Transfer of the place of residence

If a person transfers a dwelling, which he or she **used until the transfer as his or her place of residence**, the gains derived from the transfer are exempt from tax and income tax is not charged.

The Income Tax Act does not specify how many days a year a dwelling must be used in order to be called a place of residence. A person may have two or more places of residence at the same time. According to the guidelines of the Supreme Court, the actual place of residence of a person is the determining factor in the application of the tax exemption. The determination of the actual place of residence is therefore a matter of proving a fact in each case of tax exemption.

The tax exemption can only be applied to one sales transaction within two years. The two years between transactions are counted from the day following the date of entry of the sales transaction in the land register.

EXAMPLE 1

In January 2022, a person sold her apartment, which she had been using as her place of residence. The notarial purchase and sale contract was signed on 23 January 2022 and the entry in the land register was made on 26 January 2022.

The person sold her new place of residence in January 2024. The notarial purchase and sale contract was signed on 15 January 2024 and the entry in the land register was made on 18 January 2024.

The period between the sale of the first and second place of residence is shorter than two years, so the sale of the second residence must be declared in the income tax return of 2024. In this example, the two-year period starts on 27 January 2022.

If a loss arises from the sale of the second place of residence, such a transaction is not taken into account at taxation and does not have to be declared, but the documents of the transaction (concerning costs of acquisition and sale) must be kept for at least five years.

Since the transfer of residence is exempt from income tax, it does not matter how the dwelling was acquired - whether inherited, gifted, purchased, returned or privatised with the right of pre-emption.

EXAMPLE 2

A private person has two houses that he uses as places of residence.

He sells his house in Pärnu, where he lives mostly in summer and occasionally at other times. He inherited the house and is the sole owner of it. His second house is in Tallinn, where his registered place of residence is. The house in Tallinn is used as a place of residence primarily in winter.

Can the person apply tax exemption to the transfer of his Pärnu house?

The person can have two places of residence and he can choose on the sale of which he applies the tax exemption. **NB!** The tax exemption can be applied on the sale of one place of residence within two years.

The use of a dwelling as a place of residence can be proved in various ways, e.g. explanations from the taxpayer, testimony of witnesses, including neighbours, bills of paid utilities, contracts for communications services, etc.

The fact that the person has a registered place of residence in Tallinn is not decisive in this case.

In order to apply the tax exemption, it is important that the Pärnu house is used as his place of residence before it is sold and that the house is not partly used as an office (e.g. there are no rooms rented to a company) or rented out to somebody else. Using the house as a home office does not affect or annul the tax exemption of the sale of a place of residence.

The sale of the Pärnu house is exempt from tax and does not have to be declared in the income tax return.

EXAMPLE 3

A private individual uses one room in their home as a home office. The company compensates for the costs associated with the office.

If a private individual decides to sell their place of residence, what does this mean for them in terms of taxation?

If an employer has reimbursed an employee for electricity or internet expenses in connection with a home office (pursuant to **subsection 3 of § 12 of the Income Tax Act**), this does not affect the tax exemption on the sale of the residence.

However, if the immovable property, building, or apartment was used for other purposes (e.g. business, separate massage room, etc.) at the same time as it was used as a place of residence, the tax exemption is applied proportionally to the ratio of the area used as a residence to the area used for other purposes.

EXAMPLE 4

A married couple is getting divorced. They own a home together. After the divorce, the woman will continue to live in the couple's shared apartment, while the man will move into an apartment he purchased before the marriage, which had been rented out in the meantime. After some time, the man sells his new residence, which belongs solely to him, and uses the tax exemption for the sale of a place of residence pursuant to **clause 1 of subsection 5 of § 15 of the Income Tax Act**. The man then buys a new apartment.

If the man and woman wish to sell their jointly owned apartment at a later date, can they claim the income tax exemption applicable to their place of residence, or does the man have to pay income tax on his share of the proceeds from the sale?

According to **clause 1 of subsection 5** and **subsection 6 of § 15 of the Income Tax Act**, it is possible to

apply for income tax exemption once every two years when selling your place of residence. This applies if the taxpayer uses the apartment as their place of residence until the sale. Therefore, when selling their shared apartment, the woman can apply the income tax exemption to her share, but the man must pay income tax on his share of the gains. The reason for this is that the man no longer uses the apartment as his place of residence and is selling his second home within two years.

EXAMPLE 5

Until transfer, a sole proprietor used 70% of her apartment with the total surface area of 100 m^2 as a residence and 30% for entrepreneurship. Acquisition and improvement costs of the apartment have not been deducted from business income.

The sales price of the apartment is 100,000 euros. 30%, i.e. 30,000 euros, of it is the taxable part.

The acquisition cost is 70,000 euros, 30% of it, i.e. 21,000 euros, is taken into account.

The expenses related to the transfer make up 10,000 euros, 30% of this amount, 3,000 euros, is taken into account.

Gain is declared as follows: 30,000 – 21,000 – 3,000 = 6,000 euros.

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