

Dubai mortgage law: much ado about nothing



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IN EARLY JANUARY 2010, THE MEDIA WAS full of headlines about a landmark verdict and Dubai's first foreclosure, which was supposed to 'open the floodgates' for other similar actions.

The orders for foreclosure were issued by a Dubai enforcement judge in favour of Barclays Bank plc in its case against various borrowers who had taken mortgages on their real estate assets with Barclays.¹ The orders were based on Dubai Law No 14 of 2008 (Law No 14), which relates to mortgages in Dubai.

The orders puzzled commentators (mainly those with a common law background), who went to great lengths in trying to justify the measures taken by the judge and cautioned against the lack of court precedents in the UAE civil law system.

Almost a year later, the floodgates remain closed and the orders look rather isolated in the Dubai judicial scene. In light of this, it is worth examining whether the orders were actually landmark verdicts and foreclosure actions.

CIVIL CODE

Lenders in the UAE are currently prohibited from owning directly distressed assets under Article 1420 of Federal Law No 5 of 1985 (the Civil Code), which relates to civil transactions. The Civil Code provides that:

'If it is a condition of the mortgage agreement that the ownership of the asset be vested in the lender in consideration for its loan in the event that the borrower does not pay at maturity, or if there is a condition that the mortgaged asset is to be sold regardless of the legal procedures to be followed, the mortgage shall be valid but such condition shall be void.

Such condition shall also be void even if it is provided in a subsequent agreement.'

The prohibition of lenders directly owning distressed assets is derived from elements of historic French law, specifically '*prohibition du pacte comissoire*'. (Although no legal texts explicitly prohibited a *pacte comissoire* relating to real estate assets, the prohibition did apply to moveable assets).

Article 1419 of the UAE Civil Code provides that a lender may satisfy its debt out of the mortgaged asset on maturity date in accordance with the rank it holds, after following certain procedures, including those provided for in the UAE Civil Procedure Code (the Civil Procedure Code).

The obligation for the lender to have recourse to the courts to satisfy its debt and not reach an out-of-court settlement on the security registered on a mortgaged property is called *prohibition de la clause de voie parée*.

This principle is derived from French laws that influence both Egyptian and UAE law. The prominent Egyptian scholar Abdul Razzaq Al Sanhoury and the overwhelming majority of French scholars reason that such prohibitions are in the public interest because borrowers are in a much weaker positions than lenders. The reasoning for this protection is that lenders may impose any conditions that they choose on borrowers and unduly deprive them of all of their assets.

In addition to these prohibitions protecting borrowers, scholars explain that entitling the lenders to own mortgaged assets would be contrary to the purpose of the mortgage itself, which is to grant the lender a right over the value of the asset and not over the asset itself.

Are such prohibitions still valid? Arguably, they are not because banks and lending institutions are tightly controlled by bodies such as the Central Bank and other regulatory agencies, meaning that borrowers are protected and no longer in the weak position that they were when the prohibition was enacted.

In March 2006 these considerations prompted the French legislature to amend the country's civil code to allow lenders to

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NOTE

- 1) Order dated 23 December 2009 by the Dubai enforcement judge in case no 85/2009. Barclays had also submitted cases no 86 and 87 before the same judge.

acquire mortgaged real estate properties (apart from the borrowers' main residence and certain other exceptions). This move was designed to encourage consumption by allowing banks to lend more easily.

Did Dubai follow suit by modernising with Law No 14? Could such a law issued by the Emirate of Dubai contravene the provisions of the Civil Code? Under UAE constitutional provisions, individual emirates cannot single-handedly amend federal laws.

Having looked at Law No 14 more thoroughly, which is based on the Civil Code (among other pieces of legislation), it is arguable that there is no actual contravention of federal law and, more specifically, of the provisions of the Civil Code, but rather it was a subtle interpretation of such provisions that allowed the so-called landmark verdicts.

Article 25 of Law No 14 provides that:

'Upon default in payment of the debt when mature or upon fulfillment of a condition granting early repayment

status, the mortgagee/creditor or his universal or singular successor must provide the debtor or the person in possession of the mortgaged property 30 days' notice through the Notary Public before commencing enforcement proceedings.'

Article 26 provides that:

'If the mortgagor/debtor or his universal or singular successor or the guarantor *in rem* fails to pay the mortgagee within the period specified in the preceding Article, the enforcement Judge shall, upon request of the mortgagee/creditor, order an attachment against the mortgaged property so that it can be sold by public auction in accordance with the applicable procedures of the Department [the Dubai Land Registry].'

The argument that there was no contravention of federal law is reinforced by the fact that Article 225 of the Civil Procedure Code provides for an enumeration of the enforcement deeds that include 'legally registered and authenticated instruments'.

This definition could very well apply to mortgage deeds as these documents have to be legally registered and authenticated by the Dubai Land Department (see Article 1400 of the Civil Code).

CONCLUSION

On close examination, Article 1419 of the Civil Code does not explicitly provide for a lawsuit on the merits before enforcing the mortgage deed, but merely refers to 'the measures provided in the UAE Civil Procedure Code', which are mainly procedures relating to sale by public auction.

Therefore, the Dubai enforcement judge was merely following the relevant federal and local legislation when he issued the orders for foreclosure. The reports of landmark verdicts and Dubai's first foreclosure have proven to be false, since no amendment was made to the relevant legislation to allow any actual foreclosure.

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