, normally making up any difference in value with cash. Just like a normal sale, a "*permuta*" is accomplished via public deed with equal recognition under the law to other forms of conveyance . . .

Tax Implications of Swaps - *Lower or No Assessment*



The ***swap*** simultaneously accomplishes both the sale of the former *principal residence* and the purchase of the new one. In other words, since both are of equal value ("**A = B**"), there is a full re-investment of the proceeds and therefore full exemption from Capital Gains Tax is achieved by both parties . . .



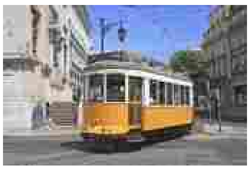
Swapping Property Company Shares

In a nutshell, a property company turns immoveable property into moveable property, substantially altering how transactions are assessed. Because the shares change hands and not the underlying properties owned by the respective company, there should be no "*IMT*" (Property Transfer Tax) except under special circumstances. There is also no 0.8% Stamp Duty charged on the deed since no property changes hands, just shares.

A Short-Term Swap

Even if your interest in an exchange may not be permanent, you may find the rewards to be interesting on a temporary basis to resolve certain underlying fiscal problems that you may face with your property.

Let's look at the example of how a *short-term swap* can eliminate most, if not all, of the capital gains tax liability that has accumulated over the years . . .



Closing Notes: News Briefs

- *Increase in Higher Rate Taxpayers in UK*
- *Living Will approval in Portugal*
- *Court Rules IMI notices are illegal*
- *New Rules on Cross-Border Succession*
- *Subsidy cuts declared unconstitutional*
- *UK Statutory Residence Test*
- *Border controls within the EU*
- *EU eases Cross-Border Succession*

*euro*FINESCO *Services:* **Tax Consultancy** ***Fiscal Representation*** **Nominee Companies** ***Estate Planning***

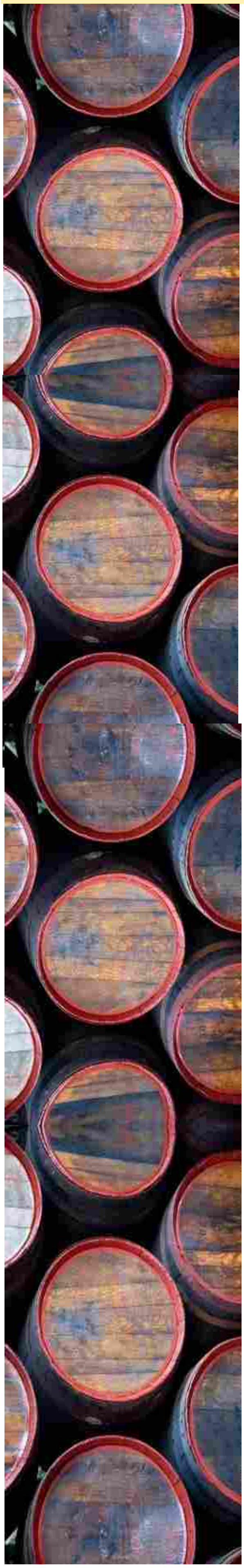
Important Dates:	*"IVA"* - online declaration	10 July
	"IRC" - 1st payment on account due	31 July

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

Lisbon
Rua Ant. M. Cardoso, 15, 4ºD
1200-273 Lisboa (Chiado)
tel: +351 21 342 4210
fax: +351 21 342 4212

Madeira
Rua do Aljube, 61, 2º Dtº
9000-067 Funchal (*Sé*)
tel: +351 291 221 095
fax: +351 291 221 103

Internet
e-mail: info@eurofinesco.com
www.eurofinesco.com
Portugal
mobile: +351 96 910 2813



"Permutas"
Property Swaps

In Portuguese, this barter exchange is called a "*permuta*". Rather than purchasing a property for money, two owners swap their respective homes, normally making up any difference in value with cash. Just like a normal sale, a "*permuta*" is accomplished via public deed with equal recognition under the law to other forms of conveyance. Once a swap is defined, the only differential to be made up is between the net values of the properties. The issue is no longer **"A + B"**, but rather **"A - B"**, turning a large tax problem into a considerably smaller one.
Direct property exchange offers a way around institutional mortgages. If no banks or middlemen need be involved, the transaction can be simpler, cheaper and potentially more beneficial to both parties.
Exchange does not have to stop with bricks and mortar. Furnishing and fittings may also be appropriate for swapping, depending on requirements. The important thing is that it is now a matter between consenting individuals without third party interference.

