

Kingdom of Saudi Arabia - Regulation of 'off-plan' sales by real estate developers

On 12/03/1430H corresponding to 9 March, 2009, the Council of Ministers issued resolution (No. 73) ("Resolution"), which is expected to be published in the Official Gazette shortly and will come into force on the date of publication.

Purpose of the Resolution

The aim of the Resolution is to ensure that real estate developers in the Saudi market are financially sound, that their business practices are transparent, that purchasers of real estate units are protected against fraud and unfair contractual terms and that the use by developers of instalments paid by purchasers is regulated by means of a 'Guarantee Account'.

New Committee to be set up

The Resolution is intended as an interim measure until the planned 'Real Estate Developments Guarantee Account Law' is enacted. The Government is expected to enact the Law by the end of 2009 (Gregorian calendar).

The Resolution provides for the establishment of a Committee to license real estate developers and regulate their activities. In particular, pre-sales (off-plan sales) of real estate units of all kinds (not just residential units) are prohibited unless approved by the Committee.

The Committee will comprise representatives of the Ministry of Commerce and Industry, the Ministry of Municipal and Rural Affairs, the Saudi Arabian Monetary Agency and the General Commission for Housing. We expect each of these to nominate its representative within two weeks from the date of publication of the Resolution in the Official Gazette. According to the Ministry of Commerce and Industry, under whose auspices the Committee is to be established, it is expected that the Committee will begin its duties immediately after it is constituted.

Developers require licences

The Ministry of Commerce and Industry will create a 'Real Estate Developers Register' ("**Register**") and issue licences to qualified real estate developers. It is not clear yet whether the Register will be publicly available. We understand that all real estate developers will need to apply to obtain a licence for each project. This understanding is based on the fact that the documents a developer is required to submit along with its application for a licence include, the title deed of the land, standard form sales contract, contract between the master developer and the sub-developer, and approved design of the units. The Resolution also contemplates that the Committee will create a separate register of sale agreements between the real estate developer and purchasers of the units ("**Special Register**"). It seems that both the Register and the Special Register will require multiple filings, because both will contain information not only about the developer, but also about each project and transactions relating to each project. So both registers will be dynamic. We believe that the Special Register will serve as the means by which the Committee ensures that there will not be multiple sales of the same unit. In addition, the Special Register may be used to inform prospective purchasers about the history of the units they plan to buy.

Client briefing
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Key Issues

Off plan sales prohibited without the consent of a Committee to be formed

Existing and new real estate developers required to register

Developers required to have a controlled 'Guarantee Account'

New Committee to have policing powers on a project-by-project basis

Details of processes and procedures not yet known

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Existing real estate developers will be required to apply, within a period of (60) days from the date of publication of the Resolution, for registration in the Register and obtain a licence for each of their existing projects. They will be subject to the same filing requirements as new entrants to the market.

Powers of the Committee

The Committee is empowered to set technical and financial conditions for the registration of real estate developers in the Register. At this early stage, it is not clear what these technical and financial conditions will be. However, it is possible that they will include the requirement for a 'track record', minimum capital requirements and a feasibility study for each prospective project.

As regards a developer's financial standing, the Resolution contemplates that each developer will be required to obtain a certificate from an accredited credit reporting body. It is not clear yet how many credit reporting bodies will be accredited or even whether there will be more than one. Nor is it clear how financial standing will be measured or how the pass/fail judgement will be made or whether the certificate will be required just once or periodically.

The Committee will regulate contractual arrangements not only between real estate developers and purchasers (including rights relating to the use and management of the common amenities of a real estate project and its shared utilities), but also between real estate developers and their sub-developers and developers and their selling agents or brokers.

Although not explicitly stated in the Resolution, it may be supposed that the Committee will regulate the amount and timing of instalment payments that developers may require from purchasers.

The Committee has punitive powers, including the power to close a developer's business and refer violations by developers to the General Investigation and Allegation Committee for prosecution before a competent court.

Guarantee Account

One of the keynote provisions of the Resolution is the requirement for real estate developers to set up a controlled bank account with a local bank into which they must deposit (i) instalments paid to them by purchasers; and (ii) any finance that they obtain for the project (Guarantee Account). While it is not yet known how the Committee will regulate the use of the Guarantee Account, the Resolution contemplates that the Committee will prescribe a form of agreement between the bank and the developer. This suggests that developers will be obliged to apply payments by purchasers and finance from lenders towards construction of the real estate units in a way similar to that in which lending banks control construction project loans to developers (that is, payments against commensurate construction value).

Exercise of Committee's powers

The Resolution is framed widely and gives the Committee potentially far reaching powers. In its application to pre-sales of commercial real estate, the Resolution goes beyond consumer protection and provides protection for commercial buyers, including sub-developers. On the face of it, the Resolution seeks to establish not only a licensing regime for developers, but also a system for policing developers on a project-by-project basis and, potentially, for monitoring periodically their financial standing. Until the Committee is convened and sets its policies, it is not possible to predict how it will interpret and use all the powers at its disposal, nor is it possible to predict whether the Real Estate Developments Guarantee Account Law will enhance or redefine those powers.

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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