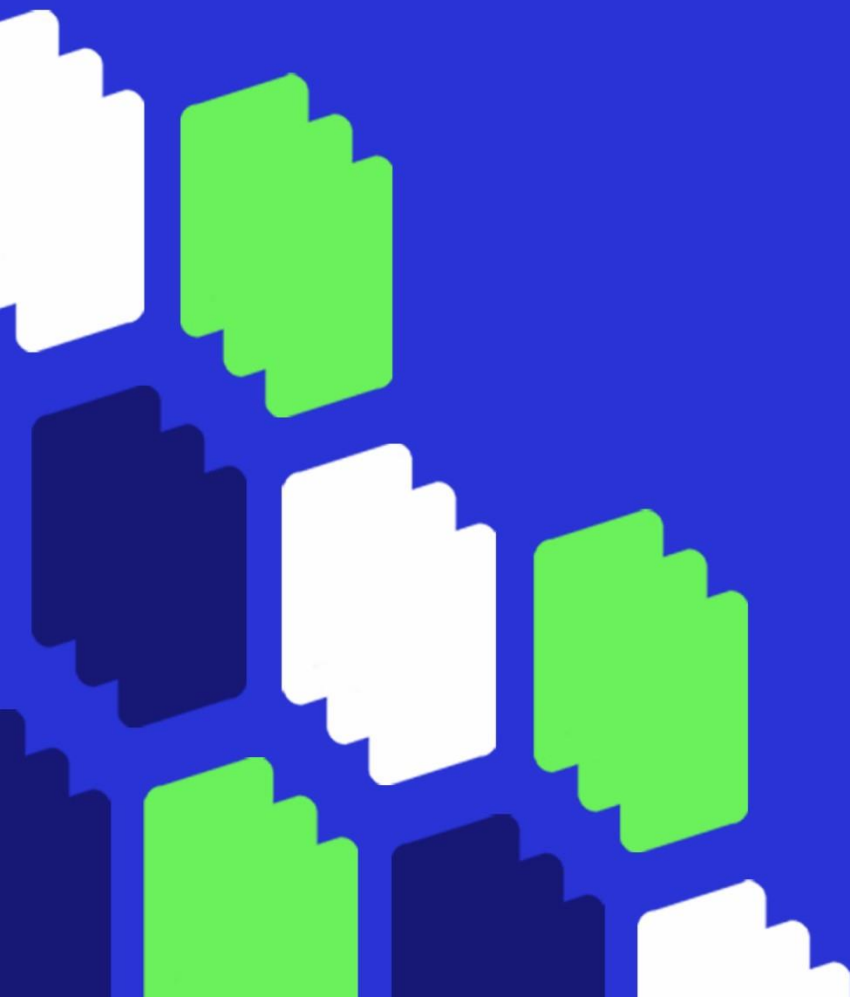




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FRAMEWORK PROPOSAL FOR THE COMPREHENSIVE REFORM OF MANAGEMENT AND DISPOSAL OF REAL ESTATE IN SERBIA

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SUMMARY

We consider the dysfunctionality of the institutional framework for the management and disposal of real estate to be perhaps the biggest development obstacle of our society.

According to the data of the Statistical Office of the Republic of Serbia, there is:


- **4.9 million real estate units registered in the real estate cadastre**, which is why they can be classified in **the category of regulated real estate market**, and
- **4.8 million real estate units outside real estate cadastre records**, of which:
 - about 2.1 million were not built in accordance with the law, which is why they are considered illegal objects, so they can be classified in the category of **unregulated real estate market**; and
 - 2.7 million buildings were built in accordance with the law, but for various reasons were not registered in the cadastre, so they can be classified as a **partially regulated** real estate market.

For these reasons, we consider the comprehensive reform of the management and disposal of real estate to be the most significant development opportunity for our country, with the potential to release real estate worth billions of euros for investments, enable successful outcome of tens of thousands of decades-long proceedings, which is suffocating our legal transactions, and ensure that hundreds of thousands of Serbian citizens obtain registration of property rights on their real estate and thus, many for the first time in their lives, in the full legal sense, become the owner of their property.

Solving such serious problems accumulated for decades cannot be simple, but it can be relatively quick. This requires a clear commitment of the state to treat this development potential as a priority and a willingness to allocate resources for it that are not small, but are minor compared to the losses that the state, citizens and the economy suffer due to not solving these problems.

