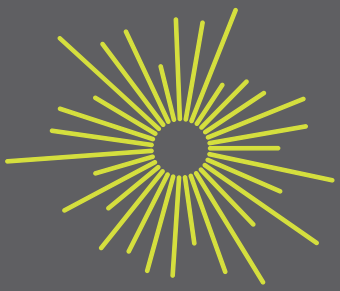

Real Estate Investments
in Denmark

Gorrissen Federspiel

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Contents

1 Introduction

Before engaging in real estate investments in Denmark a number of factors should be considered. Although the legal regime in Denmark resembles most other Western jurisdictions, substantial differences exist. For instance, some firm purchasing restrictions are in place, and a number of restrictions apply to residential leaseholds which are heavily regulated.

This publication presents a number of relevant aspects of Danish law[1] with focus on issues of general interest to foreign investors who consider making real estate investments in Denmark. The publication does not purport to be exhaustive.[2]

2 Structures for Investing in Real Estate in Denmark

The Danish purchasing restrictions render it practically impossible for most foreign investors to make direct purchases of Danish real property without permission from the Ministry of Justice. It might be possible to obtain the permission if the property is sought acquired to establish a business in Denmark, whereas grant of permission is less likely if the targeted property is purely an investment and even less so if the targeted property is a holiday home or the like. Mainly due to these restrictions investors generally choose to establish a Danish legal entity to hold the property in question. This may be done even if the Danish company/subsidiary is established only with the purpose of acquiring the Danish property in question.

The purchasing restrictions are described in the following section 2.1, whereas the different corporate entities to consider and their corresponding tax treatment are introduced in sections 2.2-2.6.

2.1 Purchasing restrictions

It is generally not possible for non-resident persons or foreign legal entities to purchase real estate in Denmark, unless they obtain permission from the Ministry of Justice or fall into one of the following categories: persons who have previously been Danish residents for at least 5 years; EU/EEA-citizens employed in Denmark or with a residence permit; EU/EEA-citizens who have established or are about to establish a business, an agency or a branch in Denmark; or legal entities lawfully established in, or with their registered offices in, another EU/EAA country, if the entity has established an agency or branch in Denmark or is going to provide services in Denmark.

For all the categories it is a further requirement that the property in question is going to be used as a permanent residence (for persons) or is neces-

[1] This publication includes prevailing law and practice up to May 2012.
[2] Please see the disclaimer below, section 12.

sary to conduct the business in Denmark (for businesses or persons establishing businesses etc. in Denmark).

The Danish Land Register checks compliance with the rules when registering a deed of conveyance to a foreign person or legal entity. This is done by requiring a copy of the permission from the Ministry of Justice. If no permission is needed, the purchaser will need to formally declare compliance with the purchasing requirements.

2.2 Overview of the relevant legal entities

In practice the options open to a foreign investor are to establish a Danish limited liability company (an "A/S" or an "ApS"), a limited partnership (a "K/S") or a partnership limited by shares (a "P/S"). When deciding which structure to choose at least the following different aspects should be considered:

(a) The entities' potential to reduce any capital gains tax and dividends withholding tax,

(b) Possible mitigation of transfer taxes and registration fees upon disposal,

(c) The possibility to deduct interest and

(d) The VAT costs

In the following it is outlined how said considerations affect the election of the Danish investment vehicle.

2.3 Danish limited liability companies (the "A/S and "ApS")

A limited liability company may be established as either a public limited liability company ("A/S") or as a private limited liability company ("ApS"). A Danish private or public limited liability company is most frequently used for investments in real estate situated in Denmark due to the advantages attached to this structure.

The Danish Companies Act[3] governs both public and private limited liability companies, regulating most aspects of the company's business, including formation, capitalization, organization and decision making, dividend payments, majority and minority rights etc. The Danish Companies Act generally provides for a more flexible regulation for private limited liability companies compared to public limited liability companies, including but not limited to the regulation of the management structure of the company.

[3] Act 470 of 12/06/2009

The minimum capital requirement is DKK 500,000 for a public limited liability company and DKK 80,000 for a private limited liability company, which may be denominated in Euro.

The shareholders of public or private limited liability companies are not obligated to make any capital contribution beyond their contribution commitment. In connection with the formation, payment of the share capital may be combined with payment of a premium (the amount exceeding the nominal share capital) which will then constitute free reserves available for dividends.

A two-tier management structure is required for a public limited liability company, typically by way of a management structure where the company is managed by a board of directors responsible for the overall and strategic management, and an executive board responsible for the day-to-day management of the company (an executive board member can be member of the board of directors), or as an alternative hereto, a management structure consisting of an executive board appointed by a supervisory board that oversees the executive board (an executive board member cannot be a member of the supervisory board).

With respect to the management structure of a private limited liability company, the company may either have a two-tier management system with a board of directors or supervisory board and an executive board, or a one-tier management system, where the company is managed solely by an executive board.

It should be noted that under Danish law, employees of public or private limited companies are entitled to elect representatives to the company's supreme governing body, corresponding to half of the number of other management members (in any event, at least two representatives), if the company has employed an average of at least 35 employees for the preceding three years. To the extent the employees are entitled to representation on the board of directors in a private limited liability company managed solely by an executive board, such company is required to introduce a two-tier management system.

A public or private limited liability company must be registered with the Danish Business Authority, which will normally be effected electronically. However, in cases where the founder is not Danish, the registration cannot be effected electronically and thus, it will take approximately 4-6 weeks before the registration of the company is in place. This delay can be avoided by purchasing a "shelf company", which has had no activity. Gorrissen Federspiel provides “shelf companies” for this purpose.

2.3.1 Corporate income tax

A public or private limited liability company will be subject to Danish income tax at a flat rate of 25% of the net taxable income. Taxable income includes rental income and financial income attributed to the real estate.

2.3.2 Property taxes

Owners of Danish real estate are generally obliged to pay property taxes, which are determined in each municipality and vary from 1.6 to 3.4%. The property tax rate in the municipality of Copenhagen is 3.4%.

For investment properties it is possible, and typical, to pass on the actual obligation to the tenant in the property lease agreement whereby a regulation of the rent payment will take place if the property tax rate is changed. Please see sections 7 and 8 for further details on rent regulation.

2.3.3 Depreciation of acquisition cost

Commercially used buildings are as a main rule depreciable. Each building which is subject to depreciation is depreciated individually on a straight-line basis. The depreciation rate may be determined by the tax payer between 0 and 4% each year. Special rates of depreciation apply for buildings subject to abnormal deterioration (if the building despite normal maintenance will have lost its value within 25 years from construction).

However, the following commercially used buildings are not subject to depreciation:

(a) office buildings;

(b) buildings used for a financial enterprise such as banking, insurance and stock brokering;

(c) post offices;

(d) residential homes, except hotels etc.;

(e) hotels that have been split into apartments; and

(f) hospitals and certain other buildings and installations for health care purposes.

Even though office buildings as a general rule are not subject to depreciation, it should be noted that office buildings that are connected to otherwise depreciable buildings and directly serve the business operation conducted in such building, may be subject to depreciation.

2.3.4 No tax on capital gains on shares

A sale of shares will not trigger a Danish tax payment for foreign investors. Thus, there will not be any Danish withholding tax levied on capital gains on the shares of the public or private limited liability company for foreign investors.