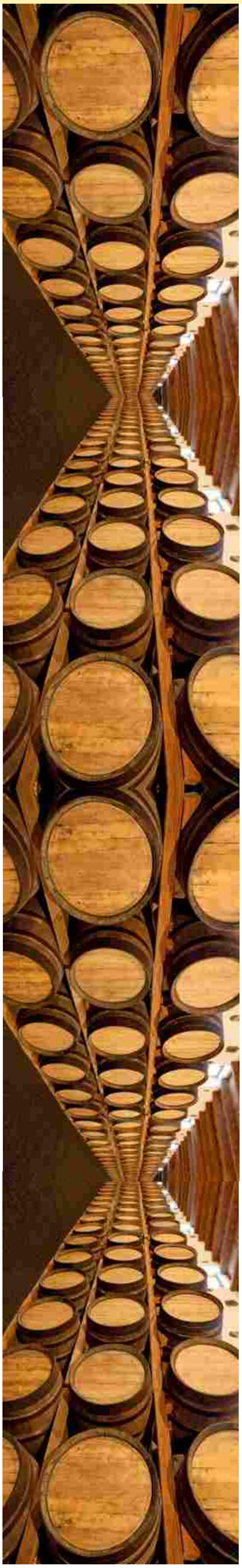
Advantages of a "*Permuta*"
In Portugal, barter exchange for property can present attractive advantages as well as offer favourable tax implications. In addition, a direct deal can meet particular needs of both buyers and sellers not necessarily available in a conventional sale.

1) No Waiting
Many property sales are delayed or fall though altogether waiting for a house to sell. With an exchange, the deal proceeds simultaneously. While there are still bureaucratic formalities to sort, they are little different from a conventional sale. However, it is important that correct procedures be followed. It is always vital to do a proper *title search* to be sure that you get getting what you expect, without any "skeletons in the closets". Consult *our* Short S30: *"Elements of a Title Search"*

2) Avoiding the Banks
By using the equity built up in your home, you can be free to make your own decisions and choose what is best for you. By exchanging what you own outright, you sidestep the need for a mortgage where a bank will dictate conditions. The final price, once above the legal minimum, is determined solely by the those making the exchange. It is for them to determine priorities to arrive at a conclusion that best meets mutual interests.

3) Let the Internet work for you
In the not so distant past, trades and bartering used to require long voyages from place to place. Now, through globalisation and the internet, you can effectively advertise and communicate with potential barterers instantly anywhere in the world. These means of communication provide the opportunity for you to make transactions regardless of location. By using existing *Internet Portals*, the new *Social Networks* and high volume *Property Websites*, cutting-edge technology is working to find a match to meet mutual interests.

4) Ample Supply and Demand
In a stagnant property market, renovating long-standing concepts like *barter* into innovative solutions is only common sense. There are plenty of potential owners anxious to find the home of their dreams in Portugal. Some will be apartment dwellers looking to upgrade to a villa, others want to downsize into a more manageable property. It is a market where neither supply nor demand are lacking. It is the conventional mortgage method that has collapsed, not people's ambition for change. A swap can prove to be the perfect solution to break through the stagnation logjam.



TAX IMPLICATIONS - *Lower or No Assessment*

a) Determining Values

As with any property transaction in Portugal, the legal minimum transaction price is the rateable value ("*VPT*"). This is the basis for annual "*IMI*" Property Rates . If one of the properties is pre-2004, there may still be a lower evaluation from the former system. Your "*permuta*" will trigger a re-appraisal 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 negociate the final value of the exchange.

b) Low or no *"IMT"*

As already stated, the final transaction value is based on "**A - B**", not "**A + B**" so "*IMT*" (Property Transfer Tax) will only be on the *difference*.

