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TRENDS™

LEGAL MAGAZINE

GLOBAL REAL ESTATE MARKETS IN REVIEW

INSIGHTS FROM:

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REAL ESTATE LAW

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CONTACT
E-MAIL: **rafaeltruan@lfnglobal.com**
TEL: **+34 9131 06660**
www.lfnglobal.com

Executive Director: **Rafael Truan Blanco**
Chairman: **Kai Graf v. der Recke** (HAVER & MAILÄNDER)
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Real Estate Publication Officer: **Jonny Nolan** (BHSM LLP)
Graphic design and DTP: **Bartosz Wiczynski** (TURCZA Kancelaria)

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REAL ESTATE **LAW**

WHAT IS INSIDE...

CHAIRMAN'S INTRODUCTION

The Law Firm Network
FAR - REACHING LEGAL SOLUTIONS

We have finally reached the end of 2020, a very complicated year for the global real estate market.

During this difficult year, the Real Estate group of The Law Firm Network (LFN) has kept close contact through regular online gatherings and has published four issues of its legal magazine TRENDS.

The main aim of TRENDS is to offer an overview of the most interesting and "hot" topics in the real estate market, as well as an update on newly enacted (emergency) legislation affecting this market around the world.

In this issue of the magazine, we shall cover the following subjects: the Italian real estate market with a possible outlook on 2021; the future of the office market in the UK; investment and leverage in the UK hospitality sector; new COVID-19 legislature affecting tenants in Ireland; foreign investment and ownership in the Korean real estate market; the latest amendments to the Karnataka land reforms in India; an overview of the notional taxation of real estate that is to be implemented in Denmark; and the latest updates from Germany on the commercial tenant rental situation.

I hope you will find our articles interesting and useful.

I also take this occasion to extend to you my best wishes for the upcoming Holiday Season.

Enjoy the reading!

Written by:

Giulia Comparini
Attorney-at-law
Co-chair, LNF Real Estate Group
Cocuzza & Associati, ITALY
COCUZZAEASSOCIATI.IT

The Law Firm Network, founded some 30 years ago in 1989, is a strong non-exclusive association of independent law firms from around the world whose principal lawyers have close personal and professional relationships. The Network has members in approximately 60 countries and we have an extended global network with quality law firms in 80 additional countries.


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NOTIONAL TAXATION OF REAL ESTATE TO BE IMPLEMENTED IN DENMARK

by Lars Hammer Wentoft & Jacob Monberg

In October 2020, the Danish government and its supporting parties entered into an agreement on notional taxation of companies' property gains. The initiative is a result of the government's agreement on the right to early retirement and the financing hereof. The newly announced rules are expected to have major tax-related consequences for a large number of real estate companies and corporations.

Ongoing taxation of companies' property gains

The Danish government wants to ensure efficient taxation of companies' property gains by introducing an ongoing taxation of value increases on companies' properties according to a notional principle corresponding to the way pension companies are taxed today, meaning that increases or decreases in the property value must be calculated annually.

The tax will be introduced with future effect from 2023 and according to the agreement, the notional tax must apply to companies etc., which are subject to the general corporation income tax of 22 percent.

Companies are already taxable on property gains, but today taxation does not take place until a profit is realised in connection with a sale of the property. Companies can thus avoid the property gains taxation by placing the property in a subsidiary and selling the subsidiary instead of the property, as gains on subsidiary shares are exempt from taxation.

Valuation

The precise delimitation of which companies and properties are covered, the access to deductions in the event of a decrease in value or in the event of a sale at a loss, as well as consequential changes in notional taxation will have to be finally determined in connection with the preparatory legal work.

Properties used in company operations

Properties which the company predominantly uses in its own operations are exempt from notional taxation. This applies to e.g., properties used by the company itself or a group company for administration, warehousing, production or agriculture.

Smaller real estate companies and personally owned properties are exempt

In order to reduce the administrative burdens associated with the proposal for both the companies and the Danish tax administration, an amount limit of DKK 100 million will also be introduced. This excludes real estate companies with smaller real estate portfolios. It is expected that this limit will be assessed at group level.

Personally owned properties are also exempt, and the notional tax will thus not apply to personally owned companies. Personally owned means for tax purposes, both direct personal ownership, but also includes tax-transparent units, which cover e.g. P/S, K/S or I/S. This means that private ownership may become more fiscally favourable in the corporate tax scheme or through partner companies (P/S) or other tax-transparent units (K/S or I/S).

The consequence for real estate investors

The consequence will be a higher and advanced tax payment, which in terms of liquidity must be financed by the real estate company. Notional taxation will place a financial and liquidity pressure on the real estate companies subject to the new rules, and it is feared that a number of real estate companies may be forced to realise all or part of their portfolio in order to be able to finance the new notional taxation.

This will continuously entail that a valuation of the properties must be made annually, which is considered to be extremely complicated, and it can also lead to conflicts about whether the assessments are correct or not and will also trigger costs.

It must also be assumed to have major consequences for real estate transactions. In this regard, the tax profits will, to the extent that will follow from the new rules which we do not yet know, be taxed on an ongoing basis. The discussion on the valuation of deferred tax and its exchange rate will be limited to any difference in value between the current revalued tax values and the trade value that emerges from the parties' agreement.

It is advisable to consider whether the ownership of one or more of the properties should be transferred from company management to personal ownership or ownership through tax-transparent units. In the case of new acquisitions, it must be considered whether the acquirer should be one or additional persons or tax-transparent entities.

The development regarding this subject will be followed on an ongoing basis at mazanti.dk, including how the different elements of the rules will end up in the final law.

Written by:

Lars Hammer Wentoft
Attorney-at-law
Mazanti-Andersen, DENMARK
MAZANTI.DK

Jacob Monberg
Attorney-at-law
Mazanti-Andersen, DENMARK
MAZANTI.DK

Key Contact:

Louise Gjessing Lund Jensen
Attorney-at-law
Mazanti-Andersen, DENMARK
MAZANTI.DK

WILL COMMERCIAL TENANTS AFFECTED BY THE COVID-19 LOCKDOWN STILL HAVE TO PAY RENT?

by Dr. Tobias Eisenmann
& Kai Graf von der Recke

The COVID-19 pandemic has a lasting effect on the legal relationship between landlord and tenant and causes considerable economic restrictions. This raises the question whether the commercial tenant remains obliged to pay the rent during COVID-19 restrictions, even if he is severely impaired in the use of the rental property, or whether the severe restrictions on use lead to claims for rent reductions or even disrupt the basis of the lease agreement.

During the first COVID-19 lockdown in April/May 2020, the right of landlords to terminate lease agreements due to rent arrears was substantially restricted in favour of the tenants. Rental debts incurred in the period 1 April 2020 to 30 June 2020 due to the pandemic do not entitle the landlord to terminate the lease, neither for ordinary nor extraordinary cause. The exclusion of termination applies to both residential and business premises. The restriction on termination ends on 30 September 2022.

