

# Managed and serviced apartments in Dubai Considerations from a Jointly Owned Property (Strata) and Hotel Operation perspective

Katrine Kofoed

k.kofoed@tamimi.com

Other names used for similar or related concepts are “Residences” and “Branded Apartments”. Generally the concept of MSA, Residences or Branded Apartments will contain the following features:

1. The Building will be of a higher quality.
2. Commonly the MSA, Residences or Branded Apartments may sit along side a singly owned Hotel development.
3. The offer of the Units by Owners for short term accommodation services is often a feature.
4. In all cases, the development is branded and both Owners resident in the development and any tenants or guests will be entitled to benefit from a range of services provided by the Hotel Operator or arranged by the Owners Association. A list of such Ameliorated Services is set down in Part C – Commercial and Practical Considerations in Structuring MSA schemes (“Ameliorated Services”).

In this article we explore the legal backdrop to the concept of MSA. It should be noted that this article does not purport to comment on the licensing requirements of the Dubai Economic Department or Dubai Tourism Commerce and Marketing

The simple description above of a MSA scheme belies what is in fact a relatively complex legal and commercial arrangement with many potential variations possible.

We consider in more detail below, the nature of MSA schemes under the following topics:

- A. The Legal Entities involved in providing MSA.
- B. The Relevant Legal Documentation.
- C. Commercial and Practical Considerations in Structuring MSA Schemes.
- D. Regulatory and other Issues Arising.

## **A) The Legal Entities involved in providing MSA**

In theoretical terms, once the development is complete the management of the “Common Areas” and general administration of the development should pass to the Owners Association formed pursuant to Law No 27 of 2007 on Ownership of Jointly Owned Properties in the Emirate of Dubai (“JOP Law”) and regulated pursuant to RERA’s “Directions” to the JOP Law.

The investors become the Owners of the Units. By virtue of their ownership, Owners are members of the Owners Association, are entitled to vote at meetings of the General Assembly and be elected as Board members of the Owners Association.

If therefore the developer wants to ensure that there is the ability for a Hotel Operator to operate from the

development, this will have to be procured by a contract with the Owners Association.

The Owners of the Units will also need to enter into their own private arrangement with the Hotel Operator for the rental of their Unit, should they wish to use the Rental Pool.

## **B) The Legal Documentation**

The principal document relevant to the creation of a MSA scheme is the Sale and Purchase Agreement (“SPA”), between the developer and investors. Ideally, the SPA should fully disclose or make sufficient reference to the documents set out and discussed below:

1. The constitutional document pursuant to the JOP Laws and Directions is known as the Jointly Owned Property Declaration. This document needs to set out clearly the role of Hold Co (discussed below) and the Hotel Operator.
2. The Hotel Operator will need to have the right to provide the Ameliorated Services, as well as operate the Rental Pool and provide various other branding and consulting services. In addition, the Owners Association may need to be compelled to provide certain Ameliorated Services. These aspects are normally dealt with in a framework agreement which, for the purposes of this Article, we will call the “MSA Framework Agreement”. This MSA Framework Agreement is not to be confused with (though may incorporate features of) an association manager’s agreement or facilities management agreements (see the table in Part C which sets out the various services).
3. Hotel Operators are normally appointed pursuant to separate operational and technical services agreements between the Hotel Owner and the Hotel Operator.
4. If the MSA development sits alongside part of a Hotel development, the developer may wish to ensure that the Owner of the Hotel has the right to also remove the Hotel Operator from the development comprising the Branded Apartments.
5. Therefore, the developer would need to ensure that the Hotel Operator did not have the MSA Framework Agreement directly with the Owners Association. Accordingly, the developer should set up a holding company (“Hold Co”) to enter into the MSA Framework Agreement and then create a separate operational and technical services agreements (on a back to back basis) with the Hotel Operator (“Operator Agreements”) in relation to the Branded Apartments.
6. Without the use of Hold Co, the Owners Association would have a contract directly with the Hotel Operator complicating the ability of the Hotel Owner to remove the Hotel Operator from the Branded Residences or the ability to assign the rights under the MSA Framework Agreement to any purchaser of the Hotel.
7. Unit Owners have jurisdiction over their Units and accordingly it is for them to enter into any arrangement with the Hotel Operator for the management of their Units. As the Hotel Operator will require rental stock to operate, a Rental Pool Agreement needs to be appended to the SPA, with the relevant investor’s agreement to enter into this. As for the MSA Framework Agreement referred to above, it may be more appropriate that the Rental Pool Agreement be between Hold Co and the investors, though operationally the Hotel Operator would be appointed (pursuant to the Operator Agreements) as Hold Co’s agent to enter into the Rental Pool Agreements and operate the Rental Pool.

