

UKRAINIAN REAL ESTATE LAW

Part two of this series of two articles focuses on the purchase, ownership and leasing of land under the recently adopted Land Code, the leasing of premises, zoning and the enforcement of rights.

• New Land Code

The new Land Code, which was recently adopted and which will come into effect on 1 January 2002 (the "Land Code"), represents a fundamental change to Ukrainian real estate law. It introduces new rights to private land ownership and land use, as well as the principle that land can be freely bought and sold. Previously, although private land ownership is permitted under the Ukrainian Constitution of 1996, it was subject to further implementation "as may be provided by the law", and the existing law was very restrictive. Under the previous Land Code of 1992 (the "1992 Land Code"), only Ukrainian individuals were entitled to own land, and only in limited circumstances, such as for rural homes, garages, farms and gardens.

The Land Code greatly expands the list of permitted land purchases. It allows land intended for non-agricultural use to be purchased by Ukrainian and, in certain cases, foreign individuals and legal entities. However, for these fundamental changes to be implemented and applied in practice, a number of supplemental legal acts will have to be adopted on such issues as land valuation, the creation of the proposed Register of Land Plots and land surveys.

The Land Code establishes transitional periods (moratoriums) before certain land transactions can take effect. To begin with, prior to 1 January 2005, land plots that are owned by legal entities or individuals for agricultural purposes cannot be sold or otherwise disposed of except by exchange or inheritance. The reference to the "exchange" of land plots is ambiguous, and might provide a way around some restrictions depending upon the imple-

menting legislation. Presumably "exchange" means in exchange for other land plots, though the Land Code fails to specify this.

Only starting from 1 January 2005, may agricultural land be used as a contribution to the charter fund of a company. Until 1 January 2010, acquisitions of land for agricultural use are limited to 100 hectares. However, even upon completion of these transitional periods, the rights of land owners may still be limited. For example, under the Land Code, land may only be mortgaged to secure bank loans, and land plots may only be contributed to the charter funds of those companies that are exclusively founded by Ukrainian individuals or entities (although apparently these Ukrainian entities can be owned by foreigners). In addition, the Land Code expressly provides that further limitations of land ownership rights may be provided by subsequent legislation.

• Ownership of Land

(a) Owners of Land

The new Land Code provides that the following persons may be owners of land in Ukraine: (1) the State, which exercises this right through the Cabinet of Ministers of Ukraine, the Cabinet of Ministers of the Republic of Crimea, and the relevant oblast, Kyiv and Sevastopol city state administrations with respect to land in State ownership, (2) municipalities, which exercise this right through local Councils (local self-governing bodies) with respect to land in cities and villages and (3) individuals and legal entities, with respect to land in private ownership.

In accordance with the Land Code, municipal land may be allocated to a private person on the basis of an appropriate decision of a local Council. In Kyiv, such authority was granted to the Kyiv City Council. Land owned by the State may be allocated on the basis of a decision of the local State administration where the land plot is located.

(b) Prior Presidential Decrees

Prior to the adoption of the Land

Code, with a view to encouraging entrepreneurship, a number of Decrees were issued by the President of Ukraine to allow privatisation of land by individuals and legal entities, such as the Decree of the President, No. 608/95, "On the Privatisation and Leasing of Non-Agricultural Land Plots for the Purpose of Entrepreneurial Activity" of 12 July 1995 (the "1995 Decree") and Decree of the President, No. 32/99, "On the Sale of Land Plots of Non-Agricultural Designation" of 19 January 1999 (the "1999 Decree"). These Decrees remain effective, and are likely to continue, until the new implementing legislation for the Land Code is adopted.

The 1995 Decree provided for the privatisation of land by means of sale to Ukrainian individuals and legal entities for the purpose of carrying out entrepreneurial activity. However, the validity of the 1995 Decree has been questioned by numerous commentators because it contradicted the then applicable 1992 Land Code, which should have prevailed.

We are aware that, nonetheless, in the past a number of land sales were conducted on the basis of the 1995 Decree and were later registered. Probably these transfers are invalid and cannot be the basis for a further transfer of good title. Apparently in recognition of this, the 1995 Decree was never implemented as would be expected.

The 1999 Decree also provided for the sale of land owned by State and municipal authorities to Ukrainian individuals (including, in particular, those registered as entrepreneurs) and legal entities. This right to purchase land only arose under the 1999 Decree for land plots underlying buildings, constructions or unfinished constructions. Undeveloped "greenfield" sites cannot be sold or otherwise privatised under this 1999 Decree.

The 1999 Decree created a right for a privately owned Ukrainian legal entity to purchase the land underneath an unfinished construction only if the unfinished construction was on a non-agricultural site and such unfinished construction had been previously privatised or purchased by it. The 1999

Decree should have applied to Ukrainian entities that were, in whole or in part, foreign owned, as no distinction was made in the 1999 Decree between Ukrainian companies that are Ukrainian, rather than foreign, controlled.