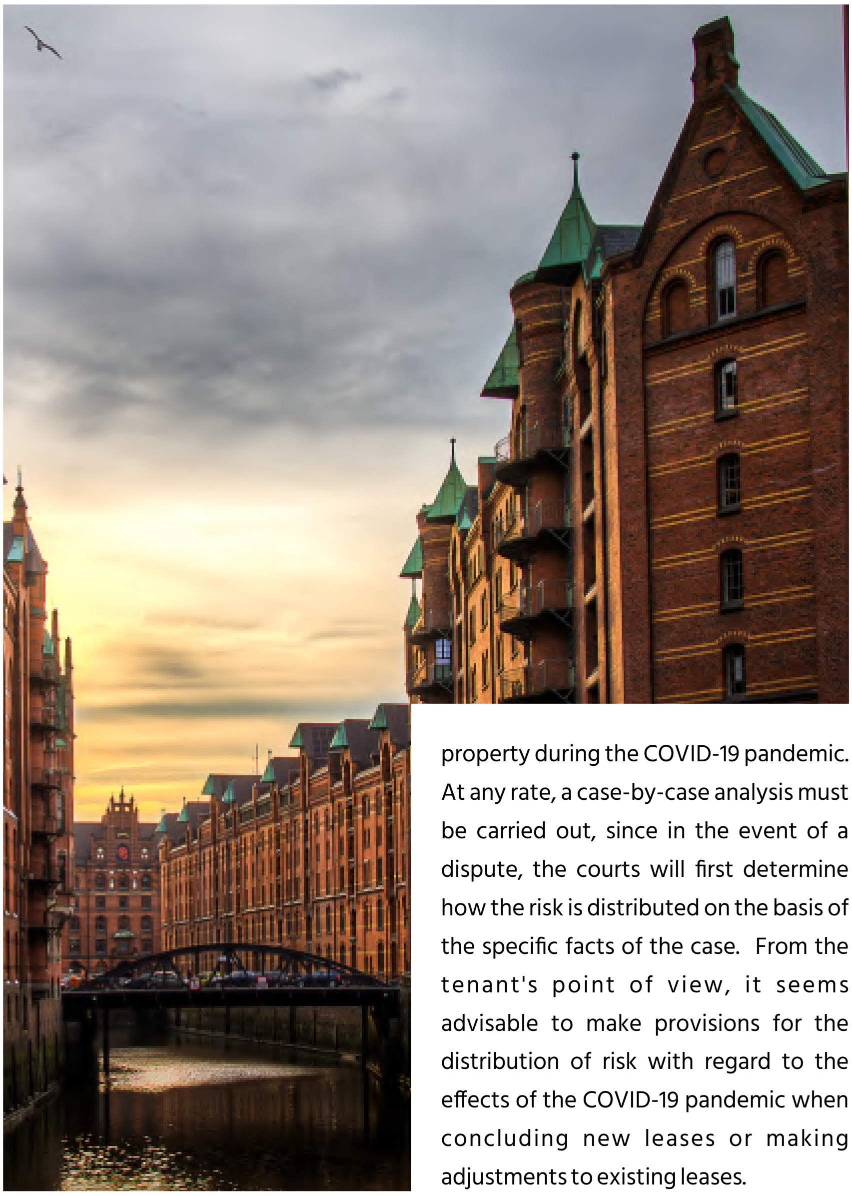
During the current / second COVID-19 wave, which has again led to an extensive lockdown, various businesses are forced to close their stores, as governments of the German federal states have identically imposed operating bans or restrictions on various facilities including clubs, discotheques, amusement facilities of all kinds, art and cultural institutions, trade fairs and exhibitions, sports facilities, taverns and restaurants, to name only a few. Operators of such facilities are wondering whether they can reduce or stop their rental payments, or whether they have a special right of termination. Ultimately, this relates to the question of who bears the risk of use if the leased property cannot be used, or cannot be used as intended, due to COVID-19 restrictions.

There is not yet any uniform case law on this, moreover no case law from the German Federal Court of Justice. The current legal sources are limited to decisions from the Courts of first instance, i.e. District Courts, which mostly relate to retail spaces. While they do show a certain tendency in favour of the landlords, this is only a

current snapshot, and any rulings by the Appeals Courts and by the Federal Supreme Court are fully open and unpredictable.

Several German District Courts have upheld the tenant's obligation to pay rent for retail space during the initial lockdown and largely rejected a rent reduction. The courts have argued that the sovereign measures ordered by the

German federal states (lockdown) serve to protect the population from general health risks and are not directly linked to the specific condition of the rental object, but only to the operation of the respective tenant. Further, the courts held that the measures are not based on the specific structural conditions, but generally on the type of use and the fact that public traffic takes place in the affected areas which favours infections. The courts held that it does not make a difference that the premises at issue were let as retail spaces with all goods for daily use and consumption. The courts ruled that the rented object is still suitable for this purpose in the same way as before the lockdown. Only its operation is forbidden, irrespective of questions regarding the condition or location of the rented property. This circumstance falls within the tenant's sphere of risk.



The courts have also ruled that the tenant cannot demand an adjustment of the contract on the basis of frustration of contract. Courts have not found such interference with the contractual relationship justified for a mere temporary closure of one or two months. The tenants were also entitled in principle to state aid, which is why the Courts did not consider it to be unreasonable for them to adhere to the rental agreement.

On the other hand, the Regional Court of Munich has ruled that since the early days of the application of the Civil Code, it has been recognised that due to prohibition of opening of sales outlets for retail or hospitality business, a defect of the leased object may exist because the suitability of the rented premises for the contractual use is cancelled or reduced. The Regional Court of Munich then referred to case-law of the Reichsgericht (German Supreme Court between 1879 and 1945) and pointed out that the now emerging literature by legal scholars includes strong voices that give priority to the right to reduce rent in order to resolve COVID-19-related conflicts of tenants. Against this background, the court considered the present restrictions of the rental object to be a rental defect and awarded the tenant a right to reduce the rent. For the time of the full lockdown in May 2020, the court came to a rent reduction of 80%, and for June 2020 of 15%, where customers were only admitted by one customer per 20 square meters and customer access was subject to a hygiene concept.

It remains to be seen how the Appeals Courts and the German Federal Supreme Court will assess the risk of use of a rental property during the COVID-19 pandemic. At any rate, a case-by-case analysis must be carried out, since in the event of a dispute, the courts will first determine how the risk is distributed on the basis of the specific facts of the case. From the tenant's point of view, it seems advisable to make provisions for the distribution of risk with regard to the effects of the COVID-19 pandemic when concluding new leases or making adjustments to existing leases.

