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FROM THE EDITOR

Fighting the crisis

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With the first shocking waves of the credit crunch behind us and a grim outlook on the year 2009 ahead, real estate law has been moving into the centre of attention. Now, more than ever, firm and reliable legal advice is crucial for the success of real estate projects and transactions. This issue of the Real Estate Law newsletter encompasses 21 articles on 16 jurisdictions and demonstrates once again the immense know-how and experience of our committee. The newsletter would not have been possible without the continuing support of many members who have sent contributions to me and my colleague Klaus Pfeiffer in the last few weeks. We are pleased to see these contributions published in the current issue and would like to take this opportunity to thank all the authors for their contributions as well as for their cooperation.

Apart from the quantity and quality of the articles, we were also surprised by the eclectic mixture of topics dealt with by the single authors. George Georgiou (Cyprus), Miguel Jáuregui-Rojas and Stephan Tribukait-Vasconcelos (Mexico) as well as Gregor Kleinknecht and Naila Wazir (United Kingdom) focused on the current economic climate in their countries and demonstrate how the credit crunch has affected these economies. Despite its adverse effects, investment may still be very lucrative.

Laura Lavia Haidempergher (Argentina), Peter Kunz and Hermann Ortner (Austria), Jorge Wahl (Chile), Katarina Fulir (Croatia), Alexey Nikitin (Russia), Owen Foley (Turks and Caicos Islands), Arthur Nitsevych (Ukraine) and Nadia Dib (Uruguay) deal with investment and project development in their countries. It is very enlightening to see how legal

Continued overleaf

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rules are designed in various jurisdictions and which measures must be taken in order to render the investment a success or, more importantly, to even get it started.

More than half the authors have provided articles on such diverse topics that they can hardly be listed under one general heading so are worth mentioning separately. Julia Fernández and Marcelo den Toom (Argentina) report on time-sharing and gated communities in Buenos Aires while Martin Foerster (Austria) concentrates on the influence of environmental law on real estate transactions. The intellectual journey proceeds with real estate transactions by text message in Belgium (Michaël Bollen, Ghislaine Goes), the so-called *Werkstattverfahren* in Germany (Roland Bomhard, Thomas Wölfl), shopping centres in Italy (Antonella Terranova) and properties involved in criminal activities in Mexico

(Fernando Orrantia). Additional topics such as due diligence in Panama (Ricardo Cambra La Duke), expropriation and restitution in Romania (Cătălin Grigorescu, Nicolae Ursu) or the right of first refusal in the United Kingdom (Stephen Hubner, Kathleen Fitzgerald) render this newsletter an extremely valuable update on real estate law.

Last but not least, I would like to sincerely thank all authors for all the articles they have provided, even if some could not be published in this particular newsletter. I would also like to thank my colleague Klaus Pfeiffer from our firm's real estate practice group for his support in editing the articles. I look forward to meeting many of you at the forthcoming Global investments in real estate: trends, opportunities and new frontiers conference at Miami, 5–6 February 2009 and to interesting discussions on the issues raised in this newsletter.

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Views expressed are not necessarily those of the International Bar Association.

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ARGENTINA

Trusts as an alternative to channelling and financing real estate projects in Argentina

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Trusts were not subject to a specific regulation in Argentina until 1995, when law No 24,441 was passed. This law regulates not only trusts, but other issues with a general financial-oriented purpose.

Section 1 of Law No 24,441 establishes that:

‘a trust shall exist when a person (settler) transfers the fiduciary ownership of specific assets to another (trustee), who commits to hold said ownership for the benefit of the person appointed in the agreement (beneficiary), and to transfer the assets to the settler, beneficiary or any other third party appointed to such ends, once a specific term has elapsed or certain condition has occurred.’

Law No 24,441 regulates specifically the trust known as ‘ordinary’, and the ‘financial trust’ (which allows public companies to obtain cash by issuing bonds). Reference to a trust created by will is also made in the Law.

However, the lack of specific regulation was not an obstacle to applying trust structures to pursue different ends: guaranty, investment, administration, voting and investment or financing real estate projects, among others.

Legal regime and requirements

Real estate investment or financing trusts must comply with the general provisions of Law No 24,441 and applicable regulations of the Argentine Civil Code. A summary of the main legal requirements is as follows:

- Provided that the trust implies the transfer into fiduciary ownership of a real estate property, the trust must be granted through public deed.
- The parties to the agreement must be the settler, the trustee and the beneficiary (as per the definition of trust set forth in section 1 of the Law set out above).
- The trustee:
 - (i) cannot be the settler or beneficiary, or acquire the trust’s assets;
 - (ii) can be any individual or legal entity, except in case of public offering in which authorised legal entities can only be trustees;
 - (iii) must act diligently and only according to the *good businessman* standard; and

(iv) is entitled to a fee and the reimbursement of expenses.

- The trust agreement must contain the following provisions:
 - appointment of the beneficiary, which can be an individual or a legal entity;
 - detail of properties to be transferred in fiduciary property and other assets to be transferred potentially in the future;
 - term of the trust, or condition of its termination, which cannot exceed 30 years;
 - determination of the application of the assets at the trust termination;
 - rights, obligations and fees of the trustee;
 - termination events of the trust agreement; and
 - provision to replace the trustee.
- The trust agreement cannot foresee clauses waiving the trustee’s accountability or discharging him/it from any liability *vis-à-vis* the trust, the settler or the beneficiary.

Finally, a key issue in this matter is that the assets transferred to the trustee in fiduciary property constitute a separated patrimony, not affected by the settler’s and the trustee’s debts. Thus, their creditors cannot subject said assets to judicial compulsory sale proceedings (ie auction) to collect the amounts owed.

Real estate investment and financing trusts in practice

After the 2001-2002 crisis which affected Argentina, construction and investment on real estate appeared as an option in a still confusing economic scenario. Since 2003, the growth in construction projects has been material, compared to other productive sectors.

This growth encompassed a spread of the trust as a mechanism to structure construction or investment projects based on real estate developments.

Legal schemes to tailor these projects vary, since multiple options and schemes of participation in the business are available in practice. The tax impact must be analysed also when a structure of this type is considered.

Even when, in general, the structures put in place are similar, projects do not adopt a fixed pattern. The choice depends on the resources that each party applies or invests in the project, and the income or advantage that they expect to obtain. However, the implementation of the project through a trust is a common element in most cases.

In consequence, trust structures are used with certain particularities - which are tailor made for each case - to organise real estate projects, related mainly to condominiums, private neighbourhoods and country clubs. The settler/beneficiaries or buyers of the apartments or houses are, in general, individual investors who provide funds to: (a) acquire the land;

(b) cover the construction costs; and (c) pay the developer's or organiser's profit.

Usually, settlers apply assets (the land or funds to acquire the land or support the construction) for the trustee to develop the project and obtain (as beneficiaries) certain new properties or an income as a result of the sale of the new properties to third parties, or both.

Many of these trusts are organised as closed groups of investors who guarantee the necessary funds to complete the construction. Other projects obtain financing for the construction through pre-sales, by which buyers obtain a lower price since they acquire a future property at an early stage of the project. These funds are applied by the trustee to pay the cost of the construction and the price for the acquisition of the land. As the project progresses, new buyers or investors join the development.

In other cases, considering the magnitude of the project, investors apply funds to a trust – sophisticated and complex - in which the trustee applies the funds to the construction and commercialisation of the potential properties. The investors pursue an important gain within a certain term - which varies depending on the project - if the business succeeds. Developers can also leverage the investment by obtaining funds from bank loans.

The trustee can be the construction company or a third party with expertise in leadership, management and commercialisation. It is important for the investor that the trustee has the necessary experience in the relevant project, since experience is the major reason for success.

Finally, the developer can be the construction company, play a role as a party to the trust or be related thereto by means of a contractual scheme (eg management or construction agreement, depending on the nature of the developer and its intervention in the project).

Conclusions

Trusts can be very useful tools when structuring a real estate project, because of their flexibility and the possibility to combine them with complementary or parallel contractual schemes, provides a myriad of possibilities to carry out different businesses.

From the developer's side, the analysis must tend to design the most cost and tax-efficient structure which also guarantees the rights of the parties and the compliance with the obligations assumed and protects the assets previously transferred in fiduciary ownership to the trust.

From the investor's or buyer's point of view, the trustee's expertise and background is fundamental. Also, it is important to have a structure which reflects the parties' responsibility for the project and the protection of the investor's rights.

Time-sharing and gated communities under Argentinian real estate law

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Argentina is a civil law country. When referring to real estate law, this fact implies two main consequences:

- (a) the constitution and transmission of real estate is highly regulated, being such regulation rather strict and formal as to the types of in rem rights to be transferred, and
- (b) a properly constituted real estate right confers substantial security to the owner.

As a result of the foregoing:

- (a) rights over certain new real estate developments cannot be included within the rather short list of in rem rights and, thus, the rights constituted in them will only be able to be enforced as in personam rights, without the safety aspects of a properly acquired in rem right;¹ and
- (b) existing in rem rights are applied to real estate developments which they did not originally intend to address, with the consequence of leaving certain grey areas to the detriment of the purchaser.

Two cases that can be considered examples of the above-mentioned situations will be discussed below. First, time-sharing, a traditionally controversial system that will hopefully become less so in the future, due to the recent enactment of Act No 26,356 (the Act). Next, we will refer to the case of gated communities, which still lack appropriate regulation.

Time-sharing

Time-sharing became famous in the last decade not only as a vacation alternative, but also because of scams involving thousands of unwary buyers who were left with unenforceable claims against insolvent companies. The passing of the Act in March 2008 with a clear user-protective approach may put a stop to this situation. Presently, there are approximately 115 time-share developments and over 20,000 accommodation spaces (beds) available in time-sharing facilities in Argentina² which will need to comply with the Act in the short term.

The Act provides that, in order to be able to constitute and commercialise time-sharing properties, a public deed must be prepared by a notary public. Such a deed must include specific information on the property, vacation units, common areas, procedure required to add units to the establishment, type of right to be transferred to users, procedure to request vacation periods and rules of use, among other requirements. The deed must be registered, with the

main effect that neither the developer will be able to change the purpose of the property nor may any third party affect the rights acquired by the user of the time-sharing unit, even in case of bankruptcy of the developer or owner of the land.

The Act comprehensively regulates all aspects of these developments, including the content of the agreement signed by the user, the obligations of the developer, marketing and promotion, etc. Time will tell if the Act will be effective to tackle the legal uncertainties experienced in the past.

Gated communities

Gated communities are residential areas, generally located in the suburbs of big cities and within a closed perimeter which consists of a wall or fence. Security concerns and the desire to improve the quality of life in the last decades have led to an explosion of these types of developments in the outskirts of Buenos Aires, where they are counted by the hundreds, and other populated cities in Argentina.

There is no specific national regulation covering these developments which has caused several provincial governments to regulate them rather partially, given that none of the in rem rights established in the Federal Civil Code (which cannot be modified by local legislation) exactly apply to them.

Gated communities are mostly constituted as condominiums, although sometimes they can also be formed by vesting a corporation as the owner of all common spaces. The main reason for which the first alternative is chosen is that Argentinian law provides for expedited ways of enforcement of credits for unpaid condominium expenses, as opposed to the situation in the second, alternative case.

Local regulations regarding authorisations for the construction of gated communities vary with each province. The comment below is limited to the case of the Province of Buenos Aires.

Act No 8,912 (1977) and Decree No 9,404 (1986) regulate, among other issues, country clubs. In the year 1998, regulation for *barrios privados* or so-called 'closed neighbourhoods' was established, through the issuance of Decree No 27/98.

There are some differences between country clubs and closed neighbourhoods, without many practical effects. Most differences refer to the size of common open spaces (much larger in the case of country clubs) and their possible location. While country clubs are limited to non-urban areas, are generally bigger and for transitory use, closed neighbourhoods may be located in any area defined by the local authority and must have a mainly residential use. The latter is the most usual type, due to the fact that they are smaller and easier to organise.

The above-mentioned regulation divides land in two ways, as mentioned above:

- (a) through a condominium; or
- (b) in lots, whereby the owner is vested with

the exclusive property over exclusive parts, and a corporation with that of common areas.

No matter the alternative selected, two validation stages have first to be followed before the local authority:

(a) *Preliminary technical validation* for issues like location and suitability of the plot, the subdivision and dominium regime to be adopted, and issuance of a water supply certificate, among others; and

(b) *Final technical validation* requiring the submission of, inter alia, an ownership certificate of the plot, a plan for the drinkable water supply system, roads and electricity networks.

Only after the final technical validation has been obtained, may subdivision of the land take place through either of the two alternatives referred to above. In the meantime, which tends to be a rather long period of time, purchasers usually are only vested with a stake in a construction trust, a less preferable situation from the legal standpoint.

Notes

- 1 Among other things, a properly constituted in rem right is not affected by the statute of limitations, and is enforceable *vis-à-vis* third parties.
- 2 Please refer to: www.camaraargentinatourismo.travel/CAT/NOTICIAS/verMasNoti.asp?codiEdic=139&codiNoti=3.

AUSTRIA

The acquisition of property in Austria: where environmental law clashes with contract law

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When industrial property is purchased, environmental liabilities are usually on the agenda of the negotiation rounds. While sellers try to exclude any liability for contamination and the like, buyers will want to be fully reimbursed for damages they may sustain. The outcome of the negotiations will, however, only have effect inter partes, it will not remove the liabilities that may exist for either party under mandatory public laws. Further, the case law of the Austrian Supreme Court is generally suspicious of contractual clauses that exclude the liability of the seller for environmental damages, creating pitfalls for the unaware contract drafter.

This article will give a short overview over the legal framework of Austrian environmental laws and the case law of the Supreme Court on contractual limitations of environmental liabilities.

