



Gide Loyrette Nouel

**Real Property Investment Law in Ukraine**



Gide Loyrette Nouel

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**TITLE****Full ownership***General*

Full ownership of real property is recognised by Ukrainian law. The right of ownership is protected by the Constitution of Ukraine.

The Ukrainian Civil Code's definition of "real property" includes land and objects located on land that are impossible to move without their depreciation and changing their designation, for example, buildings, flats, etc.

Ukrainian law makes a distinction between the title to land and the title to the buildings, constructions and other items located on the land. These rights are granted and exist separately. Therefore, an owner of a building does not always have the right of ownership to the land underneath. It is a very common situation in Ukraine when the ownership of the building differs from the ownership of the underlying land. The purchase of a building does not automatically result in the acquisition of the title to the land on which it stands. The Civil Code of Ukraine provides the legal framework for the acquisition, possession, disposal and use of developed real property. The Land Code of Ukraine provides a framework for the use and ownership of land.

**Permanent use of land**

The permanent use of land is another interest in land recognised by Ukrainian law. A permanent use is the title to land held by State enterprises, municipal enterprises and government authorities. In addition certain individuals and legal entities that held this type of title before the entry into force of the new Land Code of Ukraine are entitled to keep it. However, "permanent use" does not allow free disposal or alienation of land.

**Lease right to land**

A lease right to land allows the possession and use of the land. The Land Code of Ukraine provides for two kinds of lease; a short term lease for no more than 5 years and a long term lease for no more than 50 years.

*Acquisition*

An agreement relating to acquisition of real property must be concluded in writing and is subject to notarisation. All real property transactions, including lease agreements for the term exceeding three calendar years are subject to the State registration.

After acquisition of the real property, the title of the new owner is registered. In Ukraine the title to objects located on land (buildings, constructions, fixtures, etc.) are registered separately from registration of ownership or other titles to the land.

Ownership rights to buildings, constructions, fixtures are registered in the Registry of Titles to Real Property held by the local Bureau of Technical Inventory.<sup>1</sup> Titles and use rights to land are registered by local branches of the State Land Cadastre Centre.

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<sup>1</sup> Pursuant to the Temporary Regulation on the Procedure of the State Registration of Property Titles on Real Estate, approved by the Order of the Ministry of Justice of Ukraine as of February 7, 2002.

### Limitations on acquisition

Generally, real property may be acquired and sold by residents, non-residents, individuals and legal entities. However, some exceptions exist.

Foreign individuals, foreign legal entities and joint ventures established by Ukrainian and foreign persons are not allowed to own agricultural land. Agricultural land received as inheritance by foreigners must be alienated within one year. However, agricultural land may be leased by foreign entities or individuals.

Foreign legal entities may acquire an ownership right to non-agricultural land within settlement boundaries only in cases of acquisition of buildings or structures, or for the purpose of construction of facilities related to the execution of their business activities in Ukraine. Foreign legal entities may acquire an ownership right to non-agricultural land outside settlement boundaries in the case of acquisition of buildings or constructions. The above mentioned legal requirements with respect to foreigners are also applicable to joint ventures established by residents and non-residents.

When a foreign company acquires the shares of a Ukrainian company owning the land plot, the conditions concerning foreign ownership do not apply. Therefore, many foreign companies prefer to indirectly obtain a right to the land through the acquisition of shares in a Ukrainian company, which directly holds the land.

### Protection of ownership by courts

Ukrainian courts protect the ownership of real property.

## INTEREST IN REAL PROPERTY CAPABLE OF REGISTRATION

The following real property rights are required to be registered according to Ukrainian law: ownership; proprietary rights: which include right of possession (in Ukrainian “*право володіння*”); easement (in Ukrainian “*право користування (сервітут)*”); rights of permanent use of land plot (in Ukrainian “*право постійного користування земельною ділянкою*”); right of use of land for agricultural purpose (*emphyteusis*) (in Ukrainian “*право користування земельною ділянкою для сільськогосподарських потреб (емфітезис)*”); superficies (in Ukrainian “*право забудови земельної ділянки*”); leases of real property having a term of three year or more; and limitations of proprietary rights, arising out of mortgages, decisions of courts and other competent authorities, court injunctions.

