

All you need to know to invest in real estate



Below are the answers to some commonly asked questions to enlighten those seeking to invest in the real estate market:

What is a premium?

The amount that you pay above the original price charged by the developer. This can be a percentage of the original price, or a fixed amount. The premium plus the original price is the net selling price to the owner, and does not include transfer fees or commission.

What is a transfer fee?

This fee is paid to the developer in transferring ownership from seller to buyer. It varies between 1 per cent and 7 per cent of the selling price or original price and so can be a substantial amount, usually paid by the buyer.

What is commission?

Normally 3 per cent of the selling price and again the buyer pays, although on occasion the owner may pay 1 per cent of this.

Why do people want to know the original price?

This is the price which the original owner paid to the developer. From this you can work out the percentage premium which is often used as a guide to see if a property is good value or not. In addition, when financing, all lenders need to know the original price, as most will not lend on any of the premium.

What is the BUA?

This is the Built Up Area of a property and not just the ground floor area. This includes all floors and the balcony or terrace area. Carpet or covered area is the built up area excluding the balcony or terrace. The Plot area is the total size of the plot including the garden.

What is a Phase?

This is the release of a fixed number of units at a specific moment in time. Most developers release units over several phases and re-evaluate the prices after each release.

What is Initial Deposit?

This applies when buying direct from a developer and is paid to the developer in order to secure the property in your name. It is usually 10 per cent or 15 per cent of the selling price.

What is Holding Deposit?

This secures the property for a period up to one month usually, allowing the buyer time to organise funds through either financing or transferring of cash funds. This deposit is non-refundable and can range from Dh20,000 to Dh1,000,000 depending on the property price. During this time, the owner agrees not to increase the price or sell it to anyone else.

What is a Memorandum of understanding?

This is a contract made between the buyer and seller to secure the sale. A holding deposit is paid to the agent or seller to make the contract more binding.

Are there different types of Freehold?

If we assume that the term freehold is being used in Dubai in its international sense, then the answer is yes. Freehold usually indicates that the owner of this kind of title enjoys the most superior form of private property ownership.

A purchaser can have freehold title in land, in a free standing villa and also for an apartment, the latter kind of ownership is usually called commonhold and not freehold.

Can a foreigner hold a title in Dubai?

In May 2002, General Shaikh Mohammad Bin Rashid Al Maktoum, Dubai Crown Prince and UAE Defence Minister, announced that 100 per cent freehold ownership of certain properties in Dubai was available to all nationalities. Furthermore, while new comprehensive legislation dealing with the ownership of land in Dubai is expected soon, there is currently no UAE law that prohibits foreigners from owning property.

Can one lawfully sell freehold properties to foreigners in Dubai?

There is no provision in the law that forbids immovable property (except in an auction) from being sold to foreigners in the UAE.

In case of a husband's death, is the property distributed according to Sharia?

This is a very grey area and opinions differ widely, and is an estate planning concern. As such, I suggest that purchasers approach their lawyers or accountants to take their estate planning issues further.

Are there any restrictions imposed on freehold apartments?

Yes, there are some restrictions being imposed in most sale and purchase agreements issued by developers in Dubai; these conditions are to make sure that owners of properties pay their Service Charges in time, especially if they intend to sell their property. The new land law for Dubai of which legislation is expected soon, may also contain further restrictions.

Does the buyer have the authority to sell the property or apartment? If so, when?

If a buyer has not yet become the registered owner of a property, then he can cede (i.e. transfer) his rights in his agreement of purchase under certain conditions to another purchaser but subject at all times to the approval of the Seller. Purchasers, once they are registered owners, are able to sell their property freely subject to all Service Charges and/or penalties having been paid.

How often will the Service Charges increase or will they fluctuate?

It is expected that the Service Charges levied will be reviewed yearly and only if necessary, increased annually. Unless all the owners of the building/dwellings have to pay for an emergency expense, it is not expected that there will be dramatic fluctuations or increases in the Service Charges during the year. There should not normally be an increase by more than 10 per cent in the Service Charges per year.

What type of residency visa is received upon the purchase of freehold in Dubai?

The residency visa is arranged by the developer and is usually a 3-year renewable visa. It does not normally include a work visa. It is purely to allow the owner and his immediate family to reside here without needing to renew transit visas. You may be required to pay the fees depending on the developer.

Why are Guarantees needed?

If properties are not handed over for whatever reason to the purchaser after a particular time period, the buyer usually has the option to get his money back or receive some form of compensation. Most developers give a 10-year guarantee from structural defects.