Following the division of the real estate market into regulated, partially regulated and unregulated, the following recommendations respond to the specific needs of these three market segments. The key elements of the approach concerning the **unregulated market**, which is dominated by real estate built without or outside a building permit, are:

- a new approach to the legalization procedure, relying on digitization and implementation of mass legalization whenever possible,
- establishment of a more efficient mechanism that should enable the prevention of further illegal construction.



For the partially regulated market, which mostly consists of real estate where the factual situation and the situation in the real estate cadastre differ, we have developed recommendations whose purpose is to enable registration of rights where it is not possible now, because the documentation required for registration of rights is not complete, for whatever reason, and not because of a dispute about who has the right of ownership to a certain real estate.


We propose significant improvements for the segment of the real estate market that is trapped for investments due to inadequate spatial and urban planning basis. In order to solve this problem, we propose **the digitization of planning documentation and the participation of citizens in those processes**, as well as the improvement of the system of plans that are adopted, so that it is more aligned with the development needs of our society and the capacities of public administration.

We also see great potential for more rational management of real estate in the improvement of special procedures for real estate disposal, the value of which is measured in billions - from expropriation, through land consolidation, to bankruptcy and enforcement. Innovations in the implementation of procedures (e.g. the use of substitution in land acquisition procedures when public interest has been determined), greater transparency and more efficient mechanisms for ensuring the legality of the actions of holders of public authority are the essence of recommendations in this area.

When it comes to property taxation, the focus of our recommendations is not on securing higher revenues from this form of taxation, but, as in other segments of the Framework Proposal, on more efficient use of real estate, while improving the fairness and efficiency of taxation, which is to be achieved, among other things, by switching to mass valuation of real estate, and possibly by introducing a tax on the total net real estate worldwide.

We single out the recommendations with the greatest expected effects:

- **determination of the legal basis** and establishment of **new mechanisms** (commissions formed for the areas of municipalities/courts, public notaries and public bailiffs) for solving a huge number of cases by registering the status of "**probable, i.e. presumed right holder**";
- prescribing the procedure for **mass enforcement of legislation**;
- formation of the state real estate fund (**land bank**) for interventions in the procedures of expropriation, consolidation, public property, etc. and **transfer to the central level of competence** for the implementation of those procedures;
- the introduction of a central tax on the total worldwide net immovable property which would affect those with very valuable real estate;



The mentioned segments should enable the achievement of three overarching goals related to the management and disposal of real estate:

The first overarching goal of the reform is to bring the factual state of property rights on real estate into compliance with the real estate registration cadastre, as well as to ensure the sustainability of that compliance by codifying real rights and reduce the methods of acquiring property rights to real estate beyond registration in the real estate cadastre to the necessary minimum.

The second overarching goal is to ensure the application of best practices for the rational disposal and management of real estate in state ownership, as well as real estate that is in a certain special regime (bankruptcy, expropriation, consolidation, etc.).

The third overarching goal is to encourage the rational use of real estate through tax, spatial planning and urban planning policies, while improving the fairness and efficiency of property taxation. All this has the purpose of enabling the efficient use of real estate as one of the most important development potentials of any society.

In the following, we provide an overview of the key findings and recommendations for improving the situation in this area, which were reached through consultations with interested parties and joint assessments, which recommendations would first have a chance of being accepted and successfully implemented.


DETERMINATION AND REGISTRATION OF RIGHTS TO REAL ESTATE

Determination and registration of rights based on available documentation („convalidation“). It is estimated that for almost three million immovable properties, which does not include illegally built objects, there is no complete documentation that would enable the registration of rights in the real estate cadastre in accordance with the regulations.

We believe that first of all it is necessary to prescribe an authorization by law, which currently does not exist, to determine the status of the "probable, i.e. assumed right holder", based on incomplete documentation. Given that the number of real estate units in this status exceeds hundreds of thousands, and reaches millions, that authority should be assigned to commissions, which would be formed for the areas of municipalities/courts and act in administrative/out-of-court proceedings, public notaries, who would act in out-of-court proceedings, and public bailiffs, who would act in the enforcement procedure. All of them would be authorized to determine who is the likely/presumed right holder, which would be the basis for registration in the real estate cadastre.

Optimization of procedures for establishing rights to real estate and registering rights in the cadastre. The exchange of documents between the delivery obligee institutions that determine the rights over real estate, and the ones that register these rights, shows certain faults that essentially threaten the efficiency and legal security of this process. Namely, either the documentation is not submitted for registration (even though this is prescribed by law), or it is submitted without the data required for registration, or the registration is not carried out according to the submitted documentation, and the persons whose rights are being decided upon do not receive timely information whether the registration was carried out or not.

