

Tips for success

Those keen to enter the attractive world of Romanian real estate should listen up, says Roxana Negutu of Voicu & Filipescu

Romania's real estate market continues its upward trend, fueled by foreign investment. Over the last years we have witnessed a continual growth in the real estate market. The increased consumer spending power, accession to the EU and favourable prospects for the future of the market are just some of the factors making Romania so attractive. Land prices have increased significantly, although remaining competitive for the region.

Some foreign investors are sophisticated enough to understand all of the prerequisites involved in the acquisition and development of land throughout the world; however, the rapid expansion of the market, as well as the presence of speculators, has raised concerns. In a period in which real estate investors worldwide are carefully analysing the opportunities, Romania remains attractive because of anticipated infrastructure developments, the difference between supply and demand and the expectation of new projects. Knowing and understanding the regulatory requirements and practices, as well as the risks to which a real estate investor is exposed, are the way to success.

The buyer

Non-Romanian citizens and/or legal entities are still subject to the prohibition to acquire land in Romania in their own name. Law 312/2005 (regarding the right of foreign citizens and stateless individuals, as well as that of foreign legal entities, to obtain

private ownership of land) extended foreign citizens' rights following Romania's accession to the EU. However, the prohibition against acquiring land in Romania will continue to exist in practice for five years after Romania's accession to the EU. This will extend to land in built-up areas of the cities, on which construction may take place, and for seven years following the accession date for agricultural land and forest. Foreign investors who establish a Romanian legal entity may avoid this impediment because a Romanian corporation – even with 100% foreign ownership – is still Romanian and, as such, may own lands in Romania. Practically speaking, the investor establishes an SPV. Usually, the targeted real estate is acquired by a limited liability company before being sold to an investor. This type of transaction is preferred by participants in the Romanian real estate market, especially for reasons of fiscal efficiency. However, it must be borne in mind that land acquisitions by Romanian entities must meet the purposes for which the Romanian company was established.

The above-mentioned restriction on foreign land ownership only refers to the acquisition of land. As far as buildings and other structures are concerned, foreign individuals and legal entities may acquire title over them, as well as the right to use the land on which they are located, for the duration of the structure's existence.

Sale-purchase is the most common method for the transfer of real estate ownership rights. For the transfer of

ownership to be valid, Romanian legislation requires the notarisation of the land ownership agreement, irrespective of the location. This form is drawn up by a notary public and, in the absence of proper authentication, the act is null and void. In the case of transferring the ownership right over buildings and/or other constructions, the authentic form is not required. However, in practice, parties prefer to authenticate their agreement.

The transfer of the ownership right over private property is regulated by the principle of free circulation. However, exceptions from this rule exist, based on certain specific requirements. Some of the most common prohibitions refer to the Romanian State's pre-emption right to acquire historical monuments and the temporary 10-year prohibition against transferring the agricultural lands which were given to their owners based on the provisions of Law 18/1991, where the period was calculated from the beginning of the year following the year when the ownership was registered.

Registrations

In Romania, real estate is subject to various registrations by the cadastral authorities, fiscal authorities and the Real Estate Registry. The cadastre system is a unitary and mandatory system of technical, economic and legal record of all estates on the national territory performed on the basis of specific measurements, executed by authorised topographic experts in order to determine the accurate surface of the land, the neighbours and legal regime (agricultural/constructible, located outside or inside the city limits), as well as to grant a sole identification number.

Law 7/1996 regarding the cadastre and real estate publicity implemented the uniform system of registration at a national level. The Real Estate Registry serves to register, in the land books, the legal deeds and facts related to a certain property. To this end, a land book allows third parties to verify the following information regarding the property: description (the surface, cadastral number, purpose, category of use and any buildings located thereon), location, the name of the owner and the deed on which the ownership right was acquired, the existence or the absence of encumbrances, as well as other rights subject to registration, such as the right to use the land, the lease agreements concluded for a period exceeding three years, the right of way and servitude rights registered in favour of neighboring plots of land and the existence of litigation in

“The rapid expansion of the market, as well as the presence of speculators, has raised concerns”

relation to the property. Note that registration with the Real Estate Registry does not create an ownership right but is only a presumption that the beneficiary of the registered rights actually enjoys such rights. The draft of the new Civil Code provides for the possibility of giving the registration with the Real Estate Registry constitutive ownership effects. However, until the enactment of this draft, registration with the Real Estate Registry serves the purpose of ensuring opposability towards third parties. Also, the priority of some rights over others is established on the basis of their registration date, as the rights registered first obtain priority over subsequent ones. In the case of mortgages, the registration date provides for the rank of each mortgage, and in the case of various creditors with different ranks, those having priority are the first to obtain the restitution of the receivables.

Notaries public, who authenticate the ownership transfer, are obliged to request the registration, with the Real Estate Registry, of the rights over the plots of land established under deeds authenticated by such notaries, immediately after such authentication.