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Using a UK mortgage to buy Dubai property?

For those with real estate in the UK raising a mortgage there to buy in Dubai might appear a perfect solution. But beware the foreign currency exchange risk that you unwittingly undertake.

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At first sight the low cost finance option for Dubai property buyers with real estate in the UK is easy enough: mortgage the UK property to buy in Dubai.

Now borrowing dollars (which has a fixed rate against the dirham) against your sterling asset in the UK looks a good deal; interest rates are slightly lower than the 6-7% charged for dirham loans in the UAE.

But don't forget that sterling and the dollar have an unstable relationship. Thus what seems a good deal with sterling at \$1.80 might not seem nearly so good with sterling at \$1.20.

By way of illustration: if you mortgaged your UK house for 80% of its value in dollars, and the value of sterling collapsed, then you would have a loan obligation significantly higher than the value of your sterling asset!

What would happen then if UK house prices continue to fall as they have for the past year? Your debt cover would be further eroded. And what if Dubai real estate prices also fell?

Then you would have the worst of all worlds: a large dollar debt uncovered by a sterling British asset against a property worth less than you paid for it!

Foreign currency mortgages are not for the faint hearted. The normal rule is that you should always borrow in the same currency as your income; and perhaps to that should be added that you should only secure money against assets valued in the same currency.

The danger is that for the sake of saving a few percentage points on mortgage repayments, you end up with a debt bigger than your equity due to a falling currency.

Of course, this can work the other way round. That is what leverage and risk are all about. But at least understand that by opting to borrow in a foreign currency against a UK asset there is a serious and significant additional risk. Sure if the dollar collapses you will be better off. But ask the many foreign currency traders who lost their shirt on the fall of the euro against the dollar this year how sure you can be?

The professionals spend their lives hedging against foreign exchange risks; why on earth would you want to take on such risk when buying your home?

Indeed, in the normal 15-25 year mortgage period you are bound to be caught out at some stage - as we can be quite certain that currency movements will occur, just not when. And this might be a very expensive mistake if you happen to want to sell up for some reason within that mortgage period.

So stick with local mortgages to buy Dubai property, even if you have UK real estate to borrow against. This is not the win-win situation that it appears.

A buyers guide to the UAE

The A-Z of Dubai Property

This is a thumbnail 'who's who' and 'what's what' in the fast-paced World of the Dubai property sector.

A: Amlak Finance, leading mortgage provider.

B: Better Homes, along with Asteco, the top local estate agents.

C: Cluttons joins FPD Savills as major UK agencies in Dubai.

D: Damac Properties, largest privately-owned developer.

E: Emaar Properties, major property developer, 30% owned by Dubai Government, listed on Dubai Financial Market.

F: Fbi Property Development Company, a Dubai property development company.

G: Goldcrest, building towers in the Jumeirah Islands.

H: Hotels & Resorts IFA is a major investor in Palm Island real estate.

I: International City, tens of thousands of apartments in a themed complex behind

Dubai International Airport.

J: Jumeirah Beach Residence, development of more than 40 towers on the Dubai Marina beachfront, 100% Dubai Government owned.

K: Kinnarps of Sweden, leading office fit-out specialists.

L: Landmark Properties, another local agent.

M: General Sheikh Mohammed bin Rashid Al Maktoum, Crown Prince of Dubai and Dubai real estate sector's visionary leader.

N: Nakheel, 100% Dubai Government-owned, developer of The Palm Islands and The World.

O: Oryx, one of a new breed of Dubai property agencies.

P: The Palm Islands, one off Jumeirah and the second off the coast at Jebel Ali, massive man-made islands shaped like palm trees.

Q: Quick construction, fast-track building with minimal planning delays and no red-tape.

R: Rakbank, along with HSBC and Mashreqbank, providers of mortgage finance.

S: Springs, 4,000 town houses behind the exclusive Emirates Hills and Meadows executive homes.

T: Tamweel, home finance company, a joint venture between Nakheel and Dubai Islamic Bank, both Dubai Government entities.

U: Union Properties, the second largest listed Dubai property firm, Emirates Bank International has a controlling stake.

V: V-Kool, a Dubai firm supplying sun-reflecting window film that dramatically cuts energy bills.

W. The World, a man-made archipelago of islands in the form of a map of the world, off the Dubai coast.

X: Extremely good value-for-money property.

Y: Yachts in the Dubai Marina, a 1.8km long artificial harbour, central focus of a development of 100+ high rise towers.

Z: His Highness Sheikh Zayed Bin Sultan Al Nahyan, President of the UAE.