Written by:

Dr. Tobias Eisenmann
Attorney-at-law
Haver & Mailänder Rechtsanwälte
Partnerschaft mbB, GERMANY
HAVER-MAILAENDER.DE

Kai Graf von der Recke
Attorney-at-law
Haver & Mailänder Rechtsanwälte
Partnerschaft mbB, GERMANY
HAVER-MAILAENDER.DE

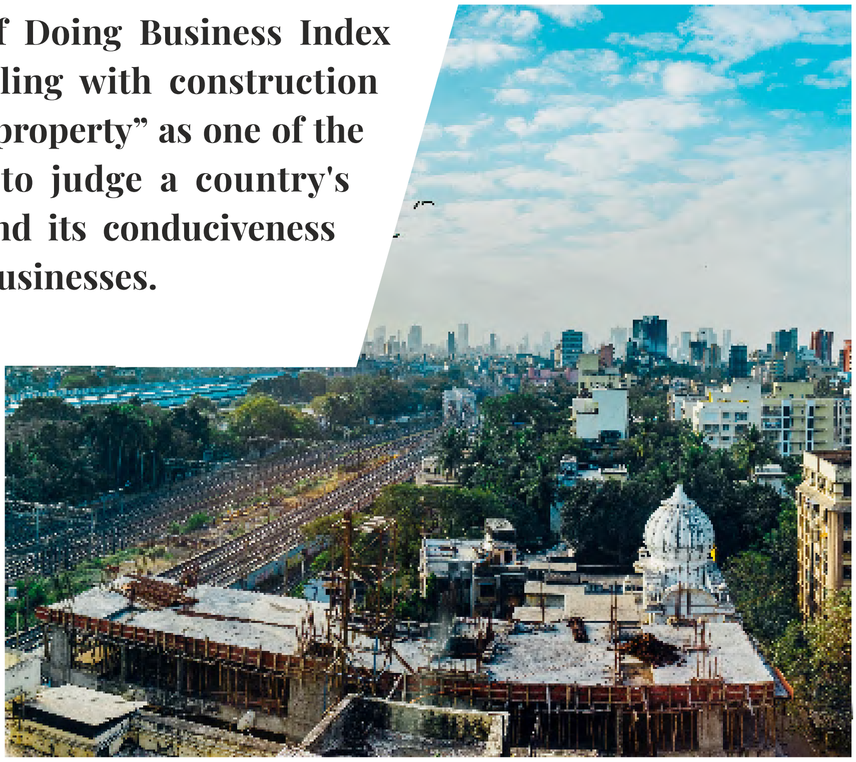
INDIA

LATEST AMENDMENTS TO THE KARNATAKA LAND REFORMS LAWS

Acquisition of agricultural land for industrial development becomes easier.

by G. Deepak Raj

The World Bank's Ease of Doing Business Index ("EoDB Index") lists "dealing with construction permits" and "registering property" as one of the 10 parameters by which to judge a country's regulatory environment and its conduciveness for starting and operating businesses.



The Business Reforms Action Plan Portal, of the Ministry of Commerce and Industry, oversees an ambitious reform program with State Governments to move toward faster, easier and simpler regulations to start and operate businesses. The efforts of the State Governments to this end will markedly impact and elevate India's image as a coming-of-age economic bellwether.

It is also to be noted that historically, Indian society has been largely agrarian, with the agricultural sector accounting for the employment of the majority of the Indian population. Foreign Direct Investment ("FDI") is currently permitted up to 100% under the automatic route for the following agricultural and plantation activities:

- Floriculture, Horticulture and Cultivation of Vegetables & Mushrooms under controlled conditions;
- Development and Production of seeds and planting material;
- Animal Husbandry (including breeding of dogs), Pisciculture, Aquaculture, Apiculture;
- Services related to agro and allied sectors;
- Tea sector including tea plantations;
- Coffee plantations;
- Rubber plantations;
- Cardamom plantations;
- Palm oil tree plantations; and
- Olive oil tree plantations.

Apart from the above, FDI is not permitted in any other agricultural or plantation activities. The Union and State Governments have undertaken a number of steps to attract investment, particularly FDI, in the agricultural sector as well as related and allied sectors, like logistical services, agricultural inputs, food storage and processing and industries.

With a view towards the EoDB Index, the Government of the State of Karnataka has enacted the Karnataka Land Reforms (Amendment) Act, 2020 (the "2020 Amendment Act") as an amendment to the Karnataka Land Reforms Act, 1961 (the "Principal Act") with retrospective effect from 20 November 2019.

Another similar measure undertaken to attract FDI to the State of Karnataka and improve India's ranking on the EoBD Index is the announcement of the

Karnataka Land Reforms (Amendment) Ordinance, 2020 with effect from 13 July 2020. Subsequently, the July Ordinance has been repealed under the re-circulated Karnataka Land Reforms (Second Amendment) Ordinance, 2020 (the "November Ordinance"), which is in effect since 2 November 2020.

Prior to the 2020 Amendment Act and the Ordinance, agricultural land could only be purchased by agriculturists and by non-agriculturists with consent or exemption.

The 2020 Amendment Act and November Ordinance have lifted significant regulatory hurdles and barriers and consequently, enable companies to acquire and sell agricultural land, subject to certain limitations.

In light of the 2020 Amendment Act, any person is now entitled to acquire agricultural lands in the State of Karnataka for industrial development projects with investments above US$2 million approved by committees like, the State High Level Clearance Committee and State Level Single Window Clearance Committee with the approval of the State Government. The amendment aims to bring about a single-stage approval process for industrial developments as opposed to a multi-tiered approval process for seeking exemptions to acquire agricultural land, project incentives, development sanctions, etc.

Furthermore, with the State Government's push to digitise land records and related approval processes, the Karnataka Udyog Mitra portal is also proposed to be integrated with the Kaveri portal. This would enable prospective investors to set a date for registration of the property, as well as pay the relevant stamp duty and registration charges online.

To summarise, the 2020 Amendment Act is a step in the right direction to promote Karnataka as a favourable destination for investments from within India and abroad and increase the ease of doing business in Karnataka.

Written by:

G. Deepak Raj
Attorney-at-law
Poovayya & Co., India
POOVAYYA.NET

LEGISLATIVE PROTECTIONS FOR IRISH RESIDENTIAL TENANTS IN THE MIDST OF THE PANDEMIC

by Siobhán Whelan

The harsh economic impact of COVID-19 restrictions has been well-documented internationally and posed unprecedented challenges for lawmakers who introduce them. This article discusses the Irish legislature's management of issues arising for residential tenants. Two pieces of Irish residential tenancy legislation arising directly from COVID-19 are the Residential Tenancies and Valuation Act 2020 and the Residential Tenancies Act 2020. This article explores the workings of each and, through a brief comparison, demonstrates the change in Ireland's management of the pandemic over time.

The Residential Tenancies and Valuation Act 2020

The Residential Tenancies and Valuation Act 2020 ("the Act") came into effect on the 1 August 2020 to replace the Emergency Measures in the Public Interest (COVID-19) Act 2020 ("Act of 2020"). The Act is to provide a new legal basis to oversee the moratorium on rent evictions and rent increases.

1. Tenants to Self-Declare

While the Act of 2020 saw a blanket ban on evictions and rental increases across the rental sector, the primary focus of the Act is to give rental protection to a category of tenants who are at risk of eviction from their rental properties by reason of failure to pay their rent. In order to get the protection of the Act the tenant must serve a declaration in writing to the Residential Tenancies Board ("RTB"), with a copy of the declaration to the Landlord. The tenant must declare that they are:

1. A "relevant person"; and
2. As a consequence, they face a significant risk of their tenancy being terminated due to the non-payment of rent.

