

Foreclosure of immovable property in Kazakhstan

by Mikhail Khlystov



A wave of foreign investments that swept through the Central Asian markets in the first decade of the twenty first century triggered a significant number of joint investment civil and industrial construction projects.

Many of these projects received foreign loan financing, which was secured by mortgaging the assets contributed by domestic partners to secure their obligations under the loan agreements. These assets usually included immovable property and parcels of land.

After the tide of investment receded, what was left was a number of preeminent projects that proved how successful the investments and the joint efforts of foreign and local partners were. However, other projects were less successful and the only thing foreign investors could do to save the rest of their investment was to undertake the foreclosure of the pledged property.

In this article we will examine the Kazakh system governing the foreclosure of immovable property that secured the obligations of local borrowers under loan agreements governed by foreign laws.

PLEDGE AGREEMENTS

The current laws of Kazakhstan provide certain requirements for a pledge agreement. Any failure to comply with such requirements will mean that the pledge agreement is at risk of being invalidated upon the claim of an interested party.

Such requirements include compliance with a written form, the prescription of provisions covering the valuation of the pledged property in the national currency, the name of the pledged property, and the nature, amount and term of the secured obligation.

When immovable property is pledged, the pledge agreement must be registered with the authorised body, which confirms this registration by making a certification statement on the agreement.

A foreign entity entering into the pledge agreement for the mortgage of immovable property located in Kazakhstan must obtain a business identification number by filing an application with the authorised local authority, which will issue the business identification number within three business days.

In most cases foreign investors insist on having the agreements governed by foreign law, putting them under the jurisdiction of foreign courts or arbitration. However, the current laws of Kazakhstan require that pledge agreements are governed by Kazakh law and are subject to the jurisdiction of the local public courts.

This does not prevent the execution of loan agreements secured by the mortgage of immovable property located in Kazakhstan in accordance with a foreign law. However, this option may lead to certain difficulties in the event of foreclosure, an issue that is addressed below.

MORTGAGE FORCLOSURE

The current laws of Kazakhstan provide for the judicial and extrajudicial foreclosure of pledged property. In both cases, the sale of property can only be done via a public auction.

Extrajudicial foreclosure is permitted when it is expressly provided for in the pledge agreement, whilst judicial foreclosure is an option in all other cases.

Extrajudicial foreclosure provides for the appointment of a trustee (a legal entity or a natural person) who acts on behalf of the pledgee under power-of-attorney. The trustee prepares a default notice, has it registered by the authorised body at the place of the pledged property and delivers the notice to the pledger.

If the borrower fails to remedy the breach of its obligations under the loan agreement or to comply with the default notice requirements within thirty days, the trustee will prepare a trade notice, have it registered at the place of the pledge agreement registration and deliver the notice to the pledger.

The next step provides for the publication of the auction announcement for a 10-day period prior to the auction.

Judicial foreclosure requires the claim for the foreclosure of pledged property to be taken to the public court at the place of the pledged property.

In rendering the judgment for judicial foreclosure the court shall fix the starting price, which may not be changed during the court judgment's enforcement procedure. The foreclosure process is implemented by the bailiff via a public auction.

Judicial and extrajudicial foreclosure allows the pledgee to take the pledged property at its estimated value if nobody else participates in the auction.

CASE LAW AND RECOMMENDATIONS

In most cases, both extrajudicial and judicial foreclosure of property involve actions brought by a pledger against a pledgee in the local courts.

Extrajudicial foreclosure is usually brought into dispute when the pledger receives a default notice and files a claim to the court for rendering the notice invalid and the foreclosure procedure premature. In such cases, the main arguments of the pledger usually include formal breaches of the foreclosure procedure as prescribed by the applicable laws and/or a lack of breach of the loan agreements secured by the mortgage of immovable property.

If the court finds that the default notice is invalid, the pledgee may send a new default notice to the pledger after the breaches set forth by the court have been remedied, or upon the default under the loan agreement if the court finds that the foreclosure of property is premature.

Public auction trades may also be challenged in the court by both the pledger and the debtor if they are formally different entities if they believe that the auction procedure prescribed by law has been violated.

Previous cases indicate that pledgees normally have to participate in several court proceedings because pledgers appeal on all possible grounds to challenge the actions of pledgees and trustees before the pledged property is finally foreclosed.

As for the judicial foreclosure of property, the initiation of the trial process in local courts usually enables the completion of the foreclosure process and resolves all potential issues in one court proceeding, although the actions of bailiffs may also give grounds for subsequent trials.

Claims for the foreclosure of pledged property must be paid in accordance with the court fees provided for by local law. The rate at which these claims must be paid is unclear as there is no such standardised practice so far.

In a number of cases, the court refused to try the case on the grounds that the claimant failed to pay the court fee at the rate calculated based on the value of the foreclosed property. The Supreme Court of the Republic of Kazakhstan recently stated that such claims must be paid at the fixed rate prescribed by local law.

Therefore, we may reasonably conclude that a single approach towards the assessment of court fees to be paid in foreclosure disputes has not been developed so far, and that local courts may still refuse to try the case until the court fee has been paid.

In addition, case law shows that the prejudicial foreclosure provisions prescribed in the pledge agreement shall not be prejudicial for judicial foreclosure. The local courts do not treat such provisions as a mandatory pre-judicial dispute settlement procedure, and opting for judicial or extrajudicial foreclosure remains at the complete discretion of the pledgee and makes the latter confident that a claim for judicial foreclosure will not be refused on the grounds that the pledgee failed to complete the extrajudicial foreclosure first.

Cases involving the foreclosure of property in Kazakhstan in which obligations are secured under loan agreements governed by foreign law lead to the longest and most complex trials. In such cases the pledgee must prove that payment obligations under the loan agreement are outstanding and that there are sufficient grounds for the foreclosure of the pledge. Case law shows that a foreign judgment or arbitral award and a foreign bailiff's statement confirming the non-payment of the granted sums may serve as sufficient evidence that the foreclosure of the pledge remains the only option for the pledgee to protect its rights against the non-payment of the debt.

Foreclosure processes involving a foreign-law governed loan agreement secured by mortgage of immovable property in Kazakhstan are very complex because they normally involve several litigation processes in different jurisdictions. In addition, local courts always require substantial evidence that obligations secured by the pledge are outstanding and that debt cannot be recovered by any means other than the foreclosure of the pledged property.

Executing loan agreements secured by mortgage of immovable property in Kazakhstan under Kazakh law, and ensuring that they are subject to the jurisdiction of the local courts, may help to extend the protection of investors' rights and ensure the smooth and prompt foreclosure of pledged property. Structuring secured loan transactions in this way will also enable debt and foreclosure claims to be tried in one proceeding, which will ultimately increase the chance of successful foreclosure.

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