

Real Estate and Housing Developers' Association Malaysia (REHDA)

Section A

The Revenue ED essentially sets out the following criteria for revenue recognition:

Para 25: An entity shall recognize revenue when it satisfies a performance obligation by transferring a promised good or service to a customer. A good or service is transferred when the customer obtains control of that good or service.

Para 26: A customer obtains control of a good or service when the customer has the ability to direct the use of and receive the benefit from the good or service. Control includes the ability to prevent other entities from directing the use of or receiving the benefit from a good or service

Para 27: The customer's ability to receive the benefit from an asset refers to its present right to obtain substantially all the potential cash flows from that asset directly or indirectly such as by using, consuming, selling, pledging or holding the asset

Para 28: If an entity retains some rights to an asset solely as protection against the customer's failure to comply with the terms of the contract (for example legal title as protection agst the customer's failure to pay) those rights are protective rights and do not preclude a customer from obtaining control of an asset.

Para 30: When the promised goods / services underlying a separate performance obligation are transferred to a customer continuously, an entity shall apply to that performance obligation one revenue recognition method that best depicts the transfer of goods or services to the customer. (In REHDA's view this would of course be the POC method)

The essential difference between the current standards and the Revenue ED appears to be one of emphasis. The old one focuses on what the seller has given up whilst the new appears to be emphasizing what has been obtained by the customer. In the case of real estate, can't really see much difference either way!

Main bone of contention is this – in developed countries the mode of operation appears to be effectively Build then Sell where largely the risks and rewards / effective control over the property only pass to the buyer upon handover. This has tended to skew the international community (IASB is UK-based) towards a preference for the completion method.

Malaysia however is truly on a Sell then Build model where the buyer, upon signing the SPA assumes much of the keys risks and rewards of property ownership (whilst the new standard speaks of control, the way in which it is defined appears to refer to the customer having obtained effective / beneficial ownership rights).

Section B

Purpose of the table is therefore to demonstrate key comparisons btw Malaysia / Aust / UK in order to persuade the IASB that they really should consider the different needs and economic realities prevailing in developing vs developed markets and not insist on a one-size-fits-all approach.

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Characteristics of off-plan sales in Malaysia vs Australia & the UK

(Based on Schedule G&H agreements for landed and strata residential properties – these are standard form agreements regulated by the Malaysian Ministry of Housing (“MOH”) which have to be used for all multi-unit residential developments and are legislated agreements being schedules to the Housing Development (Control & Licensing) Act 1966 of Malaysia)

Malaysia	Australia	United Kingdom
<p><u>A) Developer’s right to utilize progress payments</u></p> <p>Upon signing Buyer pays 10% deposit which goes directly to the Developer.</p> <p>Thereafter payment is made progressively in instalments (ranging from 5% - 15% of the purchase price) according to the stage works completed by the Developer based on a certification by the architect in charge of the project as proof that the work has been completed.</p> <p>All payments by the buyer are deposited into a housing development account regulated by the MOH which, subject to certain conditions, the Developer may utilize during the construction phase to fund the development. (i.e. the development is effectively buyer-financed)</p>	<p>There are minor variations from State to State but generally Developers do not have the right to utilize any payments by purchasers. Usually only 10% is paid as deposit and no further progress payments are permitted. The balance of 90% is only paid by Buyers at completion of the development.</p> <p>Further, pursuant to the Sale of Land Act 1958 (Vic), the deposit of 10% (and no more than 10% is currently permitted) must be held by the Developer’s lawyers trust account and the Developer has no access to these deposit funds until completion of construction/development which are certified by independent bodies.</p> <p>The Developer is required to fund the construction either from its own funds or through debt funding.</p>	<p>Generally speaking, in UK, purchasers of off plan property pay between 5% and 20% by way of a deposit. Unlike in Australia, there is no legislation restricting it to 10% but the normal practice is 10%.</p> <p>There is no general rule as far as using the deposit is concerned. In some cases it is paid to the developer's solicitor as stakeholder, sometimes as 'agent', which allows the developer to then use it to help funding and sometimes direct to the builder. That represents a risk but usually this is where the project is backed by a scheme that guarantees the return of the deposit if the builder goes bust (e.g. a National House Building Council accredited scheme), so the risk is mitigated.</p>
<p><u>B) Buyer’s right to prevent further dealings by Developer</u></p> <p>Immediately after the SPA has been executed:</p> <ul style="list-style-type: none"> the Developer is not permitted to encumber the Land without the prior approval of the Buyer If the Land is already encumbered the Developer is required to secure an undertaking from its financier to disclaim its interest over the unit sold in exchange for the payment of a redemption sum which the Buyer is authorized to pay directly to the Developer’s financier 	<p>The Buyer does not have any rights to prevent further dealings by the Developer of the property sold other than preventing the Developer from selling the property sold to another person.</p> <p>The Developer has the right to provide securities on the property (such as a mortgage) to funders for the construction loan as well as proceed to arrange subdivision and strata titles.</p>	<p>Similar to Australia</p>
<p><u>C) Buyer’s right to deal with the Property</u></p> <p>Upon signing the SPA any upside / downside in the property value belongs solely to the Buyer not the Developer</p> <p>The Buyer has a right to assign the property purchased under the SPA to obtain a loan to fund his purchase of the property.</p> <p>The Buyer also has a right to caveat the Land to protect his interests over the property purchased and prevent any further dealings by the Developer over the property sold.</p> <p>In addition, upon either:</p> <ul style="list-style-type: none"> payment of the full purchase price or prior to payment of the full purchase price, the receipt by the Developer of an undertaking from the Buyer’s financier to pay the balance purchase price <p>the Buyer may assign all his rights, interest and title in and to the property to third parties (<i>not just its financier</i>) <u>without the consent of the Developer</u>.</p>	<p>While any upside or downside of property value belongs to the Buyer upon signing of the SPA, this is conditional upon the Buyer completing the purchase with the Developer upon completion of the construction/development. The Buyer’s rights to deal with the property are also extremely limited.</p> <p>It is also prudent practice in Australia by Developers to prevent the Buyer’s right to caveat the land as this will delay subdivision and strata titling.</p> <p>While Buyers can certainly on sell their property prior to completion, this is usually prevented by Developers by contractual rights. Basically, even if this is permitted by the Developer, the Purchaser must still complete the purchase with the Developer first with a simultaneous settlement with the new purchaser (ie: 2 separate transactions). The relevant State Revenue Office also views this as 2 separate transactions for stamp duty purposes.</p>	<p>Similar to Australia although this is more governed by contractual rights between the parties whereby the Buyer is restricted from doing many things such as on-selling or assigning without consent of the Developer or if Buyer is permitted to do so, there are terms and conditions such as the price cannot be less than the developer’s price or only after all the developer’s units have been sold, etc.</p>

