

10 THINGS YOU SHOULD KNOW WHEN INVESTING IN GERMANY OR ENGLAND AND WALES

1. IN WHAT WAYS CAN OWNERSHIP IN REAL ESTATE BE ACQUIRED?

IN GERMANY

Absolute Ownership

The most common way to obtain ownership in German real estate under German Law is in the form of absolute ownership. Pursuant to statutory law, absolute ownership extends to the land and to any buildings or other structures that are firmly built on the land, as well as to (immovable) fixtures and fittings and (movable) accessories. Ownership of real estate can be acquired either by way of an asset deal (purchasing the real estate directly from the seller) or by way of share deal (purchasing the company that owns the real estate). It is currently common to purchase 89,9% of the shares in the property owning company as this does not trigger real estate transfer tax (please see point 6).

Hereditary Building Right (Leasehold)

Another less common way is to obtain a hereditary building right (leasehold). Under German Law, a heritable building right is the right to erect or maintain a building on a plot of land, usually in return for payment of a regular so-called ground rent for a certain term. From the perspective of the owner of the land, the grantor of the heritable building right, the heritable building right is a limited right in rem encumbering his land. A heritable building right can be sold and transferred as well, however most likely the underlying heritable building right agreement with the owner of the land will stipulate a consent requirement and a pre-emptive right in the landowner's favour. Upon expiry of the term of the heritable building right, the land is transferred back to the landowner against compensation.

IN ENGLAND AND WALES

Freehold

Land may be owned absolutely by:

- individuals or
- corporate entities.

Owning the "freehold" gives a permanent right and interest in land, and this cannot be challenged by any third parties (including the State) save in exceptional circumstances, the most common of which is pursuant to "compulsory purchase" powers. (These are exercisable by the relevant local authority, if it is properly deemed that the land is required to implement local planning policies, and in such cases, the private rights of the individual or corporate entity can be extinguished, subject to the authority paying the owner appropriate compensation.)

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Long leases

Whilst an investor might expect to buy a freehold, sometimes this is not possible, and it is just as acceptable to buy a long lease (for a term of between 125 and 999 years).

The City Corporation (the local governing body for the financial district in Central London), for example, owns a large amount of freehold land in and around the City of London and grants long leases.

Also, some large buildings are owned on a joint venture basis using leases. These long leases are capital interests in land and are registered at the Land Registry.

An asset acquisition is usually more costly than a share acquisition. In a share deal, an overseas investor needs to check from its own legal, regulatory and tax point of view that it can purchase and hold the entity to be acquired.

2. WHICH CONSULTANTS ARE NEEDED AND WHAT ARE THEIR TASKS?

IN GERMANY

Most likely a real estate broker will be involved to find and secure the investment object of choice. Furthermore, technical and legal advisors will be needed to carry out a due diligence process to assess and evaluate the risks of the investment in the early stages of the transaction. The legal advisors will also be involved in drafting the necessary legal documentation and assisting in the completion and closing of the acquisition. Usually each party bears the costs of their advisors.

Furthermore, appointing a notary in Germany is very important (see point 3 below). However, the role of the notary is not exactly the one of a consultant because it shall be impartial and act as an arbitrator. The notary will check the public records to ensure that there are no issues that might hinder or delay the sale and acquisition process. However, the notary will not examine the property or assess the information on its condition. The notary's job is to make sure that the required documentation is correct, that the deed of sale and acquisition is notarised in the presence of the notary and to register i.a. the transfer of ownership.

IN ENGLAND AND WALES

Most likely a real estate agent will be involved to find and secure the investment object of choice. Furthermore, technical and legal advisors will be needed to carry out a due diligence process to assess and evaluate the risks of the investment in the early stages of the transaction.

Legal advisors will advise on such things as the legal title to the building, the current tenants and income stream, and any rights or obligations that may affect a new owner. They will also be involved in drafting the necessary legal documentation and assisting in the completion and closing of the acquisition.

Usually each party bears the costs of their advisors.