*Easement* is in general granted for an indefinite period when resulting from a court decision and for a definite period when granted by the agreement. Easement, as a right which affects the property of land, is transferable with the land. The purchaser acting in good faith which acquires the land encumbered with an easement has the same obligations towards the beneficiary of the easement as the initial owner. Therefore, the acquisition of land or buildings requires a careful examination for the existence of easements.

*Emphyteusis* (a right of use of land for agricultural purpose) can be granted on the basis of the agreement. This right may be alienated and transferred as a heritage.

*Superficies* (a right of use of another’s land for construction) shall arise on the ground of an agreement or a will and may be established for definite or indefinite period. *Superficies* may be alienated by the land user or transferred as a heritage. The transfer of the property right in the land to another person shall not affect the scope of right of the owner of construction (structure) to use the land.

The general register of all kinds of real property rights and limitations does not still exist in Ukraine. The corresponding law was adopted in 2004. The general register is at the stage of formation. Currently, there are several registers where the ownership, proprietary rights and limitations are registered: the Register of Ownership to Real Property (excluding land), the State Land Cadastre, the Register of Prohibitions of Immovable Property Alienation, the State Register of Mortgages and the State Register of Encumbrances on Movable Property on Tax Liens (the tax liens over immovable property are registered therein as well).

Before notarisation of the sale and purchase agreement of real property, a notary shall check all the registers. If any restriction on alienation of a real property exist therein (namely, on the basis of mortgage, court decision etc.), the notary shall refuse the notarisation of an agreement.

### **THE DEVELOPMENT OF LAND**

The development of land in Ukraine requires obtaining of various permits and the solving of different administrative issues.

#### **Land for development**

Ukrainian law distinguishes between different types of land. Basically, only non-agricultural types of land may be used for construction purpose. If the designation of a land is not for construction, the modification of the purpose of land is required. An application of the owner of the land shall be submitted to the State or local authorities which are entitled to consider an application and may approve a modification.

Pursuant to Ukrainian law, foreign individuals, foreign legal entities and joint ventures established by Ukrainian and foreign persons cannot acquire directly agricultural land. However, a foreign investor may act through Ukrainian companies (acquired or established).

It should be noted that until 1<sup>st</sup> January 2008 a moratorium on the sale of certain types of agricultural land (in particular, farming land) is imposed. According to the moratorium it is also prohibited to modify (rezone) farming land plots owned by individuals or legal entities.

It is also possible to develop of a land based on a lease agreement.

#### **Obtaining of approval for placement of the building**

Having completed the procedure to obtain a right over the land (through acquisition or lease), a permit for placement of the building on the relevant land shall be obtained. An application for obtaining such permit shall be submitted to the local municipal authority. A permit for placement of the building on the land plot along with a letter permit for project works are issued within 2 to 4 months.

#### **Feasibility, design project documentation and its approval**

Before starting of the construction works, design project documentation for the future building shall be prepared. The project shall be prepared by specialised construction bureau and shall be concerted with the various authorities (i.e. with regard to compliance with sanitary, construction, work safety, ecological norms etc.).

**Obtaining of permit for construction works**

After approval of the design project documentation by all necessary authorities, a permit for construction works shall be obtained from architectural department of the local municipal authority. Construction works may be conducted by a developer by itself or a contractor for such purposes may be engaged. If a developer plans to conduct of the construction works by itself, an authorization is required.

**Commissioning the building**

As soon as the building is constructed, it must be “*put into operation*” by the acceptance commission, which shall include a contractor, an owner of project, and the representatives of the relevant authorities such as sanitary service, fire-fighters, local council, ecological service.

When approved, the signed acceptance act of the commission is subject to registration in the local Bureau of Technical Inventory. After the registration, a local municipal authority shall issue a certificate on ownership to the building.

**LEASES**

Buildings, constructions and land may be leased according to Ukrainian law. Leases are mainly governed by the Civil Code of Ukraine. The lease of land is governed by the Land Code of Ukraine and the Land Lease Act.

**COMMERCIAL LEASES****No specific statute**

There are no specific regulations governing commercial leases in Ukraine. Commercial leases are regulated by the general rules contained in the Civil Code of Ukraine.

