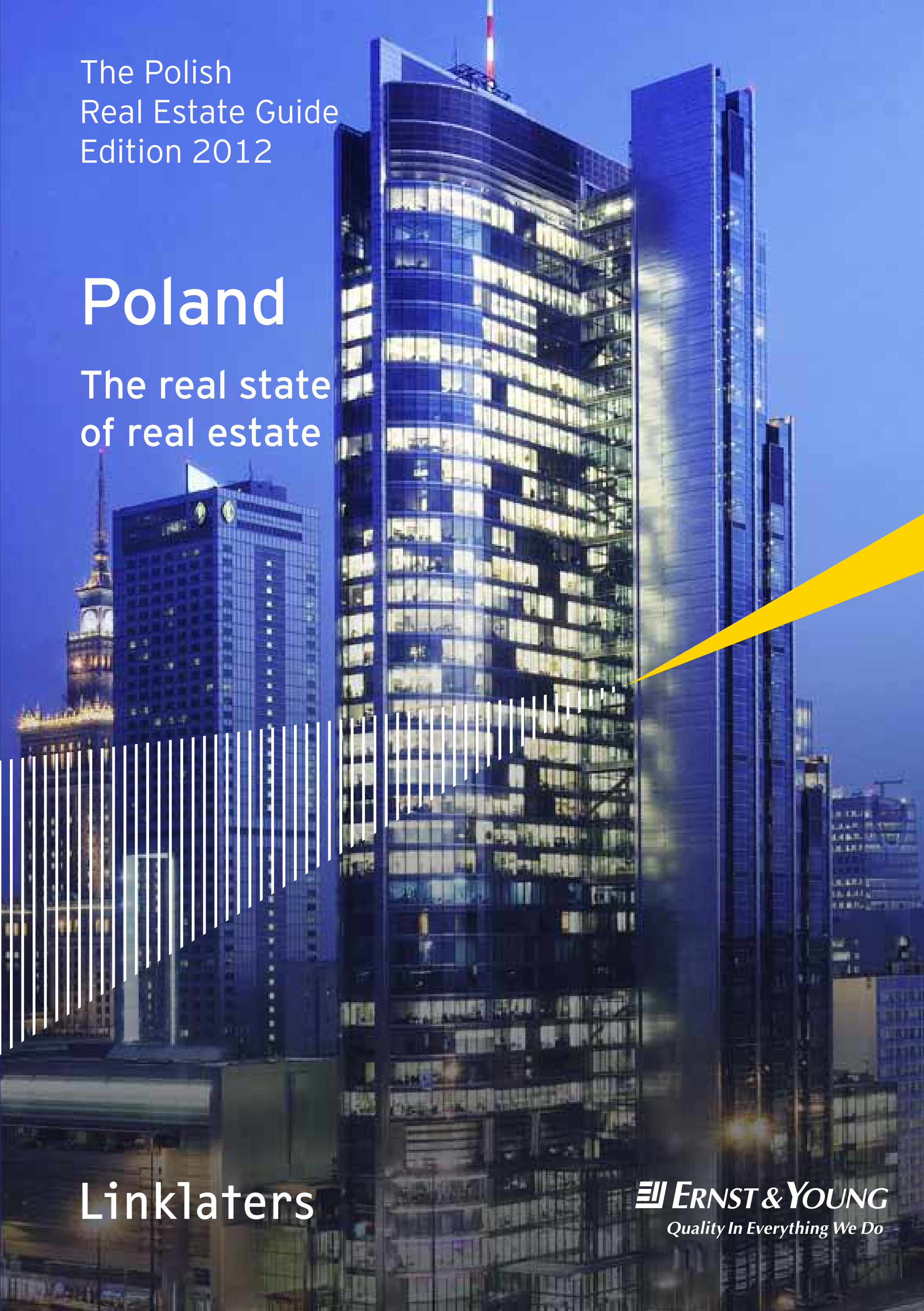
The Polish
Real Estate Guide
Edition 2012

Poland

The real state of real estate



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Preface

Ernst & Young, a global leader in assurance, tax, transaction and advisory services has joined forces with Linklaters, a market-leading global law firm, to prepare this guide to the Polish real estate market. This guide aims to provide its readers with a broad view of the market and the current investment climate, as well as legal and tax information, in a practical format to help you make informed investment decisions. Our combined expertise in this market has enabled us to produce what we hope will become an indispensable reference tool on the state of the Polish real estate market.

In conjunction with the views contained in this guide, it is important to seek current and detailed information on the commercial climate at the time of considering your investment, as this can change at any time. This guide reflects information current as of 1 January 2012 unless stated otherwise.

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1.1. Office market

Poland – general

Following major reforms in 1992, Poland experienced a boom in economic activity in the 1990's. Like other markets, the modern office market began to emerge with an initial wave of new office construction starting in the financial and political capital – Warsaw.

Until 1996, annual supply remained below 50,000 m^2, which was substantially less than the rapidly increasing demand. Because of the difficult local development and financing conditions, supply was initially slow to respond. The second half of the decade showed a rapid increase in supply, as Poland demonstrated its political stability and sound economic fundamentals. The rapid increases continued into the first part of this decade, initially addressing pent-up demand from decades of low supply, but later resulting in an office oversupply in many major cities and towns in Poland. Generally, rents were in steady decline from the 1990s until 2005. The years run up to 2009 showed a reversal of this trend, with indications of a maturing office market where new buildings come to market in a more timely response to demand and thus stabilizing rents and vacancies. Although the financial crisis temporarily affected the situation, Warsaw remains by far the largest office market in Poland and still attracts major development activity. On the other hand, other regional business centers have entered the path of strong economic growth, increasing interest in modern office accommodation even in smaller cities and towns. As far as new projects under construction and proposed are concerned, in 2011 the most important activity was observed in Krakow, Wrocław and Tri-City. On the majority of Polish office markets year 2011 was one of the weakest in terms of new supply. The strict lending criteria implemented by banks after 2008 verified most of the investment processes. Currently construction activity recovers all across Poland, after a sharp decrease in number of completions, developers have revived their previous plans.

Focus on Warsaw

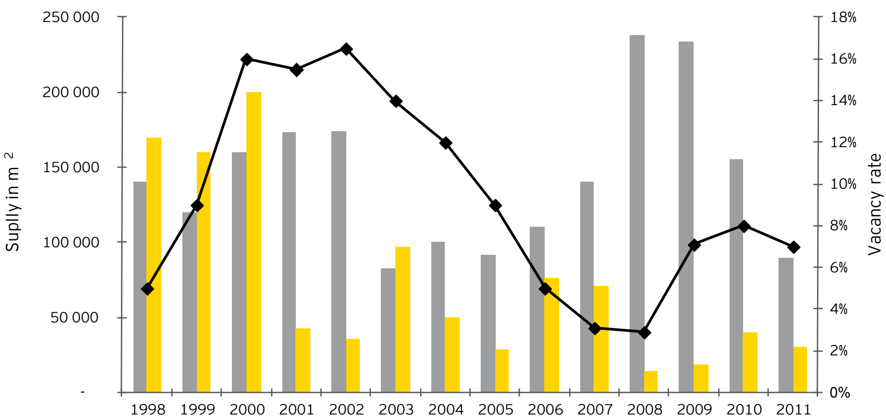
The modern office market in Warsaw started to develop rapidly at the beginning of the 1990s in response to the Polish political transition and economic reforms, followed by a growth period during recent years, in which the Warsaw area played a major role.

Because of its central functions and convenient location, the Polish capital city has received a significant share of the inflow of foreign capital. Large foreign companies, including various financial institutions, consulting companies, as well as international firms, usually choose Warsaw as a location of their headquarters in Poland. In addition, Warsaw has traditionally been the most important administrative and business center for domestic companies. This led to rapid growth of demand for modern office space in the city, which in the period from 1990 until the first half of 1998 resulted in 98% to 100% occupancy rates as well as one of the highest rental levels for office space among European cities.

Supply

The end of 1998 marked the first dramatic date for modern office space, where over the course of one year the modern office supply doubled from the 300,000 m² completed between 1989 and 1997, to 680,000 m². Two years later, stock rose to approximately 1,360,000 m² and although 54% of this was in the city center, 2001 marked the end of the central location's dominance in new annual supply. With the exception of 2003, annual delivery of modern office space in non-central locations exceeded central, and the trend continued through 2011. At the end of 2011, the total modern office space reached approximately 3,6 million m2, with non-central locations accounting for around 65%.

Annual delivery of modern office space (m²)



Source: Ernst & Young

As the supply of new space reached and surpassed demand, the market saw vacancy rates rise to very high levels. Starting from between 4 and 6% in 1998, the building boom from 2000 to 2002 helped vacancy rates rise as far as 20% in the city center and 16% in the outskirts. As the market stabilized, and non-central locations became the norm rather than the exception, central and non-central locations fluctuated back and forth between 15 and 19%, with non-central locations falling below the 10% mark (7% on average) in 2004.

Regardless of the proportion of central to non-central locations, the overall vacancy level in Warsaw has systematically decreased from 2002 until 2007, when central and non-central vacancy rates stood at the 3.4% and 2.9% respectively. With the crises came a reversal of this trend; in 2008 and 2009 vacancies doubled to over 7% overall. In 2010, vacancy rate remained stable at the level of 8%. Due to growing demand for office accommodation and limited completions in 2011, the vacancy rate in Warsaw has been falling. At the end of 2011, approximately 6,7 % was unoccupied. It is expected that the supply gap should be fulfilled within the next two years.

On the basis of location, the modern office stock in Warsaw can be divided into two groups: central and non-central. The city center is bound by ul. Towarowa, ul. Grójecka, ul. Wawelska, al. Armii Ludowej, the Vistula River and al. Solidarności. The most significant office buildings located within this area include: Rondo 1, Lumen, Skylight, Metropolitan, Warsaw Financial Center, Wolf Marszałkowska, Focus Filtrowa, Atrium City , Warsaw Trade Tower and Atrium complex. Non-central office locations include Mokotów, Ochota, Wola and Praga districts. In these locations, Mokotów Business Park, Wiśniowy Business Park, Trinity Park, Marynarska Business Park, Ochota Office Park, Jerozolimskie Business Park and Lipowy Office Park warrant closer attention.

Yearly new stock peaked in 2000 when 360,000 m^2 was added to supply and there has been growth year-on-year since 2005, when 120,000 m^2 of new supply was added.

2010 recorded the completion amounted to over 200,000 m^2 of new stock, though this was planned well before the crisis and these projects had secured financing in advance of now stricter lending criteria. In 2011 approximately 120,000 m^2 was delivered to the market. The majority of space is in office buildings located outside of the city center.

Major office developments completed, 2011

Name	Location	Area (m^2)	Developer
Lipiński Passage	City center Al. Jerozolimskie	3,500	Union Investment Real Estate GmbH
Nowy Dom Jabłkowskich	City center ul. Chmielna	2,800	Dom Towarowy Braci Jabłkowskich S.A./LHI Leasing Polska
Prosta Tower	City center ul. Prosta	5,400	Marvipol S.A.

Name	Location	Area (m²)	Developer
Mokotowska Square	City center ul. Mokotowska	8,500	Yareal / Ufficio Primo (Euro Invest)
Hortus	City center ul. Topiel	10,200	Nieruchomości Powiśle
Equator II	Non-central Al. Jerozolimskie	21,300	Karimpol Polska
Okęcie Business Park	Non-central ul. 17-go stycznia	9,000	GTC
Wilanów Office Park B1	Non-central Al. Branickiego	7,300	Polnord
Mokotów Nova I	Non-central ul. Wołoska	25,000	Ghelamco Poland
Platinium IV	Non-central ul. Domaniewska	13.300	GTC
Racławicka Point	Non-central ul. Racławicka	1.900	Capital Park

Source: Ernst & Young

According to project announcements, approximately 350,000 m² of modern office space will enter the Warsaw market in 2012 and 2013. However, that prediction is subject to a number of variables, as developers (and their lenders) take a more cautious approach to speculative projects. It is expected that some of these projects will be delayed until such time as, reasonable level of pre-leasing has been achieved.

Major office developments under construction, 2012/2013

Name	Location	Area (m²)	Developer
Senator	City center ul. Bielańska	22,000	Ghelamco Poland
Feniks	City center ul. Żelazna	8,500	Europlan Capital
Warsaw Spire	City center ul. Grzybowska / Towarowa	96,000	Ghelamco Poland
Plac Unii	Non-central Pl. Unii Lubelskiej	41,000	Liebrecht & wooD / BBI Development NFI
Green Corner	Non-central ul. Chłodna	27,000	Skanska
Wilanów Office Park B2, B3	Non-central Al. Branickiego	14,500	Polnord
Miasteczko Orange	Non-central Al. Jeorozolimskie	44,000	Qatar Holding/ (Bouygues Immobillier)
Karolkowa Business Park	Non-central ul. Karolkowa	15,000	Ablon Group

Name	Location	Area (m^2)	Developer
Konstruktorska Business Center	Non-central ul. Konstruktorska	7,300	HB Reavis Group
Platinium V, Vi	Non-central ul. Domaniewska	22,000	GTC
Business Graden phases: I, II	Non-central ul. Żwirki i Wigury	30,000	SwedeCenter

Source: Ernst & Young

Demand

The demand for modern office space comes mainly from:

- Polish and foreign companies who are based in Poland and have participated in the rapid economic growth;
- new entrants into the Polish market, particularly evident in 2004, just after accession to the European Union and again during 2007 and 2008;
- the new "Services and Information Economy" accelerating the need for up-to-date office space. Poland in particular has benefited from Business Process Offshoring (BPO).

Growth surged in 2007, with take-up reaching almost 500,000 m^2. Take-up moderated to 525,000 m^2 in 2008 and by the end of that year symptoms of a declining market had emerged, particularly for office space in the Warsaw city center. In 2009 the total volume of leasing transactions amounted to 210,000 m^2, or approximately 40% of the prior year's volume, with a market relegated to mainly small lease transactions.

Currently, demand is much less driven by business expansion rather increasingly by tenants relocating either to improve their accommodation or to reduce cost by optimizing space. Due to the crisis in 2008/2009 many tenants reduced their space and were seeking to sublet the excess. This situation changed in 2010, when, due to a more positive economic environment and optimistic forecasts, demand has recovered. In 2011 approximately 573,000 m^2 were leased, which is a 4% increase of the take up in comparison to the previous year. It is estimated that demand will grow further this year.

Rents

Along the classic supply and demand model, rents in the late 1980s and early 1990s escalated as Poland opened its borders to foreign investment, and supply of modern office space was extremely limited. Demand for office space pushed rents to their peak in 1991 of USD 50/m^2/month for office space of relatively poor quality.

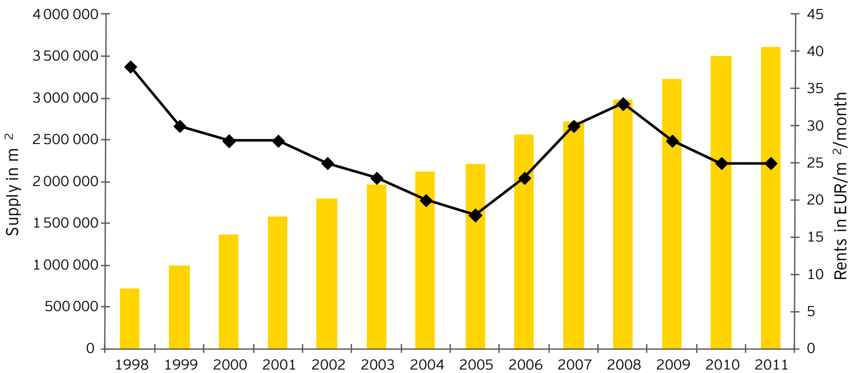
With such limited supply available, there was little segmentation in the Warsaw office market, resulting in both central and non-central locations having similar rent rates. The first building boom of the late 1990s pushed overall rents down, but it was the introduction of out-of-town office parks around 1996, that helped differentiate prices between central and non-central locations. The late 1990s noticed rents for modern city center offices typically 25% to 30% higher than for new offices in out-of-town locations. However, not all of the difference can be accounted for by location alone, as non-central locations were built for more price-conscious tenants ready to accept a lower standard.

The second part of the boom in the early 21st century brought with it additional increases in supply and a further drop in overall rent levels. This temporarily pushed the gap between locations closer, but more demanding clients helped raise the standard of central locations, and two separate markets emerged altogether.

Currencies have also played a role in the leasing markets. In the early years low standard properties were priced in PLN, with higher standard properties geared for international clientele being denominated in DM or USD. Since accession into the EU, the Euro has become Poland's standard reference currency for leases. Today, rents for centrally located, high quality office buildings are between EUR 22 and 25/m^2/month.

Current rents for prime office space located outside of the city center range from EUR 12 to 15/m^2/month. As expected in a tough market, new rental contracts are being signed well below asking rates. Our sources suggest typical effective rents are roughly 10-15% lower than asking rents. Asking rents depend mainly on location, quality of finish, size and length of lease term.

Prime office rents & cumulative office supply



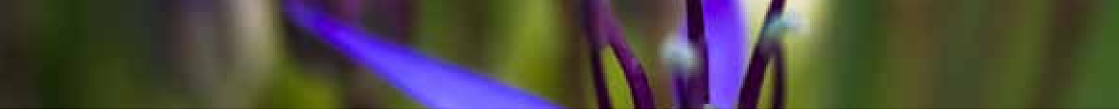
Source: Ernst & Young

Due to limited financing and only a few office buildings scheduled for completion in 2012, it is expected that the rental rates will stabilize or might grow by EUR 1-2/m^2/month, especially in the central locations. In addition, for the same reason, the difference between asking and effective rents might decrease.

Standard lease terms

The following terms for modern office buildings are regarded as common features within a typical lease agreement:

- since the introduction of the EUR, most new leases have been denominated in EUR, but paid in PLN as was regulated by Polish law until 2009 (see section on legal and tax aspects). Some older leases are denominated in USD;
- rents are typically escalated by the European (Eurostat) for Euro rents and the U.S consumer price index for USD leases;
- service charges including water, electricity, heating, air-conditioning, service, cleaning, etc. are added to net rents and calculated according to the area leased. These rates generally vary from EUR 4.0 to 5.5 /m^2/month;
- a charge for common space is usually added to the net office space. This charge calculation is based on the pro rata share of common space used (lift, lobby, reception). Such "add-on factors" generally vary from 5% to 10% of the leased area;
- in addition to rent and service charges, tenants are obliged to pay 23% value Added Tax (VAT);
- landlords usually require tenants to provide a rental deposit or bank guarantee equal to 3 months rent;
- leases range from 1 to 30 years; typical contracts are between 3-5 years, with a trend toward longer leases for larger tenants;
- typical lease incentives include:
    - rent-free period of 3 to 6 months;
    - fit-out allowance of EUR 150 - 250 per m^2.



1.2. Retail market

Poland – General

Polish retail market has undergone substantial changes in recent years, particularly in larger urban areas. From just a limited number of state-owned and small private enterprises at the beginning of the 1990s, the supply has grown to encompass an increasing number of international retail chains and good quality local outlets.

Foreign shopping center operators, investors and developers have moved across national borders in order to access new or less competitive markets or to exploit market niches. In this context the ownership of shopping centers, as well as the mix of retail tenants, is becoming increasingly international.

In the early 1990s Polish retail supply grew to satisfy the demand for food. This led to the arrival of international brand supermarkets including Billa, Hit, Rema 1000 and Globi. From 1996 on, Poland has seen a rapid expansion of major hypermarket chains such as Tesco, Hypernova, Carrefour, Auchan, Géant, E.Leclerc and Real. Simultaneously, some supermarket chains retreated (e.g. Billa), some were sold (e.g. Hit, Géant, Leader Price, Hypernova) and a few new strong brands appeared (Aldi, Alma and Piotr i Paweł). Moreover, an expansion of discount stores represented by Lidl, Plus Discount (now owned by Jeronimo Martins) and Biedronka has been observed.

Currently, the total modern retail supply accounts for 8.8 million m^2. Although the largest share in the retail market is held by Warsaw followed by other main cities such as Tri-City, Poznań, Wrocław, Krakow, Łódź and Katowice, investors have been seeking opportunities in smaller cities, thus more and more projects are being planned in towns such as Mielno (Beach City), Rzeszów (Res-Vita), Elbląg (Galeria Rapsodia), Czechowice - Dziedzice (Stara Kablownia), Gliwice (Europa Centralna), Rzeszów (City Center) and Lublin (Atrium Felicity).

Modern retail space completed in 2011 amounted to around 600,000 m^2. Major new openings included Millenium Hall in Rzeszów as well as Galeria Słoneczna in Radom and Futura Park in Kraków. Openings in the smaller cities included projects such as Galeria Jastrzębie in Jastrzębie Zdrój or Zgorzelec Plaza in Zgorzelec.

In the last 2010 year developer activity was observed mostly in small and medium cities. The actual amount of space that will be delivered to the market will depend upon availability of financing and tenant demand for retail space. The most significant proposed project is regional retail park Europa Centralna, located in Gliwice.

Supermarkets or hypermarkets are still the preferred formula for anchor tenancy, although an increasing number of projects are looking towards entertainment functions to decrease grocery retailing as the basic demand driver. Standard complementary functions still include gallery shops, service points, and a food court.

Over the last few years, new retail format types have also emerged, including factory outlets, shopping centers with a choice of interior decoration brands (e.g. Domoteka in Warsaw), and retail parks. Moreover, some of the largest hypermarket operators like Tesco or Carrefour have been introducing new formats such as mini-hypermarkets and supermarkets (e.g. Carrefour Express) in response to the rapid development of supermarket and discount chains across the country. As to the geographical distribution, developments featuring a hypermarket are typically built outside of the city center while downtown malls usually offer only a supermarket.

The major hypermarket chains in terms of sales revenues include: Metro AG (Real, Makro Cash & Carry, Media Markt, Saturn), Jeronimo Martins Dystrybucja (Biedronka), Tesco, Carrefour, Auchan, Schwarz Group (Lidl, Kaufland), Emperia Holding (Groszek, Stokrotka, Delima, Milea, Lewiatan, Euro Sklep, Społem Tychy), Tengelmann (OBI), Rewe (Bill, Selgros), ITM (Intermarche, Bricomarche), E. Leclerc.

Focus on Warsaw

Total retail supply in Warsaw exceeds 2.1 million m^2, but only approximately 1.5 million m^2 of it could be considered "modern" retail space suitable for international occupiers. This equates to around 1 m^2 of total retail space per person, which even taking into consideration the disposable incomes of Warsaw's inhabitants, is probably too low when compared to the Western European level of some 2 m^2 per person. Modern retail space includes shopping malls and hypermarkets, most of which are located outside the city center.

The remaining retailers are mostly retail units situated on the ground floors of residential buildings or department stores built before the 1990s.

2011 recorded limited new developments enter the Warsaw market. Wolf Bracka (12,000 m^2) and two Jula multistores (3,500 m^2 each) were delivered to the market.

Major shopping centers in Warsaw

Name	Location	Area (m²)	Developer	Completion
Arkadia	Śródmieście Al. Jana Pawła II	110,000	Cefic/BEG	2004
Złote Tarasy	Centrum ul. Złota	65,000	ING Real Estate	2007
Galeria Mokotów	Mokotów ul. Wołoska	59,000	Globe Trade Center	Phase I - 1999 Phase II - 2002
Wola Park	Wola ul. Górczewska	73,000	Central European Retail Property Fund	2002
Blue City	Ochota Al. Jerozolimskie	82,000	Singspiel	2004
Promenada	Praga Południe ul. Ostrobramska	66,000	ECC	Phase I - 1996 Phase II - 1999 Phase III - 2005
Sadyba Best Mall	Sadyba ul. Powsińska	27,000	Sadyba Centre S.A.	2000

Source: Ernst & Young

The prime shopping streets in central Warsaw include Pl. Trzech Krzyży, Nowy Świat and Chmielna, which are closed to private automobile traffic. Foreign and domestic retailers have also established a strong presence on the ground floor of buildings facing al. Jerozolimskie and ul. Marszałkowska. The section of al. Jana Pawła II to the north of the Atrium Business Center has traditionally been known as a shopping destination and today still features a mix of moderately priced stores. Small clusters of expensive shops are also found in hotel arcades, and on the ground floors of the major office buildings.

Several more small shopping centers are planned for construction within the next three years, but the amount of space that will actually be completed remains uncertain. The majority of planned space for the immediate term consists of extensions of existing facilities (Wola Park, Promenada, Targówek Retail Park, Tesco Kabaty) or reconstructions (Hala Koszyki). Also, a trend is emerging for building retail developments within large scale housing developments such as the planned Retail Center (GTC/Polnord) in Miasteczko Wilanów. There are two projects currently under construction (Galeria Wiatraczna and Plac Unii) with completion scheduled for 2012-2013. Moreover, there are plans for contruction of another factor outlet – Factory Annopol with completion scheduled for 2012.

The retail sector has long been characterized as undersupplied. Along with the increasing disposable income of Poles, this sector offers several characteristics to help insulate it from the current crisis.

Retail rent rates vary widely and depend mainly on type of facility, location and quality. The rates for retail units on prime streets, in the best locations, reach levels as high as EUR 100/m^2/month.

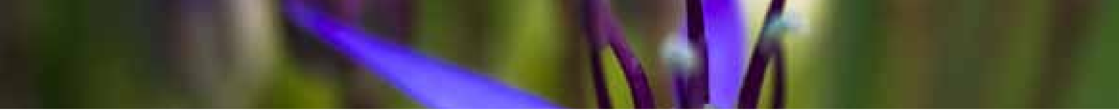
Average rents for small units in modern shopping centers in Warsaw range from EUR 40 to 50/m^2/month depending on location, unit-size and type of merchandise. Prime units of 100–150 m^2 are let at EUR 65 to 85/m^2/month (including rents in Złote Tarasy, which represent the highest retail rents in Poland). Larger units lease for approximately EUR 15 to 30/m^2/month. Usually anchor store operators occupying units of more than 1,000 m^2 pay much less than others, with average rents from EUR 9 to 12/m^2/month and even lower, say EUR 5 to 8/m^2/month for hypermarkets. Service charges for smaller space vary from EUR 4 to 8/m^2/month. Major tenants are charged EUR 2 to 3.5 /m^2/month.

Standard lease terms

Standard lease terms for retail space are similar to those in the office market. However, the typical lease length for retail space in modern shopping centers ranges from five to 10-years. Anchor tenants usually prefer 10-year lease agreements with extension options, typically for an additional 10-year period.

With the increasing supply of retail space, tenants have become more demanding and developers seeking attractive tenants frequently offer not only lower rental rates but also incentives such as:

- rent free period ranging from 1–2 months for smaller shops and up to 6 months for larger units;
- fit-out allowance at the level of EUR 50–200/m^2 for large units and up to EUR 600/m^2 for anchor tenants (i.e. with minimum 10-year lease agreements).



1.3. Warehouse market

Poland – General

The modern warehouse market in Poland began its development in the early 1990s, and currently includes over 6 million m^2 of warehouse space. Although initially centralized within the Warsaw metropolitan area, the modern market can now be subdivided into seven regions, each of which is well developed with warehouse space. These include: Warsaw, Poznań, Upper and Lower Silesia, Central Poland (Łódź, Piotrków Trybunalski), Tri-City, and Krakow. Logistics centers are located outside city limits and offering good access to major existing and planned highways.

One activity that has continued even through the crisis has been road and infrastructure construction. This continues to boost investor interest in alternative regions including Szczecin, Zielona Góra, Lublin, Toruń, Bydgoszcz and Rzeszów, but these are now mostly built-to-suit projects. The current situation in the financial markets has dampened accessibility to financing while raising the cost of capital, rendering some investments no longer feasible. This is evident in the current "tightening" by warehouse developers, who are reducing speculative construction in order to focus on managing current stock. Many have also limited new projects to privately financed, built-to-suit projects.

The most active warehouse developers in Poland

Company	Country of origin	Major locations (existing and proposed)
ProLogis	USA	Będzin, Błonie, Chorzów, Dąbrowa Górnicza, Gdańsk, Janki, Katowice, Nadarzyn, Piotrków Trybunalski, Poznań, Rawa Mazowiecka, Ruda Śląska, Sochaczew, Sosnowiec, Stryków, Szczecin, Teresin, Ujazd (proposed), Warsaw, Wrocław, Września
AIG/Lincoln	USA	Gdańsk (under construction), Gliwice, Łódź, Piaseczno, Stryków, Toruń (under construction), Warsaw (Raszyn, Ursus)
Panattoni	USA	Bielsko-Biała, Błonie, Czeladź, Garwolin, Gdańsk, Gliwice, Krakow, Łódź, Mysłowice, Ożarów Mazowiecki, Poznań, Pruszków, Robakowo, Stryków, Święcice, Teresin, Toruń, Wrocław
Biuro Inwestycji Kapitałowych	Poland	Krakow, Pruszcz Gdański, Ożarów Mazowiecki, Sosnowiec, Wrocław (planned), Poznań (planned), Mielec
Ghelamco	Belgium	Warsaw (Mokotów, Okęcie, Włochy, Żabia Wola)
Apollo-Rida	USA	Warsaw (Żerań)

Company	Country of origin	Major locations (existing and proposed)
PointPark Properties	UK/Poland	Mszczonów, Poznań
Menard Doswell & Company	USA	Błonie, Czeladź
Logistic City	UK	Piotrków Trybunalski
MLP Group	Israel	Brwinów, Pruszków, Poznań (planned), Tychy
Goodman	Australia	Gdańsk, Łódź, Modlniczka near Krakow, Poznań, Toruń, Warszawa, Wrocław
Metropol Group	Poland	Błonie, Warsaw
SEGRO	UK	Gdańsk, Gliwice, Łódź, Poznań, Stryków, Tychy, Warsaw
VALAD	Australia	Błonie, Piaseczno, Raszyn, Warsaw, Wrocław

Source: Ernst & Young

Focus on Warsaw

The Warsaw modern warehouse stock is defined as properties within approximately 50 km of the city center and is split into two zones:

- zone I: approximately 600,000 m^2 in properties located within a 15 km radius (Okęcie, Służewiec, Targówek, Żerań), warehouse facilities in this zone host mostly pharmaceuticals, cosmetics and electronics;
- zone II: approximately 2,000,000 m^2 in properties located 15 to 50 km from the city center (e.g. Piaseczno, Ożarów Mazowiecki, Błonie, Teresin, Nadarzyn, Pruszków).

Although the Warsaw metropolitan area continues to account for the largest single share in the Polish market (40% of total space in Poland), this dominance has been steadily eroding as developers push for a presence along the emerging motorways outside the major cities.

The total modern warehouse space in the Warsaw Metropolitan Area (Zones I, II and III) is estimated at approximately 2.6 million m^2 of modern space.

In 2011, around 80,000 m^2 of warehouse space was completed, in comparison with 2010 the increase of new supply was significant. Currently about 80,000 m^2 of warehouse space is under construction in Warsaw. Future supply is hard to pin-point as developers move to client focused built-to-suit projects.

The majority of space leased in modern distribution centers is let to logistics companies, which sub-let space and provide their tenants with full service, including packaging, loading, customs clearance and transportation.

Examples of class A modern warehouse developments in Warsaw area

Project	Location	Area (m^2) [existing / proposed]	Developer / Owner	Completion
ProLogis Park Teresin	Teresin	159,000	ProLogis	2000-2005
Europolis Park Błonie	Błonie	155,000 / 7,000	Menard Doswell / Europolis	2006 - under construction
ProLogis Park Błonie	Błonie	153,000	ProLogis	1999-2008
Diamond Business Park Piaseczno	Piaseczno	58,000	AIG / Lincoln	2001-2007
Żerań Park I	Warsaw, Żerań	52,000	Apollo Rida / Heitman International Poland	1999-2000
Krakowska Distribution Center	Warsaw, Włochy	11,000	Ghelamco / First Property Group	2005
Żerań Park II	Warsaw, Żerań	45,000 / 63,000	Apollo Rida	2005-2006
Manhattan Business and Distribution Center	Warsaw, Włochy	24.000	Ghelamco / Liebrecht & wooD	1998
ProLogis Park Warsaw I	Warsaw, Okęcie	39,000	Menard Doswell / ProLogis	1995-1997
ProLogis Park Warsaw II	Warsaw, Targówek	38,300	ProLogis	2006
ProLogis Park Warsaw III	Warsaw	24,000	ProLogis	2007
Diamond Business Park Warsaw	Raszyn	32,000 / 64,000	AIG Lincoln / Heitman International	1998/1999 - present
Platan Park	Warsaw, Ursynów	53,000	Platan Group	1998-2001
Łopuszańska Business Park	Warsaw, Włochy	25,000	Ghelamco	2004
Millenium Logistic Park Pruszków II	Brwinów	80,000 / 160,000	MLP Group	2007
Panattoni Park Ożarów	Ożarów	30,000 / 35,000	Panattoni	2009
Panattoni Park Pruszków	Pruszków	78,000	Panattoni	2007-2009
Tulipan Park Warszawa	Nadarzyn	50,000 / 60,000	SEGRO	2009-2011
Gate One Business Park	Warsaw	19,000	STRABAG/ Raiffeisen Immobilien-Kapitalanlage GmbH	2012

Source: Ernst & Young

Until the end of 2008, demand for modern warehouse space in Greater Warsaw ranged from 400,000 to 500,000 m^2 per year, which is higher than demand in any of the other Polish regions. In 2011 the demand for leasable warehouse space amounted to approximately 750,000 m^2 and doubled as composed to 2010.

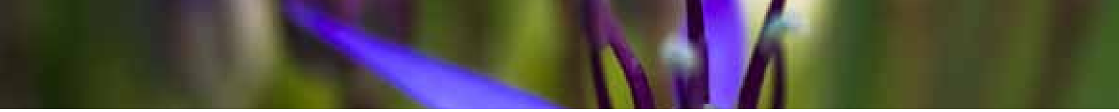
The most sought unit sizes are 1,000 – 3,000 m^2, usually leased in office/warehouse facilities of above 10,000 m^2, located in logistics parks. Areas larger than 10,000 m^2 are usually leased by logistics operators. Vacancy rates in Warsaw have stabilized at the level of 16%.

In this competitive market segment with an overhang of ready space to lease, downward pricing pressure remains strong for new leases. Warsaw big box rents for 2011 and are currently quoted at the level:

- zone I: EUR 4.0 to 5.5/m^2/month;
- zone II: EUR 2.5 to 3.0/m^2/month;
- zone III: EUR 2.0 to 2.5/m^2/month.

Incentives have also moderated, with one month for each year of lease term being a general benchmark.

In addition to rent, tenants are obliged to pay service charges for property management, maintenance, property tax, and security. A fixed amount paid in advance and adjusted annually on the basis of actual costs varies from EUR 0.7 to 1.3/m^2/month.



