Polish Real Estate Market

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Preface
EY, a global leader in assurance, tax, transaction, advisory and legal services prepared 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 2015 unless stated otherwise.
Polish Real Estate Market
1.1. Office market

Poland – general

Following major reforms in 1992, Poland experienced a boom in economic activity in the 1990s. 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 m², 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 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, 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. On the majority of Polish office markets 2011 was one of the weakest years in terms of new supply. The strict lending criteria implemented by banks after 2008 verified most of the investment processes. Currently construction activity is recovering quickly. The annual level of new supply in 2013 amounted to nearly 670,000 m², which represented significantly higher growth in comparison to previous years. The level of total completions in 2013 was the highest yearly value recorded in Poland since 2000.
New supply in 2014 amounted to 600,000 m², but taking pipeline into consideration, growing trend shall continue in following years. As far as new projects under construction and proposed are concerned, in 2014 the biggest construction activity was observed in Warsaw, Kraków, Tri-City and Katowice.

**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, when 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 2013. At the end of first half of 2013, the total modern office space in Warsaw has exceeded 4 million m², with non-central locations accounting for around 70%. Warsaw remains the most mature office market in Poland with a total office stock of approximately 4.4 million m².
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 fell and reached 6.7%. However at the end of 2012, approximately 8.8% was unoccupied. Due to the significant volume of new projects completed in 2014, the vacancy rate exceeded 13%. It is expected that the vacancy level will rise within the next few 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, Focus Filtrowa, Warsaw Trade Tower, Spektrum Tower, Plac Unii and Atrium 1. Non-central office locations include Mokotów, Ochota, Wola, Włochy and Praga district. In these locations, Wiśniowy Business Park, Business Garden, Trinity Park, Marynarska Business Park, Platinium Business Park, Poleczki Business Park, Cristal Park, Jerozolimskie Business Park and Lipowy Office Park warrant closer attention.

Yearly new stock peaked in 2000 when 360,000 m² was added to supply and there has been year-on-year growth since 2005, when 120,000 m² of new supply was added.
The year 2010 saw the completion of 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\(^2\) were delivered to the market. The majority of space is in office buildings located outside of the city center. In 2012 the market witnessed a higher growth in new office supply, which amounted to 270,000 m\(^2\).

In 2013 a record amount of new office space delivered to the market was observed exceeding 300,000 m\(^2\). Year 2014 brought slight slowdown in new supply with nearly 280,000 m\(^2\) of new space. Similarly to previous years, most of the new office buildings were situated in non-central locations. There is expected that Warsaw will strengthen its position in terms of new office supply over the next few years.

### Major office developments completed in 2014

<table>
<thead>
<tr>
<th>Name</th>
<th>Location</th>
<th>Area (m(^2))</th>
<th>Developer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gdańsk Business Centre</td>
<td>Non-central Inflancka St.</td>
<td>46,000</td>
<td>HB Reavis</td>
</tr>
<tr>
<td>Eurocentrum Office Complex I</td>
<td>Non-central Jerozolimskie Ave.</td>
<td>38,700</td>
<td>Capital Park</td>
</tr>
<tr>
<td>Warsaw Spire B</td>
<td>Central Grzybowska / Towarowa St.</td>
<td>20,000</td>
<td>Ghelamco</td>
</tr>
<tr>
<td>Nimbus Office</td>
<td>Non-central Jerozolimskie Ave.</td>
<td>19,500</td>
<td>Immofinanz</td>
</tr>
<tr>
<td>Atrium 1</td>
<td>Central Jana Pawła II Ave.</td>
<td>16,500</td>
<td>Skanska</td>
</tr>
<tr>
<td>Park Rozwoju I</td>
<td>Non-central Konstruktorska St.</td>
<td>16,000</td>
<td>Echo Investment</td>
</tr>
</tbody>
</table>

Source: EY

According to project announcements, more than 300,000 m\(^2\) of modern office space will enter the Warsaw market in 2015. 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 when reasonable level of pre-leasing has been achieved.
Major office developments under construction

<table>
<thead>
<tr>
<th>Name</th>
<th>Location</th>
<th>Total office area (m²)</th>
<th>Developer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warsaw Spire C &amp; A</td>
<td>Central Grzybowska / Towarowa St.</td>
<td>95,000</td>
<td>Ghelamco</td>
</tr>
<tr>
<td>Generation Park</td>
<td>Central Wronia</td>
<td>84,000</td>
<td>Skanska</td>
</tr>
<tr>
<td>Q22</td>
<td>Central Jana Pawła II Ave.</td>
<td>55,000</td>
<td>Echo Investment</td>
</tr>
<tr>
<td>Gdańsk Business Center II</td>
<td>Non-central Inflancka St.</td>
<td>45,000</td>
<td>HB Reavis</td>
</tr>
<tr>
<td>Postępu 14</td>
<td>Non-central Postępu St.</td>
<td>33,700</td>
<td>HB Reavis</td>
</tr>
<tr>
<td>Astrum Business Park</td>
<td>Non-central Łopuszańska St.</td>
<td>30,000</td>
<td>Prochem</td>
</tr>
<tr>
<td>Royal Wilanów</td>
<td>Non-central Klimczak/Przyczółkowa St.</td>
<td>28,000</td>
<td>Capital Park</td>
</tr>
<tr>
<td>Domaniewska Office Hub</td>
<td>Non-central Domaniewska St.</td>
<td>27,000</td>
<td>PHN</td>
</tr>
<tr>
<td>Eurocentrum Office Complex II</td>
<td>Non-central Jerozolimskie Ave.</td>
<td>25,000</td>
<td>Capital Park</td>
</tr>
<tr>
<td>Wołoska 24</td>
<td>Non-central Wołoska</td>
<td>21,000</td>
<td>Ghelamco</td>
</tr>
<tr>
<td>Atrium 2</td>
<td>Central Rondo ONZ</td>
<td>20,000</td>
<td>Skanska</td>
</tr>
<tr>
<td>Prime Corporate Center</td>
<td>Central Grzybowska St.</td>
<td>20,000</td>
<td>Golub GetHouse</td>
</tr>
</tbody>
</table>

Source: EY

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);
- state entities which are more and more interested in leasing office space rather than occupying self-owned, old and low quality buildings.

Growth surged in 2007, with take-up reaching almost 500,000 m². Take-up moderated to 525,000 m² 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 m², or approximately 40% of the previous year’s volume, with a market relegated to mainly small lease transactions.

Currently, demand is much less driven by business expansion and 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 2013 record of amount of office space (633,000 m²) were leased. In 2014 demand dropped by 3% to 612,000 m², but according to forecasts demand will continue to increase in the near future.

**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/m²/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 altogether separate markets emerged.

Currencies have also played a role in the leasing market. 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 20 and 24/m²/month.

Current rents for prime office space located outside of the city center range from EUR 11 to 15/m²/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 15-25% lower than asking rents. Asking rents depend mainly on location, building standard, size and length of lease term.

Due to the growing development activity and number of new projects scheduled for completion in 2015, it is expected that the rental rates may decrease, especially in the central locations. As a result of intense competition among landlords, the difference between asking and effective rents may increase.

**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 regulated by Polish law until 2009 (see section on legal and tax aspects);
- rents are subject to annual indexation on the basis of the consumer price index in the Eurozone (MUICP, HICP);
- 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 3.5 to 5.5 /m²/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 3-6 month rent;
- leases range from 3 to 10 years; typical contracts are 5 years, with a trend toward longer leases for larger tenants and new developments;
- Incentives for tenants are currently a common practice and their range is subject to individual negotiations, which depend mostly on the size of the occupied premises and the term of the lease agreement. Typical lease incentives include:
  - rent-free period of approx. 1 month per 1 year of lease or more;
  - fit-out allowance of approx. EUR 150–200 per m² of net office space.
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, Real) and a few new strong brands appeared (Aldi, Alma, Piotr i Paweł, Simply). Moreover, an expansion of discount stores represented by Lidl, Plus Discount, Netto and Biedronka has been observed.

Currently, the total modern retail supply accounts for 12.4 million m². Although the largest share in the retail market is held by Warsaw followed by other main cities such as Tri-City, Poznań, Wrocław, Kraków, Łódź and Katowice, investors have been seeking opportunities in smaller cities,
thus more and more projects are being opened and built in towns such as: Leszno (Galeria Goplana), Lublin (Atrium Felicity, Tarasy Zamkowe), Jelenia Góra (Galeria Sudecka, Nowy Rynek), Starogard Gdański (Galeria Neptun), Olsztyn (Galeria Warmińska), Kalisz (Galeria Amber), Elk (Brama Mazur) and Piła (Galeria VIVO!).

Modern retail space completed in 2014 amounted to around 450,000 m². Major new openings with space above 40,000 m² included Atrium Felicity (Lublin) and Galeria Warmińska (Olsztyn). Major projects in the pipeline with opening planned in years 2015-2016 are Galeria Posnania (Poznań), Zielone Arkady (Bydgoszcz), Tarasy Zamkowe (Lublin) and Sukcesja (Łódź).

Developer’s activity in small and medium cities has been observed for a few years. The actual amount of space that will be delivered to the market in 2015 will depend upon availability of financing and tenant demand for retail space. Apart from the medium - size retail projects the market is tending towards the opening of “strip malls” (convenience centers) - small retail parks with an area not exceeding 5,000 m², often located in the regional cities and constituting competition for regular shopping centers.

As in previous years in 2014 trend consisting modernization and / or extension of existing shopping malls has been observed on the market. The main extensions completed in 2014 were extensions of Gemini Park (Bielsko Biała) and CH Rywal (Biała Podlaska). Expansions being under construction are Atrium Promenada (Warsaw), Wola Park (Warsaw) Factory Ursus (Warsaw), Ogrody (Elbląg), Atrium Copernicus (Toruń), Galeria Sudecka (ex. CH Echo in Jelenia Góra), Magnolia Park (Wrocław) and Galeria Pomorska (Bydgoszcz).

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 shopping centers with a choice of interior decoration brands (e.g. Domoteka in Warsaw), DYI stores (Jula, Castorama, OBI, Praktiker, Leroy Merlin) and retail parks. The market for retail outlet centers has been developing rapidly over the last few years. Twelve centers are currently in operation in the surrounding areas of larger cities. They are operated mainly by three chains - Factory Outlet, Fashion House Outlet Centre and Outlet Center. The main schemes delivered to the market in 2014 were Outlet Centers in Lublin and Białystok. The most significant outlet center under construction is extension of Factory Ursus in Warsaw.

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 and Carrefour Market).
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 hyper and supermarket chains in terms of sales revenues include: Metro AG (Makro Cash & Carry, Media Markt, Saturn), Jeronimo Martins (Biedronka, Hebe), Tesco, Carrefour, Auchan Group (Auchan, Real, Simply), Schwarz Group (Lidl, Kaufland), Emperia Holding (Stokrotka, Milea), ITM (Intermarche, Bricomarche), E. Leclerc.

Focus on Warsaw

Total modern retail supply in Warsaw exceeds 2.1 million m², but only approximately 1.6 million m² of it could be considered “modern” retail space suitable for international occupiers. This equates to around 1 m² of total retail space per person, which even taking into consideration the disposable income of Warsaw’s inhabitants, is much lower than in major Western Europe cities, where the ratio is on average 2 m² per person.

Modern retail space includes shopping malls and hypermarkets, most of which are located outside the city center.

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

Limited new retail developments were recorded in Warsaw in 2013 and 2014. Apart from the 5,000 m² extension of Galeria Mokotów and opening of Plac Unii Shopping Center (15,500 m²) (both in 2013), there was no other key developments.

### Major shopping centers in Warsaw

<table>
<thead>
<tr>
<th>Name</th>
<th>Location</th>
<th>Area (m²)</th>
<th>Owner</th>
<th>Completion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Arkadia</td>
<td>Śródmieście Jana Pawła II Ave.</td>
<td>110,000</td>
<td>Unibail-Rodamco</td>
<td>2004</td>
</tr>
<tr>
<td>Blue City</td>
<td>Ochota Jerozolimskie Ave.</td>
<td>82,000</td>
<td>Singspiel</td>
<td>Phase I - 2004</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Phase II - planned</td>
</tr>
<tr>
<td>Wola Park</td>
<td>Wola Górczewska St.</td>
<td>73,000</td>
<td>Inter Ikea Center Poland</td>
<td>Phase I - 2002</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Phase II - planned</td>
</tr>
<tr>
<td>Atrium Promenada</td>
<td>Praga Południe Ostrobramska St.</td>
<td>66,000</td>
<td>Atrium European Real Estate</td>
<td>Phase I - 1996</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Phase II - 1999</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Phase III - 2005</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Phase IV - planned</td>
</tr>
</tbody>
</table>
In the recent years Warsaw’s high street landscape has recovered and gained importance, although in comparison to other European capitals there is still much to be done. High streets are located across the central quadrant of the city. Two retail categories dominate the high streets profile in Warsaw: gastronomy and clothing. Another well represented category is health & beauty. Also presence of luxury retailers is noticeable in some high streets in Warsaw. Nowy Świat Street is historical axis of the city linking Plac Trzech Krzyży to the Old Town and important tourist destination. There are numerous restaurants and cafés located on the street. Plac Trzech Krzyży, on the other hand, is dominated by prime and luxury brands, stylish restaurants and cafés. Another important high street in Warsaw is Marszałkowska. Chmielna Street is pedestrian walkway connecting Nowy Świat and Marszałkowska which overflow with cafés and restaurants. The opening of the second metro line is expected to enhance the attractiveness of Nowy Świat and Świętokrzyska. Prime high street rents for units of ca. 100 m² oscillate in range EUR 70-100 month/m². Units in central Warsaw vary heavily in terms of standard and accessibility. Foreign and domestic retailers have also established a strong presence on the ground floor of buildings facing Jerozolimskie Avenue and Marszałkowska Street. The section of Jana Pawła II Avenue 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.
Currently, as a result of low saturation with retail space in Warsaw and low vacancy rate (approximately 1.6%), high street locations are gaining in popularity.

Several more small shopping centers are currently under construction within the agglomeration of Warsaw: Ferio Wawer (12,500 m²), Fabryka Wołomin (31,000 m²) and Galeria Legionowo (10,500 m²). Additionally, three existing schemes are during extension works (Atrium Promenada, Wola Park and Factory Ursus) and one is being refurbished (Hala Koszyki).

Among shopping centers in the planning phase, there are Galeria Północna (64,000 m²), Galeria Wilanów (61,000 m²) and Nowa Stacja Pruszków (25,000 m²).

Retail rent rates vary widely and depend mainly on the type of a facility, location and quality. Over 2014 the rental level was stable with minor upward trend in Warsaw’s prime locations. The rates for retail units in prime locations, reach levels as high as EUR 110/m²/month.

Average rents for small units in modern shopping centers in Warsaw range from EUR 40 to 50/m²/month depending on location, unit-size and type of merchandise. Prime units of 100-150 m² are let at EUR 65 to 90/m²/month (including rents in Złote Tarasy and Arkadia, which represent the highest retail rents in Poland). Larger units lease for approximately EUR 15 to 30/m²/month. Usually anchor store operators occupying units of more than 1,000 m² pay much less than others, with average rents from EUR 9 to 12/m²/month and even lower, around EUR 5 to 8/m²/month for hypermarkets. Service charges for smaller space vary from EUR 5 to 9/m²/month. Major tenants are charged EUR 2 to 3.5/m²/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 5 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/m² for large units and up to EUR 600/m² 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 8.8 million m² of warehouse space. Although initially centralized within the Warsaw metropolitan area, the modern market can now be subdivided into seven regions, each of which has a well developed warehouse space. These include: Warsaw, Poznań, Upper and Lower Silesia, Central Poland (Łódź, Piotrków Trybunalski), Tri-City, and Kraków. 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. In the recent years situation in the financial markets has dampened accessibility to financing while raising the cost of capital, rendering some investments no longer feasible. This was evident in the “tightening” by warehouse developers, who were reducing speculative projects in order to focus on managing current stock.

After a few stable years, 2014 brought a strong upturn to the market. New supply in 2014 amounted to 1.1 M m² which is more than 14% growth of total modern warehouse stock and almost 3 times more than in year 2013. Despite the large new supply, vacancy rates decreased significantly – from c.a. 10% in 2013 to 5.5% in 2014. Rents remain on stable level.

Positive trend should continue in following years and will probably affect also regional markets such as Rzeszów, Lublin, Bydgoszcz and Opole.
The most active warehouse developers in Poland

<table>
<thead>
<tr>
<th>Company</th>
<th>Country of origin</th>
<th>Major locations (existing and proposed)</th>
</tr>
</thead>
<tbody>
<tr>
<td>AIG/Lincoln</td>
<td>USA</td>
<td>Gliwice, Łódź, Piaseczno, Stryków, Warsaw</td>
</tr>
<tr>
<td>Biuro Inwestycji Kapitałowych</td>
<td>Poland</td>
<td>Kraków, Ożarów Mazowiecki, Pruszcz Gdański, Sosnowiec</td>
</tr>
<tr>
<td>Goodman</td>
<td>Australia</td>
<td>Gdańsk, Gliwice, Kraków, Łódź, Poznań, Toruń, Sosnowiec (under construction), Warsaw, Wrocław</td>
</tr>
<tr>
<td>Menard Doswell &amp; Company</td>
<td>USA</td>
<td>Błonie, Czeladź</td>
</tr>
<tr>
<td>Metropol Group</td>
<td>Poland</td>
<td>Błonie, Warsaw</td>
</tr>
<tr>
<td>MLP Group</td>
<td>Israel</td>
<td>Bieruń, Lublin (under construction), Łódź (under construction), Poznań, Pruszków, Tychy, Wrocław (under construction)</td>
</tr>
<tr>
<td>Panattoni</td>
<td>USA</td>
<td>Bielsko-Biała, Błonie, Bydgoszcz, Czeladź, Garwolin, Gdańsk, Gliwice, Kraków, Łódź, Mysłowice, Ożarów Mazowiecki, Poznań, Pruszków, Robakowo, Rzeszów, Stryków, Święcice, Teresin, Toruń, Warsaw, Wrocław</td>
</tr>
<tr>
<td>PointPark Properties</td>
<td>UK</td>
<td>Mszczonów, Poznań</td>
</tr>
<tr>
<td>ProLogis</td>
<td>USA</td>
<td>Błonie, Chorzów, Dąbrowa Górnicza, Gdańsk, Katowice, Nadarzyn, Piotrków Trybunalski, Poznań, Rawa Mazowiecka, Ruda Śląska, Sochaczew, Stryków, Szczecin, Teresin, Ujazd, Urzut, Warsaw, Wrocław</td>
</tr>
<tr>
<td>SEGRO</td>
<td>UK</td>
<td>Gdańsk, Gliwice, Łódź, Poznaś, Stryków, Tychy, Warsaw, Wrocław</td>
</tr>
</tbody>
</table>

Source: EY

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 630,000 m² 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 2,150,000 m² 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 and II) is estimated at almost 2.8 million m² of modern space.

In 2013, around 78,000 m² of warehouse space was completed, which was over 20% decrease in comparison to 2012. In contrary to the whole Polish market, new supply in Warsaw in 2014 was significantly lower than in previous year and amounted to 38,000 m². Currently about 51,000 m² of warehouse space is under construction in Warsaw area. Future supply is hard to pin 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**

<table>
<thead>
<tr>
<th>Project</th>
<th>Location</th>
<th>Area (m²) [existing / proposed]</th>
<th>Developer / Owner</th>
<th>Completion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Diamond Business Park</td>
<td>Piaseczno</td>
<td>57,000</td>
<td>AIG Lincoln</td>
<td>2001-2007</td>
</tr>
<tr>
<td>Europolis Park Błonie</td>
<td>Błonie</td>
<td>178,000</td>
<td>Menard Doswell / CA Immo</td>
<td>2006-2012</td>
</tr>
<tr>
<td>Millenium Logistic Park Pruszków II</td>
<td>Brwinów</td>
<td>80,000 /302,000</td>
<td>MLP Group</td>
<td>2007-2014</td>
</tr>
<tr>
<td>Panattoni Park Ożarów</td>
<td>Ożarów</td>
<td>67,800</td>
<td>Panattoni</td>
<td>2009</td>
</tr>
<tr>
<td>Panattoni Park Pruszków</td>
<td>Pruszków</td>
<td>85,300</td>
<td>Panattoni</td>
<td>2007-2009</td>
</tr>
<tr>
<td>Platan Park</td>
<td>Warsaw, Ursynów</td>
<td>53,000</td>
<td>Platan Group</td>
<td>1998-2001</td>
</tr>
<tr>
<td>ProLogis Park Błonie</td>
<td>Błonie</td>
<td>153,000</td>
<td>ProLogis</td>
<td>1999-2008</td>
</tr>
<tr>
<td>ProLogis Park Teresin</td>
<td>Teresin</td>
<td>159,000</td>
<td>ProLogis</td>
<td>2000-2005</td>
</tr>
<tr>
<td>ProLogis Park Warsaw I</td>
<td>Warsaw, Okęcie</td>
<td>39,000</td>
<td>Menard Doswell / ProLogis</td>
<td>1995-1997</td>
</tr>
<tr>
<td>Project</td>
<td>Location</td>
<td>Area (m²) [existing / proposed]</td>
<td>Developer / Owner</td>
<td>Completion</td>
</tr>
<tr>
<td>--------------------------</td>
<td>------------------</td>
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<td>--------------------------</td>
<td>------------</td>
</tr>
<tr>
<td>ProLogis Park Warsaw II</td>
<td>Warsaw, Targówek</td>
<td>38,300</td>
<td>ProLogis</td>
<td>2006</td>
</tr>
<tr>
<td>Żerań Park</td>
<td>Warsaw, Żerań</td>
<td>52,000</td>
<td>Apollo Rida / Prologis</td>
<td>1999-2000</td>
</tr>
<tr>
<td>SEGRO Business Park Warsaw Żerań</td>
<td>Warsaw, Żerań</td>
<td>49,900</td>
<td>Apollo Rida/ SEGRO</td>
<td>2005-2011</td>
</tr>
</tbody>
</table>

Source: EY

In 2013 the demand for leasable warehouse space in Warsaw area amounted to approximately 344,000 m² and decreased c.a. 23% as compared to 2012. In 2014 demand increased more than 150% reaching amount of 863,000 m² - the highest score in Poland.

The most sought after unit sizes are 1,000 - 3,000 m², usually leased in office/warehouse facilities of above 10,000 m², located in logistics parks. Areas larger than 10,000 m² are usually leased by logistics operators.

Vacancy rates in Warsaw have decreased to the level of 7% comparing to the 14% in 2013.

Warsaw big box rents stay on the stable level and for 2014 are currently quoted at the following levels:

- zone I: EUR 4.0 to 5.5/m²/month;
- zone II: EUR 2.0 to 3.2/m²/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/m²/month.
1.4. Residential market

Poland – current picture

Year 2014 was the best year for residential market since the financial crisis of 2008. Record level of sales was observed. The market was driven by many factors which cumulate in that year, especially low interest rates, new government program “Mieszkanie dla Młodych” and announcement of new restrictions for mortgage granting to be implemented in 2015 as well as stable prices.

The stock of units for sale on the Polish primary residential market has been rising several years in a row until the beginning of 2012. As for Q4 2012, aggregated stock of units for sale in six main agglomerations (Warsaw, Kraków, Poznań, Wrocław, Tricity and Łódź) accounts for approx. 41,000 dwellings, which means 27% drop in comparison to the same period in 2011. It is a consequence of the “Developer Act” entered into force in April 2012. After even worse year 2013 (approx. 35,000 dwellings at the end of the year), 2014 brought upturn reaching 45,000 dwellings.

On the demand side, mortgage financing has been hampered by regulations by the Polish Financial Supervision Authority (KNF), restricting general lending terms such as creditworthiness and foreign currencies loans, leading to the ascendance of PLN-denominated loans. On the other hand, the demand is driven by exceptionally low interest rates and the new mortgage-assistance scheme “Mieszkanie dla Młodych”. However the program was introduced in the beginning of 2014 it will have major impact in following years. Although specific type of apartments fulfilling MdM program parameters are available on the market there is huge disproportion regarding price limits within the cities.
Poland - fundamentals

In the last two decades Polish residential market growth has been driven by the overall growth of the country’s economy, mortgage financing development as well as positive demographic trends.

One of the turning points determining the market shape was the boom period of 2004-2007, triggered by the EU accession and resulting inflow of investors, mortgage financing release and historically low interest rates. The boom reshaped the state of the residential market, pumping up the prices of housing and of residential land.

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 another turning point. Moderation in late 2007 led to stagnation in 2008, which ultimately gave way to price decreases in 2009.

According to data published by the Central Statistical Office, over 143 thousand units have been delivered in 2014 (1.2% less compared to the same period of 2013), out of which 58,8 thousand (41%) were constructed by developers, and 76,6 thousand (53%) by individuals. The remaining supply was delivered by housing cooperatives and municipalities, whose share remains marginal. Although number of delivered dwellings in 2014 was a bit lower than in previous year, there was a significant increase in buildings started (16%) and issued building permissions (13%).

The Polish residential market is presently the largest in Central and Eastern Europe, however, it still lags behind western EU members in terms of quality, age of stock and level of market saturation.

Moreover, statistical indicators, such as number of residential units per 1,000 inhabitants, usable floor area per one inhabitant and per average residential unit, are below the European average.

A major obstacle constraining housing supply in Poland is mainly administration-driven and consists of the limited number of zoning plans, covering below 30% of country’s area. In each single case, lack of zoning plan results in a time-consuming administrative procedure, which takes from a few months up to even a year. It is necessary to obtain zoning decision (Warunki Zabudowy), before the building permit can be applied for.