**Form**

An agreement for the lease of a building or other construction (or a part thereof) must be concluded in written form. If concluded for a term greater than 3 years it is subject to notarisation and the State registration.

An agreement for the lease of land must be concluded in writing and is subject to the State registration. However, notarization of the agreement is not mandatory.

**Duration**

Leases may be concluded for a definite or indefinite period. No minimum or maximum duration is specified by the law, except for the lease of land. If the term is not specified, the lease agreement is deemed to be concluded for an indefinite term. The maximum term of a land lease is 50 years.

**Termination**

Lease agreements for an indefinite term may be terminated at any time by either party with a three month notice. Lease agreements for a definite term may be terminated only in case of mutual agreement of the parties, or by the court's decision upon request of one of the parties based upon certain cases stipulated by law.

*Grounds for termination available to the landlord*

The landlord shall have the right to terminate the lease agreement if:

- the tenant uses the real property in violation of the agreement or the real property's designation;
- the tenant transferred the use of the real property to another person without the landlord's prior consent;
- the tenant, due to its negligence, creates a threat of possible damage to the real property;
- the tenant has not commenced the major repairs of the real property and such obligation was imposed on the tenant.

Moreover, the landlord shall have the right to renounce a lease agreement and claim the return of real property, if the tenant does not make lease payments for the use of the real property during three consecutive months. In the event the landlord renounces a lease agreement, the lease agreement shall be deemed terminated from the moment the tenant is notified by the landlord of renouncement.

*Grounds available to the tenant*

Pursuant to the Civil Code of Ukraine the tenant shall have the right to demand termination of the lease agreement if:

- the landlord transferred the leased real property, the quality of which contravenes terms and conditions stipulated by the lease agreement or the designation of the real property;
- the landlord fails to comply with the obligation to make capital repairs of the real property.

According to Ukrainian law an agreement on lease of the land shall be terminated in certain cases provided by the law, namely:

- redemption of the land for public needs and forced alienation of land on the grounds of public necessity under the procedure set by Ukrainian law;
- owner and tenant of the land are the same person;
- liquidation of legal entity that is the tenant.

Moreover, an agreement for the lease of land may be terminated upon the court's decision, in case of non-fulfilment of the obligations by the parties or in case of accidental destruction or accidental damage of the leased land plot that substantially disturbs its use.

**Right of renewal**

Unless otherwise provided by the law or lease agreement, if the tenant duly performs its obligations, the tenant should be entitled to renew the lease.<sup>2</sup>

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<sup>2</sup> Article 777 (1) of "General provisions on hiring (lease)" of Chapter 58 "Hiring (Lease) of the Civil Code of Ukraine.

**Pre-emption right of lessee**

According to the Civil Code of Ukraine a tenant that diligently fulfils its obligations under the lease agreement shall have the priority right over other perspective buyers to purchase the real property.<sup>3</sup>

The Land Code of Ukraine also grants the tenant of land the right of first refusal to purchase the rented land if it is offered for sale.<sup>4</sup> One of the conditions is that the tenant must pay the price, for which the land is planned to be sold, or in case an auction sale – his bid must be equal to the final bid of the auction. The landlord must inform the tenant about his intention to sell the land to a third person and given an indication of the price of the sale and the other sale conditions.

**Rent and rent cap**

Rent, as an essential element, must be specified in the lease agreement. The rent is freely determined by the parties. There is no any statutory rent cap with respect to the lease of private property in Ukraine.

**Rent review**

Rent is adjusted in accordance with contractual provisions. Adjustment indices based on the official inflation rate are sometimes used. A lease agreement may grant the landlord a right to change the rent in the event of a substantial changes in the economic situation or taxation.

According to the general provisions of Ukrainian law, unless otherwise provided for by the agreement, the rent calculation for land is based on the inflation rate.

**Costs rechargeable to tenants**

All costs may be rechargeable to tenant if the parties agree on it in the lease agreement. Unless otherwise provided by the agreement, the current repair of a leased property shall be conducted by a tenant at its own costs.

**Improvements**

The tenant is entitled to remove improvements provided there is no damage to the real property. Pursuant to the Civil Code of Ukraine, if the improvements are made upon the consent of a landlord, the tenant is entitled to be reimbursed the costs of non-removable improvements or to set off such costs against lease payments. If the improvements, which cannot be detached from the real property, are made without the landlord's consent, a tenant is not entitled to be reimbursed for these improvements.