Initially, as was the case for the 1995 Decree, the 1999 Decree was not fully implemented in practice. Possibly this reflected some early doubts expressed as to its constitutionality. Most commentators now appear to accept that it was validly adopted (an issue that turns on whether the 1999 Decree lawfully filled in "gaps" in legislation, or instead improperly addressed matters governed by the 1992 Land Code). As a consequence, a number of acts and resolutions of local Councils have recently been adopted to clarify the procedures for the sale of land pursuant to the 1999 Decree. For example, the Kyiv City Council has confirmed that land plots and unfinished construction sites may be sold to appropriate real property owners, including those Ukrainian entities which own the structure above the land plot or site.

(c) The Procedure for Purchases under the New Land Code

Under the new Land Code, most of the land within residential city areas and land intended for industrial use can be sold, except for land for streets, parks, beaches (some of which may be leased), cemeteries, other city areas that are in public use, railways, highways, pipelines, and the Chernobyl zone affected by radiation.

In cases where the land underneath a building was previously allocated for temporary or permanent use to a Ukrainian entity (including if foreign owned or controlled), the procedure for the entity to obtain ownership over such land plots is now rather simple. In order to obtain such land ownership an application must be submitted to a local Council or local State Administration, as appropriate, together with the current State Act for permanent use of the land plot or a land lease agreement (certifying the temporary right of use) with the local Council or State Administration, a plan of the land plot, an expert valuation of the land plot and a copy of Certificate of State Registration of the applicant.

The local Council is supposed to review the application within a one month period. The only permitted reasons for the refusal of such a land allocation, as expressly listed in the Land

Code, are: (1) the absence of any documents required for the allocation of the land plot; (2) the discovery of false data in the documents that are submitted, and (3) the initiation of bankruptcy or liquidation proceedings against the applicant. This should leave no discretion for a Council to refuse to act.

If a company wishes to purchase a land plot which was not allocated previously for its permanent or temporary use, it should submit additional documents to constitute a "project of land allocation". In this case, the process of land allocation by the local Council or State Administration may take a relatively longer time, because several State agencies are involved in drafting and providing consents on the project of land allocation.

For example, the local Department on Land Resources, the State Agency on Architecture, the local Sanitation-Epidemic Station, the State Department of Environmental Safety, and the Department on the Protection of Historical Heritage must all issue required permissions. Several land surveying agencies must also prepare project estimates and allocate the borders of the land plots. Each of these agencies is allotted from 20 to 30 calendar days to consider the application and accompanying documents and, therefore, the whole process could take up to four months. Each State inspection body named above requires the payment of certain fees for the issuance of the necessary documents.

An agreement on a purchase of the land plot must also be concluded between the company and local Council or State Administration, as appropriate, and it must be notarised. Land purchasers have to pay for the land, unless they qualify for so-called "unpaid privatization" (which applies only to Ukrainian individuals). Payment to the local Council for a land plot may be made in instalments. Following execution of the land purchase agreement and payment of the purchase price, the land purchaser should be given a State act of ownership of the land to confirm ownership of the purchased land plot.

The land underneath a residential building (including under any adjoining constructions and territory that is considered an integral part of it) will initially be allocated to the organization that administers the building (such as Zhek). However, if the building's ownership is privatised by a condominium (as discussed in part one of this series of two articles), the apartment

owners who form the condominium association can also privatise for free, or obtain use rights over, the land plot underneath.

As discussed above, until the new procedures for implementation of the Land Code are established, presumably the existing procedures for the sale of land that were established by the Cabinet of Ministers Resolution No. 440, of 24 March 1999, pursuant to the 1999 Decree (described above), will continue to apply.

(d) Purchases by Non-Residents

Under the new Land Code, foreign individuals and companies are now able to purchase land plots underneath buildings and other constructions that they own, whether located in city areas or outside a city. In addition, they can purchase land plots for construction within city areas. The basis for obtaining ownership rights to such land plots are: (1) private land purchase agreements (or certain other types of agreements) which are subject to notarisation and should contain the specified mandatory clauses on the size of the land plot, amount of payment, purpose of use of the land plot, etc; (2) inheritance; or (3) purchase of the land plot from a local Council or local State Administration.

Non-residents are still not allowed to own land intended for agricultural use. However, the procedure for changing the intended use of land has been simplified by the Land Code as compared to the similar provisions contained in the 1992 Land Code. Thus, the authority to decide on the intended use of a particular land plot is now reallocated from the Ukrainian Parliament to the local Councils and State Administrations, which can decide on a change of intended use of a particular land plot when taking a decision on its allocation to a foreign person. The new Land Code provides that a procedure for making such a change in intended land use will be established by the Cabinet of Ministers.

