This guide to the Polish real estate market was prepared by EY, a global leader in assurance, tax, transaction, advisory and legal services. It 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 market 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 recommended to seek up-to-date and detailed information on the commercial climate at the time of considering your investment, as this can change at any time. Unless stated otherwise, this guide reflects information valid as at January 2019.
Polish Real Estate Market
Poland is the most developed, diversified and mature economy across Central and Eastern Europe. Poland holds the leading position in the CEE region in terms of GDP (about €495bn in 2018 according to estimation of European Commission) which is the effect of growing wealth of society, high level of consumption and positive situation on the labour market.

**Poland in a Nutshell**

- **Population**: 38.4m, The largest population across the CEE markets
- **EU funds**: €120.1bn, The largest beneficiary of EU funding (2014-2020)
- **Inflow of FDI**: $8.1bn, Poland has joined the group of the top 20 FDI receivers in the world
- **Top BPO/SSC/R&D location**: 1,200 centres, employing 280,000 people
The Polish economy is one of the most sustainable ones within the EU with positive mid-term outlook. Poland was the only country within the EU to avoid recession over 2008-2010 and has been outpacing EU-average GDP growth for many years.

GDP growth in 2017

4.8%

vs. 2.5% in Euro Zone

One of the fastest GDP growth rates in the EU

Forecasted GDP

2018
4.7%

2019
3.9%

2020
3.6%
While Warsaw continues to be the country’s key business centre, Poland has many strong regional clusters. Cities such as Cracow, Wrocław, Łódź, Tri-City (Gdańsk, Gdynia, Sopot), Poznań and the Katowice conurbation have developed business-friendly environment and have attracted many foreign investors.

<table>
<thead>
<tr>
<th>City</th>
<th>Population</th>
<th>Unemployment Rate</th>
<th>Monthly Salaries</th>
<th>No. of Students</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warsaw</td>
<td>538k</td>
<td>1.2%</td>
<td>€1,288k</td>
<td>€123k</td>
</tr>
<tr>
<td>Poznan</td>
<td>1,288k</td>
<td>1.5%</td>
<td>€1,770k</td>
<td>747k</td>
</tr>
<tr>
<td>Krakow</td>
<td>770k</td>
<td>2.5%</td>
<td>€688k</td>
<td>1,236k</td>
</tr>
<tr>
<td>Lodz</td>
<td>1,454k</td>
<td>1.9%</td>
<td>€1,091k</td>
<td>€158k</td>
</tr>
<tr>
<td>Gdansk</td>
<td>1,204k</td>
<td>1.7%</td>
<td>€295k</td>
<td>259k</td>
</tr>
<tr>
<td>Sopot</td>
<td>123k</td>
<td>1.5%</td>
<td>€1,407k</td>
<td>118k</td>
</tr>
<tr>
<td>Katowice</td>
<td>538k</td>
<td>1.7%</td>
<td>€639k</td>
<td>1,370k</td>
</tr>
</tbody>
</table>

(1) as of June 2018
(2) as of November 2018
(3) as of 2017 for voivodeship
Poland ranks high in terms of investment attractiveness among manufacturing companies as well as business service providers, which has been confirmed by a number of rankings as well as investment placements. Investor confidence has been confirmed by the following facts:

Poland holds 5th position in EY’s European Attractiveness Survey 2018 in terms of jobs created, and 9th position in terms of the number of FDI projects.

Poland may become a beneficiary of BREXIT, attracting financial institutions and other business services that are considering a move away from London. First company which decides to move its services is JP Morgan Chase.

Kraków has taken 6th place in Top 100 Super Cities of Tholon’s Services Globalization Index 2018, which considers innovation, startup ecosystem and digital transformation as key drivers.

In September 2018 status of Poland was upgraded by FTSE Russell Index to Developed from Advanced Emerging. Thanks to this upgrade, Poland joined the most developed economies. Moreover, S&P set Poland’s long-term foreign currency credit rating to A-.

Poland’s student population exceeding 1.5 million drew companies such as Samsung Electronics, Delphi Automotive, BSH, Sanofi, GE Engineering Design Center, ABB, Intel, Google, Unilever to open their R&D centres in the country.

PropTech solutions are gaining popularity. Smart solutions are becoming popular especially in the office sector. Following the office sector, such innovations can be implemented in the industrial market (automation in logistics) and retail sector (omnichannel).
Net prime yields in selected European cities, 2018

<table>
<thead>
<tr>
<th>City</th>
<th>Office</th>
<th>Retail</th>
<th>Warehouse</th>
</tr>
</thead>
<tbody>
<tr>
<td>London</td>
<td>3.7%</td>
<td>2.3%</td>
<td>3.7%</td>
</tr>
<tr>
<td>Madrid</td>
<td>3.4%</td>
<td>3.3%</td>
<td>5.6%</td>
</tr>
<tr>
<td>Paris</td>
<td>3.1%</td>
<td>2.8%</td>
<td>4.7%</td>
</tr>
<tr>
<td>Milan</td>
<td>3.6%</td>
<td>3.5%</td>
<td>5.8%</td>
</tr>
<tr>
<td>Amsterdam</td>
<td>3.3%</td>
<td>2.8%</td>
<td>4.7%</td>
</tr>
<tr>
<td>Stockholm</td>
<td>3.4%</td>
<td>3.7%</td>
<td>5.3%</td>
</tr>
<tr>
<td>Warsaw</td>
<td>5.0%</td>
<td>4.9%</td>
<td>6.5%</td>
</tr>
</tbody>
</table>

Poland. The real state of real estate
Poland is also the largest CEE market (excluding Russia) in terms of volume of modern real estate stock. The pipeline supply remains high, supported by strong occupier demand.
At the end of 2018 the total stock of modern office space in Warsaw and regional cities reached 10.4m m². Warsaw dominates the office market with the most development, letting and investment activity. Yet, regional cities also play an important role, serving primarily as Business Process Outsourcing (BPO)/Shared Services Centre (SSC)/Research & Development (R&D) centres.
Encouraged by favourable financing conditions, positive economic performance and good prospects, all of the sector stakeholders are bullish about the future of the office market in Poland. In view of stable vacancy levels and rental rates, developers are commencing new projects, occupiers are expanding, while investors are eying up and pursuing opportunities not only in the capital, but also in the regional markets.

<table>
<thead>
<tr>
<th>City</th>
<th>Stock (m²)</th>
<th>Pipeline supply (m²)</th>
<th>Vacancy rate</th>
<th>Prime rental range (€/m²/month)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warsaw</td>
<td>5 455 000</td>
<td>750 000</td>
<td>8.7%</td>
<td>20-24</td>
</tr>
<tr>
<td>Kraków</td>
<td>1 255 000</td>
<td>280 000</td>
<td>8.5%</td>
<td>14-15</td>
</tr>
<tr>
<td>Wrocław</td>
<td>1 055 000</td>
<td>220 000</td>
<td>9.0%</td>
<td>14-15</td>
</tr>
<tr>
<td>Tri-City</td>
<td>775 000</td>
<td>175 000</td>
<td>6.2%</td>
<td>13-14</td>
</tr>
<tr>
<td>Łódź</td>
<td>469 000</td>
<td>80 000</td>
<td>8.8%</td>
<td>11.5-12.5</td>
</tr>
<tr>
<td>Katowice</td>
<td>519 000</td>
<td>60 000</td>
<td>8.9%</td>
<td>12.5-13.5</td>
</tr>
<tr>
<td>Poznań</td>
<td>479 000</td>
<td>80 000</td>
<td>7.4%</td>
<td>12-13.5</td>
</tr>
</tbody>
</table>
Trends

Office rents remain stable on both regional and Warsaw market despite different market conditions.

Due to the fact that most of big projects in Warsaw are under construction, level of new supply in 2018 was relatively low. Therefore, strong demand causes a decrease in vacancy rates without impact on rents. On regional markets high level of developers’ activity causes slightly increase of vacant office space, but in combination with strong demand, rents remain stable.

Growing importance of co-working spaces.

Following tenants’ needs for more flexible office space, many co-working operators open their offices, especially in Warsaw. They usually choose A-class office buildings in attractive locations. Such spaces are rented not only by freelancers and start-ups, but also multinational companies. This trend shows changing habits of occupiers focusing on workspaces that enables cooperation on a bigger scale and stimulates creativity and effectiveness.

Increasing construction costs may lead to growth of rents in the long term.

Office market has been experiencing the increase of construction costs, especially land costs, cost of labour and materials. Developers and investors may try to draft these costs to tenants by increasing rents.
**Further expansion of SSC in regional cities.**

Expansion of SSC is a driving factor for office market in regional cities. Beyond biggest regional markets, developers are interested in smaller ones, like Rzeszów, Częstochowa or Toruń which are characterized by lower operating costs and labor force accessibility.

**PropTech and WaaS.**

PropTech and WaaS (workplace as a service) have been gaining popularity. Smart solutions in the office space and flexible workspaces will be introduced on a larger scale in the upcoming years. Due to such changes, more impact will be put on targeting needs of potential individual clients.
Focus on cities

Warsaw

City Centre
1,260,000
5.40%
€18.00-19.50

North
105,000
2.00%
€14.25-14.75

Central Business District
880,000
5.40%
€22.50-24.00

East
235,000
9.50%
€13.50-14.50

Jerozolimskie Corridor
700,000
7.00%
€14.00-14.50

Mokotów
1,430,000
15.50%
€13.50-14.50

West
225,000
6.00%
€14.00-14.50

Żwirki i Wigury
290,000
12.00%
€14.00-14.50

Ursynów/Wilanów
127,000
4.50%
€14.25-14.75

Puławska
200,000
7.80%
€14.25-14.75

Poland. The real state of real estate
Supply of office space across the city stands at 5.45m m². About 750,000 m² is currently under construction. It is forecasted to bring 250,000 m² of new office supply in 2019, one year later about 600,000 m².

Letting activity in the CBD and City Centre accounted for 47% of total volume.

Gross take-up in 2018 reached a high level of 850,000 m², up by 4% y/y. 12-month gross take-up stands at 850,000 m². Lease renewals accounted for ca. 27% of total take-up, whereas the volume of pre-leases totalled 67,200 m² or 17% of volume of letting activity.

The vacancy rate decreased to 8.7%, which is 3.5pp lower when compared to 2017. The highest vacancy rate was recorded along in the Mokotów, which shows decreasing interest of tenants in this district. The lowest rate of 2.0% was seen in the North zone, which is one of the smallest in terms of office supply.

Prime rents in schemes located in the CBD range from €21.00 per m²/month up to €20-23.5 per m²/month for top floors in tower buildings. Prime rents in Upper South range between €13.50 and 14.50 per m²/month.
Forecast for Warsaw

Prime rents are forecasted to slightly increase in the long-term, due to growing construction costs.

Due to the output gap, vacancy rate will remain low at least till the end of H1 2019.

The Wola district will continue to attract the majority of occupiers at the expense of Służewiec which is facing structural vacancy with possible conversion of function in the mid-term horizon.
1.3 Retail Market Snapshot

**Modern Retail Stock**

Over 14.3m m²

**Average density per 1,000 inhabitants**

311 m²

**Average vacancy rate in 6 major cities**

3.9%

**New supply (2018)**

430,000 m²

**Under construction**

Almost 270,000 m²

**Prime rent in Warsaw**

€110-130 m²/month

**Prime rent in major agglomerations**

€40-60 m²/month

**Average purchasing power per inhabitant Poland / Warsaw**

€7,200 / €12,500

Poland. The real state of real estate
New retail schemes delivered to the market in 2018 totalled 430,000 m² and the aggregate modern retail stock exceeded 14.3m m². Additionally, more than 480,000 m² is currently under construction due for delivery by end of 2021.
The bulk of new supply, with large retail schemes currently under construction, is located in key markets. Further development of the modern retail sector will continue in medium and small-size cities, however the type of new retail accommodation will be mainly driven by convenience and leisure element.

While the average density rate for Poland stood at 311 m$^2$ / 1,000 inhabitants at the end of the year, there are major differences among individual cities. Some of them are clearly reaching a saturation point with density rates over 750 m$^2$ / 1,000 inhabitants.
Retailers show strong demand for prime retail locations, while in many cases restructuring their networks in secondary and tertiary locations. Interest in secondary assets is clearly shaped by local retail sector fundamentals.

Rents in top shopping centres tended to stabilize over the year, but still there was large gap between prime rental levels in Warsaw (€110-130 per m²/month) and other cities (€40-60 per m²/month). Rent differences are also prominent when comparing rents in shopping centres in secondary and tertiary markets. Clearly, the schemes that put emphasis on repositioning, and succeeded in completing it on time, enjoy an advantageous position now.

Poland is on the radar of retail newcomers. In 2018 several brands entered the market, including Dealz, Saffiano, Ximi Vogue or Armani Exchange. The lack of availability of units suitable in size in prime locations is the main entry barrier for many international retailers.

Polish brands are successfully expanding abroad with Reserved and CCC leading the way. Also one fast-food brand - Makarun expanded abroad by entering UAE market and opened first Polish spaghetteria in Dubai.
Trends & Forecast

The wave of modernisations, repositionings and extensions continues.

Even for well-performing schemes with a strong position on the market, it is absolutely necessary to constantly monitor the market trends and adopt to the quickly changing spending patterns and consumer behaviour.

Personalization.

Many young people divert from mass, repetitive retailers and service providers. They value standing out from the crowd and appreciate possibility to personalize their clothes, jewelery or meals. Retail chains need to adjust their offer to these needs to keep their turnover on expected level.

Place making, expansion of food offer and leisurertainment is in.

Shopping centres are a place for social interaction, where people not only shop, but also spend their leisure time on eating out, playing sports and entertainment. This trend is clearly visible across all of the types of retail accommodation with some of the space reconfigured into different functions (enlargement of foodcourts and catering offer, new meeting places, etc.).

Retailers and landlords need to be connected.

In order to be ahead of competition, they have to embrace the power of Big Data, Internet of Things and Artificial Intelligence. As e-commerce market is developing rapidly, omnichannel strategies have also become a common practice in Poland. This trend is set to continue and will evolve fast along with development of new technologies.
Retail as a part of mixed-use schemes.

Large agglomerations, especially Warsaw, provide the opportunity to develop multi-functional complexes, where retail offer is supporting element. By combining different commercial functions such as retail, office, entertainment and culture to form one unit, mixed-use schemes create a unique and recognizable place on the map of the city. This type of potential projects is increasingly part of developers' strategy.

Implications of ban on Sunday shopping.

