

The Real Estate Development Law No. 28 of 2014: Balancing the Interests of Developers and Buyers

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Introduction

Bahrain recently enacted a long awaited and much debated new real estate development law, the Real Estate Development Law No. 28 of 2014 (the “New Law”). It is widely hoped that the New Law will help to strengthen the real estate sector and promote investor confidence in a market which has recently suffered with the indefinite stalling of several major development projects such as the Marina West project. The sudden stalling of such projects in the middle of the development cycle may be partially attributable to an insufficient legal and regulatory framework which left both developers and buyers exposed when funds simply ran out and development stopped.

This article analyses the implications of the New Law for developers and its significance in protecting buyers. The New Law attempts to regulate the activities of developers which were generally seen to be a major contributing factor to the lack of confidence in Bahrain’s real estate sector and which often left buyers with no money, real estate or investment returns.

Scope of application

The New Law defines “Real Estate Development Project” in Article 1(5) as any work or real estate development project in any nature (infrastructure or construction) for any purpose (commercial, residential, industrial or public) whatever finance method adopted (sale of off-plan units, Musataha, etc.) by any legal entity. This definition widens the scope of the New Law’s application to arguably include most development projects in Bahrain. In practical terms the wide definition may protect buyers by encouraging them to invest in all types of real estate development which would most likely fall within the parameters of the New Law. “Developers” are defined as any legal person licensed to practice Real Estate Development Projects such as construction or off-plan unit sales.

Moreover, the New Law is applied retrospectively to all Real Estate Development Projects that commenced before its enactment. Furthermore, although the New Law came into effect on 7 August 2014, developers of existing projects have a six-month period within which to comply with it, i.e.: until 7 February 2015.

New concepts introduced

The New Law introduces several concepts to regulate the market and protect buyers throughout the life cycle of a development, and provides for the establishment of a regulatory authority to regulate both Developers and buyers (the “Concerned Authority” or “Authority”). The “Concerned Authority” has not yet been nominated, but is expected to be established by Royal Decree pursuant to the enactment of the New Law’s implementing regulations.

One such concept guards buyers’ interests by regulating the sale of off-plan units – a sales method which gained significant popularity across the region during the real estate boom years – whereby units may be sold before their completion (Article 1(9)). Buyers who traditionally bought off-plan from Developers

exposed themselves to the risk of unregistered sale transactions – often paying a percentage of the total cost of the unit upfront – without actually gaining any legal title to or interest in the unit. The sale of units off-plan has, for the first time been introduced as a legal concept in Bahrain to address this issue.

The New Law prohibits any attempted sales off-plan without prior authorisation and licensing. A real estate record to register all off-plan sales (an “Off-Plan Register”) shall be established and maintained by the Survey and Land Registration Bureau ‘SLRB’. Under Article 11, the Off-Plan Register shall contain the following information:

1. the real estate Development Licence;
2. the units which the Development Licence relates to;
3. the units’ sale agreements and all disposals affecting them;
4. details of any entry which is required to be included in the SLRB Property newsletter by Law; and
5. any other information which may be determined by a resolution from the SLRB.

It is the Developer’s responsibility to provide the SLRB with the above information. Significantly, any sale agreement which has not been submitted to the SLRB in accordance with the above will be deemed null and void.

Under the New Law, Developers must obtain a Development License from the Concerned Authority before commencing a project and submit details of the relevant units in the Off-Plan Register including prior to undertaking any promotional or marketing activities in relation to the project either inside or outside Bahrain. This provision protects buyers from misleading or fraudulent advertisements and ensures that publications in the media represent credible Real Estate Development Projects.

Article 6 of the New Law introduces a further significant concept in requiring Developers to open an escrow account (the “Escrow Account”) to hold any buyers’ contributions and all other related development funds with a Bank or financial institution licensed by the CBB (the “Escrow Bank”). The purpose of the Escrow Account is to manage the financial, administrative and legal aspects of the Development. The Developer shall provide the Concerned Authority a copy of its escrow agreement with the Escrow Bank. The Escrow Bank must provide the Concerned Authority with financial statements related to the Development, and the Authority may request further information or appoint an auditor to assist it if required.

Further, to ensure greater protection for buyers in case of a Developer’s bankruptcy or insolvency, the New Law ring-fences buyers’ deposits in the Escrow Account from the funds of creditors or other depositors. Buyers’ deposits cannot be the subject of any freezing orders under the New Law (Article 7). The Escrow Bank is entitled to maintain 5% of the value of the Development which may only be released a year after buyers receive their properties. This measure is intended to act as a guarantee and provides a window for buyers to file any complaints or take actions against Developers, as well as ensuring the continued availability of funds.

