TPA ADVOGADOS

TAXATION OF REAL ESTATE CAPITAL GAINS RESIDENTS / NON-RESIDENTS

As per the Portuguese legal system, income generated in national territory is subject to taxation. The present analysis and commentary will focus on a specific type of income – real estate capital gains.

In broad terms, real estate capital gains correspond to the difference between the value for which a property was purchased and the value for which said property was sold.

Taxation is not calculated based on the gross amount calculated as described above. The following deductions apply:

- Costs incurred over the 12 years prior to the sale, to increase the valuation of the property (for example structural improvement works);
- Expenses incurred with the property purchase and sale (e. g. notary and registration fees; the commission paid to the real estate agency; etc.)

In light of the current Code for Income Tax for Singular Persons (hereinafter CITS), tax payers are treated differently in what pertains to calculation of capital gains tax. In fact, different rules are set forth according to whether tax payers are:

- Resident in national territory for tax purposes;
- Resident (for tax purposes) at another Member-State of the European Union (EU) and/or of the European Economic Space (EES), as long as those countries have mechanisms in place for exchange of fiscal information with Portugal;
- Resident in a country outside of the EU or the EES.

For residents in national territory, capital gains are considered in 50% of their value, to determine the amount of tax owed. This means that only half of the income obtain is subject to assessment.

The taxable income is, after that, taxed at the rate applicable to the whole income generated in Portugal (for example salaries or pensions), according to the progressive rates applicable each year (currently set between 14,5% and 48%).

Until 2008, non-resident taxpayers (regardless the residence country) were taxed at a fixed rate of 28%, calculated on 100% of the real estate gain obtained.

This discriminatory treatment between residents and non-residents on national territory originated numerous litigation with Tax Authority and the matter eventually reached the Court of Justice of the European Union (CJEU). The CJEU considered the existence of discriminatory treatment for the residents in EU member states to be a clear violation of the principle of free movement of capital between Member States and between Member States and third countries as set forth on articles 63 and 65 of The Treaty on the Functioning of the European Union (TFEU).

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As a result, Portugal enacted **Law nr. 67-A/2007, of 31st December**, which introduced an amendment on article 72 of the CITS establishing that **residents in a EU or EES Member State** (as long as those countries have mechanisms in place for exchange of fiscal information with Portugal) can now choose to subject their income to the progressive rates (instead of the fixed rate of 28%).

However, this choice entails that these taxpayers declare their worldwide income in Portugal, which is an important deterrent.

Consequently, two discrimination factors continue to occur, namely:

- For all taxpayers non-resident in Portugal (inside or outside the EU), real state capital gains are considered in 100% of their value, contrasting with the 50% considered for residents in Portugal;

- For taxpayers resident outside the EU/EES, not only is capital gains tax calculated considering 100% of the gain, but they are also subject to the fixed rate of 28%, with no other option.

In light to the above, it is our understanding that an effective discrimination continues to occur, between how resident and non-resident taxpayers are fiscally treated, as indeed has been the understanding of the Court of Justice of the European Union (CJUE), the Portuguese Supreme Administrative Court (SAC) and the Administrative Arbitration Center (AAC), all of which have issued decisions stating that only **50% of the real state gains should be considered for taxation.**

In conclusion, the 2008 amendment was insufficient to balance taxation of real estate gains between taxpayers, regardless of their place of residence. Therefore, it is necessary to enact legislation that establishes the consideration of only 50% of the real estate gains for all non-residents (regardless the country) and subjecting them to either the application of the progressive rates applicable to Portuguese residents, or to the application of a fixed rate if they do not intend to declared their worldwide income in Portugal.

The basic principle of equality must be based on the assumption that the income subject to taxation is equal, as has been defended in almost all national and European court decisions.

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