More than a half year after adoption the Act of Sunday trading restrictions significant decrease of footfall among the shopping centres has been observed. Almost 20,000 small- and medium-sized shops has been closed. Restrictions have even influenced large FMCG operators, such as Tesco, which had to close more than 30 stores in 2018. In addition several international and Polish brands, including Aldo and Prójchnik decided to withdraw from shopping centres.

Despite that during first months after adoption the Act shopping centres registered turnovers' growth, it is anticipated that further restrictions might cause decrease of consumption expenditure.

e-commerce is getting significance.

Following the adoption of the Act of Sunday trading restrictions noticeable increase in e-commerce sales was observed. After introducing ban on trade on two Sundays a month large part of customers turned to the online shopping, as a convenient alternative for traditional one. Although in past months the growth rate of e-commerce share in total sales clearly slowed down further development of this sector is very likely.

Some large fashion chains are trying to increase their online shops' turnovers and websites' traffic by offering additional incentives for customers, available only on Sundays. Introduction of discounts for purchases made on the Internet on that day of the week is one of the examples how they attract customer's attention and boost their website's traffic.

Due to the fact that recently mobile devices accounted for significant volume of all e-commerce sales, apart from well-designed website also user-friendly mobile Apps are expected to be strongly desired among customers.
1.4 Warehouse Market Snapshot

Review

Total modern warehouse stock
15.8m m²

New warehouse supply delivered in 2018
2.3m m²

Overall vacancy rate in 2018
5%

Pipeline supply
2.8m m²

Prime warehouse rent
€4.50-5.00 m²/month

Average warehouse rent
€2.70-3.20 m²/month
Map of logistic hubs with road infrastructure

Primary hubs:
1. Warsaw I & Warsaw II
2. Upper Silesia
3. Poznań
4. Central Poland
5. Lower Silesia

Secondary hubs:
1. Tri-City
2. Lublin/Rzeszów
3. Cracow
4. Szczecin
5. Bydgoszcz/Toruń

Major national roads

<table>
<thead>
<tr>
<th>Highways</th>
<th>Expressways</th>
</tr>
</thead>
<tbody>
<tr>
<td>Existing</td>
<td>Existing</td>
</tr>
<tr>
<td>Under construction</td>
<td>Under construction</td>
</tr>
<tr>
<td>Planned</td>
<td>Planned</td>
</tr>
</tbody>
</table>

Poland. The real state of real estate 23
The warehouse and industrial market, spurred by very good economic indicators along with positive forecasts, has been performing extremely well over the past few years. Another reason behind it is the development of transport infrastructure, which enables faster movement of goods.

With 2.3m m$^2$ completed in 2018, the total stock stood at 15.8m m$^2$ by year-end. There are 5 key warehouse clusters as well as 5 emerging ones. The bulk of warehouse space is located within the Warsaw region (located within a 50 km radius from the capital city), followed by the Upper Silesia and Poznań regions.
Developers, encouraged by continuously low vacancy rate fluctuating around 4-5% and high level of prelets, maintain high level of construction activity, which at the end of 2018 stood at 2.8m m². Built-to-suit schemes constitute the bulk of new supply.

Gross take-up in 2018 reached level of 4m m². Warsaw region and Central Poland regions attracted the bulk of letting activity. The largest transactions includes leases of BTS projects for Amazon (expansion in three locations totalling 167,000 m³), Leroy Merlin (124,000 m² near Łódź) and Zalando (121,000 m² in Olsztyn).

Logistics operators and e-commerce were the most active occupier sectors. High level of demand has put pressure on the rents over the last year.

Actually the highest rents are for prime assets located in Warsaw I and Cracow region.

Rental levels by region (€/m²/month)

<table>
<thead>
<tr>
<th>Region</th>
<th>Rental Level (€/m²/month)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Warsaw I</td>
<td>5.00</td>
</tr>
<tr>
<td>Warsaw II</td>
<td>4.00</td>
</tr>
<tr>
<td>Upper Silesia</td>
<td>3.00</td>
</tr>
<tr>
<td>Poznań region</td>
<td>3.00</td>
</tr>
<tr>
<td>Central Poland</td>
<td>3.00</td>
</tr>
<tr>
<td>Lower Silesia</td>
<td>3.00</td>
</tr>
<tr>
<td>Tri-City Region</td>
<td>3.00</td>
</tr>
<tr>
<td>Lublin/Rzeszów</td>
<td>3.00</td>
</tr>
<tr>
<td>Cracow Region</td>
<td>4.00</td>
</tr>
<tr>
<td>Toruń/Bydgoszcz</td>
<td>3.00</td>
</tr>
<tr>
<td>Szczecin</td>
<td>1.00</td>
</tr>
</tbody>
</table>
Trends & Forecast

Prospects for warehouse and industrial market remain bright.

Poland’s central location, its size, improving transport infrastructure and its economic performance, particularly in terms of production output, retail sales and trade, are the undisputed fundamentals that stand behind a positive forecast for the warehouse sector in the foreseeable future.

Shrinking vacancy and gap between headline and effective rents.

Due to high level of tenants’ activity, a tendency of low vacancy level will continue in the next year. This is the reason for developers not to provide large incentives for tenants, which results in smaller gap between headline and effective rents.

Growing importance of „last mile delivery” and BTO.

Due to fast developing e-commerce and growing customer needs, „last mile delivery” properties located in the cities have been gaining popularity. Also BTO (build-to-own) centres becomes popular, especially among tenants, which want to invest in advanced, expensive systems in their properties and optimise their costs after implementing IFRS 16.

Emerging locations gradually turn to an alternative to mature hubs, the latter leading to labour shortages and risk of cost increase.

With very tight availability of labour force and low vacancy rates in established warehouse hubs, more and more developers as well as occupiers are eyeing up opportunities in new locations. Built-to-suit options in emerging regions such as Bydgoszcz-Toruń, Lublin, Rzeszów are more cost-effective.

Lack of qualified workforce.

Fast developing industrial market leads to shortages in human capital. Therefore, developers and users will choose emerging regions to satisfy their needs for qualified workforce.
1.5 Hotel Market Snapshot

- **32m** of tourists
- **Over 6.8m** foreign tourists in 2017
- **Almost 84m** nights spent
- **Over 16.7m** nights spent by foreign visitors
- **Over 2,500** hotels
- **72.4%** Average hotel room occupancy in Warsaw in 2017

- Increasing occupancy rate of hotel rooms by **1.0pp** y/o/y
- Increasing number of tourists staying at hotels by **6.6%** y/o/y
Review

Rapid growth of the hotel market in Poland is reflected by the increasing number of new hotels, growing number of tourists, as well as the growing interest in the Polish market from international hotel brands.

The key drivers for the development of hospitality business in Poland are: economic growth, rising popularity of Poland as a holiday and MICE destination, as well as the development of medical tourism in Poland. Another important factor positively influencing the development of the hotel market in Poland is the dynamic growth of the BPO/SSC sector.

The number of categorized hotels in Poland exceeds 2,500 and is growing year-to-year. Kraków is the city with the highest number of hotels. However, when considering the number of hotel rooms, Warsaw takes the lead with 25% more hotel rooms than Kraków.

The number of tourists staying at hotels in Poland reached almost 21m, which is an increase of 6.6% compared to the preceding year. The share of Polish guests using hotel infrastructure is rising. Foreign tourists accounted for 28.7% of the total number of tourists staying at hotels, which is 1.9pp more than in 2016. The average hotel room occupancy in Poland in 2017 equalled 51.8% and was 1.0pp higher than in 2016 (Central Statistical Office data).
As far as operating models are concerned, international hotel chains entering the Polish market are mainly interested in management or franchise agreements. Pure lease agreements are accepted only in the case of prime locations in major cities and usually by hotel chains entering the Polish market. Hotel chains that are the most active in terms of new openings in Poland are: Orbis/Accor, Hilton Hotels & Resorts, Best Western and Marriott Hotels & Resorts and Holiday Inn.

Major pipeline of hotels includes: 8 hotels by Arche Group, 3 hotels by Accor Orbis (Warsaw, Kraków and Gdańsk), 2 hotels by Hilton Hotels&Resort under Hampton by Hilton brand (Poznań, Łódź) and 3 hotels by Marriott International under multiple brands (Warsaw, Poznań, Szczecin).

Focus on Warsaw

Warsaw is the largest hotel market in Poland in terms of supply of hotel rooms. It is also usually the first choice for the international brands entering the Polish market.

According to data published by the Central Statistical Office, in 2017 there were 92 categorized hotels in Warsaw offering 13,855 rooms. Three star hotels constituted 40% of all hotels in Warsaw and accounted for 31% of hotel room supply. There were 14 five-star and 17 four-star hotels, accounting for 15% and 18% of the total number of hotel rooms in Warsaw, respectively. Almost 9.7m tourists visited Warsaw in 2017, including 3.6m using accommodation, which translates into nearly 6.2m nights spent by tourists at hotels.

The average occupancy rate for hotels in Warsaw in 2017 reached nearly 72.5%, the highest in September (83%) and the lowest in January (57%).

Warsaw is the largest event spot in Poland and one of the top MICE locations in Central and Eastern Europe with over 25,000 events organized annually. In the next two years (2019 and 2020) Warsaw will see the opening of three upscale projects - Staybridge Suites Warszawa Ursynów, Vienna House Mokotów Warsaw, Holiday Inn Warsaw Mokotów.
Trends & Forecast

Increasing stock, prices and occupancy.

The positive trends on the market will continue due to positive macroeconomic factors such as rising wages, low unemployment rate and increasing number of foreign tourists visiting Poland. Currently investors are still attracted by the Polish market thanks to the improving of major hotel indicators (occupancy, ADR), and are willing to enter the market. Average room prices increased by approximately 8% y/o/y.

Emerging global MICE destination.

The dynamically changing situation in the world, including the growing level of terrorist threats in the cities of Western Europe, changes the stream of demand towards Poland and Warsaw which are perceived as safe areas. Each terrorist act has caused turmoil in the normal operating of the MICE industry, where certain events had to be postponed or cancelled. The terrorist threats are affecting both tourism and conference and congress market in Western Europe. Due to the persisting state of emergency in countries suffering from terrorism, the cost of providing security and meeting security requirements during large events has increased drastically.

Condo-hotels and short-term rental apartments as a consequence of offer’s diversification.

Over the recent years hotel market’s supply noticeably changed due to increasing share of short-term rental apartments in the offer. They are usually cheaper than traditional hotel rooms, but often equally attractive and conveniently located which makes them an interesting alternative for less wealthy part of tourists. As a premises that guarantee higher rates of return they are also attractive for developers who aim to maximize profits. Since short-term rental apartments seem to meet visitors expectations its is highly probable that in the following years their share in supply will continue to grow.
Residential Market Snapshot

Largest residential market in Central and Eastern Europe

Almost 66k apartments delivered in 2018

Decrease in sales volume in top 6 markets 65k units and 11% decrease y/o/y

Major trends:

- rising prices
- rising construction costs
- developing rental market
Review

The Polish residential market is the largest in Central and Eastern Europe, however it still lags behind Western EU in terms of ownership structure (with a predominant share of owner occupied housing stock), undeveloped institutional rental market, age of housing stock and level of market saturation.

First three quarters of 2018 saw significantly smaller, compared to the corresponding period of the previous year, increase of supply, but fourth quarter brought another record in number of apartments delivered, which amounted to over 19k units.

Overall, in 2018 159,923 building permits were obtained and development of 131,627 new apartments was commenced. Total number of apartments completed exceeded last year’s by 6,523 dwellings, which translates into 6.2% growth.

2018 brought clear slowdown in some of the six largest residential markets in Poland. In Tri-city and Poznań number of newly constructed apartments decreased by approx. 25% compared to previous year and Wrocław noted over 40% decrease in number of building permits obtained.

After record breaking 2017, 2018 brought further, but not as much dynamic as in the previous year, increase of prices caused by rising construction costs, increasing land prices and continuously strong demand.

Among the cities that registered highest average price’s increase Warsaw (over 14%), Wrocław (over 13.5%) and Łódź (almost 9.5%) should be mentioned.

Slight decrease in supply caused drop in the volume of sales by approx. 11% in six major markets, but there is still noticeably high demand for residential units located in largest agglomerations, which customers are willing to buy even for higher prices. The reasoning behind this strong demand is the economic prosperity manifested through record low unemployment rate, relative stability of prices (low stable inflation) and rising wages. Not without significance are also historically low interest rates on mortgage loans.

Investments in the residential market have been attracting private cash investors that generate a large portion of the demand.

The upscale market segment is increasing its share particularly in the large developed markets of Warsaw, Kraków and Tri-City.
Warsaw’s residential market remains the most developed in Poland. The demand is driven mainly by in-migration, the highest income level in Poland and the lowest unemployment rate. Warsaw is also a popular location for shared service centers and office investments. Both of them result in increased demand for residential developments. Employment perspectives and major universities located in Warsaw are a magnet for young people from other regions of the country. The market reacts to the increased demand, which results in the multifamily developments being the focal point for developers. The most expensive flats of prime and super-prime segment with prices over PLN 15,000 per m² are located in Śródmieście, Mokotów, Żoliborz, Ochota, Praga Południe (Saska Kępa) and Praga Północ districts.

*source: EY market research*
Trends & Forecast

End of the upturn in the market.

Over the 2018 market noted significant slowdown compared to the previous year. Both, number of apartments delivered and sales volume noticeably decreased.

It is forecasted that along with decreased developer’s activity lower number of transactions will characterize residential market also in 2019. With limited number of new apartments entering the offer prices will slightly rise, but in longer period of time their stabilization is expected.

Construction cost and land prices on a rise.

Due to the limited availability of labour force on the market, temporarily supplemented with workers from Ukraine, and the higher minimum wage as increased by the government, construction cost ultimately resulting from higher labour cost is expected to continue to rise. The decreasing availability of development land will also be driving up the average total development cost.

Rental market development – organized and institutional players to take over?

As regards the ownership structure in Poland, high returns generated by the Polish rental market are encouraging more and more investors to develop residential investments aimed at maximization of ROI from organized rental. With possible increase of interest rates, demand for investment apartments generated by private investors might decrease. The gap will be filled by developers and investment funds. Additionally, when introduced, the REITs legislation is expected to boost the growing potential of the Polish rental market. Foreign private institutional investors already present in the market are Bouwfonds and Catella.
**Micro-apartments market development.**

Although on western markets micro-apartments are well known for decades, in Poland this type of flat has been gaining its popularity since only a few years. A high-standard, modern, located in the city centre apartments, which, by definition, should accommodate sitting space, sleeping space, bathroom and kitchen within no more than 20-30 m² were designed mainly for students and singles who do not spend much time at home and cannot afford buying bigger, conveniently located apartment without external financing. However, because of relatively high price per sq. m. micro-apartments became less affordable for target group and now are bought mainly by investors who intend to designate them for rental purposes. In Poland first project comprising micro-apartments was completed in 2013 in Wrocław by Dolnośląskie Inwestycje. Following the southern developer also Polnord, Dantex or Ochnik Development decided to introduce micro-flats in their offer. Today micro-apartments can be found in numerous projects in Wrocław, Warsaw, Poznań and Lublin.