Waste Management Act 2002

The Waste Management Act 2002 regulates the treatment of waste materials which are defined as:

- (i) materials the owner wants to dispose of (subjective definition); or
- (ii) materials whose collection, storage, transportation and treatment is necessary and in the public interest (objective definition).

Waste materials need not be individual objects. Oil or similar liquids contaminating the ground also fall within the scope of the Waste Management Act 2002 and therefore constitute waste material for purposes of this Act. The Waste Management Act, thus, has a very broad understanding of the term 'waste material'. The federal Waste Management Act 2002 is complemented by regional laws and regulations.

The Waste Management Act 2002 imposes a number of obligations on the owner of waste materials. In particular the owner must not store waste materials outside of authorised facilities or store them in a way that contravenes public interest. These rules and the very broad understanding of the term 'waste material' impose far-reaching obligations on the owner.

If the owner of the waste materials does not comply with the Act, especially where the soil has already been contaminated, then the authorities will order that appropriate decontamination measures be taken. In case of imminent danger, authorities can take emergency measures themselves and recover the cost.

Generally, the Waste Management Act 2002 follows the 'polluter-pays principle'. The polluter remains liable, even if the property is subsequently sold. If the polluter cannot be determined or cannot remedy the situation, then the authorities can request the respective measures to be taken by the owner of the land, provided that owner either consented to the storage of waste materials or tolerated the pollution by a third party without taking adequate measures to prevent it.

If the property is sold, then the buyer is generally under the same duties. The buyer can, however, raise the objection that he was not aware of the storage of waste material on the site and could not have been aware of such fact. In such a case the buyer is not liable.

Water Management Act 1959

The Water Management Act 1959 contains numerous provisions concerning the use, preservation and protection of water. The term 'water' is any liquid made of H₂O and still in its natural cycle. The term mainly refers to lakes, streams, rivers, ground water and the like.

The Water Management Act 1959 restricts the use of water in so far as there must not be any danger to the health of people, animals or plants. Ecosystems and the environment should be preserved and protected. In general the use of water is in the public interest and thus subject to long-term analysis.

Any not insignificant direct or indirect introduction of substances into water (such as firm or liquid substances, gas, radiation, etc) is subject to prior approval by local authorities. Violations may cause heavy fines and constitute a criminal offence under the Water Management Act 1959.

In addition, if activities are set without prior permission, public authorities may request measures in order to remove contaminations within a reasonable period of time and to comply with the Water Management Act 1959. In the case of imminent danger, public authorities are allowed to take action themselves and to claim costs from the violator.

Similar to the above-mentioned provisions under the Waste Management Act 2002, the Water Management Act generally follows the 'polluter pays principle'. The polluter need not necessarily be the owner of the real property, but could be a neighbour or lessee. If the owner had either explicitly consented to such actions which are in violation of the Water Management Act 1959 or had tolerated such violations without taking reasonable measures to prevent them, then the owner is also liable for decontamination measures.

If the property is sold, then the buyer is generally liable for the decontamination measures. The buyer can, however, raise the objection that he was not aware of the violation of the Act and could not have been aware of such fact. Again, an environmental due diligence is necessary to prevent subsequent surprises.

Trade Act 1959

The operation of an industrial plant is subject to prior approval according to the Trade Act 1959, in particular if the industrial plant could be harmful to the life or health of people or to the property of neighbours, especially if neighbours are subject to additional noise, smell, smoke, dust, and the like. The operation permit may (and usually will) be complemented by additional obligations in order to minimise risks.

The operation permit and the related obligations are automatically transferred to the buyer of the industrial plant if an ongoing business is sold. If, on the other hand, business activities have already ceased, then the buyer will not be subject to the obligations arising from the original operation permit. However, the closure of the facility is supervised by the public authority which will either impose obligations or clarify that no measures need to be set, both by means of an order. The order is compulsory for the buyer who has to comply with the obligations once ownership is transferred.

Contract law

In past case law, the Austrian Supreme Court has given some guidelines on the interpretation of clauses that restrict representations and warranties of the seller in purchase agreements:

- *General exclusion of liability* A clause waiving all warranty claims of the buyer is generally valid, unless contained in a consumer agreement. In the absence of fraud or gross negligence, the buyer will generally not be able to reclaim the cost of decontamination measures or other measures.
- *Actual/consequential damages* Waivers of liability are to be construed narrowly. In case of doubt, the waiver will be interpreted in such a way that it only refers to the actual defect and does not include consequential damages. The buyer may thus still be allowed to claim the reimbursement for the removal of the waste materials.
- *Reasonable expectations* Parties may also agree that the seller does not warrant a certain quality or usability of the real property. This clause, however, only refers to features the buyers could reasonably expect. Massive contaminations (for instance oil contaminating the ground and the ground water) may be interpreted as outside of this clause. Therefore, the seller may still be found liable for decontamination measures, despite the waiver clause.

The liability of the seller also depends on the type of property concerned. For example, the buyer of a (former) petrol station must be aware that there could be some contaminations in the ground. The reasonable expectations are different from those of buyers of other types of property.

Conclusion

As pointed out, the buyer of a property may be liable for decontamination measures under public law if he was aware of the contamination or could have been aware when he took over the property. Therefore, the importance of carrying out solid environmental due diligence is twofold: If the survey finds that the property is contaminated, then this can be considered in the purchase agreement one way or another, at least in the purchase price. If, on the other hand, the survey finds that the property is not contaminated, this can be used by the buyer *vis-à-vis* the authorities to demonstrate that he could not have been aware of the pollution and is therefore not liable.

Share deal or asset deal? Which deal is ideal when acquiring a real property?

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A real estate can be purchased either directly (asset deal) or by purchasing the shares in the company owning the real estate (share deal). If a share deal is more favourable than an asset deal depends on various factors. In Austria, most of the larger real estate transactions of the past years were in the form of a share deal. The reason for this is that the transfer and registration taxes for an asset deal are 4.5 per cent of the purchase price; these taxes do not incur with share deals.

Asset deal

Object of purchase

Object of purchase with an asset deal are *real properties with buildings constructed on these*. As a rule in Austria, taken from the Roman law principle *superficies solo cedit*, a real estate is part of the real property on which it was constructed. The most important exceptions of this rule are the Construction Right (*Baurecht*) and Building on Third Party Land (*Superaedifikat*); in these legal concepts, separating ownership of building and real property is possible.

Due diligence

An extensive due diligence should be made for *evaluating the purchase price*. In particular, construction fibres, possible contaminations of the real properties, and other public legal duties can strongly influence the value of a real estate.

Existing contract relationships and licence grants

Should, in addition to the real estate, existing contractual relationships or public legal licenses (eg service contracts, construction permits, etc) be assigned, then appropriate arrangements should be made in this regard in order to ensure that the legal relationships can be transferred in the purchase contract. In this context, it is important to note that a *change of contracting parties* is the result of the change in ownership of the real estate. Therefore, each individual legal relationship must be examined if the contract can be transferred to the purchaser or if an arrangement with the original contract party must be found additionally.

Lease agreements

In principle, the purchaser of a real property *may terminate* lease agreements *prematurely* ('purchase weighs more than rent'). The majority of apartment and business office tenants are protected from such terminations by a specific law (the Tenancy Act – MRG), so that the purchaser of the real property assumes the status of the seller and, therefore, has no extraordinary right of termination.

Especially if real property is bought for the rental income, then it must be examined if the tenant, due to contractual agreements, has the right to, eg terminate the contract prematurely.

Property acquisition/Land Register

The purchase of a real estate by means of an asset deal requires a purchase contract, which must comply with the strict formal requirements of the Austrian Land Register Act. The object of purchase, the purchase price and the contracting parties must be cited properly in the purchase contract. The property right by way of single legal succession will, in this case, not be acquired until the property right has been entered into the land register. No matter how the contract is registered, Austria offers – compared to international standards – a scheme with large legal security for real properties. In simple terms, anyone can rely on the registration (ownership conditions, mortgages, and rights to a real estate) in the Austrian Land Register and legally can refer to this; the institution of title-insurance, used primarily in the United States, is not necessary in Austria and, therefore, also not available.

Fees and taxes

The fees and taxes for an asset deal are *3.5 per cent real estate transfer tax* of the assessment basis (generally the amount of the purchase price) and *one per cent judicial registration fee* of the same assessment basis.

If the purchaser finances the acquisition of the real estate, a mortgage is usually put up in the land register to provide security for this outside financing. For the registration of the mortgage a judicial registration fee of 1.2 per cent of the mortgage amount becomes due.

Special regulations

In the course of the execution of a transaction by means of an asset deal, Austrian Real Property Transaction Law, Austrian and European competition law, and various Austrian special laws (eg Cadastral Constitutional Law, Monumental Conservation Act, Railway Act, Water Rights, Land Survey Act, Building Regulations, Municipal Law, etc), in addition to the Civil Law Regulations, must be observed.

Share deal

Object of purchase

In this case, the purchaser does not directly have the civil-law title of the real estate but purchases the property right to the *shares of the company that owns the real estate*. Thus, nothing changes in the property structure of the real estate and all of the contract relationships regarding this real property persist together with the legal entity as object of purchase. The extraordinary termination of existing lease agreements on part of the purchaser is not possible in this case.

Due diligence

In addition to the due diligence solely regarding the real property, an exact examination of the legal entity is necessary for a share deal to determine the value of the purchase price.

In particular, possible liability risks of the company that is intended to be purchased must be examined; these do not have to be in direct connection with the real estate that is intended to be purchased, but could be due to other reasons. For example, warranty and indemnity claims against the company could exist from previous business dealings. As the object of purchase is not the real estate itself but the shares in a legal entity, it is strongly recommended to stipulate the entailed features (eg status or amount of the rental income) of the real estate by contract. Furthermore, the seller will have to deliver a balance sheet guarantee for the purchased company.

The *book value* of the real estates owned by the company is of great importance in this context. For real properties that had been purchased by the company some time ago, it often means their book value is lower than the market value. If a company with such a low book value (asset deal) resells such real estate then the hidden reserves must be laid open and thus taxed as profits (latent tax charges).

Existing contract relationships and licence grants

Therefore, nothing changes the property structure of the real estate and all of the contract relationships regarding this real property persist together with the legal entity as object of purchase, as long as these do not contain any change-of-control clauses. This must be examined within the framework of the due diligence in advance.

Lease agreements

The purchaser of the company does not have the possibility of extraordinary termination of existing agreements. However, it must be examined if the tenant has the extraordinary termination right due to the change of shareholders.

Property acquisition/Commercial Register

If shares in a limited liability company - *GmbH* are being acquired, the according purchase contract must be concluded in the form of a notarial deed. The acquisition of stock or shares in a private company is generally formless. Nevertheless, for documentation purposes as well as for stipulating liability limitations or consequences, it is recommended to conclude a written contract. The property right is purchased with the conclusion of the purchase contract.

The entry into the Austrian Commercial Register is merely declarative. There are no changes in the land register.

Fees and taxes

The property structure is not changed in the land register; therefore, no court registration fees are incurred for a share deal. If a third party acquires tiny shares (eg also possible by means of a fiduciary model) and this way the shares are not formally unified to 100 per cent, the *real estate transfer tax can be avoided* and there is no registration tax at all. Also, the bank liabilities, if any, incorporated in the company can be transferred without incurring further costs.

Special regulations

In the course of the execution of a transaction by means of a share deal, less special laws in addition to the Civil Law Regulations must be observed since the owner is legally still the same. Also the Real Property Transaction Regulations are easier to deal with if the 'grandparental' company of the target company is being acquired.

Comparison of share deal and asset deal

As long as the sale of the company by the seller is a possibility, a share deal is preferred in practice. On the one hand, public duties can be almost completely avoided with a share deal and, on the other hand, all contract relationships remain unaffected. In particular, the sales of 'larger' real estates or of real estate packages are concluded by means of share deals as a standard rule. Also the preparation of the target company to be acquired in the course of the transaction execution so that the designated real estate is the only asset has become a general standard.

The 'price to pay' for saving duty fees is the liability for any long standing obligations concealed in the company and any latent tax charges in case the real estate has been undervalued on the balance sheet.

Asset deals usually take place in non-institutional areas, since for an owner of a condominium the acquisition of a company will not be an advantage.

Brief summary

Why a share deal?

- Avoidance of economically relevant public duties (4.5 per cent of the purchase price).
- As long as there are no change-of-control clauses, existing contract relationship remain unchanged.
- Commercial register proceedings are judicially easier than the relatively complicated land register proceedings.

Why an asset deal?

- No liability for any long standing obligations of the legal entity (since no company is being purchased).
- Purchaser does not want to assume any hidden assets/deferred taxes.
- Purchaser may eg, due to fund provisions, only purchase real estate directly.
- Purchaser merely wants to purchase real estate directly because of eg foreign tax law or double tax agreements.
- The effort to introduce the real property into a company or to structure the company so that its only asset is the real estate (eg, spin-off) in proportion to the transaction size and possible duty savings is too large.
- The purchaser is, eg a private individual and does not want to acquire a company because he/she wants to own the real estate directly.
- Owning the real estate in a company is too expensive for the purchaser due to the running expenses in connection hereto.

BELGIUM

Selling or renting your property by text messages? The (unexpected) validity of real estate transactions through e-mail, internet or text messages in Belgium

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Modern communication techniques have also entered the real estate business. However, the validity of real estate transactions effected by such techniques as e-mail, internet or short text messaging is not always unambiguous. The question becomes all the

more pertinent when one party is of the opinion that there is a binding agreement and the other party is not.

Under Belgian law, an agreement is effected when the parties concerned agree upon all aspects which are essential for that transaction. This simple rule could however ensue problems as to evidence and interpretation of the agreement, all the more when the parties have exchanged their approval by electronic means of communication (e-mail, internet sites, short text messaging).