That is why we propose to amend the Rules of Court and ensure IT connectivity in order to consistently implement the obligation of the courts to submit all documents to the cadastre service for registration in the cadastre, including all court decisions and other acts that establish the existence or termination of rights to real estate, as well as temporary measures prohibiting the disposal of real estate and acts which end those bans. Furthermore, it is necessary for the Chamber of Notaries to establish an effective control mechanism for the implementation of probate proceedings, in the domain of performing obligations of public notaries, to submit probate decisions for cadastre registration, not only the decisions in cases when the testator is registered in the cadastre, but also when testator is not registered in the cadastre, along with the documentation they have evaluated and which is eligible for registration. Also, we propose to make it impossible, through IT requirements, for



taxpayers to submit incomplete data essential for the registration of real estate rights. In this segment, we also propose to prescribe more precisely the obligation for delivery oblige institutions to provide feedback to the party when their right according to the delivered document is not registered in the cadastre. It is also necessary to automate the procedure of registering the pre-notification of a building under construction and special parts of the building under construction, so that the authorities that issue building permits will enter structured data through the information system, simultaneously with the delivery of building permits and the specification of special parts of the building under construction.


Legalization. According to estimates, the number of buildings built without proper permission is more than two million; NALED's analysis showed that performing legislation with the current dynamics would take more than 40 years.

That is why we suggest that, where possible, in accordance with the law, the method of mass legalization be applied, along with the establishment of a Single Electronic Record of Illegally Built Buildings, which would make publicly available the data on the status of legalization request, as well as on submitted reports of illegal construction and the actions of inspections and other competent authorities based on those reports. This mechanism must be accompanied by a more effective suppression of further attempts at illegal construction, relying on digital tools and through more decisive initiation of legal proceedings against investors of illegal construction, with the priority of prosecuting the more serious forms of this criminal offense (illegal construction for the market).

Conversion of the right of use on construction land into the right of ownership.

The process of conversion with a fee has been carried out for 14 years, undoubtedly unsuccessfully, since the state has received funds based on conversion fee that can be considered minor, while valuable building land is not used in an optimal way, if it is used at all.

That is why we believe that the key public interest here is to complete the conversion process as soon as possible and to put the locations that are now administratively trapped into productive use. In order to achieve this, we believe it is necessary to abolish almost all exceptions on the right to free conversion, promptly establish the jurisdiction of public authority at the republic level that would challenge the conversion within a reasonable period of time or exclude from conversion the construction land that is of public interest, and implement the automated (ex officio) registration of property rights on construction land by prescribing a mechanism that will enable mass registration of property rights on construction land acquired through conversion, without passing a separate decision for each parcel.



Cooperative property. Legal certainty, as a key quality in the use and disposal of real estate, is essentially threatened in situations where the legal system fails to effectively protect the legal owners of real estate from unfounded claims by persons who abuse the ineffectiveness of the legal system..

As a way to overcome the serious problem suffered by many owners of agricultural land, we propose to adopt the authentic interpretation of Articles 95 and 96 of the former Law on Cooperatives, which remained in force even after the adoption of the current Law on Cooperatives, which would specify the conditions under which some land can be subject to restitution. Also, we suggest that in cases where there is a reason to return the land, a mechanism for ad hoc resolution of such requests by applying real substitution (giving other suitable land) should be foreseen).

Bearing in mind the enormous value and social importance of cases concerning the determination and registration of rights on real estate, as well as their number and complexity, we consider it justified and important that the state allocate funds to strengthen the human, IT and organizational capacities of the key bearers of this reform, and above all Republic Geodetic Authority (RGA), courts and judicial professions. In addition, it is necessary to carry out an information campaign towards citizens, through local governments, the media and through various instructions regarding the ways in which they can ensure the registration of real rights in the cadastre. One of the priorities should be to integrate as many professional users as possible into the e-Cadastre system. By strengthening the capacity of key actors to determine and register real rights on real estate, a basis will be created to conduct prospective analyzes of comparative practice, justification and conditions that need to be met in order to introduce direct entry into the real estate cadastre, and after that to consider whether, who and in which cases would perform direct registration.