**Student housing as developing asset class.**

Due to low quality of existing stock and growing demand private student houses are becoming more popular in Poland. Constantly growing students population, including dynamically rising number of international students create demand for new type of assets. First purpose-build student accommodation (PBSA) are now operating and seems to became very attractive asset class for investors and developers. Supply is still very low and operating or planned in the biggest university cities (Poznań, Łódź, Lublin, Wrocław, Kraków and Gdańsk). Main players are i.e. Griffin (Student’s Depot) and Base Camp and Golub GetHouse.
Co-living is a new type of housing based on shared economy. The intention of this concept is to provide its residents with convenient accommodation and simultaneously empower them to actively participate in life of surrounding community. In order to respect individual's privacy all the members have their own micro-apartments, but they share kitchen and other common spaces such as meeting rooms, gyms or gardens, each designed for bringing people together. Tenants have lots of opportunities to better connect with other members, but they also unite around a common interest to manage space and share major expenses. Moreover, landlords ensure additional services e.g. laundry or room cleaning, so residents can focus on enjoying daily events with the rest of community, instead of doing housework. All these factors contribute to creating an attractive and convenient space to live where one can feel as a part of a commune. Although in Poland the era of co-living is just beginning, investors see increasing potential of this type of spaces. At the end of 2018 Finnish developer YIT decided to build the biggest co-living in the country – Smartti Mokotów, designated for young individuals who wants to live more creative life.
Investment Market Snapshot

Review

Volume of investment transactions in 2018: €7.2bn
Volume of the largest transaction in 2018: €700m
Invested capital allocated in office: €2.75bn

Prime office yield: 4.75-5.20%
Prime retail yield: 4.80-5.20%
Prime warehouse yield: 6.00-6.50%

Poland. The real state of real estate
2018 was the record year for Polish investment market. Total value of transactions exceeded €7bn for the first time, representing 44% y/o/y increase. Value of transactions in the office sector surpassed the value in the retail sector, which shows that investors tend to diversify their portfolios. Warehouse investment market was also characterized by strong increase, which shows growing impact of e-commerce.

Volume of the largest transaction in 2018 accounted for €700m. The transaction included internal sale of portfolio of 12 retail properties by Chariot Top Group BV to EPP. The biggest transactions in the office sector was sales of Warsaw Spire A by Ghelamco to Madison International for €350m and Gdański Business Centre C, D by HB Reavis to Savills IM and Employees Provident Fund for €200m.
Most of the capital inflows to Poland from Europe and United States. However Asian and South African investors have been strongly pursuing opportunities across Poland, focusing on Warsaw as well as key regional markets.

Due to good economic condition, investors have been eminently active on the market. Their activity has been reflected in a slight compression of prime yields. It should be noted that there is still a substantial gap between prime yields in Poland and developed Western Europe markets, thus making Poland attractive to investors looking to achieve higher returns, while maintaining a relatively low risk profile.

**Prime yields curve**

<table>
<thead>
<tr>
<th>Year</th>
<th>Office</th>
<th>Retail</th>
<th>Warehouse</th>
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</tr>
</tbody>
</table>
**Trends & Forecast**

**Poland will continue to be on the radar of investors.**

Given its size, market fundamentals, steady occupier demand as well as yields higher by 2-3pp as compared with developed Western Europe markets, Poland will attract investors' interest over the course of the coming quarters.

**Prime yields have been slightly decreasing, especially in the best-in-class office buildings and shopping centres. Pricing on non-primary assets will vary significantly and be set asset-by-asset.**

Good condition of Polish economy and high level of investors' activity leads to prime yields shrinking mostly in the office and retail sector. Despite fast developing industrial market, prime yields there remains stable. The situation with secondary assets will be more complex and asset-specific details will have to be considered when evaluating the price.

**In their search for opportunities, investors are eyeing up not only primary, but also secondary markets.**

In view of the insufficient supply of prime products in Warsaw, regional cities are much sought after by investors as a destination for capital allocation. Tier-2 and tier-3 cities have slightly higher risk profiles and a lower depth of the market, however yields are 2-3pp higher.

**Investors tend to invest more in the industrial market.**

Mostly due to growing importance of e-commerce, investors have been changing their focus from retail to industrial properties. This is the key factor, which ensures dynamic growth of the industrial sector in the upcoming years. Industrial market also offers diversified investment opportunities, which attracts different types of investors.
What does the future of Real Estate look like?

Real Estate market is undergoing changes as new technologies are introduced and becoming more common. Professionals will have to shift from traditional real estate perspective to a broader approach that takes into account technologies that will disrupt for example real estate cycles. The question is, how the cycles will be disrupted. There are arguments for and against both smoother and more extreme cycles.

Technologies and RE market

- Autonomous vehicles to instigate a location paradigm - will any real estate sub-sector not be impacted?
- AI, VR, RPA, apps versus traditional Real Estate jobs.
- ‘Co’ phenomenon - the space may change, the method to buy it will change but will people stop aspiring to own and own more?
- How far can the personalization of space go?
- How individual ownership of assets thrive in a truly connected and integrated urban infrastructure?
- How do we maintain engagement in the live/work anywhere world?
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.
Changes of the real estate law (adopted):

1. **Act on the restriction on trade on Sundays** - starting from March 2018 a ban on trade on Sundays in the commercial outlets entered into force. The ban was established mainly in order to restrict trade on Sundays in the large-format commercial facilities and shopping centres. The Act provides for certain exceptions (i.e. gas stations, trains and bus stations, airports and hotels), where the trade will still be allowed. The ban enters into force gradually, in 2019 on 3 out of 4 Sundays a month (subject to some exceptions only the last Sunday of the month will constitute “working Sunday”), and a comprehensive ban will enter into force from 2020.

In consequence, the restrictions on trade on Sundays may have a negative impact on the turnover of the tenants, what in consequence may lead to the higher number of redundancies of the employees and to the increase of the unemployment rate in general. What is more, the terms and conditions of the leases will have to be renegotiated, some tenants may even go bankrupt which could result in lower profits of the landlords.

2. **Act on conversion of perpetual usufruct of residential land into ownership** - starting from 1 January 2019 the owners of the premises in buildings developed on the residential land held under perpetual usufruct became co-owners (owners in case of the single-family houses) of the land instead of holding shares in perpetual usufruct right. The owners of the premises are obliged to pay, up to 20 years (or 33-99 years in case the premises are used for the business activity), a special fee for conversion, in the amount of the last annual fee for perpetual usufruct.

In consequence, the institution of the perpetual usufruct in relation to the residential lands in Poland disappeared by virtue of law. As for the commercial lands, the directions of possible amendments are not known, however the matter is currently publicly discussed.
Changes of the real estate law in 2019:

1. Real Estate Investment Trusts (REIT) - in accordance with the draft law, REITs are to operate only in the residential market (including retirement homes and dormitories), without the possibility to invest in the commercial real estate.

The real estate market was looking forward for introducing REITs regime in Poland, however the scope of previous drafts included also possible investments in the commercial properties (the current one only in the residential market). Economic reports revealed then indicated that adopting REIT’s investing in the commercial assets would produce many beneficial effects for the economy, including decrease of unemployment rate, increase of turnover on the Warsaw Stock Exchange (GPW), GDP growth etc. Due to the fact that adoption of the project in the current scope will not achieve the abovementioned objectives, most likely the REITs will not attract the potential investors.

2. Investment Act - works are conducted to introduce an act aiming at improvement of the investment process. However, the act will also establish certain restrictions on carrying out investments. The biggest concerns raise planned restrictions on carrying out investments on the basis of zoning decisions. Carrying out investments in the areas not covered by the local spatial development plans will be limited. Currently, due to small coverage of Poland with local spatial development plans, over half of the investments in Poland is carried out on the basis of the zoning decisions. Entry into force of the planned changes will prevent most of investments from being carrying out.

3. Mitigation of requirements related to trade of agricultural land - entry into force on 30 April 2016 of the new Act restricted the freedom of trade of agricultural land in Poland. The restrictions were imposed also on trade of other types of land, especially investment areas, which due to very broad definition of agricultural land and lack of coverage with local spatial development plan, were qualified as
agricultural lands. In accordance with the new draft act, planned changes are aimed at allowing broader trade of agricultural land and include following propositions:

- The provisions of the Act will not apply to the agricultural lands located within the areas of the cities or the agricultural lands of an area smaller than 1 ha
- State Treasury will have a right of pre-emption of shares of commercial companies only if the total area of agricultural land owned by the company will constitute at least 5 ha.

4. Simple stock company - a new type of a company is to be introduced in the Polish legal system. The new structure of a simple stock company (PSA) combine the advantages of a joint-stock company and a limited liability company. It will provide for: an easy registration process, possibility of the PSA shares’ dematerialization and introduction of the monistic board structure and deregistration of a company without carrying-out a liquidation process.

The proposed structure is to be introduced as a solution for the start-ups and new-tech environment, however, due to its universal character it can facilitate projects development.

5. Development Act - Office of Competition and Consumer Protection (UOKiK) calls for adoption of legal provisions that will provide better protection for purchasers of apartments from developers. What is more, modification of security mechanisms of open escrow accounts is planned. The accounts service purchasers’ deposits, in such a way that the payments made by the purchasers are paid out to the developer upon completion of the given phase of works, after bank's positive inspection conducted at the construction site. The open escrow account may be additionally secured by the bank or insurance guarantee. It is planned to replace the above-mentioned securities with an obligation of a developer to make a contribution payment on each payment made by the purchaser via the open or closed escrow account in the amount of 5 % of the value of each transaction, to a newly created Developer Guarantee Fund. The accumulated funds will be disbursed to the purchasers in case of the developer’s bankruptcy.

The proposed changes will increase the level of protection of purchasers of apartments, however may also contribute to increase of prices and elimination of smaller developers from the market due to potentially high amount of contributions to be paid to the Developer Guarantee Fund.
Planned changes of tax law in 2019:

Taxpayers in Poland face significant changes in tax law as of 2019. The amendments continue to be in line with global and European trends aimed at introducing measures against tax evasion and tax avoidance, i.e. actions undertaken within the Base Erosion Profit Shifting (BEPS) initiative by OECD, Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (MLI), as well as works within the European Union, which resulted in developing the Anti-Tax Avoidance Directive (ATAD).

There are also tax changes which originate from the local developments and in many cases they stretch even beyond measures recommended by international bodies.

We highlight below selected key changes which impact the real estate market in 2019.

Investment structures

For many years the Polish real estate market has developed investment structures that were widely used by investors. However, the abolishment of well-grounded investment fund structures for real estate investments last year marked a radical watershed. While legislation that led to the significant limitations of the investment fund structure was being drafted, at the same time the Polish government promised an attractive alternative for the real estate market, the REIT (Real Estate Investment Trust) regime.

Real estate investors familiar with REIT regimes of other countries were in the past not too often asking for a similar vehicle to expand into Poland. That was because investment funds offered a comparable - if not more efficient - vehicle for Polish real estate investments. These days are over now, the global real estate funds community is still awaiting the new Polish REIT to become an option. Unfortunately, the works on REIT legislation is still in progress and there is no certainty about the final shape and timing of REIT tax incentives to come into force in Poland.

Major withholding tax reform

Polish WHT regime has been significantly reshaped as of 1 January 2019.

Measures that has been introduced include:

- Replacement of the current direct application of WHT exemptions or treaty rates with a “pay and refund” system for payments exceeding PLN 2m (approx. $540k / €460k)
- Obligation to assure due
• Obligation to follow new definition of a beneficial owner, which includes, among others, test that recipient carries out “real economic activity” with a required level of substance

• Application of statutory WHT rates (19% or 20%) instead of treaty rates or exemptions, unless additional actions are taken, such as:
  ▶ Providing a statement filed by the tax remitter confirming application of lower WHT rates or exemptions
  ▶ Applying for an opinion issued by the tax office confirming WHT exemptions.

New rules relate to both intra-group and third-party payments.

The new rules are expected to expose all board members of Polish companies making cross-border payments, as well as board members of foreign taxpayers claiming refunds, to an increased level of risk related to criminal charges.

Mandatory Disclosure Regime (MDR)
As of 1 January 2019, the EU Directive (2018/822) on MDR has been implemented into Polish tax law. Under this regime transactions meeting certain hallmarks have to be reported to Polish tax authorities.

Polish hallmarks are going beyond provisions of the EU Directive.

Certain domestic transactions are also subject to reporting.

Minimum levy/tax on commercial real estate
As of 1 January 2019 minimum levy/tax applies to all buildings (with an exception for residential buildings leased under social housing programs) subject to lease regardless of their type.

The tax applies only to leased buildings (i.e. no tax on vacant buildings or parts of buildings).

The minimum threshold of PLN 10m is applicable to a whole portfolio of buildings possessed by a given taxpayer.

The minimum levy/tax can be reimbursed (assuming excess in a given year over „regular” CIT liability) if the tax authorities confirm that there were no irregularities in the amount of „regular” CIT liability.

In addition, an anti-avoidance clause applies when a taxpayer disposes of or leases his building out in whole or in part without good commercial reasons in order to avoid the minimum tax.
Exit tax
This change, that came into force on 1 January 2019, constitutes implementation of the EU Anti-Tax Avoidance Directive (ATAD) in Poland in the area of exit taxation.

A new tax, a so-called tax on unrealized profits (hidden reserves) that are embedded in a taxpayer’s property and that are potentially transferred together with such property outside of Poland within transfers of the property within the same taxpayer (e.g. transfer by a Polish resident to its permanent establishment located abroad or transfer by a nonresident operating via Polish permanent establishment to its home country or to another country in which it operates) or upon change of the taxpayer’s residence.

Exit tax on unrealized profits is calculated as the difference between the fair market value (FMV) of the property transferred (established based on separate rules) and its tax book value (that would have applied had the given property been disposed of) as of the date of the transfer.

Upon transfers into Poland, taxpayers may be allowed to credit the foreign equivalent tax (i.e., the tax due in a foreign country and which is equivalent to the tax on unrealized profits) up to certain limits.

