



Newsletter 2/17

WENGERPLATTNER

Construction and real estate law – June 2017

Delusions and confusions surrounding Lex Koller

Authors: Dr. Thomas Wetzel and Sarah Hilber

It was only in June 2014 that the Swiss Federal Parliament rejected motion 13.3975 calling for the ‘reinstatement of Lex Koller authorisation for real estate used for commercial purposes’ and motion 13.3976 calling for the ‘abolition of the privilege allowing the acquisition of shares in real estate funds and listed real estate companies under Lex Koller’.

Yet the Federal Council has insisted that some of these proposals should be implemented under a revised Lex Koller regime and initiated a consultation process on 10 March 2017. The consultation period runs until 30 June 2017.

Backward steps dressed up as ‘modernisation’

- !** A larger supply will bring down prices.
- !** No need for new bans on foreigners acquiring Swiss real estate.

Delusions and confusions surrounding Lex Koller



Dr. Thomas Wetzel

Partner of the Real Estate Team
Certified Specialist SBA Construction and
Real Estate Law
thomas.wetzel@wenger-plattner.ch



Sarah Hilber

Member of the Real Estate Team
Certified Specialist SBA Construction and
Real Estate Law
sarah.hilber@wenger-plattner.ch

Lex Koller was updated over 10 years ago to reflect the needs of Swiss and foreign investors and respond to the demands of the international market. The updated Lex Koller is favourably for the Swiss economy and for tenants, who benefit from a larger supply of housing. However, the further amendments proposed are non-essential, largely superfluous and, in some cases, may even be destructive.

Introduction

In accordance with its Article 1, the Federal Act on Acquisition of Real Property by Persons Abroad (FARPA; SR 211.412.41 is also referred to as 'Lex Koller' after the Federal Councillor who was responsible for the previous amendments to the Act) sets out the aim of the Act which is to restrict the acquisition of Swiss real estate by non-residents. Lex Koller is designed to ensure that local land is primarily reserved for Swiss residents and that ownership of real estate by foreign non-residents remains at acceptable levels over the long term. To achieve this aim, the legislation subjects the acquisitions of real estate by persons abroad to a permit. A permit must be obtained where the following three cumulative conditions are met (Art. 2(1) FARPA):

- The purchaser is a person abroad (subjective permit requirement)
- The transaction involves real estate for which a permit is required (objective permit requirement depending on the purpose for which the real estate will be used)
- The real estate is acquired within the meaning of the FARPA (objective permit requirement depending on the type of right)

Given that a permit cannot generally be granted if there are no clear grounds, as laid down in the Act, the applicable law effectively precludes persons abroad from

acquiring real estate in Switzerland for which a permit is required.

Real estate subject to permit requirement regime

Real estate subject to permit mainly includes one- and multi-family homes, condominiums and building plots intended for residential development. Within the residential segment, persons abroad are therefore virtually excluded from the market at the present time. They are only permitted to purchase apartments as their principal residence or individual apartments which must be acquired along with commercial property (in German: «Betriebsstätte-Grundstücke»). Cross-border commuters from EC or EFTA Member States are also permitted to purchase secondary residences.

In addition, under Art. 2(2)(a) FARPA, persons abroad are allowed to purchase commercial property. These are properties that are used for business purposes (e.g. manufacturing buildings, warehouse, storage depot, office, shopping centre, shop, hotel, restaurant, workshop, medical practice etc.). Under applicable law, it is immaterial whether the real estate is used personally by the purchaser or rented or leased to a third party for the purposes of carrying on an economic activity. Persons abroad are therefore permitted to acquire commercial property purely as an investment.

Key proposals put forward by Federal Council

The Federal Council has essentially proposed two amendments which would have major implications for the Swiss economy:

The first proposal is that the permit requirement regime should be reinstated for purchases of commercial property by persons abroad. Only real estate acquired for commercial use by the purchaser personally or by his company would be exempt from this requirement. This provision would preclude persons abroad from acquiring commercial property purely as an investment and thus leads to a de facto ban on acquisition.

