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Real Estate Newsletter

Recent Developments, Topics and Decisions

Spotlight: Admissibility of Shopping Centres under Construction Planning Law

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Based on a case by case assessment, an agglomeration of retail businesses over the time may be classified as a shopping centre as well entailing the strict requirements under public zoning law

INTRODUCTION: As part of real property law due diligence for a retail portfolio, a wide range of legal issues must be considered. One question of great legal and commercial significance is the admissibility under construction planning law of the retail premises to be acquired. Even if a formal building permit exists, it cannot necessarily be assumed that a project is indeed admissible under planning law. Thus, the only way for the buyer to achieve clarity is to perform a thorough legal check and assessment as part of the due diligence process.

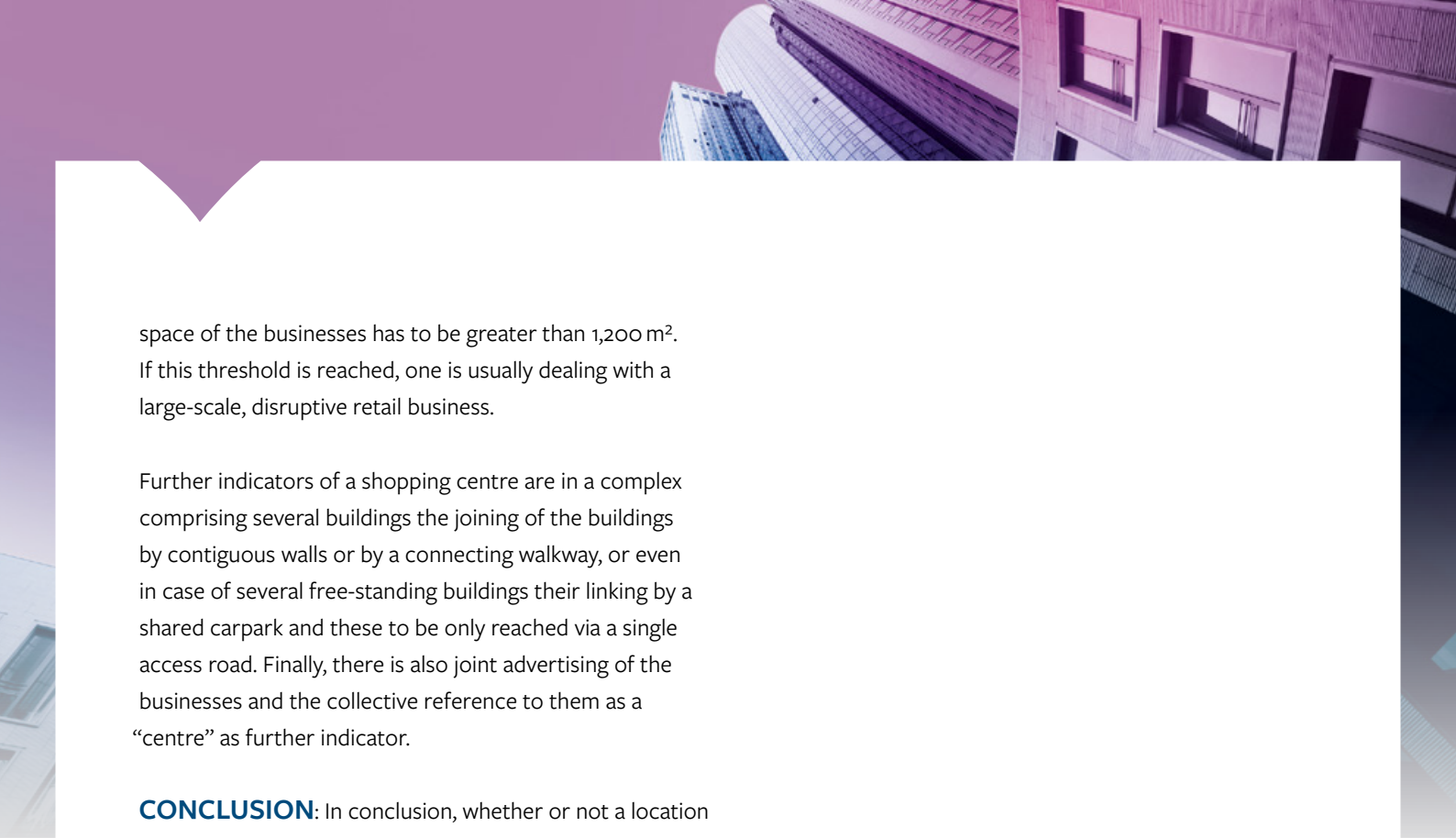
One of the most relevant statutory provision to which a lawyer will turn in checking planning admissibility for a retail portfolio is Section 11 para. 3 of the Land Use Ordinance [*Baunutzungsverordnung – BauNVO*]. The norm basically states that shopping centres and disruptive large-scale retail businesses are permissible only in those areas for which a legally valid zoning plan denotes the existence of a core or special zone where shopping centres or large-scale retail businesses can be built.