It is common in Denmark to include the value of tax assets and tax liabilities in the calculation of the book value of a public or private limited liability company. Thus, a deferred tax liability will result in a "rebate" on the sales price of the shares in the form of a reduction of the book value of the company. Similarly, tax assets (carry forward losses etc.) will result in an increase of the sales price.

2.3.5 Withholding tax on dividends

A participation exemption exists under Danish tax law. If a company shareholder tax resident outside Denmark holds 10% or more of the private or public limited liability company (subsidiary shares), dividends will be exempt from Danish withholding tax provided the taxation of the dividends is to be waived or reduced in accordance with the Parent-Subsidiary Directive (90/435/EEC) or in accordance with a tax treaty with the jurisdiction in which the company investor is resident. Further, dividends from group shares (the shareholder controls more than 50 percent of the voting rights of the company) are exempt from Danish withholding tax provided the company investor is a resident of the EU or the EEA and provided the taxation of dividends should have been waived or reduced in accordance with the Parent-Subsidiary Directive (90/435/EEC) or in accordance with a tax treaty with the country in which the company investor is resident had the shares been subsidiary shares.

Thus, if the foreign parent entity is entitled to benefit under the Parent-Subsidiary Directive or the tax treaty between Denmark and Germany, no withholding tax on dividends should apply.

2.3.6 Withholding tax on interest

A withholding tax of 25% on interest payments may be imposed if the debtor and the creditor are group-related.

2.3.7 Registration fees

Registration fees are payable on the registration of change of ownership (title deeds) and security rights over real property (mortgages). Hence, an asset deal will trigger a registration fee of DKK 1,400 plus 0.6% of the highest amount of the purchase price or the latest tax value (assessed by the tax authorities every second year).

The registration fee is reduced to a fixed amount of DKK 1,400 in case of change of ownership due to a restructuring process, i.e. a merger, demerger, transfer of assets or exchange of shares.

Registration of a mortgage triggers registration fees of DKK 1,400 plus 1.5% of the mortgage sum, though it is generally possible to make deductions corresponding to the value of the mortgages of the previous owner.

An advantage of a private or public limited liability company being the owner of a real property is that a share transfer does not trigger any registration fees or share transfer duties.

2.3.8 Interest deduction

As a main rule, interest related to commercial activity in a company is tax deductible. This implies that interest on loans as a starting point should be fully deductible for the company for corporate income tax purposes. However, there are certain limitations in the ability to deduct interest, inter alia by “thin capitalization” rules.

2.3.9 Fiscal unity regime

Danish consolidated companies as well as permanent establishments and real property in Denmark owned by foreign consolidated companies are subject to a Danish mandatory fiscal unity regime, i.e. all Danish entities are included in the tax consolidation.

The definition of consolidated companies contained in the Danish Financial Statements Act applies. According to this definition, a parent company and its subsidiaries constitute a group. A company, a foundation, a trust or an association qualifies as a parent company if it holds the majority of the voting rights in another company (the subsidiary), or if it controls the subsidiary in any other way as provided for in the Act. In the event that the consolidated financial statements of the parent company are prepared in compliance with international financial reporting standards, the definition of a group provided for in the international standards will apply; e.g. listed companies that must comply with IAS standards.

The tax group's income is made up as the sum of the taxable income for each company subject to fiscal unity. The entire income of a subsidiary will be included in the fiscal group.

The fiscal group's income is made up after setting off losses relating to previous accounting periods in each individual company. In the event that the group's income is positive, profits will be distributed proportionally between the profitable companies. In the event that the group's income is neg-

ative, losses will be distributed proportionally between the loss-making companies and will be carried forward in the company in question for set-off in subsequent accounting periods.

However, losses realised by a subsidiary upon disposal of non-depreciated buildings, i.e. office buildings, residential buildings, hospitals and hotels, can only be offset in taxable gains on other real estate realised by the same subsidiary.

The ultimate parent company in the fiscal group is appointed as the so-called administration company. In the event that there is no ultimate parent taxable in Denmark, but instead several parallel Danish affiliated companies, one of the affiliated companies will be appointed as the administration company. All companies in the fiscal group must have the same tax year as the administration company.

The administration company pays the income tax levied on the total income of the group entities. Profitable subsidiaries pay to the administrative company the tax levied on the profits regardless of whether the positive income is offset by taxable losses from other companies participating in the joint fiscal group.

2.3.10 VAT

Generally, no VAT is due on the sale of a property. However, transfer of a building site or a newly constructed building will be subject to VAT.

No VAT is due on the sale of shares in a company owning real property.

Rental income from a commercial real estate is VAT exempt. However, a lessor can opt for VAT registration if the property is rented out for purposes which allow the tenant to deduct input VAT.

The standard Danish VAT rate is 25%.

2.3.11 Conclusion

The public and private limited liability companies offer a number of advantages, including limitation of liability/risk of the parent entity with respect to the activities in Denmark; advantages of making share deals instead of asset deals comprising real estate; and the ability to deduct interest and maintain capital in the company for investment purposes at a lower taxation. In addition, a limited liability company offers an appropriate management structure with the parent entity being the only shareholder of the company. Furthermore, limited liability companies are the entities most frequently used within this area of business, and their legal framework un-

der the Danish Companies Act is well known and offers disclosure for contractors and creditors, which provides confidence among them. This is especially the case for the public limited company, which is the prevailing company form for larger business corporations.

On the other hand, the limited liability companies are subject to a detailed regulation in nearly all aspects of their business, minimizing the room for making flexible arrangements when it comes to freedom of contract, dividend payment, requirement for employee representatives on the board of directors and the like. Furthermore, regulation provides for majority and minority rights for the shareholders of the company (which are, however, of no relevance if the company is to be wholly owned by a single foreign entity). Finally, registration with the Danish Business Authority and the presentation of annual reports implies extensive disclosure concerning the business of the company.

2.4 The limited partnership (the "K/S ")

A limited partnership is defined as an undertaking in which one or more partners - the fully liable partners (in Danish "komplementarer") - are personally, jointly and severally liable without limitation for the debts and obligations of the undertaking, whereas one or more members - the limited partners (in Danish "kommanditisterne") - have limited liability for the debts and obligations of the undertaking, cf. section 2(2) of the Danish Act on Certain Commercial Enterprises[4]. It follows from this Act that a limited partnership must consist of at least one (1) fully liable partner and one (1) limited partner.

In order to limit the liability of the fully liable partner, it is often seen that the fully liable partner(s) is an A/S or ApS, in which case the limited partnership must be registered with the Danish Business Authority, in which connection some documentation and information must be made publicly available, and the K/S is required to present an annual report to be prepared in accordance with the Danish Financial Statements Act (in addition to the annual report to be prepared for the limited liability company being the fully liable partner). The limited partners are allowed to be shareholders of such A/S or ApS.

A K/S is subject to the Danish Act on Certain Commercial Enterprises, which only contains a minor legal framework of relevance to the K/S. Apart from this Act, no other comprehensive statutory regulation applies to a K/S. Thus a K/S is primarily regulated by the partnership agreement entered into between the fully liable and limited partners as well as in accordance with customary Danish legal practice. For this reason, no explicit requirements generally ap-

[4] Act 559 of 19/05/2010

ply to the K/S with respect to capitalization, payment of dividend, employee representation etc. However, to the extent that the fully liable partner is a public or private limited liability company, such company must comply with the Danish Companies Act as described under section 2.3.

