

COMMERCIAL REAL ESTATE

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1. LEASING

1.1 Practical points

(a) Securing the premises

A contracting party may secure premises prior to actually occupying them, pursuant to a pre-contract agreement or a final agreement where the parties specify the date of the subsequent occupation. It is advisable to stipulate a monetary penalty, should the landlord violate the provisions relating to the handover of the premises.

(b) Taxes and fees payable

The taking over of possession of a real property, or agreeing to occupy a real property pursuant to a lease agreement, does not create any state or local tax payment obligation in itself.

(c) Fitting-out works

The tenant needs to obtain the owner's approval to carry out works on the real property. Depending on the nature and the extent of the fitting-out works, owners usually require a detailed technical description of the contemplated works prior to their approval.

(d) Codes of practice

Apart from applicable legal regulations, there are no generally accepted guidelines or codes governing the relationship of the parties. Contracts are negotiated on a case-by-case basis. However, significant shopping centres, office buildings and industrial parks all use standard agreements.

1.2 Key commercial terms

(a) Rent

Rent is usually paid on a monthly basis in HUF or in EUR. Rental levels depend on the function, place, size and condition of the real property.

(b) Rent adjustments

Rents defined in HUF are generally increased in accordance with the indexes of the Hungarian Central Statistical Office; rents in euro are often increased in accordance with the Eurostat Harmonised Indices of Consumer Prices (HICP). Decrease of rent regulated in a lease agreement is theoretically possible; however in practice it is virtually non-existent.

(c) Other occupational costs

Upon the execution of a rental agreement, landlords usually require the occupier to pay a security deposit equalling two or three months' rent.

(d) Period of occupation

Leases may be made for defined or undefined periods. Leases for defined periods are generally made for 1, 2, 3, 5 or 10 years; it is extremely rare to make a lease for more than 15 years.

(e) Remaining in occupation

Occupiers have no legally regulated automatic right to a new lease agreement; however, it is possible to agree contractually that an occupier can renew the lease for a certain period with the same conditions, or has a right of first refusal in respect of a new agreement.

(f) Disposing of the premises

A lease for an undefined period can be terminated at any time. A lease for a defined period runs until its term expires, however, and cannot be terminated by the parties unilaterally, unless the other party seriously violates the agreement or a certain, predefined event occurs. This means that the occupier has to keep the premises until the expiration of the defined term. The occupier can only allow third parties to occupy the premises or can only sublet the premises with the prior approval of the owner.

(g) Alterations

Occupiers are usually allowed to make internal alterations to the building, while external modifications are rare. Generally any and all alterations require the prior approval of the owner; however, the owner may not request payment for the approval itself.

(h) Repair of the premises

According to statutory provisions, the landlord is responsible for the maintenance of the building, the continuous operability of the central equipment of the building, and for the repair of faults and defects in the common areas and their equipment. Other costs relating to the building and the common areas are governed by the agreement of the parties. With respect to the leased premises, unless otherwise agreed, maintenance works are performed by the tenant; while changing and replacement works are carried out by the landlord. Unless otherwise agreed, all alterations must be removed from the premises and apart from the wear stemming from normal use; the occupier has to reinstate the original state of the premises upon handing it back to the landlord. The occupier generally has to carry out all repairs made necessary by activity in the premises beyond the scope of normal use, or use agreed by the owner.

2. INVESTMENT

2.1 Practical points

(a) Exclusivity

In order to ensure the exclusivity of an investor in respect of the ownership of a real property or to secure a real property generally, it is necessary to: (i) have a written contract meeting the formal legal requirements for the sale of the real property or to establish certain rights for the investor over the real property; and (ii) register the agreement with the competent land registry office. Once the proper agreement is filed with the land registry office, third parties are considered to know about the right or claim of the investor in respect of the real property, and can only acquire rights in respect of the real property after the investor.

(b) Restrictions on disposing of property

As a general rule, real properties are freely transferable. The most notable exceptions are as follows. No non-natural entities or non-EU natural persons may acquire agricultural land in Hungary. The acquisition of other properties by non-EU natural or legal entities is subject to the approval of the regional government office, which may deny its approval if the acquisition of the real estate harms local municipal interests or if there is no reciprocity with the acquirer's home country. Legal entities registered in EU member states or natural persons that are citizens of EU member states are not subject to approval. Real estates under environmental, architectural or other similar protection are generally subject to the pre-emption right of the state or of the local municipality. Every co-proprietor of a property in undivided common ownership has a statutory pre-emption right relating to the other portions of the property.