The Rental Pool Agreement will generally entitle the Hotel Operator or Hold Co (as the case may be) to manage the Unit for a fee. The obligations on the Hotel Operator or Hold Co would generally include; arranging tenants and occupiers, maintaining the Unit, paying all outgoings in relation to the Unit and paying the balance of the revenues to the Unit Owner.

Whilst it may be possible to design the MSA scheme independently of the Hotel Operator and endeavour to incorporate the necessary flexibility to adapt to the requirements of any Hotel Operator, generally such schemes are designed in tandem with the Hotel Operator at the conceptual and design phases of the development.

The developer / Hold Co and the Hotel Operator would also enter into the Operating Agreements relating

to the Hotel and/or MSAs. It is important in doing this that any commercial considerations in such documents are also carried down through the documents referred to in 1 to 6 above in so far as they relate to or in any way impact on the legal entities referred to.

### C) Commercial and Practical Considerations in establishing a MSA scheme

Considerable effort and consideration needs to be put into MSA schemes to ensure that they meet the expectations of investors and the Hotel Operator without conflict, and with clarity on the structuring. It is important to remember that not all of the investors may want their Units to form part of the Rental Pool, and some investors may want to actually reside in the development.

For resident Owners, they may not want many of the services that the Hotel Operator provides as mandatory and for which they have to pay for. They may nonetheless be happy to pay for some services on a "User Pays" basis.

For other investors, there can be the inclination to see any Ameliorated Services as being the obligation of the Hotel Operator (as they are operating a business from the Common Areas of the development and profit from same), and therefore the costs should be met out of the Hotel revenues. Accordingly the exact service, cost and revenue matrix needs to be developed and investors made aware of same.

We consider, in simple terms, the services to be offered in relation to a development comprising MSA fall into the categories set down in the table below.

<b>Association Management Services (a service to the Owners Association ("OA")).</b>	<b>Contracted Services (facilities management) provided in relation to Common Areas.</b>	<b>Ameliorated Services (a la carte and other similar hotel type services)</b>
<ul style="list-style-type: none"> <li>• Working with OA Board to develop strategies for management of common areas;</li> <li>• Preparing annual budgets;</li> <li>• Negotiating supply contracts;</li> <li>• Supervising contractors;</li> <li>• Attending to day-to-day operational matters and correspondence;</li> <li>• Implementing decisions of OA and Board;</li> <li>• Keeping books and records as required by law;</li> <li>• Supervising defect repairs and warranty claims;</li> <li>• Coordinating insurances and insurance claims;</li> <li>• Issuing service charge notices and collecting payments;</li> <li>• Facilitate submission of technical, financial and management reports to Board and OA;</li> <li>• Dealing with complaints from Owners;</li> <li>• Coordinating and attending Board and General Assembly meetings, sending notices of meetings and maintaining minutes;</li> <li>• Follow up on legal matters on behalf of OA;</li> <li>• Representing OA with governmental and quasi- governmental entities.</li> </ul>	<ul style="list-style-type: none"> <li>• HVAC plant and equipment;</li> <li>• Electrical Systems;</li> <li>• Plumbing Systems</li> <li>• Minor Civil Works;</li> <li>• Uninterrupted Power Supply;</li> <li>• Pressurization systems;</li> <li>• General Building Supervision;</li> <li>• Maintenance of swimming pool;</li> <li>• Water tank maintenance and cleaning;</li> <li>• Lifts and Elevators;</li> <li>• Cleaning;</li> <li>• Security Services;</li> <li>• Pest control services;</li> <li>• Gardening;</li> <li>• Painting and decorating of Common Areas;</li> <li>• Repairs and maintenance of Common Areas;</li> <li>• Audit;</li> <li>• Valuations;</li> <li>• Architectural and engineering consulting;</li> <li>• Reserve Fund Studies;</li> <li>• Legal Services;</li> <li>• Design assistance.</li> </ul>	<ul style="list-style-type: none"> <li>• The Rental Pool including a booking service and property management services;</li> <li>• Housekeeping and cleaning services;</li> <li>• Arranging linen services;</li> <li>• Additional security control;</li> <li>• Childcare services;</li> <li>• Property maintenance services and repairs;</li> <li>• A mini bar service;</li> <li>• A food and beverage service;</li> <li>• The use of specialist Club facilities</li> <li>• A valet service;</li> <li>• Porterage services;</li> <li>• Bellboys;</li> <li>• Full time reception;</li> <li>• Full time caretaker;</li> <li>• Services including towels, chairs, umbrellas and related services and equipment.</li> </ul>

