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Buying and Selling Real Estate in Czech Republic

**ILN REAL ESTATE GROUP**



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## KEY FACTS OF REAL ESTATE ACQUISITIONS UNDER CZECH REPUBLIC LAW

### I. Types of Real Property Transactions

- a) Purchase of an undeveloped plot of land
- b) Purchase of a developed plot of land
- c) Purchase of a building (that is not part of plot of land)
- d) Purchase of a flat
- e) Purchase of a right to build
- f) Through a share deal with a corporation that purchases and sells the real estate

**Note:** The right to build is *right in rem* related to a plot of land consisting in a right to have an overground or underground structure whether yet existing or future. It is considered according to Czech law as an immovable asset. There is a special regulation regarding this new institute which has been incorporated into the Czech law since 1 January 2014. A detailed description of this institute exceeds the scope of this article; however, it could be useful in some cases. We will gladly provide more detailed information upon request.

### II. Major Content of the Purchase Agreement

- The contracting parties, as well as the price and the payment terms.
- An exact description of the real estate, i.e., the land, any fixtures and fittings of the building or flat and existing easements, pledges, etc. Czech law expressly regulates the description of the land and buildings used for the purpose of their registration in the

land register. Therefore, the most important document containing the description of the land is the land register.

**Note:** The review of the land register is of major importance regarding the ownership status of the seller, existing mortgages and possible ongoing proceedings. Registered there are also records called “notices” concerning the important information regarding the registered real estate or its owners or the persons holding other rights to the real estate, for instance, information regarding dispossession, execution proceedings, prohibition of disposition, and prohibition of establishing a pledge.

- Description of needed repairs or other regulations the seller/buyer has to comply with.
- Date of handover to the buyer/date of transfer of ownership (N.B. the ownership is transferred on the day of registration in the land register retroactively on the day of filing the request.
- The conditions of the change of ownership.
- Real estate charges.
- Declaration regarding the required municipal decisions such as, for instance, the occupancy permit determining the purpose of the use of the real estate.
- Detailed representations and warranties regarding the current ownership and substantial characteristics of the real estate such

as: access, connectivity to media supplies (gas, electricity etc.).

- Since 1 January 2016, the Energy Performance Certificate of the building shall be prepared by the purchaser, and it is recommended to include it in the purchase agreement as its annex.

**Note:** There are collateral provisions in the purchase agreement, which can be constituted as rights in rem and registered in the land register. These collateral provisions may facilitate the negotiations of both contractual parties by ensuring their specific requirements through these rights in rem. The collateral provisions in the purchase agreement are namely: (i) reservation of the ownership right, (ii) reservation of the repurchase, (iii) reservation of the resale, (iv) pre-emption right, (v) purchase testing, (vi) reservation of a better buyer. A detailed description of these institutes exceeds the scope of this article however it could be useful in some cases. We will gladly provide more detailed information upon request.

### III. Conclusion of the Purchase Agreement

- The purchase agreement has to be concluded in writing and the signatures of both parties must be on one document. For the purpose of the registration in the land register, it is required that the parties to the contract prove their identity by their officially certified signatures. The purchase agreement shall be thus concluded in writing with the officially certified signatures of both parties on one document.

### IV. Transfer of Ownership

- The parties provide for who will apply for the registration in the land register in the purchase agreement. In most cases, it is stated that the seller is obliged to apply for the registration in the land register within a certain period of time from the conclusion of the purchase agreement.
- To ensure that the purchase price is transferred to the seller after the registration of the ownership in favour of the buyer, the parties mostly use a deposit of the purchase price at a notary, attorney-at-law or bank. The parties to the contract thus conclude, mostly with a purchase agreement, also an escrow agreement with the bank, notary or attorney-at-law. According to the escrow agreement the bank/notary/attorney-at-law is obliged to transfer the purchase price after the fulfilment of the conditions stated in the escrow agreement, which usually includes the registration of the buyer in the land register as the owner of the transferred real estate and payment of the tax on acquisition of real estate.

### V. Agents

- The Buyer or Seller can both use a real estate agent. The contract with the agent can be concluded as an exclusive agreement.
- The Czech Chamber of Real Estate Agencies issued a book of recommended commissions for real estate agents, which is however not binding, and the real estate agent's commission is generally determined by the market situation. The commission



ranges from 3% to 7% of the purchase price.