Eurobonds exemption
Interest on bonds issued by Polish entities to foreign investors after 1 January 2019 may benefit from withholding tax exemption.

The exemption applies to bonds with a maturity of one year or longer, which are traded on regulated stock markets and on multilateral trading facilities, under the condition that the entities related to the issuer will hold no more than 10% of the bonds issued.

Sale of commercial real estate - guideline from the Ministry of Finance
For the last couple of years tax classification of asset deals on the real estate market in Poland became a real issue. Depending on the classification (sale of asset or sale of a going concern) resulting tax consequences for the seller and the buyer differed significantly (in particular, this would determine if the transaction is subject to undeductible transfer tax or whether it would be subject to VAT that generally could be deducted by the purchaser).

Poland’s Ministry of Finance published guideline on a proper classification of objects of asset transactions as either a property sold on a piecemeal basis or as a going concern (business).
The guidance sheds some light on the topic, but the current approach of closing asset deal transactions based on individual tax rulings is likely to continue notwithstanding the new guidance.

**Tax loss deductibility**
Starting in 2019, taxpayers are allowed to utilize up to PLN 5m of a tax loss incurred in a given tax year based on a one-off basis (in the five year period). General rules (i.e. possibility to utilize only a half of the tax loss in the following tax year) will apply to the excess amount over PLN 5m.

**9% CIT rate for small taxpayers**
A new reduced 9% CIT rate on income other than income from capital gains is introduced.

Broadly, the reduced rate may apply on the condition that an entity is a small taxpayer (its revenues in a given year do not exceed the equivalent of €1.2m).

The reduced rate is not available for entities created as a result of restructuring.

**Notional interest deduction**
Taxpayers will be allowed to deduct deemed interest on certain parts of equity, amounting to the reference interest rate of the Polish National Bank as of the last banking day of the preceding tax year, increased by 1 basis points; however, no more than PLN 250k of interest ($70k) in a tax year.

This regulation is planned to come into force from 2020, with retrospective effect for qualifying equity payments / transfers performed in 2019 (assuming a tax year corresponding to the calendar year).

**Tax penalties**
Another change is introduction of sanctions in the form of an additional liability of 10%-30% of the tax liability assessed by the tax authorities based on the General Anti Avoidance Regulations (GAAR) or other anti-abuse clauses, transfer pricing settlements and withholding tax cases.

**Tax rulings**
Under the new regulations it is forbidden to apply for tax rulings regarding any provisions related to tax avoidance matters (i.e. both General Anti Avoidance Regulations (GAAR) as well as other existing abuse clauses).

Any tax rulings regarding these areas obtained by the taxpayers in the past expired on 1 January 2019.
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.

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

2.1.2. Legal titles to real estate

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

Ownership right

Ownership (prawo własności) is the broadest right to real estate in Poland. As a rule, ownership comprises the right to possess and use real estate for an unlimited period of time 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 local spatial development plans adopted by local authorities (municipalities).

Right of perpetual usufruct

Perpetual usufruct (użytkowanie wieczyste) is a right to use the real estate which may be granted by the State in relation to the land owned by the State or a local authority. 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 key 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 (not less than 40 years).

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 (to be refused only in case of important social interest).

- 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 land 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 (e.g. 2% for tourists purpose).

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.

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.
Conversion of the perpetual usufruct into ownership in general requires consent of an owner of a real estate (the State or a local authority) and is executed in a civil law sale agreement (buyout). However, selected perpetual usufructuaries (in particular natural persons), subject to certain conditions, may demand perpetual usufruct be converted into ownership in a simplified administrative procedure.

The conversion is subject to a fee which is equal to the difference between the value of ownership and the value of the perpetual usufruct right. On 1 January 2019 the perpetual usufruct of lands developed for residential purposes was converted into ownership right by virtue of law.

**Leases**

Polish law distinguishes between two types of leases: lease (najem) and lease with the right to collect profits (dzierżawa). Leases are used mainly for commercial and residential premises. Leases with the right to collect profits 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 contract for lease with the right to collect profits, however, provides for the lessee’s additional right to collect profits from the real estate.

**Easements**

Easements (służebności) 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.

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 lease with the right to collect profits, 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 lease with the right to collect profits 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), the main purpose of which 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.

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.

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 acted in such belief (rękojmia 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 argue to the contrary. 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 a mention in the land and mortgage register concerning e.g. filled, but yet unexamined application to the register.

Land and Buildings Register

The land and buildings register is kept by local authorities 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 entities holding the land, buildings and premises.
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 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 separate 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, however in practice these most frequently operate as limited liability companies and limited partnership, which will be presented below as constituting legal forms most commonly used by the investors.

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 providers 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.
Partnerships

General partnership

Limited partnership

Partnership limited by shares

Professional partnership

Companies

Limited liability company

Joint-stock company
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:

<table>
<thead>
<tr>
<th>Feature</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>May be created by one or more persons for any purpose allowed by law</td>
<td>(it may not be formed solely by another single-shareholder limited liability company)</td>
</tr>
<tr>
<td>Liability of the shareholders is limited to their contribution to the</td>
<td>the share capital of the company shall amount to the minimum of PLN 5,000 (ca. €1,200) and is divided into shares of equal or non-equal nominal value</td>
</tr>
<tr>
<td>share capital of the company</td>
<td>the share capital can be covered by a contribution in-kind</td>
</tr>
<tr>
<td>Limited liability company is a legal person and as such, it is a party</td>
<td>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.</td>
</tr>
<tr>
<td>to specific rights and obligations</td>
<td></td>
</tr>
</tbody>
</table>

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 (which takes approximately 4 weeks since application to relevant court was filed).
It is also possible to register a limited liability company with the registry court via the Internet, however this includes certain restrictions - limited possibility to form the contents of articles of association and exclusion of in-kind contribution.

The SPVs may be set up directly by the foreign investor, being the only shareholder. It is possible to establish several SPVs by the same shareholder in order to divide the investment risk between them. However, depending on the preferences of the investor and bearing in mind possible overall effectiveness, a simple one step structure may be enlarged and involve, for example, a holding company, abroad or in Poland, which manages the investment holds the shares of the SPVs.

### 2.2.3 Partnerships

The main features of partnerships are the following:

- Partners act in the name of the partnership
- Partners are responsible for the liabilities of the partnership
- The assets of the partnership include any property contributed to the partnership
- There are no minimum capital requirements (excluding the partnership limited by shares in case of which the minimum share
capital amounts to PLN 50,000, i.e. ca. €12,000)

- Although it is not classified as a legal person, a partnership may acquire rights on its own behalf, including the right of ownership of real estate and other rights, incur obligations, sue and be sued.

- 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.

As a consequence, 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.

In case of limited partnerships also 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 will be a 100% subsidiary of the investor, nevertheless it may take specific functions in the SPV - e.g. management duties.

**Partnership limited by shares**

A partnership limited by shares (spółka komandytowo-akcyjna) conducts a business enterprise under its own business name, where at least one partner (general partner - komplementariusz) bears unlimited liability towards the creditors for obligations of the partnership and at least one partner is 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 of at least PLN 50,000 (ca. €12,000).

The specific features of this entity results in two kinds of involvement in the partnership, the general partner represents the partnership and takes subsidiary responsibility for the partnership's obligations, while involvement of the shareholder 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).

**Structure with limited partnership**

- **Foreign Investor (limited partner)**
- **LLC (general partner)**
- **SPV**
**Tax features**

In the case of partnerships, 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 (i.e. limited partnerships are tax transparent).

Due to CIT law changes, from 1 January 2014 partnerships limited by shares are corporate income taxpayers. 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 royalties as well as withholding tax on remuneration paid to individuals, as a tax remitter).

<table>
<thead>
<tr>
<th></th>
<th>Limited liability company</th>
<th>Limited partnership</th>
</tr>
</thead>
<tbody>
<tr>
<td>legal personality</td>
<td>YES</td>
<td>NO</td>
</tr>
<tr>
<td>can be established by a single shareholder/partner</td>
<td>YES (NO if to be established by a LLC, which has only one shareholder itself)</td>
<td>NO</td>
</tr>
<tr>
<td>can acquire real property</td>
<td>YES</td>
<td>YES</td>
</tr>
<tr>
<td>the shareholders/partners are personally liable for the company’s debt</td>
<td>NO</td>
<td>general partner - YES limit partner - NO</td>
</tr>
<tr>
<td>minimal share capital</td>
<td>5,000 PLN (ca. €1,200)</td>
<td>NO</td>
</tr>
<tr>
<td>management board</td>
<td>obligatory</td>
<td>NO</td>
</tr>
<tr>
<td>supervisory board</td>
<td>voluntary*</td>
<td>NO</td>
</tr>
<tr>
<td>Taxation of income (from exploitation or sale of assets)</td>
<td>19%/9% at the company level</td>
<td>19%/9% at the level of the partners</td>
</tr>
</tbody>
</table>
### Taxation of the distribution of income to shareholders / partners

- **Limited liability company**: 19% 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).
  - New WHT regime applies as of 1 January 2019, where a relief system is replaced with “pay-and-refund” mechanism (unless certain additional measures are taken).
- **Limited partnership**: NO

### Civil law transaction tax on shareholder / partner loans

- **Limited liability company**: NO
- **Limited partnership**: 0.5% on the value of the loan payable by the partnership

### Applicability of thin capitalization rules

- **Limited liability company**: YES
- **Limited partnership**: YES (at the level of the partners) further interest paid to the partner being the lender cannot be recognized as a tax deductible cost of this partner (on the other hand, interest received constitutes taxable income of this partner)

### Ability to offset profits and losses from various projects (carried out in separate companies / partnerships)

- **Limited liability company**: NO only in the case of establishing a tax capital group
- **Limited partnership**: YES profits and losses are compensated at the level of partners

### Taxation in Poland of the sale of shares in the company / partnership

- **Limited liability company**: 19% possible relief for foreign shareholders on the basis of double taxation treaties (depending on the treaty)
- **Limited partnership**: 19% it is not clear whether the same relief possible in the case of partnerships
The table compares the business and taxation aspects of the limited partnerships and limited liability companies:

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 and tax authorities (as regard the taxes payable at the partnership level) 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 attract taxation in Poland. A detailed analysis is required in each case.

**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 appropriately managed, seeking to avoid double taxation.

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.

Additionally, bearing in mind the general anti avoidance regulation introduced to the Polish tax regulations and 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.
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 joint venture constitutes 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
- Gaining access to cheaper sources of supply and cheaper financing
- 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 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.


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.

Establishing a 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.
Until the end of 2016 the use of this structure, if properly implemented, could have led to deferral, or even exemption from taxation, of the operating and capital gains generated from real estate, as FIZ was generally exempt from CIT in Poland.

Similarly, a foreign investment fund established in the EU or EEA country could be used (the Polish CIT law in force from 1 January 2011 provides for such a possibility explicitly).

Due to recent changes as of 1 January 2017, income of FIZ or a foreign investment fund resulting from:

- A share in profit generated by tax transparent entities
- Interest on loans issued to tax transparent entities and interest on those entities’ other liabilities towards the fund
- Interest on a share in tax transparent entities
- Donations/ gifts or other free or partially free benefits from tax transparent entities
- Interest (discount) on securities issued by tax transparent entities
- Transfer of securities issued by tax transparent entities or shares in such entities.

is no longer CIT exempt. Set-up of the structure designed for real estate holding which could benefit from the CIT exemption is, therefore, even a more complex exercise than before.

Example of a FIZ structure
2.2.6 Real estate investment trusts

General remarks

Real estate investment trust (hereinafter referred to as REIT) is a fund investing in commercial real estate, guaranteeing a regular dividend for investors. According to the European Public Real Estate Association, the average dividend funds in Europe for the period 2010-2015 amounted almost 5 percent. Worldwide, REITs offer investors many advantages: high liquidity and rate of return, exemption from corporate income tax and, finally, a regular dividend of up to 90-100 percent of profit.

However, so far, this form of investment has not been regulated by the Polish law.

Polish Parliament is currently working on the implementation of REIT regulations into Polish legal system. Based on the current draft REIT’s investments should be limited to residential real estate (including retirement homes and dormitories), with exclusion of commercial real estate, such as warehouses, shopping centers and office buildings.

According to the draft regulation, a REIT must be a public joint-stock company listed on the Warsaw Stock Exchange, created for an indefinite period of time. Its share capital must be at least PLN 50 million. At least 80% of its asset value must be comprised of real properties or shares in so called real estate subsidiaries (which must meet certain criteria similar to these of REIT), and consequently at least 90% of its net sale revenues must be gained from: 1) the lease of at least five real properties or the sale of real properties, 2) sale of residential real estate after at least 1 year of lease, 3) shares in so called real estate subsidiaries or 4) sale of shares in such real estate subsidiaries.

At least 90% of REIT’s profit must be paid out as annual dividends to its shareholders - unless the shareholders decide to allocate it for re-investment on the real estate market within next 24 months. Finally, a REIT’s liabilities may not exceed 50% of its assets.

The works on the REIT regulation are in progress, however should not be implemented before 1 January 2020. Further work on the draft law, especially the scope of investment that REIT is eligible to should be closely monitored by the investors.
Tax remarks

According to the draft act, a REIT will be exempt from CIT on on-going income from the lease and sale of real estate as well as sale of shares of other REITs and so called real estate subsidiaries (that must also meet certain criteria) until distribution. Upon dividend distribution, such a dividend shall be taxed at 8.5%. Real estate subsidiaries that meet criteria and are 95% held by REITs can also enjoy a tax exemption on certain real estate related sources of income.

2.2.7 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 21 October 2016 on Concession for Works and Services, hereinafter referred to as the Act on Concessions, which has replaced the previous Act of 9 January 2009 on Concession for Works and Services.

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
- Private partners receive payments for the service rendered
- Constitute a special form of tender agreements.
Recently, new amendments to the Act on Public-Private Partnership have been proposed by the government, however the legislation procedure is still in progress.

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 exploit the work or services that are the subject of the contract or in that right together with payment 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.

In cases where the Act on Concessions and Public Procurement Law do not apply, the selection of the private partner is made in a way that ensures the maintenance of fair and free competition, as well as the principles of equal treatment, transparency and proportionality. If the public partner brings in real estate as its own contribution, the provisions of the Act of August 21, 1997 on the Property Management (hereinafter referred to as the Act on Property Management) must be taken into account.

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, or the private partner can join the company established by the public entity.
Financial restrictions

The total joint 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.

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. 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 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. A concession contract is concluding for a limited period.