The Belgian Law of 11 March 2003, which on its turn was the transposition into Belgian law of a European directive of 2000 (Directive 2000/31/EC of 8 June 2000), determines that all legal or regulatory requirements for the formation of contracts through electronic means are deemed to be met, when the functional qualities of such requirements have been safeguarded. Any requirement of a written document will have been satisfied by means of 'a sequence of intelligible signs which are accessible for later consultation, irrespective of its support or transmission'. As a result, the electronic form of an agreement may not cause any obstacle for its validity and enforceability. This assumes, of course, that an agreement has been reached on all essential elements for that transaction.

The requirement for a signature will be met, either when a chain of electronic data is available which can be attributed to a certain person and which evidences the preservation of the integrity of the contents of what is signed, or by means of electronic signatures and certification services.

There is, nevertheless, an important exception to the applicability of this legislation: the Belgian Law of 11 March 2003 does not apply to contracts that create or transfer rights in real estate properties. However, there is an exception to this exception: a lease agreement can be entered into by electronic means, as far as no authentic deed is required. Since such authentic (ie, notary) deed is mandatory for (among others) lease agreements with an initial duration of more than nine years, only lease contracts with a duration of less than or equal to nine years can benefit from this exception.

When a future landlord and tenant come to an agreement on the principles of a lease contract, whether or not with the intervention of a broker, by exchange of communication on a website or through e-mail correspondence, neither party will be capable successfully to deny the existence of a valid and enforceable agreement, just for the reason that the agreement materialised by electronic means, without a hard copy contract.

This also means, however, that serious doubt can arise with respect to the enforceability of standard clauses which are often included in the automatic signatures or in *disclaimer* notices of e-mail messages (often phrased as 'subject to contract' or similar expressions) and which exactly aim to avoid the creation of a binding contract.

In principle, an e-mail message expressing the

consent of a party to all elements which are essential for the specific transaction or containing the explicit acceptance of an offer made earlier, and which in addition to that, is sent by a person who is legally entitled to commit that party (or by a person who could legally be assumed by a counterparty to have such capacity), will as a consequence result in a binding and enforceable lease contract. This could even be the case when such e-mail contains a standard type notice such as 'subject to contract' or similar wording.

In addition, the actual point in time at which an agreement is formed is often very important, or more generally, the moment in time at which an offer or an acceptance is received by the counterparty. This is even more important when several offers are brought out nearly simultaneously as part of a bidding process, as the case may be to separate parties (different brokers, broker and landlord directly etc). As to electronic contracts, it is generally accepted that the contract is formed at the moment of the receipt, by the other party, of the acceptance, ie the moment in time when such acceptance is accessible to the receiver. When such acceptance occurs through a website, this receipt is considered as taking place when the acceptance appears on the screen of the receiver. With respect to e-mail, the moment of receipt coincides with the moment at which the message reaches the server of the mail service where the mail box of the addressee is located.

The fact that electronic contracts as meant by the Law of 11 March 2003 cannot be used to create or transfer rights with respect to real estate (other than leases), does not prevent, however, valid and enforceable contracts from originating *between parties* through e-mail correspondence, when the mandatory conditions thereto have been met and all legally required provisions have been mentioned. This does however not alter the fact that, in general, for the enforceability of such agreements towards third parties, a confirmation of the agreement through an authentic deed still remains necessary, mostly implying the intervention of a public notary.

CHILE

Real estate financing in Latin America

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How does the legal environment influence real estate projects in Latin America? Which main challenges and opportunities we envision in this part of the world?

The case of Chile

While title insurance in Chile is almost unknown and the real estate registry system is very old fashioned, most risks may be overcome through legal due diligence entrusted to an experienced attorney, based on reliable public registries and the protection of statute of limitations.

Most real estate transactions are financed locally, through equity and debt financing provided by local bankers. Local bankers are healthy, but they are very dependent on foreign financing and as long as the later has not been available in recent days, there has been an impact on available funding along the whole construction chain.

Investment by private pension funds and insurance companies (including but not limited to real estate) amounted to US\$130 billion (the market is one of 15 million people) by the end of 2007, and thus they have been relevant players by purchasing mortgage-backed securities (MBS) and real estate assets seeking to match their long terms liabilities. Most of such MBS are backed by first class mortgage and represent less than 80 per cent of the appraisal values of the property. Neither market bubble (in fact, prices are not higher than in the late 1990s, a previous peak period for construction)¹ nor sub-prime crisis have taken place here. State debt in Chile amounts to minus US\$30 billion.

Up until September 2007, non-performing loans have been around one per cent or less, and foreclosures of mortgages have not represented a problem in a market led by local bankers, insurance companies and other financing institutions. Foreclosure of a mortgage implies a judicial procedure that leads to a public auction whereby the public and the creditor have an opportunity to buy the property. From a time perspective, it may take six months unless something goes wrong.

Another relevant issue is zoning regulations, in Chile there is a clear borderline between urban areas and agricultural lands, where developments are subject to special more restrictive permit processes including environmental clearance.

How financing is usually structured in Latin America, equity, debt alternative financing sources - options for structuring project financing

Real estate market has been led in Chile by a few large and well known local real estate developers, most of them operating as family business, of which only four companies have gone public in the Santiago's stock exchange.

At the time third parties beyond strong families ties join the business that seeks to expand equity financing sources, a close corporation becomes the appropriate vehicle, since they are controlled by the majority of the shareholders (unlike LLCs that requires unanimous consent).

Since full control is achieved with two-thirds of the stock and Chilean Law on Corporations provides for strong statutory protection to minority shareholders, controllers are forced to concentrate ownership to keep control which implies to forego opportunities to share a broader portion of the capital with outsiders. Otherwise, complex parallel shareholders agreements on common exercise of corporate control need to be negotiated.

However a recently enacted law has created a sort of joint stock corporations, removing most mandatory protection to minority shareholders and barriers applicable to preferred stock. Such flexibility enables the creation of different series of shares whereby there is ample freedom to restrict voting rights as well as to foster the right to dividend distribution, placing – if that is the idea in a given case - a shareholder in a position very close of that of a creditor.

Statutory protection minority shareholders of publicly traded securities have not been lessened and, as a result, concentration of ownership by controller is the prevailing rule. In the case of the four major real estate companies that offer their shares in the Santiago Stock exchange more than 75 per cent of the shares are owned by the ten principal shareholders.

Project financing, as separate from corporate financing, may be channelled through private real estate investment trusts (REITs) which were supposed to provide to investors the opportunity to select specific projects according to different risk profile and business preferences. However, since in practice they were most used as tax planning tools, some restrictions have been introduced as to the kind of investment they may undertake. However certain corporate structures of corporation and joint stock companies may help to isolate project risks from common corporate risks.

Convertible debt may attract investors to provide funds in the early stages of a project, which some times includes collateral by equity owners, irrespective if they ever take the chances of converting it into shares.

As to debt financing, acquisition of the land is usually afforded through equity and construction projects are typically financed by mortgage secured loans granted by commercial banks. Lease back may also be an appealing option for structuring debt financing, since avoids delays and hindrance in mortgage foreclosure and specific taxation on loans. Other structures for project financing are promise to purchase or sale agreements, as well as option agreements, with land owners or end buyers, as the case may be (advanced payments).

Local investors may not feel inclined to obtain financing in foreign currency, since most revenues are in local currency. I do not see that foreign investors may invest in local currency either. Foreign investor will face both the risk of exchange rate and internal inflation rate. Local investors are very familiar with mechanisms of indexation of internal inflation rate – loans in Chile are customarily expressed in an indexed unit - but foreign investors are not.

There are also tax considerations that for a foreign investor may affect choosing between equity and debt financing, beside corporate considerations.

Under domestic legislation, outbound interest is subject to withholding tax at a standard rate of 35 per cent on the gross interest. However, interest remitted abroad may be subject to withholding tax at a reduced rate of four per cent on the gross interest, eg when remitted to a foreign bank. In this case, however, Chilean thin capitalisation rules may apply. Under these rules interest subject to the reduced four per cent rate of withholding tax is further subject to a 31 per cent equalisation tax when it is paid to non-resident related entities or persons on excessive debt. The debt is considered to be excessive when the debt: equity ratio exceeds 3:1.

However, interest remitted to a double taxation treaty country is generally taxed at five per cent, ten per cent or 15 per cent. Dividends and profits distributed to shareholders abroad are subject to a dividend tax ('Additional Tax') at a flat rate of 35 per cent at the time of payment. However, the 17 per cent First Category Tax (corporate income tax) paid on the underlying profits is creditable against the dividend tax.

Opportunities in a stable emerging market and current situation

No-one can pretend that it has ironclad protection against a global crisis, and local market has been facing impacts, such as higher costs, including energy and steel. There is also a concern on increasing internal inflation that may reach nine per cent and more at the end of this year, which, in turn has a direct impact on debt since loan repayment is indexed according to inflation rate of local currency. Interest rate for major construction firms has been increasing.² Local banks are now facing more restrictive conditions and higher interest rates to obtain foreign financing and as a result debt financing for construction projects is becoming more restrictive and expensive, if not unavailable sometimes.

There is also an impact of global crisis on public equity, given higher risk premiums demanded by investors as a collateral effect of sub-prime crisis. In fact, shares of real estate developers have plummeted between 24 and 56 per cent in the Stock Exchange during the first eight months of this year.³

In line with the goal of diversifying risk allocation, in addition to combining different financing structures as the ones mentioned here, some companies have reduced the impact of risk of particular sectors, such as housing (an area where there is an excess of available stock), by combining investments in other real estate sectors, such as infrastructure, office buildings, commercial facilities (malls, small shopping centres), etc. Diversification in commercial and infrastructure projects has allowed some companies to overcome vulnerability of housing project to economic turmoil.

As to the prevalent trends in Chile in the last

months, favourable conditions of local economy had led many local companies to seek higher quality offices in Santiago, which fostered a strong demand for space. Quality of units helps to overcome impact of depreciation, particularly at the time of resale. In addition, foreign investment funds, in addition to local private pension funds, have become relevant players in the domestic office market by purchasing office buildings already constructed or in the process of construction. This responds to the high demand by institutional investors (mainly pension funds and insurance companies), seeking long term revenues to match their liabilities.

At the end of August 2008, class A office space market had a vacancy rate of around 0.55 per cent (around 7,440 square metres for lease or sale). It is expected that more than 100,000 square metres of class A offices should be made available during 2008. The low vacancy rate has resulted in an increase or prices (5.4 per cent increase in the last year) with sales prices of around between US\$2,000 and even more than 3,000, and lease rental of approximately US\$25 (per sq metre per month).⁴ This is a very low figure if compared to Brazil (US\$60 for Río and Sao Paulo), not mentioning Hong Kong and London (US\$191.7 and 186.1 per sq metre per month).⁵

Recent purchases of office buildings by foreign investment funds have resulted in transactions of US\$65, 57, 100 and even 200 million involving European Investment Funds, and prices for square metres range from US\$2000-3,500.⁶

Housing is now somehow depressed due to an excess of available stock amidst uncertainties related to the global turmoil.⁷ According to the forecast of some leading developers housing market should obtain a global sales figure of US\$3.3 billion, representing a 15 per cent reduction if compared with 2007.⁸

The Chilean Construction Chamber has forecast that investment in commercial and tourism infrastructure during 2008 should reach US\$1.5 billion (36 per cent increase compared to 2007), though such a figure might respond to a degree of concentration of investment in time which does not afford a similar forecast for future periods.

There has also been the case of the flourishing of real estate business around the wine industry (waste lands that went up to US\$10,000 per hectare), the concept of industrial and technological parks, intended to combine the development of industries with the availability of financial, commercial and business services in the same area, and even with the development of housing projects. In a city as extensive as Santiago de Chile this makes a lot of sense. A separate case of development of real estate has taken place in the south in the city of Puerto Montt and its surroundings, to meet necessities of the expanding industry of salmon farming.

The wine industry in Chile has not only resulted in needs for cellars and other related facilities and housing for employees. It has also fostered other

connected business such as restaurants, hotels, museums and related facilities. A couple of decades ago the city of Santa Cruz was a rural agricultural town similar to many others in Chile. Now it has premium hotels, restaurants, one of the best museums in the country and many vineyards in the surroundings always prepared to receive tourists and visitors. Not everything is easier and sometimes zoning and environmental regulations, particularly if narrowly interpreted by government officers, may cause some trouble.

Notes

- 1 Joaquín Brahm, *El Mercurio*, 18 August 2008.
- 2 *El Mercurio*, 18 August 2008.
- 3 *El Mercurio*, 2 September 2008.
- 4 Joaquín Brahm, *El Mercurio*, 18 August 2008.
- 5 *El Mercurio*, 29 September 2008. Office space under construction in Santiago would amount to 500,000 square metres.
- 6 *El Mercurio*, 27 August 2008 and 28 September 2008.
- 7 Velocity of sale process has increased to 21 months if compared with historic average of 15.5 months to exhaust the stock (2000-2008). Quarterly Macroeconomic report of Chilean Construction Chamber, as of August 2008.
- 8 Quarterly Macroeconomic report of Chilean Construction Chamber, as of August 2008.

CROATIA

Relaxation of acquisition rules for EU nationals

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As of 1 February 2009, nationals from European Union Member States will generally be free to acquire real estates in Croatia without any administrative prior approval. This effectively means that EU nationals will have the same treatment as Croatian nationals.

Currently, acquisition of real estate property in Croatia by foreign nationals is subject to various limitations. Foreign nationals may acquire real estate in Croatia provided that two linked requirements are met: (i) that reciprocity exists between Croatia and the foreigner's country of citizenship; and (ii) that prior approval of the Croatian Minister of Justice for the acquisition is obtained.

By way of exception, a foreign national may acquire real property in Croatia by inheritance, provided that the reciprocity requirement is met. Also, certain types of real estate cannot be acquired by the foreign nationals at all. The above restrictions do not apply to corporate vehicles established in Croatia, even if they are wholly owned by foreign persons.