**Transfer**

Transfer of the lease agreement by the tenant without the prior consent of the landlord is not permitted.

**Sublease**

The tenant is entitled to sublease the leased real property subject to the consent of the landlord, provided that the term of such sublease does not exceed the term of the main lease agreement.

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<sup>3</sup> Article 777 (2) of "General provisions on hiring (lease)" of Chapter 58 "Hiring (Lease) of the Civil Code of Ukraine.

<sup>4</sup> Article 9 of the Lease Land Act.

If permitted by the lease agreement or upon the written consent of the landlord, a leased land or a part thereof may be transferred by the tenant into sub-lease without change of the land's designation. If the landlord does not send a written notification with consent or objection to sublease within one month, the leased land may be transferred into a sublease.

## **TAX**

### **Transaction costs**

#### *Sale of land and buildings*

#### VAT

The direct sale of real property by legal entity or physical person - entrepreneur is subject to VAT at a rate of 20% charged on the contract price. The difference between output VAT and input VAT is paid to the State budget. The sale of pure land is exempt of VAT. However, if the value of the land on which a building is constructed is included in the sale price of the building then the whole transaction will be subject to VAT at the rate of 20%.

VAT can only be paid by a tax payer registered as a VAT payer with the Ukrainian tax authorities. The registration is required, if the profits of the entity exceeded the threshold of UAH 300,000 (approximately EUR 45,000) within the last 12 months.

#### Other taxes on the direct sale of real property

The State duty fee for notarization of the acquisition agreement is 1% of the contract price. The law does not specify which party to the contract is liable for the payment of state duty. In practice the parties to the transaction generally agree to equally share the duty.

The State Pension Fund levies a tax at the rate of 1 % of the contract price. The buyer is liable for this tax. The buyer can make the payment to the State Pension Fund prior to the notarisation of the acquisition agreement or provide the notary with the money to make such payment. It should be noted that the State Pension Fund levy is not applicable to the sale of land.

### **Taxation of capital gains**

#### *Capital gains realised by a private individual*

Taxation of incomes of individuals is regulated by the Tax for the Incomes of Individuals Act. On 1<sup>st</sup> January 2007 new amendments relating to the taxation of individuals income from the sale of real property came into force. Tax rates vary from 0% to 5% for income derived from the sale of real property, depending on the number of sale transactions and the size of the sold real property.

It should be noted, that personal income tax must be paid by the seller prior to notarization of the acquisition agreement. The notary will notarize the agreement only if the document confirming the payment of personal income tax is provided.

#### *Capital gains realised by a corporate entity*

Ukrainian corporate income tax is governed by the Taxation of Profits of the Enterprises Act. The general rate of corporate income tax is 25%. Capital gains are calculated as the market sale price of an asset minus net book value.

Capital gains from the sale of Ukrainian real property received by the companies resident in Ukraine or non-resident companies operating in Ukraine through a permanent establishment are subject to 25% corporate income tax. Moreover, non-resident companies carrying out activities and receiving capital gains in Ukraine must pay 15% withholding tax on all incomes received.

Capital gains received from the sale of shares in a real property company are subject to same tax regime. There is no mechanism in Ukraine for taxation of capital gains arising on transactions between non-residents outside of Ukraine.

### **Leases**

#### *VAT*

Rental payments are generally subject to VAT at the rate of 20%.

Accredited representative offices of foreign entities registered in certain countries are exempt from VAT in respect of rent for offices and residential premises, if certain conditions are met.

#### *Corporate income tax*

Remuneration from leases in Ukraine shall be deemed as revenue for corporate income tax purposes. The corporate income tax rate is 25 %.

#### *Personal income tax*

The proceeds from leased property are considered as income for personal income tax purposes. The rate of taxation is 15 %.

### **Land tax**

Land tax is charged annually on land (not buildings) located in Ukraine. The tax rate depends on the category and location of the land. If the land has an estimated value then the land tax is calculated at the rate of 1% of its value.

The rate of the land tax ranges from UAH 0.015 per sq. metre to UAH 0.21 per sq. metre depending on the location of the land. In cities with population of more than 1 million inhabitants, the land tax is established at a rate of UAH 0.63 per sq. metre.