The qualifying criteria in order to be deemed a "relevant person" includes:

1. Being unable, or having been unable to work, due to contracting COVID-19 without entitlement to be paid;
2. Being in receipt of, or entitlement to receive, the temporary wage subsidy or supplementary welfare allowance; or
3. Being in receipt of any other payment out of public moneys provided to alleviate the financial hardship resulting from COVID-19.

The tenant can claim protection from eviction during the "emergency period". This is defined in the Act as being from

the date of commencement of the Act up to 10 January 2021.

2. 28 Days Arrears Notice Period

The Act also affords a greater protection period for tenants who are at risk of eviction as a result of the non-payment of rent. The Act extends the arrears notice to a 28-day arrears notice; this was previously 14 days. The 28-day arrears notice must be served by the landlord on the tenant and the RTB. The RTB must then provide information to the tenant to allow them obtain advice from the Money Advice and Budgeting Service ("MABS"). If the tenant fails to pay the rent after the 28-day period, then the Landlord can serve a 28 day notice of termination which also must be served on both the tenant and the RTB. The RTB must furnish details to the tenant of their entitlements from the Department of Employment Affairs and Social Protection and inform them of their right to refer a dispute of the notice of termination to an adjudicator in the RTB with an appeal to the tribunal.

Regard must be had to the advice provided to the tenant in making any decision or determination. The Act extends the period of termination for a tenant who can seek the benefit of the Act to a period of 90 days after the service of the notice of termination or on the 11 January 2021 whichever is the later.

3. Prohibition on Rent Increases

Section 6 of the Act prohibits rent increases to 10 January 2021 unless it was an increase that came into effect prior to 27 March 2020. This section appears at odds with the intention of the Act which was to afford protection to tenants specifically affected by COVID-19. In the summary of the Bill from the Oireachtas it was noted that Section 6 was to apply to persons affected by that Part of the Act being "relevant persons". This was not carried over in the drafting of the legislation and instead of limiting the application of Section 6 to "relevant persons" being the persons defined in that Part of the Act, it reads instead that it applies to all tenants. It appears from the advices being offered by the RTB that they have adopted their own view that Section 6 of the Act only applies to "relevant persons". Clarification is certainly required on this point.

4. Commercial Tenancies Outside Parameters of the Act

The Act clears up the ambiguity brought about by Section 5(7) of the Emergency Act 2020 in that it left open the interpretation of the section that a prohibition on evictions falling outside of the Residential Tenancies Acts also extended to commercial tenancies. The Act removed this section and so it is no longer in effect, which clears up any ambiguity that there might have been.

5. Conclusion – Landlord to Shoulder the Burden of the Economic Impact Of COVID-19?

The Act attempts to strike a balance for both the tenant and landlord by setting out a list of qualifying criteria that the tenant must meet to avail of the Act. The previous blanket ban on evictions meant that Landlords were left in a situation where they could not evict a tenant even in circumstances where there was no economic impact seen by a tenant as a result of COVID-19. A false or misleading self-declaration by a tenant is a criminal offence and is an attempt to prevent abuse of the Act . There does need to be clarification on the blanket ban on rent increases which seems at odds of what the Act set out to do which was to provide protection to "relevant persons". While the Act provides a welcome reprieve to a tenant who has found themselves in difficulty as a direct result of COVID-19 it does leave some landlords in a precarious position of having to shoulder the economic burden of the consequences of the Act especially in such circumstances where previous moratoriums that were offered by banks to mortgagors are now coming to an end.

<u>The Residential Tenancies Act 2020</u>

The Residential Tenancies Act 2020 ("the 2020 Act") is another piece of emergency legislation that has evolved as a result of COVID-19. It recognises the difficulties that would be faced by tenants in finding alternative accommodation during the emergency periods and the consequences resulting from the spread of COVID-19. Signed into law on 24 October 2020, it is the latest update to the residential tenancy legislation.

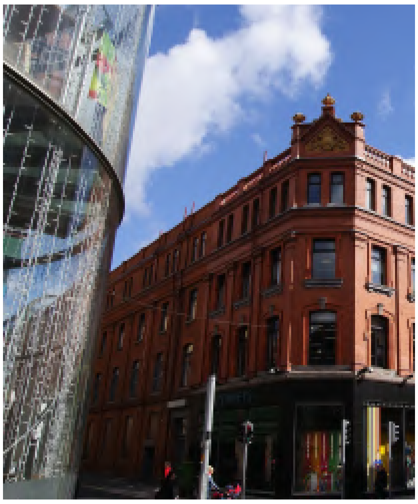
A. Operation of the Protections

The 2020 Act is only operable during emergency periods which is defined in the 2020 Act as a period in which the Minister for Health imposes a restriction on travel outside a 5km radius of a person's place of residence for a period as specified in the relevant legislation. The relevant legislation is made under Section 31A of the Health Act 1947 which allows for travel restrictions on affected areas.

B. Revised Termination Dates

The 2020 Act is to provide a level of protection to tenants against eviction where a notice of termination was served prior to or during an emergency period. The 2020 Act allows for a "revised termination date" which is the date 10 days after:

· In instances where the notice of termination was served before the emergency period, the revised date will



emergency period; or

· Where the notice of termination was served during the emergency period, the period of notice given in the notice of termination and the unexpired period of the emergency period.

Should there be any further subsequent emergency periods these periods are to be included in calculating the revised termination date.

In instances where a tenant has remained in occupation of a dwelling after the expiration of the required period of notice and before an emergency period commenced, whether that be with or without landlord consent, that tenant shall be entitled to remain in the dwelling until the revised termination date which in this scenario is 10 days after the expiration of the emergency period. The Tenant does not acquire any rights under Part 4 of the Residential Tenancies Act 2004 under this section.

C. Loss of Protection

Where a notice of termination was served for failure by tenant to comply with one of their obligations then the Tenant does not get protection of the 2020 Act. These include:

· Where a Tenant or other visitors behave in anti-social behaviour;

· Where the dwelling is used for a purpose other than as a dwelling without the owner's consent;

· Where acts of the tenant that would invalidate the insurance policy on the dwelling; and

· Where there is a threat which threatens the fabric of the dwelling.

The Act does not apply to a dwelling to which the provisions of the 2020 Act apply (as set out above) as these Tenants are separately protected under this legislation.

December 2020: An Assessment of the Provisions

A notable difference between these instruments is their definition of the concept of the "Emergency Period". This indicates the improved understanding of the pandemic gained by the legislature between their commencement dates – August and October 2020 respectively. In the interim, specifically mid-September, the Irish government had published its "Living with Covid" plan.

The plan sets out five different "levels" to public life within the State, to be determined by the national prevalence of coronavirus at any given time. These "levels" impose a spectrum of increasingly severe restrictions on public life as they increase from one to five. As the most serious level, it is level five alone which imposes the "restriction on travel outside a 5km radius of a person's place of residence", which is the sole criterion that defines a "relevant period" within the 2020 Act.