The second proposal is that persons abroad should essentially be banned from acquiring interests (generally shares) in residential real estate companies and, ultimately, from acquiring shares listed on the stock exchange. Adopting this proposal would make the trading in such shares considerably more complicated and could cause not insignificant damage to companies of this type in which many Swiss pension funds are invested. The resulting damage would not just affect the real estate sector, but the population as a whole, with insurance companies and small shareholders also losing out.

The acquisition of real estate

The acquisition of real estate, as defined in the FARPA, does not just apply to purchases of physical property, but also extends to the acquisition of shares in legal entities (e.g. companies limited by shares) whose object is, in fact, to purchase real estate. In these circumstances, the law only permits share purchases by persons abroad if the shares are listed on the stock exchange in Switzerland (Art. 4(1)(e) FARPA). In this case, the number of residential properties owned by the company is immaterial.

Shares in real estate funds may also be purchased provided these are regularly traded on the market. This also applies irrespective of the residential ratio attributable to the fund (Art. 4(1)(c) FARPA). The law therefore currently allows foreign investors to acquire shares in residential real estate companies, which are listed on the Swiss stock exchange, or shares in residential real estate funds, which are regularly traded on the market.

However, where the total shares held by persons abroad represent more than one third of the company's capital or voting rights, the company concerned is then deemed to be under foreign control (Art. 6(2)(a) and (b) FARPA). In the case of a real estate fund, there will be a presumption of foreign control if the person responsible for the administration of the fund, and the fund manager are persons abroad within the meaning of the FARPA (Art. 6(4) FARPA).

The presumption of foreign control has serious implications for the investment vehicles concerned (residential real estate companies or funds) in that they will then be deemed to be persons abroad themselves and precluded from purchasing further residential property in Switzerland. In their own interests, investment vehicles should therefore do their utmost to prevent such a situation from arising.

Perplexing desire for revision

The system broadly outlined above has proved effective and is now established practice. It also meets the objectives of the Act touched on earlier.

Momentum in the Swiss real estate market has also been ebbing for some time now. As several studies indicate, price increases on transactions have steadily ground to a halt as interest rates, at least at the long end, have climbed significantly from their lowest levels. There is an oversupply of space in many locations. Investors are generating about 10% less income than last year due to vacancy levels, discounts and loss of rent. And this is by no means confined to the commercial real estate market, which has been known for office space overcapacity and structural problems affecting retail spaces for some time now. Recent figures issued by the Federal Statistical Office show that the average rent for housing in 2015 was down 3% compared to the year before. Rents have never been lower than this since 2010.

Both rent levels and real estate prices are contingent on supply and demand. Accordingly, if indirect investments (in residential real estate companies or funds) by persons abroad, which are to some extent permitted under applicable law, or direct investments by persons abroad in commercial property were to increase the supply of residential or commercial premises, this would have the effect of reducing, rather than inflating, rents.

The measures proposed, which appear to be economically motivated (see box on the left), are not just unnecessary at this time but entirely misplaced. Because even the price increases seen in recent years have not been caused by real estate investments by persons abroad, but by other factors, such as historically low interest rates, population growth, high levels of inward migration and increased demand for individual living space. In addition, the tenancy law affords tenants optimum

As Federal Councillor Simonetta Sommaruga so aptly remarked at the close of the Council of States debate: ‘volatility is poison for real estate markets’. Hopefully, those responsible will recognise in time that this also holds true for their legislative venture.

protection against such price increases.

It is therefore hard to fathom why the Federal Council, at the suggestion of the Head of Department driving the initiative, has triggered a debate on barring foreign investors from this market.

Conclusion

In the same way as any other law, the FARPA contains inconsistencies and/or loopholes. However, the proposals put forward by the Federal Council to address these – a veritable mishmash of measures – overshoot the mark by a long way.

The agencies in charge of enforcing the law already have a range of mechanisms

to combat the abuses that are sporadically reported in the media (which of course are unacceptable), such as revoking authorisations, taking action to restore compliance with the law, imposing penalties etc. They simply need to apply these.