(c) Impacts on timing

In order to transfer a title to real estate, it is necessary to have: (i) a sale contract or other legal title; and (ii) the registration of the transfer of title with the land registry office. This procedure usually requires 30-60 days. The registration of the title with the land registry office is a necessary element of the transfer of the title. The registration has a constitutive effect; it not only declares the title, but also creates the title. Should the investor want to obtain a loan to purchase the target real property, negotiation with the banks is a relatively time-consuming exercise.

(d) Key milestones in acquisition process

The first stage of any acquisition process is the conduct of the proper due diligence procedure in respect of the real property. This means checking the ownership structure, the potential encumbrances of the real property in the land registry office and, if needed, the various agreements relating to the transfer of ownership and establishing rights or encumbrances on the real property. The circumstances might also require the review of the related zoning and construction regulations with the local construction authority.

In the case of direct investment, the most common acquisition structure involves a sale and purchase contract with deferred payment, whereby the buyer pays a first instalment upon the execution of the contract, and the sale of the real estate to the buyer, with the retention of the seller's title until the full payment of the purchase price is registered in the land registry. The registration of the sale of the property to the buyer with the

retention of the seller's title indicates that the property has already been sold but the seller keeps its title until the full purchase price has been paid by the buyer, and the buyer only acquires the title following the payment of the purchase price.

In order to subsequently register the seller's title, the buyer must give a separate declaration of consent. This is commonly placed in escrow upon the execution of the contract. The remaining purchase price is usually paid in one or more instalments, after, for example, the clearing of the real estate from encumbrances, a satisfactory due diligence or obtaining financing, etc. Upon the payment of the full purchase price, the seller consents to the registration of the buyer's title or this declaration is released from the escrow and filed with the land registry. The buyer acquires title to the real estate upon the registration by the land registry.

(e) Requirement for transfer of monies

The buyer usually transfers a 10-20% advance payment or 'earnest money' upon the execution of the sale contract, while the remainder is usually paid upon the handing over of the real property to the buyer and the issuance of the ownership transfer declaration by the seller. The transferred money is credited on the seller's account on the day of the transfer or the on the day following the handing over of the transfer instruction to the bank, at the latest.

(f) Execution procedure

All agreements relating to real properties need to be in writing. Agreements relating to transfer of ownership or establishing rights over a real property have to be prepared and countersigned by a Hungarian attorney at law or a notary public. The agreements therefore need to be signed before the given attorney at law or notary public. If such execution is not possible, the signing must take place in the Hungarian consulate or embassy of the given country, or potentially before a notary public of the given country. Depending on the country, in addition to the certificate of the local notary public an apostille may be required, in accordance with the Hague Convention. In order to purchase a real property in Hungary, all companies must be able to prove their existence and that the person signing on behalf of the company is an authorised signatory of the given company by presenting official certificates issued by the court, chamber or registrar of companies keeping the corporate register in the given country.

(g) Other procedural requirements

In order to transfer a title to real estate, it is necessary to file the sale and purchase agreement with the land registry office in order to register the transfer of title in the land registry. Simultaneously with the filing of the sale contract with the land registry, a declaration to the tax office is also filed by the buyer, and the land registry office takes care of forwarding it to the tax office.

(h) Taxes and fees payable

In the case of purchase of a real property, the buyer has to pay a duty fee amounting to 4% of the market value of the purchased real property, with a maximum of HUF 200,000,000 (approx. €645,000). The municipalities may impose taxes on buildings or plots in their localities. The maximum rate of this tax is approximately 900 HUF (about €2.90) per usable m², or 3% of the market price of the given real property. Generally transactions involving real estate are not subject to value added tax; thus, the sale of real estate is not subject to VAT except for real estate that: (i) contains a superstructure, but

has not been put into ordinary use for the first time; (ii) contains a superstructure and has already been put into ordinary use for the first time, but less than two years has passed since the relating occupational permit became final; (iii) is an undeveloped construction plot; or (iv) is owned by a company subject to VAT which, prior to the sale, registered its real estate business to be subject to VAT with the tax office.

2.2 Key commercial terms

(a) Deposit

A security deposit or earnest money is usually paid by the buyer or the tenant simultaneously with the execution of the sale or rental agreements. In case of rents, the amount of the deposit is usually equal to two or three months' rent, while in case of sales it is usually equal to 10-20% of the purchase price.