The company is managed by the fully liable partner(s), but the partnership agreement may contain provisions granting rights to the limited partners or third parties in this respect. However, it is a legal requirement that the fully liable partner(s) of a limited partnership formed after 1 June 1996 must have some managerial and financial powers, i.e. the liable partner(s) may not be a person/entity without any activity.

To obtain more flexibility it may be considered to insert an interposed company between the Danish K/S and the parent entity as an exit may then be done as a share deal at HoldCo level (sale of the shares of the interposed company). If the interposed entity is a foreign company, attention should be given to the fact that the interposed company must be the beneficial owner of the shares in the K/S.

2.4.1 Corporate income tax

A limited partnership is transparent for Danish tax purposes, which implies that any income from the real estate or capital gains/losses will not be taxed in the partnership but directly at the level of the partners. If the limited partnership will be tax resident outside Denmark, the partners are not otherwise liable to pay tax in Denmark, but will be subject to limited tax liability in Denmark of any income which can be attributed to the real estate.

The tax liability comprises the net result of commercial activity attributed to the real estate, and only the net result after deduction of interest and other expenses will be subject to the Danish taxation. As a main rule, the Danish tax regime allows deduction of interest on financing of up to 80% of the purchase price. Interest on additional debt can only be deducted if it can be documented that the debt can be attributed to the acquisition of the real estate or the commercial activity related to the real estate in question.

2.4.2 Property taxes and municipality real estate taxes

The limited partnership will be subject to property taxes in accordance with the rules as described in section 2.3.2.

2.4.3 Depreciation of acquisition cost

The partners in the limited partnership can depreciate commercially used buildings in accordance with the same rules as described in section 2.3.3.

2.4.4 Capital gains tax

Profits and losses on the disposal of real estate are calculated and included in the taxable income according to the provisions of the Danish Act on Taxation of Profits on Real Property. According to the Act, the purchaser and the seller are required to distribute (in writing) the total sales price on buildings, depreciable installations and land value as well as on artistic decorations.

Improvement and maintenance costs may be added to the acquisition costs if the expenses have not been deducted in the taxable income.

The sales price will be the cash value of the consideration. This implies that the limited tax liability will include any capital gain on loans.

At the time of disposal of the real estate, the actual acquisition costs are reduced by all deductions/depreciations in relation to which no tax benefit has been recaptured according to the Depreciation and Amortisation Act.

However, taxation of a non-leasehold property can under certain conditions be postponed by offsetting it in connection with the reacquisition of a new property. This does not apply in relation to recaptured depreciations.

2.4.5 Interest deduction

As a main rule, interest related to commercial activity in a company is tax deductible. However, in certain cases the limited partnership may be subject to limitations in interest deductions just as limited liability companies, cf. section 2.3.8.

2.4.6 VAT and registration fees

Generally, no VAT is due on the sale of a property. However, transfer of a building site or a newly constructed building will be subject to VAT.

Rental income from a commercial real estate is VAT exempt. However, the lessor can opt for VAT registration if the property is rented out for purposes which allow the tenant to deduct input VAT.

There are no other transfer taxes or indirect taxes (except for the registration fees described in section 2.3.7).

2.4.7 Conclusion

The limited partnership provides some advantages, including freedom of contract as a consequence of the limited legal regulation, and the possibility of limiting the liability of the fully liable partner(s). Furthermore, the lack of tax subjectivity may, according to the circumstances, be seen as an advantage.

On the other hand, a K/S may constitute some difficulties in the set-up, for instance with respect to the requirement of a minimum of two groups of partners.

2.5 Partnership limited by shares (the "P/S")

A P/S is defined as a limited partnership (cf. section 2 (2) of the Danish Act on Certain Commercial Enterprises) in which the limited partners have contributed a certain amount of capital, which is divided into shares", cf. section 5, number 21, of the Danish Companies Act, i.e. a P/S is an undertaking consisting of two groups of partners: A fully liable partner and a limited partner.

The rules of the Danish Companies Act governing public limited liability companies apply to the P/S company subject to necessary modifications, e.g. a P/S requires a minimum capital of DKK 500,000.

A partnership limited by shares is transparent for Danish tax purposes. Thus, the taxation of the P/S and its investors is comparable to that of a limited partnership and its partners, cf. section 2.4.

The articles of association, subscription lists and the particulars of the formation of the company delivered to the Danish Business Authority must, in addition to the details prescribed for public limited liability companies (A/S), include some additional information, including but not limited to information on the identity of the fully liable partner, and the articles of association of a P/S must include specific rules as to the legal relationship between the shareholders and the fully liable partner(s).

Below, some of the differences between a K/S and a P/S are listed

(a) The P/S is primarily regulated by the Danish Companies Act,

(b) The P/S requires a minimum share capital of DKK 500,000,

(c) The P/S must have a fixed share capital divided into shares,

(d) The P/S must have a structure as a public limited liability company and the limited partners therefore have - with respect to the managerial and financial powers of the fully liable partner - influence on the operation of the P/S,

(e) Compared to a K/S, the P/S provides for a wider access to be converted into an A/S.

Based on the above, the advantages and disadvantages of using a P/S are quite similar to the ones mentioned with respect to the K/S, cf. section 2.4.7. The major difference between the K/S and P/S is that the P/S is subject to the Danish Companies Act, which can be seen as either an advantage or a disadvantage. On the one hand this may provide confidence among contractors and creditors, but on the other hand the P/S is subject to extensive regulation by the Danish Companies Act, the scope of which in some cases is unclear as the Danish Companies Act only applies "subject to any necessary modifications".

2.6 Overall conclusion

Based on the reasoning set forth above it is often advisable to establish a public limited liability company (an A/S) for real estate investments in Denmark. This is primarily due to its inherent limitation of liability and risk, and the confidence an A/S instills in contractors and creditors given its well-known legal framework and the disclosure obligations. Furthermore, if the investors qualify for the participation exemption, dividends may be received tax free, and there is no capital gains tax on shares for foreign investors.

The legal position of a private limited liability company (an ApS) is roughly the same, but investors often prefer the A/S for non-legal reasons. The A/S form is more frequently used for real estate investments and is the prevailing company form for larger business corporations in Denmark, thus making the A/S more recognized than the ApS. Due to the smaller capital requirements, the ApS has historically been widely used for unsuccessful business ventures and, accordingly, the ApS does not have the same esteem as the A/S. However, if an investor emphasizes the importance of achieving the greatest possible flexibility it may be suitable to choose an ApS for making investments in Denmark. At the end of the day the confidence of creditors and contracting parties ought to relate to the shareholders and managers of the company and its capitalization, not the company form.

The K/S and P/S have more complex ownership structures than those of the A/S and ApS. However, if tax transparency and freedom of contract are preferred criteria, the K/S model may be the right solution. The P/S is also tax transparent, but is governed by the rules of public limited liability companies under the Danish Companies Act and accordingly provides less freedom of contract. Against the K/S structure is the (non legal) fact that such entities have historically been used by less serious asset management companies to offer the public limited partnership shares in K/S entities entirely controlled by the management company and often subsequently bankrupted. Accordingly, the general esteem of a K/S is comparable to that of an ApS.