The fiscal registration is performed for the purpose of allowing the collection of local tax on real estate, the buyers of real estate being obliged to perform the registration within 30 days following the moment of acquisition, subject to payment of fines.

Steps and structures for transfer

There are certain steps that are regularly followed in the process of acquiring real estates in Romania. The performance of a legal and technical due diligence report with respect to the real estate is the most important stage. This implies a full evaluation of the legal risks implied by the acquisition of a real estate, as well as for determining its value. Simply speaking, this evaluation includes an assessment of the ownership title of the seller, as well as the ownership history, inquiries with the public sources (such as the Real Estate Registry and the municipalities) to identify the applicable urban planning regime with the competent courts and/or applicable land book in order to determine whether the real estate is subject to any litigation or restitution claims, researches seeking to determine whether the real estate is on a list of historical monuments or may be an archeological site, and so on.

As environmental issues are of increasing interest, specific attention should be paid to environmental due diligence. Technical

Author biographies



Roxana Negutu

Voicu & Filipescu

Roxana Negutu became a partner in Voicu & Filipescu on January 1 2008 and coordinates the firm's real estate department. She has extensive experience in all aspects of commercial real estate, including property acquisition, planning and development, construction, project finance, complex lease agreements and assistance on project exit. Roxana has been actively involved in some of the largest transactions performed on the Romanian market, advising commercial, industrial,

financial, institutional and individual clients. She also covers corporate and M&A, including various aspects of business law, particularly in transaction structuring, acquisition-related matters, project management (with expertise in financing) and complex due diligence processes.

Before joining Voicu & Filipescu, Roxana specialised in commercial law, corporate restructuring, real estate and secured lending. She graduated from the Nicolae Titulescu Law School in 2000, attended the Master of Law and Economy of the European Union at Padova University, Italy in 2001 and has been a member of the Bucharest Bar Association since 2000.

Aside from her native Romanian, she is fluent in English, Spanish and has a good knowledge of Italian.

Roxana is the author of various articles published in international and Romanian magazines and has been a speaker at numerous conferences.

due diligence regularly involves various surveys, such as utilities networks, pipes and infrastructure, depending on the intended use of the properties, as well as to determine the parameters for construction on the land. More specifically, the certificate of urbanism attesting to the possibilities of development and the analysis of the general urbanism plan and/or the zoning plan, if applicable, must be assessed. The contemplated information mainly refers to the land's use category, the purpose of the same, the construction restrictions (land occupancy percentage, land use coefficient, maximum admitted height of constructions on the land, and so on). This kind of details allows the investor to decide the possibility of developing the project within the technical parameters offered by the real estate and, respectively, upon the proceedings that should be carried out in the event that such parameters do not correspond to the plans of the project. Frequently, in the case of the development of retail real estate, investors ask the competent authorities to approve a new Area Zoning Plan which corresponds to the purpose of the real estate project and to the technical parameters set out for the construction of the same. Special attention should also be paid to green areas, as changing the purpose of lands laid out as green areas and/or provided for as such in the zoning documentation, or reducing or relocating the same, are prohibited, and the deeds under which such an action would be performed are deemed absolutely null. The

technical analysis may also extend to aspects related to the real estate's infrastructure, public services, and so on.

As it may be time-consuming to determine all of the aforementioned aspects (considering the rather slow input from the Romanian authorities regarding certain required information), it is frequently upon a first analysis of the available documents (which may be more or less thorough) that the parties negotiate and agree upon the execution of a preliminary agreement representing the general framework for the performance of any subsequent operations. This is a practical instrument that allows the buyer time to evaluate the risks of the investment while prohibiting the seller from transferring the real estate to third parties. The object of such an agreement is the promise regarding the sale-purchase of the real estate, in exchange for a down payment that should preferably be deposited in an escrow account and is registered in the Real Estate Registry together with the prohibition from selling for a determined period of time. It is common that this type of agreement provides for certain precedent conditions to be fulfilled in view of the execution of the final sale purchase agreement, the most common being the satisfactory results of the due diligence. This time period may also be used for allowing the investor to find financing for the acquisition of the real estate, as the case may be. Note that a promise to sell does not transfer the title, but only creates an obligation for the seller

to execute a sale purchase agreement in the future. In case the seller changes his/her mind and refuses to execute the sale purchase agreement, the buyer may request the competent courts to issue a ruling that will have the same value, subject to full payment of the agreed price.

Upon fulfillment of the conditions precedent and assessment of the ownership title, the sale purchase agreement may be executed. There are certain formalities to be observed and mandatory documents to be obtained. The excerpt for authentication purposes from the Real Estate Registry regarding the real estate to be sold is one of these formalities, this document being requested by the notary a few days before the execution of the sale-purchase agreement. The fiscal certificate of the real estate attesting that there are no debts to the local budget and corporate approvals for the transfer from both the seller and the buyer, as the case may be, as well as Trade Registry excerpts attesting to the status of the company, are also necessary. The ownership transfer operates from the moment the sale purchase agreement is executed, save for cases in which the parties agree to delay such moment.