(b) Timing

The usual timetable for a real estate transaction depends heavily on the type of target real property, the financing requirements of the deal, and the potential encumbrances on the real property. Depending on these circumstances, the preliminary due diligence may last one day or one month, while contract negotiations may last from a couple of days to a couple of months. The payment of the full purchase price, the taking over of the property, and the registration of the buyer's ownership in the land registry usually happen within 2-3 months following the execution of a sale contract; however, this might also require much more time depending on the terms and conditions of the deal.

(c) Employees

The acquisition of a real property in itself usually does not affect the current owner's employees. Under normal circumstances the current owner has to vacate the sold real property and the employees remain employed by the current owner, at another site. However, the purchaser might become the legal successor of the current owner in respect of the labour relationship with the employees working on the purchased site, if it is considered that the investor not only purchased the given real property, but also the line of business of the current owner. In this latter case, the purchaser will become the employer of the previous owner's employees by literally replacing the previous owner in the existing labour contracts. Whether a sale agreement functions as a simple real estate deal or simultaneously as a transfer of business line naturally depends on the terms and conditions of the deal.

(d) Warranties for construction of building

The obligatory warranty period is five years under Hungarian law in the case of buildings. This warranty period is provided by the Civil Code and the parties do not need to agree on it. If the contracting parties are business organisations, the parties may deviate from this period by mutual consent. On the other hand, the parties potentially need to agree on a guarantee period if both parties are business organisations. (There are obligatory guarantee periods for B2C agreements and construction of apartment buildings, but not for construction of commercial-industrial buildings.) The difference between the warranty and the guarantee is mainly the burden of proof. In the case of a warranty, the builder needs to prove that the contractor's performance was faulty in order to be indemnified, while in case of a guarantee, the contractor needs to prove that the fault was caused by an event occurring after the handing over of the building to the builder, and that the contractor performed properly. Should an investor purchase a real property

under construction, the obligatory warranty will be transferred to the new owner; however, whether the guarantee provided by the constructor is transferred or not depends on the contractual arrangement of the parties.

(e) Transfer of other tax or financial benefits

Generally, tax or other payment obligations or financial benefits are not transferred with the real property, as these obligations or benefits are usually linked to the owner and not the real property itself. There are exceptions, however, when certain encumbrances (mortgages, environmental issues, easement rights, call options, pre-emption rights, debt enforcement rights, etc.) are registered in the land registry and can be seen on the registration extract of the real property. In case of such registrations, the beneficiary of these rights can enforce the underlying claim against the all-time owner of the real property irrespective of any changes in the ownership of the real property. The other most notable exception is the obligation of the owner to clean its real property from environmental pollution, where the current owner cannot escape liability by simply showing that the pollution happened prior to the taking over of the real property.

3. DEVELOPMENT

3.1 Practical points

(a) Land ownership and assembly

Land registry offices keep a land registry on the relevant legal (title, encumbrances, etc.) and factual (location, address, etc.) information relating to the real properties. The registration of the title with the land registry office is a necessary element of the transfer of the title. The registration has a constitutive effect; it not only declares the title, but also creates the title. On the basis of property rights registered in the land registry, it is presumed that such registered property rights exist. Such rights registered for the benefit of a good faith acquirer are – unless proven otherwise by the opposing party – presumed to be true, even if they deviate from the actual legal status.

In addition, a person acquiring a right in a property by payment of consideration, and who is also trusting in the land registry, is always considered as a party acting in good faith. This means that under general circumstances, the investor can trust in the information obtained from the land registry office upon checking the identity of the owners of certain real properties. Private investors cannot force the sale of real properties unless the state or the local municipality acquires the property through expropriation, which requires full, immediate and unconditional compensation. This can only happen when construction of public utilities and/or public roads are required for the operation of the given investment outside the target real property, and these public utilities and/or roads will eventually be handed over to the state or the local government.

(b) Land transfer

A developer does not need to buy the target real properties one by one immediately, as there are several structures that can ensure that the developer can only buy the target real properties when the whole area is secured or other conditions (for example, amendment of zoning plan, reclassification of the real property or obtaining of construction permit, etc.) are fulfilled. The developer may sign a pre-contract agreement with the sellers, but as such pre-contract agreement cannot be filed with the land registry office, it is not the safest of solutions. The investor might also establish call option rights on the target real properties, and exercise the call option only when all the required

conditions are fulfilled. The call option can be registered in the land registry; therefore it is a much safer solution than the pre-contract agreement.

The investor might also sign final sale-and-purchase agreements with the sellers, stipulating that the purchase price would only be paid (thus the real properties acquired by the investor) upon the fulfilment of certain conditions. Although the sellers do not transfer the ownership of their real properties in these agreements until they receive the full purchase price, nonetheless the agreement can be filed with the land registry, and the fact of the sale and purchase with the retention of the seller's ownership title can be indicated on the registration extract of the given real properties, providing the safest possible solution for investors in case of realisation of long-term projects.