1.4. Residential market

Poland – General

The Polish residential market is characterized by a housing shortage which the Ministry of Infrastructure estimates at around 1.5 million units and unofficial estimates put at closer to 2.5 million units. Although the growth in units built between 2005 and 2007 reached between 10% and 16% year-on-year, the yearly average of 121,000 units added to the market have done little to close the gap. Moreover, the lack of master zoning and the time-consuming processes which must be negotiated to obtain a building permit, have also worked to constrain supply. The increasing wealth of Poles, as well as the relatively easy financing terms that were becoming available during the run-up to the financial crisis, had pushed the disparity between supply and demand to new levels.

Despite the continuing need for adequate housing, demand still relies on affordability, and to cap off a few good years of strong price growth, 2007 marked a turning point. Dynamic price growth continued in that year ranging from 10% in markets such as Warsaw, Wrocław, and Krakow, while reaching as high as 50% p.a. in mid-size cities such as Katowice, Poznań, and Tri–City.

Moderation in late 2007 led to stagnation in 2008, which ultimately gave way to price decreases in 2009. Even significant developer incentives on offer did not stop price declines, especially for flats larger than 70 m^2. In 2010 the residential market stabilized, however the situation is still below the pre-crisis level. According to data published by Central Statistical Office, between January and December 2011 the number of completed residential units amounted to 132,000 which is 3% less than in 2010 and 17,7% less than in 2009. Number of construction starts reached 180,000 and it was an increase by 5,2% in comparison to the same period previous year.

Focus on Warsaw

Warsaw's residential market remains the most developed in Poland: this demand is driven mainly by in-migration, the highest income levels in Poland, and the lowest unemployment rate. Employment and education possibilities in Warsaw are a magnet for young people from other regions of Poland, and a result of this demographic is the dominance of multifamily developments in the Warsaw residential market. The share of housing units in single-family developments built in Warsaw remains under 6%.

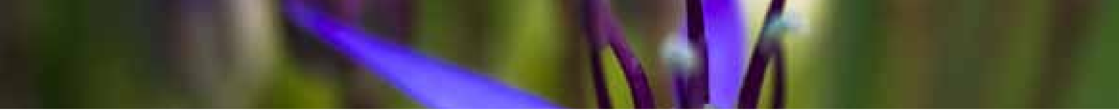
After the record year of 2001, completed units in Warsaw fluctuated between 10,000 and 15,000 for several years. In 2007 unit completions increased to 15,729 and to 18,000 for both 2008 and 2009. But in 2009 unit starts were starkly curtailed, resulting in the delivery of just 10,000 units in 2010.

According to market data the average price of apartments on the primary residential market in Warsaw is currently at a level of PLN 7,900/m^2, with the highest unit prices observed in Śródmieście (PLN 14,300), and the lowest in the Białołęka district (PLN 6,000).

The average price reported in the secondary market is slightly lower, at around PLN 7,800/m^2 for average-sized two-room apartments. More attractive locations (Śródmieście, Mokotów, and Wilanów) exceed PLN 9,000/m^2. Investors will be keen to watch sales of the most prestigious locations, where by the end of 2008 asking prices had reached levels as high as PLN 20,000/m^2; a price level not seen lately.

Since 2007 annual demand had been below supply in Warsaw. The boom of the prior few years had pushed prices to a level where the average monthly income of a Warsaw resident bought roughly one-half a square meter of an average-priced flat. This suggests that recent declines are less a sign of overbuilding, than of diminishing affordability.

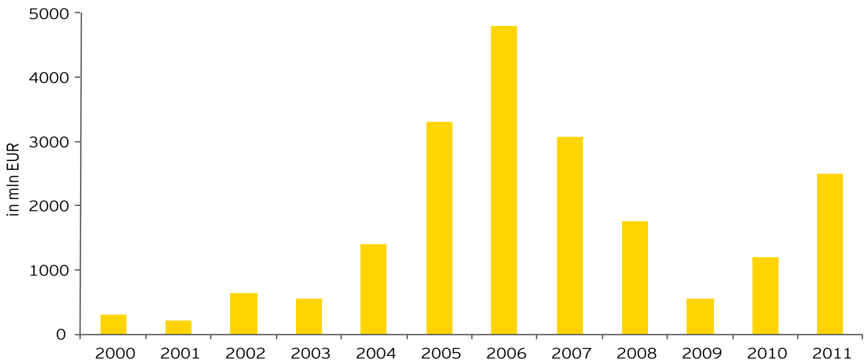
We observed increase in the number of completed and unsold permits offered in 2011 (over 4,000 in Warsaw), therefore the supply level is high. According to the Ministry of Infrastructure the popular mortgage-assistance program called "Family on its Own" will expire in 2012 which might have negative impact on demand in next few years.



1.5. Investment market

Initially, development of Polish commercial investment market trailed behind the rest of the real estate market. Investors were few and yields were in the double digits. It was not until 2004 and the advent of EU membership that the situation improved. That year marked the beginning of an intensive four year period of foreign investment in the Polish market. Over this period, the volume of transactions averaged just under EUR 4 billion a year; a far cry from 2001 when foreign investments were more or less limited to the Warsaw office market. Furthermore, the early years saw the commercial investment market plagued with a lack of available investment schemes, or mismanaged and overrented properties with high vacancy rates. The increasing number of transactions has not only stabilized investments, but completely changed the structure of yields (downward) and prices (upward).

Total investment in all sectors (office, retail, warehouse) volume 2000–2011



Source: Ernst & Young

The question for investors going forward is, will Poland bounce back from the 2008 and 2009 drop or have the fundamentals of pricing charged forever. Early indications suggest a slow but sustained comeback.

Warsaw remains an important transaction market in Poland, but smaller scale properties in secondary towns continue to gain ground. In 2011 the total volume of investment transactions in Poland amounted to approximately EUR 2,5 billion. The major investment activity was observed in the retail sector.

Transactions included both developers exiting fully let and pre–let buildings, and the conclusion of sale and lease-back agreements. It is expected that once the transaction market recovers from the current slow-down, the number of sale and lease back transactions will grow, helped in part by new legislation that will allow longer fixed lease terms (see section 2.6.). While the commercial incentives for sale and lease-back transactions have been present all along, the practice usually becomes more popular in an environment of low yields, which makes such deals more attractive to owner-occupiers.

Major investors

The main players on the real estate investment market are foreign investment funds, and to a limited extent insurance companies, banks and wealthy foreign individuals.

The Polish Act on Investment Funds allows Polish operated and registered funds to invest in real estate or in companies holding real estate assets without any specific limitations; as in the case of Arka (BZ WBK), BPH, KBC and Skarbiec.

The majority of real estate investment funds operating in Poland are foreign funds treating their properties as investments in accordance with the legal regulations of their countries of origin. Their subsidiaries in Poland work under the standard regulations of the Code of Commercial Companies and thus investments in real estate are subject only to the Act on Purchase of Real Estate by Foreigners.

Prior to 2005 the investment market was dominated by German, American, and Austrian players. After EU accession Poland witnessed an initial influx of Irish investors, later accompanied by Spanish and British investors. By 2009 the trend seemed to have reversed; German funds have emerged well intact while the Irish, and even more so the Spanish investors, appear to be hampered by their own markets back home.

The largest real estate funds active in Poland include AIB PPM, Akron Investment, Apollo Rida, DB Real Estate, GE Real Estate, DEKA Immobilien, Arka (BZ WBK), Fundusz Rynku Nieruchomości and Unibail Rodamco.

Major real estate funds investing in Poland

Name	Segment	Major Assets in Poland
AIB Polonia Property Fund	Office Warehouse	Poznań Financial Centre in Poznań Lubicz Office in Krakow Atrium Plaza (office) in Warsaw Atrium Centrum (office) in Warsaw Diamond Business Park Łódź (warehouse park) Wiśniowy Business Park (offices C, D, E, F) in Warsaw
Aviva Central European Property Found/Morley Fund Management	Office	Irydion in Warsaw, Wiśniowy Business Park A in Warsaw

Name	Segment	Major Assets in Poland
CA Immo	Office Warehouse	Warsaw Financial Center, Bitwy Warszawskiej (office) in Warsaw, Saski Crescent (office) in Warsaw, Saski Point (office) in Warsaw, Sienna Center (office) in Warsaw, Warsaw Towers (office) in Warsaw, Lipowy Office Park in Warsaw, Europolis Park Błonie (warehouse park)
Heitman European Property Partners	Office Retail Warehouse Residential	Empark (office park) Wiśniowy Business Park (building F) Żerań Park I (warehouse park) 7 Casino Shopping Centers (retail centers) in: Bydgoszcz, Warsaw (Ursynów), Janki, Katowice, Wrocław, Szczecin and Krakow
Endurance Fund (Orco Property Fund)	Office Warehouse	Orco Tower in Warsaw Prosta 69 Business Center in Warsaw Ożarów Business Centre in Warsaw Galeria Orkana in Lublin
Akron Investment CEE Fund	Office Warehouse Retail	Warsaw Trade Tower (office) Bokserska Office Center Bokserska Distribution Park Cybernetyki (office) Łopuszańska (office) Europlex (office) Crown Point (office) Crown Tower (office) Łopuszańska Distribution Center Manhattan Business & Distribution Centre Poznań Business Center ETC shopping centers (Swarzędz, Gdańsk)
Atlas Estates	Office Residential	The Hilton Warsaw Hotel and Convention Centre in Warsaw, Millenium Plaza (office) in Warsaw, Sadowa Office Building in Gdańsk, Platinum Towers in Warsaw

Name	Segment	Major Assets in Poland
Arka Investment Funds	Office Warehouse Retail Residential	Trinity Park (office) in Warsaw Aleje Ujazdowskie 10 (office) in Warsaw FDS Plaza (office) in Warsaw Winogrady Business Center (office) in Poznań Alfa Plaza (office) in Gdynia Quattro Forum (office) in Wrocław Centrum Logistyczne Ożarów (warehouse) Salvator City (residential) in Krakow Galeria Łomża Galeria pod Dębami (shopping center) in Warsaw Alfa Centrum (retail centre) in Olsztyn Pasaż pod Błękitnym Słońcem (office) in Wrocław Aleksandrowska 67/93 (office) in Łódź Puławska 435A (office) in Warsaw Red Tower (office) in Łódź Jutrzenki Business Park (office) in Warsaw
Castle Carbery Properties	Office	Antares Building Mokotów (office) in Warsaw Cirrus Building (office) in Warsaw Bliski Centrum (office) in Warsaw
DB Real Estate	Commercial Residential	Brama Zachodnia (office) in Warsaw Kopernik III (office) in Warsaw Kopernik IV (office) in Warsaw Galeria Dominikańska (shopping center) in Wrocław Galeria Łódzka (shopping center) in Łódź
DEGI	Office	Metropolitan in Warsaw Marynarska Business Park
RREEF	Office	Focus in Warsaw, Topaz in Warsaw, Nefryt in Warsaw, Grunwaldzki Center in Wrocław
Atrium European Real Estate (former Meinl European Land Limited)	Retail	Shopping centers in Warsaw, Bytom, Płock, Śrem, Olkusz, Piła, Siemianowice Śl., Świętochłowice, Tczew, Zamość, Toruń Shopping centers' Projects in Białystok, Lublin, Gdańsk
Unibail Rodamco	Retail	Galeria Mokotów in Warsaw, Złote Tarasy in Warsaw, Arkadia in Warsaw, Warszawa Wileńska in Warsaw
SEB Investment	Office	RiverSide Park in Warsaw, University Business Center in Warsaw, Trinity Park in Warsaw, Salzburg Center in Warsaw, Akrońska Business Park i Gdańsk, Philips Office Building in Łódź
MGPA	Office Retail Residential	Rondo 1 in Warsaw, CH Karolinka in Opole, Pogoria in Dąbrowa Górnicza, CH Janatar in Słupsk, Wilanów one In Warsaw, Angel Wings in Wrocław

Name	Segment	Major Assets in Poland
DEKA Immobilien	Office	Andersia Tower (office) in Poznań, Bema Plaza (office) in Wrocław, Deloitte House(office) in Warsaw, Grzybowska Park (office) in Warsaw
First Property	Office Retail	Oxford Tower (office) in Warsaw, Prokom Headquarters (office) in Gdynia, Krakow Business Park (office) in Krakow, Centrum Zana (office) in Lublin, Wallenroda Office Building (office) in Lublin, Żoliborz Plaza (office) in Warsaw, Galeria Ostrowiec (retail) in Ostrowiec Św., City Shopping Center (retail) in Włocławek
BPH FIZ	Office Retail Warehouse	Rodan (office building) in Warsaw Ideal Idea Park (logistics) Onyx (office building) in Krakow Viking House (office) in Warsaw Centrum Krakowska (retail) in Warsaw Renaissance Tower (office) in Warsaw

Source: Ernst & Young

Over the past several years, economic developments and political stability have played a key role in the increase of transactions, noting such factors as:

- EU membership;
- falling PLN interest rates;
- investors seeking to buy at high yields and sell at lower yields, expecting convergence with EU levels (i.e. cap rate compression).

While rising prices from cap rate compression have exceeded even the most aggressive expectations, by the third quarter of 2007 the economy had lost some of its momentum.

By 2008 financial turmoil around the globe had placed many investors in the "wait and see" mode, and this is only now showing signs of change.

Office properties

Capitalization rates had seen a steady decline in Warsaw from the double digit days of 1995 to 2002. They broke the 10% mark for the first time in 2003, and went on to shed roughly a percentage point a year until 2007, when deals as low as 5.5% were struck for the best performing properties, and prime office yields hovered between 6 and 6.5%.

In 2009 only a few transactions took place, mostly initiated before the crisis. Year 2010 showed a significant increase in activity of investors. Capitalization rates generally appear to be around 7%. In 2011 prime office yields for CBD locations were in the rage of the same level as year before.

Major office building transactions in Warsaw, 2011

Building	Location	Seller	Purchaser
Focus	City center Al. Armii Ludowej	Aberdeen Immobilien	RREEF Investement
Park Postępu	Non-central ul. Postępu	Echo Investment	Immofinanz
N-21	City center ul. Nowogrodzka	SwedeCenter	IVG Funds
Miasteczko Orange	Non-central Al. Jeorozolimskie	Bouygues Immobillier	Qatar Holding
Moniuszki Tower	City center ul. Moniuszki	Baltic Property Trust	Catalyst Capital
Atrium International Business Center	City center Al. Jana Pawła II	PRICOA Property Investment Management	Rockspring Property Investment Managers
Stratos Office Center	City center ul. Skorupki	Pramerica	Silverstein Properties JV Kulczyk Investment House
Mokotowska Square	City center ul. Mokotowska	Yareal	Deka Immobilien
North Gate	Non-central ul. Bonifraterska	Austrian Volksbank Group	Deka Immobilien
Zebra Tower	City center Rondo Jazdy Polskiej	S+B Gruppe	Union Investment
BTC Office Center	Non-central Al. Niepodległości	BTC Invest	IVG Funds
Aleje Ujazdowskie	City center Al. Ujazdowskie	ARKA BX WBK	IVG Funds
Equator	City center Al. Jerozolimskie	Karimpol	Immofinanz
Canal +	Non-central ul. Stawki	Hochtief Polska	Emir 23

Source: Ernst & Young

In terms of regional cities, investors are more cautious and prefer to buy A-class properties well leased and centrally located in large cities. After 2010, when three investment transaction took place, year 2011 did not bring any transaction in the regional cities.

Retail properties

Significant investment in the retail market did not start until 2001. The first major transactions were investments by Rodamco in Galeria Mokotów and in Złote Tarasy that took place in 2003, with capitalization rates at a the level of 9–10.5%.

Since that time nearly every significant property in Warsaw and other Polish cities has been the subject of a transaction. By 2005 capitalization rates were pushed downward to roughly 8% and continued this downward trend through Q3 2008 when they ranged between 5.7% and 6.5%. Due to the crisis, the capitalization rates has increased by approximately 1–1.5%.

In 2011 the value of retail portfolio transactions amounted to almost 50% of the total investment transaction volume in Poland. The major modern retail transactions are presented in the table below. Capitalization rates generally appear to be around 7-7.5%. In 2011 prime retail yields were in the range of 6-6.5%.

Major modern retail transactions, 2011

Building (Location)	Seller	Purchaser
Promenada Warszawa	Carpathian Fund	Atrium European Real Estate
Galeria Mokotów Warszawa	GTC	Unibail-Rodamco
Magnolia Park Wrocław	Octava NFI/Legnicka Development	Blackstone
Wzorcownia Włocławek	Budizol	Blackstone
Galeria Pestka Poznań	Mobel Walther AG	Blackstone
Galeria Twierdza I Zamość	Rank Progress	Blackstone
Galeria Twierdza II Kłodzko	Rank Progress	Blackstone
Galeria Tęcza Kalisz	Rank Progress	Blackstone
Galeria Echo Pabianice	Echo Investment	PH 3
Galeria Osowa Gdańsk	Carpathian, IVG	Pradera
Galeria Tulipan Łódź	GE Capital Real Estate	Pradera
Galeria Kometa Toruń	GE Capital Real Estate	Pradera

Source: Ernst & Young

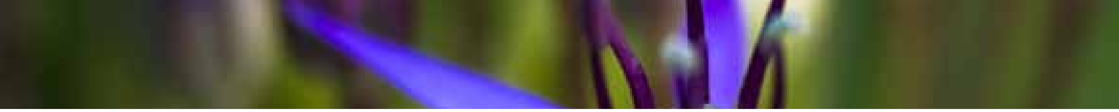
Warehouse properties

The warehouse market has historically been perceived as the least mature of the real estate sectors, with only a few significant transactions closed. The low transaction level may be partly explained by the large number of built-to-suit properties which are either owner-occupied or presold by funds before construction is complete, therefore these trades never show up on the transaction radar screen.After the crisis year – 2009 – when only one transaction was registered in the modern warehouse/industrial sector, 2010 showed a major increase in investor activity. In 2011 there were only a few investment transactions observed. Capitalization rates for the modern, best performing properties are around 8,5%.

Major warehouse space transactions, 2011

Building	Location	Seller	Purchaser
Panattoni Park (BTS for Tesco)	Gliwice	Panattoni	Invesco
Epedal Gliwice	Gliwice (sub zone of Katowice Special Economic Zone)	Epedal	Fronius
Gefco Logistic Center	Grodzisk Mazowiecki	Invista European Real Estate	NGBI Private Equity Limited
Europolis Park Błonie	Błonie	Europolis	CA Immo
Panattoni portfolio	Pruszków, Łódź, Poznań	Panattoni	Episo

Source: Ernst & Young



1.6. Key cities in Poland

Warsaw	
Population	1,720,398
Unemployment	3,5%
Major industries	Trade and services
Major companies	Anwim, Bank Pekao, BGŻ, BRE Bank, British American Tobacco, Budimex, Bumar Citibank, Coca-Cola Beverages, Colgate, Palmolive Poland, France Telecom, General Motors, Grupa Żywiec, GTC, Huta Arcelor Warszawa, IBM, ING, Kompania Piwowarska, Kraft Foods Polska, Mostostal Export, Nestle Polska, PGNiG, PKO BP, PLL LOT, Polkomtel, Procter & Gamble PZU, RWE Polska, Samsung Electronics Polska, Shell, Skanska, Strabag, T-Mobile, Unilever Polska
Office sector	
Rental level (m^2/month)	EUR 22 - 25 (class-A space) EUR 12 - 16 (class-B space)
Total office Stock	3,500,000 m^2 of modern space
Current supply	Adgar Plaza, Atrium complex, Batory Office Buildings, Blue Office, Catalina Office Center, Cristal Park, Deloitte House, Dominanta Praska, EMPARK, Equator I, Focus Filtrowa, Grzybowska Park, Harmony Office Center, Horizon Plaza, IO-1, Jerozolimskie Business Park, Kopernik Office Buidlings, Lipowy Office Park, Lumen, Marynarska Business Park, Marynarska Point, Metropolitan, Milennium Plaza, Mokotów Business Park, Mokotów Plaza, Nefryt, North Gate, Ochota Office Park, Okęcie Business Park, Park Postępu, Platinium Business Park, Poleczki Business Park, Puławska Financial Center, Rondo 1, Saski Crescent, Saski Point, Skylight, Trinity Park, Tulipan House, Warsaw Financial Center, Warsaw Trade Tower, Wiśniowy Business Park, Wolf Marszałkowska, Zebra Tower
Future supply	Ambassador, Atrium One, Business Garden, Chmielna Development Tower, Concept Office Park, Domaniewska Business Center, Eurocentrum Office Coplex, Feniks, Green Corner, Hortus, Karolkowa Business Park, Libra Business Center, Miasteczko Orange, Okęcie Business Park, Senator, Warsaw Spire, Wilanów Office Park
General vacancy level	7%

Retail sector	
Rental level (m²/month)	EUR 65 - 85 for prime shopping center units Up to EUR 75 for prime street units
Total retail stock	1,500,000 m² of modern space
Current supply	Arkadia, Blue City, CH Bemowo, CH Janki, CH Reduta, CH Targówek, CH Wileńska, Dom Towarowy Braci Jabłkowskich, Fort Wola, Galeria Mokotów, King Cross, Klif, M1 Marki, Promenada, Sadyba Best Mall, Wola Park, Wolf Bracka, Złote Tarasy
Future supply	CH Białołęka (Arkadia bis), Factory Annopol, GTC/Polnord Wilanów, Hala Koszyki (reconstruction), Retail Park in Łomianki, Tesco Kabaty (extension),
Warehouse sector	
Rental level (m²/month)	EUR 2.5 -5.5
Total warehouse stock	2,600,000 m²
Current and planned supply in Warsaw area	Annopol Logistic Park, City Point, Diamond Business Park Piaseczno, Diamond Business Park Warsaw, Europolis Park Błonie, Krakowska Distribution Center, Łopuszańska Business Park, Manhattan Business and Distribution Center, Millenium Logistic Park Pruszków I, II, Panattoni Park Ożarów, Panattoni Park Błonie I, II, Panattoni Park Garwolin, Panattoni Park Pruszków, Panattoni Park Teresin, Platan Park I, II, ProLogis Park Błonie, ProLogis Park Nadarzyn, ProLogis Park Sochaczew, ProLogis Park Teresin, ProLogis Park Warsaw I, II, III, Tulipan Park Warszawa, Żerań Park I, II, III
Krakow	
Population	756,183
Unemployment	4.7%
Major industries	Tourism, steelworks and metallurgy, tobacco, pharmaceuticals, IT
Major companies	Bayer, Can Pack, Coca-Cola Niepołomice, ComArch, Delphi, Google, HSBC, Huta im. Sędzimira, International Paper, Motorola, Philip Morris, Pliva, Shell, UBS, Vistula & Wólczanka, Wawel
Office sector	
Rental level (m²/month)	EUR 14 - 15 (class-A space) EUR 10 - 12 (class-B space)
Total office stock	490,000 m² of modern space

Current supply	Centrum Biurowe Lubicz, Galileo, Newton, Edison, Centrum Biurowe Euromarket, Cracovia Business Center, Nowe Herbewo, Azbud Business Center, Buma Square, CBil Copernicus, Brama Bronowicka, Krakow Business Park 200, 400, 800 and 1000 (Zabierzów), Rondo Business Park (Phase A, B, C) Nowa Kamienica, Wielicka 72, Onyx, Alstar Office Center, M65 Meduza, Portus, Diamante Plaza, Avatar, Kazimierz Office Center
Future supply	Enterprise Park, Bonarka4Business, Quattro Business Park II, Azbud Business Center (Phase II), Kamińskiego 47, Green Office, Alstar Business Center, Avia, Pascal
General vacancy level	8%

Retail sector	
Rental level (m^2/month)	EUR 35 - 45 for prime shopping center units EUR 50 - 80 for prime street units
Total retail stock	510,000 m^2 of modern space
Current supply	Galeria Krakowska, Galeria Kazimierz, CH Krokus, CH Zakopianka, M1, IKEA, Krakow Plaza, CH Czyżyny, Solvay Park, CH M1, Castorama, CH Wielicka, Bonarka
Future supply	Serenada Shopping Center, Cracow Futura Park, Factory Outlet

Warehouse sector	
Rental level (m^2/month)	EUR 2.8 - 3.0
Total warehouse stock	110,000 m^2
Current and planned supply	Logistic Center Kraków I, II, III, Karków Airport Logistics Centre, MARR Business Park, MK Logistics Park, Panattoni Park Kraków

Poznań	
Population	551,627
Unemployment	3.6%
Major industries	Food processing, electrotechnical, chemical, automotive, retail, services (including finance and banking), construction industry, location of major trade fairs in Poland
Major companies	Aluplast Austria, Beiersdorf, Bridgestone, Carlsberg, CPC International, Enea, GlaxoSmithKline, IKEA, Kompania Piwowarska, Lorens Bahlsen, Międzynarodowe Targi Poznańskie, Nestle, Volkswagen, Wrigley, Wyborowa

Office sector	
Rental level (m^2/month)	EUR 14 - 16 (class-A space) EUR 10 - 13 (class-B space)
Total office stock	240,000 m^2 of modern space
Current supply	Dwór Hamburski, Globis, Poznańskie Centrum Finansowe, Kupiec Poznański, PGK Centrum I & II, Centrum Biznesu, Futura Business Plaza, Winogrady Business Center, Delta, Stary Browar, Andersia Tower, Domina Prestige, Citi Park Poznań, Alfa Office Building, Nowe Garbary, Westpoint, Omega
Future supply	Andersia Business Center, Murawa Office Park, Centrum Obsługi Biznesu Bałtyk, Deptak, Maraton Business Center, Corner Point

Retail sector	
Rental level (m^2/month)	EUR 35 - 50 for prime shopping center units EUR 45 for prime street units
Total retail stock	520,000 m^2 of modern space
Current supply	Stary Browar, Poznań Plaza, King Cross Marcelin, Kupiec Poznański Auchan - Swadzim and Komorniki, ETC - Swarzędz, M1, IKEA, CH Franowo, Galeria Panorama, CH Piątkowo, Factory Outlet - Luboń, Galeria Podolany, Galeria Pestka, CH Malta, Green Point
Future supply	CH Łacina, CH Metropolis, Bulwary Poznańskie, Galeria A11, Galeria MM, Poznań Główny

Warehouse sector	
Rental level (m^2/month)	EUR 2.8 - 3.0
Total warehouse stock	900,000 m^2
Current and planned supply	CLIP Poznań,Doxler Business Park, Millennium Logistic Park Poznań, Panattoni Poznań I, II, III, Panattoni Robakowo, Park Magazynowy Logit, Point Park Poznań, ProLogis Park Poznań I, II, III, ProLogis Park Września, Tulipan Park Poznań I, II

Tri-City	
Population	742,432
Unemployment	4.9%
Major industries	Maritime industry, fuel industry, construction, food processing, tourism, IT

Major companies	Stocznia Północna, Baltic Malt, Baltis Investment, Blue Media, Bomi, DGT, Dr Cordesmeyer, Elektrociepłownia Wybrzeże, Elektromontaż, Energa, Fazer, Gdańska Stocznia Remontowa, Gdańskie Zakłady Nawozów Fosforowych, GE Money Bank, Grupa Lotos, Hydrobudowa Gdańsk, Hydroster, IKEA, Intel Technology Poland, Jysk Polska, Lido Technology Poland, LPP, Metro AG, Mostostal Gdańsk, Neste, PepsiCo, Satel, Shell, Siarkopol, STU Ergo Hestia, Tengelmann
Office sector	
Rental level (m^2/month)	EUR 12 – 15 (class-A space) EUR 8 – 11 (class-B space)
Total office stock	330,000 m^2 of modern space
Current supply	Allcon@Park, Allcon Dmowskiego Centrum, Sadowa Office Park, Centrum Biznesu Centromor, Hossa Company House, Torus, Organika Trade, Zieleniak, Haxo, Artus Park, Vigo Centrum Biurowe, Lotos HQ, Alfa Plaza Business Center, Ancora, Baltic Business Center, Centrum Biurowe Hossa, Centrum Kwiatkowskiego, Chipolbrok, Gdyńskie Centrum Biznesu, Morska Centrum, Prokom HQ, City Arcade, Krzywy Domek – Rezydent, Hestia HQ, Ka5, Łużycka Office Park I & II, Arkońska Business Park I & II, Centrum Biurowe Grunwaldzka, Abrahama Office Building, Janka Wiśniewskiego Office Buidling, Hynka Office Building
Future supply	BCB Business Park, Chmielna Office Point, Granary Island Business Center, Oliva Business Park, Olivia Gate
Retail sector	
Rental level (m^2/month)	EUR 35 – 50 for prime shopping center units EUR 15 – 35 for prime street units EUR 6 – 13 for retail park units
Total retail stock	510,000 m^2 of modern space
Current supply	Small shops and boutiques along shopping streets (Świętojańska in Gdynia, Długa and Grunwaldzka in Gdańsk as well as Monte Casino in Sopot) Modern shopping centers: Galeria Bałtycka, Port Rumia, CH Klif, Batory, ETC, City Forum, Krewetka Cinema City, Alfa Center, Madison Shopping Gallery, CH Manhattan, Centrum Kwiatkowskiego, CH Wzgórze, Matarnia Retail Park, Osowa Shopping Center, Centrum Rodzinne Witawa, Fashion House Gdańsk, Castorama, Real, Tesco, Selgros Cash and Carry, Tesco Chełm, IKEA, CH Oliwa, Galeria Przymorze, Centrum Haffnera
Future supply	CH Wzgórze (extension), Morski Park Handlowy

Warehouse sector	
Rental level (m²/month)	EUR 3.2 - 3.5
Total warehouse stock	140,000 m²
Modern warehouse stock under construction	ProLogis Park Gdańsk, Centrum Logistyczne Pruszcz Gdański, Panattoni Park Gdańsk, SEGRO Logistics Park

Łódź	
Population	737.098
Unemployment	10,0%
Major industries	Textile & clothes, food processing, mechanical engineering, chemical production, trade fairs
Major companies	ABB, Amcor, Bosch-Siemens Hausgeräte, Cacao Berry, Coca-Cola, Dell, Grupa Atlas, Idesit, Infosys, Phillips, Polish Pharmaceutical Group Pollena-Ewa S.A., Sanitec Koło, Textilimpex, VF Polska, Vistula & Wólczanka,

Office sector	
Rental level (m²/month)	EUR 11 - 14 (class-A/B space)
Current supply	Orion, Centrum Biznesu, Centrum Biznesu Faktoria, Phillips - Europejskie Centrum Usług, Red Tower, TUiR Warta, Lumiere Center, Secesja 89, Piotrkowska 270, Centrum Targowa, Pl. Wolności, Aleksandrowska, Biurowe Centrum Biznesu (BCB), Gdańska 47, Textorial Park, Orange Plaza, Centrum Biznesowe Synergia (phase I), Łódź Business Center, ING HQ, Citi Bank HQ, Aviator, Centrum Biznesu Inter-Mar, Forum 76, Sterlinga Business Center, University Business Park
Future supply	Przędzalnia Braci Muehle, Real Office, Sienkiewicza 65, Park Biznesu Teofilów

Retail sector	
Rental level (m²/month)	EUR 35 - 50 for prime shopping center units EUR 28 - 35 for shopping center units
Current supply	Small boutiques along Piotrkowska street Modern shopping centers: Manufaktura, Galeria Łódzka with Tesco, Tulipan Center with Real, Pasaż Łódzki with Real, M1 with Real, E. Leclerc, CH Carrefour Przybyszewskiego, OBI, Praktiker, Castorama, Leroy Merlin, Makro Cash & Carry, Selgros Cash & Carry, CH Ptak in Rzgów, CH Guliwer, CH Tesco Bałuty, CH Tesco Widzewska, Port Łódź

Future supply	Fabryka Biznesu
Warehouse sector	
Rental level (m^2/month)	EUR 2.8 - 3.8 for modern space
Current and planned supply in Central Poland region	900,000 Business Park Łódź, Diamond Business Park Łódź, Diamond Business Park Stryków, Panattoni Business Center Łódź, Panattoni Łódź East, Panattoni Park Łódź South, Parkridge Business Center, ProLogis Park Stryków, Tulipan Park Łódź, Tulipan Park Stryków
Wrocław	
Population	632,996
Unemployment	5.5%
Major industries	automotive, IT, business process offshoring, pharmacy/medical assortment, finances, medical machinery production, electrical, metallurgy, house appliances and food processing
Major companies	3M, Alcatel, Bosch, BZ WBK, Cadbury, Credit Agricole, Eurobank, Google, Hewlett-Packard, KRUK, LG, MacoPharma, Polifarb, Siemens, Toyota, Ultimo, US Pharmacia, Volvo, Wabco, Whirlpool
Office sector	
Rental level (m^2/month)	EUR 14 - 15 (class-A space) EUR 11 - 13 (class-B space)
Total office stock	400,000 m^2 of modern space
Current supply	Renaissance Business Center, Quattro Forum, Silver Forum, Wrocławski Park Biznesu 2 (phase I), Legnicka Business House, Bema Plaza, Millenium Tower, FIG Plaza, Wratislavia Center, Wratislavia Tower, Centrum Orląt, Times, Cuprum Novum, Centrum Biurowe Globis, Grunwaldzki Office Center, Wojdyła Business Park
Future supply	Heritage Gates, Wrocławski Park Biznesu 2(phase III), Brama Południowa, Wojdyła Business Park, Centrum Biurowe Karkonoska, Verity Business Center, Green Towers, Gamma
Retail sector	
Rental level (m^2/month)	EUR 45 - 55 for prime shopping center units EUR 40 - 50 for prime street units EUR 8 - 10 for retail park units
Total retail stock	500,000 m^2 of modern space
Current supply	Pasaż Grunwaldzki, Arkady Wrocławskie, Magnolia Park, Factory Outlet, CH Korona, Bielany Retail Park (IKEA), Auchan Bielany, Galeria Dominikańska, Szewska Center, Kaufland, CH Borek, TGG, Tesco, E. Leclerc, IKEA, CH Marino, Renoma (after modernization)

Future supply	Galeria Strzegomska, Galeria Idylla, Promenada Wrocławska, Outlet Village
Warehouse sector	
Rental level (m^2/month)	EUR 2.8 - 3.0
Total warehouse stock	570,000 m^2 of modern space
Current supply	ProLogis Park Wrocław (I & II) – Bielany Wrocławskie, Parkridge Business Center, Tiner Logistic Center – Pietrzykowice, Panattoni Park Wrocław – Bielany Wrocławskie

Katowice	
Population	306,826
Unemployment	3.8%
Major industries	Coal mining, metallurgical, steel, machinery, electrical, ceramic, automotive, printing, information and IT
Major companies	Cartotecnica Polska, Delphi Automotive System, DuPont, Electrabel Polska, Elektromontaż 1 Katowice, General Motors, GK Farmakol, GK Tauron Polska Energia, Isuzu Motors, Katowicki Holding Węglowy, PepsiCo, Philips, Polski Koks,Powertrain Polska, Roca
Office sector	
Rental level (m^2/month)	EUR 12 – 14 (class-A space) EUR 8 – 11 (class-B space)
Total office stock	260,000 m^2 of modern space
Current supply	Chorzowska 50, Altus, Millennium Plaza, Opolska 22, Korfantego 2, Green Park, Francuska Office Center, Katowice Business Point
Future supply	Silesia Business Park, Brynów Center
Retail sector	
Rental level (m^2/month)	EUR 40 – 45 for prime shopping center or street units EUR 9 – 12 for retail park units
Current supply	Silesia City Center, 3 Stawy, CH Dąbrówka, Castorama, OBI, Media Markt, Park Handlowy RAWA (IKEA), Dom Handlowy Zenit, Galeria Auchan
Future supply	Galeria Katowicka, Supersam (renovation)

Warehouse sector	
Rental level (m^2/month)	EUR 2.5 - 3.0
Total warehouse stock	1,075,000 m^2
Current and future supply in the Upper Silesia region	Tulipan Park Gliwice, Panattoni Park Gliwice, ProLogis Park Będzin I & II, ProLogis Park Sosnowiec, ProLogis Park – Dąbrowa Górnicza, ProLogis Park Chorzów, ProLogis Park Ujazd, Diamond Business Park Gliwice, Cross Point Distribution Center Żory, Millenium Logistic Park Tychy, Alliance Logistic Center Silesia, Panattoni Park Czeladź, Panattoni Park Mysłowice, Panattoni Park Bielsko-Biała

2. Legal and tax aspects of investing in real estate

This Chapter considers the most important legal and tax issues arising during each of the following five stages of a real estate investment:

- Financing
- Acquisition
- Development and Construction
- Operation and Exploitation
- Sale

The Chapter is arranged such that each of the above aspects are dealt with in separate sections (2.3.–2.8.), first considering legal implications, which are followed by an assessment of related important tax consequences.