SPATIAL PLANNING, URBAN PLANNING AND REAL ESTATE TAX REGIMES

System of spatial and urban plans. The optimal use of real estate in Serbia is prevented by the practice of spatial and urban planning, which leads to a large number of prospective zones having no plans that would serve as a basis for issuing building permits, or there are several plans with contradictory content.

That is why we propose to reclassify planning documents, both according to the competence for preparation and adoption (Republic, local government unit), and according to the method of implementation (strategic, which are not directly implemented, and regulatory, which are directly implemented through locational conditions). We suggest considering the introduction of a master plan (and/or similar documents prepared by the investor), which will represent the basis for the creation of spatial and urban plans for the implementation of significant investment projects. In this context, it is necessary to review the number of planning documents whose preparation is mandatory and apply the principle that there can be only one implementation plan for a cadastral (building) plot. Until the adoption of the appropriate number of implementation plans, it is necessary to ensure the consistent application of the by-law which prescribes the general rules and conditions for subdivision, regulation and construction.

Optimization of the process of preparation and adoption of plans. Procedures for drafting planning documents take an unnecessarily long time, and informing citizens and businesses about the content of the considered planning solutions is often not sufficiently complete or timely.

The key proposal in this segment is the complete digitization of the preparation, coordination and monitoring of the preparation of planning documents within the deadlines prescribed by law. The basic tool for this can be the establishment of a digital platform (e-Plan) which, as one segment of the future e-Spatial system, will enable holders of public authority to run their so-called completely digitally "legal regimes" (that is, rules and restrictions regarding construction), with the obligation to maintain up-to-date data on existing and planned infrastructure and to exchange such data for the purposes of creating planning documents in the prescribed digital format. This includes the establishment of a fully functional Central Register of planning documents and enabling citizens to easily download adopted plans, as well as to be informed in time about the contents of working versions of planning documents and to make suggestions for improvement. Finally, we believe that the introduction of the "urban rent" institute should be considered, as a mechanism for encouraging more efficient use of construction land.



Taxation of property. Property tax is the most important source of revenue for local government units; at the same time, we note significant room for improving the fairness of property taxes, as well as the objective inability of tax authorities to tax the income of natural persons from renting out real estate to other natural persons. The question of property tax fairness could be improved by different tax benefits, while taking care to preserve the income of local governments. In addition, the proposal is that, following the example of Italy, France, Spain or Switzerland, in addition to the existing local property tax, a central tax on the total worldwide net real estate would be introduced, which would include the real estate that the taxpayer has in the country, but also real estate that the taxpayer has abroad, where, for the purposes of this tax form, it would be allowed to reduce the basis by the borrowing costs associated with the acquisition of real estate, whereby a threshold could also be determined that would ensure that the majority of citizens would not be hit by this tax form, but only the most wealthy.

The problem of taxing the income of natural persons based on the rental of real estate could be solved by reforming the property tax (higher tax burden for real estate in which the taxpayer does not live, and for which they did not report rental income) or directly through the introduction of the presumed income category. It is also necessary to thoroughly consider all aspects of the general exemption from property tax for ownership of land up to 10 ares and the existence of a difference in the tax rates provided for land taxation and those applied for immovable property taxation. The successful and complete finalisation of the project for introducing the system of mass real estate valuation should serve as the basis for the transition to determining the basis for property tax purposes with this system.


MORE EFFICIENT MANAGEMENT AND DISPOSAL OF PUBLIC PROPERTY

Expropriation. The duration of the expropriation procedure is one of the most significant factors that delay the implementation and thus make the realization of public investments more expensive. At the same time, the rights of persons whose property is expropriated are not optimally protected.

Therefore, it is justified to establish substitution (exchange of immovable property) as a priority model of land acquisition, by introducing the obligation of the competent authority to initiate the exchange of immovable property whenever possible. The function of this model is also the formation of the state fund of land, i.e. real estate, in accordance with the concept of a land bank (land fund), which was established in international practice, and which would centrally perform the tasks of exchange, purchase and sale of land. Expropriation works should be carried out by the Ministry of Finance, within which a special sector or body would be formed to carry out these works, which would end the competence of the local governments, which now performs these works as entrusted. Also, we propose to switch to a system in which the valuation of real estate in the expropriation procedure will be performed by licensed real estate appraisers, i.e. experts, instead of the Tax Administration, until the conditions for full and automatic application of mass real estate valuation are created.

