

Supreme Court answers questions about concept of ‘essentially a new building’ for VAT purposes

On November 4, 2022 the Supreme Court issued a preliminary ruling in reply to questions referred to it by the District Court of Zeeland West-Brabant about the concept of ‘essentially a new building’ for VAT purposes. The case before the Supreme Court involved a dispute as to whether the acquisition of an office building that had been converted into a hotel should be exempt from real estate transfer tax for reasons of VAT concurrence. To be exempt from real estate transfer tax, the transfer of the hotel building to the taxpayer must be subject to VAT by virtue of law. To achieve this, the refurbishment is to have resulted in ‘essentially a new building’. The District Court asked the Supreme Court for its opinion on the circumstances under which a property qualifies as ‘essentially a new building’. The Supreme Court answered these questions in line with earlier judgments, indicating that the refurbishment must have resulted in a new and hence previously non-existent property and that this is mainly achieved by an extensive alteration in the building’s structural construction. Other factors can also play a role, but they are not decisive.

The case

The taxpayer bought a hotel in 2018 for a purchase price of EUR 15.8 million. The seller purchased the building in 2015 for EUR 4.8 million and converted it from an office building into a hotel in 2017/2018. The refurbishing costs were about EUR 7 million. The works involved stripping the interior, altering the sanitary facilities, installing a new sprinkler system and outfitting the building with a new heating system. Little to no changes were made to the building’s existing structure. The roof, floors, staircases, ceilings and elevators were not removed, nor were they replaced. The building was modified to bring it up to date with today’s building requirements and to meet the taxpayer’s wishes. The refurbishment did not result in an increase in existing surface areas. The appearance of the building was not altered either.

The taxpayer believes that the refurbishment resulted in ‘essentially a new building’, which the Tax and Customs Administration refutes. For this reason, the taxpayer referred the matter to the District Court. The District Court referred to existing case law and concluded that there are no clear-cut guidelines for when ‘essentially a new building’ has been created. The District Court acknowledged the relevance of further interpretation of the concept of ‘essentially a new building’ for the practice and asked the Supreme Court on January 31, 2022 to issue a preliminary ruling.

Relevance of ‘essentially a new building’

If a property is designated as ‘essentially a new building’, it will qualify as new for VAT purposes. The transfer of a new property is subject to VAT. The acquiring party can in principle invoke the real estate transfer tax concurrence exemption in respect of the acquisition, as a result of which no real estate transfer tax will be due.

Questions referred for preliminary ruling

The Supreme Court has answered the questions referred to it by the District Court by stating that work on an existing building will only lead to the creation of a previously non-existent building if the work is so extensive that ‘essentially a new building’ has

been created. In other words, the end result of the refurbishment should be considered on a par with a new building.

The Supreme Court has ruled that the question of whether or not 'essentially a new building' has been created should be answered based on the structural construction works the building has undergone. According to the Supreme Court, the only alterations that would justify a refurbishment being so extensive that essentially a new building has been created are structural construction changes, such as replacements of all or some of the existing structural construction. In this context, the Supreme Court said that a refurbishment is not typically likely to be so extensive that 'essentially a new building' has been created. This should be reviewed on a case-by-case basis.

In addition to alterations to the existing structural construction, the Supreme Court has also named the following factors that may point to the creation of 'essentially a new building':

- Changes to the property's structural identity/outward appearance;
- Changes to the functionality of the property in terms of its uses;
- The amount of investments in the building; and
- The added value achieved by the refurbishment.

These as well as other factors may point to a refurbishment being so extensive from a constructional aspect that essentially a new building has been created. However, in the Supreme Court's opinion, these factors individually or jointly are not decisive or required.

Relevance for real estate practice

More clarity about the concept 'essentially a new building' has long been awaited. For this reason, the real estate tax practice was eager to learn about the details of the preliminary ruling. Despite the fact that the Supreme Court has now offered guidance for assessment, it remains unclear how to weigh the factors.

The preliminary ruling shows that, for 'essentially a new building' to have been created, there must have been alterations to the structural construction as a minimum. In addition, factors such as changes to a building's structural identity and/or uses, the amount of investments and the added value achieved can point to the creation of 'essentially a new building'. That said, we are still left guessing about how to weigh the factors for determining whether or not 'essentially a new building' has been created. Each case will have to be assessed individually to determine whether or not 'essentially a new building' has been created. As a result, we believe that, similar to the matter before the judgment, cases may still lead to discussion.

The advisors of KPMG Meijburg & Co's Real Estate Indirect Tax Group can help you assess whether or not 'essentially a new building' has been created. Please feel free to contact one of them or your regular advisor.

KPMG Meijburg & Co
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