On 29 October 2001, the Stabilisation and Association Agreement between the European

Communities and their Member States and the Republic of Croatia (SAA) was signed in Luxembourg. The SAA ratification process ended on 1 February 2005 and the SAA entered into force as of that date. Article 60 of the SAA provides that within four years from the entry into force of SAA, Croatia must ensure the same treatment to nationals of the Member States as compared to Croatian nationals. This transitional period expires on the 1 February 2009.

However, restrictions concerning acquisition of the agricultural land as defined by the Agricultural Land Act and areas protected under the Environmental Protection Act will remain. The Stabilisation and Association Council will examine the modalities for extending the rights granted to EU nationals also with respect to these types of real estate. Of course, it remains to be seen at which pace and scope this extension will ultimately progress.

Finally, various limitations as described above shall continue as regards foreign nationals of non-EU countries.

CYPRUS

Cypriot real estate in the current economic climate

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2007 was an exceptional year for real estate in the Republic of Cyprus, with over €4 billion in property being sold. Naturally, this volume of sales could not continue into 2008, but the slowing-up of property sales in Cyprus has coincided with the global economic crisis. Following such a lucrative year, how much the economic crisis is to blame for the drop in sales and consequently property prices on the island, is hard to determine.

As with most tourist destinations, the majority of purchasers and vendors of holiday homes will wait and see what happens over the coming months. However, for the purchaser seeking a high-end property on the island, opportunities are for the taking.

Cyprus boasts some of the most beautiful beaches in the Mediterranean and with its endless sunshine, is an excellent choice for a holiday home. In a recent national newspaper article, Peter Turtzo, Vice President of Sotheby's International Realty stated that, 'Cyprus can become a destination for purchasers of luxury properties as it is a beautiful place with easy air access and has all the ingredients that God provided for it to be an excellent destination.' Furthermore, he states that, 'the right time for Cyprus is now because there

are many smart people that have invested and are investing in luxury properties on the island.'

Besides the climatic benefits of the island, the increase in the Cyprus property market has also been due to the legal certainty afforded by the title deeds issued by the Land Registry. The Republic of Cyprus has a fully developed system of land registration, which in conjunction with its common law legal system, is designed to protect both the vendor and purchaser of land. One particularly interesting protective element is afforded by The Sale of Land (Specific Performance) Law. After a contract for the sale of land is signed, it may be filed with the Land Registry within a specific period of time. This is an important safeguard provided by the law, which in essence informs the Land Registry that the purchaser has a right to the property and therefore any subsequent third party rights cannot be registered against the property. For example, if the vendor decides to sell the property again to an unsuspecting third party, a cursory check at the Land Registry will disclose the prior right. Moreover, if the third party claims the property, the prior registered right prevails and furthermore the purchaser may obtain a judgment from the Court directing the registration of the property in his name, if the vendor refuses or fails to transfer the property within the time agreed as per contract of sale (ie a court judgment ordering the vendor to specifically perform his duties under the contract.

The current economic crisis does not affect such safeguards provided by the laws of the Republic of Cyprus.

In essence, if you have the means to purchase a holiday home in Cyprus, now may be the time to start considering it. Prices are falling and the sun keeps shining.

GERMANY

Redevelopment in Germany: public planning workshops (Werkstattverfahren)

Public process as a tool to market the project and reconcile a diversity of interests

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Major city redevelopments in many places in Europe and the US are realised on former industrial sites for a number of reasons: they are often the only sites large enough for substantial developments in densely populated cities, they are becoming available as the industrial use is coming to an end and they are often put on the market by the former industrial owners offering attractive pricing and interesting payment conditions. If acquired at an early stage they offer from the developer's point of view huge opportunities for very substantial increases in value. The challenges developers are facing is the time-consuming change of the zoning of the site in a reluctant or even hostile environment. This comes on top of the general challenges of redevelopment, as former industrial sites require special attention before returning on the market; a notorious legal aspect being environmental law and regulation. Public planning workshops (*Werkstattverfahren*) have proven to be successful tools in Germany for site owners and developers to change the zoning of former industrial sites in a foreseeable time line, increase public visibility, change perception of the site, boost acceptance of the project in the wider neighbourhood and minimise the risk of legal challenges brought to the planning process.

The interests at stake in redevelopment projects

The practical challenges to redevelopment projects stem from the necessity to scope a whole variety of interests and resolve them in an economically feasible manner. Among these challenges, obtaining a suitable planning consent with the authorities in form of a zoning plan is the crucial aspect.

Owners of former industrial sites are not very likely to readily have specialised management and in-house support staff at their disposal to accommodate all relevant aspects of a redevelopment project. Frequently, a short-term exit is sought in order to

dispose of redundant real estate. This target is some times jeopardised by a lack of vision for profitable redevelopment scenarios.

From a planning perspective, the affected property will regularly be treated based on an out-dated zoning that can no longer reflect adequately the property's development potentials. Hence, rezoning is inevitable in the majority of cases. Public planning consent and zoning is in practice the relevant point where project-driven redevelopment visions intersect with other commercial and legal requirements from an investor's perspective.

Although, it may be argued that without a pre-defined project idea no reasonable zoning and public planning will be feasible, the statutory zoning process in Germany encompasses all relevant aspects of any property revitalisation project; namely environmental remediation actions, public planning restrictions (eg based on a regional development plan), limitations to large scale commercial developments based on market analysis, etc. Without such fact-gathering the city's planning decision would be manifestly flawed and the validity of the zoning would, thus, be at risk. This is why local planning authorities often express an own interest towards urban redevelopment properties. This interest should be utilised by the site owner for its very own project vision.

As large redevelopment properties with a long-term history of industrial use are furthermore significant to the shaping of urban patterns as a whole, such projects equally attract a political urge to be involved into the planning process at a rather early stage. This is the more true bearing in mind that all urban planning in Germany remains the ultimate responsibility of the local city/district council.

The approach of many German cities: harmonisation of interests by way of a public planning workshop

Against this background, major German cities and their planning authorities have come to establish a cooperative approach to tackle large redevelopment properties – the so-called public planning workshop (*Werkstattverfahren*). Different from the already well-known architectural contests that are held in connection with prestigious or significantly large development projects, a public planning workshop aims at exploring individual redevelopment potential based on virtually all regulatory information available from the local and regional administration in a view to test the acceptance of the zoning and to minimise challenges broad to planning decisions by neighbours and competing developments. The planning workshop is usually chaired by representatives of local government. It combines the benefits of a mere architectural contest with public sector information.

The basic concept of such a planning workshop comprises five steps:

- collection and evaluation of property and planning related information; producing a workshop

- brochure/printed project documentation;
 - setting-up workshop teams of architects and urban planners that compete in submitting redevelopment concepts for the site;
 - public events and presentations that allow input from all interested members of the public and deliver the urban concepts of the invited planning teams;
 - jury meeting of city planning authority, independent experts, city council members and representatives of the site owner to vote for a favourite concept among all submitted works; and
 - public roll-out of a master plan for the project site.
- The process as such is comprehensive and comparatively far-reaching. It is focused on developing urban and realisation-focused concepts for redevelopment. Different from the well-known architectural workshops, it goes further and brings together city planning authority, city council and interested neighbours. In doing so, it bundles planning efforts to considerably smoothen the usually long way towards achieving a revised urban zoning, which ultimately will allow a commercial redevelopment of the sites concerned.

Delivering results

Hence, the workshop process inter alia delivers the following results:

- support in shaping of ideas for a successful result (marketable product);
- in doing so it informs the investment horizon of the real estate owner;
- eye-catcher, raises public interest in the property concerned and in doing so supports soft marketing efforts;
- facilitate collecting property facts relevant to any subsequent zoning decision (environmental situation, infrastructure, planning restrictions, listed buildings on site, etc);
- active involvement and influence of the property owner over the public zoning decision;
- the workshop extends to public consultations, so that latent conflicts with neighbouring properties can be identified and mitigated more easily;
- reassurance of owner and potential investors alike with regard to any zoning-related requirements of the local authorities; and
- facilitation of formal rezoning as public workshop presentations establish consensus on redevelopment targets.

Public planning workshops are becoming a valuable tool in progressing with redevelopment scenarios. If nothing less, they ensure transparency for the site owner and an interested public alike. At the same time the workshop process can serve as an integrative factor to further a co-operation between the site owner and an investor on the one hand and the regulatory bodies on the other hand. Workshop brochures and presentations in cooperation with the local authority can further serve as a valuable marketing tool for the redevelopment property.

Nevertheless, the challenge of coordination in the run-up to a planning workshop must not be underestimated. A timely approach to the local planning authority as well as to any stake holders in the intended redevelopment is strongly recommended. Also, the suitability of this process to a given project must certainly be assessed on an individual basis.

ITALY

Shopping centres in Italy: an overview

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The starting point

Since the beginning of the 1980s, the distribution system in Italy has undergone significant changes in manifold respects. In particular, a number of concentrated properties, comprised of shops, stores and malls was built and prospered in the surroundings of large cities. With the purpose to harmonise the different legislative and regulatory frameworks that had developed at local as well as central level, the so-called Bersani Law was adopted (Law 114/98). As far as trading licences are concerned, the Bersani Law provided that in the case of small properties, no express licence was required, and it was only necessary to file a declaration with the competent municipality. After a waiting period of 30 days, the licence was deemed granted.

However, in the case of medium and large properties, the licensing process became more complex. A previous compliance check with town planning rules became required and the competent authority was the region instead of the municipality.

According to section 4.1 g) of the Bersani Law a shopping centre is composed of small, medium or large area shops that have in common some services.

Purchasing a shopping centre

It may happen that an existing shopping centre is purchased by an investor. In such a case, two different options may be considered:

- the purchase of the real estate consisting of land and buildings, and
- the purchase of the ongoing business that includes or utilises the land and buildings.

In the case of a purchase of real estate, the trading licence is obtained through complex and relatively lengthy administrative proceedings.

Conversely, in the case of a purchase of ongoing business the object of the sale is the real estate itself or the right to utilise it (typically, under a long-term lease) as well as the 'complex of assets organised by an entrepreneur for the exercise of an enterprise' pursuant to section 2555 of the Italian Civil Code. This means in practice that the trading licence(s) are transferred to the purchaser as a component of the business, along with fittings, operative contracts, utilities, appurtenances and goodwill.

The trading licence for a shopping centre

In order to open and run a shopping centre, a building permit together with a trading licence must be obtained. The national legislation has transferred to the regions jurisdiction in this respect. In most cases, the owner/developer of the shopping centre obtains from the authorities the trading licence for the entire surface, and then single trading licences are temporarily transferred to the retailers.

Two ways to transfer the use of single shops to the retailer

There are two different ways to enable retailers to run their business within a shopping centre.

The first is through a simple property lease contract. In such a case, the trading licence is not transferred to the retailer and Law 392/78, the main part of lease law in Italy, is applicable.

Law 392/78 contains a number of mandatory provisions with the purpose of protecting the tenant, as a result of which any different provisions contained in the contract that are more advantageous to the landlord are deemed void and automatically replaced by the applicable provision of the Civil Code or Law 392/78 itself.

For example, the duration of a commercial lease is set for not less than nine years. When a clause of the contract provides for a shorter duration, the longer duration applies nonetheless. Furthermore, clauses containing rent increases beyond the allowed extent (which is related to certain inflation indexes) these are void too and the tenant is entitled to challenge the validity of the clause for up to six months after expiry of the lease and claim restitution of all amounts paid in excess.

Due to the rigidity of the legal structure of commercial leases, the most common way for a landlord to transfer the temporary use of a commercial surface to a tenant is a contract of the lease of an ongoing business (as opposed to a lease of the property).

Even in such a case, certain provisions of the Law remain mandatory, but acceptable results can be achieved through an effective negotiation of the contract between landlord and tenant, utilising all legally available room to produce a balanced result.

The most significant feature to be borne in mind in a

deal structured as a lease of ongoing business concerns the potential liability of the landlord for the tenant's obligations towards employees at the end of the lease. In fact, in the case of termination of the lease of an ongoing business, the single contracts between the tenant who runs the business and his employees cannot be terminated automatically. To cater for such a case, the landlord will have to negotiate in advance special clauses and guaranties in respect of the burden of termination of the tenant's employees when the lease comes to an end.

Summing up

The legal framework applicable to relations between landlords and tenants of commercial property, in both the cases of lease agreements proper and lease contracts of an ongoing business, is fairly structured and complex; town planning and public law features are frequently relevant, and a number of provisions of the law cannot be validly contracted out by the parties. Therefore, a careful negotiation of the contract is of the essence. In most cases, a pre-existing contract is submitted by the landlord, and – except where very large properties are rented - the contractual power of the tenant is low. Hence, sound advance legal advice and careful negotiation at all stages is of crucial importance.

MEXICO

New rules for the termination of property rights in assets involved in criminal activities

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In the early days of 2008, the Mexican federal legislature approved a set of constitutional amendments aimed at reforming law enforcement in Mexico. The amendments, which became effective in June 2008, included a new instrument for prosecutors: the termination of private property rights in assets related to criminal activities.

Prior to the amendments, private property seized in connection with criminal activities concerning organised crime and certain types of crimes committed by government officials, could be forfeited in benefit of federal and state governments, through a judicial procedure which required the final determination in the corresponding criminal process. The forfeiture procedure was considered as complex and cumbersome, as the government could not dispose

of the seized assets until a final determination on the criminal case was reached. The negative view of the forfeiture procedure by government officials as an effective tool against crime was reflected in the repeated use by the mayor of Mexico City of expropriation - which requires indemnification to the owner and is reserved for cases of public interest - to take residential and commercial properties involved in criminal activity.