Focus on Warsaw

Warsaw's residential market remains the most developed in Poland: demand is driven mainly by in-migration, the highest income level in Poland and the lowest unemployment rate. Employment and education possibilities in Warsaw are a magnet for young people from other regions of Poland, resulting in the dominance of multifamily developments in the Warsaw residential market. More than 10% of Polish residential supply is provided on Warsaw market. The share of new housing units in single-family developments built in Warsaw remains under 1%. Currently the market is determined by rising volume
of transactions, resulting mainly from low interest rates, savings withdrawal and reinvestment as well as financing restrictions which started from 2014 and will be tightened in following years (since the beginning of 2015 own contribution shall be at least 10% and it will be increased by 5 percentage points in 2016 and 2017).

After the record year of 2001, completed units in Warsaw fluctuated between 10,000 and 15,000 p.a. for several years. Following the boom period, unit completions increased to 19,049 and to 19,482, for 2008 and 2009, respectively. However, in 2009 unit starts were starkly curtailed, resulting in the delivery of only 12,462 dwellings in 2010 and 9,408 in 2011. In the beginning of 2012 the situation on the residential market was mainly influenced by a very high supply of dwellings released in January-April period. This was mainly driven by introduction of “Developer Act” in the end of April. The year 2013 showed a moderate developer’s output: according to the data provided by the Central Statistical Office, nearly 13,200 apartments were completed.

According to market data, the primary market in Warsaw in Q4 2014 offered over 18,000 units for sale, out of which 3,500 have been already delivered. Warsaw remained the most expensive residential market with an average apartments’ transaction price of approx. 7,300 PLN/m².

Buyers pay on average 7.5% less than initial price. This mainly concerns the secondary market and is also due to better alignment of demand and supply, as well as large number of completed new residential investments. According to National Bank of Poland the average asking price of apartments on the primary market in Warsaw is currently at the level of 7,900 PLN/m², while the highest average prices were observed in Śródmieście (PLN 11,400/m²) and the lowest in Białołęka district (below PLN 6,000/m²). Apart from Śródmieście, the most expensive districts in Warsaw remain Mokotów, Ochota, Bielany, Ursynów and Żoliborz.

Similar to the rest of the country, demand on Warsaw market is on the upturn due to low interest rates and government support but there is a threat of a slow down after mortgage financing regulations that will be tightened gradually in following 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).

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

Warsaw remains an important transaction market in Poland perceived by many investors as core, but smaller scale properties in secondary towns continue to gain ground. In 2014 the total volume of investment transactions in Poland amounted to approximately EUR 3.1 billion. It is 6% less than in 2013 but it is still the second best value since 2006 when highest volume ever were achieved. The major investment activity was observed in warehouse and office sectors.

Transaction volumes look set to rise, supported in large part by international investment, but also Polish capital seems to catch up. In 2014 a Polish
closed-end investment fund acquired a EUR 140 mln warehouse portfolio. The transaction was one of the biggest made by Polish investor.

**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 Blackstone, CA Immo, IVG, DEKA, CBRE Global Investors, Griffin and RREEF.
# Major real estate funds investing in Poland

<table>
<thead>
<tr>
<th>Name</th>
<th>Segment</th>
<th>Major Assets in Poland</th>
</tr>
</thead>
<tbody>
<tr>
<td>AEW Capital</td>
<td>Office Warehouse</td>
<td>Good Point Puławska, Warehouses in Gliwice, Klif Warsaw, Klif Tri-City, Atrium Tower in Warsaw</td>
</tr>
<tr>
<td>AIB Polonia Property Fund/Peakside Capital</td>
<td>Office Retail</td>
<td>Atrium Plaza Warsaw, Atrium Centrum, Wiśniowy Business Park, Fashion House Outlets in Sosnowiec, Gdańsk and Warsaw, Diamond Business Park, Warsaw Distribution Centre</td>
</tr>
<tr>
<td>Allianz RE</td>
<td>Office Retail</td>
<td>Silesia City Center, Warsaw Financial Center, Platinium Business Park</td>
</tr>
<tr>
<td>Atrium European Real Estate</td>
<td>Retail</td>
<td>Reduta Shopping Center, Promenada Shopping Center, Galeria Dominikańska, Focus Park in Bydgoszcz, Lublin Felicity</td>
</tr>
<tr>
<td>Áviva Central European Property Fund</td>
<td>Office Retail</td>
<td>Irydion office building, Shopping malls (Focus Mall) in Piotrków Trybunalski, Zielona Góra, Rybnik</td>
</tr>
<tr>
<td>Axa Group</td>
<td>Retail</td>
<td>Złote Tarasy Shopping Center - partial interest</td>
</tr>
<tr>
<td>Azora</td>
<td>Office</td>
<td>Aquarius Business House in Wrocław, Cristal Park, Mokotów Plaza, Harmony Office Center Complex in Warsaw, Green Office Complex and Avatar in Kraków (JV)</td>
</tr>
<tr>
<td>BlackRock</td>
<td>Retail</td>
<td>CH Karolinka in Opole, Pogoria in Dąbrowa Górnicza</td>
</tr>
<tr>
<td>Blackstone</td>
<td>Retail Warehouse</td>
<td>Shopping malls: Twierdza Klodzko, Galeria Leszno, Magnolia Park (Wrocław), Twierdza Zamość (Zamość), Wzorcownia Włocławek, Galeria Pestka (Poznań), Galeria Tęcza (Kalisz), warehouse portfolio in Łódź, Łazy, Błonie, Czeladź, Gliwice, Kraków, Piaseczno</td>
</tr>
<tr>
<td>CA Immo</td>
<td>Office Warehouse</td>
<td>Poleczki Business Park, Saski Point, Saski Crescent, Sienna Center, Europolis Park Poland Central, Europolis Park Blonie</td>
</tr>
<tr>
<td>CBRE Global Investors</td>
<td>Office Retail</td>
<td>Warsaw Distribution Centre, Manhattan Business &amp; Distribution Centre, Idea Idea, CH Sarni Stok, CH Ogrody, Złote Tarasy - partial interest, Galeria Mazovia, Wars Sawa Junior, King Cross Praga, Prosta Office Center, Trinity Office Park</td>
</tr>
<tr>
<td>Name</td>
<td>Segment</td>
<td>Major Assets in Poland</td>
</tr>
<tr>
<td>---------------------------</td>
<td>---------------</td>
<td>------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>DEKA Immobilien</td>
<td>Office</td>
<td>Atrium 1, Atrium City, Bema Plaza (Wrocław), North Gate, Mokotowska Square, Forum Gliwice, Ibb Andersia Hotel (Poznań), Andel’s Hotel (Kraków), International Business Center (Warsaw), Intercontinental Warsaw (50%)</td>
</tr>
<tr>
<td></td>
<td>Retail</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Hotel</td>
<td></td>
</tr>
<tr>
<td>Griffin RE</td>
<td>Office</td>
<td>DH Renoma, Centrum Biurowe Lubicz I &amp; II, Microsoft House, Nordic Park, Bliski Center, Prima Court, Philips House, Batory Office Building I, Green Horizon</td>
</tr>
<tr>
<td></td>
<td>Retail</td>
<td></td>
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<tr>
<td>Heitman</td>
<td>Office</td>
<td>Marynarska Business Park, EMPARK, Galeria Tarnovia, Galeria Malta</td>
</tr>
<tr>
<td></td>
<td>Retail</td>
<td></td>
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<tr>
<td>Immofinanz</td>
<td>Office</td>
<td>Silesia Logistic Park, Łopuszańska Business Park, STOP.SHOP Legnica, IO-1, Crown Tower &amp; Point, Brama Zachodnia, Equator, Bokserska Office Center, Park Postępu, EMPARK</td>
</tr>
<tr>
<td></td>
<td>Retail</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Warehouse</td>
<td></td>
</tr>
<tr>
<td>Invesco</td>
<td>Office</td>
<td>Plac Unii, Zaufek Piękna, Galeria Kazimierz, Crown Square</td>
</tr>
<tr>
<td></td>
<td>Retail</td>
<td></td>
</tr>
<tr>
<td>IVG</td>
<td>Office</td>
<td>CH Platan Zabrze, CH Sosnowiec, Drukarnia Bydgoszcz, BTA, Norway House, Victoria Building, Jerozolimskie Business Park, Jerozolimskie Offices, Nowogrodzka 21, Miodowa 10, Metron, Ujazdowskie 10, LePalais, Feniks, Royal Trakt Offices</td>
</tr>
<tr>
<td></td>
<td>Retail</td>
<td></td>
</tr>
<tr>
<td>Kulczyk Silverstein</td>
<td>Office</td>
<td>Stratos Office Center, Plac Małachowskiego, Mazowiecka 2/4, ETHOS, Ufficio Primo, Warta Tower, Krucza House</td>
</tr>
<tr>
<td>Properties</td>
<td>Retail</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Warehouse</td>
<td></td>
</tr>
<tr>
<td>London &amp; Cambridge</td>
<td>Retail</td>
<td>CH Zielone Tarasy, CH Echo Piotrków Trybunalski, CH Echo Radom, CH Echo Tarnów, CH EMKA, Logistic &amp; Business Park Bydgoszcz, Centrum Logistyczne Jasieniska</td>
</tr>
<tr>
<td>Properties</td>
<td>Warehouse</td>
<td></td>
</tr>
<tr>
<td>PZU TFI</td>
<td>Retail</td>
<td>Galeria Jeziorak, Galeria Echo Pabianice, Alma Nowy Targ, Green Towers, Panattoni Warehouses Łódź, Gdańsk &amp; Wrocław</td>
</tr>
<tr>
<td></td>
<td>Office</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Warehouse</td>
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<tr>
<td>Name</td>
<td>Segment</td>
<td>Major Assets in Poland</td>
</tr>
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<td>--------------------</td>
<td>-------------</td>
<td>----------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>RREEF</td>
<td>Office</td>
<td>Rondo 1, Metropolitan, Green Conrer &amp; Nordea House, Grunwaldzki Center, Kopernik Office Buildings, Nefryt Warsaw, Topaz Warsaw, Focus</td>
</tr>
<tr>
<td>SEB Investment</td>
<td>Office</td>
<td>Philips Building Łódź, Arkonska Business Park Gdańsk (partly sold), University Business Center, Riverside Park Warsaw, Salzburg Center Warsaw, Trinity Park III, Marynarska Point 2</td>
</tr>
<tr>
<td>Starwood Capital</td>
<td>Office</td>
<td>Katowice Business Point, T-Mobile Office Park, Łopuszanka Business Park, Quattro Business Park</td>
</tr>
<tr>
<td>Tristan Capital Partners</td>
<td>Office Retail</td>
<td>Warsaw Financial Center (JV), Jantar shopping center (JV), Mokotów Nova, Arena, CH Borek, CH Dąbrówka, Galeria Turzyn, Zakopianka</td>
</tr>
<tr>
<td>Unibail-Rodamco</td>
<td>Retail</td>
<td>Galeria Mokotów, Arkadia, Warszawa Wileńska</td>
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<tr>
<td>Union Investment RE</td>
<td>Office Retail</td>
<td>Dominikański Office, Senator, Manufaktura, Zebra Tower, Horizon Plaza</td>
</tr>
<tr>
<td>Valad</td>
<td>Retail Warehouse</td>
<td>Technicznà Industrial Park, Raszyn Business Park, Piaseczno Business Park, Błonie Business Park, Gazowa Industrial Park, City Point, CH Ster, CH Rondo, CH Krokus, CH King Cross, CH Tulipan, CH Kometa</td>
</tr>
</tbody>
</table>

Source: EY

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. Recent few years show that investment market is on the rise again. However it is more stable and less aggressive than before 2007.
**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. Years 2011, 2012 and 2013 showed a significant increase in activity of investors. Capitalization rates generally appear to be around 6% - 7%. In 2014 prime office yields for CBD locations were in the range of the same level as year before.

**Major office building transactions in Poland, 2014**

<table>
<thead>
<tr>
<th>Building</th>
<th>Location</th>
<th>Seller</th>
<th>Purchaser</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rondo I</td>
<td>Warsaw</td>
<td>BlackRock Real Estate</td>
<td>RREEF</td>
</tr>
<tr>
<td>Matropolitan</td>
<td>Warsaw</td>
<td>Aberdeen</td>
<td>RREEF</td>
</tr>
<tr>
<td>Lipowy Office Park</td>
<td>Warsaw</td>
<td>CA Immo</td>
<td>WP Carey</td>
</tr>
<tr>
<td>Katowice Business Point, T-Mobile Office Park,</td>
<td>Katowice, Warsaw</td>
<td>Ghelamco</td>
<td>Starwood Capital Group</td>
</tr>
<tr>
<td>Łopuszańska Business Park</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>FDS Plaza, Light House, Quattro Forum, Winogrady Business Center, Red Tower, Alfa Plaza</td>
<td>Warsaw, Łódź, Wrocław, Poznań, Tri-City</td>
<td>Arka BZ WBK</td>
<td>Octava FIZAN</td>
</tr>
<tr>
<td>Ambasador</td>
<td>Warsaw</td>
<td>Kronos Real Estate</td>
<td>Hines</td>
</tr>
<tr>
<td>Plac Unii</td>
<td>Warsaw</td>
<td>Liebrecht &amp; woO, BBI Development</td>
<td>Invesco Real Estate</td>
</tr>
<tr>
<td>Libra Business Centre I</td>
<td>Warsaw</td>
<td>Mermaid Properties</td>
<td>Vienna Insurance Group</td>
</tr>
<tr>
<td>Dominikański</td>
<td>Wrocław</td>
<td>Skanska</td>
<td>Union Investment RE</td>
</tr>
<tr>
<td>Kapelanka</td>
<td>Kraków</td>
<td>Skanska</td>
<td>Reino Partners</td>
</tr>
<tr>
<td>Lubicz Office Center</td>
<td>Kraków</td>
<td>Peakside Capital</td>
<td>Griffin RE</td>
</tr>
<tr>
<td>Aquarius Business House</td>
<td>Wrocław</td>
<td>Echo Investment</td>
<td>Azova</td>
</tr>
</tbody>
</table>

*Source: EY*
In terms of regional cities, investors are more cautious and prefer to buy A-class properties, well leased and centrally located in large cities. While in 2011 no investment transaction took place, in 2012 and 2013 several transactions in the regional cities were made. Year 2014 brought significant increase, office investment volume in regional cities was doubled comparing to 2013, reaching EUR 400 million.

**Retail properties**

Significant investments 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 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%.

After very intensive year 2013, year 2014 appears to be pull back for the market. Volume in 2014 was 2.5 times less than in previous year, but prognosis are that this is only temporary slowdown and year 2015 shall be comparable to 2013. In 2014 the largest retail deals included Poznań City Center, Focus Mall Bydgoszcz and Galeria Mazovia in Płock. The major modern retail transactions are presented in the table below.

Capitализation rates generally appear to be around 7.5-8%. In 2014 prime retail yields in Poland were in the range of 5.75-7%.

### Major modern retail transactions, 2014

<table>
<thead>
<tr>
<th>Building</th>
<th>Seller</th>
<th>Purchaser</th>
</tr>
</thead>
<tbody>
<tr>
<td>Poznań City Center</td>
<td>Trigranit, Europa Capital, Polskie Koleje Państwowe S.A.</td>
<td>Resolution Property, ECE</td>
</tr>
<tr>
<td>Galeria Mazovia</td>
<td>Lewandpol</td>
<td>CBRE European Shopping Centre Fund</td>
</tr>
<tr>
<td>Focus Mall Bydgoszcz</td>
<td>Aviva Investors</td>
<td>Atrium European Real Estate</td>
</tr>
<tr>
<td>Plac Unii</td>
<td>Liebrecht &amp; wood, BBI Development</td>
<td>Invesco Real Estate</td>
</tr>
<tr>
<td>Galeria Piła</td>
<td>Rank Progress</td>
<td>Immofinanz Group</td>
</tr>
<tr>
<td>Galeria Ostrowiec</td>
<td>USS</td>
<td>First Property Group</td>
</tr>
<tr>
<td>Nova Park (50%)</td>
<td>Caelum Development</td>
<td>Futureal</td>
</tr>
</tbody>
</table>

Source: EY
**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 have been 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. In 2012 and 2013 a significant increase in the number of industrial transactions was observed. Year 2014 continues the trend with volume of EUR 700 millions and 17% annual growth. Capitalization rates for the modern, best performing properties are around 8%.

**Major warehouse space transactions, 2014**

<table>
<thead>
<tr>
<th>Building</th>
<th>Location</th>
<th>Seller</th>
<th>Purchaser</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warehouse portfolio</td>
<td>Mysłowice, Stryków, Robakowo</td>
<td>Standard Life</td>
<td>LogiCor</td>
</tr>
<tr>
<td>Pramerica and Panattoni portfolio</td>
<td>Błonie, Czeladź, Gliwice, Kraków, Łazy</td>
<td>Pramerica</td>
<td>LogiCor</td>
</tr>
<tr>
<td>Tesco warehouse (BTS)</td>
<td>Gliwice</td>
<td>Invesco</td>
<td>Prologis</td>
</tr>
<tr>
<td>Żerań Park I</td>
<td>Warsaw</td>
<td>Heitman</td>
<td>Prologis</td>
</tr>
<tr>
<td>Bokserka Distribution Park</td>
<td>Warsaw</td>
<td>Immofinanz</td>
<td>UK &amp; European Investments</td>
</tr>
<tr>
<td>Prologis Park Sosnowiec</td>
<td>Sosnowiec</td>
<td>Prologis</td>
<td>Hines</td>
</tr>
<tr>
<td>Prologis Park Gliwice</td>
<td>Gliwice</td>
<td>Invesco</td>
<td>Prologis</td>
</tr>
<tr>
<td>Warehouse portfolio</td>
<td>Pruszków, Łódź, Poznań</td>
<td>Tristan Capital Partners, AEW, Alpha Industrial</td>
<td>Segro, PSP</td>
</tr>
<tr>
<td>Idea I, II, III</td>
<td>Warsaw</td>
<td>BPH TFI</td>
<td>CBRE Global Investors</td>
</tr>
<tr>
<td>Panattoni Busines Park Portfolio</td>
<td>Łódź, Gdańsk, Wrocław</td>
<td>Panattoni</td>
<td>PZU TFI</td>
</tr>
<tr>
<td>Castorama BTS</td>
<td>Łódź</td>
<td>Invesco</td>
<td>Prologis</td>
</tr>
<tr>
<td>Europolis Park Portfolio</td>
<td>Błonie, Łódź</td>
<td>CA Immo, EBRD</td>
<td>P3, Ivanhoe Cambridge</td>
</tr>
<tr>
<td>Panattoni Park I</td>
<td>Błonie, Wrocław</td>
<td>Standard Life</td>
<td>Hillwood</td>
</tr>
<tr>
<td>Panattoni Park</td>
<td>Bielsko-Biała</td>
<td>Invesco</td>
<td>Hillwood</td>
</tr>
</tbody>
</table>

*Source: EY*
## 1.6. Key cities in Poland

### WARSAW

<table>
<thead>
<tr>
<th>Category</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
<td>1,729,000</td>
</tr>
<tr>
<td>Unemployment</td>
<td>4.3%</td>
</tr>
<tr>
<td>Major industries</td>
<td>Trade and services</td>
</tr>
<tr>
<td>Major companies</td>
<td>Accenture, Bank Pekao, BGŻ, mBank, British American Tobacco, Budimex, Bumar, Citibank, Coca-Cola, Colgate Palmolive, Deloitte, EY, France Telecom, General Motors, Grupa Żywiec, GTC, Huta Arcelor Warszawa, IBM, ING, Kompania Piwowarska, KPMG, Kraft Foods Polska, Mostostal Export, Nestle, PGNiG, PKO, BP, PLL LOT, Polkomtel, Procter &amp; Gamble, PwC, PZU, RBS, RWE, Samsung Electronics Polska, Shell, Skanska, Strabag, Unilever</td>
</tr>
</tbody>
</table>

### Office sector

<table>
<thead>
<tr>
<th>Category</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rental level (m²/month)</td>
<td>EUR 21 - 24 (class-A space) EUR 11 - 13 (class-B space)</td>
</tr>
<tr>
<td>Total office Stock</td>
<td>4.4 million m² of modern space</td>
</tr>
</tbody>
</table>
### Future supply (selected buildings)


### General vacancy level

13%

### Retail sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 90 - 100 for prime shopping center units up to EUR 75 - 90 for prime street units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total retail stock</td>
<td>1,8 million m² of modern space</td>
</tr>
</tbody>
</table>

### Current supply

Arkadia, Blue City, CH Bemowo, CH Janki, Atrium Reduta, Atrium Targówek, CH Wileńska, Dom Towarowy Braci Jablowskich, Fort Wola, Galeria Mokotów, King Cross, Klif, M1 Marki, Atrium Promenada, Plac Unii Shopping Center, Sadyba Best Mall, Wola Park, Wolf Bracka, Złote Tarasy, Auchan Łomianki, Galeria Brwinów, Factory Outlet Ursus, Galeria Rembielińska, Fashion House Piaseczno, Factory Outlet Annopol

### Future supply

Galerio Legionowo, Galeria Wilanów, Galeria Północna, Factory Ursus, Nowa Stacja, Hala Koszyki (reconstruction)

### Warehouse sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 2.5 - 5.0</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total warehouse stock</td>
<td>2,8 million m²</td>
</tr>
<tr>
<td>Current and planned supply in Warsaw area</td>
<td></td>
</tr>
<tr>
<td>------------------------------------------</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>KRAKÓW</th>
</tr>
</thead>
<tbody>
<tr>
<td>Population</td>
</tr>
<tr>
<td>Unemployment</td>
</tr>
<tr>
<td>Major industries</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Office sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rental level (m²/month)</td>
</tr>
<tr>
<td>Current supply (selected buildings)</td>
</tr>
<tr>
<td>Alma Tower, Alstar Office Center, Avatar, Azbud Business Center, Bonarka4Business Center, Brama Bronowicka, Buma Square, CBil Copernicus, Centrum Biurowe Euromarket, Centrum Biurowe Kazimierz, Centrum Biurowe Lubicz, Cracovia Business Center, Diamante Plaza, Edison, Enterprise Park, Fronton, G21, Galileo, Green Office, K1, Kazimierz Office Center, Kraków Business Park (Zabierzów), M65, Meduza, Newton, Nowa Kamienica, Onyx, Pascal, Portus, Quattro Business Park, Rondo Business Park, Vinci Office Center.</td>
</tr>
<tr>
<td>Future supply</td>
</tr>
<tr>
<td>Aleja Pokoju 5, Axis, Bonarka4Business E, F, G, Dot Office, Enterprise Park II, GO Center, Opolska Business Park, Orange Office Park II, Park Club, Quattro Business Park (next phases), Topos, Wawel HQ</td>
</tr>
</tbody>
</table>
### General vacancy level

6%

### Retail sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 65 - 75 for prime shopping center units</th>
<th>EUR 50 - 80 for prime street units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total retail stock</td>
<td>750,000 m² of modern space</td>
<td></td>
</tr>
<tr>
<td>Current supply</td>
<td>Galeria Krakowska, Galeria Kazimierz, CH Krokus, CH Zakopianka, M1 Kraków, IKEA, Kraków Plaza, CH Czyżyny, Solvay Park, Futura Park, CH Dekada Park, Castorama, CH Wielicka, Bonarka, Galeria Bronowice</td>
<td></td>
</tr>
<tr>
<td>Future supply</td>
<td>Serenada Shopping Center</td>
<td></td>
</tr>
</tbody>
</table>

### Warehouse sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 3.75 - 4.50</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total warehouse stock</td>
<td>189,000 m²</td>
</tr>
<tr>
<td>Current and planned supply</td>
<td>Logistic Center Kraków I, II, III, Kraków Airport Logistics Centre, MARR Business Park, MK Logistics Park, Panattoni Park Kraków</td>
</tr>
</tbody>
</table>

---

**POZNAŃ**

<table>
<thead>
<tr>
<th>Population</th>
<th>547,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment</td>
<td>3.2%</td>
</tr>
<tr>
<td>Major industries</td>
<td>Food processing, electro technical, chemical, automotive, retail, services (including finance and banking), construction industry, location of major trade fairs in Poland</td>
</tr>
<tr>
<td>Major companies</td>
<td>Aluplast Austria, Beiersdorf, Bridgestone, Carlsberg, CPC International, Enea, Franklin Templeton Investments, GlaxoSmithKline, IKEA, Kompania Piwowarska, Lorenz Bahlsten, MAN, Międzynarodowe Targi Poznańskie, Nestle, Volkswagen, Wrigley, Wyborowa</td>
</tr>
</tbody>
</table>
### Office sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 14 - 15 (class-A space)</th>
<th>EUR 11 - 13 (class-B space)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total office stock</td>
<td>334,000 m² of modern space</td>
<td></td>
</tr>
<tr>
<td>Current supply (selected buildings)</td>
<td>Andersia Business Centre, Andersia Tower, Centrum Tulipan, City Park, Delta, Dwór Hamburski, Galeria MM, Globis, Jet Office, Kupiec Poznański, Kwadraciak, Malta House, Malta Office Park, Nickel Technology Park, Nobel Tower, Nowe Garbary, Nowe Jeżyce, Okraglak, Omega, PGK Centrum, Poznań Financial Center, Poznańskie Centrum Biznesu, Rataje 164, RB House, Skalar Office Center, Szyperska Office Center, Temida, Winogrady Business Center</td>
<td></td>
</tr>
<tr>
<td>Future supply</td>
<td>Bałtyk Tower, Business Garden Poznań, Maraton, Ubiq</td>
<td></td>
</tr>
</tbody>
</table>

