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Real Estate

US Virgin Islands – Law and Practice
Dudley, Topper and Feuerzeig, LLP

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US VIRGIN ISLANDS

LAW AND PRACTICE:

p.3

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The 'Law & Practice' sections provide easily accessible information on navigating the legal system when conducting business in the jurisdiction. Leading lawyers explain local law and practice at key transactional stages and for crucial aspects of doing business.

Law and Practice

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Dudley, Topper and Feuerzeig, LLP is situated in Charlotte Amalie, St. Thomas. Dudley, Topper and Feuerzeig, LLP is the largest law firm in the US Virgin Islands. Six of the firm's fifteen attorneys work in the Transactional Department and focus on real estate development and management, commercial and residential sales and purchases, title insurance, land use, real

estate brokerage and representation of landlords and tenants. Within the department, attorneys also provide services related to financial services, corporate development, acquisitions and management, labour and employment, tax issues, and trusts and estates. The team also offer expertise in the negotiation of government tax incentives to further economic development.

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1. General

1.1 Main Sources of Law

The main source of real estate law in the US Virgin Islands (USVI) is a combination of applicable federal and local common law (the body of law derived from judicial decisions) and local statutory law (as enacted by the USVI legislature and codified in the Virgin Islands Code). A relatively recent decision by the Virgin Islands Supreme Court has significantly impacted the development of common law in the USVI. Due to this change, it is challenging for practitioners in the USVI to reliably predict the outcome of disputes involving certain local common law principles. The body of statutory law governing real estate has evolved over the years, but it remains somewhat limited, both in depth and scope.

1.2 Main Market Trends and Deals

Hurricanes Irma and Maria hit the USVI in September 2017. The hurricanes caused extensive damage to many hotels,

buildings and residences. While some negative pressure on prices is expected in the real estate market as a result, this has not yet materialised.

1.3 Proposals for Reform

The most significant deal in recent history in the USVI was the sale of the former Hovensa oil refinery to ArcLight Capital Partners, a US investment fund focused on the petroleum industry. The refinery was shuttered in 2015 and sold out of bankruptcy. Another significant transaction was the purchase of a closed hotel property by Wyndham Vacation Ownership, Inc., a wholly owned subsidiary of Wyndham Worldwide Corporation.

Although the USVI has a considerable timeshare industry, there is no local statutory law governing timeshares. A comprehensive timeshare statute has been in the works for the

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last few years, and it is possible it may be enacted following local elections in November 2018.

2. Sale and Purchase

2.1 Categories of Property Rights

The following categories of property rights can be acquired:

- present possessory estates (commonly “fee simple absolute” and “life estate”);
- leasehold estates (commonly “term of years” and “periodic” leases);
- future interests (uncommon);
- concurrent estates – ie ownership by more than one person or entity (commonly “tenants by the entirety,” “joint tenants with right of survivorship,” and “tenants in common”) and;
- non-possessory interests in land (commonly “easements,” “licences,” “profits,” “covenants,” and “servitudes”).

2.2 Laws Applicable to Transfer of Title

In the USVI, common law and statutory law govern the transfer of real estate title. In many cases, common law in the USVI is similar to other jurisdictions where the source of law is English common law. There are no special rules that apply to transfers of different types of real estate.

2.3 Effecting Lawful and Proper Transfer of Title

In the USVI, transfers of real estate are effectuated through deeds. Deeds must be in writing and executed in the presence of two witnesses who must sign the deed. If executed in the USVI, the grantor’s signature must be validly acknowledged by a notary public authorised to perform notarial acts in the USVI. For deeds executed outside the USVI, compliance with the requirements for recording in the jurisdiction of execution will suffice to allow for recording in the USVI; alternatively, compliance with USVI requirements (two witnesses and an acknowledgement by a notary from the jurisdiction of execution) will entitle the instrument to be recorded. The notary may act as a witness, but if doing so, must sign as such in addition to the notarial acknowledgement.

Instruments affecting title to real property are recorded in the Office of the Recorder of Deeds in the political district in which the property is located. The Office of the Recorder of Deeds is a division in the Office of the Lieutenant Governor and has two offices: the office for the St Thomas – St John District located on the island of St Thomas, which keeps records for the islands of St Thomas, St John, Water Island and the surrounding smaller islands; and the office for the St Croix District, located on the island of St Croix, which keeps records for the island of St Croix and surrounding smaller islands.