The constitutional amendments introduced a general framework for the termination of private property rights in assets involved in criminal activities, requiring a judicial procedure, separate from the criminal process, for the termination of private property rights. The new constitutional provisions limit the crimes which may cause the termination of private property rights, which are organised crime, drug-related crimes, kidnapping, vehicle theft and trafficking in persons. The assets which may be subject to the termination of private property rights under the amended constitutional rules are those which are used as instruments, objects or products of crime or used to hide assets obtained as a result of a crime. Assets used in criminal activities, owned by third parties who are not involved in such activities, may also be subject to the termination of private property rights procedure, if the owner had knowledge of the criminal activity and failed to report such activity to the authorities or failed to take preventive actions.

In early December 2008, the Mexico City legislature enacted the first local legislation implementing the termination of private property rights under the new constitutional framework. The new legislation in Mexico City provides for a procedure for the termination of private property rights along the lines set forth by the constitution rules, expanding in certain aspects, the most relevant being a detailed chapter on preliminary measures that the court may issue at the request of the prosecution in order to immobilise any assets subject to a procedure for the termination of private property rights.

President Felipe Calderón has submitted to the federal legislature a proposal for a federal law for the termination of private property rights, which is still being discussed at the federal legislature.

The constitutional amendments raised few comments in the real estate sector when published in the summer of 2008. It was not until the legislation proposals were presented at the federal legislature and the Mexico City legislative body in the later months of the year, when opinions on the subject were expressed in the media. Some leading criminal attorneys raised concerns about the potential for abuse by prosecutors under the new laws. In the real estate sector, the new law in Mexico City has stirred debate, and different views have been exchanged on the effects that the law will have in the real estate market. Some real estate agents and developers consider that the new law will have a negative effect in the market, by preventing property owners from offering their properties for

lease. Other agents consider that the new law may have a positive effect in the market by forcing property owners in conducting a proper due diligence of prospective tenants and documenting and recording their respective lease agreements. The effects of the new instrument of termination of private property rights are yet to be seen, but there is no doubt that it will depend in great measure on the use of such instrument by federal and state prosecutors.

The Mexican real estate market: mandates for the financial crisis

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Managers of investment funds have said publicly that 'the Mexican real estate market continues to have liquidity available from international funds.' The market has, however, restricted liquidity from banks because the majority of Mexican banks are internationally owned and these international banks have generally suspended financing real estate transactions worldwide. In Mexico the granting of mortgage credit by banks hinges on pricing.

The financing of and investment in viable Mexican real estate projects remains feasible. Although viable real estate projects are sought after by Mexican and international funds, financiers and investors, a sufficient number of these projects are not necessarily available in Mexico. Viable real estate projects depend on the ability of developers/promoters to follow the market and comply with the applicable local legal framework. This has to correlate with international requirements and standards, which are followed by specialised Mexican legal firms with an international orientation.

In short, there may be a scarcity of Mexican real estate projects would comply fully with international standards. Expert Mexican legal counsel is vital to achieve compliance.

Funds, financiers and international investors, interested in taking on Mexican real estate projects are advised to negotiate a detailed property term-sheet, providing the relevant terms and conditions at the outset. Without this, the agile structuring and completion of transactions can be impeded by

vague terms and conditions and a lack of targets and planning.

The main legal aspects covering the protection of participants lies in ensuring the active participation of representatives of funds, financiers and investors, as well as negative controls (if a minority investment is contemplated) and terms and conditions allowing for the surveillance of compliance with business and regulatory covenants.

The legal structuring of real estate transactions, now more than ever, requires clear descriptions of financial terms, cash flow requirements and the specific obligations of each party involved.

Finally, an additional opportunity available to funds and potential investors, consists of the acquisition of land. This activity results in territorial reserves for future real estate projects. The acquisition of land reserves in the current climate seems to be the key to successful future plans for the Mexican real estate market.

PANAMA

Due diligence in real estate transactions in Panama

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The Republic of Panama, with its unique geographical position, the territorial taxation system, the US dollar as currency, the Panama Canal and other factors have historically oriented Panamanian governments to create policies to constitute and develop what is known today as an 'International Financial Centre'.

Taking the above into consideration, Panama's Economy, as one would imagine, is largely based on the provision of services. In fact, the economy in Panama is focused on banking, construction, commerce and tourism, with the canal and the shipping business playing a very important role. Growth of the country in the last three years has been significant, creating a stable economy that is growing at a rate of six-eight per cent per year, one of the highest in Latin America. The year 2007 was particularly successful. According to figures confirmed by the Panamanian Controller's Office the economy grew 11.2 per cent in 2007. The sectors with the best performance were the ports (38.1 per cent); the construction industry (29.3 per cent) and the tourism industry (18.6 per cent).

The above factors, along with the political stability, are what principally attract the attention of foreigners looking to invest and/or relocate to Panama.

The economic bonanza has put Panama on the

map yet once more, but this time as a destination for investors in the real estate market. Individuals and companies are all looking to purchase a piece of this tiny nation in order to develop it or just retire in it or have a second home. The current global crisis may have slowed investments in the real estate market in Panama, but have not stopped it. In this sense, we keep receiving investors from other countries, like for example Venezuela and Mexico, thus it is only important to be prepared to provide the best advice possible to them.

As advisers in a real estate transaction, whether it is a deal in the thousands or in the multi-million dollar figure, we need to follow several measures before considering advising the client to sign a promise to purchase agreement or a final purchase agreement.

Legitimacy to sell

It is important to verify at the Public Registry that the seller, whether it is an individual, group of individuals or legal entities, is/are the legitimate owners of the property.

Where an individual or individuals are the owners of a property it is important to verify that their details are correct and that they have legal capacity to enter into obligations.

Where a company or other form of legal entity is the owner of the property, it is important not only to verify that the details are correct, but also that the company is in good standing, in existence and that the individual representing the company complies with the legal capacity referred to above.

Object of the transaction

Once the ownership of the property is verified, the transaction can continue its course and further due diligence must be made on the property itself when the same is owned by an individual or group of individuals. We will discuss this part further ahead in this section.

However, when the property is owned by a legal entity it is important to discuss with the seller the object of the transaction, whether it is the shares of the company or the underlying property.

Shares

Should the object of the sale be the shares of the company, it is important to review the corporate documents of the company as our experience indicates that in many cases errors and absence of important documents delay the closing of the transaction. The most common are the following:

- (1) On many occasions the subscribers of the articles of incorporation are confused as shareholders and such is a mistake that must be corrected from the start. The subscribers normally transfer their right to acquire one or more shares of the company back to the company. The company later issues

all the shares and allocates them to one or more shareholders.

- (2) The shares are not issued following the correct procedures set forth in the Law. In this case, the board of directors must issue a resolution whereby it is agreed to issue the shares and proceed to their allocation.
- (3) Meetings of the shareholders are recorded on company public records without the existence of shareholders.
- (4) Absence of the corporate books (minutes, records and share registers).
- (5) Absence of letters of resignation from directors and officers.

Further to the above, it is very important to have the seller agree to warrant the following by means of a sworn declaration or by entering a clause within the promise to purchase agreement that would be only applicable to him, that:

- the company does not have any pending judicial proceedings;
- the company has not entered into any contract that would limit selling the property;
- the shares of the company have not been pledged;
- the seller is the legitimate owner of the shares where the shares have been issued to the bearer (it does not matter there is a legal presumption that whoever holds the bearer share owns them; it is comforting for clients to have such declaration);
- the share certificate (s) is/are the only one(s) in existence;
- the shares have been totally paid and liberated;
- the company does not have any debts or obligations of any nature;
- the sole asset of the company is the underlying property; and
- the company is in good standing.

Property

Whether the transaction involves the direct purchase of a property or like above, the purchase of the shares of the company that actually owns the property, it is of utmost importance to ascertain the following:

- (1) It is important to ascertain that the property does not have any liens or encumbrances.
- (2) That the property is actually on the location indicated on the maps and blueprints provided by both the seller and the records of the Cadastral Registry.
- (3) That the details about the property that are publicly recorded, such as measurements, surface and others correspond to those on maps and blueprints provided by the seller. These details must also match those recorded at the Cadastral Registry. Clients and many attorneys, overlook this part, however, we have seen many cases where a property physically appears not to have any problems, but when checking the data on maps at the Cadastral Registry against the data on a property survey

conducted on the property, we ascertain that the property overlaps to the property next door or it is either smaller or bigger, which most definitely affects the selling price of the property.

- (4) That the property itself is in good standing as it relates to taxes and utilities.

Taxes

When a property is sold in Panama it immediately triggers a tax called the property transfer tax, which is of two per cent and payable over the updated cadastral value of the property, which is no more than the value that the government has recorded. Such tax must be paid prior to closing and signing the final purchase agreement that will be afterwards recorded at the registry for the purpose of transferring the ownership.

With the amendments to our tax system in 2005, a new tax was created. This would be the capital gains tax which is of ten per cent calculated over the capital gains. This tax must also be paid prior to closing and signing the final purchase agreement.

The above taxes are payable by the seller.

The property must also be in good standing regarding the property taxes. If any are owed the government will not issue a certificate of good standing and the transfer will not be able to be recorded.

In the case of the sale of the shares the only tax that would be triggered would be the ten per cent income tax over the profits that result from the sale of stock of a company. In this case the buyer has the obligation to withhold five per cent of the selling price and report it to the government within the next ten days of the transaction. This five per cent is discounted from the price to be paid to the seller who can in turn discount it by way of a credit to the ten per cent tax mentioned above.

Once the above measures are finalised, everything should be in place to sign the final purchase agreement, however, it is important to ensure that the parties finally comply with the following:

Seller

- Submit the good standing certificate of the property.
- Submit the good standing certificate from the water service.
- Submit the good standing certificate from the homeowners association should it be a property subject to the horizontal property regime.
- Submit the good standing of the company should it be the case of the purchase of shares.
- Payment receipt of the two per cent transfer tax and the corresponding form.
- Payment of the ten per cent gains tax and the corresponding form.
- Should the owner of the property be a company then the seller must also submit a resolution of the board of shareholders of the company that authorises entering into the transaction and selling the asset.

Buyer

- Provide the necessary documents to identify him/her or the legal entity should it be a corporate buyer.
- Pay the price agreed with the seller following the parameters set forth on the promise to purchase and sale agreement.
- Should the buyer of the property be a company then the buyer must also submit a resolution of the board of shareholders of the company that authorises entering into the transaction and purchasing the asset.

By taking the above measures, one is ensuring that the transaction will reach a happy conclusion with a satisfied client who may return to your office for more advice and help in future transactions.

ROMANIA

Expedited expropriation procedures

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A recently published addendum to existing regulations on procedure preliminary to the construction of roads is mainly aimed at simplifying the dispute resolution procedures between the expropriator and the landowners and thus to accelerate the construction of roads of national, county and local interest.¹

Expropriation corridors will include the elements of public roads (eg the location and the corresponding land area, the bridges, the tunnels, the viaducts, level crossings and other works, the parking lots, the road vegetation, the security area) and will be established by the national or local authorities. All construction works for roads of national, regional or local interest are declared as being of public interest, thus allowing for the application of expropriation laws.

The documentation related to the execution of works of national, regional and local interest must include the final version of the feasibility study. Holders of the plots of land within the expropriation corridor, potentially affected by the works included in such feasibility studies, will be obliged to allow access to their property for topographic measurements, as well as for geotechnical studies or for any other type of operations required for the completion of a feasibility study.

After the approval given by the National Agency of Cadastre and Real Estate Publicity (in Romanian, *Agentia Nationala de Cadastru si Publicitate Imobiliara* (ANCPI)) for each expropriation file, ANCPI must

send a list of the plots of land located within the expropriation corridor to the local authorities. After transmitting this list to the local authorities the issuance of any notice, permit or authorisation regarding the plots of land that form the object for the expropriation will be forbidden.

Future disputes between the expropriator and the landlords will postpone the payment of compensatory damages, but will not suspend the transfer of the ownership right to the expropriator. The compensation will be paid based on a request in this respect to which the authenticated documents or an irrevocable decision of a court of law stating the amount of the compensation must be attached.

Legal documents concluded after:

- (1) the decision stating the amount of the compensation is communicated; or after
- (2) the payment date, are void, except for those that clarify the legal status of the plots of land.

Legal documents which change the legal status of the property affected by expropriation (eg zoning conversion of land property from agricultural area into buildable area or from the public domain into the private domain of the state), will also be void. Further, any notice, permit or authorisation issued to third parties as of the date ANCPPI has approved each file of expropriation in relation to the assets affected by expropriation will be void.

Note

- 1 Law no 184/2008 regarding amendments to Law no 198/2004 regarding preliminary measures to the construction roads of national, regional and local interest, published in the Official Gazette no 740 of 31 October 2008.

Restitution claims: legal certainty at any cost?

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On 10 December 2008, the Constitutional Court of Romania rejected the claims of certain Romanian deputies and senators regarding potential breach of Constitution by the amendments (Amendments) to Law No 10/2001 regarding the restitution of immovable assets taken over by the state between 6 March 1945 and 22 December 1989 (Law No 10/2001). Following the rejection of such claims, the president of Romania is expected to give the final approval to the Amendments which will soon be published in the Official Gazette.

The Amendments were adopted by the Chamber of Deputies on 24 June 2008 against the prior negative vote of the Senate and were expected to enter into force sooner, had a claim for failure to observe the Constitution not been filed in October 2008.

The Amendments' main purpose is to put an end to the uncertainty regarding the restitution of the immovable property confiscated by the Romanian State between 6 March 1945 and 22 December 1989. Parts of such property have been restituted to their former owners based on several restitution laws enacted after December 1989, others have been sold on the basis of Law No 112/1995 to the tenants then holding such property on leasehold from the state, while other parts are still owned by the state.

Former owners have sought restitution of their properties by various legal means, mainly consisting in procedures provided by restitution laws, but also by invoking provisions of the Romanian Civil Code. The parallel existence of two legal bases has been disputed for a long time in the Romanian jurisprudence and doctrine. In June 2008 the Supreme Court of Romania issued a guiding decision regarding the admissibility of the two parallel legal remedies. According to the guiding decision, the legal issue regarding the legal basis the former owners might invoke must be solved by granting priority to the principle according to which the special legal provisions derogate from the general legal provisions. Applied to restitution laws, this principle means that special restitution laws must be applied instead of the general provisions of the Romanian Civil Code.

