



Gide Loyrette Nouel

Real Property Investment Law in Serbia



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LAND

Classification of land

Land is divided into two principal categories: agricultural land and construction land. Agricultural land may be subject to any ownership regime, including private ownership.

Construction land is regulated by the Planning and Construction Act 2003. Under the Planning and Construction Act 2003, construction land is further subdivided into:

- public construction land, which is exclusively State owned;
- "other" construction land.

Other construction land may be held under any ownership regime. However, if the land was classified as State-owned "urban" construction land before 2003, it must remain State property. The majority of land in the newer category of "other" construction land corresponds to the previous category of the urban construction land and, as a consequence, is not alienable by the State.

Right of use

The right of use over "other" construction land created by the Planning and Construction Act 2003, represents a remnant legal category. The right of use was previously granted to investors for the utilisation of the land; that is construction of appropriate structures. However, the right of use is now replaced by long term leases which serves a similar purpose. The Planning and Construction Act 2003 does not apply retroactively. Therefore, leases are not imposed upon entities already having a right of use by operation of the law.

Land held under a right of use may not be encumbered or sold directly. If a structure is lawfully erected on the land, the right of use is, in principle, irrevocable and is attached to the ownership of the structure, i.e. it is transferred to the acquirer of the structure.

Long term leases

Since the enactment of the Planning and Construction Act 2003, long term leases (up to 99 years) have been offered to investors who wish to utilise "other" construction land (i.e. construct a building on this land). Cities and municipalities have the competence to execute such lease agreements which, as a rule, are concluded after a public auction. However, there are no apparent mechanisms to secure *bona fide* negotiations to extend the initial lease period. Once a structure is lawfully erected on the land, the investor acquires ownership over such a structure but not over the land itself.

Particularities derived from the restitution process

Until the completion of the denationalisation process the Serbian legislator has proclaimed its intention to maintain limited land ownership as envisaged by the Planning and Construction Act 2003. For that reason, even the pre-nationalisation owners of land were not able to recover ownership rights.

Instead, they have been granted usage rights over land owned prior to nationalisation, while the State remains the actual owner. This usage right can be disposed of freely, irrespective of whether a building is erected on the land or not. This right clumsily bears the same title as the right of use created by the Planning and Construction Act 2003, however the two must be viewed as completely separate legal titles under Serbian law.

The law regulating full-scale restitution is yet to be enacted (possibly in 2007). The recent Reporting and Recording of Seized Property Act should facilitate the enactment of restitution legislation.

Private ownership

Private ownership in Serbia does not differ in its concept from private ownership generally recognised elsewhere. Private ownership of land entitles the owner of the structure to a full range of rights. The distinguishing feature is the rights to land are not contingent upon the maintenance of the structure.

BUILDINGS

Ownership

Once a structure has been lawfully erected on a land, it becomes the property of its investor. The investor is defined as the person who has financed the construction and who is the bearer of the construction permit. The investor's ownership of the structure is irrespective of his interest in the land (ownership, lease or right of use).

Lease

Leases of real property are governed by the provisions of the Serbian Code of Obligations. The rules are common and apply equally to the lease of residential premises or commercial premises.¹

Financial lease

Financial leasing of real property is forbidden under Serbian Law.

TITLE

Full ownership

General

Full property ownership is recognised under Serbian law for most types of real property, subject to certain limitations which mainly concern construction land.

Ownership rights are protected under the constitution.² However, the Expropriation Act 1996 gives the State the right to expropriate real property from its owner in exchange for fair compensation.

Serbian law classifies real property under three principle categories:

- private;
- state property (i.e. co-operative and public property);
- property of autonomous provinces and property of local municipalities.

¹ Articles 567 to 599 Serbian Code of Obligations.

² Article 86(1) of the Constitution of Serbia.

Natural resources and assets in common use (e.g. public roads) are State property. The social ownership of land is acknowledged by the constitution as a residual category, prone to privatisation in accordance with the law.³

Acquisition

Any agreement relating to the acquisition of real property must be concluded in writing with the signatures verified by the competent court.⁴ Rights of ownership over real property are acquired by their registration in the cadastre.

However, the cadastre encompasses only approximately 60% of real property in Serbia, with the remainder being either registered with land registry departments of courts, or simply not registered at all. Until the full implementation of the cadastre, the cadastre and the land registry shall coexist.

Limitations on acquisition

Foreign natural persons may acquire real property in Serbia for residential purposes under the same terms and conditions as Serbian nationals, subject to reciprocity.⁵ Reciprocity is assumed unless demonstrated to the contrary. If they need to acquire real property in order to exercise their business activities, foreign natural and legal persons must also obtain the prior approval of the competent Ministry.