This article will focus specifically on the question of when a development is classified as a shopping centre which will require for the appropriate designation in the zoning plan or even its own separate zoning plan.

CASE LAW: Pursuant to case law, "shopping centres generally presuppose the existence of a building complex that is planned in advance to be financed, built and managed as a uniform entity that contains multiple retail operations of various types and sizes, mostly [author's note: although not necessarily] associated with widely diverse service enterprises." An obvious example for this type of shopping centre (i.e. planned and realised by a single developer) is the Outlet Center in Zweibrücken. This consists of a diverse range of retail businesses focussing on clothes and shoes and complemented by service-providers offering customers coffee, cake or lunch to enjoy as amenity for an extensive shopping spree.

Harder to assess are those areas which are gradually developed by retail businesses over a period of time. On this point, case law states as follows: "For several businesses to constitute a shopping centre in the legal sense without having been [author's note: jointly] planned as such, then, besides their close spatial proximity to one another, a certain amount of visibly apparent joint organisation and cooperation is required that would transform the conglomeration of several businesses into a planned and integrated entity in which each business relates to the others." Otherwise one simply has a random collection of businesses, each own admissible under zoning law, in a more or less self-contained area, which requires no special designation as part of a zoning plan.

The distinction between these two scenarios is dependent in case law on a consideration of the individual circumstances. Several indicators have materialised which if fulfilled will strongly hint the existence of a shopping centre. However, case law has not yet established a specific threshold value (e.g. for a business's sales space) above which one is definitely dealing with a shopping centre. With its approx. 21,000 m² sales space, the above-mentioned Outlet Center in Zweibrücken has been judged to be a shopping centre, but so too has a conglomeration of five businesses with a total sales space of 3,360 m². In any event, the total floor



space of the businesses has to be greater than 1,200 m². If this threshold is reached, one is usually dealing with a large-scale, disruptive retail business.

Further indicators of a shopping centre are in a complex comprising several buildings the joining of the buildings by contiguous walls or by a connecting walkway, or even in case of several free-standing buildings their linking by a shared carpark and these to be only reached via a single access road. Finally, there is also joint advertising of the businesses and the collective reference to them as a "centre" as further indicator.

CONCLUSION: In conclusion, whether or not a location with several retail businesses is judged to be a shopping centre depends on several factors. These factors are to be considered by the building authorities in coming to their decision on the building permit. Nonetheless, detailed reasons for the assessment result reached by the building authorities are hardly ever cited in the building permits. For the building authorities as well as for the buyer of the properties concerned, the specific case law for individual cases on whether or not one is dealing with a shopping centre constitutes a certain amount of legal uncertainty. Especially because, the assessment as a shopping centre incurs as an absolute prerequisite for the admissibility under zoning law the appropriate designation as such in the zoning plan. Unlike in case of large-sclae retail businesses, there exists no discretionary assessment by the building authorities as to whether the lack of being situated in the proper zone can be compensated given the business has no disruptive effect on the surrounding area.

BGH Rejects Remediation Clauses *(Schriftformheilungsklausel*)*

The possibility to limit the right to terminate a commercial lease due to violation of the statutory written form requirement is put to a definite end (BGH, judgment of 27 September 2017 – XII ZR 114/16)

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INTRODUCTION: With its decision, the BGH [the German Federal Supreme Court] ended a long discussion in case law and literature on the validity of "written-form" remediation clauses, declaring them invalid per se. Such clauses have regularly been used in lease agreements for commercial premises in an effort to exclude the risk of any defects in the written form requirement pursuant to Section 550 BGB [the German Civil Code]. If a lease agreement with a term of more than one year does not comply with the requirements as to written form, it can be terminated by either party at any time, subject to the statutory notice period. Remediation clauses were hence supposed to preserve the long-term nature of a tenancy in that the parties undertook to do everything possible, and to provide all declarations necessary, to remedy a breach of the written-form requirement before the lease agreement could be terminated.