However, in order to purchase land underneath real estate property, non-residents will have to register a branch office in Ukraine that will carry out business activity in Ukraine (a taxable "permanent establishment"). A foreign person or entity that wishes to purchase a land plot that was previously leased to it would have to submit an application to the relevant state administration or Council, as the case may be, with copies of the land lease agreement and the certificate of State regis-

tration of the branch office, and a confirmation that such office is "operational" (the Land Code fails to state which documents should confirm that). In addition, the local Council or State Administration may only consider such an application if it has the approval of the Cabinet of Ministers, which apparently must be given for each transaction (as required by Article 129, sections 2, 5 and 6 of the Land Code). As a practical matter, this may greatly increase the time required for non-residents to purchase land (and will possibly effectively prevent many transactions).

(e) Land Auctions

The new Land Code has introduced public land auctions, among its new tools for land allocation. Land plots that are not privatized or sold in accordance with the procedures discussed above may be sold through such public land auctions. These auctions are expected to be held mainly to facilitate new construction.

In order to take part in such land auctions, potential purchasers should pay a registration fee and guarantee payment of certain minimum amounts based on criteria that will be established in the future. The land auction can be initiated by the local Council or State Administration or by the State Enforcement Service to implement a court order. If the land for sale belongs to the State or a municipality, the local State Administration or local Council should prepare all the required documentation for the land allocation, in particular to determine the borders of the land plot and prepare its so-called "technical passport". Information on a land auction with a detailed description of the land plot that is to be sold is required to be published in a local newspaper not later than 30 days prior to such auction, and a billboard with this information must be placed on the land plot. The land auction will only be valid if there is more than one potential purchaser and the proposed bids exceed the initially stated minimum bidding price.

• Leasing of Land

In addition to ownership of land (as discussed above) the new Land Code provides, as a second basis for use of a particular land plot, the leasing of land. (The Land Code also continues to permit permanent land use rights for lands

to be granted to State or municipal entities by local Councils and local State Administrations for any purposes (in the old Code, there were also temporary use rights, but these have been abolished.) In addition to the Land Code, land leasing is regulated by the Law of Ukraine on Land Leasing of 6 October 1998, Ns 161-XIV (the "Lease Law"), which is expected to be amended as part of the implementation of the Land Code.

Under the Land Code, land can be leased from the State or a municipality as well as from private owners. Foreigners may lease land on the same basis as Ukrainians. The 1992 Land Code limited leases granted by individuals to a term of three years, which contradicted the relevant provisions of the Lease Law on terms of lease. This limitation has been eliminated in the new Land Code.

There are now short-term and long-term leases. A short-term lease may run for up to 5 years. A long-term lease may run for up to 50 years less one day, and arguably may be prolonged (including by an agreement at the outset on a right of renewal). The Law provides that the current lessee has a priority right to prolong a land lease, but only if it matches all other terms proposed by others, such as the rent that is offered.

To be valid, leases of land must contain terms on a number of matters, such as (1) the location and borders of the land plot, (2) the duration of the lease, (3) the lease rent (amount, indexation, and payment procedure), (4) the purpose and conditions for the use of the land plot, and maintenance of the quality of the land, (5) conditions for returning the land plot to the lessor, and (6) possible limitations and burdens on the use of the land, and (7) the responsibilities of the parties under the lease. The lease contract must be executed before a public notary in the jurisdiction where the land plot is located.

Thus, if a Ukrainian or foreign entity would like to execute a lease agreement for the use of land under a building (or other construction) that it owns, the following steps must be taken in order to properly document such land lease, based on the example of an application in the city of Kiev for a lease of municipal land: (1) submission of a letter to the head of the Kyiv City Council with a request for conclusion of a lease agreement for the land underneath the building (for any peri-

od up to 50 years less one day); (2) obtaining a resolution from the Kyiv City Council confirming its agreement to allocate the land plot, which resolution should order the applicant to make a further application to the local Department on Land Resources of the Kyiv City State Administration within one month; (3) filing an application to this Department on Land Resources, with the following documents: (a) a notarized copy of the purchase agreement as proof of title to the building, (b) copies of the building's registrations with the BTI and the Kyiv City State Administration, if applicable, and (c) any other required technical information; and (4) upon receipt of a favourable response from the Department on Land Resources, entering into a lease agreement with the local Council for up to 50 years less one day for the land underneath the property.

The applicant may, if needed for reconstruction of the acquired property, request that an adjacent land plot be temporarily granted to it for such construction (for example, to site a crane or other equipment, for storage, etc.). Such leases of adjacent land can only be granted on a short term basis of up to five years.

If the land is leased from a local Council, then the lease would probably be based on the standard form of land lease agreement that was adopted by the Resolution of the Cabinet of Ministers on 17 March 1993, N°. 197. In principle, local authorities presently are usually reluctant to include any additional clauses into or otherwise modify this form of lease agreement.

