

Proof of fraud needed to file criminal cases against developers

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Investors can file a criminal case against a developer only if the reason for developer's default is criminal in nature and there is evidence to prove it, according to a lawyer.

"Investors can file a criminal case against a developer on the basis that it has not started a project and/or opened an escrow account, but only if the reason for developer's default is criminal in nature, and there is evidence to prove it on its face," Ludmila Yamalova, Legal Consultant/Partner, Al Sayyah Advocates & Legal Consultants, told Emirates Business.

Raza Mithani, Senior Associate, Al Tamimi and Company, Advocates & Legal Consultants, said: In Dubai, a criminal case may be filed where there is evidence of fraud. Failure to open an escrow account may, depending on the circumstances, constitute evidence of fraud."

Tatjana Fuhr, Legal Consultant at Fichte & Co Legal Consultancy and KK Sarachandra Bose, Partner and Corporate, Commercial and Contract Lawyer, Dar Al Adalah Advocates & Legal Consultants, agreed that a buyer can file a case against a developer who has not started the project and collected funds without opening an escrow account.

However, Ashraf Sayed, Associate, Real Estate, Hadeef & Partners, said this depends on the location of the development and the actions of the developer. "In general, unless executives of the developer have committed clear criminal acts, it is unlikely that a criminal case would be taken up by the police/public prosecutor," he added.

Can investors file a criminal case against a developer who has not started a project or opened an escrow account?

Mithani: In Dubai a criminal case may be filed where there is evidence of fraud. Failure to open an escrow account may, depending on the circumstances, constitute evidence of fraud. Failure to commence construction in itself is a civil matter, unless there is some evidence of fraud. However, Article 17 of Law No8 of 2007 provides that if construction has not commenced within six months of the date that approval was given to sell off plan without an acceptable excuse, a developer shall be cancelled from the register. That, of course, would be a regulatory rather than a criminal matter.

Bose: The buyer can file a case against a developer who has not started the project and collected funds without opening an escrow account.

Yamalova: Investors can file a criminal case against a developer on the basis that it has not started a project and/or opened an escrow account, but only if the reason for the developer's default is criminal in nature and there is evidence to prove it.

Misrepresentation and cheating are some examples of criminal acts under the UAE civil code. Similarly, under Dubai Law 8 (escrow law), criminal sanctions will be imposed where a developer either: 1)"knowingly offers to sell units in bogus property development" or 2) "embezzles, uses or squanders payments delivered to him for the purposes of construction of property developments, and misappropriates such sums."

For a case to be considered criminal there has to be undisputed or clear evidence to that effect, sufficient to convince the public prosecutor. Thus, for example, if there is a written statement from a developer himself admitting that he had never had any right to the property, but yet represented to the public otherwise, such written evidence may be sufficient.

More often than not such evidence does not exist, at least at the outset. Instead, further investigations must be conducted. This arises in cases where a contract is at issue, therefore, necessitating contract interpretation. In such cases, a public prosecutor will transfer the case to the Civil Court. At that point, the Civil Court will lodge an investigation, often by hiring an expert, to determine the nature of the claim. If at any point in the process, the court finds a developer's conduct was of a criminal nature, it will transfer the case back to the prosecutor.

Today, many investors try to file criminal cases first, mainly to use as leverage. Increasingly, however, the public prosecutor transfers such cases to the Civil Court. At that point, investors have to start from ground zero again.

Fuhr: Yes, investors might be able to file a criminal case against the developer for fraud and embezzlement. Furthermore, for Dubai, the escrow account law (Art 16 Law No8, 2007) provides a catalogue of elements of offences that justify a fine of no less than Dh100,000 or penalties of incarceration to anyone who, for example, embezzles, uses and squanders payment delivered to him for the purposes of construction of property developments and misappropriates such payments. Another offence according to the escrow account law is to carry on property development business without a licence.