THE DECISION: The BGH concluded that remediation clauses are invalid in any case, whether as General Terms and Conditions or as a clause agreed in an individual contract. It justifies its decision on the grounds that the legislator deliberately restricted the freedom of the parties to contract by stipulating that long-term lease commitments in relation to residential and commercial premises require written form. If there is no written form, there is no long-term tenancy either. Remediation clauses therefore represented an unlawful circumvention of the legislator's assessment, meaning that such clauses are invalid. However, according to the BGH, by way of an exception, a termination where there is a defect in the written form [of the lease] should be invalid if there is a breach of good faith inherent in this. The BGH identifies such a breach where the behaviour of the terminating party is an abuse of the latter's rights. This could occur, for instance, if one party uses a subsequent adjustment to the lease requested by it and which only benefits it, but which does not conform with the requirements as to written form, as an opportunity to terminate the tenancy in the proper manner. In the present case, the landlord's request addressed to the tenant for the indexation clause to be changed from 10 points to 5% only benefitted the landlord. This is because he would have been able to adjust the rent more quickly because this threshold would have already been reached sooner.

IMPACT ON DAY-TO-DAY BUSINESS: Following this decision by the BGH, compliance with the written form requirement now takes on even greater significance than before. The parties can now no longer rely on any potential defects in written form not justifying termination thanks to the remediation clause. No parties should rely on the objection that a termination based on defects in the written form is a breach of good faith. This argument of an abuse of a right should always be looked at on a case-by-case basis and can only apply subject to very strict requirements. There is therefore a risk that terminations on the basis of non-compliance with the written form will increase in future. Addenda should therefore be used to remedy defects in written form in ongoing tenancies. Purchasers of commercial real estate should insist on a remedy before completion of purchase contracts so that they do not have to live with the risk of a lease which can be terminated in the proper manner once the purchase price has been paid.

*clauses which prohibit a party to the lease from invoking early termination due to a violation of the written form requirement

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Double Written-form Requirement vs. Individual Agreement

A double written form requirement clause contained in a commercial lease agreements in the form of general terms and conditions does not hinder the amendment of such contract even by oral or implicit agreements (BGH, decision of 25 January 2017 – XII ZR 69/16)

INTRODUCTION: Double (so-called qualified) written-form requirement clauses – i.e. provisions that stipulate the written form is generally and expressly required for any changes made to the contract, including changes made to the written-form clause itself – are a normal part of commercial rental agreements. Such clauses are intended to render invalid any agreements made without the written-form requirement being met, including any agreements to deviate from the written-form requirement itself. If, however, a change to the tenancy contract is not effected due to the invalidity of the agreement, then even a breach of the statutory written-form requirement for long-term tenancy agreements, and with it the possibility of early termination, would be excluded. With regard to double written-form requirement clauses agreed as part of general terms and conditions the Federal Court of Justice (BGH) has rejected this approach.

THE DECISION: A commercial rental contract contains a double written-form requirement clause. Shortly after conclusion of contract, the landlord confirmed by unilateral letter that activities not actually allowed under the contractually envisaged purpose were in fact permitted. Subsequently a new tenant and a new landlord became party to the tenancy agreement, the former via written agreement, the latter via acquisition of the property. The new parties then agreed by way of an amendment a fixed tenancy duration of more than one year. The landlord then terminated the tenancy for cause (or by way of ordinary termination) before the expiry of the fixed duration.

The BGH has confirmed the lawfulness of ordinary termination of the tenancy agreement on the grounds of breach of the statutory written-form requirement, as any change to the contractual purpose would have required an amendment in the correct form. The individual agreement as documented by the written confirmation would take priority over the double written-form requirement clause. It would then be immaterial (as it would not be in the case of a double written-form requirement agreed by way of individual contract) whether the contradiction between the individual agreement and the content of the general terms and conditions was apparent to the parties or not. Nor is the form of the individual agreement of any material significance.

According to the BGH, there is no practical qualitative difference between a simple and a double written-form requirement clause. This would create priority for the spirit and purpose of an individual agreement, whereby special agreements between the parties could not be rendered void by deviating terms and conditions.

Even the fact that the user of the clause is the previous landlord is immaterial, for the principle of priority of individual agreements applies to all, and not just to the detriment of the user. Finally, the BGH further bases its decision on the protection that the written form requirement for long-term tenancy agreements is designed to provide, in accordance with which a buyer should not be bound long-term to incorrectly documented changes to essential parts of the contract (in this case, to the contractual purpose).