Title insurance is common; several US-based title insurance underwriters have agents in the territory.

2.4 Real Estate Due Diligence

Buyers typically undertake a title search at the Office of the Recorder of Deeds, obtain an as-built survey, and sometimes a Phase 1 Environmental Site Assessment.

2.5 Typical Representations and Warranties

Representations in the USVI include the standard five warranties of title derived from common law:

- seisin (the seller warrants possession of the property);
- no encumbrances (the seller warrants that there are no encumbrances or liens against the property that are not listed in the deed);
- right to convey (the seller warrants the right to sell the property);
- quiet enjoyment (the seller warrants that the buyer’s right to possession will not be impacted by a third party’s legal claim to title); and
- further assurances (the seller warrants to do whatever is reasonably necessary to help the buyer perfect the title should the need arise in the future).

These warranties must be included in the deed in order to be effective. Full warranty deeds are typical, but special warranty deeds and quit-claim deeds limiting the warranties are also common. The buyer’s remedies for misrepresentation are generally limited to common law tort actions for fraud, or breach of warranty and rescission of a sale in the appropriate case. There are no special statutes governing a buyer’s remedies for misrepresentation.

2.6 Important Areas of Law for Investors

When purchasing real estate an investor should consider the following:

- Local zoning and local and US federal environmental laws may limit the scope of what a real estate owner can do with a property in the USVI.
- The USVI has a relatively high stamp tax and a relatively low property tax; so when possible, investment deals involving the sale of high-value real estate should be structured to avoid or minimise stamp tax.
- The US Internal Revenue Code of 1986, as amended, applies in the USVI as the US Virgin Islands tax code through the use of a substitution scheme known as the “mirror” system of income taxation. Recent changes to the US Internal Revenue Code affecting tax brackets are applicable in the USVI.
- The USVI, for legal purposes, has not fully been made part of the US and therefore not all federal laws or all parts of the US Constitution are applicable in the USVI (48 U.S.C. § 1541).

2.7 Soil Pollution or Environmental Contamination

In certain circumstances, the buyer of real estate can be held responsible for soil pollution or environmental contamination it did not cause. This is largely governed by US federal law.

2.8 Permitted Uses of Real Estate Under Zoning or Planning Law

Permitted uses of real estate parcels for each zoning district are specified by statute. For development projects of an appropriate size, it is possible to enter into specific development agreements with relevant public authorities in order to facilitate a project.

2.9 Condemnation, Expropriation or Compulsory Purchase

The governmental taking of land is possible through condemnation. The government may take property through the USVI's "quick take" statute (28 V.I.C. § 416). Just compensation must be paid; a party unhappy with the government's offer of compensation may have the matter heard by a court.

2.10 Taxes Applicable to a Transaction

For transfers of real estate, stamp taxes are imposed at the following rates based on the higher of the assessed value of the real estate for property tax purposes, or the actual consideration paid:

- 0-USD350,000: 2%;
- >USD350,000-USD1,000,000: 2.5%;
- >USD1,000,000-USD5,000,000: 3%; and
- >USD5,000,000: 3.5%.

Recording fees are imposed at a rate of 0.1% on the higher of the assessed value of the real estate or the actual consideration paid.

The purchaser usually pays the recording fees; the stamp taxes, historically, were usually paid by the seller, but today are commonly a negotiated item particularly on larger transactions.

No fees or stamp taxes are imposed on a sale of shares or equity interests of a property-owning company.

Exemptions to stamp tax are found in 33 V.I.C. §128, and include:

- transactions from or to the government;
- transactions made solely in order to provide or release security for a debt or obligation (this has been interpreted to include deeds in lieu of foreclosure);
- corrective deeds;
- transfer of property sold for delinquent taxes;

- partitions of real property;
- deeds given pursuant to mergers, dissolution or consolidations of corporations or transfers by or to subsidiary corporations and a parent corporation for no consideration other than cancellation, surrender or exchange of the parent's or the subsidiary's stocks;
- transfers to a non-profit organisation organised under local law; and
- transfers to or from most trusts.

All individuals, organisations or entities claiming an exemption from stamp tax must do so in an affidavit accompanying the deed.