3 Securing ownership and other rights

It is no validity requirement to register rights over real property with the Land Register, and thus an agreement is enforceable inter partes without registration. In practice most rights are registered, however, since this is the only way to gain third party protection. An important exception to this rule is that most basic rights of lessees are protected against third parties by statute. Another main exception is that the tax authorities, insurance companies, and utility suppliers may have third party protected rights over the real property for which a tax, insurance premium or utility bill is outstanding without registration. Furthermore, the local planning regulation is applicable and enforceable against property owners regardless of registration with the Land Register.

Formally, the Land Register system only allows entry of the following three types of rights and obligations: ownership; mortgages; and easements. There are, however, no strict limits as to what may be agreed in a document registered as an easement, and registered ownership documents may contain all sorts of different rights apart from the transfer of title. If the right can be formulated it is, in general, recognisable and may be registered with the Land Register. So, in practice, the system is very flexible and allows for a variety of rights to be established and protected against third parties.

Though generally very flexible, there are some formal limitations to be observed. For instance, real property transactions need to adhere to the so-called unity principle, under which it is illegal to dispose over part of a real property without formal division of said property prior to disposal. Only a whole unit can be transferred, and if one would like to sell part of a property, the property must be formally divided with the National Survey and Cadastre (if possible). To avoid circumvention of this rule, it has also been outlawed to establish rights of use for a part of a real property for a period of more than 30 years. This prohibition does not apply for the lease of buildings, however.

Another notable limitation is related to the local authorities' planning regulation. To avoid interference with public plans for land development, easements governing matters which may also be governed by local plans require approval from the local municipality prior to registration with the Land Register.

3.1 A digital system

In September 2009 Denmark implemented a single digital Land Register in which any and all registrations need to be made online using a digital signature. All citizens and legal entities will be granted such digital signature upon request. The registration process requires the previous owner/beneficent to transfer his ownership/right by using his digital signature. Upon registration with the Land Register no formal title or mortgage document is issued,

but the owner receives an email with a transcript from the register when the registration process is complete.

It follows from the Land Registration Act that the Danish State is liable for faulty registrations and other mistakes made by the Land Register.

For a minor fee it is open for anyone to review rights in the internet-based system and to make transcripts from the database. There are no restrictions on public access to the Land Register. All registered information may be retrieved, including purchase sums. Copies of mortgages and easements are also available.

Registered rights take priority after registration date, and prevail over all unregistered rights unless the beneficiary of the registered right was acting in bad faith. Competing unregistered rights take priority after the date when they were granted.

3.2 Owner-occupied flats

Apartment houses may be registered as one or several individual properties in the Land Register. In the latter case the individual units are owned individually on a freehold basis as so-called owner-occupied flats (in Danish: *ejerlejligheder*).

Together with the other owners, the owner of an owner-occupied flat has joint rights of ownership to the soil of the parent property as well as joint fixtures and fixings. Ownership of the joint rights is usually determined on the basis of a distributional number for each owner-occupied flat. If no distributional number is determined, the owner-occupied flats rank equally. The owners have rights and obligations in the community based on the distributional numbers, including that the owners usually pay the common expenses (operational costs) on the basis of these distributional numbers.

The owner of an owner-occupied flat participates in an association together with the other owners. This association is called an owners' association (in Danish: *ejerforening*). Basically, this is an administrative body in which membership is mandatory for the owners. The owners' association is immediately established once a purchase agreement is entered into concerning the first owner-occupied flat in buildings that are divided into owner-occupied flats. If no articles of association have been prepared a set of standard articles apply.

Each owner-occupied flat constitutes an independent piece of real property and each owner-occupied flat has its own entry in the Land Register.

Unless the articles of association prescribe otherwise, the owner of an owner-occupied flat may let it and if such letting is for residential purposes, the Danish Rent Act applies, cf. section 8 below.

Unless the articles of association prescribe otherwise, the owner of an owner-occupied flat holds voting rights at the owners' association's general meeting in accordance with his distributional number. Note, however, that an owner of several flats in an owners' association, who has let one or more of his owner-occupied flats, cannot participate in votes according to distributional numbers for the owner-occupied flats that he has re-let. This provision is to prevent that one owner maintains ownership of a number of flats in order to maintain the majority of votes in the owners' association. The provision does not apply in connection with the first time the flat is being let as for example flats in a newly built house.

3.3 Cooperative Housing Associations

Another subdivision of property is that of cooperative housing associations under the Act on Cooperative Housing Associations (in Danish: *Andelsboligforeningsloven*). Due to the nature of these associations they are not subject to ordinary real estate investments and will, consequently, not be described further in this publication. However, in section 8.2, below, it is briefly described how Cooperative Housing Associations may arise out of tenanted properties when mandatory pre-emption rights are triggered.

3.4 Registration fees

The registration fee for registering a title deed (purchase agreement) amounts to DKK 1,400 plus 0.6% of the purchase price or the latest public valuation (whichever is higher). In some parts of Denmark it has been a tradition that the purchaser pays the fee in connection with the registration of the purchaser's rights to the real estate. In other parts of Denmark the parties have shared the expense. However, lately it has become a (new) condition to most acquisitions that the purchaser pays the registration fee, also in the parts of Denmark where the parties formerly shared expenses. The parties are free to agree upon the obligation of paying the registration fee.

The registration fee is the same for registration of conditional and absolute title deeds.

The fee for registration of mortgages amounts to DKK 1,400 plus 1.5% of the principal amount. However, if there is an existing mortgage registered on the property (regarding the seller's loans) the variable part of the fee may be lower or even inapplicable.

The fee for other types of registrations is DKK 1,400.

4 Usual deal participants and deal flow

The following briefly describes a typical deal flow and its participants.

4.1 Other parties involved in a transaction

In most transactions only the real estate agent, the parties and the parties' finance providers and lawyers would be involved. In larger transactions you may also see structural surveyors, land surveyors, environmental consultants and other technical experts involved on behalf of the purchaser. Tax consultants are rarely seen in isolated transactions, but frequently in transactions of portfolios or valuable property companies.

The real estate agent is typically remunerated by the seller on the basis of a percentage of the value of the property. The finance providers are remunerated by their respective parties and so are the lawyers and technical experts, if any. The lawyers and technical experts generally base their fees on hourly rates, although the complexity of the transaction, or the value of the property and the corresponding potential liability, may affect remuneration.

4.2 Typical deal flow

The typical deal flow would be as follows:

1. After having identified the targeted property the prospective purchaser receives a bundle of property related documents from the real estate agent or the seller's lawyers. Often, the parties already informally agree on main terms such as price, hand-over date etc. at this early stage.

2. A heads of terms agreement and a non-disclosure agreement may be negotiated and concluded. This is unusual for smaller deals, though.

3. The prospective purchaser, its lawyers, and other relevant advisers conduct a due diligence investigation and request relevant additional information.

4. The purchase agreement is negotiated between the lawyers' of the parties taking into consideration the findings of the due diligence investigation.

