

EXEMPTION FROM CAPITAL GAINS: WHAT IF ONLY ONE ROOM IS USED FOR LOCAL LODGING (AL)?

ALL FINANCE MATTERS

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A property owner seeks to obtain IRS exemption on the capital gains resulting from the sale of their permanent home. However, complications can arise if part of the property, such as the ground floor, is designated for Alojamento Local (AL) — even if it's just one room.

Monetizing a Portion of the Property:

The surge in tourism and the need for additional income have prompted many homeowners to rent out parts of their permanent residences through local accommodation. But could this create complications?

1. **Ground Floor concerns:** A taxpayer expressed uncertainty about the implications of selling their permanent home, particularly regarding the reinvestment of profits into another property. With the ground floor utilized for AL, they wondered if they would have to pay capital gains tax. Therefore, they requested a Binding Information from the Tax Authorities
2. **Single Room for Rent:** Another taxpayer faced a similar dilemma, but in this instance, only one room was used for AL activities, accounting for less than 10% of the property's total gross area. This taxpayer also requested Binding Information.

Capital Gains Tax Exemption Conditions:

In their responses to the Binding Information requests, the Tax Authority (AT) reminded that the exemption from capital gains applies to the onerous transfer of properties that serve as the taxpayer's or their family's permanent residence, provided that the following conditions are cumulatively met:

- The selling price, minus any loan repayment for acquiring the property, must be reinvested in the purchase of another property, in land for construction, or in the expansion or improvement of another property with the same purpose.
- The reinvestment must occur within 24 months before and 36 months after the date of sale.
- The taxpayer must express the intention to reinvest, even partially, specifying the amount in the income declaration for the year of sale.
- The property sold must have been used as the taxpayer's or their family's permanent residence, proven by the respective tax domicile in the 24 months prior to the sale (this period will soon change to 12 months).
- Taxpayers cannot have benefited from this exclusion regime in the year they realized the gains and in the three previous years, except in exceptional circumstances.

Important Note: This exemption does not apply if the reinvestment in another property is not intended for the taxpayer's or their family's permanent residence within 12 months from the date of reinvestment.

Understanding Permanent Residence:

Permanent residence is defined as the location where the taxpayer organizes their domestic life in a stable and lasting manner, including where they sleep, eat, and receive family and friends. Key characteristics of permanent residence include habituality, stability, and the establishment of the center of domestic life organization. However, challenges arise when this situation intersects with economic activity.

1. Local Accommodation on the Ground Floor: The AT determined that the fact that part of the property is used for AL indicates that it is not exclusively intended for the taxpayer's permanent residence (even partially, there is an allocation to the AL activity).

2. Local Accommodation in the Room: Similarly, the AT considers that if the property is used for AL in the form of "Rooms," it will also not be exclusively allocated to the taxpayer's permanent residence since there is a partial allocation.

Responses from the AT:

In both scenarios, the AT determined that the conditions for exemption were not met, resulting in the taxpayer's ineligibility for capital gains tax exemption.

Important: In practice, this means that the taxpayer loses the right to the exemption provided by law, and the profit from the sale of the property will be subject to the general rules of taxation under the IRS.

Conclusion:

Even allocating just a portion of a house, or a single room, to Alojamento Local can disqualify the property from IRS exemption, regardless of its status as a permanent residence.

Legal Basis: Binding Information nos. 25217 and 26330.

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