2.11 Legal Restrictions on Foreign Investors

The federal Alien Ownership of Land Act (48 U.S.C. §§ 1501-1508) on face value persons who are not citizens of the US or who have not declared their intention to become US citizens from owning land in the territories of the US, including the USVI. There are several significant exceptions to this prohibition on land ownership including the following:

- cases in which the right to hold such land is secured by an existing treaty;
- land ownership by any alien who becomes a bona fide resident of the US;
- the acquisition by a non-citizen of land in any "incorporated or platted city, town, or village, or in any mine or mining claim;" and
- subject to a time restriction, acquisition by inheritance or in the collection or securitisation of debts.

Standing to enforce these ownership restrictions is limited to the US Attorney General.

Although this statute has not been interpreted with respect to the USVI, it likely would be subject to constitutional attack. The US has extended due process and equal protection rights to the USVI. These rights have been found to invalidate statutes barring alien residents from participating in a scholarship fund, conditioning compensation to alien crime victims upon their residency status and limiting the rights of immigrant children to attend public school. Further, at least one state statute restricting alien ownership of land has been found invalid as a violation of the Equal Protection Clause of the US Constitution.

The USVI has, in fact, enacted legislation that specifically assumes that no restriction on foreign ownership of USVI property exists. Under local statutory law, an alien corporation (defined as one organised outside the US) owning USVI personal or real property is required to comply with certain registration and reporting requirements (14 V.I.C § 611). In addition, foreign entities and persons who are non-residents of the USVI own numerous parcels of USVI real estate; such

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ownership has occurred for many years without assertion of illegality by the government.

3. Real Estate Finance

3.1 Financing Acquisitions of Commercial Real Estate

Real estate acquisitions are typically financed through bank loans or loans from other commercial lenders.

3.2 Typical Security Created by Commercial Investors

Typical securities entered into by commercial real estate investors are mortgages and assignment of leases and rents and, occasionally, personal guarantees or other third-party guarantees.

3.3 Restrictions on Granting Security over Real Estate to Foreign Lenders

The federal Alien Ownership of Land Act (48 U.S.C. §§ 1501-1508) on face value bars persons who are not citizens of the US or who have not declared their intention to become US citizens from owning land in the territories of the US, including the USVI. This Act has never been enforced. Foreign entities and persons who are non-residents of the USVI own numerous parcels of USVI real estate; such ownership has occurred for many years without assertion of illegality by the government. As a practical matter, there are no restrictions on granting security over real estate to foreign lenders nor on the repayment of said loans. Withholding taxes are imposed in some circumstances, but a loan secured by a mortgage on real estate is exempt (33 V.I.C. § 543).

3.4 Taxes or Fees Relating to the Granting and Enforcement of Security

Regarding security, recording fees are imposed at a rate of 0.1% of the principal amount secured (plus de minimus additional fees).

3.5 Legal Requirements Before an Entity Can Give Valid Security

In a commercial transaction, there are no special legal requirements, financial assistance or corporate benefit rules that must be complied with before valid security is given over real estate assets.

3.6 Formalities When a Borrower Is in Default

When a borrower is in default a foreclosure action in the courts is required in order to enforce a security interest in real estate (ie, a mortgage). This can be time consuming and somewhat expensive. The priority of creditors is determined by the priority of the recorded mortgage, however, a “notice of lis pendens” should be filed at the time a lawsuit is commenced.

3.7 Subordinating Existing Debt to Newly Created Debt

It is possible for existing secured debt to become subordinated to newly created debt by an agreement between two lenders or through bankruptcy procedures in the case of a bankrupt debtor or secured lender.

3.8 Lenders’ Liability Under Environmental Laws

A lender holding or enforcing security over real estate can be held liable for environmental contamination if the lender acquires ownership of the property or takes possession.

3.9 Effects of Borrower Becoming Insolvent

In general, insolvency will not void a lender’s otherwise valid security interest in a real estate.

4. Planning and Zoning

4.1 Legislative and Governmental Controls Applicable to Strategic Planning and Zoning

The Virgin Islands Zoning Law (29 V.I.C. § 221 et seq.) governs all development in the Virgin Islands. The Coastal Zone Management Act (12 V.I.C. § 901 et seq.) also governs development if a property is located in the coastal zone.