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Why you should buy a property in Dubai

1. Long-term residents should be considering buying to replace rental payments. Even if your home is worth a fraction of what you paid for it after 10 years, this would still be a huge improvement on the negative return of renting.
2. Second, property prices look cheap by international standards, and rental yields are still high.
3. There is a big change in the city's geography underway. What is the fringe of Dubai today, the Dubai Marina, will be uptown Dubai of tomorrow. Thus property values will follow this curve upwards, as people relocate to the new uptown.
4. Legally, there is no law to prevent freehold purchase in Dubai, and a new federal law should shortly frame legal rights into a form acceptable to international banks for mortgages; this will push demand and prices higher.
5. Oversupply is the main fear highlighted by sceptics. But there can only be so many properties in prime locations, and the time to buy them is now.
6. Demand for freehold property in Dubai is much higher than most people can

comprehend. Certainly an economy growing at 10% plus a year has a dynamic of its own that reflects a huge demand for accommodation.

7. Any property market is going to have its ups and downs, and Dubai will be no different. All the same, Dubai has a habit of frustrating those who wait for bargains. In 1998 some thought rental prices would collapse. It did not happen.

8. Comparatively property is cheap. Dubai villas cost around \$1,000 per square metre. London, at the other end of sells apartments in London Docklands at \$5,000 per square metre.

9. Dubai is in the process of creating an international property market from scratch. As a result buyers are being given an exceptionally good deal to encourage them to be pioneers.

10. As the second-hand market emerges, and the legal position of owners becomes absolutely clear, the element of risk will go, and lower risk will mean higher property prices.

11. Dubai is a city where a lot of people earn high tax-free salaries and are in a position to support higher house prices. This is a city with a 20-year track record of strong economic growth and will continue to attract foreign and regional inward investment.

Buying a property

Buying a property is probably the largest investment most people will make and its best to have your finances in order. Property mania has certainly hit Dubai and with new developments launched almost every week. If you are considering buying property whether in Dubai or abroad, there are number of factors which you should consider.

Overseas investors

Overseas investors can buy property freehold on specific developments as well as on a 99 year leasehold basis.

What mortgage facilities are available?

There are literally thousands of mortgage options. In the United Arab Emirates, however, the choice of lenders is not as widespread and the options not as attractive as those found internationally. At present, typically you can borrow at 6.5% in Dirhams for the various property developments that are regularly advertised in the local press. Banks based overseas cannot provide lending facilities on UAE properties directly so one is confined to the locally established lenders. This situation should change in the near future.

Finance can be arranged through overseas lenders if you have assets overseas too. A number of property investors with assets overseas have taken advantage of favourable international interest rates. For example, someone with property in the UK may be able to release equity to a maximum of 80% of the value of their property (less any outstanding mortgage) to finance all or part of their property purchase in Dubai.

One should be aware of the additional costs for arranging finance. Your bank may levy a fee and once again international lenders tend to offer very competitive terms. Valuation fees, Brokers Costs, Protection fees, legal/conveyance and in some cases planning permission can all add to the costs.

If you do not have overseas property to obtain finance then another form of collateral could be an investment portfolio which could be used as security to obtain a loan. If you do not have assets elsewhere then your options are limited to those offered by the lending terms of the local banks of the UAE.

Do I need to get insurance?

Most lenders will require some form of protection for the loan. Banks on the whole do not like repossessing property and would prefer the loan to be repaid from an insurance policy should a serious event occur. Similarly, if you had to sell the property to pay the loan in the absence of a policy, the value of the property may have fallen to a level below the outstanding loan amount. With critical illness affecting 1 in 4 of us at some stage in our life, many lenders will require that you have sufficient protection to cover the amount of loan you have secured.

Seeking the right insurance is key since it comes in many forms. Get the right advice to determine which one is right for you.

Remember, if your loved one passes away unfortunately the bills do not go with them - avoid the financial trauma and have yourself correctly protected.

How do I go about buying?

Once you have decided on the property you require there are going to be a number of issues that need addressing. Here are just a few to run through...

- Can you afford it? More importantly are you prepared for the property to go down in value as well as up? Property is just like any other investment and can fluctuate according to the overall market.
- How long you are going to hold the property will determine whether you can be sure it will make money or not.
- Can you afford it if the interest payments change? Lenders can alter the interest rate or the term potentially and this could have an impact on your monthly payments.
- Check if you can pay off the loan early and if so are there any penalties in doing so? Can you change lenders at a later stage? What currency do you require?
- Can you afford the transaction costs? Typically local lenders are charging 1% of the loan value as a processing fee not to mention the insurance element too. Have you budgeted for legal, protection and any other conveyancing type cost.
- What are the ongoing maintenance costs of your property and the communal areas and are they due to rise - if so by what amount? Who controls the rise in maintenance fees - developer or the residents?