Note: services specifically related to Units in the Rental Pool are excluded from consideration in the table

as any costs associated with such Units would be for the Owner of that Unit under the Rental Pool Agreement. If the costs of providing services in relation to such Units formed part of the budget for the Owners Association this would severely prejudice those Owners who chose not to put their Units into the Rental Pool. It is the case however, that services in relation to the Units are covered in the Rental Pool Agreement, it being a private arrangement between the Unit Owner and Hold Co/the Hotel Operator and the costs of the same are deducted from the revenues obtained from letting out the Unit.

The Association Management Services are clearly a cost of the Owners Association and would be budgeted for and paid for by Owners through their payment of Service Charges. Likewise the Contracted Services would ordinarily be contracted for by the Owners Association in the same fashion.

The controversial category (should we take the view of the cost conscious resident Owner) will be the Ameliorated Services. Some of these may be able to be provided on a "User Pays" basis, such as the putting of a Unit into the Rental Pool or Unit maintenance services. If this is the case those "User Pays" services would ordinarily be removed from the Owners Association budget. Some Ameliorated Services may however be less easily categorized as "User Pays". Take for example "Reception" services and "Bell Boy" services which may be used by all Owners and occupiers and not just guests to the Rental Pool. In such cases it needs to be clear whether the Hotel meets the costs of the same or the services are procured by the Owners Association and paid by Owners through their payment of Service Charges.

Another potentially problematic aspect of MSA, is that the Hotel Operator may also want to control the nature of the services offered to the Owners Association by service providers and choose service providers to ensure that it can meet its Brand Standards. Sometimes the Hotel Operator may want to provide services itself and in such circumstances there may need to be a process to benchmark and apportion costs.

Careful consideration from both a legal and commercial perspective needs to be given to the issues raised in this Part C and it is suggested that appropriate disclosure of the arrangements may reduce the potential for disputes with Owners or the Owners Association at a later date.

#### **D) Regulatory and other Issues Arising**

Readers may appreciate that a MSA scheme is a more complicated ownership arrangement than simply owning an apartment in a building which is nonetheless regulated pursuant to the JOP Laws and Directions.

It should be emphasized furthermore that if developers could bind the Owners Association to long term contracts this could seriously undermine the freehold nature of the investment.

MSA arrangements are not surprisingly therefore regulated in the Directions. In particular the following provisions of the Directions may apply should RERA determine:

1. Restrictions on the length of all Supply Agreements (of which the MSA Framework Agreement would be one) with the Owners Association to no more than 3 years.
2. Article 17 of the Direction for General Regulation ensuring that the content of all Supply Agreements are fair, clear and have appropriate mechanisms ensuring quality.
3. Article 34 of the Direction for General Regulation which may restrict the ability of the Developer to enter into Supply Agreements on behalf of the Owners Association.

#### **In addition it is likely that RERA may require:**

1. An Association Manager, registered with the Dubai Economic Department and RERA, to be appointed to perform the various statutory association management services set down in the Direction for Association Constitution and as summarised above in Part C.
2. The Management Agreement be registered with RERA in accordance with Article 17(1)(d) of the Direction for General Regulation.

It is probable that RERA may exercise its discretion as above, having regard to the fairness of the scheme overall on Owners. In addition it is very likely that RERA may also consider, in exercising its discretion, the extent to which the developer has complied with the disclosure regime set down in the Direction for General Regulation and therefore the extent to which the investor appreciated the nature of the scheme into which he was investing.

The above represents an overview of a managed and serviced apartment scheme in the context of Dubai regulation to date. As mentioned this Article does not deal with licensing considerations.