#### General vacancy level

| General vacancy level | 13.7% |

### Retail sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 70 - 80 for prime shopping center units</th>
<th>EUR 45 for prime street units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total retail stock</td>
<td>705,000 m² of modern space</td>
<td></td>
</tr>
<tr>
<td>Current supply</td>
<td>Stary Browar, Poznań Plaza, King Cross Marcelin, Kupiec Poznański, Auchan - Swadzim and Komorniki, ETC - Swarzędz, CH M1, IKEA, CH Franowo, Galeria Panorama, CH Piątkowo, Factory Outlet - Łuboań, Galeria Podolany, Galeria Pestka, CH Malta, Green Point, Galeria Sucholeska, Galeria Malta, Poznań City Center, Park Handlowy Franowo, Galeria MM</td>
<td></td>
</tr>
<tr>
<td>Future supply</td>
<td>Posnania, CH Metropolis, Galeria A11</td>
<td></td>
</tr>
</tbody>
</table>

### Warehouse sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 3.2 - 3.5</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Total warehouse stock</th>
<th>1,023,000 m²</th>
</tr>
</thead>
</table>

**TRI-CITY**

<table>
<thead>
<tr>
<th>Population</th>
<th>747,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment</td>
<td>5.6%</td>
</tr>
<tr>
<td>Major industries</td>
<td>Maritime industry, fuel industry, construction, food processing, tourism, IT</td>
</tr>
</tbody>
</table>

**Office sector**

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 14 - 15 (class-A space)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>EUR 11 - 13 (class-B space)</td>
</tr>
<tr>
<td>Total office stock</td>
<td>540,000 m² of modern space</td>
</tr>
<tr>
<td>General vacancy level</td>
<td>11.5%</td>
</tr>
</tbody>
</table>
### Retail sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 35 - 50 for prime shopping center units</th>
<th>EUR 25 - 45 for prime street units</th>
<th>EUR 8 - 12 for retail park units</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total retail stock</td>
<td>619,130 m² of modern space (24 shopping malls)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current supply</td>
<td>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, Auchan Port Rumia, CH Klif, Batory, ETC Gdańsk, 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 Chelm, IKEA, CH Oliwa, Galeria Przymorze, Centrum Haffnera, Szperk Gdynia, CH Riviera, Morski Park Handlowy, Centrum Kowale</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Future supply</td>
<td>Forum Radunia</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Warehouse sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 3.0 - 3.5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total warehouse stock</td>
<td>210,600 m²</td>
</tr>
<tr>
<td>Modern warehouse stock under construction</td>
<td>ProLogis Park Gdańsk, Centrum Logistyczne Pruszcz Gdański, Panattoni Park Gdańsk, SEGRO Logistics Park, 7R Logistic Park Gdańsk, Port Gdynia Warehouse</td>
</tr>
</tbody>
</table>

### Łódź

<table>
<thead>
<tr>
<th>Population</th>
<th>709,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment</td>
<td>10.8%</td>
</tr>
<tr>
<td>Major industries</td>
<td>Textile &amp; clothes, food processing, mechanical engineering, chemical production, trade fairs</td>
</tr>
</tbody>
</table>
### Major companies


### Office sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 11 - 14 (class-A/B space)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total office stock</td>
<td>300,000 m² of modern space</td>
</tr>
<tr>
<td>Future supply</td>
<td>Aurus, University Business Park II</td>
</tr>
<tr>
<td>General vacancy level</td>
<td>7.5%</td>
</tr>
</tbody>
</table>

### Retail sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 45 - 60 for prime shopping center units EUR 23 - 35 for shopping center units EUR 20 - 40 for high street locations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total retail stock</td>
<td>630,000 m² of modern space</td>
</tr>
<tr>
<td>Current supply</td>
<td>Small boutiques along Piotrklowska street, Modern shopping centers: Manufaktura, Galeria Łódzka, Tulipan Center, Pasaż Łódzki, CH M1, E. Leclerc, CH Carrefour Przybyszewskiego, OBI, Praktiker, Castorama, Leroy Merlin, Makro Cash &amp; Carry, Selgros Cash &amp; Carry, CH Ptak in Rzgów, CH Guliwer, CH Tesco Bałuty, CH Tesco Widzewska, Port Łódź, Ptak Outlet, Vis a vis Street Mall, CH Carrefour Kolumny</td>
</tr>
<tr>
<td>Future supply</td>
<td>Łódź Plaza, Sukcesja</td>
</tr>
</tbody>
</table>
**Warehouse sector**

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 3.4 - 4.3 for modern space</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total warehouse stock</td>
<td>1,06 million m²</td>
</tr>
</tbody>
</table>

**WROCŁAW**

<table>
<thead>
<tr>
<th>Population</th>
<th>633,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment</td>
<td>4.3%</td>
</tr>
<tr>
<td>Major industries</td>
<td>automotive, IT, business process offshoring, pharmacy/medical assortment, finances, medical machinery production, electrical, metallurgy, house appliances and food processing</td>
</tr>
<tr>
<td>Major companies</td>
<td>3M, Alcatel, Bosch, BZ WBK, Cadbury, Credit Agricole, Eurobank, EY SSC, Credit Suisse, Google, Hewlett-Packard, IBM, KRUK, LG, MacoPharma, Nokia, Polifarb, Siemens, Toyota, Ultimo, US Pharmacia, Volvo, Wabco, Whirlpool</td>
</tr>
</tbody>
</table>

**Office sector**

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 14 - 16 (class-A space)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>EUR 11 - 13 (class-B space)</td>
</tr>
<tr>
<td>Total office stock</td>
<td>541,000 m² of modern space</td>
</tr>
</tbody>
</table>
### Current supply (selected buildings)

### Future supply
Business Garden, Dominikański, Dubois 41, Gamma Office, North Office, Nobilis, West Gate

### General vacancy level
10.4%

### Retail sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 65 - 75 for prime shopping center units</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>EUR 40 - 60 for prime street units</td>
</tr>
<tr>
<td></td>
<td>EUR 8 - 12 for retail park units</td>
</tr>
</tbody>
</table>

**Total retail stock**

670,000 m² of modern space

### Current supply
Pasaż Grunwaldzki, Arkady Wrocławskie, Magnolia Park, Factory Outlet, CH Korona, Bielany Retail Park (IKEA), Auchan Retail Park Bielany, Galeria Dominikańska, Szewska Center, Kaufland, CH Borek, TGG, Tesco, E. Leclerc, IKEA, CH Marino, Renoma (after modernization, Sky Tower, Ferio Gaj, Retail Park Młyn, Family Point, Retail Park Bielany

### Future supply
Galeria Idylla

### Warehouse sector

<table>
<thead>
<tr>
<th>Rental level (m²/month)</th>
<th>EUR 2.9 - 3.5</th>
</tr>
</thead>
</table>

**Total warehouse stock**

895,000 m² of modern space
### KATOWICE

<table>
<thead>
<tr>
<th>Population</th>
<th>303,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unemployment</td>
<td>4.7%</td>
</tr>
<tr>
<td>Major industries</td>
<td>Coal mining, metallurgical, steel, machinery, electrical, ceramic, automotive, printing, information and IT</td>
</tr>
<tr>
<td>Major companies</td>
<td>Capgemini, Cartotecnica Polska, Delphi Automotive System, DuPont, Electrabel Polska, Elektromontaż 1 Katowice, General Motors, GK Farmakol, GK Tauron Polska Energia, IBM, ING, Isuzu Motors, Katowicki Holding Węglowy, PepsiCo, Philips, Polski Koks, Powertrain Polska, PwC SSC, Roca, Unilever</td>
</tr>
<tr>
<td>Office sector</td>
<td></td>
</tr>
</tbody>
</table>
| Rental level        | EUR 13 - 14 (class-A space)  
                    | EUR 10 - 12 (class-B space) |
| Total office stock  | 352,000 m² of modern space |
| Current supply      | Altus, Apiss Center Point, Armii Krajowej 6, Atrium, Centrum Biurowe Francuska, Centrum Biurowe Katowice, Chorzowska 50, Euro-Centrum Katowice, Górnośląski Park Przemysłowy, Jesionowa Business Point, Kostki, Millennium Plaza Katowice, Nowe Katowickie Centrum Biznesu, Rawa Office |
| Future supply       | A4 Business Park II, III, Piaskowa Business Center, Silesia Business Park I, Silesia Star I, Steel Office, Żelazna |
| General vacancy level | 13.8% |
### Retail sector

| Rental level (m²/month) | EUR 50 - 65 for prime shopping center  
|                         | EUR 25 - 45 high street locations  
|                         | EUR 9 - 11 for retail park units  
| **Total retail stock**  | 1.3 million m² of modern space  
| **Current supply**      | Silesia City Center I and II (extension), 3 Stawy, CH Dąbrówka, Castorama, OBI, Media Markt, Retail Park RAWA (IKEA), Dom Handlowy Zenit, Galeria Auchan, Galeria Katowicka, Rawa Park Handlowy, Galeria Skarbek, Galeria Nowy Różdżenie |

### Warehouse sector

| Rental level (m²/month) | EUR 3.5 - 4.0  
| **Total warehouse stock** | 1.4 million m²  
| **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 |
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 so that each of the above aspects is dealt with in a separate section (2.3.–2.8.), considering legal implications first, followed by an assessment of related important tax consequences.

The section 2.1. on the legal background (below) will introduce the reader to certain concepts and terms that may not be commonplace in transactions elsewhere in Europe. This should be read as a general introduction to the legal environment in Poland. The chapter also contains section 2.2. on investment vehicles and structures presenting information on the most common structures used in real estate investments in Poland. Taken together, they form the basis for understanding the most relevant legal and tax implications of investing in real estate in Poland.

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

2.1.1. General remarks

In general, Polish real estate law provides quite clear and stable rules which allow potential investors to make well-founded decisions about entering into real estate transactions. Additionally, there are measures and institutions which enable investors to safely conclude transactions adapted to their needs and expectations. In particular, most real property deeds (sale, other transfers, establishing of a mortgage) must be executed before a notary public. A public credibility warranty of the land and mortgage register is an additional instrument which protects the purchaser against third party claims and guarantees the validity of the title acquired (as long as the purchaser acted in good faith).

Below we present some key information on real estate law in Poland which should be the base for other comments in this chapter.

2.1.2. Legal titles to real estate

The basic source of real property law in Poland is the Civil Code of 23 April 1964 (with many amendments since; hereinafter referred to as the Civil Code). Although it does not regulate this branch of law exhaustively, it constitutes a basis for other regulations regarding legal titles to real estate and their limitations or modifications.

The most common legal titles to real estate in Poland are the ownership right, the perpetual usufruct right, and obligation rights, such as lease, tenancy or leasing. Polish law also provides several limited property rights such as easements and usufruct.
Ownership right

Ownership (prawo własności) is the broadest right to real estate in Poland, equivalent to a freehold. As a rule, ownership conveys the right to possess and use real estate for an unlimited period of time (with the exception of ownership of any buildings connected with the perpetual usufruct right; see our comments below) and transfer or encumber the real estate. The ownership right may be limited by statutory law, principles of community life and the socioeconomic purpose of the right. The most common limitations result from construction law and zoning master plans adopted by local authorities (municipalities).

Right of perpetual usufruct

Perpetual usufruct (użytkowanie wieczyste) is a right of use the real estate which may be granted by the State in relation to the State-owned land or by a local authority in relation to the authority-owned land. In either case the respective entity (the State or the local authority) remains the owner of the land.

The perpetual usufruct right is similar to the ownership, however, there are several crucial differences:

- The perpetual usufruct right is created for a defined purpose (developing a project or conducting a specific activity) set out in the contract. If the perpetual usufructuary is in breach of these provisions, this may lead to an increase in the annual fees or even termination of the contract by the common court.
- The perpetual usufruct right is created for a specific term, in principle for a period of 99 years.

However, when the economic purpose of the perpetual usufruct of property does not require letting the land for a longer period, a shorter period of no less than 40 years is allowed. The holder of the right may apply for extending the term of the perpetual usufruct for a further period of 40 to 99 years following the lapse of the initial period. Refusal to prolong the time limit is admissible only on account of important social interest.

Once created, the perpetual usufruct right can be inherited, transferred to third parties or encumbered (i.e. mortgage, easements). The holder of the perpetual usufruct right enjoys the right to use the real property and to draw benefits from it, e.g. rental income.

Currently, the perpetual usufruct right may be created by contract, which generally requires putting the land up for a tender (there are several exceptions provided). The winning bidder signs a notarial deed with the owner of the real estate establishing the right of perpetual usufruct. The right, however, does not come into existence until it is registered in the land and mortgage register. Other issues involving the establishment and transfer of the perpetual usufruct are accordingly governed by the regulations regarding the transfer of ownership of real estate.

The contract under which the land is transferred for perpetual usufruct may
lay down potential limitations on the use and disposal of real property and indicate the manner in which the real estate is to be used.

If the real estate transferred for perpetual usufruct is a piece of developed land, the buildings and other constructions erected thereon are sold to the perpetual usufructuary in addition to the establishment of the perpetual usufruct right. If the buildings are erected after the perpetual usufruct right is established, they also become the perpetual usufructuary’s property. Separate ownership of the buildings due to the perpetual usufructuary is a right strictly connected with the right of perpetual usufruct and, in consequence, the buildings share the legal “lot” of the land. In particular, the ownership of buildings may be transferred only with the right of perpetual usufruct. Once the perpetual usufruct right expires, the holder of the right is entitled to a reimbursement corresponding to the current market value of the buildings and other improvements legally implemented on the land that is the subject of the perpetual usufruct right.

The perpetual usufructuary is obliged to pay to the owner a one-off initial fee which amounts from 15% to 25% of the total market value of the real property and then an annual fee of up to 3% of the total market value of the land. The rate of 3% is the basic rate provided by the law; however, there can be other rates (0.3%, 1%, 2%) applied to the real estate assigned for specific purposes, strictly listed in the legal provisions. The value of the land as established for the purpose of calculating the annual fee is subject to indexation (not more than once for three years). The perpetual usufructuary has the right to question a new valuation before the local appeal committee and, if unsuccessful, before a common court.

Subject to certain conditions, the perpetual usufructuary or his legal successors may demand that the perpetual usufruct right be converted into ownership. The legal provisions do not specify whether the term “legal successor” refers to general succession only, or whether it may be applicable to entities acquiring real property through a sale agreement. The courts more often take the view that the entities acquiring real property through a sale agreement are entitled to demand the conversion into ownership. The basic condition of acquiring the ownership of real estate is the possession of the right of perpetual usufruct as of 13 October 2005. The conversion takes place under an administrative decision of a relevant local authority and is valid as at the date when the decision becomes final. Such a decision also constitutes a basis for making an entry in the land and mortgage register.

The conversion of the perpetual usufruct right into ownership right is subject to a fee which is equal to the difference between the value of ownership and the value of the perpetual usufruct right to the land.
Leases and Tenancies

Polish law distinguishes between two types of leases: lease (najem) and tenancy (dzierżawa). Leases are used mainly for commercial and residential premises. Tenancies are used especially for industrial and agricultural property. Under a lease agreement, the lessor undertakes to hand over the real property for the lessee’s use for a fixed or non-fixed term, and the lessee undertakes to pay the lessor an agreed rent. The tenancy contract, however, provides for the lessee additional right to collect profits from the real estate.

Leasing

By a leasing contract, the financing party, who is an entrepreneur, undertakes to acquire the real estate from a specified transferor on the terms and conditions set forth in that contract and to give it over to the user for use or for use and collection of profits for a specified period. The user, however, undertakes to pay the financing party, by installments, a monetary remuneration equal to at least the remuneration or the price at which the financing party acquired the real estate.

There are two types of leasing that can be executed in Poland:

- operating leasing, in which case the leasehold is an asset of the lessor who makes depreciation write-offs and the lessee has an option to purchase the property at the end of the leasing term;
- financial leasing, in which case the leasehold is an asset of the lessee who makes depreciation write-offs and the transfer of the ownership of a real estate at the end of the leasing term may be stipulated directly in the leasing agreement.

The lessee should choose the type of leasing according to his requirements and needs with respect to tax settlements and the period of using the leasehold.

Easements

Easements (slużebności) over land are limited property rights which may be granted over a piece of real estate (encumbered property) for the benefit of another piece of real estate (master property). Depending on the content of an easement deed, the holder of the master property may be entitled to a limited use of the encumbered property (active easement), or the holder of the encumbered property may be restricted in the exercise of his own rights for the benefit of the master property (passive easement).

Polish law distinguishes between two types of easements:

- ground easements, which are established for the benefit of the owner or perpetual usufructuary of the land and are transferred together with the property (whether that encumbered or the master property);
- personal easements, which are established for the benefit of a natural person and are non-transferrable (nor can the right to exercise them be transferred).

The Civil Code also lists a separate category of easement, i.e. utility easement which
may be established for the benefit of entrepreneurs being utility providers. A utility provider may ask the land owner to establish an easement over his land in order to install (and then operate and maintain) e.g. electricity cables, installations serving to supply and to channel liquids, gas, steam or other facilities. If the real estate owner refuses, the utility provider may demand that an easement be established in return for an appropriate remuneration.

In practice, real estate may be encumbered with more than one easement or other limited property right. In such a case, as a rule, a right that arose later cannot be exercised to the detriment of the earlier right; however, there are also regulations which specify priority in a different manner.

In particular, if one of the rights is entered in the land and mortgage register, it benefits from priority against the right which is not entered in the register, regardless of the dates of their establishment.

It should be noted, however, that easements are not always disclosed in the land and mortgage register.

In consequence, the potential investor should verify whether such rights are not being executed by carrying out an on-site inspection, i.e. during a due diligence review.

Usufruct

Usufruct (użytkowanie) of real estate is a limited property right which allows its holder to use the real estate and collect benefits similar to those to which the ownership holder is entitled. The scope of the usufruct may be limited by specified profits being excluded, or to a designated part of the real estate. Usufruct is created by a contract. Usufruct is non-transferable, strictly connected with the usufructuary, so the right expires on the usufructuary’s death (or liquidation, in the case of legal entities). Moreover, a usufruct expires if not exercised for ten years.

Usufruct is similar to tenancy, yet its legal nature is different.Usufruct, as a limited property right, is effective erga omnes (it is effective in respect of third parties) and tenancy is effective only between the parties to an agreement.

2.1.3. Real property registers

There are two types of land registers in Poland: the land and mortgage register (księga wieczysta), whose main purpose is to register titles and encumbrances over real estate and the land and buildings register (ewidencja gruntów i budynków), the main purpose of which is to describe the physical features and the use of the land and buildings.

Land and Mortgage Register

Land and mortgage registers are kept by district courts and provide information on the legal status of real estate, e.g. the location of parcels of land, the ownership status of land, encumbrances on the land, mortgages.

The following real estate rights are registered in the land and mortgage
register: ownership, perpetual usufruct and limited property rights such as cooperative member’s right to an apartment, cooperative member’s right to commercial premises, right to a single-family house in a residential cooperative, mortgage, easement and usufruct. As a rule, registrations take place at the request of the party concerned.

Land and mortgage registers are publicly available for review by anybody (even those with no legal interest) and may be also reviewed on-line, via IT system.

As far as land and mortgage register files (including maps, deeds, court decisions) are concerned, only parties with a legal interest may inspect them. Legal interest is interpreted quite narrowly and comes down to those parties whose rights are registered in a given register.

Entry of a right in the land and mortgage register is presumed to reflect the actual legal status of the real estate. Should there be any inconsistency between the legal status of real estate, the content of the register prevails in favor of the person who has acquired the right of ownership or another property right by performing an act in law with a person duly registered as the holder of the right and entitled according to the public credibility warranty of the land and mortgage register (rękojmią wiary publicznej ksiąg wieczystych). In consequence, if a purchaser acquires a property in good faith from a non-owner registered as owner, the acquisition is valid and the true owner cannot render the transfer invalid. His only recourse is an indemnity claim against the vendor. In consequence, an excerpt from the land and mortgage register is the key document that should be obtained and analyzed before a decision to acquire real estate is made.

The public credibility warranty does not confer protection on gratuitous dispositions or those made in favor of the acquirer in bad faith. It is also excluded by an entry in the land and mortgage register concerning e.g. filing an application or lodging a complaint against a court decision.

**Land and Buildings Register**

The land and buildings register is kept by starostas of the poviats (or presidents of towns with the rights of a poviat) and is a uniform collection for the whole country of systematized, updated data on land, buildings and premises, their owners and other natural persons and corporate bodies holding the land, buildings and premises.

Information on land, buildings and premises is available to the public and commonly accessible. However, fees are collected for disseminated data sets and distributed extracts from the registers and directories as well as for copies of cadastral maps. Additionally, the party intending to inspect the register should prove his/her legal interest if the demanded extract includes personal data. The public credibility warranty does not apply to the land and buildings register, hence, the register does not provide the person acquiring the right of ownership or another real property right with the protection which is provided in the case of land and mortgage registers held by courts.
2.2. Investment vehicles and structures

2.2.1 General remarks

Further to the Polish Commercial Companies Code of 15 September 2000 (hereinafter referred to as the Commercial Companies Code) the legal entities, referred to therein, can be divided into two groups: partnerships and companies. There are two main differences between them: (i) generally, partners in a partnership take full responsibility for the partnership’s liabilities (subsidiary responsibility) and (ii) partnerships are not legal persons, however, they may acquire rights and incur obligations.

Investing in real property is generally carried through specially created entities – so called special purpose vehicles (SPV). Polish legal regulations do not impose any specific legal form for such an entity. Consequently, an entity organized in any form legally accepted in Poland may serve as an SPV. The SPV may operate both as a partnership and as a company.

Among all the legal forms of organizing the entity provided for in the Commercial Companies Code, we would like to present three that are the most commonly used by the investors: a limited liability company, a limited partnership and a partnership limited by shares.

The choice of the legal form for the SPV will determine the structure under which such an entity will be operating. The foreign investor may either be a direct shareholder in the SPV, remain a parent company for a foreign/Polish company controlling the SPV, or arrange any other structure that would suit its needs from the legal and tax perspective.
There are two ways for an investor to introduce the SPV into its capital structure: the SPV may be bought or established by the foreign investor. There are numerous service firms offering the sale of established companies or partnerships (so-called “shelf companies”), that can be used straight away. However, this is always more expensive than setting up a new entity.

Apart from the legal forms mentioned above, a foreign investor may also operate in Poland and invest in real property:

- directly through its branch;
- by entering into a joint-venture.

For more complex and diversified investments a formula of a closed-end fund (Fundusz Inwestycyjny Zamknięty; FIZ) can be used.

### 2.2.2. Limited liability company

A limited liability company (spółka z ograniczoną odpowiedzialnością) is commonly used as the SPV for real estate investments or development projects.

The features of the limited liability company are set out in the Commercial Companies Code, the most important of them being:

- it may be created by one or more persons for any purpose allowed by law (it may not be formed solely by another single-shareholder limited liability company);
- liability of the shareholders is limited to their contribution to the share capital of the company;
- the share capital of the company shall amount to the minimum of PLN 5,000 (ca. EUR 1,200) and is divided into shares of equal or non-equal nominal value;
- the share capital can be covered by a contribution in-kind;
- limited liability company is a legal person and as such, it is a party to specific rights and obligations;
- it acts through its body, i.e. the management board; the members of the management board, in general, are not liable for the company’s liabilities.

The Commercial Companies Code provides for an institution of a “company in organization”. This means, that a limited liability company set up by signing the articles of association may acquire rights on its own behalf, including the right of ownership of real estate and other rights, incur obligations, sue and be sued even before its registration with the registry court.

It is also possible to register a limited liability company with the registry court via the Internet. The procedure is simplified in comparison to the standard procedure and requires the registration of the company through a dedicated website of the Ministry of Justice (https://ems.ms.gov.pl/). However, during the online registration of the limited liability company it is not possible to make an in-kind contribution, hence, the entire share capital must therefore be paid in cash.
The SPVs may be set up directly by the foreign investor, being the only shareholder (bearing in mind the limitations indicated above). It is obviously possible to introduce several SPVs established (or purchased) by the same shareholder in order to divide the investment risk between them. However, depending on the intentions of the investor and bearing in mind possible tax effectiveness of the scheme, a simple one step structure may be enlarged and involve, for example, setting up a holding company, abroad or in Poland, which holds the shares of the SPVs.

In recent years the number of partnerships used for the purposes of investment structures significantly grew.

### Limited partnership

A limited partnership (spółka komandytowa) is a partnership of which at least one partner is liable to the creditors for the obligations of the partnership without limitation (the general partner-komplementariusz) and the liability of at least one partner (the limited partner-komandytariusz) is limited to the value defined in the partnership agreement.

This feature of the limited partnership results in the specific structure that needs to be implemented. Rights and obligations in the partnership should be split between two entities (limited partner and general partner). It is a common practice that the investor takes the role of the limited partner in order to avoid the full liability, whereas an additional limited liability company is established to...
serve as a general partner in the SPV. As mentioned with respect to the structures involving limited liability companies, also in case of limited partnerships various structures may be involved, depending on the specific needs of the investor. Most commonly however, the limited liability company will possess a minority position in the SPV and shall be a 100% subsidiary of the investor, nevertheless it may take specific functions in the SPV - e.g. management duties.

**Structure with limited partnership**

![Diagram](image)

**Partnership limited by shares**

A partnership limited by shares (spółka komandytowo-akcyjna) is a partnership the purpose of which is to conduct a business enterprise under its own business name, where at least one partner (general partner komplementariusz) shall bear unlimited liability towards the creditors for obligations of the partnership and at least one partner shall be a shareholder (akcjonariusz).