## VI. Forms of Ownership

- In general, all individuals and legal entities can invest into and own real estate assets.
- It is irrelevant if the owners and purchasers are resident or non-resident or which country they come from. It is only crucial that the Czech land registry recognizes the legal personality of the foreign company or individual.

### A. Acquisitions

- Real estate can be acquired by way of an asset or a share deal. The legal entities in the case of a share deal are mostly organized as limited liability companies or joint stock companies.

### B. Residential Property

Most frequent forms of ownership of the residential property:

1. **Sole ownership:** The owner is the only person authorized to control and dispose of the land in question.
2. **Co-ownership:** More than one person owns an undivided share of land. Each co-owner is entitled to dispose of its share.
3. **Joint ownership of spouses:** Each of the spouses is entitled to a share of the joint property, but is not entitled to dispose of it independently, i.e. without the consent of the other joint owner (spouse).

Ownership by legal entities is however not excluded.

## C. Commercial Property

Owners of commercial property are most frequently legal entities of either private or public law. The most commonly used entities under Czech private law are joint-stock companies (a.s.) and limited liability companies (s.r.o.). As regards the entities of public law, they are usually insurance companies, banks, funds or purely real estate companies.

### 1. Limited Liability Company – s.r.o.

- Most widely used legal form for corporations.
- Highly flexible, with relatively few obligations.

#### a) Legal Entity

- A legal entity acts autonomously, represented by executive director(s).
- Independently subject to taxation.
- The particular rights and obligations of an s.r.o. exist autonomously from those of the shareholders and the executive directors.

#### b) Formation

- The foundation act is a Memorandum of Association or Foundation Deed in the case of a sole shareholder. It has to be notarized.
- Setting up an s.r.o. is uncomplicated and can be accomplished easily. Registration is done either directly by the notaries or via Court.



- A supervisory board is not an obligatory company body.

### c) Costs of Formation

The estimated total notarial costs for the formation of a standard s.r.o. are amounting approximately to CZK 6,800 CZK (€ 250) (In case of registered capital – CZK 200,000 (€ 7,300)) plus court costs, about approx. CZK 6,000 CZK (€ 220) and fees for a legal counsel for the drafting of the Foundation Deed or Memorandum of Association. The notarial costs are calculated according to the amount of the company's registered capital. It is also possible that the registration of the established company can be performed directly by a notary based on a certificated notarial deed. The total costs are in this case a little lower.

### d) Minimum Registered Capital

- The minimum registered capital required for an s.r.o. is CZK 1 but it is recommended to set up a company with higher capital covering the initial company's expenses in order to exclude situation of insolvency (at least CZK 100,000 (€ 3700)).
- Nevertheless, at least 30% of each shareholder's monetary contribution must be paid-up in a special bank account before the company's registration in the Commercial Register. In case of sole shareholders, the registered capital has to be paid-up entirely.

### e) Limited Liability

- The shareholders of the entity are not personally liable for the company's debts. The shareholders' liability is joint and several and is limited to the extent of their unpaid contribution in the registered capital according to the Commercial Register at the time they are invited by the creditor to meet performance.
- The limitation of liability arises once the s.r.o. has been registered in the Commercial Register.

**Note:** If the corporate share is not yet fully paid, the shareholders must, if need be, pay the outstanding difference privately in full.

- The company's statutory body is one or more executive directors. The executive directors act in all matters on behalf of the company in the way of acting that is registered in the Commercial Register. The Foundation Deed and the Memorandum of Association may state that the executive directors constitute a collective body. The internal restriction of the executive directors' powers is not effective against a third party.
- Under Czech law, a violation of these duties by an executive director will not affect the validity of a contract with a third party, but the s.r.o. may



hold the executive director in question liable for damages.

## 2. Czech Joint-Stock Company – a.s.

- An a.s. (akciová společnost) is a legal entity in which the shareholders are not liable for the debts of the company during its existence.
- It is much more complicated to form and operate than an s.r.o.
- Hence, the rules of the a.s. are generally less flexible compared to the rules of forming a limited liability company.

### a) Formation

- At least one founding shareholder is required, which can be an individual or a legal entity.
- The minimum share capital is CZK 2,000,000 (EUR 80,000).
- The Articles of Association must be notarized and contain certain mandatory information.
- Application for registration in the company's register takes place in the district where the company is located.

**Note:** Previously, the founding shareholders had to pay a minimum contribution. In the case of cash contributions: each of the founders had to pay of at least 30% of its subscribed registered capital by the time of the submission of the proposal to the Commercial Register.