This change in definition from the much more specific and definite window of 1st August 2020 to 10th January 2021 shows an understanding that protective measures may be needed beyond the 10th January 2021. This idea is echoed by the "Living with Covid" plan, which self-describes as a framework to support the nation's move from a short to medium-term approach to managing the pandemic. With Ireland having just left a six-week period of nationwide level five restrictions, it is unclear whether Ireland will enter into any further Emergency Period in 2021. It is clear however that if we do, adequate legislative protection will be available to Relevant Persons.

Written by:

Siobhán Whelan
Attorney-at-law
BHSM LLP, Ireland
BHSM.IE

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FOR ENTERPRENEURS

COVID-19 EFFECTS
ON THE ITALIAN REAL ESTATE MARKET AND POSSIBLE OUTLOOK FOR 2021

The asset classes that are going to have a greater development in terms of investment opportunities in the short term, belong to the residential and logistics sectors

by Giulia Comparini

The Italian real estate market predicted that 2020 would be a historic year. That was, of course, before the COVID-19 pandemic descended.

The overall outlook was positive as strong foreign investments were expected for the year. However, there were some concerns about the limited availability of high value premises in the market and, with specific regard to retail real estate, the negative effects of e-commerce.

However, the abovementioned positive outlook was not to be, due to the extraordinary circumstances brought about by the COVID-19 pandemic. The virus hit Italy very hard and the Italian Government took very strong social distancing countermeasures to fight against the pandemic. Starting from 9 March 2020, a general lock-down nationwide was implemented, which had a tremendous effect on the economy. It is expected that there will be a GDP loss of 8.3% in 2020, compared to the previous year.

As expected, the Italian Real Estate market has suffered greatly from the impact of COVID-19.

In the first six months of 2020, the market showed a slowdown under the investment volume profile, mainly due to the hotel sector suffering an 80% decrease. The total investment volume suffered a loss of €3.5 billion, compared to the previous year (a 29% decrease on 2019). Furthermore, the number of transactions decreased from 79 from the first half of 2019 to 59 in the same period in 2020.

With regard to the retail market, the pandemic had a modest impact on supermarkets and big box retailers, while, in the short term, the high street sector has been the most affected, due to the lack of tourists and workers in city centres. Investors remain cautious in starting new retail transactions and, in some cases, projects scheduled for 2020 were put on a hold.

There was a significant reduction in office space requirements in major Italian cities: Milan registered a loss of 30% and Rome a loss of 71%, compared to the previous year. The main factor being the requirement of remote working for non-essential workers. With new social distancing guidelines, workspaces have been required to be re-designed, in order to meet new buyers' needs.

Nevertheless, it has to be noted that, thanks to the start of major urban regeneration projects registered in 2019, Milan will continue to be a safe haven for Real Estate operators.

In the first half of 2020, Milan was to be the most resilient Italian city in regard to the COVID-19 pandemic. The estimated amount of investment in the Milan real estate market was around €1.8 billion, with a solid and substantial alignment to that of 2019 (the analysis of the data shows a slight loss of around 5%).

The Milan Real Estate market represented 50% of total corporate investments in the Italian real estate market in Q1 2020 (in 2019, it accounted for 37% of the Italian real estate market). The Logistics sector, which in 2019 was one of the fastest growing sectors, suffered a decrease of 16%. However, thanks to the Mass Market Retail Business Model, this sector continues to be highly dynamic.

In general, international investors are still maintaining a central role in the Italian Real Estate market, although domestic investment has registered an increase during Q1 2020, representing 54% of the total volume invested.

In the first half of 2020, however, there was a somewhat resilient approach in the Italian Real Estate sector, with results exceeding expectations, thanks

to numerous ongoing projects from 2019 that were finalised in 2020. Of course, the second half of 2020 has not benefitted from such projects and, therefore, we are likely to see a more realistic downturn nationwide.

High valued assets shall keep their strength and role as safe haven assets, because of their ability to preserve their value. This is especially true in crisis periods like this, when investors are pushed to behave according to a "flight to quality" scheme.

In light of the above, the second half of 2020 is still characterized by great uncertainty, as the length of the economic crisis will determine the speed of recovery of the market.

However, it is a fact that the Italian real estate market is still quite interesting for investors although very peculiar and complex especially for certain sectors.

At present, the Italian real estate market is mostly concentrated on core investments given the current uncertainty about future scenarios. The asset classes that are going to have a greater development in terms of investment opportunities in the short term, belong to the residential and logistics sectors. Real estate sales are increasing due to very low rates and some institutional investors are currently investing in this sector.

Moreover, the lockdown has contributed to spark a new interest in residential homes. Logistics investments are quite attractive due to the relevant increase of the online market and the absence of unleased spaces.

Office, retail, and hotel are the sectors most affected by this pandemic and the results of a recovery in these sectors will be seen in the longer term. Especially the retail sector which was already suffering strong competition from e-commerce businesses before the spread of the pandemic.

Written by:

Giulia Comparini
Attorney-at-law
Cocuzza & Associati, Italy
COCUZZAEASSOCIATI.IT

A FOREIGNER'S INVESTMENT AND OWNERSHIP IN THE KOREAN REAL ESTATE MARKET

by K.S. Chong

Despite the current situation with COVID-19, foreign investors continue to show great interest in the Korean real estate market. From 2017 to May this year, it is reported that foreign investors bought more than 23-thousand apartment units in Korea, about US$6.4 billion[1] worth of properties.

Korean Legal Framework

In Korea, the only ownership of real estate that is legally recognised is complete ownership, which is often compared to the common law concept of a fee simple absolute. Foreigners should be aware that Korean law does not recognise so-called partial estates such as life estates, conditional estates, or future estates. However, real estate can be owned by more than one party.

Dual Registration System

In Korea, real property consists of land and buildings which constitute separate real property. Hence, a separate title registry exists for land and buildings, and ownership interests must be registered under the applicable registries accordingly.

Real Estate Investment Market in Korea

Real estate investment market continues to show strong growth in Korea. Due to its higher investment yields and its relatively lower volatility compared to other mature Asian markets, Korea continues to attract foreign investors to invest in its commercial real estate market. Real Estate Funds (REFs) and Real Estate Investment Trusts (REITs) are the most popular vehicles used by foreign investors.

Foreign Investment

With the exception of a limited list of real estates (such as land located in military facilities, protection areas, etc.), government approvals are not generally required for a foreigner to acquire real estate in Korea. A foreign person may acquire land by simply following certain procedures and reporting the acquisition to the appropriate authorities.

Reporting Real Estate Acquisition

Under the Act on Report on Real Estate Transactions, Etc., when a foreigner has acquired land located in Korea, they must report the acquisition to the appropriate local government bodies. If a foreigner has acquired real estate through a legally binding contract, they should report the contract to the relevant Si/Gun/Gu Office who has jurisdiction over the acquired real estate within 60 days from the day of the conclusion of the contract (i.e. when the contract is drawn up). However, when real estate sales contracts have been prepared and executed by a licensed real estate agent under Article 24 of the Licensed Real Estate Agents Act, it is the real estate agent who should meet the reporting requirement. For contract-based acquisition, it is required to submit (i) a copy of land acquisition contract; and (ii) a copy of ID of the real estate agent and the foreigner concerned.