IMPACT ON DAY-TO-DAY BUSINESS: For the party that has an interest in the continuation of the long-term obligations of the contract, this means, in the event of any doubt as to whether an agreement is an essential part of contract, insisting on an amendment that satisfies the statutory written-form requirement. For the party wishing to release itself from the tenancy agreement, this case law removes another potential impediment to the early termination of contract.

Qualification as Temporary Part of Constructions on Third-party Land

The classification of ownership of constructions fitted for temporary purposes depends on the expressed intention of the parties upon fitting (BGH, judgement of 7 April 2017 – V ZR 52/16)

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INTRODUCTION: German real property law links the ownership to the plot of land first and foremost and classifies the fixtures erected on and firmly connected to the plot of land as merely being an integral part thereof. Under certain conditions, however, structures and other works are to be classified as temporary parts, with the result that they can be treated as movable assets and, regardless of the plot on which they stand, transferred (referred to as "special rights faculty"). The most common instances involve their construction based on in rem rights (such as an easement) on third-party land. Another example, the details of which are much contested, is the fitting of such constructions for solely temporary purposes. In answering the question as to whether or not a construction can be considered temporary, there has so far been some dispute as to whether this is only the case if, following the fulfilment of the purpose of the fitting, there is some remaining economic useful life. According to substantial arguments, for any duration above and beyond the useful life of the constructions, the fitting should instead be considered as connection for the entire lifespan and the construction should thus be classified as an integral part.

THE DECISION: The subject of the decision was the question of whether a wind turbine, which had been erected by a tenant pursuant to a tenancy agreement, has become an integral part or whether it could be sold and assigned separately as a temporary part. The Federal Court of Justice (BGH) decided against the criterion of useful life and based its decision solely on the visibly apparent intention to rescind the connection at some point in time either voluntarily or on the basis of contractual obligation. The main argument here is the difficulty to determine in advance the useful life and the differing classification depending on the duration of the lease or rental agreement.

IMPACT IN PRACTICE: This question is significant for, among other scenarios, wind turbines, solar panels and solar farms built solely on a contractual basis and without any in rem security. It is also significant for simple warehouses and, for example, all the structures in the port of Hamburg. It is precisely for buildings, such as those of lightweight construction, that have a short useful life (as estimated based on depreciation tables) that the new judgement ostensibly creates more security. For tax purposes, the Federal Finance Court [*Bundesfinanzhof – BFH*], in determining a fixture's quality as a temporary part, always bases its decisions on the useful life. As a result, one must be wary of the fact that the same case will almost certainly be decided differently under civil case law and tax case law. There is also the risk that, where the owner undertakes construction on its own plot, it will be difficult for a buyer to determine whether the construction forms an integral or temporary part. In the event of doubt, assignment as moveable asset ought to be envisaged as a precaution.

Choice of Law when Granting a Power of Authority

Law on the amendment of regulations governing international private and civil procedural law (Federal Gazette [*BGBl.*] 2017 I, p.1607)

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This law, which took effect from 17 June, contains for the first time statutory regulations for the law applying to authorised representation in international legal matters. Up until then, case law and the literature had developed certain principles, the essence of which is now adopted in statutory form. A new Art. 8 regulating various case groups has been inserted into the Civil Code Introductory Act [*Einführungsgesetz zum Bürgerlichen Gesetzbuch* (*EGBGB*)].

A basic principle of the new provision is the choice of law as per Art. 8 para. 1, under which the authorising party can, prior to exercising its authority, select the law that is to be applied to his representation (Art. 8 para. 1 sentence 1). The choice of law is to be respected when the representing agent and the third party concerned are aware of it. Following granting of authority, applicable law can be changed only subject to the agreement of all three parties involved.

If no law is selected, then in some types of case situations special rules apply:

- For authorised agents acting in a corporate capacity: substantive regulations of the state where the authorised agent is habitually resident in the exercise of their authority, unless the third party is not aware what this state is.
- For authorised agents who are employees of the authorising agent: substantive regulations of the state where the authorising agent is habitually resident when authority is granted, unless the third party is not aware what this state is.
- For continuing authority: substantive regulations of the state where the authorised agent habitually exercises their authority, unless the third party is not aware what this state is.