Partnership limited by shares is the only partnership in case of which there are minimum share capital requirements, i.e. the share capital has to amount to at least PLN 50,000 (ca. EUR 12,000).

The specific features of this entity results in two kinds of involvement in the partnership, the general partner acts like a partner in any other partnership - i.e. represents the partnership and takes subsidiary responsibility for the partnership's obligations, while the shareholder acts like a shareholder in a joint-stock company, i.e. his involvement is purely of a financial nature.

The partnership limited by shares is subject to some additional restrictions provided for by the Commercial Companies Code:

- in case of in-kind contributions the auditor's opinion is required,
- profit-sharing occurs in groups (separately shareholders and general partners).

**Tax advantages**

Till 31 December 2013 both limited partnership and partnership limited by shares were considered transparent for the purposes of corporate income tax and therefore commonly used as SPVs in real property investments.

Due to CIT law changes from 1 January 2014 partnership limited by shares is no longer considered tax transparent and became a corporate income taxpayer. Until the end of 2013, taxation of the shareholder in a partnership limited by
shares was deferred until the profits were distributed to him by the partnership. Consequently, if there was no economic profit available for distribution - or no distribution was made - no taxation should occur at the level of the shareholder of a partnership limited by shares. The deferral was not directly indicated in the tax law but was based on the general tax ruling of the Polish Ministry of Finance. Due to transition rules, the use of partnerships limited by shares that can still enjoy the above may be still possible, in case partnerships which financial year extends beyond 2015.

In the case of limited partnership, taxable revenues and costs generated by the partnership are allocated to the partners (both limited and general) and recognized for corporate income tax purposes on an on-going basis at their level.

Partnerships 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:

<table>
<thead>
<tr>
<th>Limited liability company</th>
<th>Limited partnership</th>
</tr>
</thead>
<tbody>
<tr>
<td>possesses legal personality</td>
<td>YES</td>
</tr>
<tr>
<td>can be established by a single shareholder/partner</td>
<td>YES (NO if to be established by a Polish LLC, which has only one shareholder itself)</td>
</tr>
<tr>
<td>can acquire real property</td>
<td>YES</td>
</tr>
<tr>
<td>the shareholders/partners are personally liable for the company’s debt</td>
<td>NO</td>
</tr>
<tr>
<td>minimal share capital</td>
<td>5,000 PLN (ca. EUR 1,200)</td>
</tr>
<tr>
<td>management board</td>
<td>obligatory</td>
</tr>
<tr>
<td>supervisory board</td>
<td>voluntary*</td>
</tr>
<tr>
<td>Limited liability company</td>
<td>Limited partnership</td>
</tr>
<tr>
<td>--------------------------</td>
<td>---------------------</td>
</tr>
<tr>
<td>Taxation of income (from exploitation or sale of assets)</td>
<td><strong>19%</strong> at the company level</td>
</tr>
<tr>
<td>Taxation of the distribution of income to shareholders / partners</td>
<td><strong>19%</strong> under certain conditions there can be relief for shareholders who are legal persons (based in Poland or in the EU/EEA). Reduced rates for foreign shareholders on the basis of double taxation treaties (depending on the treaty)</td>
</tr>
<tr>
<td>Civil law transaction tax on shareholder / partner loans</td>
<td><strong>NO</strong></td>
</tr>
<tr>
<td>Applicability of thin capitalization rules</td>
<td><strong>YES</strong></td>
</tr>
<tr>
<td>Ability to offset profits and losses from various projects (carried out in separate companies/partnerships)</td>
<td><strong>NO</strong> only in the case of establishing a tax capital group</td>
</tr>
<tr>
<td>Taxation in Poland of the sale of shares in the company / partnership</td>
<td><strong>19%</strong> possible relief for foreign shareholders on the basis of double taxation treaties (depending on the treaty)</td>
</tr>
</tbody>
</table>
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.

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.

2.2.4. Joint venture

Polish legal regulations do not provide any definition of a joint venture, nevertheless, it is a useful solution to combine entrepreneurs’ efforts in achieving the common goal.

The term joint venture may be understood as a cooperation of two entities resulting in setting up a new company (the investment on such basis is carried through the given company, as described before) or it may be only a very close cooperation between the two entities, which allocate capital for activities implemented jointly by sharing costs and revenues under a joint venture contract, without creating a separate business entity.

The objectives for the creation of joint ventures are:

- gaining access to new markets,
- synergies,
- risk diversification,
- achieving economies of scale,
- providing access to cheaper sources of supply,
- joint development and sharing of technology,
- overcoming barriers and administrative duties created by the country of one of the partners.

2.2.5 Investment Fund - closed-end fund

The Polish Investment Funds’ activity is comprehensively regulated by the Act of 27 May 2004 on Investment Funds (hereinafter referred to as the Act on Investment Funds). According to that Act, the sole object of the investment fund’s activity is to invest the monies acquired from the participants in shares, securities, money market instruments and other property rights - including real property.

Investment funds differ from regular legal entities such as capital companies, as an investment fund merely forms an asset base consisting of the payments of the participants and the assets acquired for the said payments.

The Act on the Investment Funds differentiates in general between Open-End Investment Fund and Closed-End
Investment Fund (hereinafter referred to as FIZ).

FIZ is a legal person. The primary principle of the FIZ is the fixed number of participation titles (investment certificates) issued in exchange for contributions made by its participants (investment certificate-holder). FIZ does not issue participation titles on every demand of an investor as is the case with the open-end investment funds, but rather in discretionary periods of time. In order to subscribe for investment certificates, the participant has to make a contribution to the FIZ. Generally, the participants may contribute to the FIZ cash, shares or real estate.

The FIZ’s bodies are the Management Company, the Board of Investors (controlling body) and General Investor’s Meeting.

The Management Company (Towarzystwo Funduszy Inwestycyjnych) is a legal entity separate from the Investment Fund. According to the legal provisions only a joint-stock company with its registered office in Poland holding authorization to conduct the activities related to creating investment funds and managing them issued by the Polish Financial Supervision Authority (Komisja Nadzoru Finansowego), may be an investment fund management company. This means that the Management Company carries out its activities on the basis of the permit issued by the Polish Financial Supervision Authority and under its supervision.

A Management Company may be formed by an investor, however, it is common practice that already existing Management Companies are engaged to take this role. In such a case an investor makes an agreement with a Management Company. Consequently, the investor only holds investment certificates in the FIZ and through this structure invests in particular property.

The Management Company fulfils two primary functions: (i) at the beginning - it acts as a founder of the FIZ, (ii) when the FIZ is established and registered - it becomes its governing body (represents FIZ in transactions with third parties).

In accordance with the Act on Investment Funds, the Management Company shall be liable to the participants in the FIZ for all the damage caused by the failure to perform or improper performance of its duties as regards the management of the FIZ and its representation.

The above shows that the structure needed to implement FIZ is complex and requires:

a) engaging a Management Company,
b) establishing an FIZ,
c) establishing the operating companies, which may acquire the real property.

Nevertheless, establishing an FIZ structure has important advantages. First of all, it allows for additional financing for the investments to be raised by selling investment certificates. This may be very useful in entering in larger, long-term real property 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 the applicability of the tax exemption in each case.

In view of the changes introduced in the CIT law as of 1 January 2014, according to which partnerships limited by shares became taxpayers (similar to limited liability companies), alternative structures using a Polish or foreign investment fund can be used. The setup of the investment structure should be planned in advance, due to a time-consuming implementation process.

**Example of a FIZ structure**

2.2.6 Public-private partnership

**General remarks**

Public-private partnership (hereinafter referred to as PPP) is one of the rising forms of cooperation between public authorities and the private sector. It allows for an increase in the efficiency of public services through the use of private sector experience and for the sharing of risk between public and private entities.

PPP enables a mutual advantage for the public and private sector – for public entities it guarantees an additional source of capital and as a consequence provides the public sector - with funds to allocate for other purposes. On the other hand, the public sector may provide to private investors the long-term certainty of cash flows from public sources.

In Polish law the legal framework for PPP is established by two acts that regulate the cooperation between public entities and private partners:

- the Act of 19 December 2008 on Public-Private Partnership, hereinafter referred to as the Act on Public-Private Partnership,
- the Act of 9 January 2009 on Concession for Works and Services, hereinafter referred to as the Act on Concessions.

The main similarities between the Act on Public-Private Partnership and the Act on Concessions are as follows:
cooperation between a public and private partner,
- risk division between a public and private partner,
- private partners receive payments for the service rendered,
- constitute a special form of tender agreements.

**Selection of the private partner**

The Act on Public-Private Partnership basically distinguishes two ways of selecting the private partner. The ways of selection depend on the type of the private partner's remuneration and are as follows:

- If the remuneration of the private partner is represented by the right to collect benefits from the subject of the public-private partnership, or mainly such a right together with payment of an amount of money the selection of the private partner shall be done applying the Act on Concessions subject to provisions of the Act on Public-Private Partnership.

- In other cases, the selection of the private partner shall be done applying the provisions of the Act of January 29, 2004 on Public Procurement Law (hereinafter referred to as Public Procurement Law) subject to provisions of the Act on Public-Private Partnership.

**Implementation of PPP**

Pursuant to the Act on Public-Private Partnership public and private entities conclude an agreement under which the private partner commits itself to implement the project at an agreed remuneration and to cover in whole or in part the expenditures for project implementation, or cover them through a third party, while the public entity commits itself to collaborate for the purpose of achievement of the project goal, in particular by making its own contribution. The PPP contract can also provide that for the purpose of its performance, the public entity and the private partner shall establish a company, a limited partnership or a partnership limited by shares.

**Financial restrictions**

The total amount up to which bodies of government administration can contract financial liabilities on the basis of contracts of PPP in a given year is specified in the Budget Act. In 2011, 2012 as well as in 2013 it was PLN one thousand million.
However, as a rule, the financing of a project from the State budget to the amount exceeding PLN 100 million requires a consent issued by the minister responsible for public finance (excluding the funds allocated for financing of operational programs, that are specified in the Act of 6 December 2006 on Principles of Development Policy. When issuing the consent the minister responsible for public finance shall consider the influence of the planned budget expenditures on the safety of public finance.

The concession contract – legal basics

The Act on Concessions specifies the rules and procedures for contracting concessions for works or services and the legal protection measures.

The duration of a concession contract should take into account the recovery of the concessionaire’s expenditure incurred with reference to the performance of the concession and shall be no longer than:

- in case of concession for works - 30 years;
- in case of concession for services - 15 years.

Where the expected time limit of recovery of the concessionaire’s expenditure incurred with reference to performance of the concession is longer than the period specified above, the contract may be signed for a longer term.

The concessionaire under the concession signed with the concession-granting authority is obliged to perform the subject of concession for remuneration, which constitutes in case of:

- the concession for works - exclusively the right to use the work or such right with the payment by concession-granting authority;
- the concession for services - exclusively the right to use the service or such right with the payment by concession-granting authority.
2.3. Real estate financing

2.3.1. Modes of financing the SPVs / investments

The most important thing in starting investments, is to provide financing for the SPVs, so they can operate and acquire real property.

There are several methods of financing the company, some funds can be received from outside, but some may come from the capital group - e.g. from the parent company. In many cases both solutions are possible.

**Loan and credit agreement**

By loan agreement a lender undertakes to transfer the ownership of a certain amount of money or goods to a borrower, while a borrower undertakes to return the same amount of money or the same amount of goods of the same kind and the same quality. Loans can be granted by any entity / person and may be relatively freely regulated by the parties.

A credit agreement is a specific kind of external financing, which is regulated by the Banking Law of 29 August 1997 and can be granted only by banks. By a credit agreement a bank agrees to provide a specific amount of money for a specific purpose and time, and the borrower agrees to use the credit for its intended purpose, and pay back the amount of credit along with due reward in the form of bank interest.

On the financial market there is a wide choice of bank credits and their price depends on various factors as: duration, securities available, financial condition of the borrower. Additionally, banks may
charge the borrower a preparation fee for all work connected with the preparation of the credit.

Banks also generally require securities for the credits. Among others, the most popular are:

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

A mortgage is the common form of security required by Polish banks — especially required in real estate financing transactions.

A mortgage shall be defined as a right, under which the lender (creditor) may satisfy his claims from the property, regardless who is the current owner of the property, and with priority over other personal creditors of the borrower, whose credits are not secured with mortgage.

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

A mortgage is a very secure solution for the bank, as in the case of the debtor not being able to pay off his debt, the real property may be sold in a public auction and thus, the bank may retrieve the whole amount of debt.

**Shareholder’s loan**

A loan from shareholders has two important advantages over the bank loan. First, it is in general a cheaper solution and what is more, it does not bare the risk of enforcement in case of difficult financial situation of the borrower.

It is important to mention the specific rules resulting from art. 14 § 3 of the Commercial Companies Code, which provides that shareholder’s claim resulting from a loan shall be considered to be his contribution to the company in case of declaration of bankruptcy within two years from the date of the loan agreement. However, the above does not constitute an increase in the share capital of the company, and the contribution is treated as made on the supplementary capital. This provision is intended to protect creditors of the bankrupt company.

**Bonds**

Bonds can be issued by a joint-stock company, a limited liability company and a partnership limited by shares. Bonds can be defined as securities, which oblige the issuer (the company) to give certain benefits in cash or in kind to the bondholder (the buyer of the bonds).

Companies can issue registered or bearer bonds.

The advantage of this form of financing is the ability to fairly freely determine
the benefits that are associated with bonds. The construction of the security does not have to be limited to a simple financial benefit in the form of repayment of the bonds plus interest representing an income of the bondholder. While issuing bonds, the company is free to formulate the gratification to be provided to bondholders, such as the possibility of participating in profits of the company, or the conversion of bonds into shares.

The bonds may be distributed on an open market, in search for an outside financing, or serve as a mode to transfer funds from another related company. It should be noted that there are several companies in the real estate sector listed on the Polish bonds’ open market.

In the case of SPVs which aim to obtain financing from the shareholders, the gratification (a mutual benefit) to the parent company as a bondholder will be of secondary importance. A practical solution is that if the SPV generate future earnings from real property, bonds could entitle bondholders to participate in the profit. Due to the high degree of freedom in the framework of this instrument, it is very recommended as an optimal way to bring the funds downwards.

We would like to note, however, that the issuing of bonds creates additional obligations for the bond issuer, related to providing data to assess the financial condition of that entity. Additionally, if the issuer operates for more than a year, it is required to provide financial statements prepared as at the balance sheet date, no earlier than 15 months before the date of the publication of the terms of issuing the bonds, along with the auditor’s opinion.

**Promissory notes**

In order to obtain financing SPVs may issue promissory notes.

A promissory note may include a deferred payment date. It should have a clearly defined due date, in the form of a calendar date. There are exemptions from this rule - e.g. an ‘a vista’ promissory note - which provides that the payment is made on demand from the payee or within a certain period after the demand. Additionally, an ‘in blanco’ promissory note allows a payee to fill in (at its own discretion) - the conditions of such promissory note (e.g. date of payment) within the scope foreseen by a mutual agreement.

The obligation from the promissory note does not have to be accompanied by any other legal relationship that it secures. It means that the holder has an unquestionable claim from promissory note, even if, for example, promissory note liability was not based on any other particular obligations - such as loans.

Similarly as in the case of the loan agreement, the issuer of a promissory note becomes a debtor. With the use of a promissory note, SPVs can easily obtain funds from the parent company in a less formal, quicker way and easily settle the debt in any suitable timeframes.
Increase of share capital

Raising capital is a common way of financing companies. It can be carried by increasing the nominal value of the shares existing or creating new ones; both ways lead to an increase of the share capital.

This process is associated with either changes in articles of association (a formal mode that requires filing the changes in the articles of association with the National Court Register) or an increase based on the current provisions of the articles of association (informal mode). The aim is to change the capital structure of the company by defining the share capital at a higher than current level. To cover the increase of the share capital, the funds may be paid in cash or in-kind contributions can be made.

It should be noted that the share capital increase needs some additional expenses. These include the fee for changing an entry in the National Court Register (ca. EUR 60), a fee for the notification in the Court and Economic Monitor (ca. EUR 25), notary fee for the minutes documenting the capital increase and for the preparation of a deed containing a statement of acquisition of shares in the full amount (notary fees depend on the value of increase and are limited by legal provisions).

The capital increase is a more formal process in comparison to the additional contributions (referred to below) and loans, but the advantage of this form of financing is the ability to contribute in various forms, such as cash or in-kind.

A significant drawback of this method of financing SPVs is relatively difficult process of withdrawing the invested capital. This is carried through the reduction of share capital (Articles 263 - 265 of the Commercial Companies Code), which involves again additional costs (notification, registration) and is time-consuming (e.g. includes three months for objection to the reduction that can be brought by creditors).

Additional contributions

This method of financing is provided by the Commercial Companies Code, but it is applicable only to the limited liability company. According to the provisions, the articles of association of the company may require the payments (additional contributions) from the shareholders in a specific amount paid by the shareholders in proportion to their shares. In fact, it is worth noting that partnership agreements can also oblige the partners to additional payments - such a solution is possible based on the freedom of contract principle.

Payments of additional contributions in a limited liability company do not affect the value of shares in the share capital of the company, and therefore the share capital of the company remains unchanged after the additional contributions. The payments increase the company's own funds, which are thus quite freely allocated for the specific need, and this is certainly beneficial for the SPV. The amount and timing of payments is decided by the shareholders' meeting.

As mentioned above, the general obligation to additional contributions has to be
stipulated in the articles of association (if such articles do not contain such provisions, it would be necessary to amend them, as otherwise additional contributions are not possible). However, it is not enough to create an actual obligation for the shareholders to make contributions. A resolution of the shareholder’s meeting taken by an absolute majority of votes is required. After this step is complete, the actual obligation arises.

Pursuant to the provisions of the Commercial Companies Code, the additional contributions may be refunded, provided that funds gathered from those contributions are no longer required to cover the losses reported in the financial statements, and not earlier than one month after notice in writing, announcing the intended refund. Rules on the refund may be differently regulated by the articles of association, which means that this instrument is relatively flexible. Shareholders may in fact decide, contrary to the provisions of the Commercial Companies Code, that additional contribution may be refunded, even if the company’s financial statements show a loss, in less than a month from the date of publication, or even without the need to announce the refund.

Additional contributions are always made in cash and cannot be fulfilled by providing the company with non-cash benefits. Payments can be used for different purposes, and the applicable regulations do not contain restrictions in this regard.

2.3.2. 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 reorganization transactions. Contributions to a reserve capital (share premium) should not be subject to civil law transaction tax.

Generally, for Polish corporate income tax purposes, a contribution in kind (except for the contribution in kind of a business or an organized part thereof) 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 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 hold 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. This condition can be also met prospectively, i.e. after the actual dividend payment. If the condition to hold the amount of shares for an uninterrupted period of two years is not satisfied, withholding tax (as a rule at 19%) together with the penalty interest for late payment will be due.
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 an incorrect tax rate. A certificate issued by a foreign local tax office confirming the tax residence of the foreign shareholder receiving dividend payments from Poland must be obtained by the Polish company in order to allow application of the lower withholding tax rate or exemption. An additional requirement is that the Polish entity paying dividends should also hold a written confirmation from 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 hold (on or after the day when the dividend is received) 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. 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.

Other than voluntary redemption of shares (compulsory redemption of shares) as well as liquidation is taxed in the same way as dividends and is 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.

As regards liquidation proceeds, according to the current approach of the Polish tax authorities, upon liquidation, the entity that ceases to exist is taxed as if it disposed assets which are transferred to the shareholder. This approach is not shared by the courts though.

The similar approach tend to be applied to in kind remuneration for redeemed shares or dividends in kind.

However, as of 1 January 2015 the Polish CIT provisions explicitly state that in case of in kind remuneration for settling the liability (e.g. upon shares redemption or in kind dividend payment) the value of liability settled in such a way constitutes a taxable revenue of the paying entity. This applies respectively also to look through entities.
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 recognized as an activity subject to Polish or foreign VAT (e.g. bank loans);
- financing granted as a part of business activity is recognized 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 the EU Directive 2003/49/EC on the 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). As a result of that, a withholding tax exemption on interest 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) is available from July 2013. The 2-year holding period condition can be also met prospectively, i.e. after the actual interest payment. If the condition to hold shares for an uninterrupted period of 2 years is not satisfied, outstanding withholding tax (as a rule 20%) together with the penalty interest for late payment will be due. Penalty interest is charged from the day following that the day on which the above period expires.
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 was 5%.

In order to benefit from that favorable treatment the payer should hold recipient’s certificate of tax residence. An additional requirement is that the payer should also hold the recipient’s confirmation that the recipient does not benefit from 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 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 have been amended as of 1 January 2015.

According to the transitional provisions new rules apply to interest paid on loans with respect to which funds were made available to the borrower after 1 January 2015. Therefore, as regards interest paid on loans with respect to which funds were made available to the borrower before that date - old rules apply.

Old rules

The Polish old 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 to the value of the share capital (see below for details) 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 covers 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;
  - 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 old 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:
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 3

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

Legend:
- = minimal 25% voting right relationship
- = loans subject to thin-cap
- = loans qualifying for calculation of debt limit

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**New rules**

The new rules restrict deductibility of interest on a broader range of loans than the rules in force until the end of 2014. As of 1 January 2015, generally interest on all intra-group loans (also those from indirectly related entities) may be subject to deductibility restriction.

Under the new thin capitalization rules, if the value of debt owed to specified related parties exceeds the net equity of the borrower (1:1 debt to equity ratio), part (calculated based on a proportion) of interest paid on a loan from a related party is not deductible for tax purposes. For the purposes of these rules, equity is determined on the last day of the month preceding the month of interest payment without taking into account revaluation reserve and subordinated loans. The value of equity is further decreased by the value of the share capital that was not actually transferred to this capital or was covered with shareholder’s loans’ receivables and intangibles that are not subject to amortization.

The definition of a loan covers any form of debt financing, including the issuance of bonds, credits and bank and nonbank deposits. The definition does not cover derivatives.

The thin-capitalization rules apply to interest on loans granted by Polish and foreign qualified entities. They cover the following loans:

- loans granted jointly by entities that jointly directly or indirectly hold at least 25% of the voting rights in the borrower,
- loans granted by one company to another company if the same entity holds directly or indirectly at least 25% of the voting rights in both the lender and the borrower.

For general partners in a limited joint-stock partnership, the conditions concerning the minimum share (voting rights) are fulfilled, regardless of the general partner’s share.

As of 1 January 2015 the taxpayers have also a right to opt for a new alternative thin-capitalization calculation method. If chosen by the taxpayer, the abovementioned method applies to interest paid to both related and unrelated parties. The recognition of such interest for tax is limited to the amount of the National Bank of Poland’s reference rate plus 1.25 percentage point and the tax value of assets within the meaning of Accounting Act (excluding intangible assets).

The value of interest recognized by the entity cannot be higher than the value corresponding to 50% of the profit from operating activities (this condition does not concern, generally speaking, banks and financial institutions).

Interest not deducted in a given tax year can be deducted in the following consecutive 5 tax years. If a taxpayer decides to use this method it should be used for at least 3 tax years.
To be entitled to apply the above rules, taxpayers are generally obliged to file relevant notification to the tax authorities not later than till the end of first month of their new tax year.

**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 recognized 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 – asset deal and share deal

2.4.1. General remarks

As many other jurisdictions, Polish law provides different methods of acquiring real estate by an investor, among which an asset deal and a share deal are the two most commonly used.

Both methods bear various legal and tax consequences which have to be considered in any given case and therefore there is no generally accepted rule when a share deal or an asset deal shall be applicable. The interests of the seller and the buyer, the particulars of the case and the power of each party to negotiate have to be considered while choosing one of these two forms.

In practice, if a share transaction is properly structured, this can be the most tax efficient disposal method to use. In a well-organized 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 recognized for accounting purposes. Unfortunately, such goodwill cannot be amortized 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

Definition of a share deal and asset deal

Despite the fact that the share deal and asset deal are equally popular, their object and manner of conducting are different. The key differences between these two methods of acquisition concern the extension and nature of purchased items and are presented below.

- A share deal is defined as a transaction involving acquisition of shares in a company as a result of which the buyer purchases the whole or a part of the shares in the share capital of the company (i.e. the target company). Thus, in such transaction, the purchaser becomes the owner of the shares and does not obtain any direct rights to the assets (i.e. for instance real estate) which remain the property of the target company. Since in this transaction an investor purchases shares in the target company, it also acquires the risk related to the liabilities of this company (e.g. undisclosed liabilities, tax liabilities). Thus, an extensive due diligence of the target company preceding the purchase of shares is required and recommendable.

- An asset deal is where the purchaser acquires all or some of the assets of the company. Unlike a share deal, in an asset deal it is possible to divide out certain elements, such as real estate and acquire only those parts. Therefore, in an asset deal, an investor purchases the property itself and at the end owns the assets of the target company only. Since in case of this transaction it is not necessary to examine the title to the company's shares or the company's corporate structure, the due diligence preceding an asset deal is generally shorter and less extensive in comparison to the due diligence preceding a share deal. However, the assets being acquired (such as real estate) may require a more detailed analysis.

One of the most significant differences between these two types of transactions is the guarantee of the validity of the purchased title. Pursuant to the Polish law, in the asset deal the investor’s acquisition of the land from a title-holder who is registered in the Land and Mortgage Register guarantees the validity of the purchased title. This applies only when the purchaser acted in good faith (i.e. one does not act in good faith if knew, or should have known, that the legal status of the property is different than the one resulting from
the register). Such a guarantee does not apply to the purchase under a share deal, in which the validity of the company's title to the property is supported by the seller's representations and warranties that are included in the share purchase agreement.

