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HOW TO PREVENT A TAX HIT WHEN SELLING A RENTAL PROPERTY IN PORTUGAL

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Investing in rental properties in Portugal has become very attractive over the last few years. The country's popularity as a tourist destination has soared, leading to significant economic benefits. In 2024, Portugal welcomed over 30 million foreign tourists, generating revenues exceeding 27 billion euros. This impressive milestone placed Portugal 5th in Europe in terms of bookings through internet platforms.

However, while the AL (Local Lodging) sector has seen a boom over the past decade, the government has changed some of the tax rules over the years. This means that when such rental properties are ultimately sold, they can trigger significant capital gains tax liabilities.

Capital gains tax (CGT) is an important consideration for property investors in Portugal. Currently, the CGT is levied on 50% of the gain for properties that were never in the rental business or that have at least stopped the activity for more than 36 months prior to the sale. But when the property is still on the local lodging (AL) or was within the last 36 months prior to the sale, the capital gains can be levied on 95% of the gain. This means that careful planning is essential to minimize tax exposure and maximize profits.

Below you can find some effective methods to help you reduce your capital gains tax burden.

Study the rules that applied to your CGT calculations in 2020

The new rules for calculating capital gains tax for rental properties came into force in 2021. One option is to analyze the previous tax returns, in case the AL started before 2021, and see with an accountant if the option was to choose the old taxation regime. In this case, providing all the values are correct, the sale can be made in a shorter period and the capital gains will be levied on 50% of the gain as per the standard rules.

However, although this strategy may allow you to sell the asset in a shorter period, it also requires an exhaustive tax study, as, depending on the circumstances, it can be challenged by the tax authorities.

Use a rental agent or a third party to hold the AL license

This can be a tax planning strategy if an investor is planning to sell the property. The main options are normally to transfer the license to the rental agent and rent the property long-term to the agent. This way, the investor receives a rental income, instead of a business income, while minimizing the capital gains tax exposure on the sale of the property.

Alternatively, if the client does want to rent through a rental agency, the contract can be made with a spouse or descendant if this person doesn't own this property.

It's important to verify whether this rental or ceding contract has VAT implications, as it may not be a solution for all clients.

Use a Real Estate company to mitigate the CGT

This strategy can be useful for investors who are in the process of selling their property but face a potentially large tax liability.

In Portugal, it is possible to create a real estate company under the simplified regime, provided the yearly turnover is lower than 200 thousand euros. This means that one of the household members (the one holding the AL license) can sell his share of the property to this new real estate company he creates. The sale price would be lower to ensure that it does not generate a capital gain for the owner.

This immediately mitigates the capital gains in his personal sphere and transfers the capital gains exposure to the company.

The advantage is that this company will be in the simplified regime, and therefore, it will be taxed on turnover and not on profit. The coefficient in this case is 4% of the sale value, with a reduction of 50% in the first year of trading. This means that if this property is sold for 150.000€ in the first year of trading, the taxable gain would be 2% of 150k, which is 3.000€. This will lead to an effective tax rate lower than 1%.

Please note that there are several limits to using this strategy. The main one is that the company's assets cannot exceed 500.000€ and its yearly turnover cannot exceed 200.000€. This is particularly relevant under the Portuguese tax regime, as otherwise, the normal rules would apply, and the tax is applicable on the profit (capital gains made) instead of the sale value.

Avoid making mistakes that can cost you money.

Always study the tax implications of the sale before placing the property on the market, especially if it was in the AL activity within the last 36 months prior to the sale.

Portuguese tax laws provide some deductions and allowances that can help reduce the taxable gains from the sale of a property. These include deductions for property improvements, maintenance, and other qualifying expenses incurred during the ownership period. However, these are not allowed if the property was in the AL business within the last 36 months prior to the sale. By thoroughly understanding these rules, investors can adapt their strategy to minimize the capital gains tax exposure.

In conclusion, while capital gains tax on rental property sales in Portugal can be significant, there are strategic methods to manage and reduce this tax burden.

For any inquiries or support, our team can guide you through the whole moving process. Feel free to reach out to us at **info@afm.tax** or visit **www.afm.tax**.

"YOU MUST PAY TAXES, BUT THERE'S NO LAW THAT SAYS YOU NEED TO LEAVE A TIP."