However, the guiding decision of the Supreme Court also included reference according to which the special (restitution) laws must be interpreted in the light of the jurisprudence of the European Court of Human Rights. The decisions of the Romanian courts in litigation cases between former owners and tenants based on the provisions of the special restitution laws have been criticised in many cases by the European Court of Human Rights on the grounds that the former owners have been deprived of their ownership rights by giving effect to the bona fide of the tenants and without an effective compensation.

Considering the inconsistencies in the Romanian judicial practice, the Amendments have been adopted in an attempt to offer also a legal basis to the new trend the Supreme Court tried to impose, but also to deal with the criticism the European Court of Human Rights has often made of Romanian restitution laws.

According to the Amendments, the persons entitled to restitution may invoke only the provisions of Law No 10/2001. Such new provision will prohibit former owners whose properties were sold to tenants according to the provisions of Law No 112/1995 to claim ownership over such properties in litigation with such tenants. The prohibition will apply to litigations opened after the entry into force of the Amendments. However, considering the guiding decision of the Supreme Court of June 2008, the Amendments are

likely to impact also on pending litigation procedures. Because a large number of Romanian politicians and well-positioned persons were tenants and therefore, beneficiaries of Law No 112/1995, the Amendments are widely seen as providing legal certainty in the interest of certain categories of the society and against the principles of absolute ownership.

In terms of restitution principles, the Amendments provide that, as a rule, immovable property must be restituted to the former owners in kind. As an exception, former owners will be fully compensated with the value of their property evaluated according to internationally recognised standards. Compensation established according to the rule above will hopefully meet also the requirements set by the European Court of Human Rights for effective compensation. As a further exception to the restitution in kind, the Amendments explicitly state that immovable property legally sold by the state to the then occupying tenants based on the provisions of Law No 112/1995 must be exempted from the application of the principle.

The Amendments have not been published yet, but their entry into force may no longer be delayed, given the clearance by the Constitutional Court and the fact that the President of Romania has already exhausted all constitutional means of his office to request a revision of the Amendments by the Parliament.

RUSSIA

Unfinished project for sale!

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A real estate developer may face the need to withdraw from a construction project that is already in progress. This is an especially significant issue in view of the current market situation when many investors encounter difficulties during implementation of projects due to appreciation of credit funds, which will inevitably be raised at the stage of construction. Unfinished construction projects are put up for sale to mitigate losses and to raise monetary funds for other projects.

In this article we will describe two ways of withdrawing from a construction project:

- (1) sale of an unfinished construction as a real estate facility; or
- (2) sale of the company that is the client under the construction contract. An alternative is reorganisation of the company through consolidation or merger with the purchaser; however, this is a less popular option.

Sale of unfinished construction as a real estate facility

Pursuant to the legislation of the Russian Federation, a facility under construction is only the aggregate of construction materials and is not deemed a real estate until the ownership title is officially registered. Nevertheless, there are no requirements as to the degree of completion of a facility for being registered – a construction may be 90 per cent completed or only the foundation may be laid.

During registration of title to a facility under construction, the registering authority requires confirmation that the facility is not the subject of any effective construction contract. This is due to the fact that under Russian law the contractor is the owner of the facility prior to it being handed over to the client, and therefore the client needs to be the actual holder (possessor) of the facility in order to claim ownership title. Lately, adherence to this requirement has been less stringently enforced and the registering authorities are usually satisfied with a written notification submitted by a right holder instead of a signed agreement on termination of the construction contract. However, in practice the registering authority does not verify the actual state of a facility, and hence construction is not always ceased.

A facility under construction may exist as a real estate facility only provided registration of title thereto in the Unified State Register of Rights to Real Estate and Transactions Therewith. For registration a package of documents must be submitted to the local branch of the Federal Registration Service. Consideration of the documents is to be performed within 30 days, although in practice this may be much longer. In addition, the Federal Registration Service may suspend or refuse registration of title on formal grounds, and in this event the seller needs to correct the errors and resubmit the documents.

After registration is complete the owner may conclude a sale and purchase agreement in respect to the unfinished construction. The transfer process is complete when registration of transfer of title to a facility under construction takes place. Upon completion of the sale and purchase transaction a customer may enter into a new construction contract and continue construction.

The time frame of such sale and purchase transaction from termination of the construction contract until registration of the purchaser's ownership title may be from two-and-a-half to three months, provided it is carried out without any delays, though in practice this term can be substantially extended.

The transfer of ownership title or lease title to a land parcel under the facility under construction is performed during the sale of such facility. In the event the land parcel is provided for construction purposes, the new owner will need to reconclude the lease agreement in its own name. Also, such lease agreement may envisage approval by the landlord (the relevant authorised body) in order to register the facility under construction. In the event approval is not granted (for

instance, due to the tenant's breach of the terms and conditions of construction) the Federal Registration Service does not register the facility under construction and as a result it can be sold only as the aggregate of construction materials.

Pursuant to Russian tax legislation, sale and purchase transactions of real estate (save for land parcels) are subject to 18 per cent VAT that affects the facility's price and overall value for a potential buyer.

Sale of a company being the client under construction contract

This alternative is more logical when the construction project is implemented by a special purpose vehicle, which is rather common for major construction projects. This alternative has a number of advantages over the sale of a facility under construction as such, though it is still exposed to risks characteristic of this particular transaction form.

The process of disposal of a company generally starts with a potential purchaser's investigation of the corporate status of the company, in addition to the status of the construction facility and title to the land parcel. This is due to the fact that acquiring an operating company involves the purchase of associated liabilities and risks which require due assessment. In this regard, the results of such investigation may affect the structure, price, and the mere fact of whether the transaction will actually take place. In particular, in some cases relevant agreements may contain provisions under which the change of control over a company constitutes grounds for terminating or amending the conditions of such agreements.

Depending on the value of assets and scope of activities of the seller and/or purchaser of the shares in the company, the transaction may become subject to approval of the Federal Antitrust Service (FAS) in form of either a prior consent (to be issued by FAS within 30 days from submission of request) or a subsequent notification (following the signing of the sale and purchase agreement), whereas a sale transaction for a construction in progress is not subject to the consent of FAS in accordance with express provisions of the law.

Following the signing of a sale and purchase agreement for shares in the company in accordance with the procedure prescribed by law and the company's statutory documents, the new owner's ownership title is to be registered with:

- the Unified State Register of Legal Entities, maintained by the tax authority, in the event that such company is a limited liability company; or
- the Register of Shareholders, in the event that such company is a joint stock company. If the purchaser becomes the sole shareholder, amendments to the charter may need to be introduced and afterwards likewise registered with the Unified State Register of Legal Entities.

Amendments to the Unified State Register of Legal Entities must be introduced within five business

days, and the term for entering amendments into the Register of Shareholders is subject to the terms and conditions of the agreement with the registrar (amendments can be introduced on the same day). Following the successful registration, the purchaser becomes the owner of shares and thus of the company itself.

Thus, acquiring a company generally takes far less time than acquiring just the facility under construction. In the event of purchase of a company, it is not necessary to register either the title to the facility under construction – since the company remains a party to the effective construction contract, or the subsequent transfer of ownership title to the purchaser. Nor does this involve reregistration of title to land. In addition, transactions with shares are not subject to 18 per cent VAT.

An optimal scheme for transferring a construction project may not be uniform, as its development requires considering a number of factors and assessing risks in each individual case, as described above. Whatever the case, one thing is clear: transfer of construction projects in progress is indeed possible, and their acquisition may be quite beneficial for a purchaser capable of completing the project.

TURKS AND CAICOS ISLANDS

Of resorts and glue – a sticky legal problem: issues regarding enforcement of positive covenants in mixed-use resorts

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A five-star boom

The Turks and Caicos Islands (TCI) have experienced an enormous growth in luxury tourism development in recent years. As the territory has developed, the size and sophistication of resort development has increased significantly. The early days of pioneer stand-alone projects are rapidly disappearing as large scale mixed-use branded five star resorts become the norm. Recent developments include:

- Amanyara, the first Amanresort opened in the Caribbean, is located on TCI's commercial centre, Providenciales – main elements: hotel and villas.
- Work is progressing on the prestigious Dellis Cay project which will feature a Mandarin Oriental hotel

- main elements: hotel, condominiums, villas and over-water villas.
- A Ritz Carlton resort on West Caicos is near completion – main elements: hotel, condominiums and villas.
- Ambergris Cay, a large-scale private-island retreat, with its own jet-strip – main elements: villas and sporting club.

The early resort developments in TCI, primarily on Grace Bay beach on Providenciales, tended to be stand-alone condominium developments which benefited from TCI's flexible, modern and straightforward Strata Titles Ordinance which allowed for the vertical subdivision of real estate. In recent years, as projects have expanded in size, scope and sophistication, resorts have become more mixed-use, featuring hotels, condominiums, villas (standing on their own land parcel), and over-water villas. Several of the developments currently underway include a variety of other large scale amenities such as golf courses, marinas and beach clubs. The demands that this increased sophistication imposes on the resorts' TCI lawyers are significant, but hardly unique.

The 'legal glue' problem

A major concern of any sensible developer of expensive mixed-use resorts is the enforcement of ownership restrictive covenants, the legal glue that binds such developments together. When projects in TCI were stand-alone condominium resorts, there was little problem: the Strata Titles Ordinance provides an excellent legal framework for the governance of such developments. However once other components (such as villas) were introduced, matters became more complicated, due to a legal problem common in many common law jurisdictions in the English-speaking Caribbean and elsewhere.

At common law, only covenants which are negative in nature are said to 'run with the land' and bind successors in title to the original villa owner. For example, a covenant which obliges a villa owner to refrain from doing something is enforceable as a negative covenant, both against that villa owner and against any buyers from that villa owner (assuming that the covenant concerned is registered on title). However, positive covenants (an obligation to do something rather than to refrain from doing something) do not run with the land and, whether registered on title or not, do not bind the original villa-buyer's successors in title. This poses a major problem for large mixed-use developments where many covenants are positive (such as covenants to pay annual owners' association or club dues and covenants releasing the branded hotel operator from liability in relation to representations regarding return on investment or rental income, breach of US securities laws in that regard, and so on). If a buyer from the developer's original client can ignore positive covenants, the resort may come unstuck, as

enforcement of covenants against delinquent owners becomes spotty.

The TCI solution

In TCI, the problem has been resolved as follows:

- (1) By TCI law, all *condominium units* in a development must be the subject of a strata plan. The positive covenants can be laid out in those bylaws and will therefore bind both initial buyers and their successors in title under the Strata Titles Ordinance. Enforcement is by the relevant strata corporation (the homeowners' association for that condominium development).
- (2) In the case of *villas*, negative covenants set out in the duly-registered restrictive covenant affecting a villa owner's parcel will bind that villa owner and his successors in title will be similarly bound.
- (3) However, whilst positive covenants will bind the original purchaser from the developer (as a matter of contract), they will not bind that villa owner's successors in title unless additional steps are taken.
- (4) It is possible by means of a restriction¹ to impose a prohibition on disposal of the villa concerned without the consent of the applicable homeowners' association or HOA (which the developer will usually control). It will be specifically stated that such consent may be refused where the villa owner concerned is not compliant with the restrictive covenant and where the new buyer does not himself sign a restrictive covenant in identical terms with the developer or its successors (thereby imposing a new and enforceable contractual obligation on that new buyer).
- (5) Inherent in this arrangement is a requirement that villa owners must be members of the villa owners' HOA. The HOA will typically be a company limited by guarantee, the articles of association (bylaws) of which will require, amongst other matters, compliance with all the covenants, positive and negative. An owner who is not compliant will not be in good standing and the HOA will have no obligation to consent to a sale or disposal by him of his villa unless and until he cures his various defaults.
- (6) The articles of association of a company constitute a contract between each member and the company, and therefore that HOA will be empowered to enforce its bylaws (which will include the branding covenants) against its members.

In this way it is possible:

- (i) to preclude a transfer of any villa parcel to someone who is not approved by the HOA;
- (ii) to require each villa owner as a matter of contract arising out of the restrictive covenant to abide by all of the covenants, including positive ones;
- (iii) to oblige each purchaser from an existing villa owner to sign up to a new restrictive covenant in identical terms, thereby creating privity of contract between him and the developer/HOA in relation to positive covenants; and

- (iv) to require each villa lot owner, as a precondition of ownership, to be a member of the HOA, the bylaws of which will require compliance with all the covenants, including positive ones.

Note

- 1 It's important to distinguish between a restriction and a restrictive covenant. Restrictive covenants limit how an owner can use their villa. Restrictions limit how he can deal with their villa.

UKRAINE

Nota bene: amendments to land transactions in Ukraine

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The Ukrainian land law is undergoing significant changes due to the constant development of land transactions in Ukraine. In autumn 2008 one could observe an unprecedented number of amendments to the laws covering real estate issues in Ukraine.

The Law of Ukraine 'On Amendments to Certain Laws of Ukraine on Promoting Construction Activity' # 509-VI (the Law) came into force on 14 October 2008. This Law has been hailed by real estate specialists as a construction revolution in Ukraine.

The Law introduced amendments to the Land and Civil Codes of Ukraine, the Law 'On Land Lease' and a number of development and construction laws. In general, the Law is intended to secure the investments in the construction area and includes the amendments in order to simplify and shorten the construction procedures. The Law also introduced significant changes in the land transactions concerning the land auctions, more detailed procedure of land allocation and other issues intending to simplify the procedures in this area as well.

In particular, one of the innovations became the possibility of *disposal of land lease right*. Now, the right of land lease can be sold (including on land auctions), mortgaged and inherited. The owner of a land plot can also contribute the right of land lease to the capital of a company for the term of up to 50 years.