Protection of ownership by the courts

Generally, the municipal courts in Serbia are protective of ownership rights.

INTERESTS IN REAL PROPERTY CAPABLE OF REGISTRATION

Easements, mortgage, certain contractual rights such as a long term lease (executed for a period longer than 10 years), pre-emption right, option, limitations or interdictions pertaining to disposal or encumbering of real property can be registered. Given the wide wording of the Serbian law it is difficult to provide exhaustive list of these interests. The purchaser acting in good faith cannot claim that he was unaware of any interest which was previously registered. Therefore, the purchaser shall be required to respect the registered interest.

A purchaser acting in good faith shall be affected by the interest in real property entitling its holder possession over the real property. Therefore, the purchaser shall be required to respect the registered interest. However, he shall be entitled only to damages against the seller under the real property sale and purchase agreement.

There are some customary interests in favour of the State or neighbouring properties which are not capable of registration. Serbian law, however, is vague. Therefore, it is difficult to provide a list or to assess the way these interests affect a purchaser acting in good faith.

³ Article 86(2) of the Constitution of Serbia.

⁴ Article 7 of the Trade with Immovable Property Act.

⁵ Basis of Property Law Regulations Act 1980 (as amended).

DEVELOPMENT OF LAND

Rezoning agricultural land to construction land

The conversion of cultivable agricultural land into a construction land is permitted only subsequent to determination of general interest on that site in accordance with the law. The strict wording of the law might render that the converted cultivable agricultural land necessarily falls into public construction land.

However, this provision actually allows for a wider interpretation to permit conversion of cultivable agricultural land into other construction land as well.

The conversion of cultivable agricultural into a construction land requires an approval of the Ministry of Agriculture. In order to obtain the approval an investor must submit the following documents:

- proof of ownership i.e. the right of use over the agricultural land;
- minutes of the agricultural inspector describing the current state and use of the land in question;
- proof of payment of a once off administrative fee in the amount of 50% of the market value of the land.

By conversion of agricultural land into construction land, the investor obtains the right to build a structure on the land in accordance with the urban plan.

Building construction permit

Under the provisions of the Planning and Construction Act 2003⁶, a construction permit (in Serbian "Odobrenje za Izgradnju") must be obtained from either the municipality or the Ministry in charge of construction.

In order to obtain a construction permit, an application must be made to the relevant authorities by submitting the proof of ownership, lease or right of use over the land, conceptual project - preliminary architectural design, excerpt from the Urban Plan or Zoning Act whichever is applicable and other documents. If the application is complete, the construction permit should be granted within 15 days. However, in practice it usually takes a couple of months and sometimes a year. The validity of the construction permit is specified in the permit itself. A fee is charged for the construction permit. This fee is not significant. However, the fee payable to respective authorities for infrastructural land development on the site might be considerable.

The construction operations should be initiated within two years as from the issuance date of the construction permit. If construction is not initiated within two years the validity of the permit shall cease.

An investor is required to notify the competent municipal authorities on the commencement of works. The competent authorities including the authority that has issued the construction permit and the construction inspectorate.

Under Serbian law, the land zoning and issuing of building permits have to comply with Urban Plan or Zoning Act whichever is applicable.

⁶ "Official Gazette of Republic of Serbia" no. 47/2003 and 34/2006.

Permit to use the construction

In addition, the investor is obliged to obtain a permit to use the construction (in Serbian "*Upotrebna Dozvola*") at the end of the construction. This permit is granted by the same authority that issued the construction permit. The structure is subject to technical inspection before issuance of use permit in order to confirm that it was built in all segments in accordance with the main project and applicable regulations.

However, technical inspection may be done in an interim stage if (i) the investor so requests due to inability that the technical inspection is done after the completion of works, (ii) if the construction permit acknowledges standalone phases, or (iii) if a standalone phase is achieved during the construction works, and the competent municipal body concurs with that, even if the construction permit is issued for the entire structure. The investor may request (under certain conditions) that the structure is made subject to an up to one year probation period prior to issuance of the use permit.

A structure that is erected without proper permits can be demolished. The cadastre in which the building is registered keeps records when one or both required permits have not been received.

COMMERCIAL LEASES**No specific statute**

There are no specific regulations governing commercial leases in Serbia. The generally applicable provisions of the Serbian Code of Obligations also apply to commercial leases.

Form

A lease agreement must be concluded in writing and make reference to the real property which the object of the lease and the amount of rent. Otherwise, the lease is considered null and void.