4.2 Legislative and Governmental Controls Applicable to Design, Appearance and Method of Construction

The Virgin Islands building code applies to all design, construction and refurbishment of existing buildings. The federal Americans with Disabilities Act may also have an impact on these matters.

4.3 Regulatory Authorities

The government authority responsible for regulating the development and designated use of real estate is the Division of Comprehensive and Coastal Zone Planning, a part of the Department of Planning and Natural Resources. The Zoning Code governs permitted uses, density, height, setbacks, floor area ratios and similar matters. However, upon application, the designated zoning of a specific piece of real estate may be amended by the legislature of the USVI.

4.4 Obtaining Entitlements to Develop a New Project

The primary requirement for a developer to undertake a new project in the USVI is to obtain a Coastal Zone Management permit if the development is located in the coastal zone. Public hearings are required, and third parties may participate, object and appeal grants of permits. Developments outside the coastal zone face much less restrictive and onerous requirements, and while there is the potential for third-party participation and objection, this is rare unless a rezoning is required by the USVI legislature.

4.5 Right of Appeal Against an Authority's Decision

There is a right of appeal against the Division of Comprehensive and Coastal Zone Planning of decisions respecting a permit application; decisions may generally be appealed to the Board of Land Use Appeals and from there to the Virgin Islands Superior Court.

4.6 Agreements with Local or Governmental Authorities

It is possible, but not required, to enter into agreements with local governmental authorities to facilitate a development project. While a planned area development statute exists and can be used for this purpose, it is also possible to negotiate unique agreements.

4.7 Enforcement of Restrictions on Development and Designated Use

The primary enforcement mechanism for development and use is through the building permit process and/or Coastal Zone Management permit process. As part of such process, the project must be found to comply with zoning and other applicable laws. Stop work orders and fines may be imposed/levied by the Department of Planning and Natural Resources when violations by existing developments are found. Ultimately, restrictions on development and designated use can also be enforced by USVI courts.

5. Investment Vehicles

5.1 Types of Entities Available to Investors to Hold Real Estate Assets

Corporations, limited liability companies (LLC) and partnerships, including limited partnerships; limited liability partnerships; and limited liability limited partnerships, are all available to hold real estate assets. Generally speaking, LLCs and partnerships are the preferred investment vehicles.

5.2 Main Features of the Constitution of Each Type of Entity

LLCs and partnerships are the two most common investment vehicles. LLCs must have at least one member (owner); they are created by filing articles of organisation with the Division of Corporations and Trademarks (DCT). All partnership types must have at least two partners – limited partnerships must file a Certificate of Limited Partnership with DCT and limited liability partnerships must file Statements of Qualification with DCT.

5.3 Minimum Capital Requirement

The minimum capital required to set up an entity used to invest in real estate is USD1,000.

5.4 Applicable Governance Requirements

The Uniform Limited Liability Company Act was enacted in the USVI in 1998. The members of an LLC may enter into an operating agreement, which governs the affairs of the LLC and the relations of the members, managers and the company. The Uniform Limited Liability Company Act governs the relations among the managers, members and the LLC only to the extent that the operating agreement does not otherwise provide, except with respect to certain non-waivable provisions. Operating agreements are not filed with the government.

General partnerships are governed by the Uniform Partnership Act enacted in the USVI in 1998 (26 V.I.C §§ 1-274). If a written partnership agreement exists, it governs relations among the partners and between the partners and the partnership. To the extent the agreement does not otherwise provide, the Uniform Partnership Act governs such relations. Limited partnerships are governed by the Uniform Limited Partnership Act enacted in the USVI in 1998 (26 V.I.C §§ 321-575). Partnership agreements are not filed with the government.

5.5 Annual Entity Maintenance and Accounting Compliance

Corporations pay a franchise tax based on 0.15% of the capital stock used in conducting business in the Virgin Islands. LLCs pay an annual fee based on 0.15% of the capital used in conducting business in the Virgin Islands. It is usually possible to limit the franchise tax payable by a corporation to the minimum fee of USD150, however, this is less clear in the case of LLCs, which have a minimum fee of USD300. Limited partnerships and limited liability partnerships are subject to a flat annual fee of USD150.