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 exploit the works that are the subject of the contract or in that right together with payment by concession-granting authority
- The concession for services - exclusively the right to exploit the services that are the subject of the contract or in that right together with 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 develop 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 to a borrower, while a borrower undertakes to return the same amount of money. 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, available collaterals, financial condition of the borrower. Additionally, banks may charge the borrower with a different fees such as, for instance, a preparation (origination) fee for all work connected with the preparation of the credit, or a commitment fee for and undrawn portion of the credit.

Banks also generally require certain collaterals 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
- Notarial submissions to execution
- Subordination agreements.
A mortgage is the common form of security required by Polish banks - especially required in real estate financing transactions.

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 before the entry takes effect but upon receipt of confirmation of filing of the application for registration of a mortgage in the Land and Mortgage Register.

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.

**Bonds**

Bonds can be issued by a legal entities, including legal entities from outside the territory of Poland if they conduct business activity or has been established in order to issue bonds, a partnership limited by shares, credit unions, local government units and financial institutions. Bonds can be defined as securities that are issued in series and certifies that the issuer is a debtor of the bondholder and assumes an obligation towards the bondholder to provide specified benefits. Bonds may be either 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 bonds 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 (by way of a public offering), 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.

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.
## 2.3.2. Tax implications

### Equity financing versus debt financing

Below we present the main differentiating factors when considering the two forms of financing the investments.

<table>
<thead>
<tr>
<th></th>
<th>Equity financing</th>
<th>Debt financing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Forms of financing</td>
<td>Capital injection</td>
<td>Shareholder loans</td>
</tr>
<tr>
<td></td>
<td>In-kind contribution</td>
<td>Bonds</td>
</tr>
<tr>
<td></td>
<td>Additional payments to share capital</td>
<td>Other debt instruments</td>
</tr>
<tr>
<td>Receipt and repayment</td>
<td>NO</td>
<td>NO</td>
</tr>
<tr>
<td>subject to income taxation?</td>
<td>Equity financing is generally subject to a 0.5% civil law transaction tax on share capital increase.</td>
<td>Loans are generally subject to civil law transaction tax at the level of 0.5% 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; several exemptions apply:</td>
</tr>
<tr>
<td></td>
<td>Contributions to a reserve capital (share premium) should not be subject to civil law transaction tax.</td>
<td>- Loans granted by shareholders to a limited liability company or joint stock company</td>
</tr>
<tr>
<td></td>
<td>The tax must be paid within 14 days of the date of the agreement, and the tax liability rests with the company.</td>
<td>- Loans granted by foreign entities which are engaged in credit and financing activities (such as group treasury companies)</td>
</tr>
<tr>
<td>Rights</td>
<td>Shares in the company give shareholders the right to control the company and the right to financial benefits from the company.</td>
<td>Creditors have the right to interest, as a rule no control nor participation in profits.</td>
</tr>
<tr>
<td>Forms of repatriation of funds</td>
<td>Equity financing</td>
<td>Debt financing</td>
</tr>
<tr>
<td>-------------------------------</td>
<td>-----------------</td>
<td>---------------</td>
</tr>
<tr>
<td>Dividend</td>
<td></td>
<td>Interest</td>
</tr>
<tr>
<td>Redemption of shares</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Liquidation proceeds</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Deductibility of payments for tax purposes?</th>
<th>Equity financing</th>
<th>Debt financing</th>
</tr>
</thead>
<tbody>
<tr>
<td>Generally NO</td>
<td></td>
<td>YES</td>
</tr>
<tr>
<td>Exception: under new amendment to tax law, there would be a possibility to deduct from the taxable base of the hypothetical costs of obtaining external funds in case the company receives funding in the form of additional payments to equity or retained profits are used.</td>
<td></td>
<td>Subject to thin capitalization and other interest limitation rules (see below)</td>
</tr>
<tr>
<td>Capital financing costs cannot exceed PLN 250k in the tax year.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>This notional interest deduction will apply from 2020 (including also retained earnings from 2019).</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Withholding tax</th>
<th>Equity financing</th>
<th>Debt financing</th>
</tr>
</thead>
<tbody>
<tr>
<td>19%</td>
<td></td>
<td>20%</td>
</tr>
<tr>
<td>The 19% rate can be reduced or eliminated based on relevant tax treaty concluded by Poland.</td>
<td></td>
<td>This rate may be reduced or eliminated based on relevant tax treaty concluded by Poland.</td>
</tr>
<tr>
<td>As of 1 July 2019 new “pay-and-refund” mechanism applies with respect to payments subject to withholding tax (unless additional measures are taken).</td>
<td></td>
<td>As of 1 July 2019 new “pay-and-refund” mechanism applies with respect to payments subject to withholding tax (unless additional measures are taken).</td>
</tr>
<tr>
<td>(see the Appendix at the end of this book for a list of withholding tax rates under Poland’s various tax treaties)</td>
<td></td>
<td>(see the Appendix at the end of this book for a list of withholding tax rates under Poland’s various tax treaties)</td>
</tr>
<tr>
<td>Equity financing</td>
<td>Debt financing</td>
<td></td>
</tr>
<tr>
<td>--------------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------</td>
<td></td>
</tr>
<tr>
<td>YES</td>
<td>YES</td>
<td></td>
</tr>
<tr>
<td>EU Parent-Subsidiary Directive (EU PSD), subject to conditions:</td>
<td>EU Interest Royalties Directive (EU IRD), subject to conditions</td>
<td></td>
</tr>
<tr>
<td>• The entity receiving the dividend is taxed in another EU / EEA country</td>
<td>• Interest is paid to a related EU / EEA company which holds directly at least</td>
<td></td>
</tr>
<tr>
<td>(or in Switzerland) on its worldwide income (and is not subject to tax</td>
<td>25% of shares of the paying company for an uninterrupted period of 2 years</td>
<td></td>
</tr>
<tr>
<td>exemption on its total income) and</td>
<td>(or the lender and the borrower have a common parent company which directly</td>
<td></td>
</tr>
<tr>
<td>• Has held or will hold at least 10% (in the case of a company resident</td>
<td>holds 25% of shares in each of them). The preferential rate should</td>
<td></td>
</tr>
<tr>
<td>for tax purposes in Switzerland, at least 25%) of the shares in the Polish</td>
<td>be also applicable in the case where the period of two years of continuous</td>
<td></td>
</tr>
<tr>
<td>company paying the dividend for at least two years; this condition can be</td>
<td>holding of shares lapses after the day of interest payment</td>
<td></td>
</tr>
<tr>
<td>met prospectively. If the condition to hold the amount of shares for an</td>
<td>• Interest recipient is not subject to income tax exemption, applicable to all</td>
<td></td>
</tr>
<tr>
<td>uninterrupted period of two years is not satisfied, withholding tax (as a</td>
<td>revenues regardless of the place where they were acquired</td>
<td></td>
</tr>
<tr>
<td>rule at 19%) together with the penalty interest for late payment will be due</td>
<td>• The relevant DTT or another international agreement (concluded between</td>
<td></td>
</tr>
<tr>
<td>• The legal title for the holding must be ownership rather than any other</td>
<td>countries of the payer and the recipient tax residency) stipulates rights on</td>
<td></td>
</tr>
<tr>
<td>legal title</td>
<td>Poland to demand tax information from the tax authorities of the country</td>
<td></td>
</tr>
<tr>
<td>• The double tax treaty or another international agreement vests rights on</td>
<td>of residence of the interest recipient.</td>
<td></td>
</tr>
<tr>
<td>Poland to demand tax information from the tax authorities of the country</td>
<td>The EU Interest-Royalty Directive rules only applies as long as the interest is</td>
<td></td>
</tr>
<tr>
<td>of residence of the dividends’ owner or the country in which the dividend</td>
<td>set at a market level. Consequently, any off-market portion of interest can be</td>
<td></td>
</tr>
<tr>
<td>income is received</td>
<td>subject to withholding tax at the standard 20% rate (instead of the treaty-reduced</td>
<td></td>
</tr>
<tr>
<td>Irrespective of the EU PSD, as of 1 July 2019 new “pay-and-refund” mechanism</td>
<td>rate / WHT exemption) in Poland.</td>
<td></td>
</tr>
<tr>
<td>applies to all payments subject to WHT in Poland (unless additional measures</td>
<td>Irrespective of the EU IRD, as of 1 July 2019 new “pay-and-refund” mechanism</td>
<td></td>
</tr>
<tr>
<td>are taken).</td>
<td>applies to all payments subject to WHT in Poland (unless additional measures</td>
<td></td>
</tr>
<tr>
<td></td>
<td>are taken).</td>
<td></td>
</tr>
</tbody>
</table>
**Additional remarks**

Starting from 2019, Polish withholding tax system is a „pay-and-refund” system, meaning that a Polish entity remitting the payment is obliged to withhold tax at a standard rate (19% on dividends, 20% on other payments), and the recipient may apply for WHT refund. WHT exemption or application of a lower WHT rate will be possible in a limited number of cases where a Polish remitter will submit to the tax authorities statement confirming that all conditions for the relief are met (such statement may, however, trigger personal criminal penalties and additional tax liability) or tax authorities will issue a clearing in a form of a special tax opinion.

The Polish company distributing the dividend or paying out interest to non-residents 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 dividend / interest beneficiary 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 / interest should also hold a written confirmation from the recipient that the latter does not benefit from tax exemption on its worldwide income, if the exemption is to apply.

In addition, Polish tax remitter is obliged to assure due diligence when making payments subject to WHT and must follow new definition of a beneficial owner (which entails, among others, that a recipient carries out genuine business activity).

Dividends, interest and royalties would not benefit from the EU Parent-Subsidiary Directive or the EU Interest-Royalties Directive based tax exemption if such payments are connected with an agreement, a transaction, or a legal action or a series of related legal actions, where the main or one of the main purposes was benefitting from these tax exemptions and such transactions or legal actions do not reflect the economic reality. For the purpose of the above rule, it is considered that a transaction or a legal action does not reflect the economic reality if it is not performed for justified economic reasons, but results, in particular, in transferring the ownership of shares of a dividend paying entity or in earning revenue by that entity which is then paid as a dividend.

As there is no well-grounded practice regarding actual application of similar provisions, details of each structure
should be analyzed carefully to determine and address potential issues with taxation of dividends.

Dividends paid between companies which are resident in Poland for tax purposes may be 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. Due to introduction of “pay-and-refund” system, such dividends would be subject to a standard 19% WHT and the recipient could apply for a refund unless special conditions are met.

If the conditions for exemption 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) is taxed in the same way as dividends and is subject to the applicable withholding tax (taking into consideration the appropriate tax treaty).

Liquidation proceeds are subject to the same tax treatment as dividend, however, any withholding tax relief can only be sought under a relevant tax treaty.

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. Liquidation proceeds are also likely to share this treatment, even though liquidation is not explicitly mentioned in this provision.

**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 interest on loans drawn to acquire shares in a Polish company as tax deductible. Nevertheless, as of 1 January 2018 interest deductible against operating profit of an acquired entity (as a result of any „debt push down” strategies) would not be deductible. In lack of grandfathering rules, also interest resulting from “debt push down” reorganizations performed before 1 January 2018 would be disallowed as of that date.

In addition, interest on acquisition loan should be allocated to capital gains basket, therefore it does they do not decrease the taxable revenue from general business activities.

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 basis 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, based on the practice of the Polish tax authorities interest may be treated as tax deductible under the general rules (although the practice was changing in this respect over the years).

**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 he 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 (please note that starting 2019 there was a change to the transfer pricing documentation requirements).
Additionally, any interest on debt which exceeds maximum amount of a taxpayer’s credit capacity acceptable by a third party creditor is disallowed (so called “arm’s length credit capacity”).

**Restrictions on the tax deductibility of interest paid on loans**

Net financing costs (i.e. financing costs offset with interest revenue) are limited to 30% of tax adjusted EBITDA.

The limitation covers all financing (including historic debts that used to benefit from earlier thin capitalization regimes). The limitation also applies to third-party (e.g. bank) financing. Limitations apply if the net financing costs exceed PLN 3m (ca. €714k) annually. Non-deductible costs can be carried forward for 5 years.

**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 (or when the due interest is compounded) and should be allocated to appropriate revenue basket. 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

Methods of acquiring real estate by an investor

Asset deal
Purchaser acquires all or some of the assets of the company. It is possible to divide out certain elements, such as real estate and acquire only those parts.

Share deal
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).

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).

- 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.
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. 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.

• 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.

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, except for the lease agreements, the property-related rights and obligations are not automatically transferred as a result of the sale agreement. The lease agreements are transferred automatically with the acquired asset. As regards the remaining agreements, 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.

Potential restrictions related to the sale of a property

In case of transactions involving real estate, several restrictions resulting from applicable legislation may apply. As a general rule, transactions structured as assets deals are more likely to be subject to a greater number of such restrictions. These include as follows below.

A. Merger clearance

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 clearance of the President of the Office of Competition and Consumer Protection is granted.

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 worldwide turnover of undertakings participating in the concentration in the financial year preceding the year of the notification exceeds the equivalent of €1 billion or
- 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 €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 €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.

B. 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 held by State Treasury or local authority, 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 State Treasury or 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.

C. Restrictions for foreigners

As regards foreigners residing or having their registered seat within the territory of the European Union or European Economic Area, no special restrictions regarding acquisition of real estate by foreigners apply. The conditions differ with respect to the investors from remaining countries to which the following restrictions apply. As a general rule, such foreigners (or Polish entities controlled by a foreigner) are required to obtain a special permit of the Minister of Internal Affairs for acquiring a real estate in Poland. The permit is necessary when acquiring ownership of real estate or perpetual usufruct on the basis of any legal event (e.g. purchase, in-kind...
contribution, merger with a Polish entity, taking up shares in Polish entities).

The permit is issued upon a written request of a foreigner, 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.

D. Restriction in acquiring agricultural land

New legislation restricting trade of agricultural land was passed and came into force as of 30 April 2016. The new regulation restricts trade of agricultural land for both Polish and foreign (EU and non-EU) entities.

Under the new law on shaping the agricultural system, agricultural land is the land used for agricultural purposes or land that may be used for such purposes, excluding land intended for other purposes in applicable local spatial development plans.