The section on legal background (below) will introduce the reader to certain concepts and terms that may not be commonplace in transactions elsewhere in Europe and this should be read as a general introduction to the legal environment in Poland. The chapter also considers section 2.2. on investment vehicles and structures presenting information on most common structures used for investing in real estate in Poland, which form the basis of understanding the most relevant legal and tax implications.

Legal, financial and tax due diligence are also fundamental to any investment cycle and given the importance of due diligence to any transaction, we discuss the relevant procedures and key considerations in detail in section 2.9.

2.1. Legal background

Polish real estate law is stable and predictable, allowing investors to navigate through and avoid potential risks arising in real estate transactions. This section discusses certain fundamental underlying legal concepts regarding real estate dealings in Poland and should be referred to when reading other chapters.

2.1.1. Legal titles – overview

As with most European jurisdictions, full "freehold" ownership and leases are common. However, the right of perpetual usufruct (RPU) is specific to certain countries, including Poland. The RPU concept constitutes a freely transferable form of legal title, similar to full ownership. Polish real estate law also provides a number of common limited rights, such as easements.

Polish law includes a number of statutory protections for the new owners of a property against claims made by third parties. One such protection is the registration of legal title to the property in a Land and Mortgage Register, kept by a court. The register is based on a principle that protects the purchaser of real estate from a registered title-holder against third party claims and guarantees the validity of the title acquired, provided that the purchaser acted in good faith (the rule of public reliance upon land and mortgage registers).

In practice, investors may also obtain title insurance against loss caused by any defects in the title to a property. Insurance is now readily available with respect to most title defects and is no longer an unusual component of commercial transactions.

Ownership title

Ownership title in Poland is like "Eigentumsrecht" under German law or "propriété" under French law, and is very similar to the English legal concept of "freehold" title. It constitutes the broadest possible right over Polish real estate, and entails the right to possess, use, encumber, transfer and dispose of the real estate, deriving benefits and income as appropriate and subject only to specific limitations laid down by law. Ownership title is regulated by the Polish Civil Code, which is the main legislative act governing property rights.

Right of perpetual usufruct

The right of perpetual usufruct is a regular right regulated by the Polish Civil Code and is very similar to ownership title although it has some characteristics of a longterm leasehold. An RPU-holder enjoys most of the rights that attach to full ownership title. It is possible to sell, transfer, mortgage, or otherwise encumber the RPU. In the event that a third party violates an RPU-holder's rights or submits claims against RPU-holder, the RPU-holder's enjoyment of the RPU is subject to the same legal protections available to the holder of an ownership title. In this respect in 2011 the Supreme Court declared that the rule of public reliance upon land and mortgage registers (please refer to tthe beginning of this section 2.1.1.) applies also to a RPU even if the establishment of the RPU by virtue of law was defective. Such jurisprudence provides a great additional comfort for RPU-holders as an RPU in Poland is very often established by virtue of law.

Despite certain differences from ownership title (described below), an RPU is equally popular for the purposes of real estate investment and is common in commercial transactions. Many foreign investors (including strictly-regulated German funds) have acquired or built multi-million-euro development projects on properties held under an RPU. It should be emphasised that the limitations affecting RPUs have not prevented foreign and domestic banks from financing projects involving RPU titles, and insurance companies are happy to provide buildings and title insurance for such projects.

Nevertheless, it should be noted that an RPU differs from ownership title in the following respects:

- where an ownership title-holder is the ultimate owner of the land, the ultimate owner of land subject to an RPU is the Polish State or the relevant local authority, (however, any buildings and other facilities developed by an RPU-holder on the land held under an RPU are owned by the holder of the RPU);
- an RPU is limited in time and can be granted for a maximum of 99 years, but not less than 40 years; the RPU-holder also has the right to claim an extension of the RPU for an additional 40 to 99 years; in practice, the risk of an extension to an RPU relating to a property developed by the RPU-holder being refused is remote, especially since upon the expiry of the RPU, the RPU-holder is entitled to recover the "market value" (determined by a qualified appraiser) of the buildings and facilities (unless developed in breach of the provisions of the agreement establishing the RPU);
- an RPU may restrict the use to which the land is put: the Polish State or local authorities may stipulate a designated use for the property, such as e.g. residential use, and, should the RPU-holder use the property in a manner contrary to its designated use, the RPU may be terminated prior to the lapse of its term; and
- an RPU-holder is obliged to pay charges to the ultimate owner.

Initial and annual fees related to RPU

Unlike ownership title, an RPU is subject to two types of fee:

- a one-off initial fee payable upon the establishment of the RPU (i.e. when the Polish State or local authority sells the RPU to its first holder) ranging from 15 to 25% of the property's value; and
- an annual fee, being a percentage of the land value excluding the value of any buildings or structures (the rate for residential use of real estate is 1% whereas for commercial use the rate is 3%).

Both the holder of the RPU and the Polish State or local authorities may request an adjustment of the annual fee (up or down), but only if the value of the land changes (improvements built on the land are not directly taken into account for the purposes of the land valuation). The land value for the purposes of adjusting the annual RPU fee must be established by a qualified surveyor and is based on a current market, comparative approach.

To give a complete picture of the RPU institution, it must be stated that through the years 2007 to 2011 the annual RPU fee grew dramatically, in some cases (mainly in the residential market) by as much as 200%. Such increases were due to the fact that there had been no adjustments in place for many years and, at the same time, the value of land had noticeably risen. For obvious reasons, the scale and volume of the increases of the annual RPU fees were negatively perceived by RPU holders. As a consequence, certain amendments were adopted in July 2011 and the RPU fee adjustments were limited in time (under the new regulations they are possible every three years) and in scale (if the new annual fee exceeds at least twice the current fee, the RPU-holder pays an annual fee equal to twice the current annual fee and the remaining amount exceeding double the current fee (excess) is divided into two equal parts, which will increase the annual fee over the next two years; consequently the annual fee for the third year of the update is equal to the amount resulting from this update).

Conversion of RPUs into ownership title

Since 9 October 2011 a legal entity can enforce the conversion of a RPU into an ownership right if it was the RPU-holder of a given property on 13 October 2005. Its legal successors are also entitled to make such a claim. However, it is not clear if the term "legal successor" applies to general succession only or also to the acquisition of real property through a sale agreement. Since the relevant regulations are very recent the question has not yet been settled through jurisprudence.

Obviously, such a conversion (in principle) will attract a fee, which would be equal to the difference between the value of the ownership right and the value of the RPU to a land, established by a qualified appraiser.

In some situations such conversion may be recommended, e.g. in order to establish the ownership right to separate premises in a building located on two properties – one held under a RPU and the second one under the ownership right (what is quite often the case).

Before 9 October 2011, any purchase by a legal entity of the ownership right to a property held under a RPU was uncertain and possible only if the authority was willing to sell. Such possibility still exists and does not involve legal succession issue.

Other forms of title

In addition to ownership title and an RPU, Polish law recognises other rights in property and certain limited contractual rights.

Usufruct

A usufruct (*użytkowanie*) is a restricted right in property which allows the holder to derive certain benefits (the right to use and collect profits) from the land, but which does not extend to full ownership rights. The right is non-transferable, and it expires if not exercised for a period of 10 years. It may be limited to a specific part of the land.

Easements

Easements over land are limited property rights. They may be granted over a piece of real estate ("Encumbered Property") for the benefit of another real estate ("Master Property"), and may thereby increase the usefulness or value of that Master Property. Easements may be:

- Active – where the owner of the Master Property is entitled to limited use of the Encumbered Property; (e.g. by passing through the Encumbered Property to gain access to the Master Property); or
- Passive – where the owner of the Encumbered Property is restricted in the exercise of its own rights for the benefit of the Master Property (e.g. the terms of the easement may dictate that the owner of the Encumbered Property may not construct a building above a certain height on the Encumbered Property).

It is important to note that easements (e.g. rights of way) are not always registered in the Land and Mortgage Register, and it is therefore always advisable to employ technical advisors to verify the existence of such easements by carrying out an on-site inspection during the due diligence exercise.

Utility Easements

Since August 2008 the Polish Civil Code has provided for easements for the benefit of utility providers. For example, if a utility provider asks a land owner to establish an easement over his land for the purpose of installing (and thereafter operating and maintaining) electricity cables, and the land owner refuses, the utility provider may apply to the court for an utility-specific easement under the new law, which facilitates the utility provider in obtaining such an easement. This may be of interest to investors in the energy sector, especially with respect to wind farm projects, which often require the use of a third party's land.

Leases and Tenancies

Leases are contractual arrangements concluded between a land owner and a lessee which permit the use of the real estate by the lessee for a period of time (fixed or indefinite) in return for rent. Under Polish Law, there are two types of lease agreements: lease (*umowa najmu*) and tenancy (*umowa dzierżawy*). These are discussed in more detail in section 2.6.

Leasing

The presence of international real estate investors in Poland has been instrumental in the proliferation of sophisticated and internationally-recognised investment and financing mechanisms. In this respect, leasing property is growing in popularity. Under leasing, the lessee enjoys the same property rights as a lessee under a lease. The main difference between the two arises in the contractual arrangements which confer those property rights, and in particular, the structuring of the remuneration. Instead of paying simple rent, a leasing agreement operates more like a hire-purchase agreement, with an agreed sum to be paid in instalments over the course of the leasing or, if the leasing is terminated, a lump sum at the end. There are two types of leasing that can be utilized by investors in Poland: financial leasing and operational leasing.

- Financial leasing – here the lessee pays contractual payments, and at the end of the leasing term has the option to purchase the property which was subject to the leasing;
- Operational leasing – similar to financial leasing, but with no option to purchase the property at the end of the term, which can be useful for tax purposes.

Typically, Polish finance providers are willing to offer leasing structures in relation to office buildings, commercial developments, warehouses, logistics centres, hotels, and industrial properties.

However, it is important that the structure selected is carefully considered from a tax, accounting, legal and business perspective.

2.1.2. Land registration

Land and Mortgage Register

The Land and Mortgage Register maintained by Polish courts constitutes a register of the legal status of Polish real estate, providing security and consistency for land transactions. The register includes necessary information on the history of the property: it identifies the land and lists all relevant ownership details (previous and current) and encumbrances, such as mortgages, personal rights and third party claims.

The Land and Mortgage Register is publicly accessible and, pursuant to the Land and Mortgage Register Act, its accuracy is warranted (although the warranty does not extend to the beneficiaries of land transfers for which no payment is made). This provides public reliance, such that everyone who acts in good faith may assume that the relevant entries in the Land and Mortgage Register are true and correct, and that they accurately disclose the legal status of the real estate. A party is considered as acting in good faith if it cannot be demonstrated that the party was aware of, or could easily become aware of, a discrepancy between the contents of the Land and Mortgage Register and the actual legal status of the property.

Land Register

The Land Register, maintained by municipalities, contains (and thereby determines) numerical and descriptive data on land, buildings, owners and RPU-holders. The data disclosed in the Land Register constitute the basis for entries into the Land and Mortgage Register. However, the content of the Land Register is for information purposes only, and is not subject to the protections afforded by the Land and Mortgage Register.

2.1.3. Acquisition of real estate by foreigners

Since Poland's accession to European Union (EU), most of the restrictions on real estate purchase have been lifted for the benefit of citizens and corporate entities of the European Economic Area (the EEA, which includes the EU, Norway, Iceland and Liechtenstein). Therefore, no governmental permits are required for EEA citizens and corporate entities, except for the purchase of: (i) agricultural; or (ii) forest land or a company (meaning assuming control over a company) holding such land.

In contrast, the acquisition of real estate in Poland by an entity from a country outside the EEA will generally require a governmental permit and an acquisition without a permit will be held as invalid. The only exceptions to this rule (relevant also for a legal entity) are where the acquisition: (i) is of an undeveloped plot located within city boundaries with an area not exceeding 0.4 hectares; (ii) is made by a foreign mortgage bank enforcing its security over the property; or (iii) is of an apartment for residential purposes.

Such a permit is granted in the form of an administrative decision issued by the Ministry of Internal Affairs and Administration. During the decision making process, which precedes the issuance of the permit, the Ministry of National Defence (and in the case of agricultural land, the Ministry of Agriculture) must be consulted.

Where a governmental permit is required to purchase real estate, it is possible to apply for a 'promise' to provide the permit, which guarantees for a period of 12 months that the Ministry of Internal Affairs will issue the permit.

2.1.4. Acquiring real estate from public entities

A significant proportion of the real estate in Poland is still owned by the Polish State and local authorities.

As a general rule, real estate held by the Polish State or a local authority can be sold only by way of a public tender (in the form of an auction or written bid process). However, there are certain exceptions to this rule which should be considered in specific circumstances. As the seller of a public property, the Polish State or local authority must act in a transparent way and publish information in advance on their websites and in the press about the properties for sale, the tender date and its terms and conditions.

A tender organised by a public authority must be run in accordance with the statutory requirements. One of the conditions which a potential investor must fulfil in order to participate in a public tender for the acquisition of real estate, is that it must provide the public authority with a tender guarantee in the form of a cash deposit or State Treasury bond or securities admitted to trading. The tender guarantee should be not less than 5% and not more than 20% of the initial price.

The tender guarantee paid by the successful bidder will be taken into account as part of the total purchase price. However, if the successful bidder fails to conclude the purchase agreement after winning the tender, the deposit will be kept by the public authority organising the tender. Tender guarantees paid by unsuccessful bidders will be returned to them. If a public authority cancels the tender, the tender guarantees are returned to all the bidders.

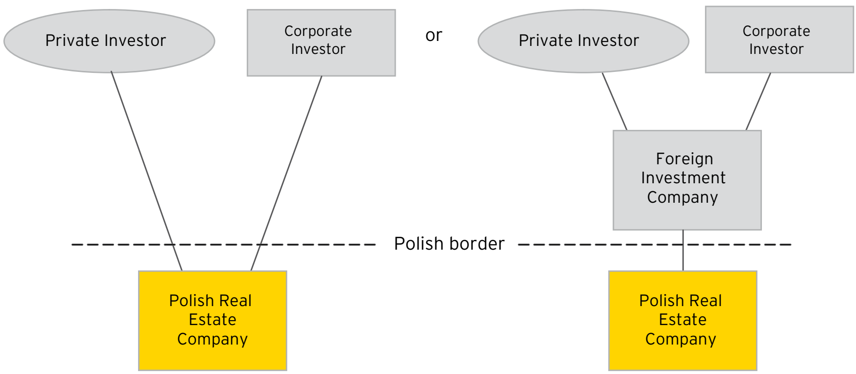
2.2. Investment vehicles and structures

2.2.1 Companies and partnerships

The most commonly used investment vehicle for real estate investment or development projects is a limited liability company (*spółka z ograniczoną odpowiedzialnością*). This is a separate legal entity in which the liability of the shareholders is limited to their contribution to the share capital of the company.

A Polish joint-stock company (*spółka akcyjna*) can also be used, and has in general the same tax status and characteristics, but is not so commonly used.

The following diagram shows the classic structures for foreign investments in Poland via companies:



The foreign investor (private or corporate) is either a direct shareholder in the Polish company, or holds shares in a foreign company controlling the Polish company.

Foreign companies are also allowed to operate branch offices or form partnerships in Poland. Recently, the latter option has become popular among investors.

2.2.2. Investment via flow-through partnerships

In recent years there has been increased interest in using flow-through partnerships (especially in the form of a limited partnership) to conduct business activity in Poland, mainly because of favourable tax treatment and the ability to limit the liability of partners.

A limited partnership (*spółka komandytowa*) is a partnership where at least one partner (the general partner) bears unlimited liability for the partnership's liabilities towards its creditors, and the liability of at least one partner (the limited partner) is limited.

A limited partnership is transparent for the purposes of corporate income tax. The taxable income earned by the partnership is allocated to its partners, in proportion to their share in the partnership's profits, and is taxed at the level applicable to that partner. Partnerships also pay other taxes, such as VAT, real estate tax, and civil law transaction tax, and they may pay withholding taxes (e.g. withholding tax on interest and personal income tax).

The table below compares the business and taxation aspects of the limited partnerships and limited liability companies:

	Capital company	Limited partnership
Legal personality	Yes	No – but the property of the partnership is separate from that of the partners (being owned by the partnership), and the partnership is able to acquire rights and undertake obligations
Limited responsibility of shareholders / partners for obligations of the company / partnership	Yes	Yes – limited to commendam sum
Taxation of income (from exploitation or sale of assets)	19% at the company level	19% at the level of the partners
Taxation of the distribution of income to shareholders / partners	19% Under certain conditions there can be relief for shareholders who are legal persons (based in Poland or the EEA). Reduced rates for foreign shareholders on the basis of double taxation treaties (depending on the treaty)	No
Civil law transaction tax on shareholder / partner loans	No	0.5% on the value of the loan payable by the partnership
Applicability of thin capitalization rules	Yes	No, although interest paid to the partner being the lender cannot be recognised as a tax deductible cost of this partner (on the other hand, interest received constitutes taxable income of this partner)
Ability to offset profits and losses from various projects (carried out in separate companies/partnerships)	No – only in the case of establishing a tax capital group	Yes – profits and losses are compensated at the level of partners

	Capital company	Limited partnership
Taxation in Poland of the sale of shares in the company / partnership	19% Possible relief for foreign shareholders on the basis of double taxation treaties (depending on the treaty)	19% It is not clear whether the same possible relief exists in the case of partnerships

The main advantages of using a limited partnership in an investment structure are as follows:

- profit distributions are not taxed: there is only one level of taxation;
- limitation of liability vis-à-vis creditors for the limited partner (who is liable only up to the amount agreed by the partners in the articles of association, called the commendam sum);
- the ability to offset profits and losses on different projects conducted at the level of the partners;
- lower taxation if income taxed in Poland is exempt from taxation in the country of residence of the partner and the rate of taxation in that country is higher than 19%.

A limited liability company can be transformed into a limited partnership, although such a process may incur taxation in Poland. A detailed analysis is required in each case.

2.2.3. Joint ventures (JV)

Given the current economic environment for development and investment projects, JV structures may have an important role to play in the property market in Poland. By combining real estate market expertise with financial resources, a JV can allow increased profits to be made from transactions that might otherwise be impossible to complete, and reduce transaction risk exposure by sharing it between JV partners.

The term "joint venture" has no specific meaning in Polish law. It describes a commercial arrangement between two or more economically-independent entities which can be structured in various forms, including the following:

- A JV company incorporated as a limited liability company (as detailed above). The main shortcoming of using a limited liability company is the lack of tax transparency and the two-level taxation requirement: tax is levied both at the level of the JV company and at the level of the JV shareholders (unless distributed profits are specifically exempt);
- A JV partnership formed as a limited partnership (as detailed above in section 2.2.2.). In Poland, these are less common than corporate vehicles, but they may be preferable in some situations. The key advantage of a JV structured as a partnership is tax transparency: each JV partner is taxed on its own participation in the profits derived from the JV;

- A JV agreement, which is a contractual arrangement, often referred to as a "cooperation agreement" or "consortium agreement". No separate entity is formed and the rights and duties of the parties derive solely from the provisions of the JV agreement;
- A funding arrangement, which is a contractual arrangement between a developer requiring finance and an institutional investor wishing to participate in a development. It may be either in the form of (a) a forward purchase (where the developer secures tenants for the scheme before or during its construction and the institutional investor is not usually required to provide interim finance but typically pays the agreed purchase price for the investment after completion and the full letting of the development) or (b) forward funding (where the institutional investor usually acquires the site at the outset and the developer is obliged to perform construction works, and in some cases the letting of the scheme). For the developer, the advantage of such funding arrangements is that financing can typically be obtained on favourable terms (either from a facility concluded with a third party such as a bank, or from its institutional investor), and there is a guaranteed sale upon completion of the project. For its part, the institutional investor has the certainty that it will acquire a completed, cash-flow generating scheme, tailored to its investment criteria and at an advantageous price.

Documenting a JV

In Poland, there is no standard template for JV documentation, and the legal structure must be designed each time in response to the business needs of the JV Parties. In preparing the JV documentation, the business objectives will have a direct impact on the JV structure. Apart from commercial objectives, the tax situation is likely to be the most important factor in structuring a JV. Additionally, JVs formed as a partnership or a limited liability company may require competition clearance (for further details on Polish merger control regulations please refer to section 2.4.2.).

In determining the most suitable structure for a JV investment in Poland, the JV parties should from the outset consider the following factors:

(a) The nature of the JV: the JV parties should establish whether it will be a single project (where a contractual structure may suffice) or a series of projects (in which case a corporate or partnership structure may be more appropriate);

(b) Contributions to the JV: it is important for the JV parties to agree on what each of them will contribute to the JV. Whether it will be finance (e.g. equity or the introduction of third-party financing), assets (e.g. real estate or shares in a company holding real estate) or intangible assets (such as resources, know-how or expertise on the specific market). If real estate is to be contributed to the JV, prior legal due diligence and valuation are usually recommended;

(c) The relationship between the JV parties: whether the JV will be a 50:50 venture or one with a minority stakeholder, with or without veto rights;

(d) Management and control: whether the JV parties will be closely involved in the management of JV, or whether a framework will be agreed within which an independent management team will operate, with only key decisions to be referred to the JV parties;

(e) Disputes and deadlock: the JV documents should define a materiality threshold triggering dispute resolution and setting out the details of the dispute resolution process itself;

(f) Extracting profits: there are a number of ways in which the JV partners may take profits from the JV (e.g. dividends, interest payable on loans, management fees) which depend on the structure of the JV and the contributions made by the JV parties. Tax considerations are key in determining the most suitable method of extracting profits from the JV;

(g) Exit: provisions for the termination of the JV need to be included in the JV documentation from the outset. One common option is that the JV is established for a fixed term, with the JV parties agreeing in advance that the venture will terminate at the end of the term or upon the fulfilment of the task for which the JV was established (e.g. the completion and sale of a residential scheme or a shopping centre or a simultaneous sale of parties' participations in the JV). Alternatively, the documentation may grant an option allowing one (or more) of the JV parties to leave the JV, after which the venture would continue under the control of the remaining JV party (or parties), or after the introduction of a new party to the JV. If it is contemplated that a new party may be introduced, the JV documentation should grant each party pre-emption rights exercisable in the event that the other JV party (or parties) are willing to transfer their shareholding in the JV. Another exit scenario is the sale of the assets and the distribution of profits among the JV partners, followed by the liquidation of the JV vehicle.

JV deals are complex and often challenging. A well thought-out drafting of the legal documentation for a JV is fundamental to the untroubled operation of the JV during its lifespan. Lawyers have to play a commercial role in tailoring the deal to meet the requirements of the JV parties. A JV usually requires a number of agreements, which should be determined and structured by lawyers from the outset.

The structure of a JV built around a limited liability company is usually based on a shareholders agreement, the constitutional documents of the JV company/partnership and its by-laws, together with share or asset purchase agreements, as appropriate.

On the other hand, a funding arrangement which does not involve the creation of an ***ad hoc*** legal entity (company or partnership) is simply based on contractual provisions which combine elements of a property purchase agreement and a development and financing facility.

2.2.4. Public-private partnership

Since Poland was elected as a co-host nation for the 2012 UEFA European Football Championship, the creation of real opportunities for the realisation of infrastructure projects (construction works, etc.) and the provision of services according to the PPP formula has become imperative. For this reason, a new PPP law was adopted in 2009, with the purpose of eliminating existing barriers in applying PPP co-operation.

Due to the fact that: (i) under the new PPP law public authorities are not required to perform any extraordinary analysis regarding whether to proceed with PPP co-operation, and (ii) the new PPP contains many investor-friendly provisions (as set out below), several PPP projects were successfully implemented in Poland over the last three years (e.g. two parking projects realised in 2010 in Cracow and in Poznań and the construction of a new section of the A2 Motorway Nowy Tomyśl – Świecko, handed over for use on 30 November 2011).

On the other hand some expected and significant infrastructure PPP projects in Poland were temporarily held up by the authorities during 2011 due to expected changes in PPP and public procurements laws. Certain changes have already been enacted (liability for consortia members) and some are still pending and awaited in order to unblock infrastructure projects (introducing changes to facilitate the competitive dialogue procedure).

Flexible procedures

For the majority of PPP projects, a private partner can be selected in accordance with a rule colloquially known as the "concession law". This provides for a fairly simple two-stage procedure, starting with a public announcement. The first stage requires a potential private partner to file an application to be selected for the PPP project, to which is attached a declaration that it fulfils all the relevant requirements (no documents need to be enclosed), and only those potential private partners selected for the second stage of the proceedings need to file a formal offer. The selection of a private partner may also occur in accordance with Public Procurement Law (depending on the type of remuneration being offered to the private partner). If this is the case, the intention behind the new PPP law is that a so-called competition dialogue (one of the simplest procedures detailed in the public procurement law) is the most appropriate procedure to use.

Accordingly a number of significant PPP projects are planned to be conducted on the basis of a competitive dialogue procedure and therefore some additional changes may be implemented in order to facilitate such procedure further (however the legislative projects are on a very early stage). The main intention is to introduce a flexible multistage procedure which will enable a contracting authority to carry out a successive reduction of bidders throughout the entire dialogue process, leaving only 2 bidders entitled to submit a BAFO.

More freedom in structuring a PPP project

The PPP law grants the parties flexibility in structuring their PPP in the most appropriate way, e.g. the definition of a "PPP undertaking" is very broad, the PPP law imposes no limits or restrictions on the type of remuneration which may be paid to a private partner in a project and the range of possible structures for cooperation is quite extensive: a stock company, a limited liability company, a limited partnership (spółka komandytowa) or a limited joint stock partnership (*spółka komandytowo-akcyjna*).

As significant change was implemented in Q4 of 2011 in order to encourage the establishment of the consortia by private partners (what is often justified from a business perspective in case of expensive and complex projects). Henceforth, joint and several liability of each and every member of the consortium through the entire lifespan of the PPP project was removed. Before, in the case of PPP projects governed by the Public Procurement Act, all members of a private partner consortium were liable for the proper performance of the obligations under the PPP agreement concluded by the consortium with a public partner.

Pre-emption rights

The PPP law expressly provides for a pre-emption right for the benefit of:

- the private partner, where **the sale of real estate** is conducted by the public partner (real estate which constitutes the public partner's contribution to the PPP) or by the company established for the purposes of the PPP project during the PPP or within one year after its completion;
- the public partner, where **the sale** is conducted by the private partner **of** its **shares** in the company established for the purposes of the PPP project.

Either the private or the public partner may exercise its pre-emption right within two months of being notified of a sale agreement being executed with a third party, unless the PPP agreement provides for a longer period.

Clarity and well-known legal concepts

The PPP law is simple, clear, and based on legal concepts which will be familiar to investors operating in other EU Member States, which should eliminate certain doubts as to how to apply the PPP law in practice and eliminate risks related to it.

Tax considerations

The complex nature of a PPP and the relationship between the public and private partners make a thorough analysis of the tax implications of each individual PPP advisable.

The recent experience has proved the PPP law to be beneficial both for the private and public sectors; it is still, however, being used to a lesser degree than expected. It seems that regulations on public debt are one of the reasons for such situation.

Public debt

In 2006, an amendment was implemented to Polish law (in connection with the EUROSTAT 18/2004 decision) in order to mitigate PPP's consequences for the public debt. Following the amendment, if the majority of risks (at least the construction and demand risks, or construction and availability risks) remain with the private partner, then such a PPP project does not burden the public debt. Despite the amendment, PPP projects are not booming in Poland, as public entities are encouraged to apply PPP only if the majority of risk is clearly allocated with the private partner and obviously the later is not happy with such situation. However, as the relevant Polish regulations reflect the EUROSTAT decision, not much can be done before the decision is changed.

PPP to speed up a highway

In Q4 of 2011 an important amendment was made to the Act on toll motorways and the National Road Fund. The amendment opened new possibilities for co-operation in respect of motorways on the simpler PPP basis (although they are not expressly defined as a PPP), and:

- eliminated a heavy and disadvantageous, for private entities, tender procedure for choosing a highway contractor/operator; henceforth, the appointment of such an entity is made pursuant to the Public Procurement Act or the Concession Act;
- extended the scope of entities authorised to collect tolls, which are currently: the General Directorate for National Roads and Motorways, road special purpose companies or a private contractor/operator;
- extended the list of possible public partners, which are currently the General Directorate for National Roads and Motorways and road special purpose companies (however, the Minister of Infrastructure has to be consulted during tender proceeding in relation to the terms and conditions of procurement);
- allowed the companies registered outside Poland to participate in proceedings.

2.2.5. Investment fund structure

An interesting way of structuring a real estate investment is to use a Polish real estate investment fund and flow-through partnership (see above), particularly if there is a portfolio of investments. The use of this structure may allow the deferral, or even exemption from taxation, of the operating and capital gains generated from the real estate.

Similarly, a foreign investment fund established in the EU or EEA country may be used (the Polish CIT law in force from 1 January 2011 provides for such a possibility explicitly). In that case also flow-through partnerships may be used to create tax effective structures for operations on the Polish real estate market. However, lack of well established practice makes it advisable to verify applicability of the tax exemption in each case.

2.3. Real estate financing

2.3.1. Introduction

Polish financial markets have developed rapidly during recent years and are now broadly comparable to western European and other international markets. Acknowledging recent difficulties in the financial markets, the market is otherwise well-developed, offering bank loans and various other products for financing every aspect of business activity for entrepreneurs and corporations operating in Poland, in particular with respect to the financing of real estate acquisitions or development projects, which have grown significantly in popularity. Over the past 10 years, Polish banking law has been adjusted to comply with European Union regulations, and the current market does not differ significantly from European Union standards. Both domestic and international banks and financial institutions operate in this market.

Although the Polish banking market has been affected by the international financial situation and Polish banks have significantly reduced their credit exposure towards the real economy, and the real estate market in particular, there are still a number of financial institutions which are ready to consider financing good and commercially-stable real estate projects in Poland.

Loans in Poland are offered in numerous currencies; however, the majority of commercial loans granted in Poland are denominated in Polish zlotys (PLN), Euros or US dollars. Private residential loans are still quite often denominated in currencies other than PLN, although it is much more difficult nowadays to obtain financing denominated in CHF. Difficulties on the banking market have resulted in new regulations being introduced by the Polish Banking Regulator, under which Polish banks are to be more restrictive in calculating the credit worthiness of all clients and should treat loans granted in foreign currencies as bearing a higher risk.

Purpose of financing

- financing is generally required for acquisitions or development, and finance may be provided through equity or debt (see below);
- the form of loans are distinguished by the stated purpose of the loan, covenants, repayment methods and type of security required, etc.

Equity financing

- share capital paid in cash or through contributions in kind, either on incorporation of the company acting as the investment vehicle or at a later date when its share capital is increased;
- additional payments to the company's capital.

Debt financing

- shareholder or group loans;
- loans from banks and other financial institutions;
- leasing of fixed assets.

2.3.2. Methods of financing Polish real estate investments

Acquisition finance

Loans granted for the purpose of land acquisitions are usually short-term:

- with respect to land acquisition – from 1 to 3 years;
- with respect to the acquisition of completed projects (i.e. office buildings, shopping centres) – from 5 to 10 years.

The majority of land acquisition loans are repaid through a "balloon repayment" mechanism, with interest repaid throughout the life of the facility agreement, but the whole of the principal amount of the loan repaid at the final repayment date.

Facility agreements typically include a covenant to maintain a loan-to-value ratio of a certain level (LTV) throughout the life of the facility agreement. As a result of recent problems on the financial market, the latest banking regulations in Poland require Polish banks to investigate the value of the property carefully and to ensure that there are regular checks of the LTV ratio.

Additionally, in the case of acquisition financing relating to projects already developed, facility agreements usually include a covenant to maintain a debt service cover ratio (DSCR) of a certain level. This is the ratio of the net rental income to the debt service, calculated for a given period of time.

Development finance

In contrast to acquisition finance, loans granted for the purpose of development are usually long-term. It is often possible for a development loan to be converted into an investment loan at a certain date, usually commencing after a 5- to 7-year period.

Development loans may allow for interest serviced in monthly, quarterly or semi-annual payments. For development loans that at a later stage would be converted into investment loans, it is common that, throughout the life of the loan, the borrower repays interest only, and upon conversion of the loan into an investment loan, the borrower starts to repay the loan principal as well.

As with acquisition finance related to developed projects, a typical development finance facility agreement will include covenants to maintain LTV and DSCR at certain levels.

Loan agreements

Polish banking practice has incorporated European market standards, including those with respect to documentation. Therefore, in financing commercial projects, the credit facility agreements used by banks in Poland are usually based on the specimen credit facility agreement prepared by the Loan Market Association, with some modifications to reflect the specific characteristics of Polish law.

Interest and costs

Commercial loans offered by banks in Poland may bear interest at a fixed or floating rate. However, the majority of loans bear interest at the floating rate. Generally, loans denominated in:

- Polish zlotys are based on WIBOR;
- Euros are based on EURIBOR; and
- US dollars are based on LIBOR.