Example:

Let's swap two homes: one worth € 225,000, the other €275,000.

Rather than being taxed on the sum (€225,000 + €275,000 = **€500,000**), the assessment is on the difference - ***only €50,000.***

Since Property Transfer Tax ("IMT") is progressive and not linear, the tax savings will be even greater. If "**A = B**", there is no "*IMT*".

c) Low or no Stamp Duty

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

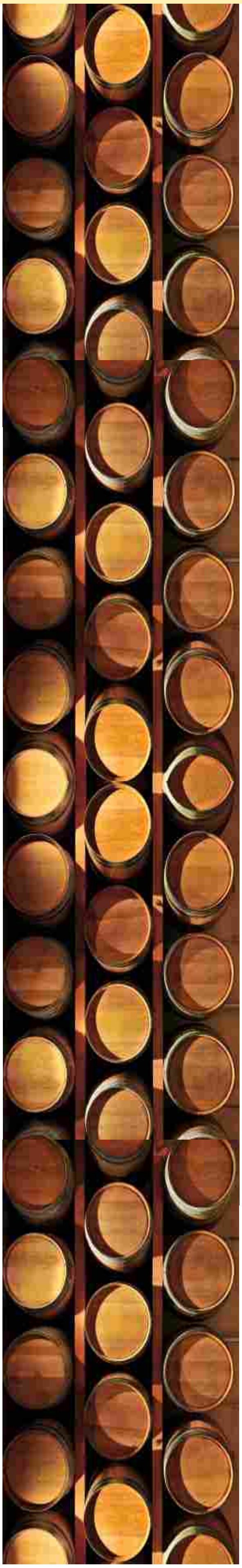
d) Partial or full CGT Exemption

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 and capital improvements within the previous 5 years. Rollover Relief is achieved when there is a full re-investment of the proceeds of the sale of the *principal residence* (as registered with *Finanças*). 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 of the former *principal residence* and the purchase of the new one. In other words, since both are of equal value ("**A = B**"), there is a full re-investment of the proceeds and therefore full exemption from Capital Gains Tax is achieved by 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.

If a loan is needed to finance the deal or there is a mortgage to repay, the amount outstanding or borrowed will not count towards the reinvestment, unbalancing the equation and creating a capital gains tax liability. Conversely, any loan repaid upon the sale will reduce the amount actually received for the property. Needless to say, with many potential variables in play, careful consideration must be applied to any eventual Capital Gains Tax liabilities to avoid nasty surprises. As always in such matters, prior professional advice is strongly advised.



Swapping Property Company Shares

Property Companies - both onshore and offshore - have been popular for years as a means to hold real property. In a nutshell, a property company turns immoveable property into moveable property, substantially altering how transactions are assessed. Because the shares change hands and not the underlying properties owned by the respective company, there should be no "*IMT*" (Property Transfer Tax) except under special circumstances. There is also no 0.8% Stamp Duty charged on the deed since no property changes hands, just shares. Finally, there should be a substantial reduction in Capital Gains Tax. With a Company Swap, CGT is calculated in the same way as direct property exchanges - only on the net difference between the respective values of the two sets of shares (**"A - B"**) - as long as there are no latent capital gains liabilities to sort as detailed in the IRS Tax Code. The gain is then taxed at a flat 10%. This is an autonomous assessment and avoids the top-slicing effect common with many forms of supplementary income.

Needless to say, if the share values are identical, there will be no gain and no CGT. For Portuguese Nominee Companies, this is an excellent solution and offers a similar array of benefits as we have seen for individuals.

Offshore Companies

Unfortunately, this procedure can pose a serious problem for many Offshore Companies. Historically, upon formation, it was common practice to set share capital of most Offshore Companies at nominal values to keep local jurisdiction Stamp Duty to a minimum. Had the asset worth been reflected at the time in the share value, thousands of Euros more tax would have been added to the cost of the transaction, turning the solution expensive and commercially unattractive.