The new law provides for major restrictions in sale of agricultural land such as:

- Agricultural land may be acquired only by individual farmers having agricultural education and residing in the same municipality where the land is located for at least 5 years.
- An obligation to obtain a permit of the Chairman of the Agricultural Property Agency for sale/acquisition of an agricultural land to/by persons other than individual farmers, including companies, under pain of invalidity.
› General prohibition on sale or transferring possession (e.g. under lease agreement) of an agricultural land within 10 years from its purchase; in ill-fated reasons a common court will be entitled to allow the sale

› Agricultural land acquired under Chairman of the National Agency for Agriculture Development (KOWR) consent within 10 years from its purchase; in case a sale or transfer of possession is necessary due to misfortune reasons being beyond the buyer's control, a common court is entitled to allow for the conclusion of the relevant agreement

› Agricultural Property Agency possess a pre-emption right to agricultural land regardless of the area (previously this right applied only to areas of at least 5ha)

› Agricultural Property Agency was given a wider buyout right in case other acquisitions that acquisitions under sale agreement e.g. merger, division or transformation of a current owner (perpetual usufructuary) of the land

› Agricultural Property Agency was given a right to buy of an agricultural land in case of partners change in partnerships

› Agricultural Property Agency was given a pre-emption and buyout right to purchase shares in companies owning an agricultural land, e.g. in case of share purchase agreements or share swap (excluding shares in public listed companies).

E. 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 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.

Key scenarios

- Asset deal
  - Sale of an enterprise / organized part of an enterprise (OPE)
  - Sale of standalone assets
- Share deal
  - Sale of shares
<table>
<thead>
<tr>
<th>Corporate income tax</th>
<th>Enterprise / OPE</th>
<th>Standalone asset</th>
<th>Share deal</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Step-up allowed</td>
<td>Step-up allowed</td>
<td>No step-up allowed</td>
</tr>
<tr>
<td>Goodwill may arise for tax purposes</td>
<td></td>
<td></td>
<td>No goodwill for tax purposes</td>
</tr>
</tbody>
</table>

**Transaction taxes**

<table>
<thead>
<tr>
<th>Enterprise / OPE</th>
<th>Standalone asset</th>
<th>Share deal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Out of scope of VAT</td>
<td>23% VAT (for commercial property), subject to VAT recovery under general rules</td>
<td>Out of scope of VAT</td>
</tr>
<tr>
<td>1%/2% transfer tax (pol. PCC) on gross value of enterprise / OPE payable by the buyer (non-recoverable)</td>
<td>VAT exemption may apply (exemption may be either obligatory or an option)</td>
<td>1% transfer tax (pol. PCC) on the FMV of shares payable by the buyer (non-recoverable)</td>
</tr>
<tr>
<td></td>
<td>If VAT exempt - 2% transfer tax (pol. PCC) on the FMV of asset payable by the buyer (non-recoverable)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>For further comments on VAT see next pages</td>
<td></td>
</tr>
</tbody>
</table>

**Contingent tax liability**

<table>
<thead>
<tr>
<th>Enterprise / OPE</th>
<th>Standalone asset</th>
<th>Share deal</th>
</tr>
</thead>
<tbody>
<tr>
<td>In general joint and several tax liability</td>
<td>No contingent tax liability for the events occurring prior to the transaction</td>
<td>Unlimited tax liability (up to the value of the investment)</td>
</tr>
<tr>
<td>Possibility to limit the contingent tax liability via pre-transaction tax certificates</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Poland. The real state of real estate**
<table>
<thead>
<tr>
<th>Reclassification risk</th>
<th>Asset deal</th>
<th>Share deal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reclassification into a transfer of standalone assets may lead to VAT arrears for the seller (additional penalties may apply)</td>
<td>Reclassification into a transfer of an enterprise / OPE may lead to challenging the buyer's right to recover input VAT charged by the seller and may result in transfer tax arrears (additional penalties may apply). For further comments on the risk see next pages</td>
<td></td>
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<table>
<thead>
<tr>
<th>Other advantages</th>
<th>Asset deal</th>
<th>Share deal</th>
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<tbody>
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<td>Less time-consuming and more straightforward legal wise. Possibility to deduct historical tax losses of the acquired company (no forfeiture rules)</td>
</tr>
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<td>Interest on any acquisition debt may not be tax effective (no debt push down possible).</td>
</tr>
</tbody>
</table>
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 gain is taxed at the rate of 19% (possibly 9% if the yearly revenue of the company does not exceed €1.2m). 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 a justified 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 buildings or structure separately.

VAT on the acquisition of real estate

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

- The supply of a building, infrastructure or part of a building or infrastructure in the course of its first occupation 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.

---

Has the supply of the building, infrastructure or part of a building or infrastructure being carried out in the course of the first occupation or prior to it?

- NO
- YES

Did a period shorter than two years elapse between the point of first occupation and the supply of the building, infrastructure or part of a building or infrastructure?

- NO
- YES

Did the supplier have the right to deduct input VAT in relation to the building, infrastructure or part of a building or infrastructure?

- NO
- YES

Did the supplier incur improvement expenses higher than 30% of the initial value of the building, infrastructure or part of a building or infrastructure?

- NO
- YES

Did the supplier have the right to deduct the input VAT in relation to the improvement expenses?

- NO
- YES

Had the improved building, infrastructure or part of a building or infrastructure been used to execute taxable activities for at least 5 years?

- NO
- YES

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**EXEMPTION WITH AN OPTION OF TAXATION**

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**TAXATION**

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Poland. The real state of real estate
According to the recently prevailing standpoint, use of a building, infrastructure or part of a building or infrastructure for the own business purpose of the owner should be considered as first occupation (provided that the owner performed VAT-able activities).

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 could not be subject to the above exemption (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 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 and infrastructure developed on the land.

The supply of ownership title / RPU to undeveloped land qualified as land for development purposes under a local spatial development plan or in a zoning decision is subject to 23% VAT (supply of other types of undeveloped 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.

As a rule, VAT tax point arises at the moment of delivery of goods, i.e. on the day of signing of the sale agreement. The invoice should be issued by the seller no later than until the 15th day of the month following the month in which the VAT point arose.

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.

Although the Polish Ministry of Finance has issued a set of guidelines with respect to VAT / transfer tax treatment of real estate asset deal transactions recently, a detailed analysis of each particular transaction is still recommended with this respect, as the guidelines are of rather general nature. Application for an advance tax ruling is still advisable.

**Recoverability of input VAT**

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

If the buyer uses the real estate partly for the purpose of exempt activities, the recovery of any input VAT 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.

Taxpayers also need to take into account so called preliminary pro-rata that limits input VAT recovery on purchases, if linked both with the economic activity of the taxpayer and other activities not related with business operations.

The recovered input VAT also 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).

**Date of input VAT recovery**

The right to recover input VAT arises in the period when - with respect to the acquired goods or services - the tax point arose (i.e. in the period in which the services were rendered to, or the goods were acquired by the purchaser). It cannot be, however, recovered earlier than in the period in which the taxpayer receives the respective invoice (prepayment invoices do not fall under this rule: they must be paid in order for input VAT to be reclaimable).

**Direct refund of input VAT**

A direct refund of any surplus input VAT 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.

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 a 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).

**Split payment**

As of 1 July 2018 split payment mechanism has been introduced to the VAT law.
At this stage VAT split payment is applicable to B2B transactions only and on a voluntary basis.

Buyers have a choice to pay the VAT amount into a dedicated bank account. If they do so, they may enjoy a number of advantages:

- No joint and several liability with respect to the amount paid on the supplier’s VAT account
- Entitlement to VAT refunds within 25 days from filing a VAT return, with no additional conditions applied
- The VAT amount payable will be decreased if a payment is made from a dedicated VAT account before the statutory deadline
- The increased penal interest rate and additional penal VAT rates of 30% and 100% will not apply.

**Share deal**

A capital gain on the sale of shares is subject to Polish corporate income tax at the standard rate of 19% (possibly 9% if the yearly revenue of the company does not exceed €1.2m). Any capital gain from the sale of shares should be allocated to the capital gain basket and hence could not be offset against costs allocated to revenue from general business activities basket (see diagram listing the items allocated to capital gains).

If the selling party is a foreign shareholder, the applicable tax treaty influences the tax implications of such a transaction. Significant part of Polish tax treaties (e.g. with Spain, France, Denmark, Sweden, Germany, Luxembourg etc.) 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 so-called Real Estate Clause).

Recently, Poland has implemented Multilateral Instrument Convention (MLI) on the basis of which most of tax treaties concluded by Poland may be equipped with Real Estate Clause and Principal Purpose Test. Verification of the current status of implementation of each such amendment under MLI is highly recommended.

The sale of shares in the Polish company is subject to a 1% civil law transaction tax (on the fair 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 generally not subject to Polish VAT.

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.
So far, other costs indirectly connected with acquisition of shares such as financing costs were in practice recognized as tax deductible costs when incurred. Due to the introduction of income baskets, the financing costs related to the acquisition of shares should in principle be allocated to capital gain basket and as a result, would not provide a tax shield against the taxation of operating profits.

**CFC Rules**

CFC is defined as:

1. a foreign entity (including i.a. company, partnership, tax capital group, trust, foundation, branch) seated in a tax heaven (as officially blacklisted by the Polish Ministry of Finance) or

   a) a foreign company (including i.a. company, partnership, tax capital group, trust, foundation, branch) having its seat or place of management in the country other than mentioned in point 1), with which:

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

<table>
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<tr>
<th>Income from capital gains shall include, among others:</th>
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<tr>
<td>• Income from sharing in profits of legal persons or other companies, including e.g. dividends, income from investment funds, income from redemption of shares, payments received as a result of a merger or demerger, interest on participation loans, etc.</td>
</tr>
<tr>
<td>• Income arising from in-kind contributions</td>
</tr>
<tr>
<td>• Other income from participation in legal persons or other companies, including income from the sale of shares, redemption or gains from a share-for-share exchange</td>
</tr>
<tr>
<td>• Income from the sale of certain receivables</td>
</tr>
<tr>
<td>• Income earned from property rights (e.g. royalties, know-how, copyrights), securities and financial derivative instruments, etc.</td>
</tr>
</tbody>
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Requirement to keep accounting records specifying revenues and costs for tax purposes, broken down by two types of sources (capital gains and other sources).
c) EU has not concluded an international agreement being a basis for requesting tax information from tax authorities of that country, or

2. a foreign company which jointly fulfills the following conditions:

a) the Polish taxpayer has on its own or together with other related entities directly or indirectly over 50% of shareholding or over 50% of votes in managerial, governing or supervising bodies of the CFC or over 50% stake in profits of CFC.

b) at least 33% 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
- Interest part of leasing rates
- Copyrights or intellectual property rights - including disposal of such rights
- Disposal or exercise of rights from derivatives
- Insurance, banking or other financial activity
- Transactions with related parties if the company does not create value added in economic terms or such value is marginal;

c) tax actually paid by the CFC is lower that the difference between the tax that would be due if the company was a Polish resident and the tax actually paid by the company in its country of residence; whereas tax actually paid means tax that should not be refunded or credited in any way.

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 significant business operations in this state. The Polish companies are obliged to hold registers of the CFC companies.

MDR

Since 1 January 2019 Poland has adopted mandatory disclosure regime (MDR) rules based on which taxpayers are obliged to report certain types of transactions to the Polish tax authorities. MDR will take a retrospective effect to any qualifying transactions executed after 25 June 2018. Any qualifying tax schemes implemented between 25 June 2018 to 1 January 2019 are reportable before 30 June 2019.
Tax arrangements commencing after 1 January 2019 are reportable within 30 days after the day when the scheme is: (i) available for the client, (ii) ready for implementation, or (iii) started, whichever is sooner. Based on the initial clarifications passed by the Polish Ministry of Finance, as transactions subject to reporting obligation would be counted especially transactions related to transfer of enterprise or share deals in case the taxpayers exceeds certain thresholds.

Considerable fiscal penalties up to PLN 10m may be imposed if the MDR information is not complete or reported late.

Taxpayers and intermediaries who have operations in Poland should review their policies and strategies for logging and reporting arrangements so that they are ready to report in early 2019.
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

Currently only a part of the territory of Poland is covered with local spatial development plans, mostly within the boundaries of bigger cities.

The two main spatial planning and development acts determining land development within a given municipality (commune) are the spatial development conditions and directions study and the local spatial development plan. However, from investors’ perspective, the local spatial development plan is of higher importance, as it determines their rights and obligations, while the spatial development conditions and directions study binds the local authorities only. In the case where no local spatial development 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 local spatial development 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 local spatial development plan (or whether such a plan will be adopted soon);

> in the event there is no local spatial development plan, whether a zoning decision has been issued for the real property in question; and

> whether the provisions of the local spatial development plan or zoning decision allow for the implementation of their investment plans.
Local spatial development plan

The local spatial development plan is adopted by the commune council and is binding for third parties (investors) as an act of local law.

Each local spatial development 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 local spatial development plan is rather complex and time consuming as the draft local spatial development plan is subject to „public consultation” with the parties concerned, as well as opinions issued by the relevant administrative bodies.

The provisions of the local spatial development 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 local spatial development plan may render the development of the given plot impossible. Moreover, in certain cases

Required to start the development of the real property:

- Spatial development plan
- Zoning decision

or
the legal provisions provide that selected investments are implemented solely based on local spatial development plans. This relates to i.a. large retail units or windfarms. It is currently planned by the government to extend the catalogue by introducing all investments substantially affecting the environment as requiring local spatial development plan in order to be proceeded with.

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

**Zoning decision**

In the case where no local spatial development 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 local spatial development plan or by a zoning decision (therefore, it can be said that a zoning decision substitutes a local spatial development 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 local spatial development plan is being adopted for a real property, zoning decisions related to this area expire if the provisions of the local spatial development 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 local spatial development plan for a given real property, prior to investment planning the investor should monitor the stage of works related to the local spatial development plan and should learn if it is possible to acquire a final building permit before the local spatial development 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. According to recent information, the government is planning to restrict the possibility of construction of investments based on the zoning decisions. Based on the initial information, it is planned to introduce a division between the areas not covered by the local spatial development plans into the developed and undeveloped areas. For the developed area, further to its determination by the municipality council, it will be possible to obtain a zoning decision. Within the undeveloped areas, implementation of new investments will, as a general rule, not be possible.

**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 local spatial development 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 21 days of the notification date.

The notification procedure pertains however generally to minor construction works or developing some of residential (single family) buildings.

**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 14 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 is granted. 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**

The EU regulations within energy efficiency of buildings, are ambitious, so is the polish legislation keeping up with the newest directions.

According to the information of the Ministry of Infrastructure and Construction, starting January 2017, the real estate market will be challenged with a new values of EP energy ratio for newly built buildings and some of the coefficient U factors for thermal transmittance of external walls of buildings. The new law, incorporated back in 2014 is entering into force gradually in order to make polish legal system compliant with the European Directive on the energy performance of buildings, according to which, until 31 December 2020 each and every newly built building shall be nearly zero-energy. Starting from 1 January 2019, nearly zero-energy performance requirement applies to all buildings owned or occupied by the public authorities.