- Tax registration is at the local tax authority.
- The company must establish a website containing the obligatory information

concerning the company without undue delay after its registration into the Commercial Register.

### b) Structure – 2 options

- There are two options regarding the company's structure: (i) the monistic structure, (ii) the dualistic structure. Both options are not implemented in Czech law in their pure forms. The company may freely change its structure by changing its Articles of Association.
- The monistic structure is a new option which exists in the Czech Republic only since 1 January 2014. This structure is typical in European countries such as Italy, France and Switzerland, and this structure is also used for a European Company (Societas Europaea).
- A company with a monistic structure has a Management Board and a Statutory Director.
- The Management Board has the controlling powers towards the Statutory Director and determines also the fundamental orientation of business management. The Statutory Director is the company's statutory body with management powers (these powers are shared with the Management Board) and it is elected by the Management Board.
- The dualistic structure, which was originally the only structure used for a joint-stock company in the Czech Republic before 1 January 2014, and currently used also in Germany, is the more common structure of a joint-stock company in the Czech Republic.



- A company with a dualistic structure has a Board of Directors and a Supervisory Board. The Board of Directors is the company's statutory body which is in charge of the company's business management. Nobody is authorized to instruct the Board of Directors in business management matters. The Supervisory Board is a controlling corporate body supervising the performance of the Board of Directors and the acting of the company. Nobody is authorized to instruct the Supervisory Board in Board of Directors controlling matters.
- The General Meeting is the third body of the a.s. in both company structures. It consists of all company shareholders. Its most important rights consist of (i) electing new members to the Board of Directors in the dualistic structure if the Memorandum of Association does not delegate this right to the Supervisory Board; (ii) electing new members in the Supervisory Board in the dualistic structure or Management Board in the monistic structure except for members of the Supervisory Board who are not elected by the General Meeting; (iii) deciding on the distribution of profits and amending the Articles of Association.

### c) Liability

- Only the company is liable towards the company's creditors and not the shareholders.

**Note:** Persons acting on its behalf are liable for the obligations which arise before the company's incorporation in the Commercial Register. If there are more

persons acting together, they are liable for such acting jointly and severally. The company can acknowledge the effect of such acts within three months from its incorporation and then it is bound by such acts from when it began.

### 3. Other types of entities

There are two other types of companies Limited partnership company (k.s.) and Unlimited partnership company (v.o.s.), that are however not often used in real estate transactions.

The same applies to private law associations that are not considered to be legal entities and where the liability of the members is unlimited.

## VII. Financing

- The usual way of financing real estate is a bank loan/mortgage for at least a part of the purchase price. Thereby, a bank generally insists on a collateral.
- The buyer normally has to provide a certain amount of the overall costs from its own sources. For large development projects banks usually require a pledge on all possible claims which the buyer can gain in connection with the real estate.
- In this connection, the buyer often has to present the seller with an irrevocable acceptance of loan financing by a reputable bank or show proof of sufficient funds before signing the purchase agreement.
- Normally, the mortgage/loan is provided for about 60%, up to 70%, of the purchase price.
- For special transactions such as large individual properties or real estate



portfolios, a common alternative to a bank loan is the use of capital market products, for instance, bonds, receivables or credit derivatives.

### VIII. Payments and Costs

- The costs and taxes are normally borne by the buyer. However, usually the seller has to bear the costs of deleting old mortgages in the land title register.
- Usually, the purchase price is transferred to an escrow account maintained by the notary, bank, or attorney-at-law, whereby the money solely gets transferred to the seller when the registration in the land registry is complete.
- The tax on acquiring real estate is 4% of the purchase price to be paid by the seller, whereby the buyer is the guarantor (and the parties may agree in writing that the tax will be paid by the buyer) but as of 1 October 2016, this tax will be paid by the buyer only.
- Agent fees.

### IX. Examinations before closing

- The buyer is advised to check the titles to the property for any potential or real deficiencies.
- Commercial buyers should additionally check if there are any planning restrictions: mostly, a construction or alteration as well as a change in use or the demolition of a building requires a building permit. The building project has to comply with the content of the local (or regional, as the case may be) development plans. Therefore, with regard to prospective plans of construction, the development and land

use should be reviewed very carefully before the closing of the contract.

- In addition to this, environmental issues should be checked before closing too.

**Note:** It is strongly recommended to undertake a due diligence review before the closing of the contract.