Tax & Business Lawyers

NEWSLETTER

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URBAN REGENERATION IN PORTUGAL: THE SCOPE AND LIMITS OF AN AUTHENTIC INTERPRETATION OF VAT PROVISION 2.23

The application of the reduced VAT rate (6 %) to works in Urban Regeneration Areas (ARUs) has returned to the centre of the debate following the parliamentary approval of an interpretative law.

Is this law already too late? It is time for businesses, the tax authorities and the Government itself to prepare for its entry into force by analysing and mapping out the situations that may fall within its scope, in order to safeguard the practical effect of an interpretation now reaffirmed by the legislature.

Advisory Team

THE BACKGROUND

The application of the reduced VAT rate (6%) to construction works in Urban Regeneration Areas (ARUs) has once again become the focus of debate.

For years, the tax authorities have maintained a restrictive interpretation of clause 2.23 of List I annexed to the VAT Code, requiring, in addition to the demarcation of the ARU, the approval of an Urban Regeneration Operation (ORU). This interpretation has led to additional VAT assessments at the standard rate on proceedings already carried out, increasing costs and uncertainty in the sector.

As we have previously noted in articles dedicated to this topic (namely NL37_26_UrbanRehabilitation_NewDraftLaw), it has always seemed to us that this interpretation lacked clear support in the legislator's intention when introducing Item 2.23.

However, case law was inconsistent in its rulings, and the Supreme Administrative Court (STA), in a Judgment on the Standardization of Case Law dated 26 March 2025 (Case No. 12/24.9BALSB, published as Judgment No. 3/2026), established its view that only urban regeneration works carried out in an ARU for which an ORU has been previously approved are eligible for the reduced rate of 6 per cent, thereby validating the position taken by the tax authorities.

Far from bringing the matter to a close, this standardization ultimately refocused the debate and highlighted the practical impact of an interpretation heavily dependent on an administrative assumption which, in many cases, is beyond the taxpayer's control.

RESTORING WHAT IS DUE

Meanwhile, the legislator reacted, seeking to return to what had always been its view regarding the rationale behind this provision. This led to the introduction of Bill No. 642/XVII/1st, the aim of which was to provide an authentic interpretation of provision 2.23, to the effect that the location of the property within a legally defined ARU would be deemed sufficient, irrespective of the approval of an ORU.

This Bill was passed very quickly, having gone through the parliamentary process which culminated, on 17 July 2026, in its unanimous approval in a final plenary vote. On the same date, the corresponding Decree of the Assembly of the Republic was published, entitled 'Providing an authoritative interpretation of item 2.23 of List I annexed to the Value Added Tax Code, as amended by Law No. 64-A/2008 of 31 December'.

It should be noted, however, that the entry into force and full effect of the legislation depends on its promulgation and publication, which are still pending.

The significance of this legislative development does not, however, lie solely in the substantive content of the approved solution. The truly decisive point is that the legislature has introduced a law characterized as interpretative, contrary to the understanding previously established by the STA, as well as the *timing* of this legislative action.

More than a mere clarification, this is a legislative intervention that seeks to resolve the debate over past situations and pending disputes.

REHABILITATING THE PAST?

The central issue is thus no longer merely a question of determining the best interpretation of item 2.23 of List I annexed to the VAT Code, but rather of understanding the practical effects of this interpretation, now referred to as the authentic one.

It should be recalled that the interpretative law forms part of the law it interprets, but excludes the effects already produced by a final and binding judgement, a settlement or acts of a similar nature. This exception is significant: amongst past situations, it is important to distinguish between cases that have already been definitively decided — which, in principle, cannot be reopened on the basis of the new interpretation — and those that have not yet become final, or which have not even been contested, in which the scope for invoking this interpretation is substantially greater — and the matter may be among the options to be considered in the context of litigation, with a view to reaching a final resolution of the dispute more swiftly.

In practical terms, by stipulating that the law takes effect from the entry into force of Law No. 64-A/2008 of 31 December, the legislature intends for this interpretation to apply to the entire period during which the wording of item 2.23 of List I annexed to the VAT Code — now the subject of an authentic interpretation — was in force — specifically, the wording in force between 1 January 2009 and the amendment introduced by Law No. 56/2023 of 6 October (Mais Habitação) — meaning that subsequent transactions remain subject to the regime established at that time, subject to the application of transitional provisions.

In other words, the specific way this interpretation is applied depends on the facts and context of each transaction. Parliamentary approval of this interpretative provision should not, therefore, be regarded as an automatic solution for all cases.

This issue was also addressed in the Opinion of the Order of Certified Accountants, issued during the public consultation phase of the legislative procedure leading to the approval of the Draft Law. In its Opinion, the Order draws attention to the practical difficulties associated with the entry into force of the proposed legislation, including the deadlines for tax regularization, the handling of pending cases, and the limitations that may arise in relation to cases that have already been definitively settled or are subject to statutory limitation periods.

And rightly so. Indeed, whilst this legislative development is to be welcomed as being in line with what we have been advocating — and which, unfortunately, was not adopted by the Supreme Court (STA) in its efforts to standardize case —, it may be too little, too late in many situations where the legal position is already well-established, as the time that has elapsed is, in itself, a problem.

We also note that an opportunity may have been missed for the legislator to establish, from the outset, an incentive, in the form of procedural costs, to bring about the swift conclusion of court proceedings or tax arbitration cases in which this issue is being debated.

The Government should, however, seek to issue guidance as a matter of urgency setting out the course of action to be followed by the tax authorities, and the timing thereof, with regard to ongoing audit and administrative appeal procedures — and it seems to us that there is nothing to prevent the tax authorities from also correcting *ex officio* assessments that are the subject of legal proceedings, with the corrective measures being added to the case file as a supervening act leading to the conclusion of the case.

In short, the Government, the tax authorities and businesses must all prepare themselves and act with a view to safeguarding, as far as possible, the practical effect of the interpretation intended by the legislator.

FINAL REMARKS

In this context, the enactment of the new law represents a significant development in the tax framework governing urban regeneration projects in urban regeneration areas (ARU). By establishing an authentic interpretation of item 2.23 of List I annexed to the VAT Code, contrary to the understanding previously standardized by the Supreme Administrative Court, the legislator materially alters the legal framework applicable to this matter.

It is precisely this type of issue that needs to be monitored closely and in advance. The legislative development is, in general terms, positive, but it does not eliminate — rather, it makes all the more urgent — the need for the entities concerned to prepare themselves.

Therefore, rather than waiting for the legislation to be published, entities potentially affected should, as of now, review their procedures and reorganize their respective files: identifying the transactions and periods covered by the previous wording of paragraph 2.23, including transitional provisions, and mapping out the status of each situation, as well as the deadlines and any applicable procedures.

It is this preparatory work that will enable them to respond effectively and in a timely manner as soon as the law comes into force.

On the part of the Government and the tax authorities, there will also be a considerable amount of work to be done in mapping out the audit proceedings and tax assessments already under challenge, which will need to be reversed as soon as the law providing the authentic interpretation comes into force, with a view to strict compliance with the principle of legality and safeguarding the practical effects of this interpretation.

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