Generally, banks charge the borrower a preparation fee for all works connected with the preparation of the financing. For holding a loan to the availability of the borrower, banks charge the borrower a commitment fee, which is calculated as a percentage of the amount of the undrawn facility. Additionally, on cancellation of the whole or part of the loan, the borrower is charged a cancellation fee and, in the case of prepayment of the loan, a prepayment fee (for long term loans, this is often limited in time).

In addition to the above, for syndicated loans, banks will usually charge an arrangement fee (being equivalent to the preparation fee paid to the arranger). Additionally, the bank taking up the role of an agent will charge an agency fee.

Security package

Polish banks may require the following security instruments in respect of financing the acquisition or development of real estate:

- mortgages;
- share pledges;
- asset and bank account pledges;
- powers of attorney to bank accounts;
- security assignments of receivables of the borrower;
- submissions to enforcement;
- subordination agreements.

Mortgages

A mortgage is the most common form of basic security required by Polish banks, and one is required in every real estate financing transaction. As of 20 February 2011, a significant amendment to the Polish Land Registries and Mortgage Act is into force. As a result of changes, the following forms of mortgage will be available:

- a mortgage securing the amount of the receivable both when the amount of the receivable is known at the date of establishing the mortgage or when the loan issued is granted up to a certain amount and otherwise to secure the interest under the loan;
- as a result of the amendment, the mortgage will also be available to secure more than one receivable of a given creditor or in favour of the security agent in syndicated loans;
- a joint mortgage (which is a form of the mortgage established in situations where the borrower owns and encumbers more than one property).

It is market practice for a mortgage to be established in the form of a notarial deed, but it may also be established by written statement of the borrower (in the case of mortgages established in favour of Polish banks).

A mortgage becomes effective upon registration in the Land and Mortgage Register. The registration takes effect at the date of filing, so even though the registration may take several months, market practice is such that banks disperse the loan upon receipt of confirmation of filing of the application for registration.

A mortgage as security enables the bank, upon enforcement of the loan, to sell the mortgaged property by public auction.

The costs connected with establishing security of this nature include: notarial fees (Polish law stipulates a maximum amount that may be charged for notarial fees and fees are usually also negotiable), registration fees (which currently amounts to PLN 200), and taxes.

Pledges over shares in the borrower

The Polish legal system recognises three main classes of pledge: registered pledges, financial pledges and ordinary pledges.

In Poland, banks commonly require the parent company of the borrower to establish a registered pledge and financial pledge over shares in the borrower, as security. Registered pledges must be registered in a public register in order to be effective. The registration usually takes from two weeks to one month, but sometimes there may be a further delay. The registration fee for establishing a pledge is currently PLN 200.

A standard share pledge agreement typically includes: (i) a negative pledge provision to restrict disposal of the shares; (ii) an obligation to establish a new registered pledge and financial pledge in case any new shares are issued; and (iii) an obligation to amend the articles of association of the borrower in order to enable the bank to execute the voting rights attached to the shares.

Such security enables the bank, upon enforcement of the loan, to seize title to the shares or to sell them at public auction. The value of the seizure may be agreed between the parties in the pledge agreement or can be based on the valuation performed upon enforcement.

Pledges over the assets and bank accounts of the borrower

Generally, banks may also require the borrower to establish a registered pledge over its assets. Similar to the common law concept of a floating charge, registered pledges over assets encumber all present and future assets of the borrower, including any rights, in particular in respect of bank accounts. However, banks often require that bank accounts are excluded from a pledge over assets, as separate registered pledges and financial pledges can be established over these.

Agreements to establish a pledge over assets typically include a negative pledge provision to restrict disposal of the assets (except for transferable goods which are traded by the borrower in the ordinary course of its business). For registered pledges and financial pledges over bank accounts, typical agreements include: (i) a negative pledge; (ii) an obligation to establish a new registered pledge and financial pledge in case the borrower opens any new bank accounts; and (iii) the obligation that the financial pledge is noted on the respective bank account.

With respect to an asset pledge, such security enables the bank, upon enforcement of the loan, to seize the business of the borrower, sell it at public auction, and take-over the administration of the business or lease it to a third party. For pledges over a bank account, the security enables the bank, upon enforcement of the loan, to seize the money deposited in the account. In each case, the value of the seizure, as well as the terms and conditions of possible administration, are agreed between the parties in the pledge agreement. In addition, financial pledges may be enforced through close-out or set-off of the money deposited in the bank accounts against the secured claims.

Power of attorney to bank account

Another form of security commonly required by banks in Poland is a power of attorney to the bank accounts. Usually, this is only required when the parties have entered into agreements to establish registered pledges and financial pledges over bank accounts. Such security enables the bank to control the flow of funds on the accounts of the borrower, and facilitates the enforcement of bank account pledges.

Security assignment of receivables of the borrower

In general, contracts to which the borrower is party are an element of its assets, and the claims the borrower may have under any such contract would be included under an asset pledge. However, it is a common practice for banks to require certain receivables of the borrower to be excluded from the scope of the pledge over assets and, instead, to be assigned in favour of the bank; for example, commercial contracts, leases, construction contracts and insurance agreements.

A standard provision included in a security assignment of receivables agreement is an obligation of the borrower to assign in favour of the bank all of its future rights, promptly upon entering into any future agreements.

Under this type of security document, the bank is entitled to claim payments from the debtors of the borrower.

Submission to enforcement

The majority of banks financing real estate projects in Poland require the borrower to make a statement on submission to enforcement. Generally, such statements must be in the form of a notarial deed, but they may also be made in simple written form (in the case of Polish banks). Where the statement is given in the form of a notarial deed, the only cost associated with establishing the security is the notarial fee (capped under Polish law and usually negotiable).

This security enables the bank, upon enforcement of the loan, to expedite the process of enforcement, as the bank does not need to present additional documents to the court to effect enforcement. Upon obtaining enforcement title, the bank is entitled to file a petition to the bailiff for commencement of the enforcement proceeding in relation to all assets of the borrower.

Subordination agreements

Frequently, banks also request that a borrower and its parent company enter into a subordination agreement. Here, the parties agree that claims to the borrower shall be subordinated to claims of the bank for the term of the loan.

Financing of residential projects (escrow accounts)

Adopted on 16 September 2011, the Act on the protection of a purchaser of residential premises or a single-family house introduces a fundamental legal regulation into the business of property development. The new rules will apply to development investments starting after the entry into force of the Act, in April 2012.

The main objective of this Act was to protect the interests of individuals buying residential units in the case of the developer's bankruptcy, but also to regulate the rights and obligations of the parties of the sale and purchase agreement, its form and content.

Under the new rules, a developer is obliged to use one of several ways to protect the customers' money: a closed escrow account - the funds accumulated on it are not available to the developer until the transfer of ownership to the customer, an opened escrow account jointly with a insurance contract or bank guarantee - funds are forwarded to the developer gradually after the completion of various stages of the investment.

Simultaneously banks shall ensure the correctness of payments made to developers through proper control of various stages of the property development in accordance with the project schedule. In the event of the developer's bankruptcy the money on the escrow account shall be excluded from the bankruptcy estate (the priority is to complete residential investments and a commitment to customers).

2.3.3. Tax implications

Equity financing

When a Polish company is financed through equity, the funds required for the investment are received in exchange for the shares in the company. Equity financing is generally subject to a 0.5% civil law transaction tax with certain exceptions for restructuring and reorganisation transactions.

Generally, for Polish corporate income tax purposes, a contribution in kind (except for the contribution in kind of a business operating as a going concern or a viable part of such a business) is a taxable event for the company making the contribution, and is subject to the standard corporate income tax rate, currently 19%. However, foreign entities will usually be exempt from Polish taxation under the relevant tax treaty.

Shares in the company give the shareholders the right to control the company and the right to financial benefits from the company. The income of the company generated through its operations is subject to corporate income tax. Any after-tax profits can be distributed to shareholders in the form of dividends. The shareholders are not only entitled to dividends but also to a share of any proceeds upon liquidation in proportion to their shareholdings.

Additional payments are contributions made by the shareholder(s) of a limited liability company where no shares are issued in exchange. Usually these payments are made when the company has made a financial loss and its level of equity is lower than the nominal value of its issued share capital. If the company's articles of association allow such additional payments to be made, and later repaid to the shareholders, then receipt and repayment is not subject to taxation. Compensation for making the additional payments may be paid to the shareholders in the form of interest payable by the company. When paid, such interest should be treated as a non tax deductible cost.

Taxation of dividends

Dividends distributed by a Polish company to a foreign owner are generally subject to a 19% withholding tax in Poland. This tax must be withheld by the company distributing the dividend on the dividend payment date, and paid to the tax office before the seventh day of the month following the month in which the tax was withheld. The 19% rate can be reduced (to a lower percentage) if the recipient is a tax resident in a country with which Poland has concluded a tax treaty. Poland has concluded many tax treaties and there are just as many ways in which the Polish withholding tax can be reduced. Usually the treaty withholding tax rates on dividends vary between 5% and 15%.

Appropriate tax planning in the initial phase of the investment should be carried out to determine in which country the recipient of the dividends should be located in order to reduce or avoid the international double taxation of dividends (see the Appendix at the end of this book for a list of withholding tax rates under Poland's various tax treaties). Double taxation occurs when the Polish withholding tax cannot be reduced to 0% by virtue of a treaty and the dividend is also subject to income tax in the country where the recipient is a tax resident. The treaties or unilateral tax rules in most countries provide a credit system to avoid such double taxation.

In addition, since the implementation of the EU Parent-Subsidiary Directive, an exemption on dividends paid to companies from other EEA countries and Switzerland applies. This is provided that the entity receiving the dividend is taxed in another EEA country (or in Switzerland) on its worldwide income (and is not subject to tax exemption on its total income) and has held or will have held at least 10% (in the case of a company resident for tax purposes in Switzerland, at least 25%) of the shares in the Polish company paying the dividend for at least two years.

It is up to the company paying the dividend to determine the applicable withholding tax rate. The Polish withholding tax system is not "a pay and refund system". The Polish company distributing the dividend can be held liable for mistakes, e.g. if it applies incorrect tax rate. A certificate issued by a foreign local tax office confirming the tax residence of the foreign shareholder which receives dividend payments from Poland must be obtained by the Polish company in order to allow it to apply the lower withholding tax rate or exemption. Additional requirement in force starting 1 January 2011 is that the Polish entity paying dividends should also hold a written confirmation of the recipient that the latter does not benefit from tax exemption on its worldwide income.

Dividends paid between companies which are resident in Poland for tax purposes are exempt from withholding tax provided that the dividend recipient has held or will have held at least 10% of shares in the dividend paying company for at least two years. If the above conditions are not met, non-creditable withholding tax is levied on dividends at the rate of 19%.

Redemption of shares and liquidation distributions

The redemption of shares and the return of equity to shareholders are permitted under Polish law. The formal procedure is time-consuming and usually takes several months. In the past, for tax purposes, redemption profits were treated in the same way as dividends and were subject to the applicable withholding tax (taking into consideration the appropriate tax treaty) or withholding tax exemption based on the Polish CIT law provisions implementing the Parent-Subsidiary Directive. However, starting from 1 January 2011 the Polish CIT law has changed and now standard, voluntary redemption of shares is subject to the same tax treatment as disposal of shares. It means that as a rule such redemption will be subject to tax in Poland, unless relevant double tax treaty provides for tax exemption. Thus, a separate analysis is advisable in each case. Liquidation profits from liquidation of a Polish company paid to Polish companies, as well as to the companies from other EEA countries or from Switzerland, are subject to the same potential tax exemptions as dividends.

Debt Financing (Loans): civil law transaction tax

Loans are generally subject to civil law transaction tax at the level of 2% of the loan principal. The tax must be paid within 14 days of the date of the loan agreement, and the tax liability rests with the borrower.

Nevertheless, the following types of loans are exempt from taxation:

- loans granted by shareholders to a limited liability company or joint stock company;
- loans granted by foreign entities which are engaged in credit and financing activities (such as group treasury companies);
- loans recognised as an activity subject to Polish or foreign VAT (e.g. bank loans); financing granted as a part of business activity is recognised as a financial service specifically exempt from VAT; therefore, no civil law transaction tax applies.

Withholding tax on interest

Generally, interest paid from Poland to a foreign lender is subject to a 20% withholding tax. This rate applies unless the relevant tax treaty provides otherwise. Please see Appendix for a list of withholding tax rates under Poland's various tax treaties. Under the tax treaties, it is generally stipulated that if withholding tax is payable it can be credited against the corporate income tax of the foreign lender. As in the case of dividends, in order to apply a treaty rate, a certificate confirming the tax residence of the foreign lender must be obtained.

After joining the European Union, Poland implemented EU Directive 2003/49/EC on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States. One of the main purposes of the Directive is to abolish withholding tax imposed by the country from which payments of interest and royalties originate when such payments are made between "qualifying EU entities", i.e. payments made between parent and subsidiary, subsidiary and parent and between direct sister companies (in all cases a minimum 25% stake and 2 year holding period is required).

However, Poland was granted an eight year transitional period for the full implementation of the Directive into Polish domestic law. As a result, until 30 June 2013 withholding tax imposed on interest and royalty payments made to qualifying EU entities by Polish entity may not exceed 5%. In order to benefit from that favourable treatment the payer should hold recipient's certificate of tax residence. Additional requirement in force starting 1 January 2011 is that the payer should also hold the recipient's confirmation that the recipient does not benefit the tax exemption on its worldwide income.

Tax deductibility of interest paid on loans

Generally, interest on loans is deductible for tax purposes when actually paid or compounded (added to the principal so that it constitutes a basis for new interest calculation), i.e. accrued interest may not be treated as a tax deductible cost until it is actually paid or compounded.

In general, it should therefore be possible to treat the interest on loans drawn to acquire shares in a Polish company as tax deductible. Careful tax planning is, however, always required in all "debt push down" structures.

It is important to note that interest accrued during the development of real estate on the part of the loan used to finance that development is not directly deductible. The cost of such interest should be added to the initial value of the newly developed real estate (i.e. the new building) in order to increase the scope of its future depreciation for tax purposes. However, this rule applies only to real estate which is the company's own fixed asset. It does not apply to projects constructed for resale (e.g. residential projects). In such cases, interest is treated as tax deductible under the general rules.

Level of interest

The Polish tax authorities are usually interested in the conditions of loan agreements concluded between related parties. These conditions should be the same as, or comparable to, the sort of financing conditions which non-related parties would agree upon, in accordance with "the arm's length principle". Too high an interest rate could lead to an adjustment of the Polish borrower's taxable income. In addition, other conditions in the loan agreement which are unjustifiable or unfavorable to the borrower could result in further tax adjustments. According to regulations governing the documentation of transactions between related parties, taxpayers are required to prepare specific transfer pricing documentation or risk paying a 50% rate on any additional taxable income assessed.

Restrictions on the tax deductibility of interest paid on loans

The Polish thin capitalization rules restrict the tax deductibility of interest on two types of loans (credits) granted by certain entities:

- loans (credits) granted to the taxpaying company by its shareholder holding not less than 25% of the voting rights in the company or loans (credits) from shareholders holding jointly not less than 25% of the voting rights in the company ("mother company" loans);
- loans (credits) granted to the taxpaying company by another company, if the same shareholder holds not less than 25% of the voting rights in each of these companies ("sister company" loans);

where the debt to equity ratio (the ratio of the value of the debt payable to certain entities (see below for details) to the value of the share capital) exceeds 3:1 at the date of the interest payment. Interest on the loans (credits) exceeding the ratio is not tax deductible (the term "loans (credits)" also cover bonds and deposits).

For the purposes of the calculation of the debt to equity ratio, the debt includes:

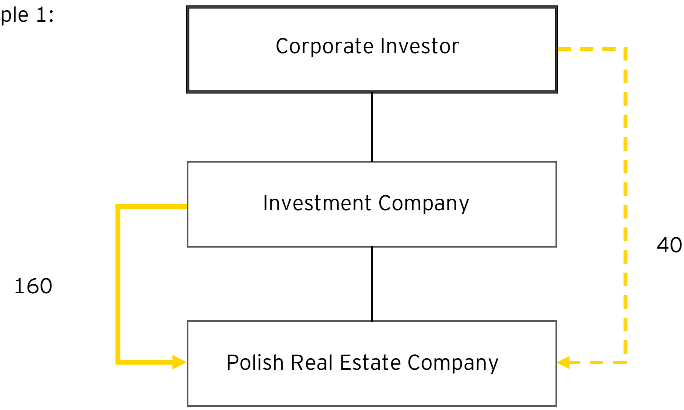
- in the case of "mother company" loans:
  - debt payable to direct shareholder(s) holding at least 25% of the voting rights in the interest paying company; and
  - debt payable to entities holding at least 25% of the voting rights in the above mentioned direct shareholders.
- in the case of "sister company" loans:
  - debt payable to direct shareholder(s) holding at least 25% of the voting rights in the interest paying company; and
  - debt payable to entities holding at least 25% of the voting rights in the above mentioned direct shareholders; and
  - debt payable to the entity granting the loan (credit).

In both cases "equity" includes the share capital stated in the company's deed of association and equal to the nominal value of the shares issued, excluding:

- capital not paid in full;
- capital converted from shareholder loans (credits) and/or related interest;
- capital formed by a contribution in kind, which is an intangible asset not subject to depreciation (e.g. goodwill).

Examples of how the thin capitalization rules work:

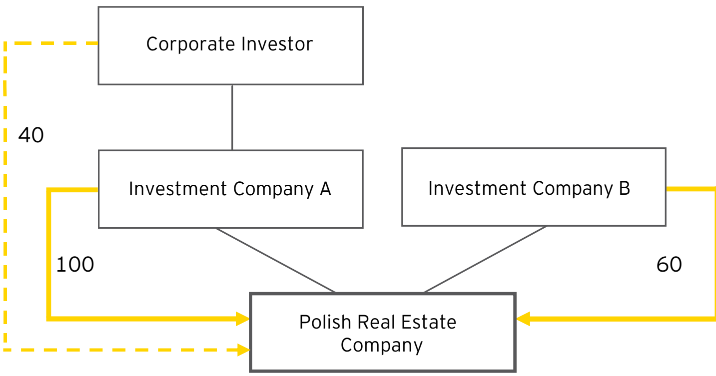
Example 1:



Assumption:
Polish Real Estate Company 's (PREC)

Nominal share capital is:	50
Debt limit is:	150
Total loans:	200
Part of loans exceeding threshold	50

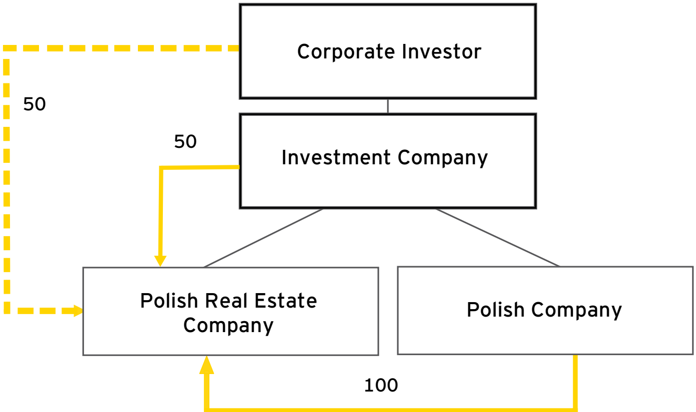
Example 2:



Assumption:

PREC 's nominal share capital is	50
Debt limit is	150
Total loans	200
Part of loans exceeding threshold	50

Example 3:



Assumption:	
PREC's nominal share capital is	50
Debt limit is	150
Total loans	200
Part of loans exceeding threshold	50

Foreign currency financing

As the foreign currency liabilities are reported for accounting purposes in PLN, foreign exchange differences (gains or losses) accrue in the accounting books of the Polish company. Foreign exchange differences accrue also on loan liabilities in PLN denominated in foreign currencies. These gains or losses are recognised for tax purposes only when realized, i.e. when the related liability is paid or set off. However, audited companies can report foreign exchange gains or losses in accordance with accounting standards upon notifying the tax authorities, provided that such reporting in accordance with accounting standards will continue for a period of at least three tax years.

2.4. Acquisition of real estate

2.4.1. Introduction – Asset deal versus share deal

From a legal perspective, there is a number of ways in which an investor may seek to acquire real estate in Poland, but, as in other European jurisdictions, the two most popular methods are through an asset deal or a share deal.

The key difference between these two deal structures is in the nature of what the purchaser acquires:

- in an asset deal, the purchaser buys the property itself;
- in a share deal, the purchaser buys shares in the target company which holds the real estate, and along with the real estate the buyer acquires all the other assets, obligations and liabilities of the target company.

Both structures are equally popular with institutional investors in Poland; however, sales by real estate funds have been increasingly structured as share deals.

In practice, if a share transaction is properly structured, this can be the most tax efficient disposal method to use. In a well-organised corporate structure, taxes on capital gains can be entirely avoided or in some cases deferred.

From the buyer's perspective, it is usually more tax efficient to buy the property directly than to buy shares in a company holding the property. The buyer can then depreciate as much as the real market value of the building for tax purposes. On the other hand, if the shares are bought at a higher price than the book value of the company's assets, goodwill paid in return for the shares can be recognised for accounting purposes. Unfortunately, such goodwill cannot be amortised for tax purposes. Furthermore, a company owning real estate with a low book value has a deferred tax exposure with respect to any future capital gains made on the disposal of that real estate. Thus, the buyer of shares will most likely try to negotiate a discount on the transaction price to eliminate this negative tax aspect.

The purpose of this chapter is to outline the main features of these two types of real estate transaction from both the legal and tax perspectives, and to examine the consequences of each structure.

2.4.2. Legal aspects

It should be noted that, in a share deal, the scope of liabilities acquired is far broader than in an asset deal. It includes:

- contingent or undisclosed liabilities (such as claims by employees and past breaches of legislation governing the operation of the company's business); and, most importantly
- all existing and undisclosed tax liabilities.

For this reason, the due diligence enquiries preceding an acquisition of shares are generally more extensive and time-consuming than those preceding an asset deal. To guarantee the purchaser an adequate level of comfort, the share purchase agreement should include more extensive representations and warranties and related indemnities. To make sure that the indemnities are enforceable, it is recommended in many cases to retain part of the purchase price in an escrow account (preferably until the expiry of all relevant tax liabilities) or to obtain a bank guarantee or parent company guarantee from the seller.

In an asset deal, the buyer acquires only the particular real estate. Any property-related tax liabilities can be identified during the due diligence process and may be excluded by obtaining tax certificates evidencing the lack of tax arrears of the Seller.

The purchaser may therefore prefer an asset deal, particularly because it will be less exposed to contingent and undisclosed liabilities, and also because the due diligence enquiries necessary are generally less extensive than for a share deal.

However, the main advantage of an asset deal over a share deal is that a guarantee of good title to the land is available by virtue of the operation of Polish law in favour of the purchaser of real estate in the asset deal. Polish law states that the purchase of land from a registered title-holder guarantees the validity of the title acquired, provided that the purchaser acted in good faith. In this context, the presence of good faith means that the purchaser was not aware of, or could not easily become aware of, a discrepancy between the contents of the Land and Mortgage Register and the actual legal status of the property. Polish law protects the buyer by presuming that the purchaser of a property purchases it in good faith. Such title guarantee is not available to the purchaser under a share deal, where the validity of the purchaser's title to the property is supported on a contractual basis by the representations and warranties of the seller. For further details on title guarantee please refer to section 2.1.2.

The statutory title guarantee available to the purchaser in an asset deal usually results in there being less extensive representations and warranties and accompanying indemnities included in the asset sale agreement than in a share sale agreement.

In an asset deal, the seller's representations and warranties usually relate to:

- the validity of the seller's title;
- the fact that the development has been carried out in accordance with the technical plans and relevant permits and that such permits are valid; and
- the enforceability of any lease agreements.

By contrast, the seller's representations and warranties in a share deal not only have to include the representations and warranties found in an asset deal, but also comprehensive representations and warranties relating to tax, employment, accounting and corporate matters.

Despite the advantages of an asset deal, it is not without its problems. Except for lease agreements, which are transferred by the operation of law, an asset purchase will not automatically result in the transfer of property-related contracts to the buyer. In particular, in an asset deal, it is necessary to obtain third-party consents for the formal assignment of lease security instruments, warranty claims under construction contracts and related performance guarantees, and IP rights to construction/architectural designs. Of the regulatory permits required for a development, only the environmental, permit zoning decision and building permit can be transferred to the purchaser of the property, and these only with the prior consent of the local authority. Most governmental permits are non-transferable in nature. However, note that occupancy permits attach to a building and do not need to be transferred. For further details on the regulatory permits required for property development, please refer to section 2.5.1.

It is therefore an advantage of the share deal structure that the typical property-related rights and obligations (such as leases, property management agreements, IP rights to construction designs, warranty claims under construction contracts and contracts of insurance) are 'transferred' without the need for formal assignment, as they simply remain with the corporate entity holding the property.

Merger control

Another issue to be addressed during the due diligence review preceding any deal is whether merger control legislation will apply. The key questions are whether notification of the transaction to the Polish competition authority is compulsory, meaning that the transaction must be suspended until competition clearance is received.

A merger control notification in Poland is required if the following thresholds are met:

- the combined worldwide turnover of the capital groups to which the merging undertakings belong in the financial year preceding the year of concentration exceeds € 1 billion; or
- the combined Polish turnover of the capital groups to which the merging undertakings belong in the financial year preceding the year of concentration exceeds € 50 million.

It is possible for a transaction to be exempt from the notification obligation where the above turnover thresholds are met, if the target's Polish turnover, or the Polish turnover generated by the assets being acquired, does not exceed EUR 10 million in either of the two years preceding the merger.

Establishment of a JV constitutes one of forms of concentrations which, provided that turnover thresholds are met, has to be notified to the Polish Competition Authority. In its guidelines issued in 2010 the Polish Competition Authority did not make a clear distinction between the establishment of a JV and an acquisition of minority shareholding (which is not notifiable). Therefore, even an acquisition of minority shareholding should be carefully analyzed since in specific circumstances it may be qualified as a JV establishment and require the antimonopoly clearance.

Documenting the transaction

It is common practice in institutional deals to record at the outset of the negotiations the key principals of the transaction in heads of terms or a letter of intent. As in other jurisdictions, heads of terms and letters of intent are morally binding only, with the exception of confidentiality and exclusivity clauses (provided that these clauses state that the parties intend them to be contractually binding).

As the due diligence review progresses, the parties to an institutional deal will usually start negotiating the transaction documents. Share purchase agreements and property purchase agreements are the principal contractual documents regulating the acquisition of shares and real estate, respectively.

The first drafts of share or asset purchase agreements are often produced by the buyer, except when the sale is to be made by way of an auction, in which case potential buyers each provide a mark-up to the draft agreements prepared by the seller. Usually, the potential buyer's comments concern the seller's representations and warranties, as well as indemnity clauses, which are the most heavily negotiated parts of the agreements, both in respect of asset deals and share deals.

The Polish institutional market has adopted standard international legal documentation, so that agreements which are currently signed can often be lengthy, depending on the size and complexity of the deal.

Types of agreement

Under Polish law, ownership title to land or shares is transferred upon the signing of a property purchase agreement or share transfer agreement. The registration of a transaction in the Land and Mortgage Register or the commercial register is legally required, but does not in itself affect the legal validity of the transaction. Exceptions to this are the transfer of any RPU, and the establishment of ownership title to separate premises within a larger property, which become legally effective upon registration in the Land and Mortgage Register (however with retroactive effect of the date of filing a relevant motion with the Land and Mortgage Register).

Although it is possible under Polish law to conclude a property or share purchase agreement in a one-off transaction, in most cases the transaction takes place in two stages (where a preliminary agreement is followed by final agreements). Where a statutory pre-emption right to purchase the property applies, an asset deal can even be structured in three stages, where the parties sign (a) a preliminary agreement which is followed by (b) a conditional agreement and then (c) a final agreement to complete the transaction.

Unconditional title transfer

The two-step structure results from the fact that Polish law (unlike other European jurisdictions such as Germany) significantly restricts the parties' ability to withdraw from an agreement to transfer the title to real estate.

Pursuant to Polish law, the transfer of real estate must be unconditional. Accordingly, should any conditions precede the closing, they need to be fulfilled (or the need to fulfil them needs to be waived by the party set to gain by that fulfilment) before the transfer of the real estate can take place. For this reason, preliminary agreements are very popular, since they allow all conditions precedent to closing to be set out. If those conditions are satisfied, the signing of a final unconditional agreement completes the transaction.

The conditions precedent provided in a preliminary agreement usually result from the due diligence findings made before or at the same time as the negotiations over the preliminary agreement. This is why a thorough due diligence exercise is of key importance in preparing transactions.

Agreement content

Apart from the representations, warranties and indemnities, an asset or share purchase agreement deals with:

- the object of the sale (by providing a detailed description of the property or shares);
- consideration (the price and payment mechanism);
- down payments and forms of security (such as a mortgage over the property or a registered pledge over the shares);
- what conditions precedent the purchase may be subject to (such as the satisfactory results of legal, financial and tax due diligence, the completion of the development or the full letting of the premises); and
- other matters such as (in case of an asset deal) the transfer of warranty claims and rental and construction guarantees.

Specific performance

It should be noted that if all the conditions precedent set out in the preliminary agreement are satisfied or waived, but one of the parties nevertheless fails to sign the final agreement, the other party can demand the execution of the final agreement (i.e. claim specific performance in court). However, to claim such specific performance, the preliminary agreement must be executed in the form of a notarial deed (in the case of an asset deal) or with signatures certified by a notary public (in the case of a share deal).

Lock-out

In the case of an asset deal, the preliminary property purchase agreement may be recorded in the Land and Mortgage Register and effectively prevent the seller from selling the property to a third party (provided that the preliminary property purchase agreement was executed as a notarial deed). In the case of a share deal, such a lock-out is only available if contractual arrangements are made, although it is still possible for a party to breach those contractual duties under such an agreement and incur damages, which renders the lock-out protection less strong than that afforded by registering a preliminary asset purchase agreement in the Land and Mortgage Register.

Third-party pre-emption rights

In the case of an asset deal where a third party has pre-emption rights (e.g. the pre-emption right of a local authority which arises on the sale of a building registered as a monument, provided that the pre-emption right is recorded in the Land and Mortgage Register), the two-step deal structure can (or must, where the third party is a local authority) be supplemented by a conditional agreement which is signed between the preliminary and final agreements. A three-step structure is necessary when the parties sign a preliminary agreement to allow the due diligence review to begin and, following satisfactory due diligence findings and the fulfillment of the conditions precedent set out in the preliminary agreement, the closing is only conditional on the decision of the holder of a pre-emption right (most commonly the local authority) not to exercise that pre-emption right.

The notary public executing the conditional agreement will send a copy of it to the local authority, which may then exercise its pre-emption right within one month of receiving the conditional agreement. If the local authority does not exercise its pre-emption right within that period, the parties can conclude the final agreement, which effects the unconditional transfer of the title to the real estate. For further information, please refer to section 2.9.1.

Formalities

As far as the formalities are concerned, property purchase agreements:

- must be signed in Polish as a notarial deed executed by a notary;
- can only be governed by Polish law if the agreement deals with the direct purchase of real estate in Poland;
- may also be executed in a foreign language version, but only for information purposes as an attachment to the notarised property purchase agreement, and the Polish language version prevails in the case of discrepancies.

By contrast, a share purchase agreement:

- requires only notarial certification of the signatures (not a notarial deed), and can be executed in a foreign language (although the standard form of notarial certification of signatures should be followed);

- may have signatures certified by a foreign notary;
- does not need to be governed by Polish law (provided that at least one party is a foreign entity, a share purchase agreement can be governed by the laws of a foreign legal system).

However, the Polish commercial registry court may request a copy of the agreement, and in such case, a sworn translation into Polish, together with an apostille or notarisation, will be required if the agreement is governed by a foreign legal system or the signatures were certified by a foreign notary.

The notarial fees for the notarisation of a property purchase agreement are capped, and the maximum fee amounts to PLN 10,000 for each agreement (i.e. the notarisation of a preliminary agreement costs PLN 10,000 but another PLN 10,000 is payable for the final agreement). However, in the case of a three-step structure, the PLN 10,000 notarial fees are split between the conditional and final agreements.

On the other hand, the notarial fees for the certification of signatures are significantly lower, and amount to a maximum of PLN 300 for each signature certified.

Residential development agreements

As of April 2012, each residential development agreement for its validity, must be concluded in the form of a notarial deed (before written form was commonly used by the developers). In addition, the cost of the notary's remuneration and court costs are divided between the purchaser and the developer. Additionally, a buyer's claim to build a single-family house or a residential premises and to transfer the property must as a rule be disclosed in the Land and Mortgage Register.

Each customer, before signing a contract, at his request, may receive an electronic or paper form of the prospectus. Under the new rules, the prospectus must contain not only data on the realized investment, but also data on the legal and financial situation of the developer, such as copies of the National Court Register and the Land and Mortgage Register, building permits, financial statements, architectural and construction projects, as well as examples of previous completed investments (penal regulations indicate criminal liability for the withholding of accurate information or providing false information in the prospectus).

The new rules also oblige the developers to hand-over the property prior to conclusion of the sale agreement, along with a protocol in which the purchaser may submit defects and faults.

2.4.3. Tax implications

As mentioned above, real estate can be sold either through the direct sale of the property (an asset deal) or indirectly through the sale of the shares in the company owning the property (a share deal). These two types of transactions are afforded different treatment by the Polish tax regulations.

Asset deal

The revenues generated on the sale of real estate are subject to the standard taxation rules of Polish corporate income tax. Taxable revenues are reduced by the net book value of the property. Effectively, only the "capital gain" is taxed at the rate of 19%. The revenue from the sale of real estate must be valued at the price set in the sale contract. However, if the price differs substantially and without good reason from the market value of the real estate, the revenue may be assessed by the tax authorities according to the market value. This transaction price adjustment may be applied to transactions between related and unrelated entities. Adjustments trigger not only a higher tax burden but also penalty interest.

The Polish tax system does not include a replacement provision. Therefore, the corporate seller cannot defer taxation of a capital gain.

Costs incurred by the buyer for the acquisition of real estate: purchase price, transaction costs including advisory, civil law transaction tax – if applicable, financial costs accrued till the purchase, etc., form the initial value of the real estate and are recognised as tax deductible costs through depreciation write-offs or upon sale. As the value of the land is not subject to depreciation, it is then important to determine the value of the land and the value of building separately.

VAT on the acquisition of real estate

The supply of buildings, infrastructure, or parts of buildings or infrastructure is generally VAT exempt, except for:

- the supply of a building, infrastructure or part of a building or infrastructure in the course of its first occupation; and
- the supply of a building, infrastructure or part of a building or infrastructure made within two years of the first occupation;

in which cases the supply of buildings, infrastructure or parts of buildings or infrastructure are generally subject to VAT.