Years later, if an Offshore Company were to exchange shares under Portuguese law, they would be caught up in the conditions limiting capital gains exemptions. If they exchange shares outside of Portugal, they will be operating under another set of rules and loose the Portuguese tax breaks that we are presenting.

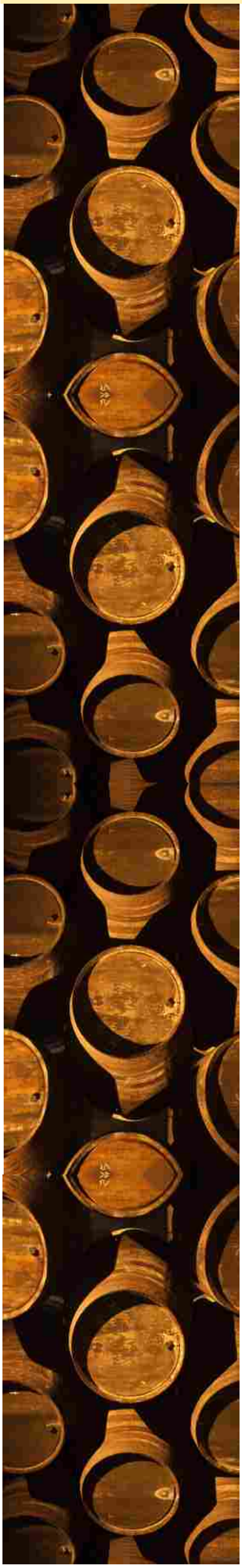
Redomiciliation

One solution is first to move your Offshore Company to Portugal prior to the exchange. This is called *Redomiciliation*. When an Offshore (non-resident) company moves to Portugal, there is no taxation on the transfer. This is because it is the Company Headquarters that is transferred, not the property, thereby avoiding any direct conveyance of the Company's assets.

As part of Company registration in Portugal, share capital needs to be recorded and should now show the *current* rather than the *historical* value of the Company. The Company's share capital should reflect the market value of the underlying property. This means that there is usually a significant uplift in the basis for eventual Capital Gains Tax assessment and many historical CGT problems can be neutralised.

Besides making an exchange viable, *Redomiciliatio*n can resolve many other problems intrinsic to Offshore Companies ownership. As many have come to realise, most of these Offshore structures have outlived their usefulness. Company owners should look to embrace fully compliant solutions in their legitimate quest to mitigate tax liabilities.

*euro*FINESCO *newsletter* n° 14e - Summer 2012



A Short-Term Swap

Even if your interest in an exchange may not be permanent, you may find the rewards to be interesting on a temporary basis to resolve certain underlying problems that you may face with your property.

Let's look at the following example of a *short-term swap*:

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 receipts, they had their dream home. Twenty years later, their modest investment was worth almost a million euros, most of which was capital gain. As they were getting on in years, they wanted to begin planning for a "*downsize*" to a simple bungalow with a small garden. But the prospect of paying almost €200,000 in CGT left them with sleepless nights.

Then came the idea of a Short-Term Swap:

1) First, they make an agreement to swap properties that are of similar value;
2) Next, near the end of the fiscal year, they swap homes - on paper only - at the identical value of €1,000,000. Because the swap involves properties of equal worth, there is no "*IMT*" and no Stamp Duty - only due on any difference in values. Because both are trading their primary residence, they are still eligible for *Rollover Relief* on Capital Gains. The "*permuta*" means that they both achieve an immediate reinvestment of the proceeds, so the transaction is exempt from Capital Gains Tax. Because both own their homes outright with no outstanding debt, the transaction is clean and simple, with no adjustments nor institutional interference.
3) Finally, early in the following year, they swap back, also for equal values of €1,000,000. Once again, no IMT, no Stamp Duty, no Capital Gains Tax.

Now both owners have as the base of acquisition of their respective properties the new €1,000,00 value rather than their respective historical purchase prices.