Sayed: This depends on the location of the development and the actions of the developer. In general, unless executives of the developer have committed clear criminal acts, it is unlikely that a criminal case would be taken up by the police/public prosecutor. It should be noted that not all emirates have escrow laws and certain emirates have its own process for dealing with developers that are alleged to have delayed a project or failed to establish an escrow account. For example, in Dubai, Law No8 of 2007 concerning escrow accounts of real estate developments in the emirate of Dubai (escrow law) deals with escrow accounts for real estate projects located in Dubai. Article 7 of the Escrow Law requires an escrow account to be established for each project; however, in practice there are exceptions. Two other emirates in the UAE have laws similar to the escrow law, Umm Al Quwain Law No3 of 2007 in respect of security accounts of real estate (security account law) and Ajman Emiri Decree No12 of 2008 amending Emiri Decree No8 of 2008 (Decree No12). Together the escrow

law, the security account law and Decree No12 (the escrow account laws) contain similar principles and themes.

In the case of the escrow account laws, penalties are set out that allow the respective competent authorities in the relevant emirates to levy fines and/or seek an order for terms of imprisonment against those who breach these laws. If there has been a violation by any party of the escrow account laws then without prejudice to any punishments stipulated by other legislation [for example the civil code or the penal code], fines and/or imprisonment may be imposed. Such breaches cover a wide range of issues, including embezzlement or use without justification of funds collected for the construction of real estate projects.

So far as we are aware no other emirates in the UAE currently operate laws similar to the escrow account laws, although we understand that Abu Dhabi is close to issuing one. Accordingly, in other emirates, the use to which the developer can put funds paid in respect of off-plan properties will be governed by the particulars of the agreements between the parties and general principles of law. If the agreement has no restriction on the use to which the developer can put funds paid as a deposit, then the developer may argue it is able to use those funds for any corporate purposes and the purchaser's remedies lie in general breach of contract if as a result of that action the development project is not delivered within the time frames specified in the agreement.

It is also worth noting that in addition, Article 404 of Federal law No3 of 1987 (Penal Code) generally makes it a criminal offence for a party who has been given funds on trust for a certain purpose to use those funds for another purpose, which could be a breach of trust or fraud and there are a range of criminal penalties for breaching the Penal Code. The ability to sustain a claim under the Penal Code, however, will be dependent on whether it was clear from the agreement that the specific funds paid by the purchasers were to be used solely for the development or whether they would constitute the general funds of the developer and subsequently the developer could substitute or replace those funds. Please note that delays concerning real estate projects are usually a breach of contract issue.

Is it advisable for people/investors to group together and file cases against a developer? Does such a move help them?

Mithani: While it is possible for investors to group together and file a complaint with the regulatory agency, it is not possible to bring class action in the UAE Courts. This contrasts to jurisdictions such as the US where class actions are a common feature of the legal landscape.

Bose: Such a grouping may help the regulatory agency to handle disputes collectively rather than addressing it one by one. Investors may benefit as they can appoint a law firm to represent them before the authority and in the courts if needed.

Yamalova: Investors acting in concert against the same developer are very effective. There are limitations, however, as to in what capacity they can group together.

For example, for the purposes of bringing a legal action in a UAE court, such collective actions are not allowed. In other words, class action suits are not within the purview of the UAE legal system, as far as courts are concerned. Therefore, investors have to file individual lawsuits.

However, tremendous economies of scale can be achieved in the due diligence necessary and/or helpful to litigate a case. For example, investors can collectively hire one law firm and/or experts to gather the factual evidence to be used in the case and share the expense accordingly. Similarly, they can collect and share research and knowledge among themselves. Also, not to be underestimated is the leverage groups of investors gain on the developer, Rera/Land Department, courts and the like. Their collective voice is much louder and, therefore, harder to ignore. Also the safety in numbers principle encourages greater number of people to come together. Finally, investor groups take teeth out of developers' attempt to set individual investor apart from all of the other investors as being the only one in default.

Another benefit of investors coming together is that certain judicial forums allow consolidation of claimants and claims. For example, Dubai International Arbitration Centre (DIAC) and Dubai International Financial Centre (DIFC) allow for class action suits. Therefore, those investors whose contracts provide for either arbitration or DIFC court will have an additional benefit in joining forces.