The regulation will cover all of the architectural and construction designs which are going to be submitted together with the applications for a construction permission in 2017. New provisions introduce a gradual increase in the level of requirements up to the year 2021. Such a phased changes allow smooth adjustment of the construction market to the applicable legal requirements.
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.

**Liability towards subcontractors**

Based on the recently implemented changes, the investor is severally liable with the general contractor for the payment of remuneration due to the subcontractor for the construction works performed by the latter, the detailed description of which was notified to the investor prior to the commencement of such works. The liability of the investor does not occur if, within 30 days from the date of such notification, the investor objects to such works.

Such notification will not be required in case the investor and the contractor determine the scope of works to be performed by the designated subcontractor in the written agreement.

Thus, the investor is liable for payment for only such works, which were duly notified to him prior to their commencement.

Additional security for the investor constitutes the fact that the said
notification must be made in writing (accordingly, such form is also required for the investor’s objection).

Moreover, the said liability of the investor towards the subcontractor will be limited to the amount due to the subcontractor under his agreement with the general contractor, unless such amount exceeds the remuneration due to the general contractor for the works included in the notification.

**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 recognized 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.

Also, it is worth mentioning that certain construction services (listed in the VAT Act) provided by subcontractors may be subject to reverse charge mechanism (i.e. self-assessment of both input and output VAT).

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 appraisers.

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 period 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% (or 9% if the company’s yearly income is less than €1.2m) 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 (unless provided otherwise under a relevant tax treaty). 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.

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.

Under the Multilateral Instrument Convention (MLI) which was signed by Poland, Poland excluded the changes to the articles related to permanent establishment though, including e.g. provisions directly addressing cases where the construction works are artificially split into various stages to avoid permanent establishment status. Further developments in this respect should be closely monitored.
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.

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. As a general rule, commercial agreements are concluded for definite terms of 5 to 10 years, with the prolongation option.

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.
**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.

**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.

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.

- Promissory note - promissory note issued by the lessee is an effective way to protect the lessor’s potential claims.

- 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 - three-month notice applies
- If the rent is due every month - one-month notice applies
• If the rent is due for a period shorter than a month - three-day notice is sufficient
• 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 the subject of lease has defects that make it impossible to use it in the way defined in the lease agreement at the time of handover of premises, 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 does not pay 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 leased premises contrary to the terms of the agreement or their purpose and, despite a warning, does not cease to do so, or if a lessee neglects it to such an extent that the the leased premises are likely to be damaged - the lessor may terminate the lease contract without notice.
2.6.1.3. Agreement for the lease with the right to collect profits (dzierżawa)

By a lease with the right to collect profits agreement, the lessor commits to hand over a subject of lease 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 lease agreement gives not only the right to use the property but also to collect benefits from it, which is why the lease with the right to collect profits agreement usually concerns land.

The duration of an agreement may be definite or indefinite. However, the agreement for a period longer than one year should be concluded in writing, otherwise it is considered to be concluded for an indefinite term. 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 lease with the right to collect profits 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 lease with the right to collect profits in the same condition. However, the parties are able to modify this rule in the lease with the right to collect profits agreement. There are also some differences between a lease agreement and a lease with the right to collect profits 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 lease with the right to collect profits agreement without notice.
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 accounting records 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% (or 9% for “small taxpayers” whose annual revenue does not exceed €1.2m).

Calculation of taxable income

Taxable revenues minus tax deductible costs constitute the tax assessment base.

Polish tax law provides for separate income basket for capital gains and disallowing the offsetting of capital gains or losses against other sources of income. This means that any qualifying capital gain could be offset only against costs allocated to capital gain basket. It will be required to keep accounting records specifying revenues and costs for tax purposes, broken down by two types of sources (capital gains and other sources).

If it is not possible to assign expenses to a particular source of income, expenses are divided proportionately.

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.

Minimum levy

If the taxpayer rents a building (part of a building) a minimum levy may apply which is calculated based on the initial value of all rented real properties (including residential properties) reduced by the tax allowance of PLN 10m. The tax rate amounts to 0.035% per month (approx. 0.42% annually). In a situation, where only part of a building is rented, the minimum levy...
will be calculated with respect to the rented part proportionally. There is an exception for office buildings used for own purposes of the taxpayer. The tax is creditable against CIT. The tax authorities may question solutions used by the taxpayer aimed at avoiding payment of the tax and applied without a legitimate economic reason based on specific anti-avoidance rule.

**Limitations in deductibility of intangible service costs**

Fees for certain intangible services and royalties exceeding in total 5% of the adjusted tax base (tax EBITDA) are not tax deductible (with a safe harbor of PLN 3m).

The limit applies to such services as: advisory, market research, advertising, management, data processing, insurance, providing guarantees and other similar services as well as payments for the use of licenses, trademarks and certain other rights made directly or indirectly to related parties.

There are exceptions for payments being direct costs of goods/services sold as well for the re-invoiced expenses.

The new regulations provide for a carry forward mechanism of 5 years for non-deducted costs. i.e. such costs may be potentially deducted for the next 5 years within the applicable EBITDA limits.

Note that the above restrictions would not apply to transactions for which a taxpayer obtains an APA with the Polish Ministry of Finance.

**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:**

<table>
<thead>
<tr>
<th>Year</th>
<th>0</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Loss)/profit</td>
<td>(100)</td>
<td>60</td>
<td>10</td>
<td>10</td>
<td>20</td>
<td>5</td>
<td>20</td>
</tr>
<tr>
<td>Loss utilised</td>
<td>-</td>
<td>50</td>
<td>10</td>
<td>10</td>
<td>20</td>
<td>5</td>
<td>-</td>
</tr>
<tr>
<td>Carry forward</td>
<td>-</td>
<td>50</td>
<td>40</td>
<td>30</td>
<td>10</td>
<td>0</td>
<td>-</td>
</tr>
<tr>
<td>Effective tax base</td>
<td>-</td>
<td>10</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<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.
Starting from 2019 taxpayers are allowed to utilize up to PLN 5m of a tax loss incurred in a given tax year based on a one-off basis (in the five year period). General rules apply to the excess amount over PLN 5m.

**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 prorata basis computed for a given year.

Beginning of 1 January 2016 preliminary prorata must also be taken into account, which might result in limited recovery of input VAT related both to economic activity and non-business activities.

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, in 2019 local authorities are bound by the following maximum PLN annual tax rates:

- For land, PLN 0.93 per m² of land
- For buildings, PLN 23.47, 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.
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.
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 occur. 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.

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, within the due diligence regarding the real estate the investor should:

<table>
<thead>
<tr>
<th>Action</th>
</tr>
</thead>
<tbody>
<tr>
<td>verify basic information on the real estate (location, area, construction, legal title etc.)</td>
</tr>
<tr>
<td>examine compliance with laws and effectiveness of acquiring a legal title to the real estate,</td>
</tr>
<tr>
<td>examine restrictions with the disposal of real estate,</td>
</tr>
<tr>
<td>examine the necessity of acquiring third parties' / administrative bodies' corporate approvals for acquiring a real estate,</td>
</tr>
<tr>
<td>examine the collaterals established on the real estate,</td>
</tr>
<tr>
<td>examine the third-party rights to the real estate,</td>
</tr>
<tr>
<td>verify the permissible use of the real estate,</td>
</tr>
<tr>
<td>verify the construction of the real estate in order to obtain required permits and approvals</td>
</tr>
<tr>
<td>verify the access of the real estate to the public road,</td>
</tr>
<tr>
<td>analyze the responsibility of the buyer for the pollution of the real state</td>
</tr>
<tr>
<td>verify the amount of public burdens related to the real estate and lack of arrears with this regards</td>
</tr>
<tr>
<td>examine the potential claims to the real estate</td>
</tr>
</tbody>
</table>

Poland. The real state of real estate
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.

**Local Spatial Development Plan**

Development of an investment on the real estate is possible provided that buildings, plants and other industrial facilities comply with the relevant local spatial development plan for a given area. Therefore, it is essential to establish during the due diligence process whether there is a local spatial development plan covering the area where the targeted real estate is located and if so, what are the conditions of this local spatial development 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 local spatial development plan.

Within the review of the local spatial development 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.

**Revitalization**

The Revitalization Act entered into force at the end of 2015. Under the act, revitalization is the comprehensive process of rescuing degraded areas from crisis through integrated actions for the benefit of the local community, space and economy. A degraded area is a terrain in which there is a concentration of negative social phenomena as well as, for example, degradation of the technical condition of buildings, a low level of transit service, and poorly adapted urban planning solutions.
Under the new legislation, it is necessary for the commune authorities to pass local government law in the form of a resolution in establishing a revitalization zone or a special revitalization zone.

It should be noted that the Revitalization Act added new cases, when a commune may exercise the right to pre-emption of real estate, i.e. in case of transactions the subject of which is a real estate located within a revitalization area or special revitalization zone. In case of considered acquisition of real estate located in one of those plans, an investor should bear in mind the pre-emption right of a commune.

**Agricultural land**

The local spatial development 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 local spatial development 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 exclusion of the area from agricultural activity an annual fee has to be paid for ten years (see comments below).

An investor considering acquisition of agricultural real estate should also bear in mind existing restrictions relating to purchase of an agricultural land. Regulations in force provide for many specific legal restrictions and limitations and new legislation are to further restrain entities other than individual farmers from purchasing an agricultural real estate (please see comments in section 2.4.2).

**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.

After the judgement of the Constitutional Tribunal dated 19 July 2016, the Act on amendment of the Act on Property Management and the Family and Guardianship Code came into force on 17 September 2016. This act provides limitations of restitution of ownership of real estate nationalized under the Warsaw decree or transferring claims for reestablishing the rights for such.

According to the new act, in case when the real estate in Warsaw is e.g. assigned or used for public purposes, the Capital City of Warsaw may refuse to establish the right of perpetual usufruct to a previous owner of this real estate.

**A new provision is granting the State**

Treasury and the Capital City of Warsaw right of pre-emption in the event of the sale of rights and claims arising from the Warsaw decree and claims for the establishment of perpetual usufruct to the previous owner of real estate located in Warsaw. The pre-emption right also applies in case of sale of perpetual usufruct right established by the way of satisfying rights and claims arising from the Warsaw decree.

As a result, the new regulation should be taken into consideration during the investment process.
Fees - holding the real estate

Zoning fee

Zoning fee („Oplata 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
- 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 local spatial development 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 local spatial development 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 local spatial development 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 local spatial development 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**

Under the Polish law there are two regimes of liability for land (soil) contamination, depending on the period from which the contamination originates (with the border line being 30 April 2007). A current holder (in particular owner or perpetual usufructuary), revealed in the Land Register, is liable for soil contamination which occurred prior to 30 April 2007 or may be attributed to activity completed prior to that date, even if such holder did not actually cause the contamination.

Parties to the sale agreement cannot contractually exclude the above mentioned administrative 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 reimburse the purchaser with expenditures borne for the clean-up.

The situation is different for „new” land contamination, i.e. any soil damage, which occurred after 30 April 2007 or could be attributed to an activity completed after that date. An entity using the environment (i.e. an entity who has relevant permits to operate and use the environment) is liable for any such damage.

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 (organized part of an enterprise), the acquirer may be held liable for the outstanding tax liabilities of the seller. This liability should be 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 a going concern or an organized part thereof), the acquirer should not be liable for the outstanding tax arrears of the seller. However, if the transaction is reclassified into a sale of a going concern, the buyer might then be held liable for the seller’s undisclosed tax liabilities.
Acquisition of shares

In the case of a share deal, all the potential outstanding liabilities that are not statute barred 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 2019 there is still a tax risk in relation specifically to a target’s corporate income tax payments for 2013-2019, and to other tax liabilities, in general, for 2014-2019.

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
- 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
- Review of clauses aiming to reduce or mitigate potential tax exposures resulted from the reclassification of an asset deal transaction.
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 structure of the transaction, for example, transforming an asset deal into a share deal or the other way round; 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 and auditing
3.1 Introduction to the accounting framework in Poland

Polish accounting is regulated by the Accounting Act as of 29 September 1994 with subsequent amendments (the Accounting Act). The Minister of Finance has also issued several regulations which cover specific accounting areas, such as: financial instruments, consolidation, accounting principles for banks, insurance companies, investment funds and pension funds. Since 1994, the Accounting Act has undergone significant changes to bring Polish accounting regulations closer to the International Financial Reporting Standards (IFRS). However, the differences between the Accounting Act and IFRS, mainly following IFRS developments in recent years, continue to exist. The following information applies to financial statements prepared for the periods beginning on or after 1 January 2019.

In order to help implement the Accounting Act, the Polish Accounting Standards Committee (‘the Committee’) prepares and issues National Accounting Standards (KSR). As of 1 January 2019, twelve National Accounting Standards had been issued on different topics including:

- Cash flow statement
- Income tax
- Construction works
- Developers’ activity
- Management report
- Agreements on public-private partnership and concession contracts for construction works or services
- Property plant and equipment.

The Committee has also issued several position papers (not referred to as standards) with respect to e.g. accounting for emission rights, inventory count, inventory valuation, green certificates, financial statements of housing cooperatives and some aspects of bookkeeping. In the areas not regulated by the Accounting Act or National Accounting Standards, reference may be made to IFRSs. National Accounting Standards and the Committee’s position papers are available on the website of the Ministry of Finance.
The Accounting Act permits or requires some Polish entities to apply IFRS, as adopted by the EU, as their primary basis of accounting, rather than applying the accounting principles of the Accounting Act. Those regulations are summarised in the following table:

<table>
<thead>
<tr>
<th>Description</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 points 1, 3, 4 and 5).</td>
<td>Not permitted</td>
<td>Required</td>
</tr>
<tr>
<td>3. Entities planning to apply or applying for a permission to list on regulated market in Poland or other European Economic Area (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 for statutory purposes in accordance with IFRS as adopted by EU.</td>
<td>Choice</td>
<td>Choice</td>
</tr>
<tr>
<td>5. Branches of a foreign entrepreneurs that prepare separate financial statements for statutory purposes in accordance with IFRS as adopted by EU.</td>
<td>Choice</td>
<td>n/a</td>
</tr>
<tr>
<td>6. Other entities</td>
<td>Not permitted</td>
<td>Not permitted</td>
</tr>
</tbody>
</table>

In 2018 the Accounting Act imposed requirement to prepare financial statements in an electronic format (see also section 3.4 below).
The provisions of the Accounting Act and related regulations are applicable to, among others, companies and partnerships that have their registered office or place of management in Poland. For those entities that apply IFRS as the primary basis of accounting instead of Polish principles, the following sections of the Accounting Act still apply:

- Chapter 2 on bookkeeping
- Chapter 3 on inventory count
- Chapter 6A on report on payments made to government
- Chapter 7 on auditing, filing with the appropriate court register, providing access to and publication of financial statements
- Chapter 8 on data protection
- Chapter 9 on criminal liability
- Chapter 10 on special and interim provisions, and
- Article 49 in regard to directors' report.