The New Law (Article 26) establishes a committee to resolve any Real Estate Development Project disputes (“Real Estate Development Disputes Committee”). The Real Estate Development Disputes Committee shall be made up of two High Court judges and an expert in real estate affairs (who shall be nominated by the Minister), and is empowered to adjudicate on all disputes arising from or related to Real Estate Development Projects. Under Article 28, an aggrieved party may appeal a decision of the Committee to the High Civil Court within 15 days of the date the judgment is made, The establishment of this Disputes Committee is an attempt to shift the responsibility from the courts to a specialised panel of experts with the specific knowledge of the real estate sector in the hope that this will result in disputes being resolved faster and more consistently.

The main obligations imposed on Developers

Developers can no longer start work on a development project unless they hold a licence from the Authority (the “Licence”). The granting of the Licence is subject to the Developer submitting the completed

master plan to the Authority together with a list of documents as mentioned in Article 4(A) establishing that it has:

- either ownership of the Development or a right to develop it by way of approval from the title owner;
- approval of the master plan and building permits;
- a draft of the template sale agreement drafted in accordance with the provisions of the New Law;
- written confirmation from a consultant engineer providing an estimate value of the Development must be approved by the Committee of Professional Engineering Practice in Bahrain (COEPP);
- written confirmation from the Development's escrow agent that a deposit of 20% of the Development's estimated value has been made in the Escrow Account (the value of the land may be included in the calculation of the deposit);
- an undertaking from both the Developer and sub-developer that development works will commence within the time stated in the building permit;
- an undertaking from the Developer to maintain ownership of the common areas;
- if reclamation of land is relevant – the prior approval to reclaim the area on which the proposed Development will be built; and
- other requirements as may be stipulated by the implementing regulations so as to verify the requisite experience of both the Developer and sub-developer.

To ensure effective monitoring of Developers' activities and their compliance, the Licence granted by the Authority shall not exceed three years, and the form of the legal entity of Developers may not be altered unless and until the Real Estate Development Project is complete (Article 9).

Additionally, Developers are prohibited from varying the Real Estate Development Project except in cases of emergency and only with the prior approval of the Authority. If the Developer is late in handing over units beyond the period agreed in the contract without reasonable justification, the contract may be voidable after ninety days from the date that the delay commenced. Thus, the New Law provides buyers with a period to get their properties back on time and aims to prevent any unnecessary delays. For Developers, the New Law encourages them to have a structured well-organised plan for completion that was seen to be lacking in the previous unregulated regime. Furthermore, to ensure certainty in completion, the Authority may order specific performance from Developers to complete projects if they suspend work either temporarily or permanently. To ensure the highest standard of work from Developers, the New Law (Article 19) requires them to undertake maintenance services for the Real Estate Development Projects for two consecutive years after the completion date.

The New Law seeks to create a balance between all concerned parties by granting Developers reciprocal termination rights in relation to terminating a sale contract in cases where buyers do not perform their obligations. Article 17 (a) stipulates that in the event a buyer breaches his obligations without justifiable cause, the Developer may serve a notice on the buyer giving him ninety days within which to rectify the position. In the event that upon the lapse of the notice period, the buyer remains in breach, the Developer may then apply to the Disputes Committee to terminate the sale agreement, after which it may sell the unit to another buyer. Upon termination of the sale agreement, without prejudice to the Developer's right to claim compensation for any damages suffered, the Developer may retain up to 10% of the purchase price of the unit and refund the remainder of what may have been paid to the buyer.

The consequences of breaches in the New Law

Heavy penalties are imposed on Developers depending on the type of breach. They may be subject to a custodial sentence of one year or a fine not exceeding BD 10,000 or both for selling off-plan units without a Licence or delaying handing over completed units beyond the period agreed in the contract. Other offences under the New Law are punishable by a custodial sentence of one to five years, and a fine of BD 10,000 to BD 30,000 for providing false information to the Authority. The New Law addresses the entire lifecycle of Real Estate Development Projects from beginning to end. It outlines the consequences of not executing work within six months of the date of the Licence and extends criminal liability (including

vicarious liability) to all legal entities that may be defined as Developers.

Conclusion

Before we may assess the practical impact that the New Law has on the Kingdom's development projects specifically, and the real estate sector generally, there are a number of related laws and regulations that need to be implemented (including the Implementing Regulations) and the Concerned Authority will need to be established to act as the sector's regulator.

Many have criticised the New Law as inadequate in addressing the issue of existing stalled projects. Whilst this may be so, the Cabinet has recently approved a draft law on the settlement of stalled real estate development projects, which aims to address the issue. Despite any criticism or ambiguities surrounding this legislation, the New Law must be considered as an important and positive step towards delineating the interests and responsibilities of both developers and buyers. As a response to the demand for a structured and regulated real estate sector in the Kingdom of Bahrain, the New Law introduces the framework for a sophisticated regulated regime which seeks to balance the interests of all concerned parties and attract further investment in the Kingdom's real estate development projects.