In order to improve legal certainty, we suggest that the owners of real estate that expect potential expropriation be given the opportunity to state their position in a timely manner in the process of drafting and adopting planning documents, i.e. in the process of determining the public interest that precedes expropriation. We consider it justified that when land is expropriated, the type of land (the dilemma of whether it is agricultural or construction for the purposes of assessing its value) is determined according to the state on the day before the public purpose of the land was determined by the planning document.

Finally, it is in the interest of protecting the property rights of real estate owners, and thus fairness, to regulate the de facto expropriation, including the situation when the public purpose of the land is determined by the planning document, and the expropriation has not been implemented for years, as a result of which the rights of the owner on that property are de facto narrowed. For those cases, it is necessary to regulate by law the owner's right to compensation in the amount of the market value of the real estate or a certain percentage of the value of the real estate, by years. As an option, there is also the prescription of the assumption that expropriation has been abandoned when a certain period has passed since the adoption of the planning document that determined the public purpose of the real estate.




Land consolidation or reparcelling. Reparcelling represents one of the powerful tools for ensuring more efficient use of land (especially agricultural land); unfortunately, the ineffectiveness of implementation of these processes means that it is used much less than there is a need for it - according to the latest research, land consolidation starts at about 10,000 hectares per year, compared to more than 40,000 hectares reparcelled annually in the period between 1955 and in 1980.

That is why we propose to establish one central national authority (e.g. the Agricultural Land Administration) which will lead land consolidation campaigns in Serbia (promotion campaigns, planning, formation and supervision of the work of compaction commissions, ensuring public interest, etc.). An essential element of the new approach to land consolidation should be the development of medium-term plans for the implementation of consolidation, for the sake of predictability and the provision of budget funds. As priority reparcelling areas, for which budget funds should first be identified, locations where the public sector has real estate whose value (i.e. rental income) can be improved by implementing land consolidation; where the public sector has an interest in acquiring rights on certain parcels of land needed to implement projects of public interest, so that consolidation is used as a preferred alternative to expropriation; where private owners show an interest in the implementation of consolidation, especially if they are ready to support this interest with investment plans in the land consolidation area, i.e. the possibility of co-financing certain costs and works related to consolidation.

We also suggest that it is impossible to implement changes in the cadastre in the consolidation area until the completion of the land consolidation procedure, in such a way that the commission for land consolidation will be responsible for all possible changes. Also, consider excluding the presentation of real estate cadastre data from the procedure after the consolidation has been carried out, so that the participation of interested parties focuses on the moment of making a decision on the distribution of consolidated mass, which is the most important moment in the process.

Management of public property. A significant part of real estate owned by public sector organizations is not registered to those organizations. These and other issues lead to the fact that the public sector does not have accurate records of the real estate at its disposal, which is a necessary condition for the efficiency of its use.

The issue of the existence of a large number of real estate with unenforced registration of public property owners is proposed to be solved with new mechanisms that we have recommended for determining the legal basis and registering rights in the real estate cadastre. Amendments to the Law on Primary Education should enable the registration of primary school facilities in favor of the owners from the local level.



For the sake of more accurate records of provincial and local governments and other users of public funds, it is necessary to clearly define the manner of keeping their records, as well as the type of data that these records should contain, by means of a by-law; additionally, it is necessary to determine the obligation of local governments, autonomous provinces and other users (public companies, capital companies...) to harmonize the data of their records with data from the real estate cadastre at least once a year.

The efficiency of the management of real estate in public property should be improved by introducing the practice of adopting a plan and program of disposal by the owner of public property, which will give clear guidelines regarding the handling of specific property (put it into public use, lease it or enable substitution in exchange for expropriation, alienate a part property that is not used, etc.). As part of this activity, it is particularly important to identify real estate (land and buildings), i.e. complexes that are in public ownership and which are not used, i.e. which are not used in the intended way, as well as to regularly inform the public about the contents of the plan and program, already during the preparation phase, in order to involve experts and the rest of the public in making proposals for the optimization of real estate management. By introducing e-Auctions, it is possible to significantly improve the transparency and efficiency of the disposal of public property. In accordance with the recommendations related to other aspects of this analysis, we propose to form a state fund of real estate for exchange, as well as to establish a unique methodology for assessing the value of property in public ownership according to the model of mass assessment, once the full conditions for its application are met - this would improve the quality of records on public property and improve the practice of using and disposing of that property.