If a foreigner has acquired real estate by means other than a contract (e.g. by inheritance, auction or exercise of right to repurchase), they should report the acquisition to the relevant local authorities within six months from the date of acquisition.

Processing of reports is completed on the same day, usually within three hours of submission.

It should be noted that there are

penalties for non-compliance with the reporting requirement as set out in the Act on Report on Real Estate Transactions, Etc. The penal provisions of the Act stipulate that persons who have signed a contract to acquire real estate but failed to report the acquisition, can be asked to pay a fine of up to KRW 3 million or KRW 5 million, a for persons who have acquired real estate by means other than a contract, a fine of up to KRW 1 million can be imposed.

Real Estate Acquisition Procedures

Different laws and procedures apply to acquisition of real estate by foreigners depending on (i) the purpose of acquisition; (ii) whether the foreigner is a resident in Korea; and (iii) whether the purchaser is an individual or a corporation.

If real estate has been acquired for profit-making purposes, the foreign investment notification procedure should be completed in addition to the real estate acquisition notification.

If a foreigner is a non-resident in Korea, they must first notify the planned acquisition of real estate to the head of a foreign exchange bank at the time of bringing the funds for the acquisition pursuant to the Foreign Exchange Transactions Act. Once the notification has been processed and the payment for the acquisition has been made, the

acquisition should be notified to the relevant Si/Gun/Gu office. When the sales contract has been concluded, the transfer of ownership must be registered within 60 days of the conclusion.

If a foreigner is a resident in Korea, the notification requirement as set out in the Foreign Exchange Transactions Act does not apply, and therefore, they simply need to register the transfer of ownership at the relevant Si/Gun/Gu office within 60 days of concluding the sales contract.

Outlook

Potential investors, however, must note that South Korea's ruling party is currently seeking legislation to levy a heavier tax on property speculation by foreigners, in order to stabilise the soaring prices of local real estate. It has been reported that the bill may impose a 20 percent tax on home purchases by foreign nationals if the buyers have not resided in the region for more than six months in the past 12 months without a valid reason.

Written by:

K.S. Chong
Attorney-at-law
LIWU Law Group, SOUTH KOREA
LIWULAW.COM

THE FUTURE OF THE OFFICE - STRIKING A NEW LEGAL BALANCE

John Dingle, Partner in Blandy & Blandy Solicitors Commercial Property team, discusses the future of the office and looks at how both landlords and tenants can protect their interests whilst taking advantage of the opportunities.

by John Dingle

According to former transport secretary, Lord Adonis, the "Death of the office is massively exaggerated" and "Most people can't wait to get back to the office."

Lord Adonis suggested that "there is no reason to believe that once the pandemic is over, life won't return back to normal" during a live news broadcast on the same day that construction began on Hs2.

Of course, landlords and tenants may choose to adopt a more cautious position than his clear optimism over the future of the office, at least in the short term.

79% of respondents to a recent Royal Institution of Chartered Surveyors' (RICS) UK Commercial Market Survey said that demand for office space had fallen during the second quarter of 2020. 93% also predicted that occupier space requirements will decrease over the next two years.

Research conducted in partnership with consultancy Leesman highlighted that almost 80% of employees said that working from home boosted their productivity.

The ongoing situation clearly offers differing opportunities for landlords and tenants. On one hand, a reduction in demand may allow occupiers to negotiate more favourable rents and terms. Whilst landlords and investors with distinctive and contemporary offices located in and around the Thames Valley may be well placed to benefit from tenants who are reassessing their needs and consolidating, 'downsizing' or relocating to the region, such as from London.

A report by Savills[1] in June this year found that 89% of workers still believe that the office plays a key role, but that office designs, and how they are used, needed to evolve.

According to a RICS article[2] published in 2019, "future proofed" workplaces will have planned for technological advances, been designed with employee wellbeing and productivity in mind, be "green", provide a clean and modern feel and adopt a forward thinking outlook.

So, given the above, what steps can landlords and tenants take so that they maximise opportunities?

Lease term

A shorter and more flexible lease term will be a clear occupier focus, so as to enable tenants to better respond to business need during an uncertain time. Landlords who are willing and able to offer a shorter term, as well as a tenant break, will be well placed to meet that need. Tenants are advised to ensure that any right to break should be as unconditional as possible – whereas a typical landlord requirement is that, in order to successfully trigger a break, a

[1] https://www.savills.co.uk/insight-and-opinion/savills-news/301232/89--believe-the-office-is-vital--but-needs-to-change

[2] https://www.rics.org/uk/news-insight/future-of-surveying/sustainability/futureproof-office-buildings/

tenant must comply with various conditions such as to pay all monies due, yield up with vacant possession, and comply with all other lease covenants, all of which presents a number of pitfalls for the unwary and in some cases may be extremely difficult to achieve at all.

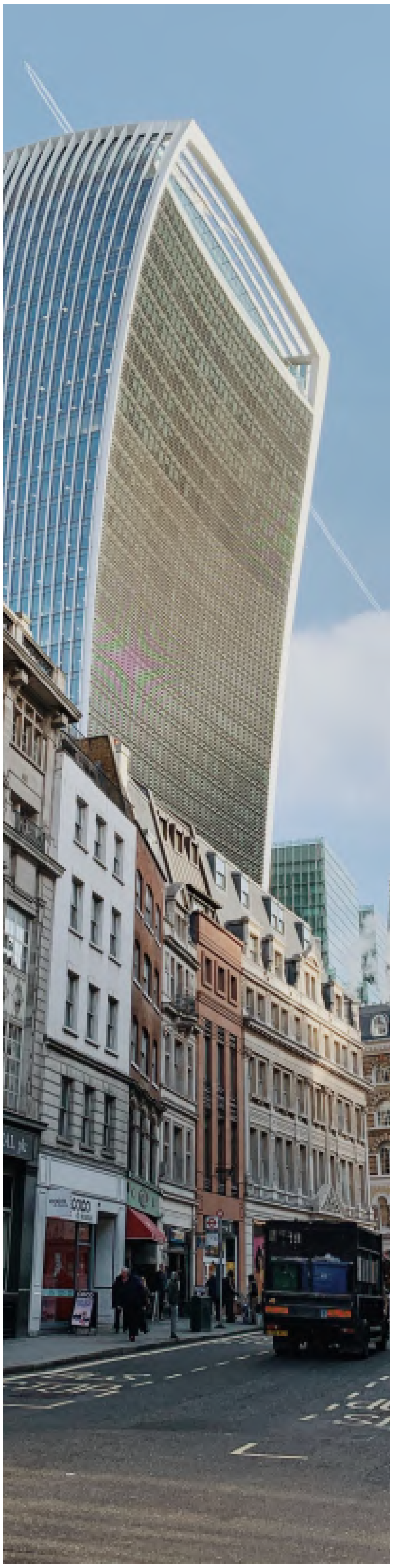
Rent and other costs

Clearly the amount of the rent will be key for tenants seeking cost certainty, and as always we would strongly advise that landlords and tenants seek advice from a surveyor to ensure that the rent – and any concessions, such as rent free periods – reflect the market. Turnover rents are making a name for themselves in certain sectors, such as retail and restaurant premises and, whilst not necessarily applicable to the office market, perhaps show that the landlord who is able to be innovative and flexible with its rental structures may prove more attractive to prospective tenants who are keeping an even closer eye on their financials.