After the lease agreement is executed and notarised, it should be registered with the relevant department on Land Resources of the State Administration. In Kyiv, such registration is carried out by the Department on Land Resources of the Kyiv City State Administration in accordance with the Regulation of the Cabinet of Ministers of Ukraine of 25 December 1998, N°2073. The following documents have to be submitted for such State registration of a lease contract:

(1) application for registration,

(2) lease agreement (the failure of the lease agreement to cover any of the substantive issues described above may constitute a basis for the State authorities to refuse such registration)

(3) plan of the land plot,

(4) a decision of the local Council or State Administration confirming its

agreement to lease the land plot if the local Council or State Administration is the lessor, or a copy of the State act or results of a land auction confirming the land ownership rights of the lessor if it is a private entity or an individual.

Under the Land Code, leased land can be sub-leased, however the Lease Law makes this conditional on the consent of the lessor. Such sub-lease agreements will also have to be registered with the relevant Department on Land Resources, but should not need to be notarised.

• Zoning

All Ukrainian real property, including premises and undeveloped land, is ordinarily subject to use zoning. Most urban offices and apartments in urban buildings will be zoned for either residential or non-residential use. Changes in zoning can be difficult to obtain, and therefore the zoning status should always be confirmed prior to any acquisition or renovation.

According to Article 6 of the Housing Code of Ukraine of 30 June 1983 (the "1983 Housing Code"), residential premises may only be used for the accommodation of individuals. Therefore, if residential premises have been purchased and their status has not been changed to non-residential, their use for offices or other non-residential uses will violate the 1983 Housing Code and make the parties to the lease subject to substantial penalties as well as court orders prohibiting further non-residential use. According to Article 8 of the 1983 Housing Code, a change of use from residential to non-residential is prohibited save for exceptional cases. Therefore, where a non-permitted use is anticipated, the necessary change in zoning should always be carried out before the property acquisition is completed and payment is made.

• Leasing of Premises

Leases of offices, residential dwellings and buildings may be validly granted, including to foreigners, as noted in part one of serious of these articles. Unlike for leases of land, no restrictions currently exist to limit the duration of such leases (however permission from the appropriate State agency, in Kyiv from GDIP, is apparently required, as discussed in part one of serious of these articles). Typically, a lease should define the

, the term, the extent and type of permitted refurbishments, and may provide for first refusal rights should the premises be offered to a third party purchaser. In general, the lease provisions can cover whatever else the landlord and tenant agree. Leases shall be in Ukrainian (but may also be in one or more other languages) and may, but need not, be executed before a notary. If the lessor conveys title to the leased premises to another person, then unless the lease provides otherwise, the transfer is subject to the lessee's continuing rights to the leased premises under the existing lease.

• Dispute Resolution and Enforcement against Unlawful Occupation

Normally legal proceedings over property disputes involving any individuals must be brought before the State common courts. Where only corporate entities or entrepreneurs (individuals registered as sole traders) are involved, then any legal proceedings must be initiated in the State commercial courts (until recently misleadingly called "arbitration courts"). Alternatively, the parties to a transaction can provide for arbitration of their disputes by one of the existing institutional arbitration tribunals or by an adhoc arbitration in Ukraine or abroad.

If an owner-occupier sells premises, but improperly refuses to vacate them, then the purchaser can bring proceedings for damages and to have the former owner evicted or, if provided by the contract, to have the transaction set aside. If a tenant stays on after its, his or her lease expires, or a third party improperly occupies the premises, a claim for damages may be brought as well as for eviction. Once an eviction order is obtained, it can be enforced by the State Enforcement Service of the relevant regional department enforce-

ment office, which acts pursuant to the Law "On the State Enforcement Service" of 24 March 1998.

• The New Civil and Commercial Codes and Future Legislation

It is anticipated that the new Ukrainian Civil and Commercial Codes (adopted on 28 November 2001, but effective only as of 1 January 2003) and the Housing Code (likely to be adopted in 2002) should resolve many but not all of the problems identified in part one of these series of articles. These Codes were developed with reference to the laws of other civil law countries, in particular the Netherlands and Germany, and generally provide for real estate laws along the lines of those in the civil law countries of the European Union.

The new Civil Code, for example, describes in much greater detail the rights and obligations of the sellers and purchasers of real estate and creation of condominiums, as well as the use of mortgages and other encumbrances. It also provides for mandatory State registration of immovable property and any transactions with it, and makes information on such registrations and operations publicly available. However, this Code fails to provide time deadlines for such registration or for priorities in title based on when registration is made. There may still be multiple transfers of title to immovable property between legal entities before any registration of such title is made to give notice to third parties. It is anticipated that these remaining problems will be dealt with in the near future by amendments to the new Codes and further implementing legislation.

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