6. Commercial Leases

6.1 Types of Arrangements Allowing the Use of Real Estate for a Limited Period of Time

Leasehold estates in real property allow a person, company or other organisation to occupy and use real estate for a limited period of time without a corresponding purchase obligation. Leasehold estates are generally governed by an agreement between the parties (ie, the lease).

6.2 Types of Commercial Leases

There are no formally distinct types of commercial leases. The terms and conditions of commercial leases vary according to the agreement between the parties.

6.3 Regulation of Rents or Lease Terms

Rental and lease terms of commercial leases are freely negotiable.

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6.4 Typical Terms of a Lease

The length of a lease term is freely negotiable and usually depends on the amount of leasehold improvements undertaken in the lease. With a limited investment from the lessee, a five-year term with one or two five-year renewal options is not uncommon.

The maintenance and repair of real estate occupied by a tenant is typically the tenant's responsibility, except for major structural repairs and exterior maintenance (when the premises is part of a larger structure). However, the extent of a tenant's responsibility for repairs is frequently the subject of negotiation based on the length of a lease.

The frequency of rent payments in commercial leases is freely negotiable. Monthly payments are most common though.

6.5 Rent Variation

Whether rent remains the same throughout the duration of a lease is freely negotiable and governed by the lease; cost of living (CPI) or set percentage increases are common.

6.6 Determination of New Rent

Whether and how rent is changed or increased is freely negotiable. A CPI increase provision or a set percentage increase is most common.

6.7 Payment of VAT

There is no VAT payable on rent, but a 5% gross receipts tax is payable by a landlord on all business income including rents.

6.8 Costs Payable by Tenant at Start of Lease

A tenant will often be required to pay a security deposit and the last month's rent up front. "Key money" is less common than in prior years due to a soft market. The cost of insurance is also typically a cost for a tenant at the start of a lease.

6.9 Payment of Maintenance and Repair

Most commonly, tenants pay for the maintenance and repair of areas used by multiple tenants via common area maintenance charges imposed by a landlord; however, in some cases this is built into the rent, and the landlord nominally bears the expense.

6.10 Payment of Utilities and Telecommunications

Utilities and telecommunication charges are typically paid in one of two ways; either the properties are sub-metered and a landlord assesses and collects the charge as additional rent, or each tenant has its own meter and pays the utility directly.

6.11 Insuring the Real Estate That Is Subject to the Lease

Most commonly, tenants pay for the cost of insuring a real estate under lease via insurance charges imposed by the

landlord; however, in some cases this is built into the rent, and the landlord nominally bears the expense. Tenants typically pay the cost to insure any leasehold improvements made by the tenant.

6.12 Restrictions on Use of Real Estate

Restrictions can be imposed by a landlord on how a tenant uses a real estate. In fact, landlords can (and typically do) impose restrictions on a tenant's use. Zoning laws also restrict permitted uses.

6.13 Tenant's Ability to Alter and Improve Real Estate

Whether a tenant is permitted to alter or improve a real estate is freely negotiable by the parties to a lease. Some leases permit tenants to make improvements; however conditions on such improvements, which often includes requiring the permission of the landlord, are common.

6.14 Specific Regulations

There are no specific regulations or laws applying to categories of real estate leases.

6.15 Effect of Tenant's Insolvency

An insolvent tenant can reject a lease in bankruptcy, in which case a lease will terminate and the landlord will need to pursue a claim for any unpaid rents up to the time of termination through the bankruptcy. A tenant that does not reject the lease must keep the rent current. Bankruptcy/insolvency is typically an event of default under most commercial leases.

6.16 Forms of Security to Protect Against Failure of Tenant to Meet Obligations

A cash security deposit is a common form of security provided to a landlord to protect against failure by a tenant to meet its obligations; in addition, a landlord may claim a security interest in the tenant's personal property at the leased premises. To be perfected, this security interest must comply with applicable perfection rules under the Uniform Commercial Code as enacted as a part of the Virgin Islands Code.

6.17 Right to Occupy After Termination or Expiration of a Lease

A tenant has no right to continue to occupy a real estate after the expiration of a commercial lease; however, the landlord is prohibited from using self-help to regain possession from a tenant who holds over. A tenant who holds over can be evicted through an action for "forcible entry and detainer" filed in a USVI court, which provides for expedited procedures to obtain a court order of eviction. To guard against holding over, a landlord should send a "notice to quit" at least 30 days in advance of the expiration date of a lease.