5. The purchase agreement is concluded.

6. The purchaser makes an escrow deposit or provides a bank guarantee for the full purchase price. In deals involving larger, financially sound purchasers it may be agreed that no deposit or guarantee

needs to be made or issued. Instead the purchase price is paid in full on the hand-over date.

7. The seller and the purchaser digitally sign the absolute title deed. The deed will be submitted to the Land Register for registration. The seller will not sign the deed prior to having received the full purchase sum or adequate security for the purchase sum.

8. The seller clears mortgages and other registrations as agreed. It is often agreed that the deposited purchase sum may be used for this purpose. A turnaround time of (typically) a few weeks must be expected.

9. The title deed is then clear of all adverse endorsements.

10. The purchase price is released to the seller from the escrow account, except for any amount owed to the purchaser according to the completion statement. If the completion statement has not been agreed at this point, but is expected to be in favor of the purchaser, it is common practice that an estimated amount is being withheld on the escrow account.

A conditional title deed is drawn up instead of an absolute title deed if certain conditions remain unsettled before the transfer can be completed. Often this is relevant if the property is undergoing a division as part of the deal.

5 Liabilities of the parties to real estate transactions

In any Danish transaction, including that of real property, the seller is under a duty to loyally disclose any and all relevant information to the purchaser. The relevant information is normally disclosed in the sale and purchase agreement. Even though there are no formal requirements for the sale and purchase of real estate (even a verbal agreement may be binding) all agreements are, in practice, in writing with a detailed regulation of the terms of the transaction. Formal transfer of title requires a registration to be made with the digital Land Register[5], but this title registration typically only includes the most important terms, such as the hand-over date, the purchase sum and the parties' names. Therefore disclosure of relevant information, warranties, limitations etc. will not be submitted as part of the electronic title registration, and hence this information will not be made publicly available.

If the seller breaches his disclosure obligations the purchaser may claim damages for losses related to the lack of information and may, in severe cases, terminate the contract too. The purchaser may lose these rights if the non-disclosed information could have been revealed by the purchaser's rea-

[5] See further on this issue in section 3 above.

sonable investigation prior to concluding the contract of sale. Any information provided by the seller may lead to liability if incorrect or misleading.

Sellers usually only provide warranties relating to title, mortgages and other encumbrances. For most other issues relating to the transfer, the seller will normally only provide information "to the best of seller's knowledge". Though the purchaser may rely on the seller's warranties, a due diligence will in practice always cover the warranted issues.

Whether or not it is expressly agreed by the parties, a strict liability is imposed on the seller who does not have full ownership and the full right to transfer this ownership.

5.1 The Danish Limitation Act and Transitional Provisions

A new Danish Limitation Act came into force on 1 January 2008. According to the Act, the general limitation period is 3 years with an absolute limit of 10 years calculated from the time where the claim came into existence (claims regarding construction defects came into existence before the time of hand-over).

The 3-year limitation period runs from the day on which the claimant (the purchaser or the employer) became aware, or ought to have become aware, of the claim.

The Act is applicable to all claims, whether they have come into existence before or after 1 January 2008. Time-barring generally did not occur before 1 January 2011, unless time-barring would have occurred before under both the old and the new Danish Limitation Act.

In connection with construction contracts entered into on the basis of either the ABT 93 (General Conditions for Turnkey Contracts) or the AB 92 (General Conditions for the provision of works and supplies within building and engineering) between professional parties, the limitation period for certain claims, including claims for construction defects, set out in the standard agreed documents (a 5 year period) applies between the parties, notwithstanding the 3-year limitation period set out in the Act.[6] Professional parties are free to agree on a different time-barring than the limit set out in the Act.

The Limitation Act contains a transitional rule concerning a pro rata reduction of the price in case of soil contamination. The final limitation period of these claims is 20 years until 1 January 2018. Subsequently, the final limitation period is 10 years.

[6] See further on building works and contracts, below section 11.

6 Finance and banking

The Danish lenders are heavily regulated by statutes and executive orders issued by the Danish FSA.[7] The lenders must generally adhere to these rules regardless of the status and type of the borrower, though some protective rules are only applicable when dealing with consumer borrowers.

Private lenders may issue loans informally, but shall still observe the Land Register requirements in order to secure the loans by way of registered mortgages.

6.1 Main methods by which real estate lenders seek to protect themselves from default

The prevailing method of securing loans is by way of mortgages over the property in question. Since 2006 two types of legal charges have also been available and are frequently used; the company charge (in Danish: *virksomhedspant*); and the receivables charge (in Danish: *fordringspant*). The more sophisticated lenders may also require negative pledges, account pledges, share pledges, assignments of receivables etc. and springing mortgages (mortgages which initially are not registered with the Land Register in order to save fees, but may be so at the will of the lender).

6.2 Proceedings for realisation of mortgaged properties

A mortgage lender who does not receive payment may put the property up for a forced sale. Forced sales are managed by the enforcement courts (in Danish: *Fogedretten*). Mortgagees are covered in order of priority and uncovered mortgage loans will be deleted from the Land Register. However, the mortgagees will keep their personal claim against the borrower. It typically takes 4-8 months from default until a forced sale can be carried through.

In a large number of cases the mortgagee and the mortgagor agree on an informal sales procedure where the property is put on the market and sold in the ordinary market. Such voluntary sales often lead to an improved purchase price, but may only take place if both mortgagor and mortgagee approve the procedure.

6.3 Protection from claims by other creditors

A real estate lender needs to register his mortgage with the Land Register to be protected against third party rights over the property. Company charges, receivables charges and negative pledges also need to be registered for third party protection, whereas assignments and account pledges are perfected by giving notice to the debtor (the bank holding the account). Share pledges

[7] The most important being the comprehensive Financial Business Act, the Mortgage-Credit Loans and Mortgage-Credit Bonds Act, the Act on Measures to Prevent Money Laundering and Financing of Terrorism, the Payment Services Act, the recent Act on Financial Stability, the Securities Trading Act, and the Executive Order on Good Business Practice for Financial Undertakings.

are generally perfected by notification to the company and upon registration in the company's share register.

7 Danish Business Lease Law

The Danish Business Lease Act governs most aspects of business lease agreements. The Business Lease Act governs leases of buildings only, so the lease of land without buildings thereon will be unregulated thus requiring detailed contract drafting. Finance leases generally also fall outside the scope of the Business Lease Act.

The Act is generally considered well balanced, though a number of sections in favour of lessees are mandatory. Some of these clauses relate to termination, as the lessor may normally only terminate the agreement if the lessor 1) is going to use the leasehold himself and the termination is deemed reasonable taking both parties' interests into consideration, 2) can prove that the building is to be demolished or needs to undergo maintenance which requires that the leasehold is vacated, 3) in certain cases of a lessee's breach of the contract, or 4) if another substantial reason makes it important for the lessor to be released from his obligations towards lessee.

If the lessor is allowed to terminate the lease agreement, a 3-month notice period shall be observed (12 months if termination is for reason 1) above). The lessor is required to compensate the lessee for any loss suffered due to termination, unless termination is based on the lessee's breach of contract.

The lessee, on the other hand, is free to terminate the contract with 3 months' notice after expiry of an agreed non-termination period, or from the outset if no such period has been agreed.

