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## 7 ISSUES WHICH YOU HAVE TO BE AWARE OF BEFORE STARTING YOUR DEVELOPMENT IN POLAND

### 1. *Title to Land: Learn about differences between ownership or perpetual usufruct:*

In order to obtain a building permit, you obviously need a title to the land you develop. It does not have to be ownership. Tenancy is sufficient as well. Please note, however, that the maximum term for which you may enter into a tenancy is 30 years. After the lapse of that term, the tenancy for a specified term of 30 years turns into a tenancy for an unspecified term, which means it may be terminated subject to notice.

Very often, however – according to preferences of local authorities and the State Treasury – land in Poland is given into perpetual usufruct. It is a strong property right established on public land and is freely transferable. It is usually established for 99 years subject to the possibility of prolongation for a minimum 40 years and maximum further 99 years. Buildings developed on such land become the ownership of the perpetual usufructuary. The advantage of the perpetual usufruct versus ownership is that for establishment of the perpetual usufruct only a fee of 15-25% of the value of the land is charged and then 0.3-3% of the value annually instead of charging upfront 100% as in the case of ownership sale. The disadvantage is that you are bound by construction start and termination deadlines stipulated in the perpetual usufruct establishing agreement.

Naturally sale-and-lease back models are also available and often applied.

### 2. *Purchase Permits – Check if your real estate purchase requires an administrative permit of the Minister of Internal Affairs and Administration:*

The general rule is that acquisition of real estate (whether in the form of ownership title or perpetual usufruct title) in Poland by foreigners requires a permit. Similarly, a permit is required for a foreigner to purchase shares in a Polish company that owns real estate or holds it in perpetual usufruct in Poland (this does not apply to public listed companies). For that purpose, foreigners are defined as foreign citizens, foreign-seated legal persons and Polish-seated legal persons controlled by the former two.

There is, however, a general exception, which actually is so broad that it becomes a rule. This rule refers to companies established in Poland or any other EEA country (European Economic Area, i.e. EU plus Liechtenstein, Norway, Switzerland and Iceland). They do not need a permit to purchase real estate or shares in companies in Poland subject to few exceptions. It causes that in practice only investors from outside EEA who want to be owners of the property directly may need the permit.

Another broad exception is provided for closed-end investment funds or open-end investment funds. Their acquisitions do not need permits, either.

There are also some exceptions from those exceptions and there is a special liberated regime for individuals, but even when it comes to the very issuance, permits are usually granted but naturally it creates additional an cost and takes time. The permit procedure may take from 2 to 6 months in more complicated cases (even though the statutory maximum is 2 months). Once a permit is issued, it is valid for two years and an acquisition should take place within that time. Refusals are rare and may be challenged in the administrative courts.

### 3. *Zoning – Check formally what is the zoning destination of your plot and how it may be developed before you purchase it:*

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If there is a zoning plan, no zoning permit is needed to apply for a building permit. Anybody may then learn of the zoning designation of the plot by ordering an excerpt from the zoning plan.

However, in many major cities of Poland, including Warsaw, new zoning plans are still under preparation. Old ones expired in 2002 and 2003. That means that before issuing a building permit it is necessary to obtain a zoning permit. It is advisable to obtain such zoning permit before making a decision on purchasing a given plot in order to avoid surprises after the purchase.

When issuing a zoning permit the so-called “good neighborhood” rule is applied. It means that allowed zoning has to fit in functionally and proportionally with the development on neighboring plots. In other words, it means that there needs to be some development on neighboring plots, and the official issuing the zoning permit has considerable discretion in estimating what may finally be built. However, there are some legal regulations to limit somehow that discretion.

### 4. *Reprivatization Claims in Warsaw – Have them clarified before purchasing encumbered real estate:*

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In Warsaw, many plots may still be encumbered with so-called “Warsaw decree” reprivatisation motions. The history of the motions begins in 1945, when all plots in Warsaw were communalized. In consequence, ex-owners and their successors were granted 6 months to file a motion to regain their plots but only for perpetual usufruct - a specific right which in merit entails the use of the land for 99 years. The authorities were and are obliged to give such plots back in perpetual usufruct to the ex-owners or their successors in all cases where such usufruct is in compliance with a zoning plan. In other words, a refusal could be made only in cases of plots used or reserved for such public purposes that exclude private ownership. Many refusals were unlawful and are now being challenged with new motions.

That is why many of those motions are still pending and keep numerous plots belonging to the City of Warsaw or the State Treasury off the market. Some of these motions are not legitimate and may be ignored although they do create a potential risk of litigation. That is why if an investor chooses a plot which is subject to legitimate restitution motions but is too attractive to be ignored, then the investor should have the reprivatisation motion issue resolved before acquiring it or taking it into perpetual usufruct. There may be two basic models to achieve it. First, a three party agreement may be concluded whereby a claimant would waive its restitution motion, and the investor would pay it a compensation which would be applied against the purchase price to be paid to the public owner. Second, the investor could purchase the restitution rights arising out of the motions and then enforce them against the public owner and acquire the plot in perpetual usufruct on its behalf. It is a difficult procedure but authorities start to treat motions more and more seriously. Besides the added value to the public owner in the second model is that the restitution motion is satisfied and the plot may be finally developed – in addition a perpetual usufruct fee is payable.