**Representations and warranties**

In order to secure the purchaser’s interest extensive representations, warranties and related indemnities should be included in the share purchase agreement. This is usually one of the most important parts of the agreement subject to extensive negotiations. The scope of warranties and representations as well as detailed legal consequences of their breach have to be regulated in the sale agreement in details as Polish law does not provide for a specific legal regulation of this issue.

Please note that representations, warranties and accompanying indemnities included in the asset sale agreement are usually less extensive than in a share purchase agreement.  

- In an asset deal, the seller's representations and warranties concern, in particular, the validity of the seller's title to the real estate, the information regarding encumbrances (if any), the statement confirming that the development has been carried out in accordance with the binding provisions of law and technical plans and that relevant permits are valid.
- The seller's representations and warranties in a share deal usually include the representations and warranties typical for an asset deal regarding real estate, but also extensive representations and warranties relating to all aspects of the company’s activity: in particular tax, employment, accounting, corporate and contractual matters.

It is recommended that the sale agreement provides for specific instruments supporting the enforceability of the indemnities securing the representations and warranties. In market practice, part of the purchase price is retained in an escrow account or a bank guarantee is obtained from the seller.

**Types of agreements**

There is a number of documents related to both transactions. Usually, in order to clearly state the intentions, goals to achieve during negotiations and the key principles of the transaction, the parties sign a letter of intent prior to signing the real estate purchase agreement. Such letter is a good solution for parties who intend to conduct multi-stage negotiations and to those who would like to agree on minor details of the transaction. In such a case, parties may determine the time frame of the negotiations and the moment of their completion, as well as all issues that have to be discussed.

Pursuant to the Polish law, the legal title to the purchased property or shares of a company holding the real estate is transferred on the basis of an agreement executed in the relevant form.
In case when circumstances surrounding the transaction are straightforward, such agreement may be executed immediately, without undertaking any additional actions. However, in some cases purchase of a real estate or shares may be effected by executing two separate agreements, i.e. a preliminary agreement followed by a final agreement. The transaction structured in two separate stages is especially relevant when there is a need to obtain consents for the transaction or to fulfill certain conditions. The Parties usually conclude such an agreement once a letter of intent has been drawn up and before the final purchase agreement has been executed. In order to be valid, the preliminary agreement must include the essential content of the final agreement (i.e. the subject of the sale and the purchase price). In practice, the preliminary agreement regulates all issues related to the real property or shares.

Please note that, in general, pursuant to the Polish law, each transfer of property is registered, as the mortgage register system in Poland aims to have all properties registered. However, the function of such obligation is merely informative and does not determine the transfer of the ownership rights to the purchased property. Nevertheless, certain property rights, such as the perpetual usufruct right can only be transferred if there is an entry in the Land and Mortgage Register made. Thus, the agreement is not sufficient to transfer the perpetual usufruct right and the date of the above entry determines the date of the transfer.

The transfer of the real estate must be unconditional which means that before it takes place, all conditions foreseen by a preliminary agreement need to be fulfilled or the obligation to satisfy these conditions needs to be disclaimed. In that case, the execution of an unconditional agreement completes the transaction.

**Transfer of the property-related rights**

In many transactions, it is necessary to obtain various types of consents or permits regarding the transfer of the rights related to the property, the lack of which may affect the legal effect of the entire transaction.

In the share deal the purchaser does not obtain any direct rights to the assets as these remain the property of the target company. Consequently, the property-related rights and obligations (such as leases, property management agreements, warranty claims under construction contracts and contracts of insurance, permits) remain with the corporate entity holding the real estate and no formal assignment is required.

In the asset deal, the property-related rights and obligations are not automatically transferred as a result of the sale agreement. In case of contracts as for the formal assignment it is, in general, necessary to obtain the consent of the other party of each contract. In case of licenses, decisions etc. it should be analyzed case by case what actions have to be undertaken in order to transfer them to the purchaser. This
means that the ability to assign the property-related rights or assuming the obligations is examined individually, in light of specific regulations or contractual provisions, which may prevent or restrict transferability.

Therefore, a share deal is a type of transaction usually considered by investors when the target company conducts regulated activity as all permits required for its operation stay in the company.

**Formalities**

- **Purchase Agreement content**
  
  Pursuant to the Polish law, the asset purchase agreement and the share purchase agreement should describe at least such elements as the object of the sale and the price. In practice, the agreements are complex and provide for the following main information:

  a) the detailed description of the property or the shares that are subject of the transaction (the sale object);

  b) the price and mechanism of payment (including down payment if any, as well as the price adjustment mechanism);

  c) security instruments (to be determined by the parties, e.g. a mortgage over the property, a registered pledge over the shares, the bank guarantee);

  d) representations, warranties and indemnities;

  e) other matters such as in case of an asset deal the transfer of rights and obligations related to the real estate, the method of resolving a dispute etc.

- **Other requirements**
  
  The requirements regarding form, language and governing law of the agreement depend on whether we deal with an asset or a share deal transaction.

  The form of a notarial deed is required for the execution of a real estate purchase agreement, while such requirement is not necessary for the execution of the share purchase agreement. The share purchase agreement requires the notarial certification of the signatures of the parties.

  Considering the above, since the real estate purchase agreement must be executed in a form of a notarial deed, it must be also concluded in Polish. By contrast, in a share deal a purchase agreement does not require the form of a notarial deed but just notarial certification of signatures and, therefore, it can be executed in a foreign language. However, the Polish commercial registry court that will register the transfer of shares may request a sworn translation of such agreement.

  The real estate purchase agreement can be governed by Polish law only. Such requirement does not apply to the share purchase agreement which can be governed by a foreign
law (provided that conclusion of the agreement is connected with the law of at least two different countries).

- **Costs**

Property purchase agreement requires the notarial deed form, which is subject to a notarial fee, depending on the value of the transaction, but not exceeding PLN 10,000 for each agreement. The fee for the certification of signatures is much lower and does not exceed the amount of PLN 300 for certification of each signature.

**Merger control**

Due diligence review preceding any asset or share deal should answer the question whether the legislation governing merger control will be applicable, in particular, whether a notification of the transaction to the Office of Competition and Consumer Protection is required. Should such notification be required, the closing of the transaction must be suspended until the permit of the Office of Competition and Consumer Protection is issued.

A notification on the planned transaction to the Office of Competition and Consumer Protection is required if any of the following conditions is met:

- the combined turnover of undertakings participating in the concentration in the territory of Poland in the financial year preceding the year of the notification exceeds the equivalent of EUR 50 million.

However, the Polish antitrust law provides for certain exceptions from the obligation of notification even if the above conditions are met, in particular, when the turnover of the undertaking over which the control is to be taken did not exceed in the territory of Poland in any of the two financial years preceding the notification, the equivalent of EUR 10 million; the concentration arises as an effect of insolvency proceedings, excluding the cases where the control is to be taken over by a competitor or a participant of the capital group to which the competitors of the to-be-taken undertaking belong; the concentration applies to undertakings participating in the same capital group.

**The pre-emption rights**

It may happen that the public authorities have a statutory preemptive right to real estate which is about to be sold. The right of pre-emption is a right to acquire the property before it can be purchased by any other person or entity. Where the real estate is subject to a right of pre-emption, it may only be sold to a third party under the condition that the beneficiary of that right does not exercise it. If such a property is sold without observing this right, the sale is considered to be null and void.
The notary executing the conditional agreement will send a copy of it to the local authority, which may then exercise its preemptive right within one month of receiving the conditional agreement. If the public authority does not exercise its preemptive right within that period, the parties can conclude the final agreement, which effects the unconditional transfer of the title to the real estate.

**Acquisition of real estate by foreigners**

Foreigners from the European Economic Area or Switzerland may quite freely acquire real estate in Poland. They are required to obtain a special permit of the Minister of Internal Affairs only if they wish to acquire agricultural and forest land during the period of 12 years from Poland’s accession to the European Union (i.e. up to 1 May 2016). In consequence, obtaining a permit is not necessary in the case of acquiring other real estate in Poland and acquiring or taking up shares in companies that are owners or perpetual usufructuaries of real estate located in Poland even if the real estate is agricultural or forestry land.

As far as other foreigners are concerned, in general the acquisition of the right of ownership to real estate or the right of perpetual usufruct on the basis of any legal event by such entities requires a permit of the Minister of Internal Affairs. A permit is issued upon the written request provided that:

- a foreigner’s acquisition of real estate does not pose a threat to the State’s defense, national security, public order and is not contrary to the social policy and public health considerations;
- the foreigner proves that there are circumstances confirming his bonds with Poland (i.e. for example the buyer has Polish origins or is conducting business or agricultural activities in the territory of Poland under the Polish law).

The Minister’s decision concerning real estate acquisition should be issued within one month (two months in particularly difficult cases). The permit is valid for two years from the day of issuance.

The acquisition of real estate without a permit is invalid. A foreigner intending to acquire real estate in Poland may apply for a promise of the permit. The promise of the permit is valid for one year. During this period a permit cannot be refused unless the actual circumstances pertinent to the decision have changed.

**Acquisition of real estate from public entities**

In Poland, real estate is often acquired from the State or local authorities. Such type of acquisition is considered to be safe and an attractive alternative to acquisition of real estate from private owners. Nevertheless, in practice, acquisition of real estate from public entities is subject to additional specific requirements such as an obligation to dispose the land via public tenders.

An investor interested in acquiring real estate from the State or local authorities
should ask the authorities for information on the contemplated property to be acquired. Unfortunately, it is not possible to purchase such real estate on the spot, as there is a special procedure of selling real estate held in public entities’ possession. With only a few exceptions provided by the law (e.g. real estate being sold to its perpetual usufructuary), real estate held by the State or local authorities may be disposed by way of public tender, after a lengthy procedure is completed.

2.4.3. Tax implications

As mentioned above, real estate can be sold either through a direct sale of the property (an asset deal) or indirectly through a 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 recognized 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 any building separately.

Starting 1 January 2013 tax deductible costs have to be adjusted if the related liability is not settled within the specified deadlines. Effectively the cost recognition is deferred until the settlement date. This rule also limits tax deductibility of depreciation write offs.

**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 or prior to it; 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 joint 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 a perpetual usufruct (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 / RPU to undeveloped land qualified as land for development purposes is subject to 23% VAT (supply of agricultural land is as a rule 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 a reduced 8% VAT, except for part of residential buildings whose usable floor space exceeds 300 m² and apartments whose usable floor space exceeds 150 m². In such a case only the part of residential building and/or apartment which fits within the above limits benefits from the 8% VAT rate, whereas the part exceeding the thresholds is subject to a standard 23% VAT rate. Depending on the legal case underlying the transaction, sale of a parking space sold jointly with the apartment but constituting a separate legal property, can be subject to a standard 23% VAT.

Starting 1 January 2014, as a rule, VAT tax point arises in the month of delivery of goods or rendering the services to the purchaser. The invoice should be issued by the seller no later than until the 15th day of the month following the month in which the goods were delivered or the services were rendered.

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 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, including any goodwill that would crystallize on such transfer). Civil law transaction tax constitutes an additional cost of the transaction and is non-recoverable.

**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 VAT 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 VAT with taxed activities or exempt activities directly.

Starting 1 January 2013 the recovered input VAT has to be adjusted if the liability resulting from the invoice documenting the expense incurred is not settled within the specified deadlines (as a rule 150 days). Additional sanctions may apply if no adjustment is made (i.e. additional tax liability up to 30% of tax resulting from the not settled invoices, which has not been accordingly adjusted).

**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.

Significant part of Polish tax treaties (e.g. with Spain, France, Denmark, Sweden, Germany and - following recent changes of Polish tax treaties - also Luxembourg that used to be a preferred jurisdiction for holding structures) 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 recognized as tax deductible costs upon the sale of shares.

Other costs indirectly connected with acquisition of shares such as financing costs may be recognized 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.

Additionally, bearing in mind the general anti avoidance regulation that is considered to be introduced to the Polish tax regulations and introduced as of 1 January 2015 CFC (“Controlled Foreign Company”) rules, the cross border investments should be each time carefully examined and properly structured also from the business perspective to ensure their effectiveness from the tax point of view.

**CFC Rules**

The new CIT regulations regarding CFC defines CFC as:

1. a foreign company seated in a tax heaven (as officially blacklisted by the Polish Ministry of Finance) or
2. a foreign company having its seat or place of management in the country other than mentioned in point 1), with which:

   a) Poland has not concluded an international agreement, in particular double tax treaty, or
   b) EU has not concluded an international agreement

   - being a basis for requesting tax information from tax authorities of that country, or
3. A foreign company which jointly fulfills the following conditions:

a) The Polish taxpayer has a direct or indirect shareholding (for an uninterrupted period of at least 30 days) of at least 25% shares or 25% voting rights or a 25% stake in profits of the CFC;

b) At least 50% of annual revenues of the CFC consist of a passive income, i.e.:
   - dividends and other income from sharing profits of legal persons
   - disposal of shares, receivables
   - interest or benefits from all types of loans, securities or guarantees
   - copyrights or intellectual property rights – including disposal of those rights
   - disposal or exercise of rights from derivatives;

c) At least one of the sources of passive income (listed in point b) is not subject to tax, is tax exempt or is subject to tax at a lower rate by at least 25% than the Polish statutory CIT rate (now 19%) in the CFCs country of residence (unless the tax exemption results from of the Parent Subsidiary Directive).

CFC provisions should not apply in the case where:

- The CFC, which is subject to taxation on its total income in one of the EU / EEA Member States, carries out actual business operations in this state, or
- The CFC revenues in a tax year are below EUR 250 000; or
- The CFC carries out actual business operations outside of the EU or EEA Member States in which it is subject to tax on its total income and its net income does not exceed 10% of revenues earned from the actual business operations in this state - subject to the condition that there is a legal basis resulting from the agreement between Poland or EU and a respective state, based on which the Polish tax authorities may request information from the tax authorities of that particular state.

The Polish companies are obliged to hold registers of the CFC companies

**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). Careful tax analysis is always required before carrying out such transaction.
2.5. Development and construction

2.5.1 Legal aspects

2.5.1.1 Land development issues

Land development issues are important for real estate investors, as they determine the possible method of investing in a given area. Regulations on land development may influence the shape of the planned building, but sometimes they also prevent the investor from the investment.

Legal background

Land development issues represent one of the main difficulties in the real estate investment process in Poland. As a result of the introduction of the Zoning Act of 27 March 2003 (hereinafter referred to as the Zoning Act), all zoning master plans adopted before 1 January 1995 expired as of 1 January 2004. For this reason, as well as due to the complex procedure for adopting a zoning master plan, currently only a part of the territory of Poland is covered with zoning master plans, mostly within the boundaries of bigger cities.

The Zoning Act sets out the principles for the land development process. In particular, it grants authorization to the relevant local authorities to develop and manage spatial policy. The Zoning Act also sets forth the procedure under which zoning acts are to be adopted by these authorities. The two main zoning acts determining land development within a given municipality (commune) are the zoning study and the zoning master plan. However, from investors’ perspective, the zoning master plan
is of higher importance, as it determines their rights and obligations, while the zoning study binds the local authorities only. In the case where no zoning master plan has been adopted for a given area, the investor may apply for a decision on land development and management conditions (hereinafter referred to as the zoning decision). Where a building permit is required for an investment, either a zoning master plan or a zoning decision are required to start the development of the real property, since, as a rule, no building permit may be issued without them.

Therefore, before buying the real property, it is crucial for investors to verify:

- whether the real property in question is covered by a zoning master plan (or whether such a plan will be adopted soon);
- in the event there is no zoning master plan, whether a zoning decision has been issued for the real property in question; and
- whether the provisions of the zoning master plan or zoning decision allow for the implementation of their investment plans.

**Zoning study**

A zoning study is an internal document issued by each municipality (commune), which covers the whole territory of the relevant commune. A zoning study provides the background/guidelines for drafting a zoning master plan. As an internal document, a zoning study does not bind investors but only the local authorities which design and adopt zoning master plans. Zoning master plans may not be contrary to the assumptions of a zoning study. Therefore, zoning studies may be a good source of information for the investor on the future directions of a given area’s development.

**Zoning master plan**

The zoning master plan is adopted by the commune council and is binding for third parties (investors) as an act of local law. Each zoning master plan determines the manner of development of the territory covered by that plan. In particular, it determines the designation of plots (land use – agricultural, forest, building purposes, etc.), development conditions and types of facilities which can be located on the plots. The procedure for adopting a zoning master plan is rather complex and time consuming as the draft zoning master plan is subject to “public consultation” with the parties concerned as well as opinions issued by the relevant administrative bodies.

The provisions of the zoning master plan are crucial for investors, as the planned development of the plots covered by such a plan must comply with its provisions, in particular, regarding the distance of a building from the plot’s border or the height of a building. Sometimes the provisions of a zoning master plan may render the development of the given plot impossible. Moreover, although still disputable in the legal doctrine, the prevailing view is that large retail units...
with a surface exceeding 2,000 m² can only be constructed if a zoning master plan providing for retail development has been adopted for a given area.

Therefore, to be able to implement their investment plans, sometimes investors start a procedure of amending the zoning master plan, which may prove to be rather time consuming.

### Zoning decision

In the case where no zoning master plan has been adopted for the given area, an investor may apply for a zoning decision, which sets out all the required conditions for the development of that area. Before the building process is started on the given plot under a building permit, the plot must be covered either by a zoning master plan or by a zoning decision (therefore, it can be said that a zoning decision substitutes a zoning master plan for an investor).

A zoning decision is issued by the governing authority of the commune. The procedure for issuing zoning decisions includes performance of a zoning analysis by the local authority’s architecture department and it may, therefore, take even up to several months.

If a zoning master plan is being adopted for a real property, zoning decisions related to this area expire if the provisions of the zoning master plan differ from those of the zoning decision. However, this shall not happen if a final building permit has already been issued for the real property in question. Therefore, in the case where there is no zoning master plan for a given real property, prior to investment planning the investor should monitor the stage of works related to the zoning master plan and should learn if it is possible to acquire a final building permit before the zoning master plan is adopted.

An application for a zoning decision may be filed with the relevant authority even when the applicant does not hold any title to the land in question. A zoning decision may be transferred to third parties. This means that investors may use a decision issued for the seller of a real property, as they do not have to apply for the decision once again after acquiring the real property (the investor only applies for the transfer of such a decision to himself). Investors may also apply themselves for such a decision before deciding on the investment.

### Building permit

A building permit is an administrative decision issued by a local authority (starosta or mayor in bigger cities) which allows an investor to start the development process on the site.

The documents attached by the investor to the application for a building permit should include, in particular, a declaration of having legal title to use the real property for construction purposes. Moreover, the application must also enclose approvals of the local authorities responsible for local infrastructure, in particular utilities, roads, environmental
protection and sewage treatment. The building permit will only be granted if the construction design is consistent with the assumptions of the zoning master plan or zoning decision as well as with the regulations governing technical conditions for the development.

As a general rule, a building permit expires either if construction works have not been started within three years of the date on which the permit became final or if construction works have been discontinued for more than three years.

Not all construction works require a building permit. Construction of certain structures which are listed in the Building Law of 7 July 1994 (hereinafter referred to as the Building Law) may be commenced upon a notification sent to the relevant authorities if no objections have been raised by them within 30 days of the notification date.

**Usage of the building**

Depending on the individual case, the use of a building or structure after its completion requires either notifying the construction supervisory authorities that construction works have been completed or acquiring a permit for use.

In the case where only a notification is required, under the general rule the investor may occupy and use the building or structure if no objection has been raised by the authorities within 21 days of the date of notification.

In cases where a permit for use is required, the building may be occupied only after the decision granting the permit for use becomes final. The granting of a permit for use is preceded by a technical inspection of the building or structure to confirm that all construction works have been performed in compliance with the terms and conditions of the building permit as well as technical requirements.

Occupying a building in breach of the above-mentioned regulations may result in a fine.

**Environmental issues**

The building process has many environmental aspects that must be taken into account. The Polish law provides that an environmental decision must be obtained prior to obtaining a zoning decision and a building permit for the given project. Pursuant to the Polish law, from the environmental law point of view, the investments are divided into two groups:

- projects that always have significant impact on the environment;
- projects that may have significant impact on the environment.

Environmental decision must be preceded by the environmental impact assessment proceeding (which includes preparation of environmental impact assessment report) in case of projects that always have significant impact on the environment (i.a. parking lots, buildings of a particular size etc.). However, the environmental impact assessment proceeding may be also ordered by the authority issuing
the environmental decision in relation to projects that may have significant impact on the environment.

Despite of the fact that environmental impact assessment is carried out at the stage of issuing the environmental decision, it may also be repeated (in certain circumstances) at the stage of issuing a building permit.

Environmental impact assessment is a legal instrument that allows to determine the effect of the planned investment on the environment (i.e. water, land and air quality as well as impact on flora and fauna). Environmental impact assessment proceeding, beyond the identification of specific impacts that the proposed project may have on the environment, concentrates on the ways to prevent and minimize the effects of the planned project.

Pursuant to the Polish law, authorities must inform the general public about the environmental impact assessment proceeding and allow the general public to submit comments and recommendations to the proceeding.

Moreover, Polish law in certain circumstances allows a broad access to the environmental impact assessment proceeding to non-governmental environmental protection organizations.

Environmental decision may be transferred (as well as the building permit issued on the basis of a zoning decision).

**Energy efficiency**

In implementing their pro-environmental policy, EU member states have decided to adopt legislation the main purpose of which is to limit emission of greenhouse gases by increasing energy usage efficiency. As a result, a number of regulations regarding energy efficiency have been introduced into the Polish law, inter alia by establishing energy performance certification systems for buildings and premises.

In general, certificates should determine the amount of energy that must be used in order to satisfy the relevant needs of a given building/premises. The provisions of the Building Law determine the cases in which energy performance certificates should be issued. In practice, energy performance certificates are obtained for newly constructed buildings, in particular public utility buildings with usable floor space exceeding 1,000 m².

The energy performance certificate does not only inform the owner of the building/premises about the energy usage involved and the related costs but may also positively influence the value of the building as being “environmentally friendly”.

An important thing here is that if such a certificate includes false data, it is treated as a physical defect of the building under the Building Law.
2.5.1.2 Construction issues

Legal framework for construction works contracts

The Civil Code includes provisions which establish the legal framework for construction works contracts. Most of those provisions are general in nature and enable contracting parties to structure the construction works contracts in a way that addresses their particular business needs. Such a flexible legal framework allows the parties very often to use international standards for construction works contracts, including the popular FIDIC forms. However, not all the provisions of international standards for construction works contracts comply with the requirements of the Civil Code and the Building Law.

In particular, a more detailed analysis should be performed with respect to contractual clauses regarding statutory warranty periods, contracts with and liability towards subcontractors as well as contractor’s payment guarantees. Below we present the key legal regulations in this areas.

Statutory warranty periods

Under the Polish law, the statutory warranty period for acquired real estates, including buildings is five years from the property’s hand-over date. The above mentioned statutory warranty period of five years applies also in the construction works contracts.

Approval of a contract with a subcontractor

Before a subcontract is concluded by the general contractor with a subcontractor, such a subcontract should be approved by the investor in writing. Upon being provided with the draft subcontract, the investor reviews it and decides whether the subcontract should be dismissed or approved. The investor should respond in the matter of dismissing or approving the subcontract within 14 days of its receipt. If no response is given by the investor, the subcontract is deemed to have been approved. In the case where an investor has dismissed a subcontract, such a subcontract signed between the general contractor and the subcontractor is unenforceable against the investor.

Liability towards subcontractors

In the case where the investor has approved the subcontract between the general contractor and the subcontractor, the investor is jointly and severally liable with the general contractor for the payment of the remuneration to the subcontractor. The parties must not change this rule in a contract. Therefore, contracts often include a clause under which the investor is not obliged to pay the remuneration to the general contractor unless the general contractor presents a confirmation of payment to the subcontractor. There are also some other methods of securing the investor’s risk of a double payment (to the general contractor and to the subcontractor),
which must always be adjusted to the business requirements of given investment.

**Contractor’s payment guarantee**

One of the inconveniences for investors signing construction works contracts is the obligation to grant a payment guarantee to the general contractor. Under this obligation a general contractor is entitled to a statutory claim against the investor for a payment guarantee up to the maximum amount of the contract value. The investor may satisfy the general contractor’s claim by issuing a payment guarantee in the form of a bank guarantee, an insurance guarantee, a letter of credit or a bank’s suretyship. The statutory claim for a payment guarantee may be raised at any time and can be extended to include the value of any additional works agreed in writing during the term of the construction works contract.

**Construction design contracts**

One of the key elements of the building process is drawing up a construction design. A construction design is a formal requirement for obtaining a building permit for most of building investments. Under the Polish law a construction design must be drawn up and signed by a certified architect, who takes responsibility for the technical aspects of the construction. The architect should prepare a design under a contract for architectural services which, depending on its scope, may either transfer the copyright to the construction design to the investor or provide the investor with the right to use the construction design for the purposes of the relevant investment. It is worth mentioning that a contract for architectural services may include various restrictions with regard to the copyright or the use of the design. Such restrictions may be crucial for the investment development process, in particular when they regard the possibility of entering modifications to the construction design or transferring the copyright to other entities.

**Public procurement contracts**

**General overview**

Thanks to a number of EU funding programs every year Polish authorities have billions of euros at their disposal to be spent on development. A considerable part of this funding will be designated for infrastructural projects, in particular road and railway infrastructure, which is still not very well developed in Poland. For this reason, many of the infrastructural investments developed on the Polish market will be carried out under public contracts.