Tenants also typically face a raft of other leasehold costs, such as service charge, insurance rent, business rates, and utilities, and a landlord who is able to offer an inclusive rent/cost package may find its stock rising in a world where overheads are more important than ever.

Other terms

Tenants will likely be keen to ensure too that their lease builds in the ability to assign, sublet or share occupation, so as to retain flexibility in the event of a change in tenant need. Can the lease be sold on to a third party, and does the tenant have the ability to sublet or share space and therefore share in the occupational costs? The ability to surrender back part of the premises during the lease term – whilst meaning some additional work and cost prior to lease completion to cater for a possible future surrender – may also be attractive



to a tenant; the tenant is able to reduce its footprint and costs whilst the landlord retains its tenant and income (albeit reduced).

Quality and safety

Flexible and cost certain lease terms will be more attractive than ever, and landlords able to offer those terms will find more opportunities than those who will not or cannot, particularly when allied to office space that meets the demands of the modern tenant for a quality, efficient, green, tech-enabled, and employee-focussed space. Despite the comments and statistics referred to above, the increase in home working is clearly here to stay, which will inevitably lead to reduced demand for office space. Offices must also however be able to meet the needs of a tenant and its workforce in the pandemic era. Hot desk arrangements – whilst placing downward pressure on floorspace need – is not necessarily an effective solution in a Covid-19 world. The fall-out from the pandemic may therefore act to counteract that downward pressure to an extent.

A landlord's response to, and the cost of, a pandemic related incident – such as a further lockdown or an infection in another part of a multi-let building – will be another key question. How will a landlord safeguard each tenant, and how will the cost of a lockdown or additional cleaning be apportioned? Landlords able to offer clear policies and outcomes will stay ahead of the curve.

Both landlords and tenants should take advice from a surveyor as well as legal advice before proceeding to ensure that their interests are protected.

Written by:

John Dingle
Attorney-at-law
Blandy & Blandy Solicitors, UNITED KINGDOM
BLANDY.CO.UK

GRABBING OPPORTUNITIES: INVESTMENT AND LEVERAGE IN THE HOSPITALITY SECTOR IN THE CURRENT MARKET

"Banks and sponsors had looked at the pandemic as a temporary issue, and now understand that it will not go"

by Nick Vasquez

Hospitality continues to suffer the devastating impact of the coronavirus pandemic, with the feared second wave rolling in during the Autumn and Winter months. Deals slowed to a trickle from March, following which there was an expectation among many that distress in the industry would result in feeding frenzy for the cash-rich opportunists.

The general consensus right now is that the deal market has not kicked off yet. There has been distress and some signs of activity, particularly where there were businesses already under pressure (such as in the casual dining market), but no widespread wave of transactions. The reasons are well rehearsed, as businesses scrambled to survive the crisis, helped along by supportive government schemes, moratoria and (so far) abundant patience in landlord / tenant, supplier / customer and lender / borrower relationships. All those dynamics are spurred by a feeling among all stakeholders that the crisis will abate at some point and there will be a recovery, so there has been a desire to work together to get through it. The main issue is timing of the recovery, and what to do until it comes – recent news of breakthroughs in vaccines are encouraging but there is still a long road ahead.

On the lender side, the crisis so far has been characterised by triaging emergency situations, with waivers and restructurings keeping bankers very busy. But, as the cash crisis persists, the expectation now is of a more intense phase of discussions with borrowers. Continued lender waivers will not be a solution to continue to keep things on an even keel, particularly as some governments scale back support measures for the economy. As a result, in the next couple of quarters the catalyst for activity will be banks taking, or threatening to take, real action.

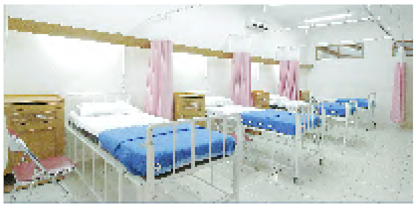
As one panellist at Brown Rudnick's recent hospitality-focused webinar put it, "banks and sponsors had looked at the pandemic as a temporary issue, and now understand it may not go". While banks have so far not been fast to react in accordance with their contractual rights (having learnt restraint following the Global Financial Crisis), difficult decisions will start being made. They will expect co-operation from sponsors and management and new cash to refresh

balance sheets, however they can find it. Co-operation is still often (albeit not always) the preferred route for lenders, where they are looking for survivability of a business over 12-18 months of severely impacted cashflows. That will leave owners with hard choices on finding more cash, be it from equity, new mezzanine debt or otherwise, or crystallising the losses that come with bank action or forced sale.

One alternative to fresh equity is the still active market for ground rents (or "sale of the fee-simple" in US terms), allowing owners to split a property interest into a freehold and long leasehold interest, and selling the freehold interest at a relatively low yield (looking at around 15% of enterprise value at a 2% yield) to free up cash in the equity value. While that invariably involves refinancing the debt stack to a lower loan-to-value amounts, banks tend to like the release of liquidity with the net effect of a more sustainable business, and the long term view taken by ground rent purchasers make pre-crisis cashflows very relevant. Brown Rudnick has acted on successful ground rent structures both before and after the Covid crisis began and is actively pursuing strategies on behalf of clients to use this solution.

In the consensual M&A activity that has been happening in the hotels sub-sector, discounts are inevitable given the current increase in risk premium, and 5-15% of pre-crisis are being agreed using a variety of supportive pricing structures. Sale and leaseback, or sale-and-manage back, deals active now guarantee EBITDA over a number of years while retaining an interest in long term cashflows via a management role. In another structure, deferred consideration is conditional on hitting EBITDA milestones.

What is yet to be seen is the deep discounting that will be found when



owners and lenders decide, or are forced, to say enough is enough, and the pace of insolvencies accelerate. One feels that despite the huge hit hospitality is taking, travel and leisure will return to trend eventually, in contrast to other sectors such as retail, office and logistics, where longer term structural changes are at play. In the meantime furlough schemes and enforcement moratoria are scaling down, lockdown measures returning and the pandemic is still raging. There is some hope now with vaccines, but unless vaccination programmes prove to be swift and effective, the waiting game for the opportunists may be coming to an end.

Brown Rudnick hosted a webinar on Grabbing Opportunities in October 2020, focusing on the current environment for investments in the hospitality industry, with panellists Ian Corfield at FRP, Pierpaolo Iasci from Societe Generale and BR's own hospitality practice leaders Tuvi Keinan and Nick Vasquez. We had some great insights and learning come out of the session, with panellists sharing their practical experience on the ground. Those shared insights have helped shape and inform this article.