In case of material breach of contract the injured party may terminate without notice and demand compensation for losses suffered.

Both the lessee and the lessor may generally hold their current counterparty contractually liable for breach of contract, regardless of whether the breach was committed by the counterparty's predecessor. Therefore, a purchaser of a property with leaseholds should ensure a right to hold the seller responsible, in case the lessee at a later stage puts forward claims stemming from the seller's ownership period.

The green lease concept is not in practical use in Denmark although many market participants emphasize sustainability and low energy consumption.

7.1 Typical business lease terms

In the following the typical provisions for leases of business premises in Denmark are described with regards to: (a) length of term; (b) rent adjustments; (c) tenant's right to sell or sub-lease; (d) insurance; (e) change of control of the tenant; and (f) repairs.

(a) Length of Term

In Denmark, business premises are generally leased on a minimum term during which the lease is non-terminable unless the contract is breached. The period of non-termination varies a lot depending on the type of leasehold and the investment made by the lessor to prepare the leasehold for the lessee, but is typically twice as long for the lessor as for the lessee.

(b) Rent Adjustments

Most often an indexation clause has been agreed between the parties, so the rent increases every year according to the net price index, but with a minimum increase of, say, 2 or 3 %. Sometimes, a maximum increase is also agreed. Apart from that the lessor is practically always allowed to increase the rent proportionally with increases in taxes or utilities, or other costs paid by the lessor with relation to the leasehold.

Under the Business Lease Act either party may require that the rent be adjusted to the market rent by observing a special procedure. Such adjustments may take place 4 years after commencement of the lease agreement or 4 years after the latest previous adjustment to the market rent.

(c) Lessee's right to sell or sublease

Under the Business Lease Act the lessee may assign the lease agreement to a third party within the same line of business, unless the lessor has weighty reasons to object to such assignment, e.g. due to the third party's lack of experience or financial situation. Subleases are not permitted. The sections of the act about assignments and subleases are mostly derogated by agreement.

(d) Insurance

It is typically agreed that the lessee must insure his business and inventory, whereas the lessor must take out building insurance.

(e) Change of Control of the tenant

The Business Lease Act does not govern change of control or restructuring situations, so these are generally permissible unless otherwise agreed between the parties. However, most lease agreements drafted by legal advisers contain change of control clauses requiring the lessor's permission prior to such event (or at least enabling the lessor to object to the change of control under defined circumstances).

(f) Repairs

It is typically agreed that any external maintenance is the responsibility of the lessor, whereas the internal maintenance (painting of the walls, maintenance of all installations, floors, locks and so on) is the responsibility of the lessee. At the same time it may very well be agreed that lessor is entitled to be reimbursed for repair costs related to the leasehold.

8 Danish Residential Lease Law

Residential leases are strictly regulated in Denmark. The relevant legislation, the Rent Act and the Act on Temporary Regulation of Housing Conditions, are overall tenant-friendly and mandatory. At the same time the legislation is very complicated, and - even though extensive case law exists - many issues are not entirely clarified.

The legislation applies to agreements regarding the lease of accommodations, including sub-lease, regardless of whether the tenant is a natural or legal person. The Act on Temporary Regulation of Housing Conditions applies in accordance with the provisions set out in the Act.

8.1 The different rental regimes

For residential leaseholds there are several different legal regimes in terms of permissible rent levels and rent adjustments. The rules vary with the type, age and location of the property, the physical state of the dwelling, and what is agreed in the tenancy agreement. Hence, specific advice on rent levels and adjustment possibilities requires knowledge of the property and a review of the tenancy agreement in question. Some general information about the typically applicable rules will, however, be provided in the following.

Most tenanted properties which are traded for investment purposes fall under one of these three categories:

(a) Properties with at least 7 tenancies situated in a so-called regulated municipality (cf. 8.1.2 below)

(b) Properties situated in a so-called unregulated municipality (cf. 8.1.3 below)

(c) Properties put in use for the first time after 1991 (cf. 8.1.4 below)

8.1.2 Tenanted properties in regulated municipalities (at least 7 tenancies)

The majority of the tenanted residential properties on the property investment market fall under this category. This is due to the fact that most (and almost all of the larger) municipalities have chosen to be so-called regulated municipalities for which a strict rental regime applies for most properties with at least 7 tenancies.

Under this regime the maximum rental level is fairly low and based on complex calculation rules. The overall principle is that the rent must continuously correspond to the landlord's costs with a fixed extra charge to allow for some return on his investment. Hence, the landlord is only allowed to pass on property taxes; costs incurred in the day-to-day operation of the property; and a prescribed charge to cover maintenance costs. The permissible capital charge constituting return on the investment is generally 7% of the property value as of 1973, but may for properties built after 1963 be higher, in certain cases up to 14% of the purchase sum.

As the landlord must abide to the maximum rent, it is generally not possible to increase the rent for the tenancies mentioned in this section. One notable exception is that the rent for dwellings which have been substantially improved at the landlord's expense, may be set at the rent level applicable for similar properties in the same area disregarding the complex mathematical calculations of maximum rent mentioned above (see the following section for further information). A dwelling is normally considered to have been substantially improved if the landlord has spent more than roughly EUR 31,000 in total or EUR 265 pr. sq. meter on the improvements. This threshold is adjusted and published annually and the figures mentioned are from 2011.

8.1.3 Tenanted properties in unregulated municipalities

For tenanted properties in so-called unregulated municipalities the parties may freely decide the initial rent level. However, if the rent substantially differs from the rent level for similar properties in the same residential area, both parties may ask the Rent Tribunal for a rent adjustment. Such request may generally be put forward at any given time, so in practice the rent is capped at the level which is considered generally applicable in the area in question, taking into consideration the type, size, quality and condition of the dwelling and the available facilities.

Another general rule is that rental increases may not take place during agreed periods of non-termination of the tenancy. The landlord is, however, normally always free to demand a rental increase based on an increase in property taxes.

8.1.4 Newly built tenanted properties

Properties put to use for the first time after 1991 are generally exempt from rent control if the tenancy agreement fulfills certain requirements.

As a general rule the parties to such tenancies may not demand rent adjustments apart from what has been agreed. However, in most cases it is stipulated in the lease agreement that the rent increases annually according to the net price index or by a fixed percentage, so the need for additional increases is limited.

8.2 Rights of pre-emption

The tenants have mandatory pre-emption rights for properties with a minimum of 13 residential tenants. This threshold is lowered to a minimum of 6 residential tenants if the property contains residential tenancies only (as opposed to business tenancies). The pre-emption rights are not affected by the construction year of the property.

If the pre-emption rights apply, the tenants must be offered to purchase the property on the same terms as any outside purchaser has offered and shall be given a period of minimum 10 weeks (the month of July does not count towards this period) to decide on the offer.

8.2.1 The all-or-nothing principle

For the mandatory pre-emption rights of Danish tenants an all-or-nothing principle applies. Under this principle, the tenants in each property will have to decide whether they – collectively – are willing to purchase the whole property. If they decide to purchase the property by the relevant majority they will have to establish a co-operative housing association (in Danish: *Andelsboligforening*).[8]

The co-operative housing association is then to become the formal owner of the property with the individual tenants holding a share of the association entitling them to live in their respective flats.