Poland, as one of the EU Member States, was obliged to implement regulations governing public procurement proceedings. The provisions of EU directives on public procurement were implemented to the Public Procurement Law, which constitutes the legal framework for this matter in Poland. The
Public Procurement Law is supplemented by additional legal acts which relate in particular to public-private partnership and licenses for construction works and services.

The main goal of public procurement regulations is to establish clear and competitive rules and procedures for awarding public contracts to the suppliers of works and services as well as to provide measures for supervision over the public authorities awarding public contracts. The key objective of the Public Procurement Act is to ensure that public contracts are awarded while applying equal treatment to all entities taking part in tender proceedings as well as to ensure impartiality and objectivity of the final decision.

**Procedure**

Under the Polish public procurement regulations there are numerous different procedures for awarding public contracts. The ones that are most commonly applied are open tendering and limited tendering. Both procedures must be followed by a public notice. Notice on contract performs the aim of providing proper implementation of the rule of equal treatment in the very beginning of the procedure. The obligation of publishing a notice also provides non-confidentiality and transparency of the applied public contract systems.

In general, open tendering is a simple procedure, meaning that entities familiarize themselves with the information in the notice and in SETC and, if they are interested in submitting tenders in such procedure, they submit a tender which shall then be evaluated by ranking.

Under limited tendering procedure, entities interested in being awarded a public contract submit requests for participating in the tender and the awarding party decides which bidders may submit their proposals. Other public procurement procedures such as competitive dialogue, negotiated procedure with publication, negotiated procedure without publication, single source procurement, request for quotations or electronic auction can only be applied under specific circumstances stipulated in the binding law.

A similar course of action should be applied to the above main types of the public procurement procedure. Each of them is comprised of pre-qualification, submission of proposals and selection of the winning tenderer phases. In the pre-qualification phase the awarding party sets out the requirements / criteria to be met by the tenderers. Based on the specific requirements / criteria, tenderers draft their proposals and submit them to the awarding party. In the proposal each tenderer demonstrates its compliance with tender requirements by referring to its competencies, such as experience, knowledge and financial capacity to perform the contracted work. After reviewing all submitted proposals the awarding party selects the best tenderer with whom the public contract is to be signed.
However, this is not necessarily the end of the public procurement process as there is a possibility of appealing against the decision of the awarding party. In practice, the appeal procedure is quite commonly used by the tenderers who lost a public contract, which often results in delays in the completion of the investment project concerned.

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 recognized 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 where the usable floor space exceeds 300 m² and apartments where the usable floor space exceeds 150 m². In such cases only construction of the part of the residential building and/or apartment, 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 during construction will typically include Polish VAT. This input VAT could 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 is 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 (resulting from purchase invoices), but no output VAT is incurred. 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) occur 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 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 output VAT on importation of services was recognized (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 increased by the customs due. 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 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, provided that the acquirer is in possession of a purchase invoice or will obtain it within 3 months.

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 recognized 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

2.6.1.1. Introduction

According to the Civil Code, parties of the contract may benefit from the principle of freedom of contracts, which gives them an opportunity to modify the statutory types and provisions of the civil contract. However, there are some mandatory provisions and limitations, which have to be considered by the parties. Among all types of property exploitation agreements, the below are the most common for the Polish real estate sector:

- Lease (najem) - regulated in articles 659 to 692 of the Civil Code,
- Tenancy (dzierżawa) - regulated in articles 693 to 709 of the Civil Code,
- Leasing of real estate (leasing nieruchomości) - regulated in articles 709(1) to 709(18) of the Civil Code,
- Property management (zarządzanie nieruchomościami) - regulated in the Act on Property Management.

2.6.1.2. Lease agreement (najem)

Under the lease agreement the lessor grants to the lessee the right to occupy premises (office, residential etc.) in exchange for the payment of rent. In general, everything that can be subject to the ownership right, may be also subject to this agreement, nevertheless in case of real estate, the more strict provisions may apply.
**Duration**

The duration of a lease agreement may be definite or indefinite. The lease agreement may be concluded in any form, however, in case of a lease of a real property for a period longer than one year, the agreement shall be concluded in writing. In case of a lack of a written form, the lease agreement shall be deemed to have been concluded for an indefinite period of time.

The duration of a lease agreement may be freely fixed by the parties, however, there are certain restrictions. The lease agreement concluded for a period longer than ten years, is, after this period, deemed to have been concluded for an indefinite period of time. The rule above is different for the lease agreements concluded between entrepreneurs. In this case the lease agreement concluded for a period longer than thirty years is deemed to have been concluded for an indefinite period of time after the thirty years' period has passed.

**Rent**

Paying rent is the principal obligation of the lessee. The lessee is obliged to pay rent within the agreed time. If the due date is not fixed in the agreement, the rent should be paid in advance: if the lease is not longer than one month - for the whole lease period, and if the lease is longer than one month or if the contract is concluded for an indefinite period of time - monthly, no later than on the tenth day of the month. In practice, the lease agreements regulate in details the payment of the rent.

**Maintenance and expenditures settlement**

The lessor should hand over the property to the lessee in a condition fit for the agreed use. It should be maintained by the lessor in this condition throughout the lease term. Minor repairs connected with the normal use of the property should be fixed by the lessee, unless the lease agreement provides for otherwise. If the subject of lease is destroyed due to circumstances for which the lessor is not responsible, he is not obliged to restore it. If, during the lease period, the property requires repairs which encumber the lessor, the lessee may set the lessor an appropriate time for repair. After this period the lessee may carry out the repairs needed at the lessor’s cost.

If the lessee improves the subject of lease, the lessor may - after the expiry of the lease term, at its discretion, either demand that the previous condition be restored or pay the lessee a sum corresponding to the improvement value at the time of return. In practice, these issues are usually covered by the provisions of the lease agreements.

**Subletting and disposal of the leased property**

The general rule is that the lessee may hand over the property or part of it to a third party for free of charge use or
sublet it, if the lease agreement does not forbid it. However, when the subject of lease constitutes premises or retail areas, hand over the property or part of it to a third party for free of charge use or sublet it requires the lessor’s consent. If the leased property is handed over to a third party, both the lessee and the third party are liable towards the lessor for using the property in accordance with the provisions of the lease agreement. The relationship arising from a contract for free of charge use or subletting concluded by the lessee is terminated, at the latest, when the main lease agreement is terminated. In practice, the lease agreements forbid subletting the property to a third party or require the prior written consent of the lessor.

The leased property can be disposed of during the lease period. In this case the acquirer becomes a party to the lease agreement as a lessor in place of the seller. The approval of the lessee is not required. The new owner may terminate the lease agreement retaining statutory notice periods. However, the new owner does not have a right to terminate the lease agreement if it is concluded for a definite period of time, in written form with an authenticated date (data pewna) and the subject of lease has been delivered to the lessee. If, as a result of the lease agreement being terminated by the acquirer of the leased property, the lessee is forced to return the leased property earlier than he would have been obliged to under the lease agreement, he may demand compensation from the seller.

Security

Lessors often use the special clauses in the lease agreements to secure their potential claims to lessees such as money deposit, promissory note, surety and bank guarantee.

- Money deposit – it is a sum of money submitted by the lessee in order to secure the lessor’s potential claims in case of non-fulfillment of the lease agreement or damages caused by the lessee. As far as the lease of commercial premises is concerned, there is almost unlimited discretion in determining the content of the clause. In the case of lease of residential premises, which are the subject to regulation of the Act on the protection of lessee’s rights of 21 June 2001 (hereinafter referred to as the Lessee’s Protection Act), the freedom of parties forming the content of this additional contractual claim is limited. A money deposit cannot exceed twelve times the monthly rent for the premises and the rent should be calculated at the rate applicable at the date of the lease.

- Promissory note – promissory note issued by the lessee is an effective way to protect the lessor’s potential claims. In case of default in payment of rent or in case of other claims against the lessee, the lessor can make use of the promissory note and request the lessee to redeem it. In case the lessee does not fulfill its obligations from the promissory note, the lessor can start the court procedure against the lessee.
• Surety – in the contract of surety, the guarantor undertakes to perform certain obligation of the lessee towards the lessor if the lessee does not perform them, mostly this refers to the payment of due amounts. The liability of the guarantor is equivalent, not subsidiary. This means that the lessor may request a payment from both the lessee and the guarantor.

• Bank guarantee – it is a unilateral obligation of the guarantor’s bank, according to which the bank will provide funds to the beneficiary of the guarantee - the lessor, if the lessee does not fulfill its obligation. The parties of the lease agreement typically determine a period that has to elapse from the payment due date and after which the lessor has the right to execute a bank guarantee.

Termination

A lease agreement concluded for an indefinite period of time may be terminated by any party with a prior notice of termination (its length is in practice defined in the lease agreement). The statutory period of notice of termination for the lease agreement concluded for an indefinite period of time is as follows:

• if the rent is due for a period longer than a month - the contract can be terminated by giving a three-month notice, effective at the end of the calendar quarter;
• if the rent is due every month - the contract can be terminated with a one-month notice, effective at the end of the calendar month (three-month notice in case of lease of premises or retail areas, effective at the end of the calendar month);
• if the rent is due for a period shorter than a month - the contract can be terminated with a three-day notice;
• if the rent is due for one day - the contract can be terminated one day in advance.

The lease agreement concluded for a definite period of time may be terminated only in cases specified in the contract. However, the Civil Code stipulates that the parties can terminate the lease agreement immediately if certain conditions defined by the above code occur. This applies to contracts concluded for both definite and indefinite period of time:

• if, at the time of handing it over to the lessee, the subject of lease has defects that make it impossible to use it in the way defined in the lease agreement, or if the defects occur later and the lessor does not, despite receiving a notice, remove them in an appropriate time, or if the defects cannot be removed - the lessee may terminate the lease agreement without notice;
• if the lessee defaults in paying rent for longer than two full payment periods - the lessor may terminate the lease agreement without notice (in case of lease of premises or retail areas, before termination, the lessor is obliged to warn the lessee in writing by giving him an additional one-month period to pay the overdue rent);
if the lessee uses the subject of lease contrary to the terms of the agreement or the purpose of this and, despite a warning, does not cease to use it in this way, or if a lessee neglects it to such an extent that the subject of lease is at risk of being lost or damaged - the lessor may terminate the lease contract without notice.

Lease of premises for residential purposes

Residential lease agreements, due to their purpose are subject to special protection which arises from the provisions of the Lessee’s Protection Act. This protection applies mainly to the limited possibility of termination of the lease. There is also a specific regulation regarding the rent increase.

2.6.1.3. Tenancy agreement (dzierżawa)

By a tenancy agreement, the lessor commits to hand over a subject of tenancy to the lessee’s use and collection of profits for a fixed or a non-fixed term. In exchange, the lessee commits to pay the agreed rent. The tenancy agreement gives not only the right to use the property but also to collect benefits from it, which is why the tenancy agreement usually concerns land.

The duration of a tenancy agreement may be definite or indefinite. However, the tenancy agreement for a period longer than one year should be concluded in writing, otherwise it is considered to be concluded for an indefinite term. Also a tenancy agreement executed for a longer period than thirty years is deemed to be concluded for a non-fixed term, after this period passes.

Under the Civil Code, if the rent payment period is not specified in the contract, rent is payable in arrears on the date customarily accepted, and in the absence of such custom, semiannually in arrears. If the lessee defaults in payment of rent for at least two full payment periods and, in the case of rent paid annually, he defaults in payment for over three months, the lessor may terminate the tenancy without notice. However, the lessor should warn the lessee by giving the lessee an additional three-month period to pay the overdue rent.

The lessee is responsible for the costs of all repairs to the extent necessary to keep the subject of tenancy in the same condition. However, the parties are able to modify this rule in the tenancy agreement. There are also some differences between a lease agreement and a tenancy agreement in the field of subletting a property. The lessee cannot sublet the property without the lessor’s consent. If the above obligation is violated, the lessor may terminate the tenancy agreement without notice.

2.6.1.4. Leasing agreement (leasing nieruchomości)

By a leasing agreement, the financing party undertakes, within the scope of operations of its enterprise, to acquire a property from a specified transferor
and to hand it over to the user to use for a defined period. In exchange, the user commits to pay the installments agreed in the contract. The lessor retains ownership of the property, however, when the contract expires, the lessee has a right to take over the ownership of the property. In practice, there are two main types of the leasing agreement:

- **operating leasing** – in this type of leasing the subject of lease agreement remains the asset of the lessor who makes the relevant depreciation write-offs. After the end of the leasing term the lessee may purchase the subject of the agreement for remuneration. An operating lease is commonly used to acquire equipment on a relatively short-term basis;
- **financial leasing** – in this type of leasing the lessor remains the legal owner of the asset, however, it is the lessee who makes the depreciation write-offs. The transfer of an ownership of a subject of a leasing agreement after its termination may be stipulated directly in that agreement.

The duration of the financial leasing contract is usually longer than the operating leasing and similar to the economic utility of the subject of leasing.

There is also another form of the leasing agreement which is often used in the real estate market called sale and lease-back. The essence in this case is the sale of property by the owner to a leasing company. Afterwards, the leasing agreement is signed between the same parties allowing the previous owner to use the property as the lessee. This operation allows the release of funds and gives the opportunity to invest them in other activities. More detailed legal and tax comments are presented in section 2.8.

### 2.6.1.5. Property management agreement *(zarządzanie nieruchomościami)*

Property management is a professional activity carried out by property managers. It is regulated in the Act on Property Management, under which management of a particular property is based on the property management agreement between the owner of the real estate and the property manager. The agreement for property management should be concluded in writing, otherwise null and void.

The property manager is required to have a compulsory insurance of civil liability for damage caused in the course of activities.

### 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 recognized 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 expenses (e.g. the costs of representation) 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:

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<th>3</th>
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<td>10</td>
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<td>0</td>
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<td>20</td>
</tr>
</tbody>
</table>

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 0.90 per m² of land;
- for buildings, PLN 23.13, per m² 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).

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 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 legal and tax consequences of both are presented in section 2.4.
2.8. Sale and lease back

Legal aspects

A sale and lease back transaction consists of two stages. The first stage assumes selling the target real property by the seller to the purchaser. In the next stage the seller concludes the agreement on the lease of the real property from the purchaser. As a result of the sale, the owner (or perpetual usufructuary) of the real estate changes. However, due to leasing the real property back, the real estate remains under the operational control of the original party (the seller).

From the legal perspective it is important to secure the sellers’ interest already in the first stage of the transaction, i.e. to establish the obligation of the purchaser to lease the real property back in the agreement on the sale of the real property. It is also important for both parties to agree details of the lease (duration, price, etc.) as soon as possible, especially if the seller and the purchaser do not belong to the same capital group.

The main advantage of such a sale and lease back operation is the release of the seller’s capital as a consequence of the sale of the real property. This capital may be thereafter used e.g. for investment purposes. However, the decision on choosing such a solution shall be made on detailed calculation of all the costs related, including the lease costs.
**Tax implications**

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.

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.

A sale and lease-back arrangement has an 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.
2.9. Due diligence as part of the acquisition process

The main purpose of the due diligence process is to provide investors with a complex overview of the situation of the real estate being the subject of the acquisition from the legal, financial and tax perspective. Taking into account the specific status and features of a given real estate, a broader due diligence review, conducted by technical and environmental experts, may be recommended.

2.9.1. Legal due diligence

The due diligence process is all about mitigating investment risks. In practice, the legal due diligence review consists in gathering information and should provide the potential investor with a comprehensive view of the legal issues regarding the real property he considers acquiring.

By the end of the due diligence process, the investor should have a fair idea of whether the real estate is worth investing time and money. In this regard, a due diligence should be as comprehensive as possible.

The scope of the legal due diligence will depend on the structure of the deal. In a share deal, the scope of the due diligence will generally be wider than that required for an asset deal, as it needs to cover all the aspects related to the activity of the company. In case of an asset deal mostly the legal status of the real estate should be taken into consideration and examined carefully.

Within the legal due diligence, the review bases mainly on data and information provided by the seller and on enquiries and discussions with the seller and/or the management of the target. Additionally, publicly
available sources (such as data in court registers) are explored. In practice, the due diligence regarding the real estate usually covers review of the following matters:

- legal documents related to the seller’s title to the real estate in use (e.g. real estate acquisition agreements, extracts from the land and mortgage register, extracts from the land and buildings register, etc.);
- documents related to the encumbrances over the seller’s real estate;
- lease agreements for the real estate concluded by the seller;
- development and construction documentation;
- planning and zoning issues;
- utilities supply documentation;
- environmental issues (permits, licenses etc.).

Review of other aspects is usually agreed with the seller and strictly depends on the type of transaction (share or asset deal).

The aim of the legal due diligence review of the real estate is to identify areas of investment risks but also other specific legal aspects regarding performing of business activity on the real estate and its sale. Below we present certain issues that need to be analyzed during the due diligence process and which may influence the structure of the transaction, or even a decision on entering into the transaction.

**Zoning Master Plan**

The zoning master plans are issued by the local authorities (municipalities) for a given area. Generally, zoning master plans are local acts and define conditions for land use and destination and the scope of business that can be conducted within a given area. Municipalities issue zoning master plans with a view to local development and public interest. Development of an investment on the real estate is possible provided that buildings, plants and other industrial facilities comply with the relevant zoning master plan for a given area. Therefore, it is essential to establish during the due diligence process whether there is a local zoning master plan covering the area where the targeted real estate is located and if so, what are the conditions of this zoning master plan in order to confirm whether it will be possible to perform the planned investment. Please refer to the section 2.5.1. for more detailed information regarding the zoning master plan.

Within the review of the zoning master plan, in particular, the issues of the conservation and historic preservation zones and agricultural land should be verified.

**Conservations and historic preservation zone**

The zoning master plan may provide that the area where the real estate subject to the potential investor’s interest is located falls within a conservation and historic preservation zone where some specific rules apply in order to protect the historical monuments located in the zone. Depending on the type of the real estate and its historical status there may be
additional requirements and limitations established by the provisions of law.

**Agricultural land**

The zoning master plan may provide that the real estate is assigned for agricultural activity. As a rule, the development of real estate designated for agricultural use requires a special procedure involving the modification of the zoning master plan. Such a procedure may be time-consuming and is connected with the risk of third parties challenging the proposed changes to the plan. Additionally, real estate classified as agricultural land in the Land and Building Register, but not covered by the master plan, should be also excluded from agricultural production by obtaining an administrative decision from the relevant authority.

It should be noted that after the exclusion of the area from agricultural activity an annual fee has to be paid for ten years (see comments below).

Certain regulations are also in force as regards the acquisition of agricultural real estate and they provide for many specific legal restrictions and limitations. In particular, prior to the acquisition of the agricultural land by foreigners (including citizens and corporate entities from the European Economic Area), a permit from the Ministry of Internal Affairs must be obtained. These rules do not change in case it is the shares in the company owning the agricultural land that are subject of the transaction. Additional limitation that has to be taken into consideration is the pre-emptive right towards arable land of an area of at least 50,000 m² which is granted to the Agricultural Property Agency.

In consequence, an investor considering acquisition of agricultural real estate should be prepared for additional actions to be taken and costs to be incurred in order to execute his plans regarding the acquisition and development of the land.

**Restitutions claims**

Under the nationalization laws passed in Poland after the Second World War, many real properties and functioning enterprises (including their real estate assets) were “nationalized” (or “communalized”). However, currently, there are no specific reprivatisation laws in force in Poland to deal with the restitution matters and claims. As a result, the legal status of nationalized properties is quite often subject to uncertainty. Under specific conditions, former owners or their successors may apply to civil courts and initiate proceedings aimed at the restitution of such real estate. As the current owner benefits from the land and mortgage register’s public credibility warranty, the outcome of such claim will primarily depend on the apparent good faith of the current and previous owner at the time they acquired the property. Nevertheless, this issue needs to be subject to analysis during the due diligence.

In Warsaw, on the basis of the special “Warsaw decree” on land ownership of 1945, the City of Warsaw gained ownership rights to the major part of
real estate in the city. However, subject to specific conditions, former owners of the real estate were granted the right to apply for obtaining usufruct rights to real estate or compensation. Currently, such applications which were not resolved or were resolved in contravention of the law may be the base for successful claims for reestablishing the rights of the previous owners or their successors. In consequence, it is essential during the due diligence to investigate whether any such proceedings are pending with respect to the target property located in Warsaw.

**Fees - holding the real estate**

**Zoning fee**

Zoning fee (“Opłata Adiacencka”) is a charge which may occur with regard to the increase of the value of the real property resulting from:

- division of the property;
- merging and subsequently dividing the property;
- the construction of infrastructure with the use of public funds (placing water pipes, sewage pipes, heating systems, electricity gas and telecommunications facilities).

The amount of the fee depends on the amount of the increase in the property’s value and is usually established based on an opinion of an independent expert determining how much the value of property has increased by.

The amount of fee shall not be higher than 50% (with respect to the division following a merger and the construction of infrastructure with the use of public funds) and not higher than 30% (with respect to a division) of the increase in value of the property.

Additionally, adoption of the zoning master plan may also lead to an increase in real estate market value, e.g. when a forestry land or an agricultural land is reclassified in the zoning master plan into public roads, its value usually increases. In such cases the zoning fee (“Renta Planistyczna”) may be established as a percentage (not higher than 30%) of the increase in value of the land calculated as at the date of the transfer of the given real estate.

The percentage for calculation of the zoning fee should be provided for in the master plan. 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**

Entrepreneurs are often interested in changing the purpose of use of the agricultural and forest land in order to develop the land and realize an investment. 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 land subject to exclusion;
- quality of the land (class of soil);
- market value of the land subject to exclusion.
It should be noted that if the land excluded from agricultural production is sold, the obligation to pay the annual fees passes to the purchaser.

**Environmental issues**

**Introduction**

Polish environmental law affects the conduct of economic activity for most business entities. One of the most important requirements imposed by the environmental law is the requirement to obtain permits related to the rules of having an impact upon the environment. It is usually examined during the due diligence whether the seller (or the target company) fulfills the environmental law requirements.

**Permit requirements**

Environmental permits can be basically divided into two groups. The first one includes permission obtained in the course of the investment process and the second group includes permission related to the use of the property.

In certain circumstances Polish environmental law imposes an obligation to obtain an integrated permit, which includes a number of permits governing the use of the environment. The obligation to obtain integrated permit relates to, inter alia, the following branches of industry: metallurgy and steel industry, the mineral industry and the chemical industry.

Besides, it is important to take into account the permissible level of noise. Permission is required only if the noise level exceeds the noise limits, which should be evaluated taking into account the provisions of the local plan.

**Liability for contaminated land**

Pursuant to the Polish environmental law, a holder of the land (i.e. an owner of the property or other entity indicated in the land registry as a holder) is responsible for the land contamination, notwithstanding when the contamination occurred. Thus, the holder of the land will be liable for the clean-up even if the contamination has been caused by his predecessors.

Parties to the agreement cannot contractually exclude the liability of the purchaser for clean-up of contaminated land so when a potential investor intends to buy a property (especially one that was used for industrial purposes) a detailed study on pollution of the land is required.

To secure purchaser’s interest, the seller of contaminated land may agree to indemnify the purchaser against the liability for the clean-up. However, in practice it may be difficult to achieve.

**Environmental impact assessment**

According to the section 2.5.1 where the environmental decision and environmental impact assessment where described, in some cases - especially for large investments an environmental impact assessment proceeding may be required.
2.9.2. Financial due diligence

Not many investors perform due diligence when completing a real estate transaction. Often the investor’s own internal procedures require due diligence to determine whether or not the transaction is in the best interest of the investor.

Although for transactions of a smaller scale this may not be a good way to evaluate a deal, most investors understand the value of expert outsourced financial due diligence services. This rings especially true when taking into account larger time-sensitive transactions (auction processes for example).

Although some investors choose to forego due diligence when acquiring new assets, they should understand that financial due diligence can indicate how the acquired assets will affect metrics such as revenue and net operating income. In addition, due diligence is able to discover unforeseen problems such as discrepancies between the amount paid for rent as described in lease agreements vs. the actual amount being paid per the accounting books.

A buyer usually makes use of financial due diligence to assist in identifying major issues concerning a transaction:

- the value of the property's NOI taking into account the existing lease portfolio
- any provisions in the lease that affect the NOI adversely (for example, discounts on rent for any given period of time or for improvements made by lessee)?
- bookkeeping in use being adequate for the business, and how does it looks next to the investor's bookkeeping procedures
- lessee ever being late with the rent, or it taking longer to collect rent;
- charges made by the lessee being enough to cover the costs of maintaining the building; and any service charges not settled for any reason

Analyzing financial issues

The items listed below should be considered when seeking to resolve the previously mentioned issues concerning financial due diligence:

- the financial figures being viable: can the figures be traced back to its origin reliably;
- critical bookkeeping procedures being applied consistently and appropriately;
- the influence of the bookkeeping procedures on the financial figures;
- assuring that the creation and level of management information is accurate and adequate for the business being considered;
- evaluating the contractual obligations the business has and their influence on profitability and cash flow;
- evaluating critical problems influencing earnings position;
- recognition of the need for cost recharges incurred and focus on areas for improvement;
- recognizing the “normal” working capital and cash flow tides of the business and probable funding needs down the line;
making sure constructions costs are properly reflected in the bookkeeping records;

- recognizing the net asset base for acquisition; addressing possible balance sheet valuation discrepancies; making sure everything has been adequately addressed in evaluating the underlying earnings;

- comparing the rent roll against the rental agreements and bookkeeping records;

- comparing the service charges incurred against the bookkeeping records; and

- going over rental agreements to identify 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.