## **LEGAL COSTS REGARDING REAL PROPERTY ACQUISITIONS**

### **Notary fees**

Official costs (state duty fee which is used by public notaries) for notarisation of an acquisition agreement amounts to 1 % of the value of the real property sold as indicated in the sale agreement. State duty fee for notarization of a mortgage agreement is equal to 0.01% of the value of the mortgaged property indicated in the agreement. State duty fee for notarisation of a pledge agreement amounts to 1% of the value of the pledged property, but not more than UAH 850 (c. EUR 120).

If the agreement is notarised by a private notary, then notary's fees are agreed among the parties, but they *may not be less than the state duty fees*.

Moreover, for the State registration of the agreement in the Register of Transactions, the official fee in the amount of UAH 17 (c. EUR 2.5) shall be paid to the notary.

**Lawyers**

There are no statutory restrictions.

**Real Property Title Registries**

Currently, titles to real property (buildings, constructions, fixtures, etc.) in Ukraine are registered separately from registration of ownership or use rights to the land. There are two separate procedures and different costs for registration of titles.

Fees for registration of titles to real property (except for land) are paid to the municipal authorities of the administrative districts (regions) where the real property is located.<sup>5</sup> In the city of Kyiv, the fees for registration of the title to real property depend on the registration time. The fee varies from UAH 39.85 (c. EUR 6) for a 30 day registration to UAH 99.61 (c. EUR 15) for a 3 day registration. The official fee for the registration of a new owner is UAH 25 (c. EUR 4).

Under Ukrainian law, prior to the issuance and registration of a new owner by a “land ownership act” the development of technical documentation for land is required. For this purpose, the buyer shall conclude an agreement to prepare such documentation with the specifically authorised entity. The preparation of technical documentation includes the cadastral survey, the cadastral survey of adjacent property and land area calculation. In Kyiv, such entity is a separate department of the Kyiv Chief Administration on Land Resources. The cost for development technical documentation for land in Kyiv is UAH 5,700 (c. EUR 860).

**Publication**

There are no publication requirements.

**SECURITY USED IN REAL PROPERTY FINANCINGS**

A mortgage, a pledge over other assets, suretyship, parent guarantees and guarantees of Ukrainian banks are all common forms of security used in Ukrainian real property financings.

**Mortgage**

Under Ukrainian law various types of immovable property may be subject to mortgage. The mortgage is a specific type of pledge that may be created, *inter alia*, over land or buildings. A mortgage may be imposed on the basis of agreement, court decision or law. The mortgaged building shall remain in the use and possession of the mortgagor. Unfinished buildings may also be mortgaged. The mortgage of a building or construction must include the mortgage of underlying land plot, otherwise it shall be deemed invalid.

A mortgage may be established in a separate mortgage agreement, or be included in the agreement establishing a principal obligation (i.e. a loan agreement).

The mortgage agreement must be executed in writing and is subject to notarisation. It must also include the essential mandatory terms required by the law. The parties may include the price of the mortgaged property in the mortgage agreement, although it is not mandatory. The mortgage is subject to registration in the State Register of Mortgages. Failure to register does not invalidate the agreement.

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<sup>5</sup> Temporary Regulation on the Procedure of the State Registration of Property Titles on Real Property as approved by the Order of the Ministry of Justice of Ukraine as of 7<sup>th</sup> February 2002.

However, registration of a mortgage determines the ranking of its enforcement against other secured creditors. The fee for such registration is UAH 34 (c. EUR 5).

Unless otherwise stipulated by the agreement between the parties, the mortgagee does not have the right to directly acquire title to the mortgaged property upon default of the secured obligation. The mortgaged property is subject to sale at a public auction, once the execution procedure has been carried out. A mortgage may be enforced under the agreement, notary superscription or judicial decision.

### **Pledges**

In the event a debtor (pledgor) does not fulfil the obligation secured by the pledge, a creditor (pledgee) shall have the right to satisfaction at the expense of the pledged property prior to other creditors of this debtor, unless otherwise specified by the law.

