

## **Challenges Facing the Real Estate Market (January 2006)**

Dubai's economic boom is still confounding the critics. In fact, the Department of Economic Development (DED) in Dubai reported a 16% growth in the emirate's economy. At this rate Dubai is one of the fastest growing economies in the world. The DED attributed the current growth to its transparent policies that support private enterprise, which has generated confidence in the economy.

We had earlier said in a previous article that the setting of economic developmental objectives and their integration into an overall strategic vision form the key components of an effective land development planning process.

The most effective planning approach is an integrated regional approach, which includes local, regional and national goals, objectives and plans.

The policies related to Economic Development in most of the Emirates, and particularly the Emirate of Dubai, encourage local and foreign investments in commercial and industrial projects, and create the appropriate environment for such investment, including real estate investments. In fact it is widely perceived that the government initiatives have enabled a continuous inflow of foreign capital, a trend that is expected to be maintained with the prevailing lucrative return on investment in key sectors, including the real estate sector.

Experts predict that the emirate's economic growth will continue apace if supported by further business-friendly governmental policies.

Now let us examine more particularly one of the key economic sectors, namely the real estate sector. Leading experts anticipate another round of strong macroeconomic performance in 2006 in the wake of high oil revenues, strong liquidity as a result of the diversion of funds from the western capital markets to the maturing markets in the GCC, and the outstanding performance of leading real estate developers. Some analysts go beyond even and visualize that the real estate market in Dubai and the UAE is set to witness an enormous growth rate in the next seven years. The single most important factor that triggered this growth is the flexibility in local and regional property laws and regulations that have allowed foreigners and GCC nationals to own real estate. This vision was heightened by the enactment of new local property laws in the emirates of Abu Dhabi and Ras El Khaimah, and assurances that Dubai's own property law will be enacted in early 2006. In fact, the UAE's growth curve has defied analysts' predictions. For the past five years, almost every expert had described the growth phenomenon as a bubble ready to

burst. The reality proved to be the opposite. The facts are that the real estate industry is booming and its success in the region is unparalleled.

Senior officials had stated that the construction sector in the UAE is worth Dh 31.8 billion with projects like Dubailand, Jebel Ali Airport City, the World, and Business Bay project which contribute tremendously to the GDP of the economy. The real sector is expected to see the total value of developments rise to more than \$50 billion by the year 2010.

However, such uptrend in the development and growth of the real estate sector will face numerous real ... challenges in 2006 and the following years.

First Challenge. 2006 may see the focus somewhat shifting to other building hotspots throughout the region. The success of mega real estate projects in Dubai triggered a wave of copycat projects by other GCC countries. All of them are eager to emulate the Dubai model. Nowhere is this more evident than in the development of offshore islands, such as the Wave in Muscat and the Pearl in Qatar.

The upside however is that the UAE based developers who created such mega projects in Dubai and the UAE are cashing-in on their success by expanding their operations across the region, spreading the Dubai development model as they go, and contributing to the development of such other building hot spots in the region. The largest such project is the US\$26 billion King Abdullah Economic City to be developed by Emaar Properties in Jeddah, KSA.

Second Challenge. The infrastructure must keep pace with the rate of growth of the real estate sector and urbanization. In fact, ten years from now Dubai's urban sprawl will have grown two-and-a-half times covering an area of 604.8 square kilometers, according to a top municipal official.

Steps must be taken to prevent unplanned growth, particularly in special projects outside the direct control of Dubai Municipality, where the infrastructure is the responsibility of the developer. An emphasis must further be put on urbanization and community planning, and planning procedures and zoning regulations should be improved.

Road infrastructure should also be improved to decrease the ever increasing traffic congestion, and an integrated transit system should be provided in which each of the main components like road network, public transit, traffic technologies, and transport policies and legislation, plays its appropriate and complementary role in tune with other components and the Government's vision for Dubai and the UAE to become a regional and international hub for business and finance.

Third Challenge. Institutions are the "rules of the game" of a society. A modern market-based economy depends on various bodies of laws and institutions. Regulation is one of many instruments for public intervention in real estate and other urban markets. In fact, one of the major sources of market failure is the absence of clearly defined and enforceable property rights.

It seems that each emirate has chosen the route of developing its own real estate market body of laws and regulations on its own pace.

We still believe that a UAE Federal Property Law is essential to set a unified model and guidelines for the emirates to follow in enacting their own local real estate legislation. We believe that certain matters of ownership of real estate should and could only be dealt with on the Federal level, under the umbrella of such Federal Law.

In fact, the rules of conflict of laws between the federal and local legislation prescribe that federal laws supersede local laws. One area of special concern to foreigners, who are residents in the UAE, is the issue of applicable law on inheritance matters of foreigners owning free hold real estate in the UAE.

Under UAE Federal laws in effect, matters relating to real estate are excluded from the application of the law of nationality of the decedent in inheritance issues. Rather, the law of the place where the property is situated, *lex loci*, applies to matters relating to real estate. In this regard Article 18 of the Civil Code provides that "*Possession, ownership and other rights over property shall be governed by the lex situs in the case of real property....*". Furthermore, Article 17(5) of the Civil Code provides that "*The law of the United Arab Emirates shall apply to wills made by foreigners disposing of their real property located in the State.*"

The above articles have been the subject of controversial interpretations. Some say it can be inferred from the application of the above articles that the law which applies to the immovable properties, forming part of the estate of a foreigner who is resident in the UAE, is the law of the UAE, including matters relating to ownership rights in immovable property and the distribution of respective shares in the ownership. Such interpretation may lead to the application of Sharia law to immovable properties forming part of the estate of a non-Muslim foreigner who is resident in the UAE. Concerns of such possible interpretation and application of UAE laws, has convinced non-Muslim UAE residents dealing in or owning real estate property in the UAE, to transfer their ownership to offshore vehicles. Henceforth the demise of the foreigner would not affect or alter the ownership rather held by the special

purpose vehicle, and the distribution of such immovable properties between the heirs would become an issue of distribution of stakes in the vehicle itself, which falls under the laws of the jurisdiction where the vehicle was established.

Others say that one has to distinguish between matters relating to ownership rights in immovable property, which of the heirs may be entitled to be a legitimate owner and his respective share in the ownership, and matters relating to rights and obligations of the owners *per se*. Issues which relate to the core of the inheritance and do not, in reality, touch the property itself, such as ownership rights in immovable property and distribution of the estate amongst the heirs, should be governed by the law of the nation from which the foreigner is a citizen. However, matters relating to the rights and obligations of the owners of the property and any rights *in rem* shall be subject to UAE law as these are matters which are deeply related to the property itself, even if they arise incidentally in an inheritance issue.

Given such controversial interpretations to issues of great concern affecting behavioural trends in the real estate market, we believe that solutions for such issues should be at the core of a federal national legislation, to avoid any possible conflicts between federal and local regulation of the market.

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