3. WHICH FORMAL REQUIREMENTS APPLY WHEN ACQUIRING REAL ESTATE?

IN GERMANY

An agreement concerning the transfer of ownership in real estate in the form of an asset deal must be in the form of a notarial deed. Any ancillary agreements (written or oral) outside of the deed that amend the deed may result in the entire sale and acquisition agreement to be invalid. The notarisation requirement however does not apply for certain share deal scenarios if a property is acquired by purchasing the shares in a company that owns the real estate.

IN ENGLAND AND WALES

In England & Wales, acquiring real estate is usually a two stage process: the parties first exchange the sale contract and secondly complete the sale by means of a transfer deed. Occasionally both happen simultaneously.

Simply signing a contract does not make it binding. Exchange of the contract is usually carried out between the buyer and seller's lawyers to make it binding.

The contract does not contain representations and warranties. The seller is not obliged to provide a statutory warranty for the title to the property. There is also no requirement for a developer to provide a warranty for the quality of the building structure, or the state of the property (however, it is common that such provisions are negotiated under the contract if buying directly from a developer). The contract deals with the mechanics of the sale and how income is apportioned at completion.

4. MUST (ACQUISITION) CONTRACTS BE SUBJECT TO THE LAW OF?

GERMANY?

German law differentiates between the agreements of obligations (Verpflichtungs-geschäft) in which the parties agree on the obligation to transfer the ownership and the material transfer agreement (Verfügungs-geschäft) in which the parties agree on the actual transfer of title as such.

For the agreements of obligations, the parties may freely choose the law that shall be applicable for this part of the sales and acquisition agreement (including e.g. representations and warranties).

The material transfer agreement of a German real estate must however be governed by German law.

ENGLAND AND WALES?

Yes, the law governing the contract and transfer deed will be the law of England and Wales.

5. ARE THERE ANY RESTRICTIONS CONCERNING THE PERSON OF THE PURCHASER ESPECIALLY CONCERNING FOREIGN INVESTORS?

IN GERMANY

There are no restrictions on the person of the purchaser. The purchaser might either be a natural person or a legal entity and be of any nationality. For foreign purchasers certified and apostilled powers of attorney will be required for notarisation of the sale and acquisition agreement.

It should further be noted, that the Transparency Register was established by the Money Laundering Act (AMLA) in 2017. The register is intended to record the ultimate beneficial owners of entities specified in the Act. In order to register the ultimate beneficiary for foreign entities certain requirements must be observed and notarised certificates of representation will be required.

IN ENGLAND AND WALES

There are no restrictions on foreign ownership or occupation of real estate in England or Wales, although various tax, anti-money laundering and other regulatory matters must be complied with.

Where the buyer is an offshore entity, the seller will require a legal opinion from lawyers in the jurisdiction where the buyer entity is based, stating that the buyer has power and capacity to enter into the transaction documents and is solvent.

6. WHICH TAXES NEED TO BE CONSIDERED WHEN INVESTING IN PROPERTY?

IN GERMANY

The two main taxes to be considered when investing in German real estate are real estate transfer tax (RETT) and value added tax (VAT). There might be many more taxes applicable depending on the structure and objective of the transaction.

RETT is imposed on the acquisition of German real estate (asset deal). In cases of a share deal, a threshold of acquisition of 90% of the shares in the property owning company is applicable to trigger the RETT. Furthermore, the proportion of the shares must be held for ten year, otherwise RETT is also triggered.

Generally, the acquisition of real estate located in Germany is exempt from VAT. However, in certain scenarios, the contracting parties may opt for VAT to be added to the purchase price so that the purchaser may claim for input VAT regarding the expenses related to the real estate.

IN ENGLAND AND WALES

The main taxes to be considered are stamp duty land tax (SDLT) and value added tax (VAT). There might be other taxes to consider depending on the parties, structure and objective of the transaction. SDLT is imposed on the direct acquisition of real estate (in an asset deal). The rate payable may vary depending on the asset, parties and transaction. In a share deal, a lower level of stamp duty is payable on the transfer of the shares.

Generally, the acquisition of real estate located in England and Wales is exempt from VAT. However, it is not uncommon for sellers to opt for VAT to be payable in which case that element (20% currently) may need to be added to the purchase price in certain circumstances. It may be possible for the buyer to claim back that VAT after completion.