6.18 Right to Terminate Lease

The lease, not legislation, governs the right to terminate a lease. A landlord can typically terminate a lease for breach of the lease by a tenant (provided this is specified in the lease). Typical defaults include non-payment, bankruptcy, failure to maintain insurance and failure to discharge liens against the leased premises. Similarly, a tenant can terminate a lease for breach by the landlord.

6.19 Forced Eviction

A tenant can be evicted for defaulting. This will typically take at least 45 days and can take significantly longer if the tenant disputes the existence of the default.

6.20 Termination by Third Party

A lease can be terminated by the government as a result of the taking over of the property or the leasehold by the government. Just compensation must be paid in such cases, including for the value of the leasehold estate. Leases often contain provisions governing what happens in this case.

7. Construction

7.1 Common Structures Used to Price Construction Projects

Fixed-price and cost of the work plus a fee arrangement are both commonly used to price construction projects.

7.2 Assigning Responsibility for the Design and Construction of a Project

An architect is typically responsible for the design of a construction project, and a contractor is responsible for the construction of a project. Occasionally, both responsibilities are merged into a design-build agreement.

7.3 Management of Construction Risk

Owners will typically seek warranties as to construction work on a project. Architects and contractors will typically seek to limit their liability for design and construction defects respectively. There are no legal limitations to how the parties allocate risk for these matters; thus the contract will generally govern any issues. These matters may be heavily negotiated and are typically covered by insurance.

7.4 Management of Schedule-Related Risk

Parties are permitted to agree that an owner is entitled to monetary compensation if certain milestone and completion dates are not achieved. These types of provisions are fairly common in construction contracts.

7.5 Additional Forms of Security to Guarantee a Contractor's Performance

In certain circumstances, an owner may seek a performance bond to guarantee a contractor's performance on a project.

The requirement is often driven by lender requirements, as lenders may require a performance bond or alternatives such as a letter of credit.

7.6 Liens or Encumbrances in the Event of Non-Payment

Contractors, architects and materials suppliers may file construction liens to encumber property for non-payment. Liens are automatically discharged if the party filing the lien fails to file a suit within a specified timeframe from the time of filing the lien. If a suit is filed, the owner will have to prevail in the suit or pay the party filing the lien to have the lien removed, unless a bond is obtained and evidence thereof is filed for record. The bond must be in an amount equal to 150% of the amount claimed by the party filing the lien.

7.7 Requirements Before Use or Inhabitation

A certificate of use and occupancy is required before a construction project can be inhabited or used for its intended purpose.

8. Tax

8.1 VAT

There is no VAT payable on the sale or purchase of commercial real estate, but a sale of commercial real estate by a person engaged in the business of selling commercial real estate in the Virgin Islands will be subject to a 5% gross receipt tax. A single sale not in the ordinary course of a seller's business would likely not be considered to constitute doing business for the purposes of the gross receipts tax. A stamp tax will be assessed based on the value of the property.

8.2 Mitigation of Tax Liability

Stamp taxes can be avoided by the acquisition of the entity that owns the real estate in lieu of purchasing the asset directly. This approach is often considered and sometimes used, despite concerns about inheriting the liabilities of the entity being acquired.

8.3 Municipal Taxes

There are no municipal taxes in the USVI.

8.4 Income Tax Withholding for Foreign Investors

The Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) withholding applies on sales of Virgin Islands real property by foreign investors. Foreign investors include non-resident alien individuals (as determined under US law) foreign (non US) entities, and US (non-USVI) domiciled corporations. In the absence of an exemption, tax will be imposed at a rate of 10% of the gross consideration. An exemption or reduction in withholding can be obtained from the Virgin Islands Bureau of Internal Revenue if it can be established that there will be no gain on the transaction, or

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that the tax on the gain will be less than the amount of withholding otherwise imposed. Income tax is imposed on rental income and is payable by a landlord. Rents paid to foreign investors are subject to a 10% withholding fee.

8.5 Tax Benefits

Depreciation deductions are available for owners of commercial real property.

8.6 Key Provisions in the Federal Tax Reform Legislation

Provisions of the recently enacted US federal tax reform legislation will, in most cases, apply in the USVI.

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