Each entity is obliged to maintain its accounting books and other documentation which, in particular, comprises:

- A description of the entity's accounting principles
- Rules for keeping subsidiary ledgers and their link to general ledger accounts.

It should be noted that the violation of the Accounting Act requirements by a person responsible for drawing up the financial statements (usually the Management Board and Supervisory Board) may be recognised as a criminal offence, which is punishable by imprisonment for a term not exceeding two years, by a fine, or both.

The regulations, summarised in Chapters 3.3.- 3.5 below, apply to all entities in general. Certain types of entities such as banks, insurers, or investments funds might be governed by additional specific regulations.
Financial statements must be prepared in the Polish language and expressed in the Polish currency. Financial statements consist of:

- A balance sheet
- An income statement
- A statement of cash flows
- A statement of changes in equity
- Notes to the financial statements (split into an introduction and additional notes).

A cash flow statement and a statement of changes in equity are only required by entities whose financial statements are subject to a statutory audit.

For some specialised types of entities additional exceptions or requirements might apply in relation to primary financial statements such as, for example, a summary of investments for the investment funds and alternative investment companies.

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 for entities preparing their financial statements in accordance with Polish GAAP are determined by the Accounting Act. Companies listed on the Warsaw Stock Exchange, when preparing the financial statements in accordance with Polish GAAP, are guided by specific regulations for public issuers. This includes reconciliation between the results reported in accordance with Polish accounting principles and those that would have been met if IFRS, as adopted by the EU, had been applied.
Financial reporting

All entities governed by the Accounting Act are obliged to prepare their standalone and consolidated financial statements (the latter ones only if certain criteria are met) for each financial year. The financial year doesn’t have to be the calendar year. Listed companies are additionally obliged to publish semi-annual and quarterly reports. An entity must also prepare financial statements as of the date of the close of accounting records, and as a result of other events leading to the termination of the activities of an entity, for example, the close of business (liquidation date).

The standalone and consolidated financial statements should be prepared within three months after the balance sheet date and approved within six months after the balance sheet date.

Directors’ report

Specific entities such as, for example, joint-stock companies, limited liability companies, selected partnerships, mutual insurance companies, co-operatives, state-owned companies, investment funds and investment companies prepare, in addition to the financial statements, a financial review by management - the management report (the Director’s report). The scope of the report is defined in legal regulations and includes topics such as:

- Description of events that significantly impact upon the entity’s performance and that occurred during the reported period and after its closing date, till the date the financial statements are approved
- Predicted development of the entity
- Major achievements in the research and development area
- Actual and planned financial situation, including financial ratios
- Details about transactions in own shares
- Information on branches (business units)
- Financial risk management objectives and methods
- Key financial and nonfinancial efficiency metrics in relations to operations, as well as information on employment and natural environment
Information on the application of corporate governance rules (only public companies).

**Statement of non-financial information**

The listed entities that exceed the given thresholds are also required to present a statement and a consolidated statement of non-financial information. This statement includes among others:

- Description of the business model
- Key non-financial performance ratios
- Description of social, environment, human rights and anti-corruption policies, the associated risks and the effects of application of those policies
- That statement may be published on the entity’s web pages.

**Publication requirements**

Management is required to file the annual financial statements to the registration court together with the following documents:

- Auditor’s opinion, if the statements were subject to an audit
- Shareholders’ resolution on the approval of the financial statements and distribution of profit or coverage of loss
- Directors’ report (if applicable)
- The report on payments to the public administration (if applicable).

If not approved within 6 months after balance sheet date, additional filling is required from the entities which have not managed to approve their financial statements in the prescribed dates.

Listed companies are also required to file their financial statements with the Polish Financial Supervision Authority including interim (quarterly and semi-annual) reporting.

**Electronic format of financial statements**

In 2018, the Accounting Act imposed a requirement to prepare the financial statements in an electronic format. Financial statements need to be signed with a qualified electronic signature or a signature confirmed by the Polish trusted ePUAP profile. The electronic financial statements should also be filed electronically to the National Court Register.
In addition, financial statements (as of today - other than those prepared under IFRS) should conform to the logical structure published by the Ministry of Finance.

Audit requirements

Polish statutory audit requirements apply to all annual consolidated financial statements and to the annual standalone financial statements of the following entities that operate as a going concern:

- Banks, insurance companies, reinsurance companies, pension funds, investment funds (including alternative, closed, open and specialised funds), investment fund management companies, joint-stock companies and public companies, payment institutions, brokerage houses and firms

- Other entities that meet at least two of the following three thresholds in the financial year preceding the financial year for which the financial statements were drawn up:
  - Annual average employment (equivalent of 50 individuals employed full-time)
  - Total assets of at the end of the financial year (the PLN equivalent of €2.5 million or greater)
  - Net sales including financial income for the financial year (the PLN equivalent of €5 million or greater).

The statutory audit requirements also apply to entities after merger for the year when the merger occurred.

All statutory IFRS financial statements are subject to audit requirements.

There are also additional requirements in relation to audit or review of interim financial statements of public companies and investment funds.

Audits are governed by the relevant legal requirements in force which include:

- Chapter 7 of the Accounting Act
- Auditors Act
- National auditing standards issued by the National Council of Statutory Auditors
- Regulation (EU) No 537/2014 of the European Parliament on the council on specific requirements regarding statutory audit of public-interest entities.
Consolidation requirements

A capital group is a group which comprises a holding company and its subsidiaries.

According to the Accounting Act, a holding company is a company that controls another entity.

A capital group draws up its consolidated financial statements on the basis of standalone financial statements of entities that belong to the group. Groups which, in the preceding and current financial years, did not exceed at least two out of three of the following thresholds before intragroup eliminations:

- Annual average employment - equivalent of 250 individuals employed in full time
- Total assets of all group entities - PLN38.4 million
- Total sales and financial income of all group entities - PLN76.8 million.

or after intragroup eliminations:

- Annual average employment - equivalent of 250 individuals employed in full time
- Total assets of all group entities - PLN32 million

Total revenue of all group entities - PLN64 million are exempted from drawing up the consolidated financial statements.

A subsidiary is excluded from consolidation if:

- The shares in such entity were acquired, purchased or otherwise obtained for the sole purpose of subsequent resale within one year from the date of acquisition
- There are severe long term restrictions on the exercise of control over the entity which prevent free disposal of its assets, including net profit generated by this entity or which prevent exercise of control over the bodies managing the entity
- It is impossible to get the information necessary for preparation of a consolidated financial statement without delay incurring unreasonably high cost (applies in exceptional cases only).

A subsidiary doesn’t have to be included in the consolidated financial statements if the amounts stated in that entity’s financial statements are immaterial in relation to the holding company’s financial statements.
**Consolidated financial statements**

Consolidated financial statements comprise:

- A consolidated balance sheet
- A consolidated income statement
- A consolidated statement of cash flows
- A consolidated statement of changes in equity
- Notes to the consolidated financial statements (split into an introduction and additional notes).

Consolidated financial statements should be accompanied by a Group Directors’ report prepared by the Management Board of the holding company. Group Directors’ report can be prepared together with a Directors’ report of the holding entity as a single report.

Consolidated financial statements should be prepared at the same balance sheet date and for the same financial year as the financial statements of the holding company. If this date is not the same for all entities within the group, then consolidation may cover financial statements drawn up for a twelvemonth period different to the financial year, if the balance sheet date of those financial statements is earlier by no more than three months of the balance sheet date adopted by the group. Companies included in the consolidation should adopt consistent accounting policies and consistent methods of preparation of financial statements. If the accounting policies of consolidated entities differ from those applied for consolidation, then appropriate adjustments must be carried out at the consolidation level.

**Methods to include entities in consolidated financial statements**

A subsidiary is consolidated using the full consolidation method. Jointly controlled entities are consolidated using a proportional consolidation method or accounted for using an equity method. Associates are accounted for using the equity method. When the associate prepares its consolidated financial statements, the equity method applies to the net consolidated assets of the associate.
Hot topics in accounting with potential implications for the real estate industry

- IFRS 16 (Leases)

Introduction

Nowadays, a number of entities in Poland apply International Financial Reporting Standards (IFRS) for their accounting and reporting purposes (see section 3.1. above). Companies reporting under IFRS continue to face a steady flow of new standards and interpretations that may affect different areas, such as the presentation of financial statements, financial instruments and leases.

Some of the changes have implications that go beyond matters of accounting, as they may impact business decisions, such as the new regulations on leases (IFRS 16).

IFRS 16 - highlights and implications

The new standard will affect lessees across many sectors. The scale of impact is typically driven by the volume of operating leases and whether they contain multiple components such as lease and non-lease component.

- **Less complex**
  - Majority of current leases classified as finance leases
  - Contracts of less than one year and leases of low-value assets
  - Lease contract data readily available and easily accessible
  - Centralised operations and processes
  - Contracts do not contain non-lease components
  - Lease portfolio contains similar assets, terms and conditions
  - Standard, straightforward lease contract terms and consideration

- **More complex**
  - Majority of current leases classified as operating leases
  - Long-term contracts, such as commercial property
  - Lease contract data not readily available, e.g., stored manually, in multiple locations
  - Decentralised operations and processes
  - Lease contracts contain both lease and non-lease elements
  - Lease portfolio contains dissimilar assets, terms and conditions
  - Lease contracts contain variable consideration and renewal, purchase and termination options
Contrary to accounting by landlords, IFRS 16 significantly changes the accounting for lessees that are real estate tenants, requiring them to recognise most leases (i.e. rental contracts) on their balance sheets as lease liabilities with corresponding right-of-use-assets. Tenants will apply a single model for most leases. Generally, the profit or loss recognition pattern will change as interest and depreciation expense will be recognised separately in the statement of profit or loss (similar to today’s finance lease accounting). However, tenants can make an accounting policy election, by class of underlying asset to which the right of use relates, to apply accounting similar to current IAS 17’s operating lease accounting to ‘short-term’ leases and leases of ‘low value’ assets.

**Lessee accounting brings most leases on balance sheet**

<table>
<thead>
<tr>
<th>Initial recognition and measurement</th>
<th>Measure the right of use (ROU) asset and lease liability at present value of lease payments.</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROU asset</td>
<td>Depreciate the ROU asset based on IAS 16, or use alternative measurement basis under IAS 16 and IAS 40, if applicable.</td>
</tr>
<tr>
<td>Liability</td>
<td>Accrete liability based on the interest method, using a discount rate determined at lease commencement. Reduce the liability by payments made.</td>
</tr>
<tr>
<td>Profit and loss</td>
<td>Interest and depreciation are recognised and presented separately. Generally front loaded expense for an individual lease.</td>
</tr>
</tbody>
</table>

Today, tenants that enter into net leases of single-tenant properties may make different decisions about whether to lease or purchase the property. Many factors will influence a tenant’s decisions, including the nature of its business, its real estate requirements, debt and equity covenant restrictions, and access to capital.
Also, tenants may reassess their needs when negotiating their rental contract terms and payment. For example, a higher proportion of variable payments compared to fixed payments or shorter initial rental terms may result in smaller lease liabilities.

Landlords should consider the potential impact that shorter lease terms and an increased amount of variable rent would have on their business, including their financing costs, the value of the properties and, perhaps, increased operating costs as more frequent lease negotiations are held.

Tenants may request that landlords separately price non-lease components to help them support the allocation of consideration between the lease and non-lease components to minimise the financial statement impact of IFRS 16. However, landlords may be reluctant to disclose this information for proprietary reasons. Although a contractually stated price may be the stand-alone price for a good or service, it is not presumed to be for accounting purposes.

For tenants, recognising lease-related assets and liabilities could have additional financial reporting implications, such as:

<table>
<thead>
<tr>
<th>Impact</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><img src="image.png" alt="Graph" /></td>
<td>Increase in total assets and liabilities</td>
</tr>
<tr>
<td><img src="image.png" alt="Graph" /></td>
<td>Increase in net debt and earnings before interest, tax, depreciation and amortisation (EBITDA)</td>
</tr>
<tr>
<td><img src="image.png" alt="Graph" /></td>
<td>Increase in finance expense; decrease in operating expense</td>
</tr>
<tr>
<td><img src="image.png" alt="Graph" /></td>
<td>Shifts in cash flow statements (from operating to financing)</td>
</tr>
<tr>
<td><img src="image.png" alt="Graph" /></td>
<td>Front loading of lease expense on individual rental contracts</td>
</tr>
<tr>
<td><img src="image.png" alt="Graph" /></td>
<td>Deterioration of debt-related ratios</td>
</tr>
<tr>
<td><img src="image.png" alt="Graph" /></td>
<td>Change in deferred tax assets and/or liabilities</td>
</tr>
</tbody>
</table>
IFRS 16 may have additional business implications for tenants, such as:

- Off-balance sheet accounting (an important advantage today of leasing compared to buying an asset) will diminish under IFRS 16, so leasing may become less attractive.
- Debt covenants may need to be modified.
- Changes in the administration of rental contracts, management reporting, employee remuneration policies and key performance indicators.
- The volume of balance sheet driven sale and leaseback transactions is likely to decrease.

As demonstrated above for tenants, recognising lease-related assets and liabilities could have significant financial reporting implications that may potentially lead to a change in current business practices in relation to rental contracts.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019.

**Anticipated accounting impact of IFRS 16 on real estate entities - perpetual usufruct**

One of major impacts of IFRS 16 for real estate entities relates to accounting for perpetual usufruct (PU) of the land (see section 2.1.2), which meets the definition of leasing under IFRS 16. As such, under IFRS 16 entities record a right-of-use asset (ROU) and a lease liability corresponding to PU payments.

Residential developers present ROU with respect to PU related to work in progress within inventory balance and classify the lease liability as current. Otherwise, ROU with respect to PU is usually classified as non-current asset and accounted for accordingly (i.e. at cost less depreciation and impairment or at fair value). The corresponding lease liability is split between current and non current portion based on general IFRS guidance.
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