Duration

A lease may be concluded for a definite or indefinite period. No minimum or maximum duration is fixed by law. Leases concluded for more than 10 years can be registered in the cadastre as an encumbrance.

Termination

Leases concluded for an indefinite period of time may be terminated with eight days' notice by either party.

Lease agreements concluded for a definite period of time end after the period for which they are concluded elapses. If the tenant continues to use the premises and the landlord agrees, it is assumed that a new lease is concluded for an indefinite time period on the same terms as the previous lease.

The landlord may terminate the lease without notice if the tenant fails to comply with the designated use of the property or does not maintain the premises in a proper state. The law further provides that the landlord may terminate the lease if the tenant does not pay his rent within two weeks of receipt of notification from the landlord.

No right of renewal

The tenant has no statutory right to renew his lease. A lease is renewed automatically only if the conditions outlined above are fulfilled.

No pre-emption right of tenant

The tenant has no statutory pre-emption rights.

Rent and rent cap

The rent is freely determined by the parties. Rent must be quoted in CSD (Serbian dinars) or in another currency or the calculation used must be stated. Otherwise, the lease is rendered null and void.

If not determined otherwise, rent is paid twice a year for leases of one or more years in length. If the lease period is shorter than one year the rent is paid at the expiration of the lease period.

Rent review

The law does not provide for any rent indexation provisions. Therefore, rent is adjusted in accordance with contractual provisions.

All costs rechargeable to tenants

All costs may be recharged to the tenant.

Use

The tenant shall use the premises according to their designated purpose and in accordance with the lease agreement. The tenant is responsible for any damage caused by the use of the premises (except that caused by normal wear and tear), regardless of whether the premises are used by the tenant himself, by the subtenant, or by any other person entitled by the tenant.

Maintenance

Unless otherwise specified in the lease agreement, the tenant is responsible for minor repairs and maintenance work required for the day-to-day use of the premises.

The landlord shall carry out all the necessary repairs in order to allow the tenant to use the premises in accordance with their designation. The landlord must ensure the maintenance of the building and of all essential equipment (heating, electricity, gas and water supplies, elevators, etc.).

Improvements

After termination of the lease, the tenant must return the premises in their initial condition, unless the contract provides otherwise.

If a tenant has carried out improvements, the landlord is entitled, at the end of the lease, either to keep the improvements in consideration for a payment equal to their value at the time the premises revert to the landlord or to require the tenant, at his expense, to restore the premises to their original condition.

Transfer of the lease by the tenant

Unless specified to the contrary in the lease agreement, transfer of the lease by the tenant without the prior consent of the landlord is not permitted.

Sublease

The law provides that the tenant can sublet the premises without the prior consent of the landlord if the contract does not provide otherwise. If the landlord's consent is required by the contract, the law provides that this consent cannot be unreasonably withheld. In any case, the tenant guarantees the landlord that the subtenant will comply in full with the provisions of the lease agreement and will respect the designated use of the premises.

TAX**Transaction costs***Sale of real property*Transfer tax

The transfer of real property ownership and the rights of use relating to other construction land is regulated by the Property Tax Act.

This tax is levied at 5% of the sale and purchase contract price. In different cases the tax authority may decide to levy the tax on the property's market value.

The seller must file a tax declaration within 10 days of the onset of tax liability, accompanied by all necessary documentation for the determination of tax base. The tax is due within 15 days of the notification of the decision, stating the amount due. In accordance with the law, the transfer tax is payable by the seller. The parties may agree that it should be born by the buyer.

VAT

Value Added Tax Act 2005 came into force on 1st January 2005. VAT at the general rate of 18% is levied on:

- the first transfer of the newly built structures or economically divisible units within the framework of such structures;
- the first transfer of the owner's share in newly-built structures or economically divisible units within the framework of such structures.

However, a special rate of 8% is applicable to the first transfer of residential structures.

VAT is not payable on land transfers and is not cumulative with transfer tax.

Capital gains*Capital gains realised by individuals*

Capital gains, accrued pursuant to the sale of real property by individuals, are subject to taxation at 20% as set out in the Individual Income Tax Act.

The tax payer may be exempted from the payment of capital gains tax if the proceeds of the sale are invested in the acquisition of other real property for his or her own accommodation or that of a family member within 60 days of the date of sale.

The tax paid can be refunded to the tax payer if such an investment was made within 10 months.

Capital gains realised by legal entities

Corporate Income Tax Act governs the taxation levied on corporate profits at a rate of 10%. This 10% rate also applies to income resulting from the sale of real property rights. Capital losses suffered in the same fiscal year are eligible for set-offs against capital gains.