Following or even during acquisition, project financing and, consequently, the securities that may be requested by the financing banks, represent the next issue. Mortgages are the most common and will be established and registered in the Real Estate Register. The mortgage over any improvements to the initial mortgaged asset should also be registered with the Electronic Archive for Security Interests. It is worth mentioning that even though the creation of the mortgage under Romanian law does not imply the interdiction to transfer the ownership title, a special interdiction prohibiting the right to transfer, lease, further encumber or otherwise dispose of the mortgaged real estate is often registered. Also note that in Romania a mortgage cannot be established over future assets, save for mortgages established as security for mortgage loans, in accordance with special provisions. Consequently, the existing real estate, together with the other warranties, should give sufficient comfort to the financing bank.

Restitution

A specific issue to be carefully considered by investors in real estate is represented by the claims of the former owners with regard to real estates abusively nationalised during the communist regime and currently under restitution process. Even 19 years after the

“Knowing and understanding the regulatory requirements and practices, as well as the risks to which a real estate investor is exposed, are the way to success”

fall of communism, the restitution process is far from being finalized, even though various enactments have been issued since 1991. The most important legislations are Law 18/1991 regarding the land law, as further amended, and Law 10/2001 regarding the status of real estates abusively nationalised by the state between 1945 and 1989. The restitution legislation provides for the right of the previous owner to reestablish ownership right on the former location, provided that this request is filed within the deadline provided for by the legislation. However, most of the real estates requested for restitution tend either to be in attractive locations, represent a part of sites transferred to state-owned companies that were subsequently privatised or assets already sold to individuals by the state. In this context, real estate developers should carefully assess the ownership history of their potential investments. Also, note that despite the existence of the special legislation which allows the former owners to request in-kind restitution due to significant delays in the process or to the exceptions included in the law (which only permit pecuniary compensation in certain cases), there have also been requests made in court by former owners, based on the general principles of the Romanian Civil Code, which allows any person who claims entitlement to a property to initiate legal action against the current owner. For all of these reasons, it is necessary to conduct a detailed due diligence investigation on the background of the ownership over the property.

Taxation

Real estate transactions are subject to certain taxes:

- (i) Transaction fees. Transfer of ownership of real estates is subject to notary fees and fees for registration with the Real Estate Registry. Both fees are determined as a percentage of the value of the transaction. As a rule, both fees are paid by the buyer, but the parties are free to make different arrangements.
- (ii) VAT. In all cases in which the seller is

VAT registered, the transfer of the real estate is subject to the payment of VAT amounting to 19% of the transfer value. It is the responsibility of the buyer to pay VAT when acquiring real estate properties (both constructions and land). If the buyer is also VAT registered, it shall obtain the reimbursement of the VAT, pursuant to a control carried out by the competent tax authority.

(iii) Income resulting from real estates. The transfer of ownership right is subject to income tax, which is paid by the seller as follows: (i) 16% of the profit for legal entities, (ii) 2.5% of the income for 2008 for micro enterprises; and (iii) for individuals, it is a tax that ranges between L4,000 (\$1,800) + 1% of whatever exceeds a certain threshold, or L6,000 +2%, depending on whether the real estate was held in ownership for more or less than three years.

Past, present and future

In order to successfully enter the Romanian real estate market and to adjust one's expectations to the realities of the Romanian business environment, one must carefully examine the real estates through legal and technical due diligence processes. Over the last few years, the Romanian real estate market has offered foreign and local investors a background that is extremely favourable to the development of successful businesses in the field. The real estate projects initiated over this period targeted residential or retail units and registered substantial profits for their promoters. In 2006, the launch of a new project on the Romanian market was announced on a weekly basis. The annals record 2007 as a year for the completion and delivery of previously initiated projects, which presented equal opportunities for the entry of new investors on the real estate market and for new projects across the country. We expect 2008 to be a year of consolidation and development, the first semester of the year seeing continuous interest from investors in the Romanian market.

**VOICU
FILIPESCU**
in association with
Squire, Sanders & Dempsey LLP

Union International Center II, 5th Floor
26–28 Stirbei Voda Street, 1st District,
010113 Bucharest, Romania
Tel: +40 21 314-02-00
Fax: +40 21 314-02-90
www.vf.ro

**Property is the safest
way to welfare.
Make it safe by knowing its rules!**

Commercial, industrial, residential, offices legal advise on real estate • Secured lending and workouts • Purchase, sale, mortgage and servitude of all types of properties • Examination of title and issuance of title legal opinions • Land use and zoning • Real estate partnerships and joint ventures • Construction contracts • Structuring and negotiation of complex construction loans • Lease transactions, including ground lease, office leases, warehouse leases and retail shopping center.