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Malaysia	Australia	United Kingdom
<p><u>D) SPA effectively non-cancellable</u></p> <p>The Developer has the right (not obligation) to terminate the SPA in the event of breach (essentially non-payment) by the Buyer. If the Developer decides to terminate the SPA the Buyer loses 10% or 20% of the purchase price as agreed damages to the Developer.</p> <p>There is however no express provision made for the Buyer to terminate the SPA. The Buyer's rights in the event of liquidation of the Developer are discussed in E) below.</p> <p>Both parties have the right of specific performance against the other.</p>	<p>Both parties have the right to terminate the SPA if certain acts are not done by the Developer by a sunset date. As such, the risks lies with the Developer to ensure these acts are undertaken within the specified time. These acts include:</p> <ul style="list-style-type: none"> - completion of construction to enable Occupancy Permit to be issued - registration of subdivision plan at Land Registry with new titles issued <p>In the event of termination, the 10% deposit is fully refundable to the Buyer</p>	<p>Similar to Australia. More often than not, the sunset date is extendable by reason of force majeure but if this is the case, there is usually an ultimate long stop date anyway.</p>
<p><u>E) Ownership of property in the event of liquidation of the Developer</u></p> <p>In the event of liquidation of the Developer, the creditors of the Developer do not have any rights to the property which has been sold to the buyer. The liquidator may only claim whatever amounts which have been billed to the buyer for work done but which remain unpaid.</p> <p>If the liquidator disposes of the incomplete development to a White Knight, the White Knight will have to buy the incomplete development subject to the pre-existing beneficial interests of the Buyers. On the practical side the Buyers and White Knight would have to come to an agreement for the White Knight to either complete the construction of their uncompleted units or buy over their interests in the same.</p> <p>Secured creditors would also not have any claim over the Buyer's properties pursuant to the disclaimer required to be given pursuant to B) above.</p>	<p>In event of liquidation of Developer, the Buyer has very limited rights to the property.</p> <p>If the development doesn't proceed and as such, the receiver of the developer cannot complete the Contract for failure to carry out certain acts, then the Contracts are terminated and the deposit of 10% fully refundable to the Buyer.</p> <p>If there is a White Knight, the White Knight does buy the development subject to the pre-existing beneficial interests of the Buyers but the White Knight steps into the shoes of the developer and carries the risk to complete the development by the sunset date or face the possible termination of the Contracts resulting in full refund of deposit to the Buyers.</p>	<p>Similar to Australia.</p>

The "Sell then Build" model adopted in Malaysia has been criticized by some quarters for the amount of downside risks Buyers are exposed to especially in the event of Developers' failure.

However what critics fail to see is that it is precisely because a significant portion of the risks (along with the benefits) of property ownership has been assumed by a large and dispersed pool of Buyers and their mortgage-financiers during the construction phase that the housing industry in Malaysia has developed as quickly as it has. Given that the Buyer assumes such risks, this necessitates the upfront vesting of control over the ability to deal with the property in the Buyer or his financier. Over time Malaysian laws and regulatory oversight have both been tightened to improve buyer protection without changing the essence of the Sell then Build model described above.

An alternative model is the Build then Sell model (or a variant of that in which the Buyer pays 10% upfront and 90% only upon completion) which is common in developed countries. Whilst this would technically offer greater buyer protection, it is not suitable for a developing nation such as Malaysia. This is because the concentration of credit risk on the Developer alone would increase not just funding cost but would also greatly reduce supply (due to a reduced number of "bankable" developers in the market). This would result in much higher housing prices which would not meet the needs of a developing nation seeking to promote affordable home ownership as one of its goals.