Written by:

Nick Vasquez
Attorney-at-law
Brown Rudnick LLP, UNITED KINGDOM
BROWNRUDNICK.COM

OUR AUTHORS

MAZANTI– ANDERSEN

Louise Gjessing Lund Jensen
ATTORNEY-AT-LAW
+45 3314 3536
glj@mazanti.dk
Amaliegade 10
1256 Copenhagen K
DENMARK

MAZANTI– ANDERSEN

Jacob Monberg
ATTORNEY-AT-LAW
+45 3314 3536
jmo@mazanti.dk
Lenzhalde 83-85
Stuttgart, D-70192
DENMARK

MAZANTI– ANDERSEN

Lars Hammer Wentoft
ATTORNEY-AT-LAW
+45 3314 3536
lhw@mazanti.dk
Lenzhalde 83-85
Stuttgart, D-70192
DENMARK

YDÈS Société d'Avocats

Faye Tadros
ATTORNEY-AT-LAW
+33 (0)1 70 92 95 95
faye.tadros@ydes-avocats.com
12, cours Albert 1er
75008 Paris
FRANCE

HAVER & MAILÄNDER RECHTSANWÄLTE

Kai Graf v. der Recke
ATTORNEY-AT-LAW
+49 (0) 711 22744 41
kr@haver-mailaender.de
Lenzhalde 83-85
Stuttgart, D-70192
GERMANY

HAVER & MAILÄNDER RECHTSANWÄLTE

Tobias Eisemann
ATTORNEY-AT-LAW
+49 (0) 711 22744 41
te@haver-mailaender.de
Lenzhalde 83-85
Stuttgart, D-70192
GERMANY

Poovayya & Co. ADVOCATES SOLICITORS

G. Deepak Raj
ATTORNEY-AT-LAW
+91 80 4656 3000
deepakraj@poovayya.net
121 Dickenson Road,
Bangalore 560 042, Karnataka
INDIA

bhsm

Rob Gibbons
ATTORNEY-AT-LAW
+353 (0)1 440 8338
rgibbons@bhsm.ie
6-7 Harcourt Terrace,
Dublin 2
IRELAND

bhsm

Aidan McMahon
ATTORNEY-AT-LAW
+353 (0)1 440 8337
amcmahon@bhsm.ie
6-7 Harcourt Terrace,
Dublin 2
IRELAND

bhsm

Siobhán Whelan
ATTORNEY-AT-LAW
+353 (0)1 440 8337
swhelan@bhsm.ie
6-7 Harcourt Terrace,
Dublin 2
IRELAND

COCUZZA & ASSOCIATI Studio Legale

Giulia Comparini
ATTORNEY-AT-LAW
+39 02-866096
gcomparini@cocuzzaeassociati.it
Via San Giovanni Sul Muro 18
20121 Milano
ITALY

HOOGEWERF & CO.

Maurizio Zanella
ATTORNEY-AT-LAW
zanella.maurizio2@gmail.com
LUXEMBOURG

WIERINGA ADVOCATEN

Sebastian Levelt

ATTORNEY-AT-LAW

+31(0)20 5313024
levelt@wieringa.nl

IJdok 17
1013 MM Amsterdam

NETHERLAND

TURCZA®
Kancelaria Radców Prawnych

Marek Turcza

ATTORNEY-AT-LAW

+48 61 666 37 60
marek@turcza.com.pl

ul. Palacza 144
60-278 Poznań

POLAND

TURCZA®
Kancelaria Radców Prawnych

Łukasz Kwaśnik

ATTORNEY-AT-LAW

+48 61 666 37 60
kancelaria@turcza.com.pl

ul. Palacza 144
60-278 Poznań

POLAND

ABREU & MARQUES
ASSOCIADOS

Mariana Oliveira Monteiro

TRAINEE ATTORNEY-AT-LAW

00351 21 330 7100
mariana.monteiro@amsa.pt

Rua Filipe Folque, nr 2-4
1069-121 Lisboa

PORTUGAL

ABREU & MARQUES
ASSOCIADOS

Afonso Barroso

ATTORNEY-AT-LAW

00351 21 330 7100
afonso.barroso@amsa.pt

Rua Filipe Folque, nr 2-4
1069-121 Lisboa

PORTUGAL

LIWU Law Group

K.S. Chong

ATTORNEY-AT-LAW

+82-2-524-9600
kschong@liwulaw.com

(06595) (Seocho-dong, YangJin Bldg.)
3F, 5F, 138, Banpo-daero, Seocho-gu,
Seoul
SOUTH KOREA

THOMÁS DE CARRANZA
Abogados

Iñigo Sanchez del Campo

ATTORNEY-AT-LAW

(+34) 91 310 66 60
inigosc@tc-abogados.com

Paseo de la Castellana,
116, 9ª Planta, 28046 MADRID

SPAIN

THOMÁS DE CARRANZA
Abogados

Maria Garcia

ATTORNEY-AT-LAW

(+34) 91 310 66 60
maria.garcia@tc-abogados.com

Paseo de la Castellana,
116, 9ª Planta, 28046 MADRID

SPAIN

BLANDY & BLANDY
solicitors

Nick Burrows

ATTORNEY-AT-LAW

+44(0)118 951 6851
nick.burrows@blandy.co.uk

One Friar Street
Reading RG1 1DA

UK

BLANDY & BLANDY
solicitors

John Dingle

ATTORNEY-AT-LAW

+44(0)118 951 6933
john.dingle@blandy.co.uk

One Friar Street
Reading RG1 1DA

UK

BLANDY & BLANDY
solicitors

Katja Wigham

ATTORNEY-AT-LAW

+44(0)118 951 6933
katja.wigham@blandy.co.uk

One Friar Street
Reading RG1 1DA

UK

brownrudnick

Nick Vasquez

ATTORNEY-AT-LAW

+1.617.856.8496
nvasquez@brownrudnick.com

8 Clifford Street
London W1S 2LQ

UK

brownrudnick

Mathew R. Kinell
ATTORNEY-AT-LAW
+1.617.856.8496
mkinell@brownrudnick.com
One Financial Center Boston,
MA 02111
USA

brownrudnick

Samuel Zuckernik
ATTORNEY-AT-LAW
+1.617.856.8287
szuckernik@brownrudnick.com
One Financial Center Boston,
MA 02111
USA

IC Indochine Counsel
Business Law Practitioners

Le Nguyen Huy Thuy
ATTORNEY-AT-LAW
+84 28 3823 9640
thuy.le@indochinecounsel.com
Unit 305, 3rd Floor, Centec Tower
72 -74 Nguyen Thi Minh Khai, District 3
Ho Chi Minh City
VIETNAM

IC Indochine Counsel
Business Law Practitioners

Steven Jacob
ATTORNEY-AT-LAW
+84 28 3823 9640
sdjacob30@gmail.com
Unit 305, 3rd Floor, Centec Tower
72 -74 Nguyen Thi Minh Khai, District 3
Ho Chi Minh City
VIETNAM

brownrudnick

Thomas J. Phillips
ATTORNEY-AT-LAW
+1.617.856.8383
tphillips@brownrudnick.com
One Financial Center Boston,
MA 02111
USA

LFNGLOBAL.COM

TRENDS™
LEGAL MAGAZINE