"First occupation" means handing over a building, infrastructure or part of a building or infrastructure within the context of the performance of VAT-able activities (subject to VAT or VAT exempt) to the first acquirer or user, after the:

- initial completion; or
- improvement (if the expenses incurred for the improvement constituted at least 30% of the initial value);

of that building, infrastructure or part of a building or infrastructure.

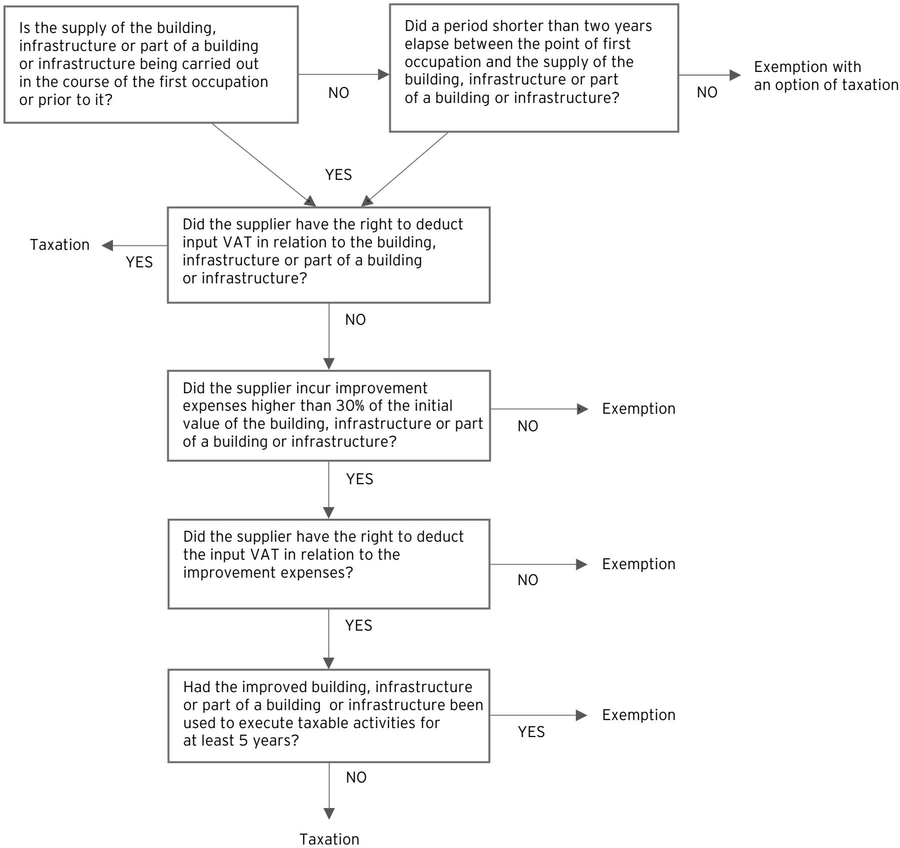
Taxpayers may choose not to apply the exemption and charge VAT if:

- both buyer and seller are VAT registered; and
- before the day of supply they submit the appropriate statement to the tax office of the purchaser.

The supply of buildings, infrastructure or parts of buildings or infrastructure which should be subject to VAT (i.e. supply in the course of first occupation or within two years of the first occupation) must be VAT exempt (no option to tax allowed) if:

- the seller was not entitled to deduct input VAT; and
- the seller did not incur improvement expenses on which he had right to deduct VAT, or such expenses did not exceed 30% of the initial value of the building, infrastructure or part of a building or infrastructure (unless the improved real estate was used for taxable activities for no less than 5 years).

The diagram below outlines VAT rules on the taxation of the supply of buildings, infrastructure or parts of buildings or infrastructure.



Generally, the VAT treatment of ownership title to land or an RPU over land follows the VAT treatment of the buildings developed on the land.

An exception to the above rule is when an RPU is acquired for the first time from the State or local authority, in which case, the RPU is always subject to 23% VAT, even though the buildings developed on the land may be exempt from VAT.

The supply of ownership title to undeveloped land or an RPU over land planned for building purposes is subject to 23% VAT (supply of agricultural land is exempt from VAT).

If subject to VAT, the supply of real estate is subject to 23% VAT. However, the supply of residential buildings and separate apartments is subject to reduced 8% VAT, except for part of residential buildings whose usable floorspace exceeds 300 m^2 and apartments whose usable floorspace exceeds 150 m^2. In such a case only part of residential buildings and apartments which is, within the above limits, benefits from 8% VAT rate, whereas the part exceeding the thresholds is subject to standard 23% VAT rate.

If the supply of real estate is VAT exempt, it is subject to civil law transaction tax payable by the buyer. The applicable rate is 2% of the market value of the real estate.

If the business of the Polish company or part of its business is sold as a going concern, the transaction falls outside the scope of VAT. The assets of the business or part thereof sold will be subject to civil law transaction tax payable by the buyer at the rate appropriate for a particular item (2% for land, buildings and other tangible property, 1% for intangibles).

Recoverability of input VAT

Input VAT is recoverable if the company performs or intends to perform activities in the future which are subject to VAT (e.g. lease of the commercial real estate). Input VAT will not be recoverable if the company performs or intends to perform activities in the future which are VAT exempt. If this is the case, the input VAT will increase the initial tax basis of the real estate.

For example, certain financial activities performed by banks, financial institutions and insurance companies are exempt from VAT: these institutions have no (or limited) output VAT and therefore they are not entitled to refunds or any other kind of recovery of input VAT incurred in the course of their VAT exempt financial activities (in certain cases there may be a limited recovery available).

If business activities are partly exempt, the recovery of any input VAT which cannot be matched directly either to VAT-able sales or VAT exempt sales should be effected in line with the proportion of the net value of the taxed supplies to the total value of all supplies (a so called pro rata recovery). During a calendar year, the proportion is calculated based on the volume of supplies made in the previous year. At the year end, the amount of deductions is adjusted to the actual percentage calculated for the whole year. In the case of tangible or intangible assets subject to depreciation for tax calculation purposes, the percentage of input tax which may be deducted is subject to adjustments over the period of 5 or even 10 years (in the case of real estate).

Calculation of the percentage of input VAT to be deducted is necessary only if it is not possible to match input tax with taxed activities or exempt activities directly.

Date of input VAT recovery

Input VAT cannot be recovered earlier than in the month in which the services were rendered to, or the goods were acquired by the purchaser incurring the input VAT (prepayment invoices do not fall under this rule: they must be paid in order for input VAT to be reclaimable).

Direct refund of input VAT

A direct refund of any surplus input VAT incurred should be made within 60 days of the submission of the application for the refund (the VAT return) on condition that the taxpayer performed VAT-able supply in the period for which the refund is claimed.

Please note that this deadline can be shortened to 25 days at a taxpayer's request if the input VAT to be refunded resulted from invoices that have been paid in full.

It is possible to get a refund of input VAT even if VAT-able supplies are not made in the period for which the refund is claimed. However, in such case the period for the refund is extended to 180 days, unless a form of security, e.g. a bank guarantee is provided (in which case the refund must be made within 60 days).

Share deal

A capital gain on the sale of shares is subject to Polish corporate income tax at the standard rate of 19%.

If the selling party is a foreign shareholder, the applicable tax treaty influences the tax implications of such a transaction. Under most tax treaties concluded by Poland the right to impose taxes on the sale of shares in corporate entities is allocated to the country where the shareholder is a tax resident. In such cases Polish income tax rules are not applicable and the fiscal rules of the country in which the shareholder is a tax resident govern the transaction. In some countries capital gains on shares are exempt from taxation. The rationale behind this exemption is that the taxation of capital gains on shares constitutes double taxation: the profit within the company is taxed using the normal income tax rate and, therefore, the profit on the share transaction should not be taxed again. In international taxation terminology this exemption is known as the Participation Exemption. Some countries limit this Participation Exemption to capital gains on share transactions involving domestic shares only. Other countries enable the Participation Exemption to be applicable to transactions involving the shares of foreign companies as well.

Certain Polish tax treaties (e.g. with Spain, France, Denmark, Sweden and Germany) provide that a sale of shares in a company holding mainly real estate assets should be regarded as a sale of real estate. Consequently, income earned on the sale of shares in the Polish company will be taxed in Poland.

The sale of shares in the Polish company is subject to a 1% civil law transaction tax (on the market value of shares) payable by the buyer. This is irrespective of where the transaction takes place or where the parties to the transaction are resident for tax purposes. A share transaction is not subject to Polish VAT. However, where a share transaction is treated as being made in the course of business activity (rather than as a one–off transaction), it may be classified as a VAT exempt financial service. However, it will still be subject to civil law transaction tax.

Costs which must be incurred in order to acquire shares (e.g. purchase price and notary public fees) may be recognised as tax deductible costs upon the sale of shares.

Other costs indirectly connected with acquisition of shares including advisory and financing costs may be recognised as tax deductible costs when incurred (in certain cases recognition over time may occur).

Cross-border structure

Typically, foreign investments are structured in such a way that the overall level of taxation of the financing, exploitation, and potential capital gain is kept as low as possible, seeking to avoid double taxation. International tax planning should determine the final structure of the investment. Commonly, a structure involving more than two jurisdictions is used to optimize the overall tax position. The tax treatment of all the relevant legal transactions involved in a Polish real estate project differs according to the other jurisdiction(s) involved. The tax treaties concluded by Poland should prevent double taxation. Investigating the tax treaties and the applicable rules in the different relevant jurisdictions will help to determine what structure, given the specific circumstances, should be arranged. Therefore, it is fair to say that there is no typical cross-border investment structure, and that each investment project is unique.

Nevertheless, the following points should be considered when designing the most efficient structure:

- interest payable in respect of any debt financing of the investment should be fully tax deductible;
- interest income should be reported as taxable income in a jurisdiction with a relatively modest tax rate;
- the exploitation and operational costs of the real estate should be tax deductible to the largest extent possible;
- profits from the exploitation of real estate should be taxed at the lowest rate possible;
- after-tax profits should be easily distributed;
- Polish withholding tax should be reduced as much as possible;
- revenues from the future sale of real estate or the shares of a company should be taxed at the lowest rate possible or should be exempt from taxation;
- all strategies for the postponement of the tax payment date should be explored.

Addressing these points will help to design and implement a tailor-made structure.

Step-up of initial tax basis of assets

Polish tax regulations in some cases may provide the opportunity to increase the initial tax basis of assets, which provides a tax shield (by increasing the ability to make tax depreciation write-offs and to minimize taxable capital gains upon sale). An increased tax basis may be achieved e.g. upon the liquidation of a company. Careful tax analysis is always required before carrying out such transactions.

2.5. Development and construction

2.5.1 Legal aspects

As in many jurisdictions, in Poland the legal requirements relating to construction and development can be complex and present a potential mine-field for an inexperienced or poorly-advised investor. Adequate planning and thorough due diligence performed by legal and technical professionals (especially in the context of applicable zoning restrictions, formal designation of land, etc.) are essential. Mistakes or omissions at the acquisition or development planning stage can delay or even – in the worst case scenario – derail the whole process.

Nevertheless, although the Polish construction legal environment (influenced by EU laws, especially in the field of environmental requirements) may pose various difficulties for investors, a large and ever-increasing number of impressive (and internationally-acclaimed) "green field" developments (which are both commercially successful and contribute to the architecture of Polish cities) is clear evidence that there are effective legal means of doing this kind of business in Poland. In particular, despite recent difficulties in the financial markets, Poland continues to offer interesting and relatively high-yielding opportunities for international investors.

Zoning

Zoning master plans and zoning study

Local authorities (municipalities) in Poland adopt zoning plans which determine how particular areas of land may be developed. Therefore, such plans are of crucial importance to any prospective developers, as they constitute the basis for the issuance of building permits, which must strictly comply with the conditions of the applicable zoning plan.

Incidentally, on 1 January 2004, all local zoning plans in Poland adopted before 1995 expired by virtue of law, which means that a large portion of the country is currently not covered by any binding local zoning plan. Most Polish municipalities are still working to adopt new local plans. At the end of 2011 for example, 28.79% of the area of Warsaw was covered by new local zoning plans, while the figure for Katowice was 20.5% (38.5% excluding forests and parks), for Kraków 36.1%, for Wrocław 46.1%, for Gdańsk 70-72% and for Łódź 5.34%.

In some cases, if a zoning plan does not provide for the possibility of developing land with the desired structures, it is possible to initiate a procedure to amend the existing zoning plan, which is unfortunately time-consuming. The duration of the procedure and the prospects for eventual success depend on the local municipality's willingness to cooperate and, to some extent, on the local community's acceptance of the investor's initiative.

As a general rule (subject to certain exceptions), where there is no local zoning plan for a given area, it is still possible to develop a property, but an investor is required to apply for a zoning decision before obtaining a building permit.

So-called zoning studies are the preliminary (draft) stage of zoning plans and should therefore be verified before making a decision as to whether to proceed with the purchase of a property (if there is no local zoning plan for the area).

Zoning decisions

If an investment is planned for an area where there is no zoning plan (e.g. the zoning plan expired and a new one has not yet been adopted), it is necessary to obtain a zoning decision from the competent local authority, which substitutes for the plan. In such a case, the building permit will be based on the provisions of the zoning decision (the zoning decision must be obtained before the building permit).

A zoning decision is transferable to third parties, therefore, it is possible to purchase a property with a valid zoning decision (which certainly speeds up the process). The procedure of issuing a zoning decision usually takes several months.

If a zoning decision has already been issued for a certain development, but the newly-adopted local zoning plan designates the land for other types of development, the zoning decision automatically expires.

Shopping centres and wind farms

The development of facilities with a sales area exceeding 2,000 m^2 currently requires specific inclusion in the local zoning plan before it can take place. There are, however, certain opinions to the contrary and whilst some local authorities issue zoning decisions for shopping centres, such possibility is questioned by the majority of the doctrine and in October 2011 was again denied by the Administrative Superior Court. In other words, if the zoning plan does not provide that a particular parcel of land can be developed with a large supermarket, a building permit will not be issued.

The situation is similar for wind farms; although it is rather clear that a find warm investment cannot be carried out if not provided for in a valid zoning plan.

Construction permits

Building permit

A building permit, as a final administrative decision, constitutes an indispensable condition for the commencement of construction works. A building permit is transferable to a third party as long as three conditions are satisfied: (i) the consent of both parties; (ii) acceptance by the transferee of all the conditions contained in the building permit; and (iii) the transferee being able to prove that the real estate is at its disposal for building purposes (e.g. on the basis of ownership, perpetual usufruct or a lease title). Accordingly, the existence of a valid and binding building permit is often a key commercial element in a real estate transaction, and this obviously increases the value of the property.

The building authority has the power to inspect the building site works at any time. In this respect, further laws and regulations must be taken into consideration (e.g. laws regarding environmental protection and protection of historical buildings or areas). Observance of such regulations is of great importance, as any failures or errors on the part of an investor may result in significant difficulties (for instance, the suspension of construction works or refusal to grant an occupancy certificate).

The industry warmly welcomed an amendment to the law which extended the validity of building permits from two years to three. As of mid 2008, all newly-issued building permits will expire if the construction works to which they relate are not commenced within three years from the date on which the building permit became final, and also if those construction works are subsequently suspended for a period of more than three years.

Procedure and timing

The granting of a building permit is preceded by a formal application, which must be filed with the authorities by the investor within the period of validity of the related zoning decision (unless there is a zoning plan). The investor must demonstrate that it has real estate at its disposal for building purposes. The authorities verify whether the design of the development is in line with the local zoning plan, studies and other laws, including the technical conditions of the development.

The authorities should issue a decision within one month of submission of a complete application. Where matters are particularly complicated, the authorities are formally entitled to two months but, in practice, these procedures are usually more time-consuming.

Environmental issues

As part of the construction process, there are certain environmental aspects which need to be considered. An investor has to be particularly sensitive if it intends to proceed with large-scale developments. Developments are segregated into different categories, which are subject to more or less stringent legal restrictions.

The most important requirement, which has to be fulfilled before any application for a zoning decision (if the zoning permit is required) or a building permit can be submitted, is the obligation to obtain an environmental permit, which in turn must be preceded by a formal environmental assessment. As also discussed in section 2.9.1. below, the authorities may demand the preparation of a detailed environmental report before an environmental permit is issued (there is also a category of large-scale investments, with respect to which the preparation of such a report is mandatory, e.g. power plants, highways, harbours, etc.). Consequently, the investors may be compelled to carry out relatively detailed planning at an early stage of the project. However, if there is a local zoning plan covering an investment area, an environmental permit will be obtained at a later stage of the investment (i.e. before the building permit). It is also possible for an investment to be subject to an environmental assessment process twice - first, at the stage of the zoning decision, and again at the building permit stage. However, the general rule is that if an environmental permit is issued prior to the zoning decision, a further environmental permit will not be required prior to the issuance of the building permit. The environmental regulations allow for the transfer of an environmental permit to another entity.

Development completion

Occupancy certificates

In Poland, the occupation of any building or other structure is in principle subject to the issuance of an occupancy certificate by a competent authority. The only formal party to the proceedings for the issuance of an occupancy certificate is the investor, which makes for a simple procedure, particularly since neighbouring parties may not appeal. Prior to the issuance of this certificate, the authorities carry out an obligatory inspection of the development and verify whether it was constructed in accordance with the terms of the building permit.

Energy performance certificates

The increasing EU legislation requiring EU member states to cut greenhouse gas emissions is also impacting the real estate sector. Both building owners and occupiers are becoming more aware of the energy efficiency of their premises, not only because of the legal requirements, but also because locating their premises in a "green building" (premises with low energy consumption) may positively affect their image.

Consequently, Polish regulations provide for a mandatory assessment of the energy efficiency of new buildings and flats. An energy assessment must be completed before an occupancy certificate can be obtained.

In relation to used (i.e. previously occupied) buildings and flats, an energy assessment must be carried out prior to the sale or letting of the building or flat in question, or if there has been a change to the energy efficiency credentials of the building as a result of its reconstruction. The results of the assessment must be confirmed by the issuance of an energy performance certificate, which is valid for 10 years. The Energy Performance Certificate contains certain information about the energy efficiency of the building/premises (i.e. the amount of energy required for the proper functioning of the premises, measured in kWh per year per square meter).

Upon the sale or letting of the building or flat, an energy performance certificate should be provided to a purchaser or a tenant. If the certificate provided to the purchaser contains false or inaccurate data, the purchaser has the right to demand a price reduction or even cancellation of the sale contract.

However, the new law fails to regulate the situation where the seller of a property does not provide the buyer with an energy performance certificate at all. Initial indications suggest that the position taken by notaries (whose participation is required for the transfer of real estate and who are responsible for the validity of a transfer) is that they will allow a property sale to take place without an energy performance certificate in place.

Construction contracts

Current market standards

Polish law provides a legal framework for structuring construction contracts. However, as the relevant regulations of law are quite general in nature, with certain exceptions (including those described below), investors and contractors have room to apply such standards and forms as give them a suitable level of comfort. Conveniently, many foreign investors utilize this flexibility and use contract forms that have already been tested in other countries (including the popular FIDIC forms). After certain necessary adjustments, such recognised contract forms can function as appropriate legal tools for operating on the Polish market.

Accordingly, construction contracts applicable on the Polish market are often similar to those appearing in other jurisdictions. Their length depends on the complexity and value of a given project, though they should always include a set of provisions which will correctly secure the interests of the parties under Polish law. The involvement of Polish lawyers in their preparation and associated negotiations is therefore always recommended.

Contractors vs. subcontractors

Polish law provides for certain statutory solutions which differ from those in many other jurisdictions. One of them is possible joint and several liability of an investor (together with a general contractor) in respect of the payment of fees payable to subcontractors engaged by the general contractor.

Specifically, before concluding an agreement with any subcontractors, a general contractor should obtain the prior consent of the investor. The investor has the right to review and/or reject a draft subcontract. If the investor approves it, or simply fails to respond within 14 days, the subcontract is deemed to have been approved.

From the moment in which the subcontract is approved by the investor and signed by the general contractor, the investor becomes liable (together with the general contractor) for the payment of the subcontractor's fees under the subcontract (despite the fact that the investor is not a formal party to the subcontract).

These regulations are very favourable to subcontractors, but may obviously cause a very serious risk to an investor, who will not be released from its obligation towards subcontractors by proving that the general contractor has already received a fee applicable to a specific aspect of work. In the worst case scenario, the investor will be forced to pay twice for the same task (once to the general contractor, and secondly to a given subcontractor, if the general contractor fails to pay the subcontractor for any reason).

The above law is mandatory and may not be contracted out by the parties to a construction contract. However, there are various possible legal solutions which may be applied in order to reduce or even eliminate this risk, and specific legal advice should be sought by investors prior to the execution of a construction contract.

Contractor's remuneration

There is also another mandatory regulation of Polish law which is to the great benefit of contractors, but is equally unfriendly towards investors.

A general contractor may, at any time during the construction process, demand from the investor the delivery of a security instrument covering an amount up to the full fee under the construction contract (which is to secure the actual payment of the fee). Such security can take the form of, for example, a bank or insurance guarantee. Failure to provide the security may constitute a valid reason for the contractor to discontinue the works and demand payment of the fee, irrespective of the fact that the development has not been completed (however, the general contractor's remuneration should be decrease of the amount of savings made due to non-execution of works).

This obligation as well cannot be contracted out, but there are several legal structures that make it possible to properly secure the interests of both parties (the investor and the contractor).

Warranty periods and security instruments

Warranty periods and their associated security instruments are most often established by the parties under the relevant provisions of construction agreements. Usually, warranties relating to general construction quality have a period of three years, though for certain selected elements (such as roofs or facades) a longer warranty period (e.g. 10 years) is normally agreed.

In addition, the statutory provisions of law provide for some automatic liability of a contractor in the event that construction defects are identified (the duration of such liability is three years in the case of a building).

Bidding for public procurements

Many commentators and economists believe that public contracts (mostly for roads and railway infrastructure) will become one of the main engines supporting the Polish economy also in 2013, in particular, as the Polish government and municipal budgets will still be fuelled by billions of euros from European funds designated for Poland. Poland received euro 67 billion to be used during 2007-2013 and by mid-2011 only approximately 60 per cent of this amount was spent.

From a legal perspective, all public contracts of any significant value are subject to EU public procurement rules. This guarantees that all foreign investors (from within the EU) are granted equal rights and that the applicable tender rules are understandable and transparent.

As in other European jurisdictions, bidding for public contracts (including those related to construction works) usually requires participation in a public tender (open tenders and two-stage limited tenders are the two main statutory procedures). All tender participants must satisfy various specific legal requirements, providing appropriate tax and other certificates, letters from banks confirming their financial standing, reference letters, etc. (failure to do so may irrevocably eliminate them from the tender procedure).

Accordingly, the participation of lawyers (advising both bidders and public entities) experienced in this field is essential to ensure a smooth "walk" along the legal path of the tender (allowing the tender participants to concentrate on important business aspects).

Euro 2012 UEFA Football Championships

If public contracts do indeed become an important stimulation for the Polish economy, then undoubtedly contracts related to Euro 2012 were a key component in this category. The government (together with the largest cities) was guaranteeing billions of zlotys for investments designated for the development of stadiums, roads, transportation infrastructure, etc. The construction of the National Stadium in Warsaw (with more than 50,000 seats) is the flagship investment.

The Polish authorities have established an extraordinary legal environment for the realization of EURO 2012-related projects which has proved to work quite effectively, and UEFA has held it up as an example to the Ukrainian government (as Ukraine is co-hosting the championships with Poland).

Design/architectural contracts

The engagement of professional architects in construction projects in Poland is not only practically necessary, but also a formal requirement. Construction designs – when filed with the relevant authorities for their approval – must be signed by an architect having all the necessary licences who, by his or her signature, accepts responsibility for the compliance of the designs with all legal requirements and norms.

In the context of structuring agreements on architectural services, architects hold copyrights over construction designs in line with the applicable regulations. Accordingly, the use of such designs and, especially, any further modifications to them, may be subject to various restrictions, depending on the wording of the agreement. The involvement of lawyers specializing in intellectual property might be of key importance and help to avoid restrictions.

2.5.2. Tax implications

Tax treatment of the construction costs

Costs related to construction process and accrued prior to putting the assets into use form the initial value of the real estate and are recognised as tax deductible cost through depreciation write-offs or upon sale.

Costs related to future operation / exploitation of the assets should be recognised for tax purposes based on general rules.

VAT and the construction process

During the construction process, the most important tax is VAT. The standard rate of VAT in Poland is 23%. A reduced VAT rate of 8% applies to the construction of residential houses/apartments except for part of residential buildings whose usable floorspace exceeds 300 m^2 and apartments whose usable floorspace exceeds 150 m^2. In such a case only construction of the part of residential buildings and apartments, which is within the above limits, benefits from 8% VAT rate, whereas construction of the part exceeding the thresholds is subject to standard 23% VAT rate.

Purchases the investor needs to make for the construction will typically include Polish VAT. This input VAT should be deducted from the output VAT that the investor has to pay to the tax authorities as a result of his business activities. As the construction process usually takes a considerable period of time and requires the availability of substantial financial resources, it is essential that the input VAT paid be recovered during this process. Rules of VAT recovery and refunds are presented in section 2.4.3. However, during the construction process the typical situation is that the company has to pay high input VAT, but no output VAT. Therefore, specific rules need to be observed to ensure the recoverability of input VAT paid during the construction process.

Services of foreign contractors

The place of the supply of services (i.e. the place in which services are deemed to be rendered and should be taxed accordingly) depends on the nature of a particular service. Under the general rule, services rendered to a VAT taxpayer (or a legal person not being a VAT taxpayer) is where the service recipient is located. However, services connected with real estate are generally taxed where the real estate is located, i.e. in Poland. Services connected with real estate include the construction works, services of architects and firms providing on-site supervision and the services of real estate agents and property valuers.

If the place of supply of a particular service is Poland, it is possible for a foreign construction company to register in Poland as a VAT-payer. This implies that the foreign company will itself be liable for Polish VAT. The recipient of the services can recover the VAT paid to the service provider as input VAT under the general rules.

If services are deemed to be rendered in Poland and the foreign service supplier does not register and account for Polish VAT on his invoice, the Polish recipient (in this case the real estate company) must self-assess the VAT due on the basis of the reverse charge mechanism. This can then be declared by the recipient as input VAT and be deducted from its output VAT. Such a deduction may be made in the same month in which the VAT on importation of services was recognised (which means that the company suffers no adverse cash flow effect).

Taxes due on imported goods

Imported goods are always subject to import VAT when they cross the EU border (or in the EU destination country when the goods are transported under a special customs procedure). This VAT is calculated based on the customs value of the goods. It is possible to offset this input VAT against output VAT in accordance with the general VAT rules. Typically, in Poland the VAT rate is 23%.

Import VAT can be settled without the need for an upfront cash payment through the VAT return rather than being paid directly to the customs office and thereafter reclaimed (this mechanism is sometimes referred to as “postponed accounting for VAT”). This rule applies only to those importers using the simplified customs procedure.

The regulations concerning imports do not apply if goods are transported from another EU Member State. Such a transaction is classified as an intra-Community acquisition and is subject to VAT. The company is obliged to self-assess VAT on the acquired goods at the rate appropriate for them (usually 23%). At the same time self-assessed tax may be treated as input VAT and deducted from output VAT in the same month in which it was incurred.

No excise tax is due on typical construction equipment and materials.

Taxation of a foreign construction company

In some cases it is not necessary for a foreign construction company to do business through a Polish company. The construction work can be performed in Poland directly by the foreign entity. In this case the question arises as to whether the foreign company is subject to Polish income tax on the revenues generated from the construction work. Poland is indeed allowed to tax this income at a rate of 19% if the activities of the foreign company constitute a permanent establishment in Poland. Whether or not the given foreign construction company has a permanent establishment is determined by the relevant tax treaty which Poland has concluded with the country in which the foreign company is based. In general, a construction site becomes a permanent establishment once the duration of the construction works exceeds a certain period of time. Usually this period is 12 months. If the work is finished within 12 months, then no permanent establishment has been created. If the construction period takes longer, then a permanent establishment is recognised and the income derived from the work is subject to Polish income tax. It should be remembered that in such cases the permanent establishment is deemed to exist from the start of the construction activities in Poland. Standard rates and tax rules are applicable to determine the tax due.

Please note that if the activities of a foreign company in Poland extend significantly beyond a single contract, the company may be required to set up a branch. Setting up a branch will most likely lead to the creation of a permanent establishment in Poland.

2.6. Operation and exploitation

2.6.1. Legal aspects

There are no standard form lease agreements used in Poland, and lease agreements differ according to the type of property/development which is the subject of the lease (although appropriately adjusted Anglo-Saxon standards are quite common).

Lease agreements do not have to be concluded in Polish; an agreement in a different language is sufficient to make it enforceable.

As the Polish legal system recognises the principle of freedom of contract, parties may in most respects construct their legal relationship as they see fit. There are, however, certain mandatory statutory provisions, the operation of which cannot be excluded by contract, as well as certain other limitations which should be taken into account when drafting a Polish law lease. Nevertheless, it should be emphasised that Polish law allows a good degree of flexibility where lease agreements are concerned.

Leases

Types of lease agreements

Under Polish law there are two kinds of leases: a lease agreement (*najem*) and a tenancy agreement (*dzierżawa*).

Lease agreements can relate to all kinds of premises (residential, office, retail, etc.), while tenancy agreements traditionally concern land (but this is not a formal distinction and exceptions are not uncommon). For instance, the tenancy agreement has become a very popular legal device for wind farm operators (where the ownership title to land is usually held by individual farmers, who grant long-term tenancies under which the wind turbines and associated infrastructure are installed and operated).

The main formal difference between a lease agreement and a tenancy agreement is that a lease grants the right to use the land which is the subject of the lease, while the tenancy gives the right to use the land and to collect benefits from it ("benefits" being understood in the traditional sense of physical products, such as agricultural crops, minerals, etc.). This obviously does not mean that premises held under a lease agreement may not be used for business activity and the relevant profits kept by the lessee (on the contrary, the lease agreement is a very popular legal device for business entities operating in the retail industry).

Term

The duration of a lease may be fixed or indefinite. Previously, leases could only be entered into for a fixed period of up to ten years (after which the term could be extended for another defined period, but the law did not allow the parties to contract for a term in excess of ten years at the outset). Since January 2009, Polish law allows the creation of leases between business entities ("entrepreneurs") with a fixed term of up to 30 years. This change was warmly welcomed by the business community, as it clearly offers greater scope for real estate deals also sale and lease-back transactions (see section 2.8.).

A tenancy agreement may also run for an indefinite term or for a fixed period of up to 30 years (even if the parties to the tenancy contract are not business entities).

Termination options

The decision to select either a fixed term or an indefinite term has consequences for the termination of the contract. If the parties have concluded an agreement for a specified period of time, the right of either party to terminate the contract before the expiry date depends on whether the parties have stipulated in the agreement the exact events on the occurrence of which such termination is possible (and the "important reasons" may appear insufficient). Without such stipulations, the termination of a contract concluded for a specified period of time is not possible by either party, save for certain situations provided by law. It is therefore common for parties to provide in the lease agreement a detailed list of circumstances in which they will be able to terminate the contract.

In the case of a contract with an indefinite term, either party can terminate the contract by giving notice, without stating its reasons for doing so.

Rent and other charges

Lease agreements usually stipulate that the rent is subject to indexation, based on the MUICP index or (less often) upon the inflation index published by the Polish Central Statistical Office.

In addition to rent (sometimes also based on a turnover formula, in the case of retail premises), tenants are usually required to pay service charges, which represent the tenants' participation in the costs incurred by the landlord for the upkeep and operation of common areas of a development, such as repairs, renovations, insurance, cleaning, security services and waste disposal. From the landlord's perspective, it is preferable that such potential expenditures are listed in the agreement in the form of an open catalogue (i.e. if certain other costs arise, which are not listed, the tenant can be required to pay them). On the other hand, a tenant will usually try to achieve certain contractual limitations (such as caps on services charges or an exhaustive catalogue of expenses).

Payment of service charges is usually made by the tenant in the form of monthly or quarterly advance payments. Later, usually at the end of the financial year, the total operating costs of the property are settled between the parties, and, in consequence, any underpayments or overpayments are accounted for.

Less often, the parties agree on fixed service charges, which makes it easier for the tenant to budget.

Utilities and other private services provided to the tenant by third parties are usually paid for by the tenant and settled on the basis of individual meter readings or their equivalent.

Maintenance and repair

In the case of lease agreements, by law, the tenant is only responsible for ordinary minor repairs. The parties to the lease may modify these statutory duties by extending or limiting the tenant's responsibilities.

As mentioned above, in the case of a building occupied by a large number of tenants (such as a shopping centre), the landlord quite often expects to recover the costs of repairs recovered by tenants in the form of the service charges.

In the case of a tenancy agreement, the costs of all repairs, whether major or minor, are borne by the tenant to the extent necessary to keep the property in the same condition, unless the contract provides otherwise.

Expenditures settlement

By law, after the expiry of the lease term, the landlord may decide if any alterations or additions made by the tenant to the property should be removed by the tenant or surrendered to the landlord, in which case the landlord must reimburse the tenant for their market value. This rule is not mandatory, which means that the parties may make alternative arrangements in the lease contract.

Subletting and assignment

As a general rule, a tenant is allowed to sublet a leased property, unless the subject of the lease is an individual set of premises, in which case subleases require the landlord's consent. However, it is common for a landlord to reserve the right to approve any subletting in all cases. Subleases terminate by the operation of law simultaneously with the termination of the main lease agreement (as certain doubts arise if the same consequence relates to lease agreements executed on the basis of a tenancy agreement specific attention should be paid to such situations).

The landlord itself is normally permitted to assign its rights under the agreement without the tenant's approval (usually the entities lending money to a landlord will wish to obtain a conditional assignment of the benefit of the lease as security).

In the event that a leased property is sold or otherwise transferred by the landlord to a new owner, the new owner automatically becomes the new landlord under the existing lease. However, the new owner may terminate the agreement unless the following conditions are all satisfied: (i) the lease has been concluded for a definite period; (ii) the lease is in writing and has a notarially certified date; and (iii) the leased property has been delivered to the tenant. The tenant – for its own legal protection – should always make sure that the above conditions are satisfied as soon as practically possible.

In the event that a lease concluded for a definite period is terminated as a result of the sale of the property, the tenant may demand compensation from the seller.

Insurance

Commercial lease agreements usually require that the landlord takes out and pays for insurance for the property, the cost of which is later passed on to the tenant as a component of the service charge. The tenant, at its own expense, is also usually required by the lease agreement to take out a separate insurance policy covering civil liability, and any damage to the equipment or installations brought into or installed in the leased premises by the tenant.

In the case of a tenancy agreement, the obligation to insure the property is normally borne solely by the tenant.

Security

Common forms of security under lease agreements are either an unconditional and irrevocable bank guarantee (payable upon first demand of the landlord), or a cash deposit equal to three months' rent and service charges.