- Do you need to purchase through an offshore company or Trust? Property law in Dubai is based under Sharia principles and as such in the event of the demise of your husband; the property may bypass the wife as the new legal owner.
- Can you sell the property on without restrictions? Similarly, you may wish to mitigate your death tax exposure by using some form of offshore structure. Buying property in Dubai will not avoid death taxes from your home country unless correctly structured.
- Have you sought professional help with protecting the property should a serious event occur? Life Cover, Income Protection, Critical Illness Cover, Permanent & Total Disability in their various forms should reviewed and budgeted for.

Seek the professional services of a good agent who is willing to spend time understanding your profile so the right properties are selected for you. Likewise, take guidance from a lawyer if buying locally and employ a suitable conveyance group when buying overseas. And finally, secure sound financial advice from an independent source.

Venturing Into Real Estate

Given today's real estate market conditions of rapidly rising rental rates, attractive rates of return and potential appreciation of the property, private real estate ventures are providing investors with opportunities to diversify their investments. Most prudent financial planners recommend asset allocation between stocks, bonds and recommend 5% to 10% invested in real estate investments.

Private real estate ventures provide investors, who are also businessmen and decision makers, an opportunity to actively participate in their real estate investments. This allows more control over their investments which may provide better returns than passive investments in real estate partnerships.

The initial step in a private real estate venture is the selection of a real estate brokerage firm to assist in finding potential real estate acquisitions. A Certified Public Accountant who practices in the real estate industry is a good source of referral for investors engaging a real estate firm.

Before the real estate firm's search for potential acquisitions, the investors should furnish the real estate firm with such information as:

- Cash available for investment.
- Region or location of the property.
- Acceptable rate of return, ie., cash on cash and total returns.
- Types of investments, commercial office building, residential rental, warehouse, etc.

When engaging a real estate firm, the investors should reach an agreement, preferably in writing, as to how the real estate firm is compensated. This includes the fee for selection of property, broker commissions for tenants, management services or any other technical services provided.

As to potential acquisitions, in addition to the purchase price, an offering document should be obtained from the seller's brokers. This document should include information about the physical descriptions of the property, capital improvement programs, property information, historical and budgeted operations, prospective cash flows and net operating income, and tenant information (including background and tenant lease information). At the point in time when it appears a bid will be made on a particular real estate property, it is important to engage a real estate lawyer who practices in the state and region where the property is located. An accountant may be a good source of referral for a real estate lawyer. When selecting the lawyer, it is important to assess that he/she be not only knowledgeable in real estate law but have the skills to provide advice to the real estate team. The attorney is important in negotiating the terms of the real estate contract and also the mortgage loan agreement.

Due to the fact that usually all the good deals go fast, it is important that the financing be obtained through a real estate financing firm because they have a faster turnaround than a general financing firm. The contract usually provides no more than 60 days to close; therefore time is of the essence. The real estate financing firm screens potential lenders, relying on prior experience when evaluating them. The lender is an important player in closing the deal because of his/her ability to close it at terms acceptable to the buyer. This is crucial in determining the quality of the deal (i.e. a good deal doesn't have a contingency clause in the contract).

The fee charged by the real estate financing firm is usually between 3/4% and 1 % of the loan. The contract provides for a due diligence period after the signing, during which the buyer has to inspect, examine and/or investigate the premises, and all physical, environmental, financial, leasing, municipal and legal aspects thereof. In the event that the buyer, after performing all diligence procedures, determines that the premises are not acceptable to the buyer, he/she shall have the right to terminate the agreement by written notice to the seller at any time prior to the expiration of the due diligence period. The written notice has to be stating the reasons that the premises are unacceptable, together with copies of any applicable reports or information.

An accounting firm specializing in real estate can perform the due diligence on behalf of the buyer. A due diligence checklist is provided.

Due Diligence Check List

- Obtain and evaluate current marketing reports effecting the region and county when the property is situated.
- Obtain an engineering report, environmental phase 1 report and an appraisal of the property by firms acceptable to the lender.
- Obtain a title search and updated survey.
- Obtain certificate of occupancy of all tenants
- Obtain and review all tenant leases and service contracts.
- Inquire about commissions due.

Satisfy the buyer as to the income and expenses for the property, both historical and prospective, by examining underlying documentation.