The definition of a property-unit generally follows the unit-division of the title registration system. So one would have to look in the title register to see how many flats the property in question comprises. In most cases a proper-

[8] See above, section 3.3.

ty would consist of one building, but it is possible to see properties consisting of several buildings with the corresponding number of flats.

If for instance a purchaser were to acquire two buildings with 50 flats each and with 25 tenants wishing to exercise pre-emption rights, the buildings may constitute one or two separate properties. If the buildings constitute only one property, the purchaser will end up with all flats or no flats at all. In the example the purchaser would probably acquire the property, since the 25 tenants would probably not constitute the sufficient majority. If the buildings are registered as separate properties the purchaser would end up with either both buildings (100 flats), one building (50 flats) or with nothing at all. If the 25 tenants wishing to purchase are divided evenly between the two properties they would probably not constitute the sufficient majority in their respective properties. But if the 25 tenants are in the same building this may be enough for the pre-emptive rights to be exercised in this building (but not the other).

Where multiple tenanted properties are traded at once, the purchaser would normally negotiate a right to stand down from the whole agreement (or at least get a price reduction) if pre-emption rights turn out to be exercised for one or more properties.

8.2.2 Purchase of property companies

The pre-emption rights are mandatory and applicable in case of a change-of-control of the owner company. However, the statute does not explicitly state whether the pre-emption rights also apply if control of the parent company of the owner company changes. This question has been tried and ended up in the Danish Supreme Court, which in a 1993 decision[9] held that the pre-emption rights only apply in case of change of control of the owner-company. Hence, the pre-emption rights are not triggered by a change of control in the parent company of the property owning company.

According to this decision the shares in a parent company (the HoldCo) owning a property-owning company may be transferred freely, whereas the transfer of shares in the company holding title to the property (the PropCo) triggers pre-emption rights (if the majority of the voting rights are transferred).

9 Environmental considerations

Environmental issues are increasingly addressed via EU or national legislation. The most common environmental issues that arise in relation to real property transactions relate to contaminated soil. These rules will be briefly described in section 9.1.

[9] U.1993.868H

Furthermore, the rules on energy performance require performance certificates to be issued in most transactions. These rules are mentioned in section 9.2.

9.1 The Soil Contamination Act

The Soil Contamination Act (in Danish: *jordforureningsloven*) applies to any soil and ground water contamination, regardless of when and how it has arisen.

The Act is based on the "polluter pays" principle, which means that the public authorities can issue clean-up orders without having to prove negligence on the part of the polluter, if the pollution - or the majority of it - took place after 1 January 2001.

A "polluter" is defined as:

> 1) the person who, for commercial or public purposes, either carries on or carried on the business or uses or used the facility from which the pollution originates; and
>
> 2) the person who has caused pollution by negligent behaviour or by behaviour which is covered by rules imposing a more strict liability for pollution pursuant to specific legislation.

A landowner who has not caused pollution cannot be held liable for contamination caused by former owners or users of the land if the new landowner in the use of the land has not himself contributed to such pollution. However, a new landowner may be liable for clean-up orders issued against the former landowner if the acquirer was aware of, or should have been aware of, the order (and the order was not fulfilled before the acquisition).

In order to avoid this situation, the new landowner (or his advisers) should make enquiries to the authorities about clean-up orders issued in respect of the property.

In any case a landowner must always accept that clean-up ordered against the polluter is performed on his property.

According to the Soil Contamination Act, the regional and local authorities must "list" contaminated areas at one of two levels, depending on the extent of specific knowledge of contamination. All listed areas are entered into a special register managed by The National Survey and Cadastre.

A listed property is subject to certain restrictions. Change in the use of a listed area to certain types of use, such as housing, requires approval by the municipal council. Also commencement of construction works may require

approval by the municipal council. The municipal council may grant its approval subject to certain conditions, requiring the applicant to defray certain costs in connection with the use of the area or the carrying out of the construction work.

If the property is a registered property, it can be listed at one of the following two levels:

- Knowledge level 1: it is likely that the former use of the area has led to soil contamination (suspicion).

- Knowledge level 2: the existence of contamination may have a harmful effect on human health or the environment (knowledge originating from investigations).

Due to a minor amendment to the Danish Soil Contamination Act, all urban zone properties are now recorded as subject to surface contamination unless the relevant municipality has verifiable information to prove the opposite. The registration work in this regard has to a large extent been completed for urban zone properties in 2008. However, it should be emphasized that the recording of surface contamination is at a significantly different level than listings at knowledge level 1 or knowledge level 2.

Listings at knowledge level 1 or knowledge level 2 may imply restrictions as to the future use of the property if such future use is sensitive (e.g. housing, child-care centre or playground) and calls for a special permission from the local municipality. Also in connection with building and construction work, special permits may be required or special conditions may be set out in a building permit which may imply extra costs.

Listed areas can be divided into 3 different categories of contamination, F0, F1 or F2, whereas F0 means an area, where the contamination constitutes no risk for the actual use of the property for residential purposes. Information on the listing category is not registered in the land register.

9.2 The Act on Energy Performance in Buildings

Denmark has implemented the Directive on Energy Performance in Buildings by the Act to Promote Energy Savings in Buildings. It follows from the Act that most buildings must be provided with an energy label basically consisting of a statement of the building's energy status and proposals for energy saving measures as well as advice on reducing energy consumption. The labelling needs to be carried out by an energy consultant approved according to the Act and the executive orders issued in pursuance thereof.

The purchaser of a property will often be entitled to demand an energy label to be produced by the seller or have it produced at the seller's expense.

10 Planning and zoning

Denmark has a simple spatial planning system that strongly decentralises responsibility to the local municipal councils. These are responsible for detailed local planning, permits for construction works and changes in land use in rural zones.

The planning system is laid down by the Planning Act (in Danish: *planloven*) which officially seeks to ensure that the overall planning synthesizes the interests of society with respect to land use and contributes to protecting the country's nature and environment by a sustainable development of society. It follows from the Planning Act that planning and control of the use and development of land takes place at four different levels (in descending order):

1. National planning
2. Regional development planning
3. Planning and building regulations for municipalities
4. Local planning[10]

The individual plan ranks in order of priority after plans listed at a higher level.

Planning and building regulations for the municipalities define the local planning framework.

Local plans that are prepared by the municipal council apply to a limited part of the municipality, such as a certain area or even a single building. Normally, a local plan sets out detailed provisions governing the use, size, design, construction, demolition, preservation and siting of buildings, roads, green areas, public areas etc. In certain situations, the municipal council must prepare a local plan before larger construction or demolition works etc. of a certain size can be initiated.

Local plans are the only plans that are binding upon the authorities as well as upon individuals. However, the municipality may grant an exemption from the regulation of a local plan provided the exemption does not violate the principles of the plan.

[10] In this document the terms "local planning" and "local plans" are used to describe spatial plans made pursuant to chapter 5 of the Danish Planning Act.

Local plans regulate future matters only. This means that current buildings and activities remain as they are. The local plan has no impact on the ongoing use of buildings and undeveloped areas. However, the local plan can be a factor in connection with extensions/additions to buildings or changes in the use of buildings.