(c) Taxes and fees payable

The acquirer of the real estate must pay a duty fee. The rate of the duty fee depends on (i) the type and (ii) the value of the real estate, as well as (iii) the type of the acquisition. The general duty fee rate for the acquisition of real estate for consideration is 4% of the market value of the property up to HUF 1bn (roughly €3,225,000), and 2% of the market values above the 1bn threshold. The maximum amount of the payable duty fee is HUF 200m (roughly €645,000) per real estate. The market value is defined as the value of the unencumbered real property, reduced by the amounts set forth in the relevant legal rules if there are encumbrances on the real estate.

Among the various exceptions from the above general rules, note that a preferential 2% duty fee is applicable for acquisition for the purpose of real estate trading by professional real estate trading companies if the real property is subsequently resold within two years. Note also that no duty fee is payable if any entity acquires ownership of a plot suitable for the construction of a residential house and builds a residential house on such property within four years following the date of the acquisition.

Generally transactions involving real estate are not subject to value-added tax, thus, the sale of a property is not subject to VAT except for properties that: (i) contain a superstructure, but have not been put into ordinary use for the first time; or (ii) contain a superstructure and have already been put into ordinary use for the first time, but less than two years has passed since the relating occupational permit became final; or (iii) are undeveloped construction plots. In such cases, the VAT rate is 27%. It is important to note that a company dealing with real estate might declare to the tax office that it wants to apply VAT on the lease fee of its real estate and/or on the purchase price of its sold real estate, even if the transaction would otherwise be exempt from VAT. In case of such VAT declaration, the previously paid VAT may be deducted to the extent that the real estate is used for the sale or services subject to VAT, even if the given transaction would not have been subject to VAT without the company's VAT declaration.

Although currently there is no general state real estate tax, the municipalities may impose taxes on buildings or plots in their localities. The maximum rate of this tax is approximately 900 HUF (about €2.90) per usable m², or 3% of the market price. If a municipal tax is applicable, it is applicable to both foreign corporate or private investors as well.

If an investor has income from a Hungarian real estate, personal income tax must be paid subject to the rules of the applicable treaty for the avoidance of double taxation. Generally, such treaties require that taxes on the income from real estate in Hungary be paid in Hungary. The current rate of personal income tax for rental income is 15%. If a corporate investor has income from Hungarian real estate, corporate tax must be paid

subject to the rules of the applicable treaty for the avoidance of double taxation. Generally, such treaties require that taxes on corporate income from real estate in Hungary be paid in Hungary. The general rate of corporate tax is 10% on a tax base of up to HUF 500m (roughly €1.6m), and 19% above a HUF 500m tax base.

3.2 Key commercial terms

(a) Price

The price of real estate heavily depends on the type, location, condition, and the development potential of the target real property. Generally prices of real properties have suffered serious losses during and following the 2008 global economic crisis, but from the beginning of 2014 the prices started to climb back. The market is showing clear signs of recovery, and the price level generally reached the heights of 2008. Sellers naturally tend to value their real estate higher than its actual market value but, depending on the circumstances, generally 5-10% discounts can be reached, or in certain cases reductions even up to 15% can be bargained.

(b) Payment structure

In most cases the purchase of a real property is executed through a sale-and-purchase contract with deferred payment, whereby the buyer pays a first instalment equalling 10-20% of the purchase price upon the execution of the contract. The remaining purchase price is usually paid in one or more instalments, after, for example, the clearing of the real estate from encumbrances, a satisfactory due diligence or obtaining financing, etc. The remainder or the last instalment is usually paid upon the handing over of the real property to the buyer and the issuance of the ownership transfer declaration by the seller.

(c) Deal structures

In the case of direct investment, the most common acquisition structure involves a sale-and-purchase contract with deferred payment, whereby the buyer pays a first instalment upon the execution of the contract, and the sale of the real estate to the buyer with the retention of the seller's title until the full payment of the purchase price is registered in the land registry. The first instalment may be considered a simple advance payment or earnest money. Earnest money is a sum given upon the entering into a contract in order to show the commitment of the buyer. If the transaction later fails because of the buyer's fault, the seller may keep the earnest money. If the transaction later fails because of the seller's fault, double the amount of the earnest money must be returned to the buyer.