If it transpires in the above cases that the third party concerned cannot determine the relevant location, then under Art. 8 para. 5 sentence 1 EGBGB (revised), the substantive regulations of the state where the authorised agent exercises their authority in this instance (place of use) shall apply. If the third parties and authorised agents must have known that the authority in question was to be exercised solely in a specific state, then the substantive regulations of that state apply. If the third party is not aware of the place of use, the regulations that apply are the substantive regulations of the state where the authorising agent has their habitual residence at the time the authority is exercised.

A special regulation applies for the disposal of and rights to properties: for such properties, the law applicable where the property is situated applies (Art. 8 para. 6 EGBGB revised). This is of practical significance for transactions involving German properties, if one of the parties is resident abroad and, for the notarisation process, is represented before a German notary by an authorised agent. If this proxy says nothing with regard to applicable law, then by force of law, German law will apply for the proxy.

The form of the authorisation and the reach of the proxy statute are not provided for under Art. 8 EGBGB (revised). As before, the relevant law for the form is therefore the law applicable at the place the authorisation was granted. This so-called proxy statute encompasses the granting, existence, content, interpretation, duration and revocation of the proxy.

For authority granted before the law came into force, the hitherto applicable international private law remains in force. Material deviations ought not to arise because, as explained above, the new law has assumed the basic principles of case law and literature.

Overview Real Estate Transfer Tax Rates

Tax

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The following table provides an overview of the current status of the real estate transfer tax rates in the individual federal states (28. November 2017). Changes since the last issue in winter 2016 are marked in **bold**.

Baden-Württemberg	5.0 %
Bavaria	3.5 %
Berlin	6.0 %
Brandenburg	6.5 %
Bremen	5.0 %
Hamburg	4.5 %
Hessen	6.0 %
Mecklenburg-Western Pomerania	5.0 %
Lower Saxony	5.0 %
North Rhine Westphalia	6.5 %
Rhineland-Palatinate	5.0 %
Saarland	6.5 %
Saxony	3.5 %
Saxony-Anhalt	5.0 %
Schleswig-Holstein	6.5 %
Thuringia	**6.5 %**

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- Distressed real estate
- Transfer tax, property tax and assessment challenges
- Real estate litigation

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OUR CLIENTS include real estate institutional investors; pension funds and advisers; private equity funds; opportunity funds; real estate investment trusts; commercial, investment and industrial banks; governments; statutory bodies; insurance companies; real estate holding companies; developers; and multinational corporations.

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Selected Experience 2016/2017

The team has "excellent industry knowledge and skills".

Legal 500 Germany 2016

Advised the open real estate fund **BERENBERG Real Estate Hamburg**, which was set-up by Joh. Berenberg, Gossler & Co. KG (Real Estate Office) as real estate manager and Universal-Investment, on the acquisition of the office and retail complex "Neues Steintor" from a pension fund located in Northern Germany. The entire ensemble "Neues Steintor" characterizes Hamburg's skyline with its two office towers and has a lettable area of around 34,000 sqm with more than 600 parking spaces in an integrated parking garage.

Credit Suisse Asset Management Immobilien KAG on disposal of the shopping centers "Rathaus-Galerie", Leverkusen (approx. 37,000 sqm), "Mercado-Center", Nuremberg (approx. 43,500 sqm) and "Le Befane", Rimini as the so-called "Melody Portfolio" to Union Investment. The transaction is considered one of the largest shopping center transactions in Germany in 2017.

Universal-Investment with GPEP GmbH as portfolio manager on the acquisition of 12 retail stores with Netto Marken-Discount as anchor tenant as well as a retail centre. The properties with a gross lettable area of around 20,000 sqm were sold by a project developer.

INTERNOS Global Investors on the acquisition of a shopping and retail center for Novapierre in Riesa (Saxony, Germany). The newly renovated center which was built in 1993 with a lettable area of around 45,300 sqm is home to e.g. real, toom Baumarkt, MediMax, Aldi and Rossmann. Seller on the 270,000 sqm property was Invista European RE Riesapark.

Universal-Investment with GPEP GmbH as portfolio manager on the acquisition of 32 retail stores with a gross lettable area of around 40,000 sqm. Annual rental revenue is around four million Euro. Seller was an institutional fund.

BNP Paribas on the sale of real estate properties to La Francaise. The properties are located on a construction site in the town of Leutkirch im Allgäu. The project includes 250 luxury cottages covering 25,000 sqm as well as a property with a spa, restaurants, shops and play grounds with around 2,500 sqm.

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