

TO: Clients and Friends of the Firm
FR: Frishberg & Partners
RE: Securing Land Rights for Commercial Use

As a starting reference point for any investor, Ukrainian land is either state-owned or it is already in private hands. This obvious distinction is absolutely vital, because no sane investor wants to deal with a government bureaucracy, especially a Ukrainian one.

Getting access to state-owned land for construction purposes, whether by leasing or auction purchase, requires significant time and financial investment. And yet, the government has the most land available in the best locations... So what's a poor investor (resident and non-resident alike) to do?

I. Every Investor's Dream

Every investor's dream ("Dream") is to acquire either ownership or a lease agreement to a legally defined parcel of land with a specific purpose allocation to construct a building to the investor's needs and specifications (e.g., a residential/office high-rise, a two-story restaurant, etc.).

Theoretically, such parcel of land exists somewhere on a secondary (private) market in Ukraine, but finding and acquiring such a parcel in Kiev at a reasonable price remains a Dream. Even if an investor finds an acceptable privately-owned land parcel in the center of Kiev, there will probably be a need to change the initially allocated "specific purpose" (see below) to fit its new owner's business profile.

The next best option, entering into a lease agreement with the Kiev City Council, is extraordinarily risky due to the Council's occasional unilateral cancellations of numerous lease agreements in 2006. This unprecedented event put a harsh spotlight on the fragile legal status of lease agreements in today's booming real estate environment. Hence, by default the next best choice is to purchase a desired land parcel from the government at land auctions.

II. Allocation for a Specific Purpose

In accordance with current legislation, land parcels can be (a) leased (short or long-term) or (b) purchased. Unfortunately, permanent free use of land is now granted only to non-profit organizations (invalids) and connected enterprises, as well as persons who already own finished buildings on the land. The latter are allowed to purchase the land they have always used at new, outrageous prices.

In either case, according to Articles 19-20 of the Land Code, the land has to be allocated for a certain, specific purpose (e.g., an office building or a restaurant). Subsequent deviation from the initial purposeful designation may result in termination of the land ownership or use/lease rights (see Articles 141-143 of the Land Code). Plus, to a far less significant degree, there is an administrative fine of between 3 and 25 of non-taxable monthly minimum wages.

If the party with land rights tries to transfer (sell) its rights to another entity, the original allocation purpose must be preserved. Should the subsequent land user alter the purpose of the land (e.g., change from an office building to a casino), it must legally revise the allocation accordingly. The terribly painful, drawn-out and expensive process is similar to the initial land allocation itself.

III. Sale of State-Owned Land

In accordance with the Law "On Land Valuation," dated Dec. 11, 2003, any state or communally-owned land alienation must undergo a "valuation" process. According to Article 127 of the Land Code, sale of state-owned land to legal entities and physical persons should take place on a competitive basis (auctions, competitions), except buy-outs of land with finished buildings thereon. Unfortunately, experienced land developers routinely complain that the best parcels never make it to auction.

IV. Foreigners and Other Non-residents

Foreign investors without political connections cannot buy land directly from the Ukrainian government, as the sale of federally-owned land to non-residents (i.e., foreign legal entities and governments alike) requires consent of the Cabinet of Ministers, together with approval of the Supreme Council of Ukraine (aka, the Parliament). On a local level, the sale of communally-owned land to foreigners requires consent of the local council of people's deputies, plus that of the Cabinet of Ministers. That is why foreign investors usually purchase land from private owners, and then easily change the "profile" (zoning) to suit their needs.

V. Conclusion

In cases where an investor expresses an interest in entering into a lease or a sale-purchase agreement (via an auction), the land bureaucrats have a "take-it-or-leave-it" attitude. No meaningful negotiations regarding specific provisions take place, even in cases of unreasonably short terms in lease agreements or near-extortionate prices in sale-purchase agreements.

Until recently, the government had all the best properties, so the negotiating power was truly on the side of its underpaid employees. These days, however, much of the land has been sold to private companies. Much of the land is currently for sale, with prices ranging from 100 USD up to 15,000 USD per "sotka" (0.01 hectare). The price difference throughout the nation is simply astounding and the land market continues to boom.