Ukrainian law considers mortgage and pawn as specific types of pledge. Mortgage shall be pledge of the real property that remains in possession of a pledgor or a third person. While, pawn (in Ukrainian “zaklad”) shall be pledge of movable property being transferred into possession of a pledgee or by his order – into possession of a third person.

Under Ukrainian law pledges can be created under agreement, law or court decision. Except for some restrictions, any property (objects, securities, property rights), which can be freely alienated by the pledgor, may be seized.

A pledge agreement must be concluded in writing. Notarisation is required for mortgages of immovable property. The parties may also agree to notarise other pledge agreements. Upon the parties' decision, a pledge over movable property may be registered in the State Registry of Movable Property Charges. The registration of the pledge in relevant Register provides the pledgor with the priority right to enforce the pledge over other later secured creditors.

If a secured party wishes to enforce its security interest over pledged assets, then the secured party has to seek for a court order or judgment, unless there is a "notary endorsement." A "notary endorsement" is a separate notary procedure from the notarisation of a pledge agreement. A secured party can apply directly to an execution officer (similar to a marshal) to enforce a pledge.

Subsequent pledges are permitted unless expressly prohibited by a preceding pledge agreement or by law. As a principle, claims under subsequent pledges shall be satisfied from the value of the pledged property which remains after satisfaction of claims under preceding pledges. The pledgor must provide each subsequent pledgee with information about all existing pledges on the relevant property. If the pledgor fails to do so and such failure causes any losses to pledgees, the pledgor will be liable for all such losses.

Ukrainian law recognises the following types of pledges:

- pledge of goods in circulation;
- pledge of rights;
- pledge of shares;
- pledge of bank accounts, etc.

**Suretyship**

Under a surety agreement, a surety assumes liability before a creditor of another person (the primary debtor) for the performance by the primary debtor's obligation towards the creditor in full or in part. A surety may be provided by one person or several persons.

In the event that the primary debtor fails to perform or improperly performs the obligation secured by a surety agreement, the surety provider and the primary debtor shall be jointly and severally liable towards the creditor, unless the agreement provides for the secondary liability of the surety. Upon default, the creditor may require the discharge of the obligation directly from the surety rather than first applying for the discharge by the primary debtor. The surety may invoke the same objections as available to the debtor against the creditor. The surety is liable to the creditor to the same extent as the primary debtor, including payment of the principal debt as well as interests, penalties and losses.

Once the surety has performed the obligation to the creditor the surety provider is entitled to recover his debt from the primary debtor. The surety provider is also entitled to receive remuneration for the provision of surety. The parties are advised to include an agreement pertaining to the price of the suretyship since the legislation contains no such a provision.

A surety agreement must be executed in writing. Generally, a surety agreement defines the scope of liability of the surety provider. In the absence of such provision, the surety provider will be liable to a creditor to the same extent as the primary debtor, including payment of interest, reimbursement of court expenses for recovery of the debt and other losses of the creditor caused by improper performance or non-performance of the primary debtor's obligation.

**Guarantee**

By virtue of the guarantee, a bank, another financial institution, or an insurance company (a guarantor) gives a written commitment to pay a cash amount to the creditor in accordance with the conditions of the guarantee given by the guarantor upon the creditor's presentation of a written demand that such amount be paid.

The guarantee is similar in some respects to a suretyship. The difference is that the guarantee can be issued only by a bank, financial institution or insurance company. Similar to the suretyship the guarantor is liable to the creditor when the debtor fails to perform his obligation.

A guarantee shall be in force only for the period for which it was issued. A guarantor cannot withdraw the guarantee unless otherwise is stipulated in the agreement.

A guarantee does not depend on the secured (primary) obligation of the debtor. Therefore, the guarantor may not refuse payment under the guarantee based on any issues arising from the relations between the creditor and the debtor or based on the invalidity of the primary obligation secured by the bank guarantee. The guarantor is obligated to pay to the creditor upon submission by the creditor of a written demand and the documents required under the bank guarantee.

The guarantor is entitled to recover the amount of the guarantee paid to the creditor from the primary debtor, unless otherwise agreed by the parties.



### *About the Law Firm*

**Gide Loyrette Nouel** is an international law firm that has been advising real estate investors since 1920. Gide Loyrette Nouel has been present in Central and Eastern Europe since 1991.

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