Bank guarantees are often non-transferable, which should be taken into consideration by landlords when accepting a bank guarantee provided by a tenant.

Some lease agreements include the provision of a parent company guarantee, which is less favourable for the landlord than a bank guarantee as it only backs up the proper performance of the tenant's obligations under the lease agreement, and does not result in immediate payment.

Destruction

Polish legal regulations concerning the destruction of leased property do not cover all eventualities and only provide that, in the event that the property is destroyed through no fault of the landlord, the landlord is not required to effect the restoration of the property (and the lease expires).

In the case of a commercial lease for a larger property, market practice is that the parties put in place much more sophisticated contractual provisions whereby the landlord is granted an option to restore the destroyed property within a certain period of time, during which the lease is suspended (but does not expire).

Eviction

In line with Anglo-Saxon standards, lease contracts quite often state that if the tenant fails to surrender the property upon the expiry or termination of the lease, the landlord may enter the premises, cut off the utilities, and evict the tenant together with its moveable property.

Such eviction clauses may prove to be invalid, as any eviction in Poland may only be performed within the limits prescribed by court enforcement procedures. The contract may, however, protect the landlord's rights in other ways, for instance, by making high value penalties payable to the landlord if the tenant fails to surrender the property, or by requiring the tenant's consent at the initial conclusion of the lease contract to a separate instrument called a "submission to enforcement" (in the form of a notarial deed) which would significantly speed up the enforcement process.

Residential leases

Residential leases are governed by separate statutes which provide special protection to tenants. Such statutes impose additional obligations on the owner of the property and stipulate a number of circumstances under which the eviction of a tenant from the leased premises is prohibited.

Green leases

An increasing number of developers and landlords are deciding to apply for green certificates for their buildings. In Poland, this tendency mostly applies to office buildings. The most popular rating systems applied on the market are LEED and BREEAM, which have been adopted from other EU states. The investors' motivation is to improve the environmental sustainability of their buildings, to reduce operational costs (for example by reducing electricity consumption) and to use the green ratings for marketing purposes (to attract environmentally-conscious tenants).

One of the legal tools that landlords use in connection with these ratings are lease forms imposing certain obligations on tenants, preventing the negative impact of their activity on the environment (reducing waste, reducing water consumption, etc). Leases that include various provisions aimed at improving the sustainability of business activities in a given property are, in the jargon of the international construction industry, known as "green leases".

In addition to leases introduced by landlords in order to obtain and keep a "green" rating, the market practice is enriched by some tenants, usually branches of large multinational corporations, that bring their own green lease standards to Poland (not only voluntarily proposing certain restrictions regarding their own activity, but also imposing various environmental requirements on landlords).

Although there are a number of known projects where green leases have been used, green leases are not yet very popular in Poland. However, there are certain new laws that may clearly promote and inspire the use of such leases. In August 2011 the Energy Efficiency Act came into force, imposing on public sector entities an obligation to perform at least two from a catalogue of actions aimed at saving energy. One of these actions is the lease of energy-efficient buildings (meaning that the lease would need to include provisions ensuring energy efficiency, and would thereby become a "green lease"). Even though they are only just starting to be used, it is a common belief that the market importance of green leases on the Polish market will grow.

2.6.2. Tax implications

Income subject to tax

Taxable income comprises the entire income generated from business activities (trade or services). Taxable income is calculated on the basis of financial statements prepared in accordance with Polish accounting standards after significant adjustments relating to the tax base. Taxable income is as a rule recognised for tax purposes on an accrual basis. The applicable tax rate is 19%.

Calculation of taxable income

Taxable revenues minus tax deductible costs constitute the tax assessment base. The costs are deductible if they were incurred for the purpose of revenue earning or maintaining/securing the source of revenue. For the exploitation of real estate, the most important costs, such as interest payments, the costs of exploitation and maintenance and depreciation write-offs, are considered tax deductible. Polish tax rules specifically exclude certain expenses from tax deductible costs. For example, doubtful receivables can only be deducted under very strict conditions. Also business entertainment costs (e.g. the cost of meals with potential customers) are non-deductible.

Loss carry forward rules

Polish legislation provides for carrying forward tax losses over five consecutive tax years following the year when the loss was incurred. The amount which can be utilized in any of these five years cannot exceed 50% of the total loss, however.

Example:

Year	0	1	2	3	4	5	6
(Loss)/profit	(100)	60	10	10	20	5	20
Carry forward	-	50	10	10	20	5	-
Effective tax base	-	10	0	0	0	0	20

Total loss effectively carried forward: 95, unutilized loss: 5.

Tax losses cannot be carried forward following certain legal transactions involving the company (e.g. mergers where the losses pertain to entities which no longer exist after the merger). There is no tax loss carry back.

Depreciation rate for real estate

The standard depreciation rate for most new buildings for tax purposes is 2.5% per year. Hence, the costs of real estate investment are generally deducted over a period of 40 years. Newly acquired buildings, used previously by a former owner, can be depreciated for tax purposes during the period equal to the difference between 40 years and the number of years that have passed since the building was put into use for the first time (that period cannot be shorter than 10 years). Land is not subject to tax depreciation.

If residential buildings constitute fixed assets used for business purposes (e.g. if they are leased) they are depreciated at a rate of 1.5% per year.

Under certain circumstances it may be worth carrying out a cost split analysis of investment expenditures prior to putting a building into use. This is because some machinery may – under specific regulations – be excluded from the value of the building and be treated as separate fixed assets depreciated at higher rates (4.5% – 20% per year). This could lead to significant tax savings as the costs incurred could be deducted over a shorter period of time. A cost split analysis should be also possible in case of the purchase of an already developed building.

Calculation of the depreciation base

The depreciation base consists of all costs incurred in making the investment: construction costs, building materials, designs, interest and foreign exchange differences accrued during the construction period, commission and potentially non-recoverable input VAT related to the building incurred before it was put into use. As the value of the land is not subject to depreciation, it is then important to determine the value of the land and the value of the building separately.

VAT implications of renting out real estate

Rental income is subject to 23% VAT. This VAT is added to the rent due and is payable by the lessee to the lessor. If the lessee is a regular VAT payer, he can deduct the VAT paid in the rent invoice from his output VAT liability resulting from taxable activities.

If the lessee performs VAT exempt business activities, the input VAT on the rent is irrecoverable. For example, the activities of banks, financial institutions and insurance companies are exempt from VAT.

If the lessee performs exempt activities, as well as taxable activities, then the input VAT on the rent can be deducted proportionately on the pro rata basis computed for a given year.

Rental of residential units for housing (but not the rental of residential units for the purposes other than housing) is VAT exempt.

Real estate tax

Real estate tax is charged to the owner (or in some cases the holder) of the land or buildings and infrastructure which are used for business activities. The local authorities set the real estate tax rates and collect the taxes. However, local authorities are bound by the following maximum PLN yearly tax rates:

- for land, PLN 0.84 per m^2 of land;
- for buildings, PLN 21.94, per m^2 of the usable surface of a building;
- for infrastructure (e.g. roads, pipelines), 2% of the value of the infrastructure calculated according to specific regulations (initial value determined for the purposes of tax depreciation).

The local authorities may differentiate between tax rates for different types of activities or locations and grant exemptions for certain types of real estate.

2.7. Exiting the investment

The investor's choice of exit strategy will also be predominantly tax driven, and it is important at the outset of the investment process to have a clear idea of the possible exit mechanics. The due diligence findings made during the acquisition phase are likely to bear relevance to the question of which exit strategy to choose, and should be given proper consideration so that the investor's position on exit will be as strong as possible.

Generally, the exit may be structured as an asset or share deal. The tax consequences of both are presented in section 2.4.3.

2.8. Sale and lease back

Under current market conditions, many companies' need for capital may bring the sale and lease-back of commercial property into the spotlight in Poland as a practical corporate finance tool.

In a sale and lease-back transaction, a company sells real estate to a financial institution and then leases it back under a long–term lease. The tax implications are fairly neutral, and in some specific circumstances can even be beneficial for the parties involved as compared to a direct financing instrument. Polish companies owning high-value assets can use a sale and lease-back to release capital which can be re–invested into business operations, resulting in a higher return.

Commercial aspects of a sale and lease-back transaction

For the seller/lessee, a sale and lease-back is a way to raise capital that is tied up in the assets because their market value has increased. This capital can be invested in the core business of the company, typically generating higher returns. These higher returns are likely to exceed the costs of the lease.

For the purchaser/lessor, a sale and lease-back is a way to carry on its core business while generating a relatively higher yield on the investment, and aiming at a substantial increase in the residual value of the property during the lease contract.

From a legal perspective, a sale and lease-back is comprised of the sale of real estate (as a straight asset sale) which is followed by the immediate leasing of that real estate back to its seller. The structure allows the seller to retain operational control over the asset, to use and manage the real estate as before, and while the purchaser pays the purchase price, it is not heavily involved in running the property.

Depreciation costs in the lease transaction

If a sale and lease-back transaction is structured as an operational lease, the buyer/lessor is in most cases the owner, and will be able to depreciate the value of the investment at the standard depreciation rate of 2.5%. Accelerated depreciation for used buildings can be considered in some cases. Other costs related to the maintenance and exploitation of the building are tax-deductible for the lessor.

Capital gain on sale and lease-back contracts

If, under a sale and lease-back contract, the real estate asset which is the subject of the contract is sold at a higher price than its net book value, a taxable capital gain will result. Under Polish legislation, it is not possible to defer the taxation of such a capital gain in order to use it for reinvestment.

Sale and lease-back versus straight debt financing arrangements

A sale and lease-back arrangement has the advantage for the seller/lessee that the lease payments are fully tax deductible as costs incurred for the purpose of earning revenue. By contrast, for the borrower party to a normal direct financing arrangement, only the interest payments made on the loan are tax-deductible. The repayment of capital is not a tax-triggering event. Under a direct financing arrangement secured by a mortgage, the debtor would still be the owner of the real estate. As such, the debtor would be unable to depreciate the value of the land. Under a lease contract, the lease payments are partly a compensation for the use of the land. Therefore, payments for the use of the land are tax-deductible for the benefit of the lessee.

The possibility of leases with a fixed term of up to 30 years (please refer to section 2.6.1. Term) will allow the Polish sale and lease-back market to move into line with that in other jurisdictions, and operate on a similar economic footing.

Due diligence

When considering a sale and lease-back transaction, the due diligence findings (for details on the due diligence process, please see section 2.9.) should be properly taken into account, not only in the sale agreement but also in the lease agreement. However, as noted above, there is no actual change in the entity running the property, and therefore, the operational risks identified in the course of due diligence may have less impact than they would in a simple asset acquisition.

2.9. Due diligence as part of the acquisition process

As a part of the investment process, investors interested in the acquisition of real estate in Poland usually conduct a due diligence review on the assets which are the subject of an asset deal or on the companies whose shares are the subject of a share deal.

The due diligence review generally focuses on an examination of the financial, tax, and legal status of the real estate or, in the case of a share deal, the target company and the real estate. Usually, the due diligence exercise is carried out by the buyer's financial, tax and legal advisors, often in conjunction with the buyer's own personnel. In addition to the financial, tax, and legal due diligence, it is quite often necessary for the buyer to retain other expert advisors, such as technical and environmental consultants or qualified surveyors.

2.9.1. Legal due diligence

Like financial and tax due diligence reviews, a legal due diligence review is an information-gathering exercise which should provide the buyer with a complete picture of the legal issues relevant to the property it wishes to acquire. A legal due diligence helps to identify areas in which the buyer will require protection, the level of protection it will require, and any risks so major that they are "deal breakers".

The scope of the legal due diligence will depend on the structure of the deal. As previously mentioned, in a share deal, the buyer assumes a greater level of risk, and so the scope of the due diligence will generally be greater than that required for an asset deal.

In particular, a legal due diligence should focus on the following issues:

- title to the property;
- third party rights and claims to the property;
- planning and zoning issues;
- development and construction documentation;
- utilities supply documentation;
- leases;
- environmental matters; and
- corporate issues pertaining to the company holding the property (in the case of a share deal).

For the purposes of the due diligence exercise, the buyer's legal advisors usually rely on the documentation provided by the seller in response to a due diligence questionnaire which the buyer's legal advisors send to the seller at the start of the process. In addition, the buyer's legal advisors should examine publicly available sources, and undertake searches of files stored at the Land and Mortgage Register and the commercial registers.

Common legal due diligence issues

This chapter does not attempt to review all matters in detail, but is intended to bring to the reader's attention certain common material issues specific to Poland.

Pre-emption rights

A pre-emption right provides an entity with a right of first refusal, allowing it to purchase the property in question for the same price as the property is offered to a potential purchaser. Initially, the parties to a transaction should execute a conditional purchase agreement, and notify the pre-emption right holder of the existence of such agreement. A final property transfer agreement (necessary to transfer the title to the real estate) will only be concluded if the pre-emption right is not exercised (i.e. if expressly waived or not exercised within a specified period - often one month).

Pre-emption rights can arise: (i) by statute - in which case, any sale of real estate without notice to the pre-emption right holder renders the sale invalid; or (ii) by contract - in which case, a sale without notice to the pre-emption right holder will be valid, but will provide grounds for a claim for damages and, in the worst case scenario, may be held as ineffective against the pre-emption right holder.

The most common statutory pre-emption rights in Poland are those benefiting a municipality, often relating to the purchase of:

- undeveloped real estate originally acquired from the State Treasury or local authorities;
- RPUs relating to undeveloped land, regardless of how the right was acquired by the seller;
- real estate designated for, or situated in, an area designated for use for public purposes or public investment projects under the local master plan or administrative decisions;
- real estate entered in the register of historic monuments, unless such right is not entered in the Land and Mortgage Register.

Secondly, pre-emption rights often affect agricultural lands, where the beneficiary is the Agricultural Property Agency. Statutory pre-emption rights also relate to properties located in special economic zones and should also be considered in detail in such cases.

The statutory pre-emption right is common in Poland, but such rights are rarely exercised by the authorities. In the majority of cases the issue may be considered a formality, and part of the acquisition procedure. It should be noted that this will cause a slightly extended transaction timetable, requiring a two-stage (or sometimes three-stage) process with conditional (preliminary) and final agreements. Transaction costs are likely to be slightly higher. However, given the potential invalidity of a transaction if the correct procedure is not adhered to, it is essential to identify all pre-emption rights related to a property during the due diligence process, and to verify whether such rights have been properly respected in the past.

Restitutions claims

In the aftermath of the Second World War, many real properties and any functioning enterprises (including their real estate assets) in Poland were "nationalised" (or "communalised"). Currently, Poland is the only country in Central and Eastern Europe that has not introduced specific laws to deal with restitution matters. As a result, the legal status of nationalized properties is quite often subject to uncertainty; although recently the jurisprudence is fairly unanimous as regards protection of the purchaser of nationalized plots acting in good faith and the irrevocable legal effects (which relate to civil acts i.e. property purchase agreements). Former owners or their successors may initiate proceedings aimed at the restitution of such real estate.

Warsaw

In 1945, under a special decree on land ownership applicable only to Warsaw, the City of Warsaw gained ownership rights to the majority of real estate in the city. However, the decree granted former owners the possibility to obtain usufruct rights to the real estate that had been nationalised, or compensation. Owners would have to satisfy two conditions: filing a motion within six months of the City taking ownership, and using the real estate in a manner consistent with the zoning plan in force at that time. During the 1970's, many such applications were re-examined and it was often found that decisions were made in contravention of the law – allowing successful claims for invalidity today. Again, with respect to Warsaw-based transactions, it is essential to investigate whether any such proceedings are pending with respect to the target property.

The City of Warsaw published a list of real properties located within the city's boundaries which are affected with restitution claims. According to its content, the districts of Warsaw with the highest number of such claims are Śródmieście (City Center), Praga Południe, Mokotów and Bielany. The list is accessible for the purposes of the above-mentioned investigations, but it is unofficial in nature.

Many claims for return of the expropriated properties are also based on the argument that the real estate is no longer useful for the purpose identified in the original expropriation decision, for instance, where the authorities decide that the property was in fact not used or was redundant for the purposes of expropriation. Restitution claims may also be based on arguments against the validity of the original nationalisation decision, usually because procedural conditions were not satisfied at the time.

Previous owners might apply to a civil court to have property returned if they have a legitimate restitution claim and a historic administrative decision on nationalisation is revoked. Such claims might be successful where the property is in the hands of the state/municipality or legal successors of state-owned enterprises (the irrevocable legal effects did not occur in such a case). Alternatively, the property might currently be held by a private individual or entity. However, in such a case, a claim is only likely to be successful if the existing or previous owner acquired the property from the state/municipality acting in bad faith. Prior to such action, claimants must apply for a court decision declaring recent property acquisitions/transfers (following nationalisation) invalid. As the current owner benefits from public reliance on the Land and Mortgage Register, the outcome of such a claim for invalidation will primarily depend on the apparent good faith of the current and previous owner at the time they acquired the property (see section 2.1.2. on Land Registration).

However, despite the risk of restitution claims, in practice, property acquisitions are typically successfully finalised and any associated legal risks can be mitigated, for instance, by due diligence or by purchasing title insurance if a restitution claim is pending.

Agricultural land

In Poland, specific regulations and treatments attach to agricultural land. For instance, prior to the acquisition of agricultural land by any foreigner (including citizens and corporate entities from the EEA), a permit from the Ministry of Internal Affairs must be obtained. Note that the proceedings for the issuance of a permit last between one and two months. Additionally, investors should bear in mind that the Agricultural Property Agency has a pre-emptive right towards arable land of an area of at least 50,000 meters.

Furthermore, the development of agricultural land is not always possible, or may be more difficult than with respect to industrial or other land. Before commencing construction, arable land should be re-designated as "non-arable" in the local zoning plan. Subsequently, a further decision is also required for the exclusion of the land from agricultural production. These requirements impact on the timing of a development and on the costs – we discuss the associated fees briefly in the section on Fees below.

These complications are becoming less commonplace, in particular, because the area of arable land in Poland is rapidly declining, mainly due to two factors. Firstly, as of 1 January 2009, all agricultural land located within the administrative boundaries of cities is no longer subject to the restrictions applicable to other agricultural land. Secondly, local zoning plans are increasingly being adopted, which is an early stage of the change of the designation of land from arable to non-arable use. However, such land will still require actual exclusion of the land from agricultural production.

Fees

Charge for a rise in the value of land (further "adiacencka" fee)

If the value of a property increases due to its division, division followed by a merger, or the construction of infrastructure with the use of public funds (placing water pipes, sewage pipes, heating systems, electricity, gas and telecommunications facilities), the owner of the real estate (or perpetual usufructuary) may be obliged to pay an "adiacencka" fee. However, an "adiacencka" fee may not be higher than 30% (with respect to a division) or 50% (with respect to a division followed by a merger and the construction of infrastructure with the use of public funds) of the increase in value of the property. The "adiacencka" fee does not apply to the construction of infrastructure on real estate designated in the zoning plan for arable or forestry purposes.

Zoning fee

The adoption of a zoning plan may sometimes lead to an increase in property value, and also requires the payment of a zoning fee, which may not be higher than 30% of the increase in value of the property. The zoning fee is payable by the vendor in the case of a transfer of the property within 5 years from the day when the zoning plan came into force.

Exclusion from agricultural production fee

Exclusion from agricultural production is subject to an initial fee and subsequent annual payments. The value of such payments depends on:

- the area of the site subject to exclusion;
- the quality of the land (class of soil); and
- market value of the site in question.

Due diligence and title insurance

The Polish real estate market is becoming relatively mature, and is now competitive and features most of the usual services and advisors as you would expect in any European market. Legal, accounting and financial advisory services are provided to an international standard. Due diligence is an essential component of most transactions and, where provided by well-regarded advisors, allows for reliance by insurance providers, often significantly reducing potential risk to investors by identifying problematic issues, and resolving them or insuring against them.

Investors pushing for higher yields are often ready to accept a higher level of risk, and such activity has driven the development of sophisticated instruments to mitigate these risks. Title insurance is available in various forms to cover issues identified during due diligence, but it may also be applied to protect against unknown risks that may arise after completion of the transaction. The use of title insurance often provides for smoother negotiations, or can be used as a bargaining tool; it can be arranged in advance so that the seller can present a complete package to potential bidders, and it fundamentally allows the possibility of dealing with a property subject to known risks in a market where new investors may feel less comfortable with the legal regime. The costs vary, depending upon the nature of the risk and, perhaps, the time-frame of the transaction, but are rarely excessive, and often allow for cost savings through a shorter negotiation process.

Environmental issues

Introduction

Environmental laws and regulations in Poland affect the business operations of most entities in a number of ways, including by requiring consent to emit pollutants into the natural environment. Given the problems with existing land contamination in some areas of Poland, particular attention should also be given to the land contamination regime.

Permit requirements

There are basically two types of environmental permit, one related to the construction investment process, and the other to the operation of a commercial entity, covering, for instance: waste management and the emission of pollution or disposal of sewage into any surface/ground water. Sewage disposal may affect the operation of any business when the level of pollution exceeds the applicable norms. Sometimes an integrated permit covering all permits related to the operation of an entity is required. Particular attention to such permits should be paid in the case of the acquisition of industrial installations (especially power plants, factories and other large industrial establishments).

Noise standards should also be considered. A permit is only required if the noise emissions exceed the applicable standards. In certain scenarios (e.g. wind farm investments), noise restrictions should be considered in conjunction with the zoning conditions of the site, which may prohibit installations in the vicinity of residential estates.

"Green Building" requirements and Energy Performance Certificates have been discussed previously under section 2.5.

Polish regulations provide for the possibility of transferring an environmental decision (as discussed in section 2.5) and allow for amending a building permit after an environmental decision is issued without the need to re-apply for the environmental decision.

Liability for contaminated land

According to the applicable regulations, if the land is contaminated, the responsibility for carrying out decontamination works and for bearing the associated costs depends on when the contamination occurred.

Two different regimes governing liability for soil contamination exist in Poland.

In summary, the current situation regarding liability for soil contamination is that:

- if the land was contaminated before 30 April 2007, the purchaser could be held liable for the cost of decontamination works; however, if the contamination occurred before 1 September 1980, the purchaser may only be obliged to conduct decontamination where the pollution presents a threat to life or health, or where there is a threat of further damage or of the pollution spreading;
- if the soil was contaminated after 30 April 2007, the original polluter will be liable for soil decontamination.

The risk associated with potential liability for soil decontamination depends on the condition of the site, and in practice usually only arises when heavy industrial activity was previously conducted on the site. This may be assessed by the buyer's environmental consultants in the course of their on-site investigation. Moreover, investors may wish to take out environmental liability insurance to reduce exposure.

Environmental impact assessment

In respect of large-scale developments, a specific environmental impact study may be required (with respect to such projects as power plants, highways and harbours, such a study is mandatory). Prepared by independent entities, the study describes the impact that the intended development may have on the environment.

The outcome, presented in the form of a report, constitutes the basis for the local authorities to issue an environmental permit (as discussed in section 2.5.), which includes a list of detailed conditions.

This stage is crucial for construction investments and must be verified in detail during the due diligence process. Any shortcomings may affect the validity of later decisions, and impact on the development timetable and budget.

In order to make proceedings more transparent, the new law allows a number of entities to actively participate in the proceedings. For instance, ecological organisations have been granted the right to participate in environmental assessment proceedings. Such entities may appeal against a decision (an environmental or building permit) even if they did not participate in the first instance proceedings.

The subject regulations have been widely criticised by the industry since their adoption.

2.9.2. Financial due diligence

There are very few investors who do not conduct financial due diligence as a part of a real estate transaction. This may be done internally and informally as a part of the investor's own procedures, in order to assess the viability of the transaction.

Whilst this may be a successful approach, particularly for smaller transactions, many investors recognise the value of outsourcing financial due diligence to an expert third party professional service provider. This can be especially valuable for larger transactions, where the investor may often be under time pressure from the vendor (e.g. in an auction process).

Some investors considering asset deals may be tempted not to complete due diligence as they are not acquiring a company, but they should be aware that a financial due diligence process can show them how such assets will perform after the transaction in terms of revenues and net operating income (NOI). Due diligence may also reveal some issues such as inconsistencies between rents described in lease agreements and the actual payments received as per the accounting records, which need to be clarified.

Typically a purchaser uses financial due diligence to help address the following main concerns in relation to a transaction:

- what is the NOI of the property, based on the existing lease portfolio?
- is the NOI distorted by lease incentives (e.g. reduced rentals for a period or improvements made by tenants)?
- are the accounting policies used appropriate for the business and how do they compare with the investor's own accounting policies?
- is there any evidence of tenant delinquencies or that the lengths of time taken to collect rent are worsening?
- do the service charges made by tenants cover the running costs of the building and are there any disputed service charges?

Financial issues analysed

In order to address the above questions within the scope of a financial due diligence review the following actions would normally be taken:

- considering whether the financial results presented are reliable and the figures/information contained in them can be reconciled with reliable source data;
- assessing the appropriateness and consistency of key accounting policies and practices;
- assessing the impact which the accounting policies may have on the financial results;

- ensuring that the generation and quality of management information is appropriate and sufficient for the business in question;
- assessing the contractual commitments of the business and their impact on the future profitability/cash flows of the business;
- assessing key issues affecting the underlying earnings position;
- understanding the basis for cost recharges made and identifying areas for improvement;
- understanding the "normal" working capital and cash flow cycles of the business, and the likely future funding requirements of the business;
- ensuring that construction costs have been appropriately accounted for in the company's books;
- understanding the net asset base being acquired; identifying potential balance sheet valuation issues; ensuring that all issues have been properly treated in assessing the underlying earnings;
- checking the rent roll against the lease agreements and accounting records;
- checking the service charges levied against the accounting records; and
- reviewing lease agreements to check for off balance sheet liabilities.

2.9.3. Tax due diligence

Tax due diligence, in general, focuses on assessing material tax risks pertaining to assets or shares by reviewing the tax position of the target company. By identifying tax risks during due diligence conducted before the transaction, the investor may seek protection or indemnification from the seller.

From a tax perspective, it is also important to ensure that the appropriate tax structure is used, which usually involves a pre-transaction study and the preparation of the transaction structure in accordance with the Polish and international tax regulations. In addition, it can also include an assessment of the tax implications of a future exit scenario.

Acquisition of assets

In the case of an asset deal deemed to be the acquisition of business as a going concern or a viable part of that business, the acquirer may be held liable for the outstanding tax liabilities of the seller. This liability is excluded if the acquirer could not have become aware of the seller's tax arrears despite acting with due diligence in attempting to identify such tax arrears. Performing a tax due diligence review is thus a way to limit or exclude such liability.

In the case of a sale of single assets (not constituting the viable part of a business), it is still possible (because the relevant tax regulations are unclear) that the acquirer may become liable for the outstanding tax arrears of the seller, but only for periods before 2009.

This liability is in practice of a 'subordinated' nature, as even if a formal decision declaring that the acquirer is liable for the seller's tax arrears is issued, the claim against the acquirer may crystallize only if the enforcement procedure against the seller is ineffective (and tax claims against the seller are not satisfied).

According to the tax regulations the acquirer (with the seller's consent) or the seller may submit to the tax authorities a formal request for a certificate which lists all the tax liabilities which are transferable to the acquirer. The acquirer is then liable only up to the value of the tax liabilities presented in the certificate.

Acquisition of shares

In the case of a share deal, all the potential outstanding liabilities remain with the acquired company. As a consequence, the acquirer faces the possibility of incurring an economic loss on the transaction if undisclosed tax liabilities become apparent afterwards. Tax due diligence is therefore conducted to allow the acquirer to assess and minimize this risk.

Generally, the period of limitation for tax liabilities is 5 tax years following the year in which the tax is payable. In practice this means that from the perspective of 2012 there is still a tax risk in relation specifically to a target's corporate income tax payments for 2006–2012, and to other tax liabilities, in general, for 2007–2012.

Tax issues analysed

The scope of a tax due diligence review depends on the structure of the planned transaction.

In the case of an asset deal, the scope of due diligence depends on the subject of the transaction and the extent to which the acquirer may be liable for the seller's tax liabilities.

In the case of a share deal, as the acquirer faces the full impact of any tax liabilities assumed, full due diligence is usually conducted.

The tax due diligence in case of a share deal usually covers the following areas:

- review of tax returns for periods previously filed and review of tax calculations for periods that are not yet filed with the tax authorities;
- review of the results of past tax audits to detect tax risks for periods that are still open for tax audits by the tax authorities;
- review of any obtained tax rulings;
- review of any losses carried forward, tax credits and special tax privileges to identify related tax risks for unaudited periods and to assess whether such tax benefits will be available post transaction;

- review of withholding tax procedures and exemptions available;
- review of significant historical reorganizations and one-off transactions and their impact on the tax accounts;
- review of intercompany transactions and present transfer pricing policy in the company;

as well as an examination of areas typical for a real estate company, such as:

- the existing debt financing structure (e.g. debt push down schemes), thin capitalization and other pending restrictions on the tax deductibility of interest payments on the debt;
- any large differences between book and tax basis of assets, analysis of the deferred tax calculations, in particular identification of any deferred tax liability, e.g. from accrued foreign exchange gains;
- rules for capital expenditure recognition and the impact of foreign exchange differences on the initial value of fixed assets for tax depreciation purposes;
- policies for the tax depreciation of assets, including a review of cost segregation schemes;
- cash incentives offered to tenants such as a rent free period or step-up rent and their impact on the tax accounts;
- treatment of the investment costs incurred by lessees (leasehold improvements) when the lease expires;
- tax recognition of management charges payable by special purpose vehicles to servicing companies within the group;
- any step-up in the value of the real estate performed;
- review of input VAT refunds in the investment phase; and
- policies for real estate tax

A review of the sale and purchase agreement (SPA) for the acquisition of a real estate target usually covers the following tax points:

- review of the tax definitions in the SPA, and of the tax representations and warranties;
- review of the tax indemnity clauses in the SPA; and
- analysis of the SPA from the perspective of other protection available against tax exposures.

2.9.4. Using the due diligence results in negotiations

At the end of the due diligence process, the investor is provided with an overall assessment of the financial and tax risks, which constitutes source information for negotiations with the seller and helps fine tune the financial model used for valuation purposes.

This information may be used to obtain price reductions in order to offset potentially significant tax liabilities and in the drafting of warranties and indemnities in the SPA.

This information may have a direct influence on the structure of the transaction, e.g. a change from a share deal to an asset deal, as well as serve for post-acquisition tax planning purposes.

Together with the results of the tax and financial due diligence, the results of the legal due diligence review should help the buyer to decide whether to complete the acquisition and if so, on what terms. Due diligence investigations allow the buyer's legal advisors to draft the transaction documents in a way that provides the buyer with an appropriate level of comfort and protection. As a result of the due diligence, the legal advisors will know which issues need to be addressed by the inclusion of conditions precedent, and which issues can be addressed by requesting representations and warranties from the seller. The legal advisors will also be able to assess whether such representations and warranties will need to be supported by an indemnity clause or other legal instruments permitted under Polish law.

All this makes the financial, tax and legal due diligence reviews a powerful bargaining tool which may have an impact on the outcome of negotiations, and particularly the final price the buyer is willing to pay.

3. Accounting aspects of investing in the Real Estate market

3.1. Polish accounting regulations

3.1.1. Introduction to the accounting framework in Poland

Polish accounting is regulated by the Accounting Act of 29 September 1994 (the Act). The Minister of Finance has also issued several regulations covering specific accounting areas such as financial instruments, consolidation, accounting for banks, insurance companies, investment funds and pension funds. Since 2002 the Accounting Act has been undergoing significant changes to bring Polish accounting principles closer to the International Financial Reporting Standards (IFRS). However, due to the many changes in IFRS, some differences continue to exist between the Act and IFRS as noted below.

In 2002 the Accounting Standards Committee was established. Since that time up to October 1, 2009 it has issued National Accounting Standards to implement the Act.

- KSR 1 "Cash flow statement"
- KSR 2 "Income taxes"
- KSR 3 "Construction contracts"
- KSR 4 "Impairment of assets"
- KSR 5 "Leasing"
- KRS 6 "Provisions, accruals, contingent liabilities"

The Committee also issued four standpoints (not a standard) on topics related to bookkeeping, accounting for emission rights, inventory valuation and green certificates. In any matters not regulated by the Act or Decrees issued by Ministry of Finance an entity may apply National Accounting Standards. In the absence of relevant local regulations, the entity may apply International Financial Reporting Standards.

The amendments to the Act, which came into force on 1 January 2005, permit some Polish entities to apply IFRS as adopted by the EU as their primary basis of accounting. The application criteria are summarized in the following table:

	Standalone financial statements	Consolidated financial statements
1. Entities listed on a regulated market in Poland or other European Economic Area (EEA) country.	Choice	Required
2. Banks (other than those included in 1, 3 and 4).	Not permitted	Required
3. Entities that applied for permission to list on a regulated market in Poland or other EEA country*.	Choice	Choice
4. Entities that are part of a group where the parent prepares consolidated financial statements in accordance with IFRS as adopted by EU.	Choice	Choice
5. Branches of a foreign entrepreneurs.	Choice	Not applicable
6. Other entities.	Not permitted	Not permitted

*** The Companies which filed prospectus to the Financial Supervision Committee in Poland or other EEA country.**

As of 18 March 2008, further amendments to the Accounting Act were published. The majority of the amendments became effective as of 1 January 2009 and have been applicable to financial statements for the annual periods beginning on or after 1 January 2009. It required the following additional disclosures in the notes to the financial statements: agreements not recognized in the balance sheet, significant related party transactions not on an arms' length basis and remuneration of the auditor or the audit firm. Amendments to be applied in the financial statements for the financial year beginning in 2009 amongst others included:

- recognition of changes in the fair value of investment properties and intangible assets classified as investments;
- possibility to cease application of IFRS as the primary basis of accounting;
- change of the capital group definition;
- changes to application of the pooling of interest method for business combinations.

3.1.2. Application of the Principles of the Accounting Act

The provisions of the Act shall apply, subject to the provisions of Paragraph 3 of the Act, to the following entities whose registered offices or place of executive management are located on the territory of the Republic of Poland:

- commercial companies (partnerships and companies, including those in the process of setting up) and civil partnerships, as well as other legal persons, except for the State Treasury and the National Bank of Poland;
- natural persons, civil law partnerships established by natural persons, general partnerships established by natural persons and professional partnerships, if their net revenue from the sales of goods for resale, finished goods and financial transactions for the prior financial year amounted to at least the Polish zloty equivalent of EUR 1,200,000;
- organizational entities operating on the basis of the Banking Law, regulations on trading in securities, investment fund regulations, insurance regulations or regulations on the organization and operation of pension funds, regardless of their level of revenue;
- communes, provinces, voivodships and their associations, as well as state, communal, district and provincial entities such as:
  - auxiliary units of public sector entities;
  - budget entities;
  - special purpose funds without the legal personality;
- organizational units without the legal personality, except for partnerships;
- foreign legal persons, foreign units without the legal personality and foreign natural persons conducting activities in the Republic of Poland personally, through an authorized person, with the aid of employees - in respect of business activities conducted in the Republic of Poland, regardless of the level of revenues;
- entities not mentioned above, if they receive subsidies or subventions from the State budget, budgets of local authorities or special purpose funds for carrying out relevant assignments - from the beginning of the financial year in which those subsidies or subventions were granted.
- natural persons, civil partnerships established by natural persons, registered partnership of natural persons and professional partnerships may apply the accounting principles specified in the Act from the beginning of the subsequent financial year, if their net revenue from the sales of goods, and products and financial transactions for the preceding financial year are less than the Polish zloty equivalent of EUR 1,200,000. In that case, such persons or partners are required to notify, before the beginning of the financial year, the tax office relevant to income tax matters.