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.

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. However, as a rule, tax liabilities regarding the period before 2009 should already be subject to statute of limitation.
**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 2015 there is still a tax risk in relation specifically to a target's corporate income tax payments for 2009–2015, and to other tax liabilities, in general, for 2010–2015.

**Tax issues analyzed**

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 lessees 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. The use of due diligence results when negotiating

After the whole process of due diligence, the investor gets a general financial and tax risk overview, which makes up the origin of the information for negotiations with the seller and assists in adjusting the financial model for valuation.

This can be used to get a decrease in price in order to alleviate possible tax liabilities and can be used when writing warranties and damages in the SPA.

The results may directly affect the composition of the transaction, for example, transforming a share deal to an asset deal; they may also be used for post-acquisition tax planning.

Along with the tax and financial due diligence results, the legal due diligence review should assist the buyer in determining whether or not to complete the transaction, and if so, in what form. Due diligence investigations let the buyer’s legal team construct the conditions of the deal so that the buyer is afforded with an adequate amount of comfort and protection. The legal team will then be in a position to address specific problems by asking for further explanations and/or promises or warranties from the seller. The legal team can also evaluate whether or not such promises or warranties need to be covered by an indemnity clause or other legal language allowed under the Polish law.

When taken together, the financial, tax and legal due diligence results are a very strong tool which can very easily have an influence on the final result of negotiations, and, in particular, how much the buyer will ultimately pay.
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 with subsequent amendments (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 the 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 in Poland. Since that time it has issued the following National Accounting Standards (‘KSR’) 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”
- KSR 7 “Changes in accounting policies, estimates, correction of errors, post balance sheet events – accounting and presentation”
- KSR 8 “Developer activity”
- KSR 9 “Management report”
The Committee also issued several 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 the 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:

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

* 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 included amongst others:

- recognition of changes in the fair value of investment properties and intangible assets classified as investments;
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, cooperative savings banks 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 budget entities;
  - communal, district and provincial budget institutions;
  - state special purpose funds.
- 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;
- 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.

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 unrealized gains/losses recorded in the profit and loss account;
- **available for sale** – measured at fair value, with an unrealized 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 the 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 National Accounting Standard 3 (KSR 3) “Construction contracts”**

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 the 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 a 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 National Accounting Standard Income Taxes (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 their 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. As required by the Act the 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.

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.

The same regulations apply to the parent entities that 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, translated into Polish by a worn 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 favourable 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 to protect the 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 BondSpot (previously: 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.
<table>
<thead>
<tr>
<th>Type of the report</th>
<th>Content includes</th>
<th>Filling deadline ***</th>
</tr>
</thead>
</table>
| 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 month 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

Audit 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, and the annual financial statements of entities which are prepared in accordance with IFRS, 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 (applicable for annual periods beginning on 1 January 2013)

3.2.1. Introduction

Nowadays, a number of real estate entities apply IFRS for their accounting and reporting purposes. Companies reporting under International Financial Reporting Standards (IFRS) continue to face a steady flow of new standards and interpretations. The volume of changes to IFRS is significant and is likely to continue in the foreseeable future. The nature of the changes ranges from significant amendments of fundamental principles to some minor changes included in the annual improvements process. They will affect many different areas of accounting of real estate entities such as the presentation of financial statements, financial instruments, leases. Some of the changes have implications that go beyond matters of accounting, as they may impact business decisions, such as the design of joint arrangements or the structuring of transactions. The challenge for preparers will be to gain an understanding of what lies ahead.

Below we concentrate on the implications of the newly issued IFRS 10, 11, 12 and 13 for the real estate and construction industries.
3.2.2. Interaction between IFRS 10, IFRS 11 and IFRS 12

3.2.2.1 Introduction

In May 2011, the International Accounting Standards Board (IASB) issued three new standards that amended consolidation rules of entities:

- IFRS 10 Consolidated Financial Statements,
- IFRS 11 Joint Arrangements and
- IFRS 12 Disclosure of Interests in Other Entities.

These new standards are effective for annual periods beginning on or after 1 January 2013, and must be applied retrospectively (with some modifications). In Poland and in the whole European Union standards come with an effective date of 1 January 2014, so for the majority of companies 2014 was the first year new rules were applied.

The major changes introduced are as follows:

- IFRS 10 establishes a single control model that applies to all entities. The changes introduced by IFRS 10 require management to exercise more judgement to determine which entities are controlled, compared with the previous requirements that were in IAS 27. IFRS 10 does not change consolidation procedures (i.e., how to consolidate an entity) from the requirements that previously existed in IAS 27. Those requirements have simply been moved to IFRS 10. Rather, IFRS 10 changes whether an entity is consolidated, by revising the definition of control and adding requirements to consider when making control decisions.

- IFRS 11 deals with jointly controlled entities (JCEs) and addresses only two forms of such joint arrangements (joint operations and joint ventures). One of the primary reasons for the issuance of IFRS 11 was to increase comparability within IFRS by removing the choice available for JCEs to use proportionate consolidation. Instead, JCEs that meet the definition of a joint venture (as newly defined) must be accounted for using the equity method. This also converges with US GAAP, which generally requires the equity method for joint ventures. For joint operations (including former jointly controlled operations, jointly controlled assets and, potentially, some former JCEs), an entity recognises its assets, liabilities, revenues and expenses, and/or its relative share of those items, if any. IFRS 11 is intended to broaden the focus for classifying a joint arrangement, so that the structure of the joint arrangement is not the only factor considered. Whereas previous regulations of IAS 31 focused exclusively on the legal form of the entity, IFRS 11 focuses more broadly on the rights and obligations arising from the arrangement.

- IFRS 12 summarizes all the disclosure requirements related to an entity’s interests in subsidiaries,
joint arrangements, associates and structured entities, including a number of new disclosures. One of the most significant changes introduced by IFRS 12 is that an entity is required to disclose judgements that were made in determining whether it controls or has joint control over another entity. Even if management concludes that it does not control an entity, the information used to make that judgement will be transparent to users of financial statements. The new disclosures will also assist users of financial statements to make their own assessment of the impact on the financial results of the group in case reaching a different conclusion regarding entities to be consolidated - by providing more information about certain unconsolidated entities.

Diagram 1 - Interaction between IFRS 10, IFRS 11, IFRS 12 and IAS 28
3.2.2.2. IFRS 10 - Consolidated Financial Statements

Consistent with previous requirements IFRS 10 requires that a parent (unless exempt) present consolidated financial statements. That is, IFRS 10 requires financial statements of the group, in which the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries, are presented as those of a single economic entity. IFRS 10 applies to all types of entities, including corporations, partnerships, limited liability corporations, trusts, and other types of entities. A group consists of a parent and its subsidiaries (i.e., entities that the parent controls). When an entity is a parent it needs to assess whether it (the investor) controls the other entity (the investee). IFRS 10 provides a new definition of a control together with a changed guidance on assessing whether the entity has control of an investee.

In many cases, when decision-making is controlled by voting rights that also give the holder exposure to variable returns, it is clear that whichever investor holds a majority of those voting rights controls the investee. However, in other cases (such as when there are potential voting rights, or an investor holds less than a majority of the voting rights), it may not be so clear. In those instances, further analysis is needed based on the facts and circumstances (considering the Application Guidance in IFRS 10), to determine which investor, if any, controls an investee. Diagram below illustrates this assessment.

Excerpts from IFRS 10:

6  An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee.

7  Thus, an investor controls an investee if and only if the investor has all the following:

   (a) power over the investee;
   (b) exposure, or rights, to variable returns from its involvement with the investee; and
   (c) the ability to use its power over the investee to affect the amount of the investor’s returns.
Diagram 2 - Definition of control

**Power**
Determine which party, if any, has power, that is, the current ability to direct the relevant activities. Power arises from the rights, which may include:
- Voting rights
- Potential voting rights (e.g., options or convertible instruments)
- Rights to appoint key personnel
- Decision making rights within a management contract
- Removal or „kick-out” rights
However, power does not arise from protective rights.

**Returns**
Assess whether the investor is exposed, or has rights to variable returns from its involvement with the investee. Returns can be positive, negative or both. Examples of returns include:
- Dividends
- Remuneration
- Economies of scale, cost savings, scarce products, proprietary knowledge, synergies or other returns that are not available to other interest holders

**Linkage**
Evaluate whether the investor has the ability to use its power to affect the investor’s returns from its involvement with the investee. If applicable, determine whether the investor is a principal or an agent, considering:
- Scope of its authority
- Rights held by other parties
- Remuneration
- Exposure to variability from other interests

The first criterion to have control relates to power. An investor has power when it has existing rights that give it the current ability to direct the relevant activities. Therefore, when assessing whether an investor has power, there are two critical concepts:
- **Relevant activities**
- **Existing rights**

Relevant activities are the activities of the investee that significantly affect the investee’s returns. Examples of relevant activities include:
- Determining and changing operating and financial policies (which might include the items below)
- Selling and purchasing goods and services
- Managing financial assets during their life
- Selecting, acquiring or disposing of assets

In many cases, more than one activity will significantly affect an investee’s returns. Thus, in order to decide which party, if any, has power, it is important to identify the activities that most significantly affect returns. This differs from joint control, defined as the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. Joint control is discussed in more details later.
Once the relevant activities are identified, the next step is to determine which investor, if any, carries existing rights, i.e. has the current ability to direct those activities, which gives him the power over the investee.

In order to give the power the rights need to be substantive. For example, the following should be considered when evaluating whether an investor’s rights are substantive:

- Why were the rights granted?
- What compensation was given (or received) for the right? Does that compensation reflect fair value?
- Did other investors also receive this right? If not, why?

In addition IFRS 10 introduces a new term of protective rights, defined as: rights that are designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate. Control does not arise from protective rights. Examples of protective rights include the right to:

- Restrict an investee from undertaking activities that could significantly change the credit risk of the investee to detriment of the investor
- Approve an investee’s capital expenditures (greater than the amount spent in the ordinary course of business)
- Approve an investee’s issuance of equity or debt instruments
- Veto transactions between the investee and a related party

In some cases, a right might be deemed protective, such as the ability to sell assets of the investee if an investee defaults on a loan, when default is considered an exceptional circumstance. However, if the investee defaults on a loan, the investor holding that right would need to re-assess whether that right has become a substantive right (rather than a protective right), based on the change in facts and circumstances.

**Example – Veto right over annual budget – protective or not?**

An investor determined that approving the annual operating budget of an investee is the relevant activity. For example, this might be the case if the operating budget is detailed and management has little latitude to deviate from the budget. An investor has the right to veto this annual operating budget. If that investor does veto the budget, management of the investee must re-draft and re-propose the budget, and re-submit the budget to the investor holding the veto right.

In this fact pattern, because approving the annual operating budget is the activity that most significantly affects the investee’s returns, then a veto right over the annual operating budget would be substantive, and is not a protective right. Evaluating whether approving an annual operating budget is the most relevant activity will depend on facts and circumstances, and requires judgement.

The second criterion for assessing whether an investor has control of an investee is determining whether the investor has an exposure, or has rights, to variable returns from its involvement.
with the investee. Returns can be positive, negative or both. Examples of exposures to variable returns include:

- Dividends, fixed interests on debt securities that expose the investor to the credit risk of the issuer, variable interest on debt securities, other distributions of economic benefits and changes in the value of an investment in an investee
- Remuneration for servicing an investee’s assets or liabilities, fees and exposure to loss from providing credit or liquidity support, residual interests in the investee’s assets and liabilities on liquidation of that investee, tax benefits and access to liquidity that an investor has from its involvement with the investee
- Economies of scale, cost savings, scarce products, proprietary knowledge, synergies, or other exposures to variable returns that are not available to other investors

Simply having an exposure to variable returns from its involvement with an investee does not mean that the investor has control. To control the investee, the investor would also need to have power over the investee, and the ability to use its power over the investee to affect the amount of the investor’s returns. For example, it is common for a lender to have an exposure to variable returns from a borrower through variable interest payments that it receives from the borrower. However, the lender would not control the borrower if it does not have the ability to affect those variable interest payments (which is frequently the case). It should be emphasised that with respect to this criteria, the focus is on the existence of an exposure to variable returns, not the amount of the exposure to variable returns.

The third criterion for having control is that the investor must **have the ability to use its power over the investee to affect the amount of the investor’s returns**. The link between power over an investee and exposure to variable returns from involvement with the investee is essential for having control. An investor that has power over the investee but cannot benefit from that power, does not control that investee. An investor that has an exposure to a variable return from an investee, but cannot use its power to directs the activities to most significantly affects the investee’s returns, does not control that investee.

When decision-making rights have been delegated or are being held for the benefit of others, it is necessary to assess whether the decision-maker is a principal or an agent to determine whether it has control. This is because if the decision-maker has been delegated rights that give it power, the decision-maker must assess whether those rights give power for its own benefit, or merely power for the benefit of others. As an agent cannot control over the investee, it does not consolidate the investee. A principal may have control over the investee, and if so, would consolidate the investee.
3.2.2.3 IFRS 11 - Joint Arrangements

There are many reasons why one might use a joint arrangement to conduct business, such as to:

- Accelerate the development of new technologies
- Turn existing technologies into marketable products
- Enter new markets or industries
- Expand geographically
- Protect supply chain and production capacity
- Leverage intellectual property held by others (including competitors)
- Distribute risk
- Act as an alternative to raising bank or equity financing
- Bring in additional expertise
- Comply with the requirement of a government stakeholder
- Facilitate distribution of product
- Take the first step in acquiring a business

As discussed in more detail below, IFRS 11 covers all arrangements in which there is joint control. In practice, some agreements that are referred to as ‘joint arrangements’ or ‘joint ventures’ actually include arrangements whereby only one party has control, or no parties have joint control. Other arrangements may not use the term ‘joint arrangement’ or ‘joint control’, but could still be joint arrangements, as defined by IFRS 11. Some arrangements split ownership equally (50/50) between two parties – while others may give a greater financial interest to one of the two parties. No matter what terminology is used to describe the arrangement, or its purpose, management will need to carefully evaluate the terms of the arrangement, and the relevant facts and circumstances, to determine if it qualifies as a joint arrangement.

Excerpts from IFRS 11:

4 A joint arrangement is an arrangement of which two or more parties have joint control.

5 A joint arrangement has the following characteristics:
   (a) The parties are bound by a contractual arrangement.
   (b) The contractual arrangement gives two or more of those parties joint control of the arrangement.

6 A joint arrangement is either a joint operation or a joint venture.

7 Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.
Diagram 3 - is it a joint arrangement?

Does the contractual arrangement give all of the parties (or a group of the parties) control of the arrangement collectively?

- NO

Do the decisions about the relevant activities require the unanimous consent of all of the parties that collectively control the arrangement?

- NO

- YES

Joint arrangement

IFRS 11 states that decisions about the relevant activities require the unanimous consent of all the parties, or a group of the parties, that collectively control the arrangement. Accordingly, it is not necessary for every party to the arrangement to agree to have unanimous consent. To have unanimous consent, only those parties that collectively control the arrangement must agree. The requirement to have unanimous consent ensures that no single party controls the arrangement. While the requirement for unanimous consent is not new, IFRS 11 clarifies when unanimous consent exists. For example, in some cases, a contractual arrangement may require a minimum proportion of the voting rights to make decisions. When that minimum can be achieved by more than one combination of the parties agreeing, the arrangement is not a joint arrangement unless it specifies which parties (or combination of parties) are required to agree unanimously to decisions about the relevant activities of the arrangement. Two scenarios presented below in Diagram 4 clarify on this.
Diagram 4 - Joint control?

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Scenario 1</th>
<th>Scenario 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>75% vote to direct relevant activities</td>
<td>75% vote to direct relevant activities</td>
<td></td>
</tr>
<tr>
<td>Party A</td>
<td>50%</td>
<td>50%</td>
</tr>
<tr>
<td>Party B</td>
<td>30%</td>
<td>25%</td>
</tr>
<tr>
<td>Party C</td>
<td>20%</td>
<td>25%</td>
</tr>
</tbody>
</table>

Conclusion
Joint control – A and B collectively control the arrangement (since their votes and only their votes, together meet the requirement). Because they are the only combination of parties that collectively control the arrangement, it is clear that A and B must unanimously agree. No joint control – multiple combinations of parties could collectively control the arrangement (i.e., A and B or A and C could vote together to meet the requirement). Since there are multiple combinations, and the contractual agreement does not specify which parties must agree, there is no unanimous consent.

IFRS 11 states that there are two types of joint arrangements: either a joint operation or a joint venture.

Diagram 5 - Joint operation vs Joint venture

<table>
<thead>
<tr>
<th>Type of Arrangement</th>
<th>Joint operation</th>
<th>Joint venture</th>
</tr>
</thead>
<tbody>
<tr>
<td>Definition</td>
<td>The parties with joint control have rights to the assets and obligations for the liabilities of the arrangement.</td>
<td>The parties with joint control have rights to the net assets of the arrangement.</td>
</tr>
<tr>
<td>Parties with joint control</td>
<td>Joint operator – a party with joint control in a joint operation</td>
<td>Joint venturer – a party with joint control in a joint venture</td>
</tr>
</tbody>
</table>
Type of Arrangement

<table>
<thead>
<tr>
<th>Joint operation</th>
<th>Joint venture</th>
</tr>
</thead>
<tbody>
<tr>
<td>A joint operator accounts for the following in accordance with the applicable IFRS:</td>
<td></td>
</tr>
<tr>
<td>- Its assets, including its share of any assets held jointly</td>
<td></td>
</tr>
<tr>
<td>- Its liabilities, including its share of any liabilities incurred jointly</td>
<td></td>
</tr>
<tr>
<td>- Its revenue from the sale of its share of the output arising from the joint operation</td>
<td></td>
</tr>
<tr>
<td>- Its share of revenue from the sale of the output by the joint operation</td>
<td></td>
</tr>
<tr>
<td>- Its expenses, including its share of any expenses incurred jointly</td>
<td></td>
</tr>
</tbody>
</table>

A joint venturer accounts for its investment in the joint venture using the equity method — proportionate consolidation is not a choice anymore.

Although the term ‘joint venture’ is broadly used in practice, this term is narrowly defined in IFRS 11. Under previous regulations of IAS 31, joint ventures included JCEs, jointly controlled assets and jointly controlled operations, whereas under IFRS 11, a joint venture is only one type of joint arrangement.

Diagram 6 – Similar concepts, different terms

<table>
<thead>
<tr>
<th>Jointly controlled operations</th>
<th>Jointly controlled assets</th>
<th>Jointly controlled entities</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounting: recognise its assets, liabilities, expenses and its shares of income</td>
<td>Accounting: recognise its share of assets, its share of liabilities, its income, its expenses and its share of expenses</td>
<td>Accounting: equity method or proportionate consolidation</td>
</tr>
</tbody>
</table>

Joint operations
The parties that have joint control have rights to the assets and obligations for the liabilities relating to the arrangement.
Accounting: recognise its assets, liabilities, revenue and expenses, and/or its shares of assets, liabilities, revenues and expenses incurred jointly

Joint ventures
The parties that have joint control have rights to the net assets of the arrangement.
Accounting: equity method

Joint arrangements
When classifying a joint arrangement as either a joint operation or a joint venture, the first step is to assess whether there is a separate vehicle. If not, the joint arrangement is automatically a joint operation. However, if there is a separate vehicle, the following factors need to be considered:

- Legal form of the separate vehicle
- Contractual terms and conditions
- Other facts and circumstances

**Diagram 7 – Classifying a joint arrangement**

Is the joint arrangement structured through a separate vehicle?  
- NO

Does the legal form of the separate vehicle give the parties rights to the assets and obligations for the liabilities relating to the arrangement?  
- YES

Do the terms of the contractual arrangement give the parties rights to the assets and obligations for the liabilities relating to the arrangement?  
- NO

Do other facts and circumstances give the parties rights to the assets and obligations for the liabilities relating to the arrangement?  
- YES

When classifying a joint arrangement as either a joint operation or a joint venture, it is critical to understand the purpose and design of the joint arrangement. It is critical to understand whether the joint arrangement:

- Primarily aims to provide the parties with an output (i.e., the parties have rights to substantially all of the economic benefits of the assets)

• Depends on the parties on a continuous basis for settling its liabilities

If both of the above are characteristics of the joint arrangement, then that indicates that it is a joint operation. In some cases, significant judgement will be involved to decide.
Example – Construction and real estate sales

Fact pattern – A separate vehicle is established, over which two parties have joint control. Neither the legal form nor the contractual terms of the joint arrangement give the parties rights to the assets or obligations for the liabilities of the arrangement. Other facts and circumstances are as follows:

- The purpose of the joint arrangement is to construct a residential complex for selling residential units to the public
- Contributed equity by the parties is sufficient to purchase land and raise debt finance from third parties to fund construction
- Sales proceeds will be used as follows (in this priority):
  - Repayment of external debt
  - Remaining profit distributed to parties

Analysis – Since there is a separate vehicle, and because neither the legal form nor the contractual terms of the joint arrangement give the parties rights to the assets or obligations for the liabilities of the vehicle, the preliminary analysis indicates that this is a joint venture. The fact that the parties are the only source of cash flows at inception does not mean that the joint arrangement is a joint operation. Accordingly, there is nothing in the facts and circumstances that suggests the parties have rights to the assets, or obligations for the liabilities, since they only expect to receive any net profits after the external debt is repaid. Therefore, this would be a joint venture.

Variation – The contributed equity is not sufficient to purchase the land and raise debt financing. There is an expectation, or requirement, that the parties will have to contribute cash to the joint arrangement through a series of cash calls. Determining whether the series of cash calls implies that the parties are substantially the only source of cash flows contributing to the arrangement, and therefore, whether the parties have an obligation for the liabilities of the arrangement, (i.e., whether the arrangement is a joint operation) is a matter of judgement. If the joint arrangement gives the parties rights to the net assets, it would be a joint venture.
To sum up it seems that the main impact of IFRS 11 will be felt where proportionate consolidation was used to account for JCEs under IAS 31, and such entities are classified as joint ventures under IFRS 11. This is because the transition to IFRS 11 will result in substantial changes to the financial statements of the joint venturer. Joint ventures must be accounted for using only the equity method under IFRS 11. This will result in recognising only a single line item investment in a joint venture in the statement of financial position, and a single line item for the proportionate share of net income and changes in equity in the statement of comprehensive income. This could potentially be a significant change in the presentation of these areas of the financial statements of affected entities.

3.2.2.4. IFRS 12 - Disclosure of Interests in Other Entities

IFRS 12 combines the disclosure requirements for an entity's interests in subsidiaries, joint arrangements, associates and structured entities into one comprehensive disclosure standard.

In comparison to previous regulations the additional disclosures appears mostly in relation to subsidiaries that are not wholly owned. One of the new requirements of IFRS 12 is that an entity discloses the significant judgements and assumptions it has made (and changes thereto) in determining whether or not it has control over an investee. The requirement in IFRS 12 is more expansive than the requirement in IAS 27, which only required entities to disclose circumstances when: (1) a subsidiary was consolidated and the parent owned less than a majority of voting rights; and (2) an investee was not consolidated, and the investor owned more than a majority of voting rights. This change in the disclosure reflects the degree of judgement that is required to determine whether an entity is controlled, and consequently, consolidated. For example,

Excerpts from IFRS 12:

1. The objective of this IFRS is to require an entity to disclose information that enables users of its financial statements to evaluate:

(a) the nature of, and risks associated with, its interests in other entities; and

(b) the effects of those interests on its financial position, financial performance and cash flows.

3. If the disclosures required by this IFRS, together with disclosures required by other IFRSs, do not meet the objective in paragraph 1, an entity shall disclose whatever additional information is necessary to meet that objective.

4. An entity shall consider the level of detail necessary to satisfy the disclosure objective and how much emphasis to place on each of the requirements in this IFRS. It shall aggregate or disaggregate disclosures so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics.
an entity is required to disclose how it evaluated potential voting rights (e.g., options) and whether it is a principal or an agent.

Similarly additional disclosure requirements arises in relation to significant judgements and assumptions made when determining whether or not the joint control over an arrangement exists. The requirements in IFRS 12 reflects the degree of judgement that is required to determine whether an entity has joint control. The following are examples of significant judgements for which disclosure may be required:

- Whether a right is merely a protective right (which does not give joint control) or a substantive right that gives an entity joint control
- Whether a manager of an arrangement is acting as principal or as agent, which would likely affect the conclusion whether the manager has control or joint control
- Whether a joint arrangement is a joint operation or a joint venture, since its classification is not merely based on legal form under IFRS 11 (as it was under IAS 31)

3.2.3. IFRS 13 Fair value measurements – implications for the real estate sector

IFRS 13 was issued by the International Accounting standards Board in May 2011 and started to be effective for annual periods beginning on or after 1 January 2013. IFRS 13 describes how to measure fair value under IFRS when it is required or permitted by IFRS. The standard does not change when an entity is required to use fair value, but provides a framework for situations where another standard requires or permits fair value measurements.

IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions (i.e. an exit price) regardless of whether that price is directly observable or estimated using another valuation technique.

The fair value measurement assumes that market participants have sufficient knowledge and awareness of the asset or a liability that would be usual and customary in such a market transaction. The definition emphasizes that the fair value should be based on market measurements, maximizing the use of observable market inputs, such as quoted prices. If the observable market inputs are not available, other valuation techniques should be applied.

IFRS 13 does not prescribe which valuation technique must be used in a particular circumstance. The valuation technique used to measure fair value should be appropriate for the circumstances, and one for which sufficient data is available. Valuation techniques that are typically used include the market approach, the income approach and the cost approach. The market approach uses prices and other relevant information generated by
market transactions involving identical or comparable assets. In income approach, the valuation is based on estimated future income and profit or cash flows. The cost approach reflects the amount that currently would be required to replace the service capacity of an asset (often referred to as current replacement cost).

