

Perpetual usufruct is protected by the public warranty of land and mortgage registers



Introduction

By means of a resolution approved by a panel of seven judges on 15 February 2011 (case file ref. III CZP 90/10), the Supreme Court put an end to the controversies that have appeared to date in literature and judgments, stating "the public warranty of land and mortgage registers protects a buyer of perpetual usufruct even in the case of a defective entry in the land and mortgage register of the State Treasury or local government entity as the owner of the real property."

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Key issues:

- **A perpetual usufructuary is protected by the public warranty of land and mortgage registers even if, despite an entry in the land and mortgage register, the real property does not belong to the State Treasury.**
- **A secondary effect of reconciling the protection of the public warranty of land and mortgage registers with the essence of perpetual usufruct is the fact that the State Treasury (local government entity) retains ownership title to the real property on which the perpetual usufruct was established.**
- **The former owner of a real property has a compensation claim against the State Treasury (local government entity) in respect of the definitive loss of the ownership title to the real property.**

Małgorzata Z. and Maria K. applied to the court against the State Treasury – the president of the city of Cracow and the "Ziemia Krakowska" Housing Association - for the content of a land and mortgage register to be adjusted to reflect the actual situation at law. They applied to be recorded in the land and mortgage register as the owners of a real property in place of the State Treasury and for the deletion of the housing association's perpetual usufruct right. The State Treasury was recorded in the land and mortgage register on the basis of a certificate issued by the Land Department [*Urząd Ziemski*] in November 1946 on the takeover, for agricultural reform purposes, of property which included, among others, the real property that was the subject of the lawsuit. Under a decision of Małopolski Voivode of August 2003, the entry proved unjustified because – as it was established – the agricultural reform decree did not apply to that real property. An examination of the situation at law of the real property showed that the State Treasury did not become its owner on the basis of any valid title. In light of those facts, the first instance court granted the demand made in the lawsuit and found that the deletion of the perpetual usufruct recorded for the benefit of the housing association should be a consequence of the State Treasury's lack of title to the real property because perpetual usufruct cannot arise on the real property of natural persons even if the buyer was acting in reliance on the land and mortgage register.

The defendants appealed against this judgment. In granting the appeal, the second instance court changed the judgement and dismissed the lawsuit. The appeal court found that the housing association had bought the perpetual usufruct from the Agricultural Academy in Cracow based on the situation at law recorded in the land and mortgage register, which contained no references or warnings. The cassation appeal that the claimants filed against that judgment was the basis of the resolution of the panel of seven Supreme Court judges which is discussed below.

The issue of whether the public warranty of land and mortgage registers provided for in Art. 5 of the Act on Land and Mortgage Registers and Mortgages of 6 July 1982 (Journal of Laws of 2001, No. 124, item 136, as amended) (hereinafter the "Act on Land and Mortgage Registers") may protect the buyer of perpetual usufruct on the basis of an act in law in the event of a defective entry in the land and mortgage register of the State Treasury, local government entity or association of local government entities as the owner of land was not unequivocally resolved. This fact resulted in uncertainty in transactions and undermined the rule of protection of third parties acting in good faith because perpetual usufructuaries could not be entirely certain of the validity of their title to the real property, in particular if after acquiring the perpetual usufruct right they learned of claims brought by the former owners. The importance of this legal issue is crucial because, as the Supreme Court stressed, in recent years there have been frequent instances where administrative decisions declaring a takeover or declaring grounds for acquisition of ownership title to certain real properties for the benefit of the State Treasury (and consequently – also for the benefit of local government entities as a result of the municipalization of real properties) have been challenged. In practice, this concerns land unlawfully taken away from private owners by the State in breach of the agricultural reform decree, other statutes of law and nationalization decrees and provisions on the expropriation of real properties in force at the time.

At this point, there arose controversies concerning the validity of the perpetual usufruct title in the event of a defective takeover of a real property by the State Treasury (local government entities). It was not clearly explained whether in similar situations the public warranty of land and mortgage registers protects the buyer of a perpetual usufruct right.

Until now, two views on the situation have prevailed in judgments and literature. One view ruled out the possibility of applying Art. 5 of the Act on Land and Mortgage Registers to the protection of a buyer of perpetual usufruct entirely, with the argument that this was in conflict with the essence of perpetual usufruct as expressed in Art. 232 of the Civil Code, pursuant to which perpetual usufruct may be established only on real property belonging to the State Treasury and local government entities or associations thereof.

According to the opposing view, there were justifiable grounds to extend the public warranty of land and mortgage registers to protect perpetual usufructuaries in the circumstances in question. This view was shared by an extended panel of the Supreme Court in the resolution under discussion. Under that decision, the Supreme Court accorded primacy to the rule of protection of third parties acting in good faith in transactions at law faith and to the rule of security of transactions in law, which rules are expressed in the Act on Land and Mortgage Registers, over the rule expressed in Art. 232 of the Civil Code.

For the protection of the above rules, defective conduct of the State Treasury resulting in a change to the legal status of real property may not deprive a perpetual usufructuary of legal protection, even against the owner of the land.

To reconcile the rule of protection of third parties acting in good faith and the rule of security of transactions in law with the essence of perpetual usufruct found in Art. 232 of the Civil Code, the Supreme Court accepted a concept according to which there are two basic effects:

- acquisition of the perpetual usufruct right from an unauthorised entity (primary effect) and
- acquisition of ownership title to the real property by an unauthorised entity (the State Treasury, local government entities) (secondary effect).

In such a situation, the former owner of real property is left with a compensation claim against the State Treasury (local government entity) in respect of the definitive loss of ownership title to the real property because, it should be stressed, the secondary effect of the warranty does not eliminate the unlawfulness of the State Treasury's actions in connection with the takeover of the former owner's real property.

A few words on perpetual usufruct right

The right of perpetual usufruct (*użytkowanie wieczyste*) is one of the most important property interests in land, specific to Poland.

Perpetual usufruct may only be created on land belonging to the State Treasury or local authorities. Once created, it can be inherited, transferred to third parties and encumbered (mortgage, easements, usufruct). The perpetual usufructuary is the owner of buildings and other constructions built on the land. In comparison with the wide powers granted to the holder of the perpetual usufruct right, the owner of the land (the State Treasury or the local authority) is substantially restrained in its powers: it cannot encumber the property or sell it to an entity other than the holder of the perpetual usufruct right. Only the holder of the perpetual usufruct right is entitled to use and collect income from the land.

One of the fundamental differences between perpetual usufruct and ownership is that perpetual usufruct is supposed to be created for a defined purpose (the development of a project or for conducting some sort of activity) as set out in a contract. The period may vary from 40 to 99 years depending on the purpose of its creation, but usually it is 99 years.

Upon termination of a perpetual usufruct contract, the perpetual usufructuary loses his right, and the land (together with the buildings and other improvements) is taken over by the owner. The owner is, however, obliged to reimburse the perpetual usufructuary for the current market value of the buildings and other improvements legally made on the land. For more information on the perpetual usufruct right we refer to our Real Estate Investment In Poland guide at http://www.cliffordchance.com/publicationviews/publications/2011/03/real_estate_investmentinpoland-yourlega.html

This Client briefing does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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