The Corporate Income Tax Act provides a single annual tax depreciation rate of 2.5%, applicable to all real property.

Leases

VAT

The lease of land, apartments and residential buildings are exempt from VAT. VAT is to be paid on all other kinds of leases, including commercial leases.

Corporate income tax

Corporate income tax applies to income resulting from the lease of real property at the rate of 10%.

No land revenue tax

There is no land revenue tax.

Real property tax

The Property Tax Act provides for a general property tax on any owner or user of real property located in Serbia.

The Property Tax Act defines real property as follows: land, residential and business buildings, business premises, garages, hotels and recreational property, and other buildings. However, there are some exemptions such as real property used for educational, cultural, scientific, social welfare, health care, humanitarian or sports purposes on which property tax is not due.

The tax is payable by the person owning or enjoying the use of the property (owner, user or other). Property tax rates are as follows:

- on the rights to real property of a taxpayer that keeps account books: 0.4%;
- on the rights to real property of a taxpayer that does not keep account books: sliding scale ranging from 0.4% to 3% of the market value of the real property according to the table below:

Real property value (CSD)	Rate applicable (CSD)
Under 6,000,000 (approximately EUR 75,000)	0.4%
Between 6,000,000 and 15,000,000 (approximately EUR 75,000 to 187,500)	24,000 + 0.80% on the amount exceeding 6,000,000
Between 15,000,000 and 30,000,000 (approximately EUR 187,500 to 375,000)	96,000 + 1.50% on the amount exceeding 15,000,000
Over 30,000,000 (approximately EUR 375,000)	321,000 + 3.0% on the amount exceeding 30,000,000

A tax declaration must be filed with the relevant local municipal authorities by 31st March of each year. The tax due is usually payable in four equal instalments.

LEGAL COSTS REGARDING REAL PROPERTY ACQUISITIONS

Real property transactions usually involve the following costs: certification fees, legal counsel's fees and real property land register fees.

Certification fees

Certification fees for sale and purchase contracts are proportional to the value of the relevant transaction, but can not exceed the Serbian dinar equivalent of EUR 300.

Legal counsel

The fees for drafting an agreement on the sale and purchase of real property are up to 1.5% of the value of such real property.

Real property land register

Registration fees vary but are low.

SECURITY USED IN REAL PROPERTY FINANCINGS

Mortgages

A new law on mortgages came into force in January 2006. Mortgages may be established over fully owned real property, registered in the land registry or in the cadastre.

Mortgages are established by their registration in the land registry or in the cadastre on the basis of:

- a mortgage agreement (a new way of constituting a mortgage);
- a judicial settlement (most common way of establishing a mortgage under the previous law);
- a unilateral declaration of the owner, by which he authorises the creditor to be paid on the sale of the immovable property (in Serbian "založna izjava");
- a court decision;
- a law.

The signatures on the mortgage agreement and on the unilateral declaration must be certified by the competent municipal court. If these documents contain certain mandatory provisions prescribed by law (precise description of the real property, *clausula intabulandi*, owner's authorisation to have recourse to an out of court sale of his/her real property, etc.), they are considered to be writs of execution.

If the debtor does not fulfil his obligations on time, the creditor may proceed with an extrajudicial sale of the immovable property (after the issuance of two unsuccessful summons and only on the basis of a mortgage agreement or a declaration that fulfils the conditions prescribed by law) or with judicial enforcement proceedings (on the basis of a judicial settlement, a mortgage agreement or a declaration).

Mortgages terminate when, *inter alia*, the obligations arising from the main obligation between the parties are wholly performed or the mortgaged property is destroyed (the creditor then has a pledge on the insurance claim).

The costs related to the establishment of a mortgage are as follows:

- for a mortgage agreement or a unilateral declaration – up to EUR 300 for certification costs and up to EUR 30 for registration costs;
- for a judicial settlement – up to EUR 400 for judiciary costs and up to EUR 30 for registration costs.

Other common security

A mortgage is currently the only form of security commonly used in real property financing in Serbia. Since the creation of a register of security interests over movable assets in August 2005, some other forms of security have been infrequently used in real property financings, such as share pledges, cash pledges and pledges over rental income. The pledge agreement has to be registered in the register of pledges in order to be enforceable. Registration fees vary but are low. Signatures on share pledge agreements have to be certified by the competent municipal court. Certification fees are also low.



About the Law Firm

Gide Loyrette Nouel is an international law firm that has been advising real estate investors since 1920. Gide Loyrette Nouel has been present in Central and Eastern Europe since 1991.

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