Of course, sometimes there are difficult restitution cases. These usually concern lack of legitimate representation of the entitled party or missing inheritance procedures, which prevent prompt resolution of claims. If that is the case, there may be several options for the claimants and the investor to urge the authorities to proceed quickly, whether being enforced individually or jointly. Such solutions include: insurance of the title; buying out the restitution claims from those who are represented and if possible from a special guardian established for that purpose by a court; or annulling co-ownership of the restitution claim and afterwards dealing just with the one that has taken it over.

### 5. *Costs of Purchase and Taxes:*

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Contracts regarding transfer of title to real estate must be in the form of a deed prepared by a notary. The notary shall charge between 0.5% to 0.25% of the transaction value as his fee but not more than 6-times the average monthly salary in the national economy announced by the Chief Statistical Office (now the maximum fee is approximately 13.500 PLN). If the transfer is preceded by a preliminary agreement, notaries usually agree that the above fee should be divided into two – half for the preliminary agreement and half for the final one.

Acquisition of title to the real estate requires also entry of the new owner or perpetual usufructuary into the perpetual book. Such entry is now charged approximately 1.5% of the transaction value but soon shall be charged only 200 PLN due to a new law passed recently. This law generally reduces all court fees.

Apart from the above, acquisition of title to real estate as a general rule is also subject to VAT. It may be 7% or 22%. Sometimes it is exempt from VAT but then is subject to 2% civil law transaction tax. That is why from VAT point of view each case should be analyzed individually as Polish tax regulations are very casuistic perhaps similarly as all tax regulations in the world.

As for the future, there are two possible scenarios. As of 2008 VAT where 7% VAT is applicable now it shall be increased up to 22% or all basic tax rates (VAT, CIT and PIT) shall be established at 15%. Parliamentary elections will be in the autumn of 2005 and the outcome shall determine whether any serious tax reform shall take place and when.

Real estate tax for possessing a real estate is still charged on generally applicable rates that vary from community to community up to maximum of approximately 18 PLN per meter. Although it is contemplated to introduce a real estate tax based on the value of real estate, such solutions is not expected to be introduced soon.

When purchasing a real estate you may become liable for tax arrears of the seller. In order to avoid this you need to take a certificate from the tax office not earlier than 3 days before the transfer in which the tax office confirms that the seller does not have any tax arrears.

As far as other debts or encumbrance on the real estate are concerned, as a general rule, they are indicated in the perpetual book (one exception is the abovementioned "Warsaw decree" motions about which you need to learn with the local authorities or you are notified directly by claimants). Good faith of purchaser basing on the entries in perpetual book is protected in Polish law. It means that as a general rule a purchaser purchases such a title as is described in the perpetual book unless the purchaser knows or should know the title is encumbered somehow. If the purchaser knows or should know the title may be encumbered but cannot be sure of it and still wants to take a risk, an instrument called "insurance of title" is what may be the only solution actually helpful and giving pecuniary protection if the title turns finally to be encumbered somehow.

#### 6. *Building Permit – Get all necessary sub-permits before applying for the building permit:*

After you acquire a title to the real estate you may apply for the building permit.

Due to much blocking of investments by neighbors or environmental organizations the building permit procedure has been recently simplified.

Neighbors are also more carefully verified before being admitted as parties to proceedings.

Parties challenging building permits at the administrative courts and claiming upfront the withholding of such permits are required to establish a security for potential damages caused by such withholding. Otherwise, their withholding motions should be disregarded.

Environmental organizations have ceased to be parties to building permit procedures and instead are parties to procedures regarding environmental approval of an investment, which needs to be obtained before applying for a building permit.

All kinds of other sub-permits (road and traffic management, monument conservator etc.) are advisable to be obtained before applying for a building permit. Thus, within the building permit procedure you may concentrate only on architectural issues and in consequence limit the possibility of disputes with other parties at this final stage.

#### 7. *Agreements with Contractors – Address some controversial issues expressly:*

When all zoning and building permits are in place you may choose a general contractor. Polish law, however, has started giving contractors more and more protection, especially contractors for building works.

**Firstly**, there is a general rule applied statutorily that a contractor may always require establishment of a security for payment of its remuneration (e.g. bank guarantee or surety).

**Secondly**, an investor may statutorily become jointly and severally liable with its contractor for payment of remuneration to its subcontractors unless within 14 days from being provided with a copy of a draft agreement between the contractor and its subcontractor disagrees to such agreement.

Please also note that the maximum payment term is 30 days from the due date. Longer deadlines are ineffective and may only trigger higher interest (applicable to tax arrears instead of slightly lower interest usually applicable to civil law obligations).

There are some contractual ways to mitigate the above legal risks, but the risks are there and in general should be taken seriously by investors.

*We hope the above information on selected legal issues will be useful to you and wish you a successful investment.*