Fuhr: Investors can group up and file a complaint with the regulatory authority asking to cancel the project. The more the majority of investors in a project signing the complaint, the more likely their complaint will be heard. Unfortunately if the investors decide to approach a court they will have to file each case [meaning each single sales and purchase agreement] separately, which means court fees and lawyer fees for each case.

Sayed: The general legal consensus is that the current UAE legal framework does not support class actions in the sense prevalent in, for instance, the US legal system, except in certain types of labour matter. As a result, to the extent investors are in touch and have disputes involving the same developer, they might approach real estate regulators on a collective basis to relay common concerns. In Dubai, one should approach Rera, and in Ajman, Arra. Groups often form by use of website forums or blogs, or by reference to a large law firm which acts against developers. Pressure in numbers and concern about adverse publicity would often make the real estate regulator look more closely at investors concerns. Although we have seen some levels of activity by real estate regulators where there are issues of developer compliance with regulations, directives and policies, if the matter of concern is a contractual dispute, this is usually referred to the courts or arbitration bodies in accordance with UAE laws and applicable contracts.

Should a dispute reach the courts, an investor owning numerous units in the same project, may file one case against the developer. However, the Dubai Courts usually require an individual investor with more than one unit in the same real estate project, to pay separate court fees for each unit particularly where the investor holds separate sale and purchase agreements for each of the units. Consolidation of cases where arbitration clauses apply is similarly complicated. In the case of court action, separate investors can only come together and file one case against the developer if all the investors are party to one single sale and purchase agreement, a situation that is uncommon.

How much cost benefit does such a move offer?

Mithani: If the law as amended to allow parties to bring class actions, it would offer significant benefits not only to individual litigants but also to the administration of justice. First, it offers the advantage, particularly in a legal system where there is no system of binding legal precedent, that consistent decisions will be reached in cases against a particular developer involving the same issues, such as delay in construction. Second, it offers costs savings to both claimants and defendants. This has particular relevance in a situation where there may be an inequality of resources between the parties, as there may be between a large developer and a number of small investors. If the investors have the option of pooling their claims, there is a greater chance of them being on a level playing field.

On the law as it stands there is nothing to prevent a group of investors from instructing a single lawyer, which may result in some costs

savings and may provide them with greater leverage but each case will be dealt with separately by the courts. The costs savings will be less than if the law permitted class actions.

Bose: Such a move is cost-effective for the following reasons: they can be represented by one person, preferably a lawyer specialised in property laws, rather than spending money and time individually; they can appoint one lawyer so that a reduced fee may be possible.

Yamalova: Collective efforts by investors provide enormous cost benefit. First, as far as legal and expert fees are concerned, they can share the expense. Second, any costs incurred in gathering due diligence to litigate a case can be also split across the board. Even bigger cost benefit could be achieved if, because of their collective force, investors work out a settlement with the developer without going to court.

Fuhr: There are no cost benefits since filing a complaint with regulatory agency is free of charge.

Sayed: As discussed above, group court actions are not currently supported by the UAE legal system. However, legal costs can be reduced by investors in common projects appointing the same law firm and joint approaches being made to the developer and the real estate regulators. It should be noted that the real estate regulators in Ajman and Dubai have the capacity to approve and cancel real estate projects in their respective emirate. For instance, Article 5 of Dubai Law No9 of 2009 provides that "the agency [Rera] may, following a grounded report, cancel a real estate project, in which case the developer must return to the purchasers all the amounts paid by them in accordance with Law No8 of 2007 [the escrow law]". Accordingly, it would seem that pressure from investor groups would encourage real estate regulators to investigate disputed projects especially where insubstantial progress has been made over an extended period of time. Notwithstanding this power, there has not yet been any officially published decision of the cancellation of a project in such circumstances by real estate regulators based on investor pressure. It is likely, however, that a number of projects must be candidates for such action.

Investor groups should also consider jointly approaching UAE law firms to receive generic legal advice regarding a particular real estate project. Although court fees would be payable per case file, investors could seek to reduce legal fees by filing similar statements of claim in front of the court and thus achieving economies of scale. It should be noted cases can differ from one individual case to another even in the same project, for instance due to different contracts, facts and investment timing.

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