Decisions made according to the Danish Planning Act may be appealed to the Nature Protection Board of Appeal. However, an appeal can only be lodged against a legal issue in planning decisions.

In connection with the preparation of a municipal plan or preparation of a local plan which requires changes to a municipal plan, the municipality must carry out an environmental investigation regarding buildings and constructions which could have an impact on the environment, locally or more broadly. This investigation is called a VVM investigation.

A VVM investigation is an evaluation estimating the consequences and impacts that construction projects, for example road making or road widening, have on the environment. The evaluation also deals with conditions such as economy, traffic and ownership. The evaluation is made by The National Road Directorate and it involves public hearings. When the evaluation is completed, a statement is provided to the ministry of energy and transportation.

11 Construction works

The employer (builder) and the contractor have considerable freedom to regulate their relationship. There are no formal requirements for the construction contract. However, in most cases standard forms (agreed documents) constitute the contractual basis of the parties.

In general, construction contracts are being entered into on the basis of the agreed document AB 92 (General provisions for the provision of works and supplies within building and engineering). In turnkey contracts the similar agreed document ABT 93 (General provisions for turnkey contracts) is used.

The agreed documents were drafted by representatives of both the employer and contractor side and regulate relevant contract issues, e.g. guarantees, defects and liability. Some of the main features of the documents are described in the following subsections.

11.1 Guarantees/Performance bonds

Unless otherwise agreed (in the tender documents or in the construction contract) the contractor must provide security of due performance to the employer. The security may be provided as a bank guarantee, an insurance guarantee or adequate security.

Normally, the security will be in the form of a bank guarantee or a contract of guarantee from a professional guarantee association. The security regards all potential claims under the construction contract including potential extra work.

During the construction period and until the handing-over, the security must correspond to 15% of the contract sum. As from the handing-over date the security must correspond to 10% of the contract sum provided no defects have been listed in connection with the handing-over inspection. Otherwise, the security is reduced when the defects are remedied.

The security is further reduced as from the 1 year inspection, corresponding to 2 % of the contract sum.

The security ceases 5 years after the handing-over unless a prior claim from the employer for remediation of defects has been made. In that case the security ceases when the defects have been remedied.

If the employer requests payment under the guarantee, the employer must make the request in writing to both the contractor and the guarantee association specifying the type and extent of defects as well as the claimed amount. Unless the contractor objects to the claim to the Arbitration Board of Building and Construction (in Danish: *Voldgiftsnævnet for Bygge- og Anlægsvirksomhed*), the requested payment has to be disbursed to the employer within 10 workdays from the request.

11.2 Handing-over of the construction works

According to AB 92/ABT 93 the contractor must inform the employer before completion of the work and the employer must then convene the contractor to a handing-over meeting on site. Unless material defects are discovered on the handing-over meeting, the employer must accept the work as handed over upon the conclusion of the meeting.

Normally, the parties will draw up a handing-over protocol listing claims for defective work and any circumstances pointed out by the employer in addition to the comments of the contractor thereon. It must appear from the document whether the parties consider the work as having been handed-over or not.

11.3 Notice of defects

According to AB 92/ABT 93 works are deemed defective

- if the work has not been performed in accordance with the contract,

- if the work has not been performed with due professional care and skill,

- if the work has not been performed in accordance with instructions given by the employer (given the instructions are correct), or

- if the contractor has failed to provide other services agreed upon in the contract.

The materials used in the construction works may be defective if they are not as agreed or if they are not of a general, good quality.

The handing-over date determines whether the work is to be considered as defective or not even if the defects are hidden.

The contractor is obliged to remedy all defects pointed out at the handing-over meeting. However, the employer must in writing inform the contractor of a time-limit to remedy the defects. The time-limit is set out taking the type and extent of the defects into consideration.

If the contractor fails to remedy the defects within the time-limit, the employer is entitled to have the defects remedied by use of another contractor at the original contractor's expense.

After the handing-over date the contractor is obliged to remedy all defects pointed out in the work for a period of 5 years. Consequently, the contractor is responsible for his work for 5 years after the handing-over date.

The employer must make a complaint within a reasonable time after the defect was discovered, or ought to have been discovered. However, if the contractor is guilty of gross negligence or fraud, this limitation does not apply. In these cases the employer may even make a complaint after the expiry of the 5-year liability period.

When a defect has been discovered the employer has to set out a written time-limit for the contractor to remedy the defect. The time-limit has to be set out in consideration of the type and the extent of the defect. If the contractor fails to remedy the defects, the employer is entitled to have the defects remedied at the contractor's expense.

The contractor's obligation to remedy the defects lapses if remediation implies disproportionately great costs.

The employer is entitled to claim a pro rata reduction of the price, if the contractor does not remedy the defect within the time-limit, if remediation of defects implies disproportionately great costs, or if remediation is rendered impossible.

11.3.1 1 and 5 years inspections

The employer convenes the contractor to an inspection to take place within 1 year after the handing-over date. If the employer omits to convene and make the 1 year inspection, or if the inspection is not carried out with due care, the employer cannot within a reasonable time thereafter point out defects that would have been discovered in connection with a careful inspection.

The liability of the contractor does not change after the 1 year inspection. The basis of liability is the same throughout the contractor's liability period. However, the employer should point out defects within a reasonable time after they have been discovered.

Within 5 years after the handing-over date the employer convenes the contractor to a final inspection of the construction work.

In connection with the inspection an inspection protocol should be drafted listing any claims for defective work as well as other circumstances pointed out by the employer, and comments from the contractor in this respect. The inspection protocol must be signed by both the employer and the contractor.

11.3.2 When AB 92 or ABT 93 is not agreed

If AB 92 or ABT 93 is not agreed between professional parties, the principles set out in AB 92/ABT 93 will, in several matters be regarded as complementary law.

However, some notable differences between being in- and outside the scope of AB92/ABT93 should be mentioned:

AB 92, Sections 6-7, concern the obligations of the employer or the contractor, respectively, to provide a guarantee. If AB 92 is not agreed upon, neither party is obliged to provide a guarantee.

According to section 14 of AB 92, the contractor is entitled to carry out additional works ordered by the employer provided that such extra works are connected to – but not included in – the construction contract. If AB 92 is not agreed upon, the employer may have the additional works carried out by another contractor.

Under section 34 of AB 92 the contractor is not liable for operating loss, loss of profit or indirect loss. If AB 92 is not agreed, the employer is entitled to full compensation including indirect losses, provided that the contractor is held liable for negligence.

AB 92, section 36, concerns the absolute period in which the employer can give notice of defects. The general rule is a period of 5 years from hand-over of the property to the employer. Furthermore, the employer is obliged to give notice of any defect within reasonable time after such defect is or ought to have been discovered.

If the parties have not agreed on AB 92, the Danish Limitation Act applies. The Act provides that the absolute limitation period is 10 years, whereas the limitation period is 3 years after the time where a defect was or ought to have been discovered, please refer to section 5.1 above.

AB 92, section 47, concerns disputes. If the parties have agreed on AB 92, any legal dispute between the employer and the contractor must be settled by arbitration (contrary to disputes that are to be settled in a court of law in instances where AB 92 is not agreed upon). The advantage of arbitration is that there is no publicity, and it is a one-tiered system with no possibility of appeal.

12 Disclaimer

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