With respect to the sale of real estate, it must always be taken into consideration that the title to the real estate is only transferred upon the registration of the transfer of the title with the land registry office. The registration of the sale of the property to the buyer with the retention of the seller's title only indicates that a sale and purchase agreement has been signed in respect of the property, but the seller keeps its ownership title until the full purchase price has been paid by the buyer, and the buyer only acquires the title following the payment of the purchase price, which can take place theoretically even years after the execution of the sale contract under this structure. This registration does not give ownership title; it is only an indication to third parties that a sale contract has already been made to the property, therefore certain risks are involved, as creditors of the seller can enforce their claim by way of court execution procedure against the real property in question. However, the parties may avoid this risk if they immediately

request the registration of the ownership of the real property to the buyer from the land registry office, but ask the land registry office to suspend such registration until payment of the full purchase price. The only pitfall of this method is that the maximum period of the suspension is six months; therefore this structure can only be applied if the full purchase price is paid within six months following the execution of the sale contract.

In order to subsequently register the seller's title, the buyer must give a separate declaration of consent. This is commonly placed in escrow upon the execution of the contract. The remaining purchase price is usually paid in one or more instalments after, for example, the clearing of the real estate from encumbrances, a satisfactory due diligence or obtaining financing, etc. Upon the payment of the full purchase price, the seller consents to the registration of the buyer's title or this declaration is released from the escrow and filed with the land registry. The buyer acquires title to the real estate upon the registration by the land registry.

In the case of a share deal, the buyer acquires the target company as of the date of the contract, but the new shareholder/member must be registered with the court of registration as well. The two most important differences are the tax treatment and the liability aspects of the transaction. In the case of a share deal, the title to the real estate is not transferred, thus no duty fees (generally 4% of the market value) are paid, which may be a significant cost. However, in case of the transfer of real estate holding companies (at least 75% of the value of its assets is comprised of real properties) the 4% duty fee has to be paid, albeit with certain exceptions. Further, the acquisition of the real estate company may expose the investor to liabilities that are not relevant when buying a bare property.

(d) Taxes and fees payable

The acquirer of the real estate must pay a duty fee. The rate of the duty fee depends on the (i) type and (ii) the value of the real estate, as well as (iii) the type of the acquisition. The general duty fee rate for the acquisition of real estate for consideration is 4% of the market value of the property up to HUF 1bn (roughly €3,225,000), and 2% of the market values above the 1bn threshold. The maximum amount of the payable duty fee is HUF 200m (roughly €645,000) per real estate.

4. FINANCING

4.1 Practical points

(a) Level of loan

Commercial banks do not usually provide loans over 75% of the market value of a commercial real property.

(b) Security

The most commonly used securities by the bank are the various types of mortgages. These mortgages can be registered on the target real property and also on other movable or immovable assets of the debtor. Banks may also require third persons to provide guarantees for the repayment of the loan.

(c) Lender due diligence

The extent of the due diligence carried out by the lenders depends on the type of the target real property. Lenders check the general legal status of the target real estate and

also the development and profit-generating potential. Usually the investors are required to prepare a detailed business plan to be judged by the banks prior to receiving the required loan.

(d) Enforcement

Lenders can request enforcement upon any serious violation of the financing agreements by the debtor, including the violation of the repayment deadlines, serious loss in the value of securities, using the loan or the target real property for different purposes than agreed, etc. The lenders have to turn to court before they can enforce their claim, however in certain cases, when the loan facilities are incorporated in notarial deeds, the lenders may directly initiate enforcement without prior litigation before the court.

4.2 Key commercial terms

(a) Length of loan

The usual length of loans is around ten years in case of real estate financing, but occasionally loans up to 20 or 25 years are also provided.

(b) Interest rate and payment dates

The base interest rate of the National Bank is at its all-time lowest level at 0.90%. Currently there are several favourable loan constructions available, where the National Bank sponsors the financing of the commercial banks. The interest rates are also often linked to the EURIBOR, LIBOR or, in case of HUF loans, to the BUBOR rates. The general interest rate is quite low at the moment and it is possible to obtain loans even in HUF at around a 5-6% rate. Interest is usually paid monthly together with the repayment of the instalments of the principal. Sometimes the first several months or even the first year of a loan can be secured as a grace period, when no interest is payable to the bank.

(c) Repayment

The loans are usually repaid in equal monthly instalments, where the debtor pays interest and the tranches of the principal simultaneously. The lenders may terminate loan agreements with immediate effect upon any serious violation of the financing agreements by the debtor, including the violation of the repayment deadlines, serious loss in the value of securities, using the loan or the target real property for different purposes, than agreed, etc. In these cases the repayment of the whole principal and the accrued interests become due immediately.

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