Entities should have documentation which describes, in Polish, its adopted accounting policies, in particular those related to:

- the determination of the financial year and reporting periods covered by it;
- the methods of measuring assets, liabilities and equity, and determining the financial result;
- the manner of keeping the books of accounts, including at least a corporate chart of accounts with adopted principles of events classification, principles of keeping subsidiary ledger accounts and their linkages with general ledger accounts;
- a list of the books of accounts and, in the case of computerized books of accounts, a list of data files composing the books of accounts on electronic data media, with the specification of their structure, mutual linkages;
- a description of the data processing system and, in the case of computerized books of accounts, a description of the computer system, including a list of programs, procedures or functions;
- a system protecting data and its files.

Accounting records should be kept and financial statements drawn up in the Polish language and expressed in the Polish currency.

3.1.3. Valuation of selected balance sheet items applicable for real-estate sector entities

Investment property

The definition of investment property includes properties, which are not used by the entity for its own purposes, but which are held for the purpose of generating profits through capital appreciation and/or proceeds from rental. Investment property is valued at a purchase price decreased by depreciation and impairment write-offs (cost model) or at its fair value (fair value model). Each entity has a policy choice for the valuation model used.

Fair value model

If the fair value model is selected, the changes in the fair value of investment property are recognized in the income statement as other operating costs or other operating income (before the amendments to the Act which came into force on 1 January 2009 changes in the investment property fair value were recognized through equity).

Cost model

If the cost model is applied, investment property is recognized and subsequently measured at acquisition or construction cost, less accumulated depreciation and accumulated impairment write-offs. Land is valued at its acquisition cost reduced by impairment write-offs. investment properties, except for land, are depreciated on a straight-line or other systematic basis over the investments' estimated useful lives.

Borrowing costs which relate to the construction, adaptation, assembly or improvement of an investment property are capitalized as part of the cost of the asset, where those borrowings have been drawdown for that specific purpose through to the date of the completion of the construction or improvement.

Other investments

Financial instruments

Financial instruments are initially recognized at their acquisition cost (price), being the fair value of the consideration given. The costs of the transaction are included in their initial value.

After initial recognition, financial assets (including derivatives and embedded derivatives) are classified into one of the following four categories and reported as follows:

- held to maturity – measured at amortized cost, calculated using the effective interest rate;
- loans and receivables – measured at amortized cost, calculated using the effective interest rate. Short term receivables for which no interest rate has been set are measured at the amount due;
- held for trading – measured at fair value with unrealised gains/losses recorded in the profit and loss account;
- available for sale – measured at fair value, with an unrealised gains/losses recognized in the profit and loss account or in the revaluation reserve component of equity until the investment is sold or impaired at which time the cumulative gain/loss is included in the profit and loss account – the policy choice should be made by the management of entity.

Loans and borrowings are initially recognized at cost, being the value of the funds received and including transaction costs associated with the borrowing/loan. After initial recognition, all interest-bearing loans and borrowings, other than liabilities held for trading, are measured at amortized cost, using the effective interest rate method.

Financial liabilities, except for hedged items, are valued at amortized cost not later than at the end of the reporting period. Liabilities which are held for trading are subsequently measured at fair value. Any gain/loss from re-measurement to fair value is included in the net profit/loss for the period.

The companies that do not meet statutory audit requirements may elect not to apply the above valuation methods if it does not affect the true and fair presentation. In this case, investments may be accounted for as follows:

- short-term investments – at the lower of cost or market value, at fair value or at amortized cost (if a maturity date is known) with gains/losses recognized in the profit and loss account;
- long-term investments – at cost less impairment or at fair value with gains/losses recognized in the revaluation reserve in equity (surplus over the cost of investment) or in the profit and loss account (when the fair value is lower than cost of the investment). If a maturity date is known, long-term investments may be stated at amortized cost.

Investments in subsidiaries, associates and jointly controlled entities and other long-term investments

Investments in subsidiaries, associates or joint ventures can be carried at historical cost, equity accounted or at fair value. If carried at fair value, an increase in the fair value is recorded in the revaluation reserve. A decrease in the fair value of a previously re-valued investment, which does not exceed the amount of the previous revaluation, reduces the revaluation reserve if the surplus on revaluation has not been amortized by the date of the measurement. In all other cases, the effects of a decrease in the value of an investment are recognized as financial costs. An increase in the value of an investment, which is directly related to a decrease that has been previously recognized as finance costs, is recognized as financial revenue up to the amount of such expense.

The fair value of financial instruments traded on an active market is established with respect to the prices listed on such a market as at the balance sheet date. If there is no such a listed market price, the fair value is estimated based on the listed market price of a similar instrument or based on the expected cash flows.

Inventories

The inventory should be stated at the lower of cost or net realizable value. Capitalization of financial costs in the inventory is permitted if the production process requires a necessary long period of manufacturing. No specific provisions related to real estate inventory exist.

Construction contracts and provisions of KSR 3

According to the Act, revenues from construction contracts shall be determined at the balance sheet date in reference to the stage of completion providing that:

- the performance period of the service is longer than 6 months;
- the substantial part of the service has been carried out before the balance sheet date;
- the stage of completion, as well as the anticipated total cost, may be estimated reliably.

The stage of completion shall be estimated using the method approved by an entity and based on:

- the share of costs incurred from the contract commencement date in total estimated service performance costs;
- the number of working hours attributable directly to the service performance;
- the measurement of work carried out;
- another method – provided that it reflects the stage of completion reliably.

Regardless of the revenue calculation method used, when it is probable that total contract costs will exceed total contract revenue, the expected loss shall be recognized as an expense immediately.

In November 2006 the National Accounting Standard 3 "Construction contracts" was issued. The standard covers, among other, the following topics: determination of the stage of completion, determination of revenues and costs of uncompleted construction contract, presentation and disclosure of information in the financial statements, deferred tax resulting from construction contracts. The provisions of KSR 3 are in general in conformity with the IAS 11 Construction Contracts, although certain differences between these two regulations do exist.

Foreign currency transactions

Transactions denominated in foreign currency are translated into Polish currency at the actual exchange rate applied on the date of the transaction, or, if the actual rate is not known, at the rate published by the National Bank of Poland.

At the balance sheet date, assets and liabilities denominated in foreign currencies (other than shares in subsidiaries and associates valued using equity method) are translated using the National Bank of Poland rates.

Foreign exchange differences arising on revaluation are generally recorded as financial income or financial expense. For certain types of long-term investments denominated in foreign currencies gains are recognized in the revaluation reserve. Foreign exchange differences relating to liabilities which are used to finance the assets under construction are capitalized to the cost of the constructed assets.

Deferred tax

Deferred tax is calculated, using the liability method, on all temporary differences at the balance sheet date between the tax base of assets and liabilities and their carrying amounts. Deferred tax liabilities are recognized for all taxable temporary differences. Deferred tax assets are recognized for all deductible temporary differences and unused tax losses, to the extent that it is probable that taxable profit will be available, against which the deductible temporary differences and unused tax losses can be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply (as enacted at the balance sheet date) in the period when the asset is realized or the liability is settled. The Income Taxes Standard (KSR 2) also requires that additional tax credits given to companies operating in Special Economic Zones are recognized as government grants e.g. giving rise to a deferred income. Such a deferred income is to be amortized over the useful life of the asset.

Those companies that do not meet the criteria for statutory audit (see section 3.1.6. below) may elect not to recognize deferred taxes.

Leases

A lease is classified as a finance lease if at least one of the following seven conditions is met:

- the legal title is transferred upon lease expiry;
- the asset may be purchased by the lessee at a price lower than the market value upon lease expiry;
- the lease term is longer than 75% of the economic useful life of the leased asset;
- the sum of the discounted minimum lease payments is higher than 90% of the market value of the leased asset as at the lease inception;
- the lease can be extended on more favorable terms;
- if cancelled, the lessee bears all cancellation costs;
- the asset is adapted to the specific needs of the lessee.

Those companies that do not meet criteria for statutory audit requirements (see section 3.1.6. below) may adopt simplified accounting for leases, i.e. to account for the leases in accordance with the tax treatment.

Business combinations

Business combinations that are not under common control are accounted for using the purchase method. The pooling of interest method may be used for business combinations that are under common control.

3.1.4. Financial statements

All entities required to apply the provisions of the Act are obliged to prepare its financial statements and consolidated financial statements (if applicable) for each financial year. The financial year need not be the calendar year.

Financial statements must be prepared in the Polish language and expressed in the Polish currency. Financial statements consist of:

- introduction;
- balance sheet;
- income statement;
- statement of cash flows;
- statement of changes in equity;
- additional notes and explanations.

Joint-stock companies, limited liabilities companies, insurance companies and state-owned companies are required to prepare, in addition to the financial statements, the Director's report – detailed content requirements are specified in Article 49 of the Act.

The format of the balance sheet, income statement, statement of cash flows, statement of changes in equity and the contents of notes to the financial statements are determined by the Accounting Act. Companies listed on the Warsaw Stock Exchange when preparing the financial statements in accordance with the Act are guided by specific regulations for public entities, which include a reconciliation between the results reported in accordance with the Act and those in accordance with IFRS as adopted by the EU.

The financial statements of issuers of securities admitted to, issuers of securities intending to file for admission to, or issuers of securities pending admission to trading on one of the regulated markets of the European Economic Area, may be prepared in accordance with IFRS. Consolidated financial statements of issuers of securities admitted to public trading on a regulated market of the European Economic Area shall be prepared in accordance with IFRS. In addition, the financial statements of entities being members of a capital group, in which a parent company prepares consolidated financial statements under IFRS, may be prepared in accordance with IFRS. The decision in respect of the preparation of financial statements in accordance with IFRS, shall be taken by an approving body.

Entities which prepare their financial statements in accordance with International Financial Reporting Standards shall apply the provisions of the Act in matters not regulated by IFRS including:

- the principles of maintaining accounting books (it will not, however, include the format of financial statements) (Chapter 2)

- stock taking (Chapter 3)
- auditing and publishing financial statements (Chapter 7)
- directors' report (Article 49)
- protection of data (Chapter 8)
- penal liability (Chapter 9)
- specific and interim provisions (Chapter 10)

The entity's management shall ensure that the annual financial statements are prepared within three months from the balance sheet date. The annual financial statements shall be approved by the approving body within 6 months from the balance sheet date. Prior to the approval, if required, the annual financial statements are subject to an audit. If the annual financial statements of an entity are required to be audited, they shall be filed with a relevant court register together with a statutory auditor's opinion, a copy of the resolution or decision of the approving body concerning the approval of the annual financial statements and the resolution on profit distribution or loss coverage, as well as with director's report, within 15 days from the date of the approval of the annual financial statements.

Additionally, an introduction to the financial statements being a part of the notes to the financial statements, a balance sheet, a profit and loss account, a statement of changes in equity, and a cash flow statement for the given financial year, together with a statutory auditor's opinion, and a copy of the resolution of the approving body on the approval of the financial statements, and the profit appropriation or loss coverage are required to be published in Dziennik Urzędowy Rzeczypospolitej Polskiej "Monitor Polski B" and in the case of co-operatives, in "Monitor Spółdzielczy" within 15 days from the financial statements approval date. The publication requirement relates to the companies which meet the audit requirements.

The same regulations apply to the parent entities which prepare the annual consolidated financial statements of the capital group with the exception that a parent company, which is a subsidiary of another entity having its registered office or the place of executive management located within the European Economic Area (higher-level parent company), is not required to prepare consolidated financial statements, if:

- a higher-level parent company holds at least 90% of its shares, and all other shareholders of the parent company have agreed on exemption application, and
- a higher-level parent company will be consolidating both the parent company being its subsidiary and all other subsidiaries of the parent company which was exempted from preparing the consolidated financial statements.

In such a situation the consolidated financial statements and the consolidated annual report of a higher-level parent company together with the statutory auditor's opinion, transferred into Polish by a certified translator, shall be filed with a relevant court register within 30 days from their approval date.

3.1.5. Financial reporting of listed companies

Regulatory environment

The basic principles of the Polish capital market are set out by the following regulations:

- the Act on Trading in Financial Instruments;
- the Act on Public Offering and on Terms on which Financial Instruments are Introduced to an Organized System of Trading as well as on Listed Companies; and
- the Act on Supervision over the Capital Market.

These provisions implement the European Parliament and Council Directives regarding the capital markets, adjusting the Polish provisions to the European Community standards. The manner in which prospectuses are prepared is in line with the EU Prospectus Regulation, and securities admitted by other EU regulators can under Polish provisions also be admitted to trading in Poland. Polish regulations were adjusted to the provisions of the Transparency Directive, making the market more favorable for foreign investors and foreign public companies. Increasing attention is also applied to market communication, protection of minority investors, counteracting fraud and insider trading.

The regulations regarding investment funds, contained in the Law on Investment Funds dated 27 May 2004, as amended, reflect the appropriate provisions of the EU law concerning undertakings for collective investments in transferable securities. In particular, the offering of foreign investment funds in Poland is now regulated in detail.

The Polish capital market is supervised by the Financial Supervision Authority (Komisja Nadzoru Finansowego – FSA). The FSA is a single regulatory authority supervising insurance, pension funds, banks and financial markets institutions. The FSA's main function is is to protect interests of investors.

The role of the FSA also includes supervision of brokerage houses, collective investment institutions and public companies acting or offered in Poland. The competences of the FSA include both initial control, as well as subsequent supervision of the activity by the aforementioned entities, as well as over brokers and investment advisors. The FSA may impose fines and other administrative measures upon market participants who fail to comply with Polish regulations. In case of entities which are also subject to supervision within other EU jurisdictions, the FSA cooperates with local market regulators in exercising supervision.

The Warsaw Stock Exchange (Giełda Papierów Wartościowych w Warszawie – WSE) is the principal market in Poland where stocks, bonds, derivatives and other financial instruments are traded. Securities are traded on two different markets within the WSE: the "main floor" (primary market) and the "parallel market". In addition, the

WSE also owns a stake in an OTC market called MTS-CeTo, and operates NewConnect, a multilateral trading system. In 2009 the bond market Catalyst was opened. Traded derivatives include future contracts on indices and selected stocks, options on indices, and other instruments.

Financial Reporting Requirements

Financial reporting of the entities admitted to public trading by the FSA is regulated by the Decree issued by Minister of Finance dated 19 February 2009 *on current and periodic information published by issuers of securities and conditions for recognition as equivalent the information required by laws of non-EU member states*.

The financial reporting requirements for particular periodic reports (both standalone and consolidated) are summarized in the table below.

Type of the report	Content includes:	Filling deadline ***
Quarterly	‣ Condensed Financial Statements for the quarter ended and for all quarters to date together with comparable data ‣ There is no requirement to file the report for the second quarter as the semiannual report is filed (does not apply to funds) ‣ There is no requirement to file the report for the fourth quarter if the annual report is filled within the quarterly report filling deadline	‣ No later than 45 days after the quarter end ‣ For the fourth quarter no later than 60 days after the fourth quarter end
Semiannual	‣ Condensed Financial Statements for the six months period ‣ Independent Auditor's Review Report on the Condensed Financial Statements for the six months period	‣ No later than 2 months after the half-year end
Annual	‣ Annual Financial Statements ‣ Independent Auditor's Opinion	‣ No later than 4 months after the year end ‣ No later than 80 days after the year end if the entity decides not to fill report for the fourth quarter

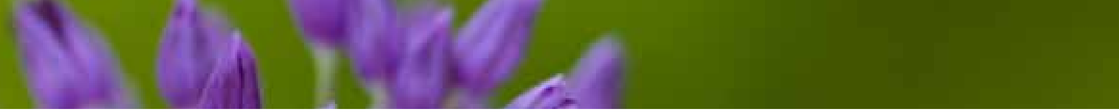
*** A listed company is obliged to publish the filling dates for all periodic reports within the first month of a given year in the form of a current report. The filling dates of all periodic reports need to be in line with the dates announced in this current report.

3.1.6. Audit requirements

The audit and the publication shall be required in respect of annual consolidated financial statements including annual financial statements of capital groups, as well as the annual financial statements of the following entities which continue as a going concern:

- banks and insurers;
- entities which operate under regulations on trading in securities and regulations on investment funds;
- entities which operate on the basis of regulations on the organization and operations of pension funds;
- joint stock companies, except for companies which are in the setting-up process as at the balance sheet date;
- other entities which, in the prior financial year for which the financial statements were prepared, met at least two of the following conditions:
  - the annual average number of employees in full-time equivalents amounted to at least 50 people;
  - the total assets as at the end of the financial year were at least the Polish zloty equivalent of EUR 2,500,000;
  - the net revenue from the sales of goods for resale and finished goods and the financial transactions for the financial year, was at least the Polish zloty equivalent of EUR 5,000,000.

Additionally, the financial statements of acquirers and newly-formed companies as a result of a business acquisition, prepared for the financial year in which the business combination took place, are required to be audited. Furthermore, combined annual financial statements of investment funds, which have separate sub-funds and annual financial statements of the sub-funds, are required to be audited and published.



3.2. Selected Aspects of Accounting for Real Estate under International Financial Reporting Standards

3.2.1. Introduction

Historically, the objectives of the financial reporting have varied in different countries, and this fact is reflected in the relative importance given to the various parties who have an interest in accounting information. Financial reporting in certain countries has developed on the basis that shareholders are the most important group entitled to receive financial information. Consequently investors required regular reports to assess the performance achieved by management and future prospects, and annual accounts ensured that stewardship function was being conducted properly.

Prior to the adoption of IFRS there was no common broad-based statement of generally accepted theoretical principles that underpinned financial reporting across the individual Member States of the European Union (EU). Clearly, though, it was not the lack of conceptual framework that caused the differences in the European financial reporting practices. European accounting evolved over many countries, and the differences that exist throughout the Europe were shaped by the conditions in each European country. Until recently, the principal mechanism employed by the European Union to reduce these differences was the adoption of Directives under its company law harmonization program. These Directives are not laws that apply directly to companies, but instructions to Member States to alter their own national legislation, if necessary, so as to ensure compliance with the provisions of the Directives. The most significant Directives in the area of financial reporting are the Fourth and Seventh. The principal objectives of the Fourth Directive was to achieve harmonization in respect of formats, valuation rules and note disclosure, whilst the Seventh established a requirement for EU companies to prepare consolidated accounts on a common basis. Both Directives have provided a base level for harmonization of financial reporting in the EU, and have undoubtedly led to improvements in the quality and comparability of company accounts throughout the Union. They have contributed also to improving the conditions for cross–border business and have allowed mutual recognition of financial statements for the purpose of quotations on securities exchanges throughout the EU. Moreover, a further important contribution of the Directives has been in the area of creditor protection through the public availability of financial information.

Nowadays, a number of real estate entities apply IFRS for their accounting and reporting purposes. In many cases IFRS offers a choice between different accounting treatments for the same transaction and event or it is silent on particular issues. Consequently, preparers of financial statements may choose the treatment that is the most relevant to their business.

Application of International Financial Reporting Standards as any general accounting framework raises concerns, including such Standards not being:

- industry specific; or
- addressing specific matters.

Due to lack of specific guidance on application of IFRSs in the real estate industry there are very active industry associations like EPRA, INREV and IVSC publishing guidance on industry practices for financial reporting. Some key standards were recently and will be amended (for example, property under construction, deferred tax and leases).

3.2.2. Investment Property

IAS 40 - Investment property - is a rare example of the particular commercial characteristics of an industry resulting in the special treatment of a certain category of property (investment properties), even though the assets themselves are not intrinsically different from those within the scope of IAS 16 - Property Plant and Equipment. Nevertheless, despite being focused on the needs of the investment property industry, the standard allows entities a free choice between two measurement models: historic cost and fair value. It should be borne in mind also that it is not only investment property companies that hold investment property; any property that meets the investment property definition is so classified, irrespective of the nature of the business of the reporting entity.

Investment property is defined in IAS 40 as a property (land or a building – or part of a building – or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

- use in the production or supply of goods or services or for administrative purposes; or
- sale in the ordinary course of business.

This means that any entity, whatever the underlying nature of its business, can hold investment property assets.

In contrast, "owner-occupied" property is defined as "property held" (by the owner or by the lessee under a finance lease) for use in the production or supply of goods or services or for administrative purposes. Such property falls outside the scope of IAS 40 and is accounted for under IAS 16, together with IAS 17 – Leases - if relevant.

The following are examples of investment property:

- Land held for long-term capital appreciation rather than for short-term sale in the ordinary course of business;
- Property that is being constructed or developed for future use as investment property;

- Land held for a currently undetermined future use;
- A building owned by the entity (or held by the entity under a finance lease) and leased out under one or more operating leases; and
- A building that is vacant but is held to be leased out under one or more operating leases.

The following are examples of items that are not investment property:

- Property intended for sale in the ordinary course of business or in the process of construction or development for such sale (IAS 2 Inventories);
- Property being constructed or developed on behalf of third- parties; and
- Owner occupied property including (among other things) property held for future use as owner-occupied, property held for future development and subsequent use as owner occupied property, property occupied by employees (whether or not employees pay rent at market rates) and owner occupied property awaiting disposal.

Recognition

An investment property should be recognized as an asset when it is probable that the future economic benefits, that are associated with the investment property, will flow to the entity and its cost can be measured reliably.

IAS 40 has a single set of recognition criteria for any costs incurred, whether initially or subsequently. This means that all investment property costs, whether at initial or subsequent recognition (for example, to add to or replace part of a property), must meet the recognition criteria at the point at which the expenditure is incurred if they are to be capitalised.

As part of annual improvements process in May 2008 the IASB approved changes that brought the investment property under construction (IPUC) into the scope of IAS 40 Investment property. The change is effective for annual periods beginning on or after 1 January 2009. As a result entities reporting under IFRS should apply provisions of IAS 40 for investment properties under construction, i.e. entities which selected the fair value model for investment properties' valuation must also measure their IPUC at fair value.

Initial measurement

IAS 40 requires an investment property to be measured initially at cost, which includes directly attributable transaction costs such as professional fees, property transfer taxes and other transaction costs.

Measurement after initial recognition

Once recognized, IAS 40 allows entities to choose between one of two methods of accounting for investment property: the "fair value model" or the "cost model". There is one exception to the choice of measurement: a property interest that is held by a lessee under an operating lease may be classified as an investment property - provided that the fair value model is applied for the asset recognized and, consequently, for all investment properties.

The only exception to the requirement that an entity must apply either the fair value or the cost model to all its investment properties relates to insurance companies and other entities that hold investment properties which return is directly linked to the return paid on specific liabilities. These entities are permitted to choose either the fair value or the cost model for such properties without affecting the choice available for any other investment properties they may hold. However, all properties within a given fund must be held on the same basis and transfers between funds are to be made at fair value.

The fair value model

Under this model all investment properties are measured at its fair value at the balance sheet date. The changes in the fair value from one balance sheet to the next one are included in the income statement for the period.

The standard defines fair value as "the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction". Fair value specifically excludes an estimated price inflated or deflated by special terms or circumstances such as atypical financing, sale and leaseback arrangements that are not at market rates or special considerations or concessions granted by anyone associated with the sale. Transaction costs, which may be incurred by the vendor on sale, are not deducted. The fair value of investment property does not reflect future capital expenditure that will improve or enhance the property and does not reflect the related future benefits from this future expenditure. There is no difference in this area comparing to the Polish Accounting Act.

IAS 40 requires specific disclosures regarding the valuation methods and judgments used. In particular, the methods and significant assumptions applied in the determination of the fair value of investment property, including a statement whether the determination of fair value was supported by market evidence or was more heavily based on other factors because of the nature of the property and lack of comparable market date, are required.

The cost model

The cost model requires that all investment properties are to be measured after initial recognition at historical cost less accumulated depreciation and accumulated impairment losses as required by cost model defined in IAS 16 Property, plant and equipment. This means that the asset must be recognized at cost and depreciated systematically over its useful life. The component approach defined in IAS 16 Property, Plant and Equipment applies.

Transfer of assets into or from investment property

IAS 40 Investment Property specifies the circumstances in which a property becomes, or ceases to be, an investment property. There must be a change in use, evidenced by:

- the commencement or end of owner-occupation;
- the commencement of development with a view to sale, at which point an investment property would be transferred to inventory. The standard allows a transfer to inventory only when there is a change of use evidenced by the start of a development with a view to subsequent sale;
- entering into an operating lease to another party which would generally require a transfer from inventory to investment property.

However, some changes in status do not result in transfers:

- If an entity decides to dispose of an investment property without development with a view to sale, it may not be transferred to inventory;
- An existing investment property that is being redeveloped for continued future use as an investment property by the entity must remain classified as an investment property and is not reclassified as owner-occupied property during the redevelopment.

Transfers to and from the status of investment property under the fair value model are accounted for as follows:

- Transfers to inventory or owner-occupation: the cost for subsequent accounting under IAS 16 Property, plant and equipment or IAS 2 Inventory should be its fair value at the date the use changed;
- Transfers from owner-occupation: IAS 16 Property, plant and equipment will be applied up to the time that the use changed. At that date any difference between the IAS 16 carrying amount and the fair value is to be treated in the same way as a revaluation under IAS 16.75.

Up until the time that an owner occupied property becomes an investment property carried at fair value, depreciation under IAS 16 Property, plant and equipment continues and any impairment losses up to the date of change of use must be recognised in accordance with IAS 36 Impairment. The difference between the carrying value under IAS 16 and the fair value under IAS 40 is accounted for in the same way as a revaluation under IAS 16 Property, plant and equipment. If the owner occupied property had not previously been revalued, the transfer does not imply that the entity has now chosen a policy of revaluation for other property accounted for under IAS 16 in the same class. The treatment depends on whether it is a decrease or increase in value and whether the asset had previously been revalued or impaired in value. Paragraph 62 of the standard sets out the treatment as follows:

Up to the date when an owner-occupied property becomes an investment property carried at fair value, an entity depreciates the property and recognises any impairment losses that have occurred. The entity treats any difference at that date between the carrying amount of the property in accordance with IAS 16 and its fair value in the same way as a revaluation in accordance with IAS 16. In other words:

- any resulting decrease in the carrying amount of the property is recognised in profit or loss. However, to the extent that an amount is included in revaluation surplus for that property, the decrease is charged against that revaluation surplus;
- any resulting increase in the carrying amount is treated as follows:
  - to the extent that the increase reverses a previous impairment loss for that property, the increase is recognised in profit or loss. The amount recognised in profit or loss does not exceed the amount needed to restore the carrying amount to the carrying amount that would have been determined (net of depreciation) had no impairment loss been recognised;
  - any remaining part of the increase is credited to revaluation surplus via other comprehensive income. On subsequent disposal of the investment property, the revaluation surplus may be transferred to retained earnings. The transfer from revaluation surplus to retained earnings is not made through profit or loss.

When the business uses the cost model for investment property, transfers between investment property, inventory and owner occupation do not change the carrying amount of the property transferred.

3.2.3. Borrowing costs

Application guidance

In accordance with the IAS 23 (Revised) - Borrowing Costs, an entity shall capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. An entity shall recognise other borrowing costs as an expense when incurred. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are included in the cost of that asset. Such borrowing costs are capitalised as part of the cost of the asset when it is probable that it will result in future economic benefits to the entity and the costs can be measured reliably.

Borrowing costs may include:

- interest on bank overdrafts, short-term and long-term borrowings;
- amortisation of discounts or premiums relating to borrowings;
- amortisation of ancillary costs incurred in connection with the arrangement of borrowings;
- finance charges in respect of finance leases recognized in accordance with IAS 17 Leases; and
- exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

Depending on the circumstances, any of the following may be qualifying assets:

- inventories;
- manufacturing plants;
- power generation facilities;
- intangible assets; and
- investment properties.

Inventories that are manufactured, or otherwise produced, over a short period of time, and assets that are ready for their intended use or sale when acquired, are not qualifying assets.

Commencement of capitalization

An entity shall begin capitalization of borrowing costs as part of the cost of a qualifying asset on the commencement date. The commencement date for capitalisation is the date when the entity meets all of the following conditions:

- it incurs expenditures for the asset;
- it incurs borrowing costs; and
- it undertakes activities that are necessary to prepare the asset for its intended use or sale.

Suspension of capitalization

An entity shall suspend capitalization of borrowing costs during extended periods in which it suspends active development of a qualifying asset.

Cessation of capitalization

An entity shall cease capitalising borrowing costs when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

When an entity borrows funds specifically for the purpose of obtaining a particular qualifying asset, the borrowing costs that directly relate to that qualifying asset can be readily identified. To the extent that an entity borrows funds specifically for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalization as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings. To the extent that an entity borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalization by applying a capitalization rate to the expenditures on that asset. The capitalization rate shall be the weighted average of the borrowing costs applicable to the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs that an entity capitalises during a period shall not exceed the amount of borrowing costs it incurred during that period.

3.2.4. Property, plant and equipment

Introduction

Based on IAS 16 Property, Plant and equipment the Property, plant and equipment are tangible items that:

- are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and
- are expected to be used during more than one period.

The cost of an item of property, plant and equipment shall be recognized as an asset if, and only if:

- it is probable that future economic benefits associated with the item will flow to the entity; and
- the cost of the item can be measured reliably.

Measurement at recognition

An item of property, plant and equipment that qualifies for recognition as an asset shall be measured at its historical cost.

The cost of an item of property, plant and equipment comprises:

- its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates;
- any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management; and
- the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period.

Examples of directly attributable costs are:

- costs of employee benefits (as defined in IAS 19 Employee Benefits) arising directly from the construction or acquisition of the item of property, plant and equipment;
- costs of site preparation;
- initial delivery and handling costs;
- installation and assembly costs;
- costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment); and
- professional fees.

Measurement after recognition

An entity shall choose either the cost model or the revaluation model as its accounting policy and shall apply that policy to an entire of property, plant and equipment.

Cost model

After recognition as an asset, an item of property, plant and equipment shall be carried at its historical cost less any accumulated depreciation and any accumulated impairment losses.

Revaluation model

After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations shall be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the balance sheet date.

Depreciation

Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately. The depreciable amount of an asset shall be allocated on a systematic basis over its useful life. The residual value and the useful life of an asset shall be reviewed at least at each financial year-end.

The depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. The depreciation method applied to an asset shall be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method shall be changed to reflect the changed pattern. Such a change shall be accounted for as a change in an accounting estimate in accordance with IAS 8 (Accounting Policies, Changes in Accounting Estimates and Errors).

While determining a depreciation period and an annual depreciation rate, the economic useful life of a given item of property, plant and equipment is taken into account. An economic useful life depends on the following:

- the number of shifts during which an item of property, plant and equipment is used;
- the pace of technological and economic progress;
- the productivity of an item of property, plant and equipment, measured with the number of work hours or the number of finished goods produced, or on the basis of another, suitable measure.
- legal or other limitations of the time for which an item of property, plant and equipment may be used; and
- the expected net selling price of material remains of the item of property, plant and equipment at a time of scrapping.

At the date when an item of property, plant and equipment is commissioned for use, it is necessary to determine its depreciation period or rate and depreciation method. An entity should verify the correctness of applied depreciation periods and rates of its property, plant and equipment on a regular basis, leading to an appropriate adjustment to depreciation charges being made in subsequent financial years.

3.2.5. Inventories

When an entity is constructing assets which are:

- held for sale in the ordinary course of business;
- in the process of production for such sale; or
- in the form of materials or supplies to be consumed in the production process or in the rendering of services,

the entity should follow IAS 2 Inventories prescriptions to recognise and measure such assets. This standard is applicable for example to residential units developers and developers of commercial properties designated for sale. The cost of inventories shall comprise all costs of purchase including borrowing costs, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

When inventories are sold, the carrying amount of those inventories shall be recognized as an expense in the period in which the related revenue is recognized. The amount of any write-down of inventories to net realisable value and all losses of inventories shall be recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realisable value, shall be recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs.

Real estate sales

Around the world it is common practice for developers to start marketing their developments well before the start of the construction and often this activity will continue throughout the construction period. A typical "of plan" arrangements will generally involve a buyer entering into a sale agreement with a developer to acquire a specific unit (usually a house or an apartment) upon completion on construction. To secure the property the buyer is usually required to pay a deposit which would be refundable only if the developer failed to deliver the unit in the agreed upon conditions.

In the past some real estate developers recognized revenue as construction contracts applying the stage (percent) of completion of the development concept while others recognized revenue at the end of construction when the completed unit is handed over to the buyer. To address the diverse practice IFRIC 15 – Agreements for the Construction of Real Estate was issued to provide guidance on determining when a sale agreement that involves the sale of units is a construction contract within the scope of IAS 11 – Construction contracts, or the contrast for the sale of goods that would fall within the scope of IAS 18 – Revenues.

IFRIC 15 proposes that revenue can only be recorded as construction progresses if the real estate developer is providing construction services to the buyer's specifications. If the developer is in substance simply selling completed real estate units, the revenue can only be recognized at completion.

IAS 11 applies if the sale agreement meets the definition of a construction contract in IAS 11. IAS 18 applies if the sale agreement is instead an agreement for the sale of goods (completed real estate). IAS 11 defines a construction contract as "a contract specifically negotiated for the construction of an asset or a combination of assets". A sale agreement meets this definition if it is an agreement for the seller to provide construction services to the buyer's specifications. Features that, individually or in combination, may indicate such situations include:

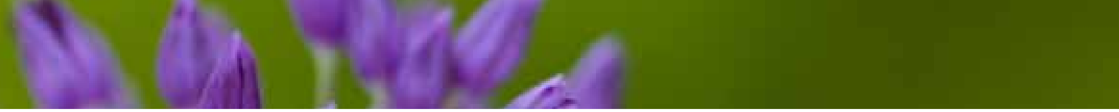
- the buyer being able to specify the major structural elements of the design of the real estate before construction begins and/or specify major structural changes once construction is in progress (whether it exercises that ability or not);

- the seller transferring to the buyer control and the significant risks and rewards of ownership of the work in progress in its current state as construction progresses. Indications that the seller transfers control of the work in progress in this way may include, for example:
    - the construction taking place on land that is owned or leased by the buyer;
    - the buyer having a right to take over the work in progress (albeit with a penalty) during construction, e.g. to engage a different contractor to complete the construction;
    - in the event of the agreement being terminated before construction is complete, the buyer retaining the work in progress and the seller having the right to be paid for work performed (subject to buyer acceptance).