Certain changes were made in the Land Code of Ukraine with regard to such rights to land as '*superficies*' (the right to construct on the land plot owned by another person) and '*emphyteusis*' (the right to use the land plot owned by another person for agricultural purposes). From this moment, these rights to land of state and municipal ownership can be sold only by auctions. Previously, the Ukrainian law stipulated the obligatory auction procedure only for sale and lease of state and municipal land. As we see, one of the

main principles in land transactions in Ukraine is the competitive basis of state land purchase and use.

Thus, the Land Code now establishes the right of a person to alienate (sell, inherit, contribute to the charter capital of a legal entity) and to pledge the rights of lease, *superficies* and *emphyteusis* regarding land plots.

At the same time, the Law contains certain restrictions with regard to state and municipal land. The rights to land of state and municipal ownership (lease, *superficies* and *emphyteusis*) cannot be alienated by land users, mortgaged and contributed to the capital of a company.

With adoption of the new amendments to the Land Code, the Ukrainian legislator finally specified what types of land do not need auctions for the purchase or lease, namely:

- land occupied by buildings owned by individuals or legal entities without state shares, unless the owner of the building located on the land plot refuses to buy or to lease the respective land plot;
- land used for usage of natural resources and special water usage according to the special permits (licences);
- land used by religious organisations legalised in Ukraine for the location of religious buildings;
- land or buildings located on such land operated by state or municipal enterprises, institutions or organisations, or an enterprise or public organisation in the sphere of culture and the arts, including by national artistic unions;
- land used for location of diplomatic and similar representative offices of foreign states and international organisations in accordance with the international treaties of Ukraine;
- land used for construction and maintenance of line transportation or energy infrastructure (ie roads, railways, petroleum and water pipelines, power transmission lines, airports, petroleum terminals, power stations, etc);
- land used for the complex reconstruction of a residential quarters of an old residential fund in accordance with the law; and
- land used for construction of social and affordable housing in case there was a relevant construction tender.

The above-mentioned amendment saved the players of the real estate market from lots of confusion, as before that it was not clear what procedure had to be used for such categories of land.

The Law establishes general requirements for carrying out auctions of state land and the rights to state land purchase, defining in more detail the procedure of their purchase, and the procedure of plot preparation for auctions. In this respect it is necessary to note that the Law provides for payment in advance when buying state land that was not provided before. The rejection of an advance payment is one of the grounds for denial of land purchase.

In general, the Law presents a number of positive

innovations that will let the players of the land market avoid different deadlocks and conflicts caused by the earlier contradictions and discrepancies in Ukrainian legislation. With the adoption of this Law, the Ukrainian legislator has made a significant step towards making the procedures in construction and land transactions more transparent and increasing foreign investment into the Ukrainian market.

UNITED KINGDOM

Tenant's right of first refusal – up in the air!

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Part 1 of the Landlord and Tenant Act 1987 (the Act) enables tenants to have a right of first refusal at the time a landlord proposes to sell the reversion of its lease. The intention behind the legislation was to provide tenants with the opportunity to become their own landlord, in certain circumstances. The drafting of the 1987 Act was regarded as unclear and the Housing Act 1996 introduced amendments to the 1987 Act. The amendments strengthened the force of the Act providing that:

- Non-compliance by the landlord is a criminal offence; and
- the date of exchange of contracts is treated as the date of 'relevant disposal'.

In the main, there are four conditions which require to be satisfied, namely:

- (1) the premises must be one to which the 1987 Act applies;
- (2) the landlord must not be an 'exempt' landlord;
- (3) the tenant must be a 'qualifying' tenant; and
- (4) there must exist a proposed 'relevant disposal'.

Premises

The premises affected by the 1987 Act include the whole or part of a building if they contain (i) two or more flats held by qualifying tenants and (ii) the number of flats held by such tenants exceeds 50 per cent of the total number of flats in the whole of the premises. Where a building is a combination of flats and for example, shops, the 1987 Act will apply where the floor area of the flats exceeds the floor area of the shops.

Landlord

The landlord will be the person who is the tenant's

immediate landlord. If that landlord does not own freehold or the reversion of at least seven years, then the superior landlord is also regarded as a landlord for the purposes of the 1987 Act. Those landlords who are exempt include local authorities, housing corporations, certain housing associations and private sector residential landlords where the premises are their only or principal residence and have been for a period in excess of the 12 previous months.

Tenant

Any tenant qualifies under the 1987 Act unless his tenancy is:

- a protected short hold tenancy,
- a business tenancy under the 1954 Act,
- a tenancy terminable on cessation of employment; or
- an assured tenancy under the Housing Act 1988.

In the main therefore most qualifying tenants will be long leaseholders at low rents or where the tenancy is regulated.

Relevant disposal

A relevant disposal for the purposes of the Act will be a transfer of a freehold or leasehold reversion. The difficulty for landlords is that there is no actual definition of 'building' in the 1987 Act and accordingly the matter of what is included in a 'building' has been left to be determined by the courts.

Case law

The recent case of *Dartmouth Court Blackheath Limited v Beresworth Limited* [2008] EWHC 350 (Ch) is an example of a case where the lack of a definition of the building led to a dispute between, on the one part, a landlord who was disposing of part of his property to a developer and, on the other, the tenants of the flats which formed part of the landlord's property. In this case, the whole premises consisted of a block of 72 flats, a caretaker's office, common landscape, garages and an electricity sub-station. The disposal was first of all of the garages, the office space and the electricity sub-station and secondly, a grant of a long lease of the roof and air space above the building to the developer for the purposes of building additional flats.

In terms of the 1987 Act, when a landlord proposes to make a disposal, he is required to serve a notice on the tenants. The notice should set out the main terms of the offer of sale and the deadline and the procedure for acceptance. In this case the landlord had elected not to serve notices on the tenants since none of the flats themselves were being disposed of. The landlord was of the opinion that the disposals were not caught by the terms of the 1987 Act.

The courts decided that the first disposal, ie of the garages, office and electricity sub-station was not a relevant disposal in terms of the 1987 Act. Accordingly, in that instance the tenants were not entitled to be

given notice of their right of first refusal to purchase the landlord's reversion. However, in the case of the disposal of the roof and air space, the courts interpreted the definition of 'the building' to include the appurtenances of the building and not just the block of flats. The term 'appurtenances' could be said to include gardens, roadways, paths, etc but the court decided that the actual definition would be a matter to be interpreted the individual circumstances of each case. The landlord's argument was that the parts being leased to the developer were not in fact residential accommodation.

However, the courts clearly believed that it was the proper interpretation that appurtenances which were used by the occupiers of the residential flats must be included in the definition of the building. The question of the air space was further discussed and was regarded as also included on the basis that the occupiers of the building may require to enter the air space in order to comply with any obligations for roof maintenance, etc. In this case, the tenants ought to have been notified of their right of first refusal in relation to the lease and the landlord's failure to do this barred it from granting the lease to the developer. The tenants were to be entitled to that lease and accordingly, the development that was proposed did not proceed.

Conclusion

There are instances where a 'relevant disposal' in contravention of the 1987 Act may still proceed. In such cases the landlord will be liable for a criminal prosecution and possibly also in a civil action. However, the disposal once made remains valid. Good title passes on to the purchaser. It is important however to ascertain the position in the pre-contract enquiries for a purchaser in order to avoid the possibility of potential challenges to a transaction that may cause delay and affect the purchaser/developer's decision to proceed. Also, the purchaser/developer needs to be aware that if it acquires the property in contravention of the provisions of the 1987 Act, the qualifying tenants may have rights against the purchaser as successors in title. It may be the case that the qualifying tenants once they have had their opportunity to acquire the interest, choose not to. In such cases, the landlord is at liberty to sell the interest on to another party within a period of 12 months, subject to the deal being on the same terms and conditions that were offered to the qualifying tenants.

In an economic climate where development projects will be facing numerous difficulties, it is yet another hurdle that may be faced by developers. Where land is in short supply and margins are small, a developer will be less likely in many properties to be able to take advantage of the clever use of space (eg air space) in order to progress with property development.

The impact of the credit crunch on the UK property market

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How did it all start?

In the United States, lenders had become very lenient as to whom they lent money to in the lead-up to the credit crunch, as the current financial crisis has become known. Billions of dollars' worth of mortgages were extended to sub-prime borrowers who had insufficient income and assets to service the loan and/or poor credit ratings.

The reasoning behind these transactions was apparently that if borrowers defaulted on their mortgage repayments, then rising house prices would mean either that the borrower could remortgage the property or that the lender could repossess without the risk of negative equity, ie without the risk that the outstanding amount of the loan and associated charges may exceed the market value of the property. The problem was, however, that this would only work if interest rates continued to remain low and house prices continued to rise.

Therefore, as interest rates in the United States began to rise, house prices began to fall, and borrowers started to default on their mortgage payments.

How did this turn into a global crisis?

US banks sold the debt to investors, packaging sub-prime home loans into mortgage-backed securities known as CDOs (collateralised debt obligations). The loans were then sold to investment banks and hedge funds world-wide in the hope that they would generate high rates of return. However, when borrowers began to default on their obligations, the value of these investments plummeted, causing large scale losses for banks globally.

UK financial institutions had invested billions of pounds in such sub-prime backed investments and subsequently had to write off large losses as it became impossible to sell these investments. Distrust between banks as to the strength of their balance sheets and their credit worthiness as borrowers in the inter-bank market resulted in a credit crunch as banks became reluctant to lend to each other and commercial lending dried up.

How has the credit crunch affected the UK property market and house prices?

The down-turn in the property market caused by the sub-prime crisis and the economy now being in recession has affected not only the residential but also the commercial property market.

The most recent price index published by Nationwide (a leading mortgage lender) shows that the annual rate of fall in property prices had actually moderated in December 2008 to 15.9 per cent since January of 2008. Nevertheless, house prices have now fallen for 14 consecutive months. The cost of an average home in the UK has declined by approximately £30,000 since December of 2007 but still stands at some £17,500 higher than five years ago. It has been reported that the affluent south-east of England has been hit the hardest. Poor economic conditions and a weakening labour market are expected to continue to put pressure on the housing market, in particular, because property remains expensive relative to earnings. (House prices are at a record 5.8 times earnings, above the 20-year average of four times earnings, even after the recent price fall). Experts expect prices to drop by some further 15 per cent before the market stabilises.

Although there is a clear down-turn in the residential property market, there are also a number of significant differences between the current situation and the last property crash in the early 1990s:

- (1) mortgage payments as a percentage of earnings have increased recently but, at 24 per cent, they are still considerably lower than at their 35 per cent peak in 1989-1990 (when interest rates stood at 14 per cent);
- (2) although the Royal Institute of Chartered Surveyors (RICS) was predicting a 50 per cent increase in the number of repossessions to 45,000 for 2008, this too is a long way short of the 1991 level of 75,000; and
- (3) the current economy remains stronger: both unemployment and inflation are (for the time being) lower and more stable. In the early 1990s, inflation was running at around 10 per cent and unemployment rose rapidly from one million to three million.

One of the consequences of the credit crunch has been that banks are reluctant to lend to one another, making it more difficult for financial institutions to offer mortgage finance deals (both in terms of the availability and costs of funds). Where banks are still lending, they are charging higher interest rates to cover their perceived or actual risk.

While the Bank of England's Monetary Policy Committee has further reduced interest rates in December 2008 to an historic low, these rate cuts are not necessarily passed on to borrowers who are on their lender's standard variable rate although the government is increasing pressure on lenders to pass on rate cuts. (The reluctance of lenders to do so is at least in part due to the fact that LIBOR (the London Interbank Offered Rate) remains stubbornly higher

than official Bank of England interest rates). Borrowers on fixed rate deals will not be benefiting immediately from rate cuts although the estimated one-third of borrowers on tracker rates will benefit directly.

Some two million low-cost fixed rate mortgage deals were expected to have expired by the end of 2008. When this happens, many borrowers' monthly finance costs will increase and there will be fewer mortgage products available in the market place for mortgagees to choose from. Lending criteria are also being tightened, eg by reference to the ratio between the amount of the loan and the value of the property, and as to the amount of the loan as a multiple of earnings.

Although falling property prices should in principle be good news for first-time buyers, they are still finding it extremely difficult to get on the property ladder. They are now required to have saved up at least 25 per cent of the property value as deposit in order to obtain a mortgage for the remaining 75 per cent of the purchase price.

The squeeze on the availability of mortgages has meant that purchasers are often unable to fund the acquisition of properties. Frequently even agreed sales are not continuing to completion as lenders are revoking their lending decisions prior to completion.

Sellers in turn either have to withdraw their property from the market, or accept a much lower price, but at best properties are taking longer to sell. Indeed, as a result of current market conditions, it has been recommended that sellers should hold on to their properties unless it is absolutely necessary to sell. Not surprisingly, turnover rates in the housing market have fallen to historic lows and many estate agents are fearing for their survival.

Stamp duty land tax holiday

In order to support the housing market, the government in a somewhat symbolic gesture decided to suspend Stamp Duty Land Tax (SDLT), ie the tax payable on property acquisitions as a proportion of their value, for certain residential conveyancing transactions from 3 September 2008 for a period of one year.

Before the tax holiday was introduced, SDLT on properties worth between £125,000 and £250,000 was charged at one per cent, three per cent was payable on properties worth more than £250,000, and four per cent if worth more than £500,000.

Now, SDLT has been suspended for a year until 2 September 2009, on houses costing less than £175,000 (as opposed to the previous threshold of £125,000 at which one per cent stamp duty became payable) in order to revive the property market and encourage first-time buyers. This will save qualifying homebuyers £1,750.

How effective will this initiative be? First, it only applies to residential properties. Secondly, Nationwide has reported that the cost of an average home in December 2008 was £156,828 and that, based on

average house prices, the change will make a difference only in four regions of the UK. This does not include London and the outer metropolitan region: according to the Nationwide, the average property price in inner London is £257,963 and few London buyers will actually benefit from the tax relief. Other areas where buyers will not benefit from the relief because of high prices include East Anglia, the South West and the South East.