Real estate entities may be affected by IFRS 13 in various aspects of their business when:

- Measuring property interests at fair value
- Testing property interests for impairment
- Determining the fair value of identifiable assets and liabilities as part of the purchase price allocation applied in a business combination
- Measuring an interest in a real estate joint venture or associate at fair value
- Compiling and disclosing information on the fair values of property interests, including but not limited to significant assumptions, adjustments to unobservable inputs and qualitative and quantitative sensitivity analysis.

Regardless of whether valuations are performed externally or internally, management must understand the methodologies and assumptions used in the valuations and determine whether the assumptions are reasonable and consistent with the requirements of IFRS 13.

IFRS 13 requires an entity to maximize the use of relevant observable inputs and minimize the use of unobservable inputs. IFRS 13 also includes a fair value hierarchy based on the inputs used to determine fair value as follows:

- Level 1 - quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 - inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 - unobservable inputs (valuation techniques that do not make use of observable inputs).

Many of the IFRS 13 disclosures are required for each class of assets (and liabilities). IFRS 13 requires these classes of assets (and liabilities) be determined based on:

(a) the nature, characteristics and risks of the asset or liability; and

(b) the level of the fair value hierarchy within which the fair value measurement is categorised.

The determination of the appropriate class of assets will require significant judgement. At one end of the spectrum, the properties in an operating segment (as defined by IFRS 8 Operating Segments) may be a class of assets for the purpose of the disclosures required by IFRS 13. This may be the case even if there is a large number of properties in the segment, if the properties have the same risk profile (e.g., the segment comprises residential properties in countries with property markets of similar characteristics). At the other end of the spectrum, IFRS 13 disclosures may be
required for individual properties or small groups of properties if the individual properties or groups of properties have different risk profiles (e.g., a real estate entity with two properties – an office building in a developed country and a shopping centre in a developing country).

The previous requirements in IAS 40 for how fair value is determined have been replaced by the requirements in IFRS 13. However, certain disclosure requirements under IAS 40 will remain effective. The new disclosures are to be applied prospectively for annual periods commencing on 1 January 2013. The new disclosures will not require comparative data.

Illustrative set of disclosures for a real estate entity that has investment properties measured at fair value on its statement of financial position, in its first set of financial statements following the adoption of IFRS 13 is presented below.

<table>
<thead>
<tr>
<th>Disclosures</th>
<th>IFRS 13 New requirements</th>
<th>IFRS 13 Old requirements</th>
<th>IAS 40 New requirements</th>
<th>IAS 40 Old requirements</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fair value at the end of the reporting period</td>
<td>Required</td>
<td>Required</td>
<td>Required</td>
<td>Required</td>
</tr>
<tr>
<td>Level of the fair value hierarchy within which the fair value measurement in its entirety is categorised</td>
<td>Required</td>
<td>Not required</td>
<td>Required</td>
<td>Not required</td>
</tr>
<tr>
<td>For Level 2 and Level 3 measurements, valuation technique and the inputs used, and changes in the valuation technique, if applicable, and the reasons for those changes</td>
<td>Required</td>
<td>Not required</td>
<td>Required</td>
<td>Not required</td>
</tr>
<tr>
<td>For Level 3 measurements, quantitative information regarding the significant unobservable inputs</td>
<td>Required</td>
<td>Not required</td>
<td>Not required</td>
<td>Not required</td>
</tr>
<tr>
<td>Amount of transfers between Level 1 and Level 2, the reasons and related accounting policies</td>
<td>Required</td>
<td>Not required</td>
<td>Not required</td>
<td>Not required</td>
</tr>
<tr>
<td>For Level 3 measurements, reconciliation from the opening balances to the closing balances (including gains and losses, purchases, sales, issues, settlements, transfers in and out of Level 3 and reasons and policies for transfer and where all such amounts are recognised)</td>
<td>Required</td>
<td>Required</td>
<td>Not required</td>
<td>Not required</td>
</tr>
<tr>
<td>For Level 3 measurements, the total gains or losses included in profit or loss that are attributable to the change in unrealised gains or losses relating to those assets and liabilities held at the reporting date, and a description of where such amounts are recognised</td>
<td>Required</td>
<td>Required</td>
<td>Not required</td>
<td>Not required</td>
</tr>
<tr>
<td>Disclosures</td>
<td>IFRS 13 New requirements</td>
<td>IFRS 13 Old requirements</td>
<td>IAS 40 New requirements</td>
<td>IAS 40 Old requirements</td>
</tr>
<tr>
<td>---------------------------------------------------------------------------</td>
<td>---------------------------</td>
<td>--------------------------</td>
<td>--------------------------</td>
<td>--------------------------</td>
</tr>
<tr>
<td>For Level 3 measurements, a description of the valuation processes used by the entity</td>
<td>Required</td>
<td>Not required</td>
<td>Not required</td>
<td>Not required</td>
</tr>
<tr>
<td>For Level 3 measurements, a narrative description of the sensitivity of the fair value measurement to changes in unobservable inputs if a change in those inputs might result in a significantly different amount and, if applicable, a description of interrelationships between those inputs and other unobservable inputs and of how they might magnify or mitigate the effect of changes in the unobservable inputs</td>
<td>Required</td>
<td>Not required</td>
<td>Not required</td>
<td>Not required</td>
</tr>
<tr>
<td>If the highest and best use of a non-financial asset differs from its current use, disclose that fact and the reason for it</td>
<td>Required</td>
<td>Not required</td>
<td>Required</td>
<td>Not required</td>
</tr>
</tbody>
</table>
3.3. Selected IFRS issues and their implications for real estate entities

3.3.1. Bank covenants

With significant number of real estate loans maturing in Europe in the next years, the financing and refinancing of property activities is still one of the key challenges for the real estate sector and should, inevitably, be one of the key attention items in financial reporting. Taking the above into consideration, the appropriate covenants disclosures in the financial statements are key to provide to the recipients of the financials significant information about liquidity of the company. International Financial Reporting Standards describe which disclosures are required, however the companies should consider any other information that may be valuable for the readers and are perceived on the market as a good practice.

IFRS 7:

“18 For loans payable recognized at the end of the reporting period, an entity shall disclose:

(a) details of any defaults during the period of principal, interest, sinking fund, or redemption terms of those loans payable;

(b) the carrying amount of the loans payable in default at the end of the reporting period; and

(c) whether the default was remedied, or the terms of the loans payable were renegotiated, before the financial statements were authorized for issue.

19 If, during the period, there were breaches of loan agreement terms other than those described in paragraph 18, an entity shall disclose the same information as required by paragraph 18 if those breaches permitted the lender to demand accelerated repayment (unless the breaches were remedied, or the terms of the loan were renegotiated, on or before the end of the reporting period).”
Below we present some of the leading practices in disclosing the financial debt covenants in the financial statements.

**Company A** disclosed a table with a breakdown of all loans, including all applicable covenants.

<table>
<thead>
<tr>
<th>Loan type</th>
<th>Transaction</th>
<th>Carrying amount 31.12.2012 (€/000)</th>
<th>No. of properties used as security</th>
<th>Market value 31.12.2012 of properties used as security [€]</th>
<th>Final due date</th>
<th>Reimbursement</th>
<th>Financial covenants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mortgage loan</td>
<td>Montenero shopping mall, Bisaccia</td>
<td>17,352</td>
<td>1</td>
<td>31,910</td>
<td>02-Apr-13</td>
<td>annual repayment of € 1.4 million with final balloon of € 17.4 million</td>
<td>N/A</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>FIAT portfolio</td>
<td>45,604</td>
<td>3</td>
<td>121,090</td>
<td>30-Jun-15</td>
<td>annual repayment of € 2.4 million with final balloon of € 40.3 million</td>
<td>LTV (= 70% DSA) &gt;= 10%</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Comit Pension Fund Portfolio</td>
<td>162,438</td>
<td>10</td>
<td>281,570</td>
<td>19-Dec-15</td>
<td>Bullet</td>
<td>LTV &lt;= 80%</td>
</tr>
<tr>
<td>Mortgage current account</td>
<td>RGD - IGD (50% BS)- Darsena</td>
<td>16,529</td>
<td>1</td>
<td>18,875</td>
<td>30-Nov-12</td>
<td>Bullet</td>
<td>Debt/Equity &lt;= 5</td>
</tr>
<tr>
<td>Mortgage current account</td>
<td>Property in Beinasco</td>
<td>6,176</td>
<td>1</td>
<td>9,770</td>
<td>21-Dec-15</td>
<td>Bullet</td>
<td>N/A</td>
</tr>
<tr>
<td>Mortgage current account</td>
<td>Property in Beinasco</td>
<td>21,714</td>
<td>1</td>
<td>37,630</td>
<td>21-Dec-15</td>
<td>Bullet</td>
<td>N/A</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Fondo Immobili Pubblici portfolio</td>
<td>88,826</td>
<td>13</td>
<td>126,469</td>
<td>24-Apr-13</td>
<td>Bullet</td>
<td>LTV &lt;= 70% Consolidated LTV &lt;= 65% ICR &gt;= 1.1</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Property in Corso Matteotti, 4-6 – Milan</td>
<td>61,342</td>
<td>1</td>
<td>107,330</td>
<td>2-Aug-15</td>
<td>annual repayment of € 2.0 million with final balloon of € 58.0 million</td>
<td>LTV &lt;= 60% ICR Until 2/08/13 &gt;=120% then 150%</td>
</tr>
<tr>
<td>Bonds</td>
<td>Telecom properties of the Imser 60 securitisation (*)</td>
<td>521,547</td>
<td>177</td>
<td>1,796,103</td>
<td>20-Sep-21</td>
<td>repayment plan as described below (***))</td>
<td>LTV &lt;= 80%, ICR &gt;=159% (<strong>)) LTV= 80% ICR &gt;= 1.59 (</strong>*)</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Various properties in major Italian Cities (Project Office)</td>
<td>65,897</td>
<td>5</td>
<td>126,450</td>
<td>28-Jul-14</td>
<td>annual repayment of € 2.5 million with final balloon of € 62.5 million</td>
<td>LTV &lt;= 60% ICR &gt;= 1.300</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Property in via Messina, 38 - Milan</td>
<td>14,594</td>
<td>1</td>
<td>22,700</td>
<td>19-Nov-14</td>
<td>Bullet</td>
<td>LTV &lt;= 65% ICR &gt;= 1.7</td>
</tr>
<tr>
<td>Loan type</td>
<td>Transaction</td>
<td>Carrying amount 31.12.2012 (€/000)</td>
<td>No. of properties used as security</td>
<td>Market value 31.12.2012 of properties used as security [€]</td>
<td>Final due date</td>
<td>Reimbursement</td>
<td>Financial covenants</td>
</tr>
<tr>
<td>------------</td>
<td>-------------------------------</td>
<td>-----------------------------------</td>
<td>-----------------------------------</td>
<td>-------------------------------------------------------------</td>
<td>---------------</td>
<td>-----------------------------------</td>
<td>----------------------------------------------------------</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Property in Nerviano</td>
<td>27,946</td>
<td>1</td>
<td>55,920</td>
<td>31-Dec-16</td>
<td>annual repayment of € 1.9 million with final balloon of € 21 million</td>
<td>N/A</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Property in Galeria del Corso, 4 - Milan</td>
<td>44,553</td>
<td>1</td>
<td>84,230</td>
<td>4-Aug-15</td>
<td>Bullet</td>
<td>Property LTV &lt;= 65% LTV BS &lt;=75% ICR IMMOBILE from &gt;=1.15 to &gt;=1.20 from 30/06/13 ICR BS &gt;=1.30</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Properties in Rozzano -Milanofiori and via Pergolesi - Milan</td>
<td>56,758</td>
<td>2</td>
<td>88,630</td>
<td>29-Dec-15</td>
<td>Bullet</td>
<td>ICR &gt;= 170% - LTV &lt;= (70%Y1-Y3 -65% Y4- 60 Y5)- Consolidated LTV &lt;= 65%</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Property in Corso Marconi, 10 Turin</td>
<td>14,634</td>
<td>1</td>
<td>34,540</td>
<td>24-Feb-15</td>
<td>annual repayment of € 0.3 million, € 0.75 million from March 2013 and final balloon of € 13.2 million</td>
<td>N/A</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Property in via Volta, 5 - Varese</td>
<td>12,456</td>
<td>1</td>
<td>20,800</td>
<td>31-Dec-16</td>
<td>Bullet</td>
<td>N/A</td>
</tr>
<tr>
<td>Mortgage loan</td>
<td>Property in Piazza Sigmund Freud, Milan</td>
<td>141,130</td>
<td>1</td>
<td>252,360</td>
<td>27-Jul-16</td>
<td>Bullet</td>
<td>LTV &lt;= 65% Consolidated LTV &lt;= 60% ICR &gt;= 110% Consolidated ICR &gt;= 140%</td>
</tr>
</tbody>
</table>

2012 Annual financial report of Beni Stabili S.p.A. SIIQ
Company B disclosed a table showing the loan covenants and the level of compliance as at 31 December 2012:

<table>
<thead>
<tr>
<th>Financing</th>
<th>Ratios/covenants</th>
<th>Limit(1)</th>
<th>12/31/2012</th>
<th>12/31/2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Syndicated loans and bilateral loans Klepierre SA</td>
<td>Net debt/Value of holdings (Loan-to-Value)</td>
<td>≤ 60%</td>
<td>43.6%</td>
<td>45.8%</td>
</tr>
<tr>
<td></td>
<td>EBIT DA/Net interest expenses</td>
<td>≥ 2.0</td>
<td>2.6</td>
<td>2.5</td>
</tr>
<tr>
<td></td>
<td>Secured debt/Value of holdings</td>
<td>≤ 20%</td>
<td>15.7%</td>
<td>14.5%</td>
</tr>
<tr>
<td></td>
<td>Value of holdings, group share</td>
<td>≥ €6 Bn</td>
<td>€13.1 Bn</td>
<td>€13.2 Bn</td>
</tr>
<tr>
<td>Bond issues Klepierre SA</td>
<td>Ratio of financings of subsidiaries (excluding Steen &amp; Strom) over total gross financial debt</td>
<td>≤ 30%</td>
<td>3.6%</td>
<td>7.9%</td>
</tr>
<tr>
<td></td>
<td>Secured debt/Revalued Net Asset Value (excluding Steen &amp; Strom)(2)</td>
<td>≤ 50%</td>
<td>9.0%</td>
<td>9.2%</td>
</tr>
</tbody>
</table>

(1) Most constraining contract limit.
(2) NAV including transfer duties after deferred tax.

Kleppiere 2012 Annual Report

Additional disclosure that is not required by IFRS 7 (as presented above) but is considered to be good practice is sensitivity analyses with respect to the applicable covenants. It is recommended to include information about impact of a rational change in the operating ratios (e.g. fair value of properties) on the financial covenants as well as a terminal values of these ratios, that would lead to breach of covenants.

Below we present the sample disclosure that give the information about headroom between the entity’s operating ratios and its minimum financial covenants:

„The Group tested its compliance with its financial covenants regularly and operated comfortably within these limits throughout 201X. Property values could decline by 50% at the balance sheet date before there would be a breach of financial covenants.

In case of breaching one or more covenants the entity’s management would be required to disclose additional information as described in point 18 (b) and 19 of IFRS 7. If breaches in meeting the financial covenants permit the bank to immediately call loans and borrowings, the company is obliged to present that part of a loan as a current liability in its statement of financial position as at year end. The current or non-current classification of loans may directly impact the perceived and real liquidity of the entity, especially where loan covenants are breached. That is why the management should determine that appropriate waivers are obtained prior to year-end to support any current...
classification of the liability as well as assess the impact of waivers obtained prior to the year-end, and whether they effectively provide a period of grace ending at least 12 months after the reporting period.”

3.3.2 IFRS 10 Consolidated Financial Statements – implications for fund managers

Recently issued IFRS 10 Consolidated Financial Statements has a significant impact on the consolidation process of the real estate investment funds and fund managers accounting for their funds. Determining whether or not a fund managers have to consolidate their managed funds has long been an issue. The new standard have changed how fund managers shall assess the funds they manage for consolidation. It is likely to change the number of funds that are consolidated as fund managers may reach differing consolidation conclusions over funds they manage compared with their previous practice.

The new definition of control included in IFRS 10 (further discussed in Chapter 3.2.2.2) may lead to consolidation of entities that were not previously included in the group, potentially resulting in more assets and liabilities on the books. As a result asset or fund managers may be obliged in certain circumstances to consolidate the asset or funds into their own financial statements in a situation when they have:

- power over the investee,
- exposure, or rights, to variable returns from its involvement with the investee,
- ability to use its power over the investee to affect the amount of the returns to the asset manager.

In most cases, it is clear when all three criteria have been met. However, careful consideration will be required to assess whether an asset manager acts as a principal (and, therefore, may need to consolidate the fund) or as an agent (in which case, it recognizes only its direct interest and its management fee).

The factors to be considered include, but are not limited to:

- Scope of the asset manager’s decision making authority (An asset manager does not usually have discretion to make changes either to the activities that it is permitted to direct, or to the decisions that it is permitted to make without the prior approval of the other investors in the fund. This would generally indicate that it is an agent acting in a fiduciary capacity. However, consideration must also be given to the level of involvement the asset manager has in determining the scope of its authority: that involvement may indicate that the asset manager has the opportunity and incentive to obtain the ability to direct the relevant activities, which could indicate that the asset manager is a principal.)

- Rights held by others (If one party (investor) holds a removal right (that is, a single investor can decide to kick out the asset manager), and that right is substantive, then the asset manager is...
considered an agent. However, if their exercise requires agreement by more than one party, then it is not conclusive as to whether the asset manager is a principal or an agent. The more investors that would have to agree to remove the asset manager, the less important that removal right is, when determining if the asset manager is a principal);

- Exposure to variability in returns through the remuneration of the asset manager (If the fee received is commensurate with the services provided, and the arrangement includes ‘market’ terms, the asset manager is likely to be considered an agent. However, the greater the fee, and exposure to variability, relative to the expected returns from the investee (the fund), the more likely it is that the asset manager is a principal, and would consolidate the underlying investments).

- Variable returns held through other interests (When an asset manager holds other interests in an investee, which is not uncommon in the real estate industry, this may indicate that it is not an agent. By virtue of holding other interests, decisions made by the asset manager may differ from those it would have made if it did not hold those other interests. For instance, this may be the case when an asset manager provides credit enhancement to the fund, or holds a large direct interest.)

IFRS 10 includes the following examples that highlight all four factors discussed above, but, in particular, they illustrate how third party rights and variability of total returns should be qualitatively considered in the assessment of a principal/agent relationship. In general, the examples demonstrate that the more easily the fund manager can be removed, the higher a level of exposure to variability of returns will be required before the entity would conclude it is acting as a principal. Although these examples provide guidance on assessing a principal/agent relationship, they are not intended to create ‘bright lines’ but, rather, are for illustrative purposes only.

<table>
<thead>
<tr>
<th>Example (IFRS 10 reference)</th>
<th>Scope of decision making rights</th>
<th>3rd party rights to remove fund manager</th>
<th>Remuneration</th>
<th>Other interests</th>
<th>Principal/Agent</th>
</tr>
</thead>
<tbody>
<tr>
<td>13</td>
<td>Narrowly defined remit</td>
<td>None</td>
<td>1% of net asset value</td>
<td>10% direct interest</td>
<td>Agent</td>
</tr>
<tr>
<td>14A</td>
<td>Wide ranging discretion</td>
<td>Removal for cause</td>
<td>1% of net asset value and 20% of profits after a hurdle is reached</td>
<td>2% direct interest</td>
<td>Agent</td>
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</tbody>
</table>
3.3.3 Accounting for investment property under construction

2009 was the first year that companies had to apply the amendment to IAS 40 that includes investment properties under construction. As a result of this amendment, companies that measure their investment properties at fair value also need to measure their investment properties under construction at fair value unless the fair value is not reliably determinable. IAS 40 paragraph 53 states the following: “If an entity determines that the fair value of an investment property under construction is not reliably determinable but expects the fair value of the property to be reliably determinable when construction is complete, it shall measure that investment property under construction at cost until either its fair value becomes reliably determinable or construction is completed (whichever is earlier).”

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 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 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 straightforward 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.
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The range of her expertise covers conducting legal due diligence and providing legal advice in connection with M&A transactions and restructuring projects. She has strong experience in providing legal support related to the real estate matters including the real estate due diligence and the transactions of the real estate acquisitions (i.e. both the asset and the share deal transactions). She also supports clients in drafting and negotiating the lease agreements and the management contracts of commercial and industrial spaces.
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Katarzyna Kłaczyńska, LL.M., is an attorney specializing in energy and environmental matters. She has advised on a number of high-profile regulatory projects, including acting as a leading counsel for power sector companies and the Polish government regarding climate change regulations and developing advocacy strategy concerning revision of the current Environmental Impact Assessment model on behalf of the Business Association of Polish Power Plants. She has worked on a number of environmental and regulatory due diligence projects for the variety of sectors. She is also experienced in environmental aspects of shale gas investments.

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

<table>
<thead>
<tr>
<th>Country</th>
<th>Dividends (%)</th>
<th>Interest (%)</th>
<th>Royalties (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>5/10 (d)</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td>Algeria (gg)</td>
<td>5/15 (d)</td>
<td>0/10 (k)</td>
<td>10</td>
</tr>
<tr>
<td>Armenia</td>
<td>10</td>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td>Australia</td>
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<td>10</td>
<td>10</td>
</tr>
<tr>
<td>Austria</td>
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<td>0/5 (k)</td>
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<tr>
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<td>10</td>
<td>10</td>
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<td>Bangladesh</td>
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<td>0/10 (k)</td>
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1 Generally effective 1 January 2014.
<table>
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<th>Royalties (%)</th>
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<td>0/10 (k)</td>
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<tr>
<td>Country</td>
<td>Dividends (%)</td>
<td>Interest (%)</td>
<td>Royalties (%)</td>
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<td>0/10 (f)</td>
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<td>0/5/10 (mm)</td>
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<td>19 (t)</td>
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<td>5/15 (f)</td>
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<td>United States</td>
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<td>0/15 (k)</td>
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<td>Nontreaty countries</td>
<td>19</td>
<td>20</td>
<td>20 (x)</td>
</tr>
</tbody>
</table>

(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 copyright, 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 company paying the dividends. The 5% rate applies to dividends paid to 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 lower 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 withholding tax rates listed in the table are effective from 1 September 2013.

(jj) The lower rate applies if the recipient of the dividends is a company (other than a partnership) that owns directly at least 10% of the payer. Certain limitations to the 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) The 0% rate applies to dividends paid to a company (other than a partnership) that 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-months. The 0% rate may also apply to dividends paid to certain pensions funds.

(mm) The 10% rate applies to interest paid before 1 July 2013. For interest paid on or after 1 July 2013, the 5% rate applies unless an exemption applies. The 0% rate applies to such interest if any of the following conditions is satisfied:

• the beneficial owner of the interest is a company (other than a partnership) that holds directly at least 25% share capital of the payer of the interest.
• the payer of the interest holds directly at least 25% of the share capital of the beneficial owner of the interest.
• an EU/EEA company holds directly at least 25% of the share capital of both the beneficial owner of the interest and the payer of the interest.

(nn) For royalties paid before 1 July 2013, the 10% rate applies if Switzerland imposes in its local provisions a withholding tax on royalties paid to nonresidents. Otherwise, a 0% applies. For royalties paid on or after 1 July 2013, a 5% rate applies unless an exemption applies. The 0% rate applies to such royalties if any of the following conditions is satisfied:

• the beneficial owner of the royalties is a company (other than a partnership) that holds directly at least 25% of the share capital of the payer of the royalties.
- the payer of the royalties holds directly at least 25% of the share capital of the beneficial owner of the royalties.
- an EU/EEA company holds directly at least 25% of the share capital of both the beneficial owner of the royalties and the payer of the royalties.

Furthermore, if Poland enters into an agreement with an EU or EEA country that allows it to apply a rate that is lower than 5%, such lower rate will also apply to royalties paid between Poland and Switzerland.

(oo) The lower rate applies if the beneficial owner is a company (other than a partnership) that holds directly at least 10% of the capital of the company paying the dividends for an uninterrupted period of 24 months.

(pp) The 0% rate applies to:
- interest arising in Poland and paid to a resident of Canada with respect of a loan made, guaranteed or insured by Export Development Canada, or a credit extended, guaranteed or insured by Export Development Canada,
- interest arising in Canada and paid to a resident of Poland with respect of a loan made, guaranteed or insured by an export financing organization that is wholly owned by the State of Poland, or a credit extended, guaranteed or insured by an export financing organization that is wholly owned by the State of Poland,
- interest arising in Poland or Canada and paid to a resident of the other Contracting State in respect of indebtedness arising as a result of the sale by a resident of the other Contracting State of any equipment, merchandise or services (unless the sale of indebtedness is between related parties or where the beneficial owner of the interest is a person other than the vendor or a person related to the vendor).

(qq) The lower rate applies to copyright royalties and similar payments with respect of the production or reproduction of literary, dramatic, musical or artistic work and royalties for the use of, or the right to use, any patent or for information concerning industrial, commercial or scientific experience (with some exceptions).

(rr) The agreement with the Socialist Federal Republic of Yugoslavia should apply to Bosnia-Herzegovina.

(ss) The 5% rate applies if the recipient is a company (other than a partnership) that holds directly at least 25% of the capital of the company paying the dividends.
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