Conversely, features that, individually or in combination, may indicate that an agreement is for the sale of goods (completed real estate) include:

- the negotiation between buyer and seller primarily concerning the amount and timing of payments, with the buyer having only limited ability to specify the design of the real estate, for example, to select a design from a range of options or specify minor variations to the basic design; and
- the agreement giving the buyer only a right to acquire the completed real estate at a later date, with the seller retaining control and the significant risks and rewards of ownership of the underlying work in progress until that date.

If a sale agreement is for the sale of goods, revenue shall be recognized when all the conditions required by IAS 18 have been satisfied. Two of the conditions require the entity to have transferred to the buyer the significant risks and rewards of ownership of, and effective control over, the goods sold. These conditions shall be applied to the underlying real estate in its current state, not to the buyer's right to acquire the fully constructed real estate at a later date. In some cases, real estate may be sold with such a degree of continuing involvement by the seller that effective control and the risks and rewards of ownership are not transferred when the buyer obtains possession. Examples are sale and repurchase agreements that include put and call options, and agreements whereby the seller guarantees occupancy of the property for a specified period, or guarantees a return on the buyer's investment for a specified period. In such cases, the nature and extent of the seller's continuing involvement determines how the transaction is accounted for. It may be accounted for as a sale, or as a financing, leasing or some other profit-sharing arrangement. If it is accounted for as a sale, the continuing involvement of the seller may delay the recognition of revenue.



3.3. Principal differences between Polish and International Financial Reporting Standards applicable for real estate entities

The main differences between Polish Accounting Standards (PAS) and International Financial Reporting Standards (IFRS) are presented in the table.

Description	PAS	IFRS
Functional currency	Functional currency concept does not exist.	Functional currency concept underlies the preparation of the financial statements.
Long term contracts	Long term contracts approach need only be applied for contracts with a period exceeding 6 months.	Construction contracts approach should be applied to all contracts of this type, regardless of the period.
Investment property	Assets under construction shall be presented at cost and cannot be fair valued.	In May 2008, as part of its annual process, the IASB approved changes that brought investment property under construction (IPUC) into the scope of IAS 40 for annual periods beginning on or after 1 January 2009. This means that entities who wish to measure their completed property at fair value has to also measure their IPUC at fair value.
Impairment of assets	Assessed annually if there is high probability that the assets (including goodwill and intangibles) will not bring expected benefits. Write assets down to selling value or, if that is not available, to fair value.	Assessed annually if there are indicators that assets may be impaired (including goodwill and intangibles). If indications exist, write assets down to the higher of fair value less costs to sell and value in use. Even if there are no indicators, goodwill, indefinite life intangible assets and intangible assets not yet in use are subject to an annual test.

Description	PAS	IFRS
Business Combinations	Accounted for as an acquisition in transactions that are not under common control. Group reorganizations among entities under common control might be accounted for using pooling of interest method.	A business combination must be accounted for by applying the acquisition method, unless it is a combination involving entities or businesses under common control.One of the parties to a business combination can always be identified as the acquirer, being the entity that obtains control of the other business (the acquiree). Formations of a joint venture or the acquisition of an asset or a group of assets that does not constitute a business are not business combinations. In accounting for business combinations involving entities or businesses under common control entities should apply either the: ‣ pooling of interest method; or ‣ purchase method.
Goodwill and adjustments to fair value on acquisition	Goodwill on acquisition (including associates) is the difference between the purchase price and the fair value of all assets and liabilities acquired. Changes in the initial fair values of acquired assets and liabilities which are identified during the financial year in which the acquisition took place should adjust goodwill. Goodwill is amortized over the useful life, generally not expected to be longer than 20 years. Negative goodwill: ‣ relating to future losses acquired is deferred and amortized over the period of the loss; ‣ otherwise, up to the value of the depreciable assets is deferred and amortized over the depreciable life; ‣ balance is recognized as income.	Goodwill on acquisition is the excess of (a) over (b) bellow: (a) the aggregate of: ‣ the consideration transferred, which generally requires acquisition-date fair value; ‣ the amount of any non-controlling interest in the acquiree; and ‣ in a business combination achieved in stages, the acquisition date fair value of the acuirer's previously held equity interests in the acquiree; (b) the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed. Changes in the initial fair values of acquired assets and liabilities if only provisionally assessed at the date of acquisition, which are identified within 12 months of the acquisition, are adjusted against goodwill. Goodwill is not amortised, but subject to an annual impairment test. Gain on bargain purchase is recognized as income.

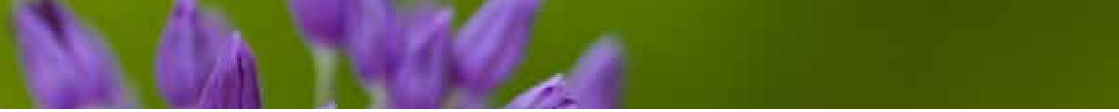
Description	PAS	IFRS
Fixed assets	Fixed assets may be revalued only on the basis of separate regulations to a value not exceeding the fair value. There is no requirement under PAR to distinguish items with a cost that is significant in relation to the total cost and to depreciate it separately.	Fixed assets may be revalued to their fair value. Each part of an item of property, plant and equipment with a cost that is significant in relation to the total cost of the item shall be depreciated separately (component accounting).
Capitalization of borrowing costs	All borrowing costs incurred in the period of construction of and attributable to tangible and intangible assets are capitalized as part of the assets' cost. FX gains/losses are also included as part of the borrowing costs. A choice is given to capitalize borrowing costs into inventory which takes considerable time to complete.	Capitalization of borrowing costs required on specific and general borrowings to finance the construction of individual qualifying assets. FX gains/losses are also included as part of the borrowing costs, to the extent they represent an adjustment to the interest charge.
Investment tax credits	Investment tax credits used give rise to a deferred tax asset and are recognized as a government grant to be amortized over the useful life of the asset (per standard issued by Accounting Standards Committee).	Unused investment tax credits give rise to a deferred tax asset and affect the tax charge in the year granted.

In any matters not regulated by the Act or the associated Decrees, an entity may apply national accounting standards issued by the Accounting Standards Committee. In the absence of relevant local regulations, the entity may apply International Financial Reporting Standards.

Changes to IFRS

New and amended standards and interpretations applicable to December 2011 year-ends:

- *IFRS 1 First-time Adoption of International Financial Reporting Standards – Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters* – effective for annual periods beginning on or after 1 July 2010;
- *IAS 24 Related Party Disclosures (Revised)* – effective for annual periods beginning on or after 1 January 2011;
- *IAS 32 Financial Instruments: Presentation – Classification of Rights Issues (Amendment)* – effective for annual periods beginning on or after 1 February 2010;
- *IFRIC 14 Prepayments of a Minimum Funding Requirement (Amendment)* – effective for annual periods beginning on or after 1 January 2011;
- *IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments* – effective for annual periods beginning on or after 1 July 2010;
- *Improvements to International Financial Reporting Standards (issued 2010)* – generally effective for periods beginning on or after 1 January 2011 unless otherwise stated. Earlier application is permitted in all cases.



3.4. Selected accounting issues

Although IFRS is the most common accounting platform applied by the international and national listed and non-listed entities, in many cases IFRS offers a choice between different accounting treatments for the same transaction and event or it is silent on particular issues. Consequently, preparers of financial statements may choose the treatment that is the most relevant to their business. The purpose of this section is to outline selected interpretative issues in IFRS that may be encountered by the real estate and construction companies.

Accounting for investment property under construction

Under the revised IAS 40 a question may arise regarding the main valuation principles to be applied in relation to the investment property under construction under fair value model.

A lack of transaction prices of similar properties under construction usually requires the use of estimation models. IAS 40 does not contain any specific guidance as to the valuation of IPUC and reference is often made to International Valuation Standards (IVS). The valuation of IPUC is complex and judgmental area, therefore there is a need for more detailed guidance. Common methods found include: (i) the hypothetical developer's method otherwise known as the "residual method" valuation, and (ii) the discounted cash flow (DCF) method. The hypothetical developer's method deducts costs of construction, finance and anticipated profit (a percentage cost) from an exit value, i.e. the gross development value of the completed project. The DCF approach uses (project) risk adjusted discount factors.

Both the European Public Real Estate Association (EPRA) and the International Valuation Standards Board (IVSB) have released more detailed guidance to assist (and improve consistency amongst) preparers of financial statements, valuers, advisers and investors.

The valuation principles agreed by EPRA members are as follows:

- The starting point for any valuation of investment property under construction should be a completed property. Such a valuation should be based on current valuations applicable to similar existing completed properties with comparable encumbrances to property rights. In practice, property is not usually fully let on completion, but an appraiser will still be able to value the IPUC and should normally be able to demonstrate possible scenarios;
- The gain which may be attributable to realizing project objectives is the difference between the value of a completed building and its construction costs – including the cost of the land, finance costs incurred during the construction and any directly attributable costs;

- Project risks relate to risks associated with realizing the project objectives. The existence of unmitigated project risks can impact the quantum of the project gain to be recognized, if any. The significant project risks associated with the development should be identified;
- When project risks are minimized or eliminated, some project gain may have been achieved and the value of the project increased. However, the project gain should only be recognized in a valuation of an investment property under construction when a substantial amount of the project risks have been reduced or eliminated. An appraiser should disclose the significant judgments used in determining the stage at which a substantial amount of the project's risks have been eliminated;
- Notwithstanding the above, if the land has increased in value, for example, via the issue of government permits and this is corroborated by comparable prices for land in that condition in an active marker, then that part of the project gain should be recognized;
- Valuations should be based on project cash flows and outflows, taking into account the time value of money and remaining project risks. The cash outflows must include all construction and other project costs still to come, based on contracted terms and current best estimates; and
- The transparency of the valuation estimate is important. Appraisers should include a description of their valuation methodology and the key assumptions used in their report to the client. In particular, the appraiser must also identify how the remaining risks of the project have been dealt with in the valuation. Any contingent element, deductions or risk adjusted discount rates, should be quantifies and explained with reference to the remaining project risks.

The IVSB principles are substantially consistent with EPRA, with the exception that IVSB does not specifically caution against the recognition of a development gain until the project risks are substantially eliminated.

As a result of the guidelines presented above a question may arise when the fair value for investment property under construction can be reliably determined. The answer to this question is not straight forward as it involves judgment and, in principle, it is management that needs to assess the reliability. As mentioned above EPRA advises caution against recognizing a development gain until a substantial part of the project risks has been reduced or eliminated.

However, EPRA does not provide guidelines as to which criteria should be applied. Indicators that may be used to assess whether the substantial risks are eliminated may include:

- All required building and letting permits have been obtained;
- Development costs can be reliably estimated. This may be the case when a fixed price construction contract with the main contractor is agreed; and

- The value of the completed property can be reliably estimated. This may be the case when a substantial proportion of the rentable area has been leased to tenants.

According to the IVSB, it is important that all project risks have been identified, evaluated and quantified. Based on these identified risks and the assessment of sufficient comparable market data, the valuer normally determines the adjustment needed to reflect project risks. In any event, any investment property under construction carried at cost is still subject to impairment provisions of IAS 36 Impairment of Assets. IAS 36 requires a recoverable amount to be determined as the higher of: (i) value in use; or (ii) fair value less cost to sell. Even if fair value is considered unreliable, a value-in-use calculation must be performed, which is a discounted future cash flow analysis. If such a discounted future cash flow must be prepared for IAS 36 purposes, it may not be that difficult to change entity specific assumptions into market specific assumptions.

Presentation of investment property under construction under the new requirement of IAS 40

Certain doubts may arise in relation to the presentation of the investment property under construction in a particular entity's financial statements. In general, investment property under construction can be presented as part of total investment property on the face of the balance sheet. However, an entity may also wish to show completed investment property and investment property under construction as separate items within the total on the balance sheet or in the notes to the balance sheet. In general, at a minimum, separate information on investment property under construction and completed investment property in the notes to the balance sheet should be provided, as both categories are generally subject to a different set of assumptions and accounting estimates. Moreover, IFRS also require separate presentation of investment property (including investment property under construction) at cost (where fair value cannot be reliably estimated) and investment property (including investment property under construction) at fair value.

Accounting for contracts to construct a real estate

Certain issues may also arise in relation the question whether a contract to construct a real estate should be scoped within IAS 11 Construction contracts or IAS 18 Revenue. An example may be a developer having access to a piece of land and intending to develop it into an office and selling it. The developer negotiates the major structural elements of the design with the user/lessee and enters into lease contract with them. After the completion, a property investment company will buy the office and take over the lease agreement from the real estate developer. Legal title only transfers to the buyer on completion of the office. In such cases the following two scenarios may be considered:

- The lease is classified as an operating lease;
- The lease is classified as a finance lease.

In the first scenario, the lessee/user cannot be considered as a buyer. Therefore, the agreement does not meet the definition of a construction contract and is scoped within IAS 18. However, if the lease is a finance lease, the lessee/user can be considered as a buyer and thus, the contract meets the definition of a construction contract and is scoped within IAS 11. Although there is an agreement under which the real estate developer is required to construct the office based upon the design negotiated with a third party and the third party is ultimate user, that third party is not the buyer – it is only the lessee. There has not been any negotiation with respect to the major structural design with a buyer in the real estate sales contract. Therefore, it does not meet the definition of a construction contract as laid out in paragraph 3 of IAS 11 and as interpreted by paragraph 11 of IFRIC 15 Agreements for the Construction of Real Estate.

In the second scenario paragraph 42-44 of IAS 17 Leases on manufacturer finance leases apply. These paragraphs state that a finance lease from a manufacturer - lessor's perspective gives rise to profit or loss equivalent to the profit or loss resulting from an outright sale of the asset. Therefore, the lessee is in substance the buyer and the agreement does not meet the definition of a construction contract as laid out in paragraph 3 of IAS 11, as interpreted by paragraph 11 of IFRIC 15.

Accounting for income from tenanted development property

When the development property is tenanted a question arise how should rental and similar income generated by existing tenants be accounted for, i.e. whether it should be capitalized and offset against the cost of development, or should be recognized directly in the income statement? The issue may be analyzed using the following example: A real estate developer acquired a property some years ago which was let, generated rental income and classified as an investment property under IAS 40. Management now intends that this property will be redeveloped and subsequently again be held for rental for the foreseeable future. Management have commenced activities including negotiating with the tenants to exit the existing leases, obtaining planning permission and drawing up plans for redevelopment. In such a situation the rental and similar income generated by existing tenants in an investment property and intended for redevelopment should not be capitalized against the costs of redevelopment. Rental and similar income should be recognized in the income statement in accordance with the requirements of IAS 17 Leases together with related expenses. For these purposes it is irrelevant whether the investment property is held at cost or fair value. The similar accounting should be applied for the residential units developed for sale in the ordinary course of business (scoped within IAS 2 Inventory), which have been leased to tenants before the sale is completed.

Accounting for lease incentives by lessor

When a lessor leases out real estate investment property in an operating lease it happens frequently that an incentive (for example a rent free period) is granted to the lessee. The case below will be analysed assuming application of the fair value for investment properties. As the lease incentive (the rent free period) is an integral component of the lease agreement it is assumed that, in exchange for the rent free period to be enjoyed under the terms of the lease, the lessee undertakes to provide a flow of lease rental payments to the lessor in periods following the period when the lease incentive was granted which are higher than they would be if no incentive was provided. As a result it is assumed that the rent free period is taken into account by the appraiser in arriving at the fair value of the property on the day of investment property valuation. Consequently, in this case the costs resulting from the rent free period being granted are incurred in relation to the asset which is measured at fair value and the benefits earned from these costs, if any, are normally already reflected in the fair value of the asset. Hence separate identification of an asset (resulting from the rent free period) to be amortized is not necessary and would result in double counting. The cost of the incentive should be therefore recognized as a reduction of rental income over the lease term on a straight line basis as required by paragraph 4 of SIC Interpretation 15 Operating Leases—Incentives and debited to gains and losses in the fair value of investment properties so as to avoid double counting in the balance sheet.

In this way the income statement reflects the cost of the incentive as a reduction of rental income over the lease term on a straight-line basis and any impact on the company's net result is avoided. Alternative view presumes that a separate asset is recorded for straight lining the cost of the consideration in the form of the lease incentive over the term of the lease. To avoid double-counting, it is necessary for the lessor to adjust the carrying value of the investment property downwards to take account of the fact that the actual return to the lessor will be lower because the lessor has agreed to offer a rent free period and has recorded this lease incentive separately as an asset.

Definition of the business under IFRS 3 (revised)

When an entity is acquiring a real estate property it shall determine whether a transaction or other event is a business combination by applying the definition from IFRS 3R (Business Combination). If the assets acquired are not a business, the reporting entity shall account for the transaction as an asset acquisition.
IFRS 3R has redefined a business as:

"An integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants."

A business consists of inputs and processes applied to those inputs that have the ability to create outputs. Although businesses usually have outputs, outputs are not required for an integrated set to qualify as a business. The three elements of a business are defined as follows:

- Input: any economic resource that creates, or has the ability to create, outputs when one or more processes are applied to it. Examples include non-current assets (including intangible assets or rights to use non-current assets), intellectual property, the ability to obtain access to necessary materials or rights and employees.
- Process: any system, standard, protocol, convention or rule that when applied to an input or inputs, creates or has the ability to create outputs. Examples include strategic management processes, operational processes and resource management processes. These processes typically are documented, but an organised workforce having the necessary skills and experience following rules and conventions may provide the necessary processes that are capable of being applied to inputs to create outputs. (Accounting, billing, payroll and other administrative systems typically are not processes used to create outputs.)
- Output: the result of inputs and processes applied to those inputs that provide or have the ability to provide a return in the form of dividends, lower costs or other economic benefits directly to investors or other owners, members or participants.

To be capable of being conducted and managed for the purposes defined, an integrated set of activities and assets requires two essential elements – inputs and processes applied to those inputs, which together are or will be used to create outputs. However, a business need not include all of the inputs or processes that the seller used in operating that business if market participants are capable of acquiring the business and continuing to produce outputs, for example, by integrating the business with their own inputs and processes.

The nature of the elements of a business varies by industry and by the structure of an entity's operations (activities), including the entity's stage of development. Established businesses often have many different types of inputs, processes and outputs, whereas new businesses often have few inputs and processes and sometimes only a single output (product). Nearly all businesses also have liabilities, but a business need not have liabilities.

An integrated set of activities and assets in the development stage might not have outputs. If not, the acquirer should consider other factors to determine whether the set is a business. Those factors include, but are not limited to, whether the set:

- has begun planned principal activities;
- has employees, intellectual property and other inputs and processes that could be applied to those inputs;
- is pursuing a plan to produce outputs; and
- will be able to obtain access to customers that will purchase the outputs.

Not all of those factors need to be present for a particular integrated set of activities and assets in the development stage to qualify as a business.

Determining whether a particular set of assets and activities is a business should be based on whether the integrated set is capable of being conducted and managed as a business by a market participant. Thus, in evaluating whether a particular set of assets is a business, it is not relevant whether a seller operated the set as a business or whether the acquirer intends to operate the set as a business.

In some situations, there may be difficulties in determining whether or not an acquisition of a group of assets constitutes a business and judgment will be required. Management should keep the impacts of the changes in mind when negotiating any future transactions. Companies operating in industries that are characterised by the use of expensive assets and relatively trivial processes (e.g. real estate industry) will need to assess carefully the impact of IFRS 3R in particular that the accounting for a business acquisition differs from the asset acquisition accounting what may have significant impact on the financial statements.

4. Contacts

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In 2005 he completed a post-graduate School of Real Estate Valuation at the Warsaw School of Technology.

In 2011 he completed postgraduate program in Property Valuation and Management at the Sheffield Hallam University in United Kingdom and became the member of The Royal Institution of Chartered Surveyors (MRICS).

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Anna Pleskowicz is Manager in Tax Real Estate Group at Ernst & Young's Warsaw office. She has been with EY since 2004. She is a certified tax advisor. Her skills include advising on global restructurings, international tax planning (corporate issues, financing etc.), providing tax advisory services on domestic tax law. She was involved in projects concerning tax issues in relation to the process of setting up, operating and restructuring of companies, tax assistance in establishing tax effective exit scenarios, advise on tax effective planning methods, including international tax structuring projects. In 2008 Anna worked at the Polish Tax Desk in New York. Anna is a co-author of the book "Taxation of the Polish Real Estate Market" and co-author of the book „International tax planning", an author of various articles relating to tax issues.

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4.2. Linklaters

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Artur Kulawski is a partner, and head of the real estate practice at Linklaters' Warsaw office. He has over seventeen years of Polish real estate experience, gained while working on large-scale real estate, corporate, finance, cross-border and domestic transactions.

His extensive advisory and transactional experience encompasses all aspects of investment in and development of commercial real estate. Artur also has expertise in handling administrative proceedings, including advising on all matters relating to development and construction permits, zoning, and environmental matters.

His expertise also covers areas of infrastructure and renewable energy projects development. He regularly represents investors, developers, financiers, asset managers and energy-generating and distribution companies. He has provided legal advice on land acquisitions, retail, office and residential development projects, infrastructure projects, as well as PPP and PFI projects, and transaction financing. He has also developed corporate structures for transactions, and has participated on numerous occasions in negotiating leases for retail, industrial and office space.

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Jarosław Miller is a partner and head of the finance and projects practice at Linklaters' Warsaw office. He has sixteen years of banking and finance experience, including investment banking law and transactions in capital markets. He is experienced in organising and conducting issues of commercial paper, debenture bonds, certificates of deposit and loan syndications, as well as project and structured finance. His knowledge also covers the market of derivatives, the swap market, and legal frames for operations on the open market. Jarosław has advised various financial institutions and entities in project and structured finance transactions, including the biggest finance transactions in the energy market, as well as in the real estate market, including advising financial institutions on the refinancing of existing projects, financing real estate developments, and portfolio transactions.

Jarosław is fluent in English and French.

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Weronika Guerquin-Koryzma is a senior Polish real estate lawyer and managing associate with thirteen years of experience in real estate and construction law. Weronika's experience includes advising domestic and international investors, developers and financiers in acquiring office buildings, warehouses, commercial centres and greenfields throughout Poland; advising on the preparation and implementation of construction and development projects (including transaction structuring and financing, obtaining administrative permits for construction processes, concluding agreements with architects, contractors and consultants) as well as advising in connection with sale and leaseback transactions and leasing.

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Rafał Zboch is a senior Polish real estate lawyer with twelve years of experience working for international law firms operating on the Polish market. Within the last decade, he has worked on a variety of complex real estate-related deals, both on the domestic market and involving multi-jurisdictional and international matters. Rafał focuses on all legal aspects of the construction process in Poland. He has been involved in a number of real estate sale transactions, leasing, sale and leaseback, real estate financings, joint ventures, restructurings, PPP, IPO, bankruptcy, real-estate-related litigations and arbitrations.

He has significant experience working for public entities.

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Patryk Figiel is a senior Polish real estate lawyer with ten years of experience. He advises a wide range of clients on the various aspects of carrying out real estate transactions and development work. He also focuses his practice in the area of energy related complex project development work. Patryk has a unique track record of advising developers and investment funds in the CEE/SEE region, including one year spent on secondment to Linklaters' former Bucharest office (now Kinstellar) from where he acted for international clients across a number of sectors in emerging markets (Bulgaria, Moldova and Romania).

Patryk is fluent in English and German.

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Janusz Dzianachowski is a Polish real estate lawyer, an associate with eight years of professional experience. He has been providing legal advice to domestic and international clients, primarily with respect to real estate transactions. He has taken part in numerous real estate acquisitions (including sale and leaseback and cross-border transactions), real estate due diligence projects relating to property acquisitions, and financings and IPOs of development companies.

Janusz has also advised clients in respect of property development and has negotiated lease agreements for office and warehouse space as well as with respect to the implementation of joint venture structures for real estate investments. He frequently cooperates with Linklaters' finance and projects practice in connection with property financings, in which he is responsible for real estate issues.

Janusz is fluent in English and French.

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Ewelina Laskowska-Żółw is a Polish real estate lawyer, an associate with more than seven years of experience in advising Polish and foreign entities in the areas of real estate law and corporate law. The range of her expertise covers legal due diligence and legal advice in connection with acquisitions and the management of commercial, industrial and office real estate, including negotiating lease agreements. She is also advising investors in wind farm development and exploitation matters.

Ewelina is fluent in English.

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Anna Kuszewska-Niberon is a qualified Polish legal adviser at the real estate practice of Linklaters' Warsaw office. She graduated from Warsaw University's Faculty of Law and Administration and completed studies in French and European law (DESS en droit français et européen des affaires). She has eight years' experience in representing domestic and foreign entities in matters involving many areas of law, particularly real estate law and construction law, public procurement law, and matters concerning the initial phase of implementing public private partnership structures in Poland. Anna also has experience of matters of commercial law as well as with commercial arbitration and real estate finance.

She is fluent in English and French.

Appendix

Withholding tax rates under Poland's double tax treaties (payments from Poland)

	Dividends (%)	Interest (%)	Royalties (%)
Albania	5/10 (d)	10	5
Algeria (gg)	5/15 (d)	0/10 (k)	10
Armenia	10	5	10
Australia	15	10	10
Austria	5/15 (a)	0/5 (k)	5
Azerbaijan	10	10	10
Bangladesh	10/15 (a)	0/10 (k)	10
Belarus	10/15 (e)	10	0
Belgium	5/15 (cc)	0/5 (k)	5
Bulgaria	10	0/10 (k)	5
Canada	15	0/15 (k)	0/10 (f)
Chile	5/15 (c)	15 (dd)	5/15 (h)(ee)
China	10	0/10 (k)	7/10 (h)
Croatia	5/15 (d)	0/10 (k)	10
Cyprus	10	0/10 (k)	5
Czech Republic	5/10 (c)	0/10 (k)	5
Denmark	0/5/15 (s)	0/5 (k)	5
Egypt	12	0/12 (k)	12
Estonia	5/15 (d)	0/10 (k)	10
Finland	5/15 (y)	0/5 (k)	5
France	5/15 (a)	0	0/10 (p)
Georgia	10	0/8 (k)	8
Germany	5/15 (jj)	0/5 (k)	5
Greece	19	10	10

	Dividends (%)	Interest (%)	Royalties (%)
Hungary	10	0/10 (k)	10
Iceland	5/15 (y)	0/10 (k)	10
India	15	0/15 (k)	20 (bb)
Indonesia	10/15 (c)	0/10 (k)	15
Iran	7	0/10 (k)	10
Ireland	0/15 (kk)	0/10 (k)	0/10 (v)
Israel	5/10 (b)	5	5/10 (h)
Italy	10	0/10 (k)	10
Japan	10	0/10 (k)	0/10 (i)
Jordan	10	0/10 (k)	10
Kazakhstan	10/15 (c)	0/10 (k)	10
Korea (South)	5/10 (a)	0/10 (k)	10
Kuwait	0/5 (z)	0/5 (k)	15
Kyrgyzstan	10	0/10 (k)	10
Latvia	5/15 (d)	0/10 (k)	10
Lithuania	5/15 (d)	0/10 (k)	10
Luxembourg	5/15 (d)	0/10 (k)	10
Macedonia	5/15 (d)	0/10 (k)	10
Malaysia	0	15	15
Malta	0/10 (hh)	0/5 (k)	5
Mexico	5/15 (d)	0/10/15 (k)(aa)	10
Moldova	5/15 (d)	0/10 (k)	10
Mongolia	10	0/10 (k)	5
Morocco	7/15 (d)	10	10
Netherlands	5/15 (a)	0/5 (k)	5
New Zealand	15	10	10
Nigeria (gg)	10	0/10 (k)	10
Norway	0/15 (hh)	0/5 (k)	5
Pakistan	15 (j)	0/20 (k)	15/20 (n)
Philippines	10/15 (d)	0/10 (k)	15
Portugal	10/15 (o)	0/10 (k)	10
Qatar	5	0/5 (k)	5
Romania	5/15 (d)	0/10 (k)	10
Russian Federation	10	0/10 (k)	10 (w)
Singapore	0/10 (r)	0/10 (k)	10
Slovak Republic	5/10 (c)	0/10 (k)	5
Slovenia	5/15 (d)	0/10 (k)	10
South Africa	5/15 (d)	0/10 (k)	10
Spain	5/15 (d)	0	0/10 (f)

	Dividends (%)	Interest (%)	Royalties (%)
Sri Lanka	15	0/10 (k)	0/10 (l)
Sweden	5/15 (d)	0	5
Switzerland	0/15 (ll)	10	0 (ii)
Syria	10	0/10 (k)	18
Tajikistan	5/15 (d)	10	10
Thailand	19 (t)	0/10/20 (k)(m)	5/15 (f)
Tunisia	5/10 (d)	12	12
Turkey	10/15 (d)	0/10 (k)	10
Ukraine	5/15 (d)	0/10 (k)	10
United Arab Emirates	0/5 (z)	0/5 (k)	5
United Kingdom	0/10 (ff)	0/5 (k)	5
United States	5/15 (g)	0	10
Uruguay (gg)	15	0/15 (k)	15
Uzbekistan	5/15 (c)	0/10 (k)	10
Vietnam	10/15 (d)	10	10/15 (q)
Yugoslavia (u)	5/15 (y)	10	10
Zimbabwe	10/15 (d)	10	10
Nontreaty countries	19	20	20 (x)

(a) The lower rate applies if the recipient of the dividends is a company that owns at least 10% of the payer.

(b) The lower rate applies if the recipient of the dividends is a company that owns at least 15% of the payer.

(c) The lower rate applies if the recipient of the dividends is a company that owns at least 20% of the payer.

(d) The lower rate applies if the recipient of the dividends is a company that owns at least 25% of the payer.

(e) The lower rate applies if the recipient of the dividends is a company that owns more than 30% of the payer.

(f) The lower rate applies to royalties paid for copyrights, among other items; the higher rate applies to royalties for patents, trademarks and industrial, commercial or scientific equipment or information.

(g) The lower rate applies if the recipient of the dividends is a company that owns at least 10% of the voting shares of the payer.

(h) The lower rate applies to royalties paid for the use of, or the right to use, industrial, commercial or scientific equipment.

(i) The lower rate applies to cultural royalties.

(j) This rate applies if the recipient of the dividends is a company that owns at least one-third of the payer.

(k) The 0% rate applies to among other items, interest paid to government units, local authorities and central banks. In the case of certain countries, the rate also applies to banks (the list of exempt or preferred recipients varies by country). The relevant treaty should be consulted in all cases.

(l) The 0% rate applies to royalties paid for, among other items, copyrights. The 10% rate applies to royalties paid for patents, trademarks and for industrial, commercial or scientific equipment or information.

(m) The 20% rate applies if the recipient of the interest is not a financial or insurance institution or government unit.

(n) The lower rate applies to know-how; the higher rate applies to copyrights, patents and trademarks.

(o) The 10% rate applies if, on the date of the payment of dividends, the recipient of the dividends has owned at least 25% of the share capital of the payer for an uninterrupted period of at least two years. The 15% rate applies to other dividends.

(p) The lower rate applies to royalties paid for the following:

Copyrights

The use of or the right to use industrial, commercial and scientific equipment

Services comprising scientific or technical studies

Research and advisory, supervisory or management services

The treaty should be checked in all cases.

(q) The lower rate applies to know-how, patents and trademarks.

(r) The lower rate applies to certain dividends paid to government units or companies.

(s) The 0% rate applies if the beneficial owner of the dividends is a company that holds directly at least 25% of the capital of the payer of the dividends for at least one year and if the dividends are declared within such holding period. The 5% rate applies to dividends paid to pension funds or other similar institutions operating in the field of pension systems. The 15% rate applies to other dividends.

(t) Because the rate under the domestic law of Poland is 19%, the treaty rate of 20% does not apply.

(u) The treaty with the former Federal Republic of Yugoslavia that applied to the Union of Serbia and Montenegro should apply to the Republics of Montenegro and Serbia.

(v) The lower rate applies to fees for technical services.

(w) The 10% rate also applies to fees for technical services.

(x) The 20% rate also applies to certain services (for example advisory, accounting, market research, legal assistance, advertising, management and control, data processing, search and selection services, guarantees and pledges and similar services).

(y) The 5% rate applies if the beneficial owner is a company (other than a partnership) that controls directly at least 25% of the capital of the company paying the dividends.

(z) The lower rate applies if the owner of the dividends is the government or a government institution.

(aa) The 10% rate applies to interest paid to banks and insurance companies and to interest on bonds that are regularly and substantially traded.

(bb) Because the rate under the domestic law in Poland is 20%, the treaty rate of 22.5% does not apply.

(cc) The lower rate applies if the recipient of the dividends is a company that owns either of the following:

At least 25% of the payer

At least 10% of the payer, provided the value of the investment amounts to at least €500,000 or its equivalent

(dd) The treaty rate is 15% for all types of interest. However, under a most-favored-nation clause in a protocol to the treaty, the 15% rate is replaced by any more beneficial rate agreed to by Chile in a treaty entered into with another jurisdiction. For example, under Chile's tax treaty with Spain, a 5% rate applies to certain types of interest payments, including interest paid to banks or insurance companies or interest derived from bonds or securities that are regularly and substantially traded on a recognized securities market.

(ee) The general treaty rate for royalties is 15%. However, under a most-favored-nation clause in a protocol to the treaty, the 15% rate is replaced by any more beneficial rate agreed to by Chile in a treaty entered into with another jurisdiction. For example, under Chile's tax treaty with Spain, the general withholding tax rate for royalties is 10%.

(ff) The 0% rate applies if the beneficial owner of the dividends is a company that holds at least 10% of the share capital of the payer of the dividends for an uninterrupted period of at least two years.

(gg) The treaty has not yet entered into force.

(hh) The 0% rate applies if the beneficial owner of the dividends is a company that holds directly at least 10% of the capital of the company paying the dividends on the date on which the dividends are paid and has held the capital or will hold the capital for an uninterrupted 24-month period that includes the date of payment of the dividends.

(ii) The rate is 10% if Switzerland imposes a withholding tax on royalties paid to nonresidents.

(jj) The lower rate applies if the recipient of the dividends is a company (other than partnership) that owns directly at least 10% of the payer. Certain limitations to application of the preferential rates may apply.

(kk) The lower rate applies if the beneficial owner of the dividends is a company that holds directly at least 25% of the voting power of the payer. Under the Ireland treaty, if Ireland levies tax at source on dividends, the 0% rate is replaced by a rate of 5%.

(ll) 0% applies to dividends paid to a company (other than a partnership) which holds directly at least 10% of the capital of the company paying the dividends on the date the dividends are paid and has done so or will have done so for an uninterrupted 24-month period in which that date falls. 0% rate may also apply to dividends paid to certain pensions funds.

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