7. WHAT INFORMATION IS VISIBLE TO AN INVESTOR FROM THE LAND REGISTER OF THE PROPERTY?

IN GERMANY

Every property in Germany is recorded in the land register of the respective local court. To complete the transfer of ownership, the new owner must be registered in the respective land register. Any third person especially the prospective purchaser of the real estate may rely on the contents of the land register. The purchaser can rely on the correctness of the land register. As long as the purchaser does not have knowledge to the contrary, he can acquire ownership in good faith.

IN ENGLAND AND WALES

Most property in England and Wales is registered at the Land Registry, which gives a State guarantee of title. To complete the transfer of ownership, the new owner must be registered as such at the Land Registry. Any person, especially the prospective purchaser of the real estate, may rely on the contents of the register. The register will disclose rights and encumbrances on the title, the price paid by the buyer, any security registered against it, leases to which it is subject and any restrictions that may need to be complied with in future dealings.

8. CONTRACTUAL MECHANISMS TO SECURE MUTUAL OBLIGATIONS SUCH AS PAYMENT OF THE PURCHASE PRICE

IN GERMANY

Large-scale investments by foreign investors are usually secured by additional contractual mechanisms to secure interest of both parties.

In particular, such sale and acquisition contracts can include detailed escrow mechanisms, such as escrow accounts are usually held by the notary. This provides an additional layer of security for the parties. However, there are legal requirements as to when an escrow account may be opened. The statutory law stipulates that an opening may only take place if there is a justified security interest according to § 54a Abs 2 Beurkundungsgesetz (BeurkG).

IN ENGLAND AND WALES

It is usual for the buyer to pay a deposit of 10% of the purchase price on exchange of the contract. That is then held by the seller's lawyers in escrow until the sale is completed. The contract sets out how this is dealt with.

Large-scale investments by foreign investors may need to be supported by a form of guarantee under the terms of the contract to underwrite the performance of the buyer.

9. WHEN IS THE TITLE TRANSFERRED TO THE NEW REAL ESTATE OWNER?

IN GERMANY

The title of ownership is not transferred directly when signing the purchase agreement. Several outstanding issues regarding the sale must be checked by the notary after signing first (e.g. that no pre-emption right (Vorkaufsrecht) is exercised). Once there are no outstanding issues, the new owner can be registered in the land register. The change of ownership is effective from the date of registration. Deviating agreements in the purchase agreement are only limited to the internal relationship between the parties of the purchase agreement.

IN ENGLAND AND WALES

Under English & Welsh law there is a distinction between the "legal title" and "beneficial title". Whilst the beneficial title in the property will pass to the buyer on completion of the purchase and dating of the transfer deed, legal title to the property does not transfer to the buyer until it has been registered at the Land Registry.

After completion the buyer's lawyers submit a transfer tax (SDLT) return and deal with the payment of the SDLT. They also register the asset transfer deed at the Land Registry. Land Registry fees are payable by the buyer, but are relatively small.

10. HOW ARE EXISTING LEASE AGREEMENTS TREATED WHEN TITLE OF OWNERSHIP IS TRANSFERRED TO A NEW REAL ESTATE OWNER?

IN GERMANY

If the acquired property (commercial or residential) is let to a third party the lease agreement will transfer automatically with all its rights and obligations to the new property owner (pursuant to Sec. 566 of the German Civil Code). The new property owner is then bound by the lease agreement and its term. This is because, as long as a lease agreement for a longer period than one year is concluded in writing, neither party can terminate it, except for good cause.

IN ENGLAND AND WALES

If the acquired property (commercial or residential) is let to a third party the lease agreement will transfer automatically with all its rights and obligation to the new property owner. The new property owner is then bound by its terms.

As England & Wales do not have a civil code, an occupational lease to which a building or any part of it is subject must largely contain all the conditions and rules that a tenant must abide by. As the income from tenants is key to the capital value of a building the lease terms must be scrutinised carefully. Note: residential leases are subject to considerably more regulation.