Total costs of the double transaction:

Disbursements for registrations, notary charges and legal fees:

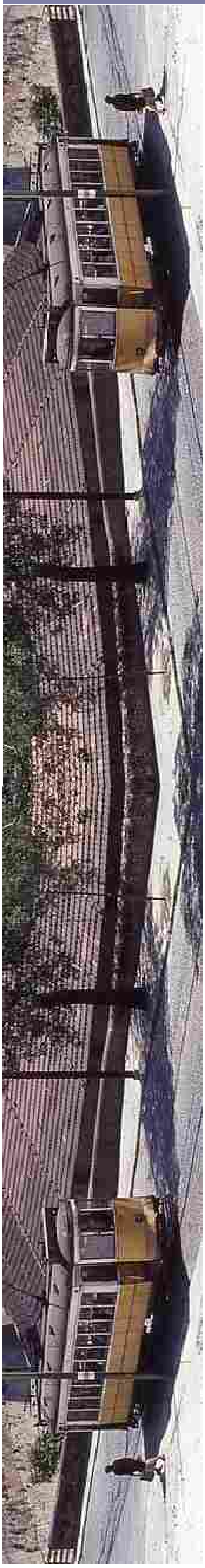
± €1,500 X 2 per property plus an *ad valorum* success fee.

With no outstanding capital gain tax liability on the property, they can now sell for €1,000,000, buy their little bungalow and invest the balance to supplement their retirement income. *A happy ending!*

Conclusion

Few doubt that we live in a globalised world. The "good old" days of *self-sufficiency* - and all of its limitations - are long gone and, despite whatever nostalgia we may occasionally feel, there is no turning back. However, interdependence does not necessarily imply loss of *self-reliance*. Counting on ourselves and doing what is appropriate for ourselves will always be a constant to achieve success, no matter what the endeavour. If easy money from institutions no longer works, relying on our own initiative to achieve goals will likely prove to be the most effective answer.

We suggest a fresh look at the ancient practice of *barter* - in this case, **property exchanges** - as an alternative to conventional buying and selling of villas or apartments as a means of sidestepping current austerity difficulties. Interestingly, these swaps have surprisingly pleasing tax implications under Portuguese legislation that can make it appealing to turn theory into reality.



Closing Notes

Increase in Higher Rate Taxpayers in UK
Recent statistics published by HM Revenue & Customs have revealed that the number of taxpayers paying tax at higher rates (40% and above) has risen from 3.8m to 4.1m, an increase of almost 8%.

Subsidy cuts declared unconstitutional
The Portuguese Constitutional Court declared unconstitutional the suspension of payment of holiday pay and Christmas bonus to civil servants and pensioners for violation of the principle of equality. The effects of the declaration of unconstitutionality are not applicable in 2012, but only in the future.

Living Will approval in Portugal
Living Wills - written instructions by individuals when they are no longer legally competent addressed to medical professionals - are expected to receive final Parliamentary approval.

UK Statutory Residence Test - *the next stage*
HM Treasury have released their response to the consultation into implementing a Statutory Residence Test as of April 2013. It is a three-tier test, broken down into: 1) those who are found to be conclusively non-resident; 2) those determinately resident; or 3) connections an individual has with the UK and the number of days spend in the UK. The response also contains draft legislation comprising of a surprising 62 pages.

Court Rules IMI notices are illegal
An Administrative Court of Porto judge (TAF) has ruled that the "*IMI*" (Municipal Property Tax) demands received by owners every year to claim payment of Municipal Property Tax are illegal due to lack of appropriate substantiation.

Reintroduction of internal border controls within the EU
Ministers of Home Affairs of the EU approved the reintroduction of border controls in case of illegal migratory pressure. To reach final approval, this agreement will now be discussed by the European Parliament.

New Rules on Cross-Border Succession
Under up-coming EU regulations, the place of habitual residence of the deceased takes effect as the sole criterion for determining jurisdiction and the law applicable to cross-border succession, even when that State is not an EU member. Citizens living abroad may, however, choose to submit succession to the law of the State of which they are nationals.

EU eases Cross-Border Succession
The EU Council of Ministers has created a European Certificate of Succession and approved the Commission's proposal aims to facilitate cross-border succession by reducing the legal formalities on the death of a person who has property in another Member State. Member States have 3 years to harmonize their national legislation to apply these new EU rules.