Despite the decision to limit the relief to properties costing less than £175,000, around half a million buyers are still expected to benefit at a cost of £600 million to the government.

The Council of Mortgage Lenders has commented that the overall level of transactions in 2008 was lower than 2007 and overall it is questionable whether the tax holiday will incentivise sufficient numbers of buyers who would not have entered the market anyway. The National Federation of Builders dismissed the government's package as being 'little more than a political sticking-plaster'. Finally, the tax relief does not address the root problem of the current crisis, namely, the collapse of the mortgage market.

Transaction chains

Most residential property transactions take place in a chain, ie home owners will not be able to complete on their purchase of a new property unless and until they can complete the sale of their existing home at the same time. The current market difficulties have made these property chains even more fragile than usual, and further contributed to the slow-down in the market, since the failure of a single transaction in a chain can lead to the collapse of a whole series of transactions. Today's sellers face a 50 per cent chance of deals falling through, due to the current uncertainty in the market, and until the fall in house prices slows down and the availability of mortgage finance improves, there will continue to be high levels of aborted sales.

Negative equity and repossessions

Two other problems, which increasing numbers of home owners face, are negative equity and repossessions by mortgage lenders following payment defaults.

Market experts expect that house prices will fall by up to 30 per cent from their peak levels in 2007 until 2010, compared to the early 1990s when house prices dropped only 20 per cent. 60,000 homeowners a month are apparently already plunging into negative equity as a result and some two million households are expected to enter into negative equity by 2010 if current trends continue. During the last property crash in the 1990s, 1.8 million households were affected. As a result, hundreds of thousands of people are unable to sell their properties because their home is worth less than the value of their mortgage.

Due to the economic down-turn and rising unemployment, defaults on mortgage payments are also on the increase. Standard & Poor's, the ratings agency, has said that banks are aggressively seizing homes whose owners have slipped just a few hundred pounds behind on their mortgage payments. Housing charities have given examples of a bank having launched repossession proceedings where a home owner owed just £800 in arrears, even though the property was estimated to be worth approximately £180,000 and contained about £40,000 of equity.

Indeed, repossessions have gone up by 12 per cent in the third quarter of 2008, bringing the total up to that point to 30,200. The Council of Mortgage Lenders expects a total of 45,000 properties to have been repossessed in 2008 (which would amount to a still very modest repossession rate of 0.38 per cent) but expects repossessions to reach 75,000 in 2009. With some 168,000 borrowers already behind with their repayments, the problem is likely to grow.

According to the Council of Mortgage Lenders, there are no industry guidelines for how deeply in arrears a mortgagee has to be for a home loan provider to be entitled to launch repossession proceedings. However, in response to government demands for a more sensible approach to repossessions, leading mortgage lenders recently agreed to delay repossession proceedings by six months and work with customers to find workable payment solutions before taking action.

New guidelines have also come into force for dealing with house repossession in court. The new rules say that borrowers and lenders should take all reasonable steps to discuss the cause of any arrears and how they might be sorted out before they bring a case to court. This could include making alternative arrangements, such as a full or partial repayment holiday, changing the type of mortgage, or extending the repayment term.

In addition, late last year, the government announced a new scheme to help people who suffer a temporary loss of income stay in their home. The new Homeowner Mortgage Support Scheme will enable households that experience a significant and temporary loss of income as a result of the economic downturn to defer a proportion of the interest payments on their mortgage for up to two years. The government will guarantee the deferred interests payments in return for banks' participation in the scheme. The country's eight largest banks have already pledged that they will work with the government to develop the scheme with a view to it being available to customers early this year.

Mortgage fraud

A further effect of the crisis in the property market appears to be the growing incidence of all forms of mortgage fraud. The Council of Mortgage Lenders has estimated that there could be as much as £17 billion worth of fraudulent loans on bank and building

society books, representing between 30,000 and 60,000 properties in the UK having been bought with fraudulent loans.

This ranges from employment, income, or appraisal fraud, where applicants for mortgages give wrong information as to their employment, income, or the value of their property, to obtain a loan, over attempts simultaneously to obtain multiple loans for the same property, to instances of identity theft, where property fraudsters assume the identity of a homeowner and then proceed to register a transfer of ownership of the property into a new name. The fraudsters will then obtain a new mortgage under the new name, and disappear with the money.

Commercial property

The full force of the credit crunch is now also being felt in the UK commercial property market, where investment levels in 2008 were expected to decline by 55 per cent year on year, and the market downturn currently underway coincides with the economy falling into recession. According to the RICS, large office and shopping centre transactions are particularly affected by the relative lack of available funding and investment. The principal problems appear to be that deals are taking longer to complete and, where external funding is required, the extra scrutiny put in place by the banks is adding further to the delay and uncertainty of transactions actually completing. Capital values continue to decline. However, at the same time increasing property yields are starting to provide an attraction for some investors.

Occupier demand continues to decline sharply, in particular, in the retail market, followed by offices and then industrials. At the same time, in the third quarter of 2008 the amount of floor space available for occupation increased at the fastest pace since 1999. Given the volume of available properties, the value of inducements offered by landlords to new tenants to secure a letting has increased further, and remains at a record high. The most negative rental outlook appears to affect the Central London office market where inducements are rising rapidly.

Landlords across most regions have generally lowered rental expectations. Rental expectations are lowest in the office sector, followed closely by the retail and then industrial market. Tenants are firmly in the driving seat and have greater bargaining power pushing lease lengths down at the fastest pace on record.

Another direct result of the credit crunch has been that a lot of businesses can no longer afford to pay rent at the prevailing levels and therefore have no choice but to vacate their premises.

With its confidence shaken and uncertainty over pricing impacting almost as much as the lack of affordable debt, the commercial market is expected to go through a troubled immediate future.

Conclusion

The property market in the UK has clearly been adversely affected by the credit crunch and the deteriorating economic climate. According to Nationwide, conditions remain highly volatile going into 2009 with no current signs of the economy and labour market, and therefore consumer sentiment, stabilising. Government stimulus measures, such as the SDLT relief, will assist first-time buyers of residential property in some regions although they will have no discernible positive effect in Greater London. Further interest rate reductions (if passed on to customers) may well have a more significant impact, but the availability of credit will remain an issue. The commercial property market will have to ride out the recession before any improvement is likely to filter through to the market. However, for commercial tenants the current market may hold incentives to upgrade their rental properties on very favourable terms. Also on the bright side, the recent revaluation of sterling against major currencies such as the dollar and euro, combined with falls in property values and increases in yields, are starting to make property investment in the UK a very attractive proposition for overseas investors.

URUGUAY

Real estate foreign investment in Uruguay

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Uruguay is recognised for its political and social stability, and for having solid democratic institutions. Uruguayan governments have historically supported the private investment with investment-friendly laws and policies.

The current international crisis – with restrictions to credit, decrease in prices of commodities, etc – will probably affect the Uruguayan economy, but will present interesting challenges and opportunities ('every crisis brings an opportunity').

The real estate sector, which is continuously expanding in Uruguay, is a good example of opportunities. Residential, commercial, office, rural, hospitality and infrastructure projects are growing very fast. And as we usually say, 'bricks' are always a safe investment option.

Investment regime

The Uruguayan Investment Law (Act No 16,906) ensures foreign investors the same treatment as for

Uruguayan ones, as well as free transfer of capital and profits in freely-exchangeable currency.

Additionally, the investment law and its amendments and regulations provide for two types of benefits:

(a) Automatic benefits are applied in general to Business Income Tax (RAE) taxpayers engaged in industrial (manufacturing and extracting) or in agriculture activities, without having to obtain a government pronouncement.

Regarding real estate, there is an IRAE exemption up to 20 per cent of the amount of the investment made during the year on income used in construction and expansion of hotels, motels and inns and construction and expansion of buildings for industrial activities.

The period for the benefit's computation extends over three years, ie that of the investment and the following two years.

(b) Non-automatic benefits that may be granted to companies or specific activities that are declared 'promoted activities' by the Executive Branch.

The Executive Branch is empowered to grant benefits to industrial, agricultural and certain commercial and service activities upon investment project approval.

The new regime establishes levels of investment and benefits.

The benefits include net worth tax exemptions, VAT reimbursement and business income tax exemptions (at least 51 per cent of the investment for three to 25 years depending on the projects level).

In the 'Big' and 'Great Economical Significance Projects', Business Income Tax exemption can reach 100 per cent of the investment for the maximum term of 25 years.

Another introduction is that the Executive Branch has a fixed term for the project's approval.

Real estate legal framework

Uruguay has a reliable property system, which protects the acquisition and disposition of property, with no discrimination whatsoever regarding the nationality or residence of the owner, except for the different tax regime applicable in each case.

There are no exchange controls presently in effect in Uruguay, nor legal obstacles to commercial or financial agreements being drawn up in foreign currency. Legal enforcement of contracts may be made either in local currency or in the foreign currency originally agreed upon by the parties.

The ownership of every real property is registered in the Property Public Registry –Real Estate Section - through the registration of the title deed. Each real property has a registration number and a map, which is also registered upon the Cadastre Office.

Main investment areas

The real estate investment in Uruguay is primarily concentrated in: Punta del Este and other seaside areas; rural land (for agricultural and forestry

investments); historic buildings (that are then refurbished); residential; hospitality; industrial or commercial developments; and infrastructure works.

Who may own real property in Uruguay?

Real estate acquisition or development may be:

(a) Direct, by:

(1) Local or foreign individuals, resident or not: As previously said, in Uruguay there is no discrimination whatsoever regarding the nationality or residence of the investor, and both local and foreign individuals can invest in real estate on an equal footing.

(2) Local and foreign legal entities: Local legal entities as much as foreign ones can acquire properties in Uruguay.

(b) Indirect, by acquiring the shareholding package of a company (domestic or foreign) owner of the property, or investing in a real estate trust.

The election between the different options depends on the investor, the kind of the investment, the tax efficiency of the vehicle chosen, and has to be analysed case by case.

Notwithstanding the above, an interesting and common way to acquire a property or develop a real estate project in Uruguay, is through a local corporation (*Sociedad Anónima*).

The main characteristics of Uruguayan corporations are:

- They can be incorporated in one single act by a group of founders or through public offer of shares. In order to avoid any delays, it is also possible to acquire off-the-shelf corporations that have carried on no activity whatsoever. These companies have broad corporate purposes and their by-laws and capital structure can be subsequently amended.
- Applicable Uruguayan regulations allow wholly-owned corporations comprised by a single shareholder.
- Capital stock can be represented by bearer, registered or book entry shares, of one class or more. Shares can be ordinary or preference.
- In the case of bearer shares, the anonymity of the shareholder is guaranteed. There are no public registries or corporate record books for shareholders registration. The transference of bearer shares is not levied by any tax.
- Shareholders meetings must be held in Uruguay at the place of the legal domicile of the corporation. Shareholders can be represented at shareholders' meetings by third parties through simple letters of attorney. Shareholders' meetings can be regular or special.
- The shareholders' liability is limited to the initial contributions. The company's creditors are not allowed to claim payment of debts from the company's shareholders. The company is a legal entity independent of its shareholders and with its own assets.

- Corporate administration is in charge of a board of directors formed by one or more directors or an administrator, individuals or legal persons. Directors can hold office for unlimited consecutive periods. There are no restrictions as to nationality or residence of the directors or to their capacity as shareholders.
- Companies can establish internal control systems by appointing a controller or a control board.
- Uruguayan corporations can operate in Uruguay or abroad. When the corporation's main purpose is to own assets in other companies, it is more suitable to adopt the structure of an investment corporation. These are local (not 'offshore') companies whose main, but not exclusive, purpose consists of investing in other entities' assets.
- In principle, investment corporations that maintain all their operations abroad are not subject to Business Income Tax. Although in some cases the General Revenue Service finds that they must pay on a notional amount.
- The board of directors, the corporation legal domicile and the eventual shareholders agreements must be informed to the National Trade Registry in order to be opposable to third parties.

Rural real estate ownership

The Rural Real Estate Ownership Law (Act No 18,092) establishes some limitations to rural real estate ownership, introducing a restrictive description of the subjects who can own rural real estate. In the case of companies owning rural real property, the Law determines that shares must be registered and the shareholders must be individuals.

However, the Executive Branch is empowered to authorise exceptions to that limitation in the following cases:

- (i) if the company proves that the number of shareholders or the company's nature turns impossible that the share capital only belongs to natural persons; or
- (ii) when the activities to be performed by the company are part of a project considered a priority for the productive development of the country.

According to our interpretation of the ruling regulations, the legal requirements do not prevent that a natural person trustee cannot be the shareholder of a Uruguayan corporation which owns rural property in Uruguay. The natural person (trustee) will stand as the owner of the shares of the corporation that owns the real estate and not the settler (beneficial owner). For that reason we understand that the implementation of a trust will not interfere with the compliance of the land tenancy regime. However, it must be taken into consideration that since these regulations have been recently passed there are no judicial decisions yet.

Tax aspects

The Uruguayan tax system follows the source criterion. As a result, only Uruguayan sourced income as well as property located within Uruguayan territory will be subject to taxation. Therefore, only incomes derived from activities performed, property located or rights used in Uruguay, regardless of the nationality, domicile or residence of the parties participating in the transactions and the place where the transaction agreements are subscribed, are subject to taxation in Uruguay.

In 2007, Uruguayan tax system has been subject to a substantial reform (Act No 18,083), but the source criterion was maintained.

Conclusion

Summing up, Uruguay has lots of opportunities to invest in real estate, and a safe and serious legal framework.

As shown here, we have tax efficient and flexible investment vehicles and real and easily obtainable investment benefits.

All this, turns Uruguay into a very good option when thinking of investing in real estate.