Implementation of public infrastructure projects. It is considered that the Law on Special procedures for the realization of projects of construction and reconstruction of line infrastructure facilities of special importance for the Republic of Serbia, as one of the key ones for realization of public infrastructure projects, is not in accordance with the legal acquis of the European Union.

That is why it is necessary to develop a whole set of laws, other regulations and standards, which regulate the construction of linear infrastructure systems and other so-called "engineering facilities" of class G. Also, it is necessary to invest in human resources and technical equipment in order to ensure the improvement of the practice of planning and execution of projects of high investment value that have a key impact on GDP growth.

RESTITUTION AND PROPERTY ASPECTS OF BANKRUPTCY, FORECLOSURE AND MORTGAGE

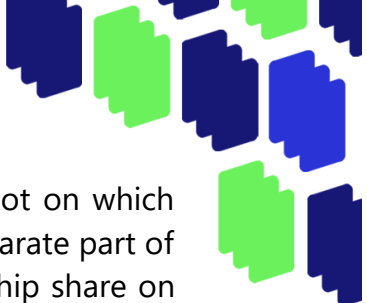
Restitution, bankruptcy and enforcement. The fact that restitution procedures are still being carried out in Serbia speaks volumes about the delay that our transition process shows in elementary regulation of property-legal relations. This affects the interests of not only claimants for restitution, but other persons whose rights may be the subject of decisions in restitution proceedings. As a result, the general insufficient arrangement of property-legal relations directly affects the efficiency and legal certainty in the functioning of the bankruptcy, execution and mortgage system.

A key prerequisite for the optimization of bankruptcy and enforcement procedures is the efficient completion of previous procedures regarding real estate rights (conversion, legalization and restitution) so that these problems do not burden the bankruptcy and enforcement procedures; similarly, the problems with restitution are related to the other problems identified in this document, especially those related to the establishment of rights, legalization and introduction of all immovable properties into the cadastre, so solving them will improve the implementation of restitution. In terms of execution, we suggest that the portal of electronic public bidding be functionally improved so that it provides all the necessary information to potential buyers, with the aim of increasing competitiveness at public auctions and consequently achieving higher sales prices.

Based on the rules and positive experiences from the enforcement procedure, we suggest that the electronic sale of assets in bankruptcy be introduced as a sales model as soon as possible. We also propose to allow the use of the property of bankruptcy debtor to establish a pledge in favor of the potential buyer of bankruptcy property, i.e. that the property of the bankruptcy debtor can be used as an object of securing the bank's claim against the buyer of that property based on a loan. In bankruptcy proceedings, separate and pledged creditors should have the opportunity, in accordance with the amount of their secured claim and the sequence of registered pledges, to participate in sales as potential buyers without paying a deposit and without paying the price.

Mortgage. The relatively good performance of lien law in the previous period can be further improved by solving several challenges that are the result of uneven legal practice, i.e. the consequence of wider problems with the legal regime of immovable property in Serbian private (real, property) law.

We propose to introduce the provisions into the Mortgage Law by which mortgages of the highest amount, i.e. mortgage security of framework loans, will be expressly allowed and regulated. Furthermore, it is necessary to consistently implement the principle of the unity of immovable property in mortgage law, so that the law will



explicitly stipulate that the mortgage on the building extends to the plot on which the building is built and vice versa, as well as that the mortgage on a separate part of the building includes the common parts of the building and co-ownership share on the land, and that by sharing the building, the mortgage on the building as a whole turns into a joint mortgage on separate parts of the building. Also, it is necessary to explicitly provide that the mortgage on a separate part of the building includes any subsequent change of that separate part of the building, in the sense of its increase by a new survey or annexation of the common part of the building. We also propose that the law establishes that all forms of establishing a new mortgage are possible only if it is expressly agreed upon with a third party and if this agreement is recorded in the real estate register.

A mortgage on the (entire) building under construction should be allowed only when it is built on publicly owned land; in other cases priority should be given to the unity of real estate so that the mortgage on the land *ex lege* includes everything that is built on it; the mortgage on a separate part of the building under construction should be arranged in such a way that it is only possible when the special part of the building under construction is registered in the cadastre, and in a way that ensures a higher level of legal certainty than pre-recording of rights. It should also be foreseen that the consent of the mortgage creditor who has a mortgage on a separate part of the building under construction is necessary for the amendment of the building permit, which in any way changes the structure, position, square footage or other important features of that particular part, and in order to preserve the identity of the subject of the mortgage upon completion of construction.



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