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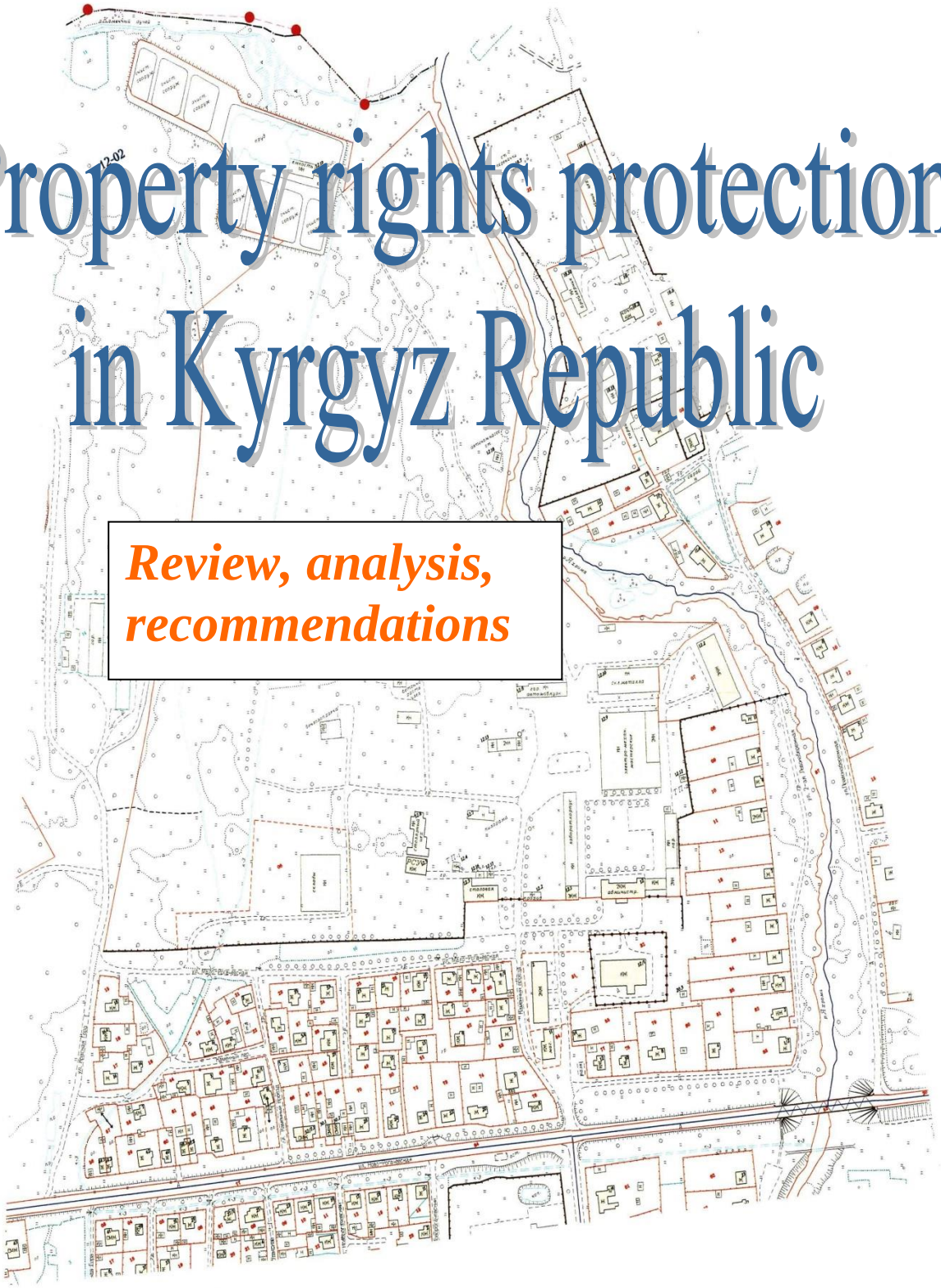
Property rights protection in Kyrgyz Republic



Review, analysis, recommendations

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Private property is the only guarantor of personal freedom.

Volter

I. INTRODUCTION

The International Business Council has conducted research into the condition of property rights for the purpose of defining problems that have a negative influence on the development of the investment and business climate in the Kyrgyz Republic. The primary goals of the survey were:

- identification of problems concerningthe protection of property rights
- development of recommendations and initiatives for IBC activity tp address the problems identified.

It is widely understood that property is the basis of economic systems. Forms of distribution, exchange and consumption derive from the nature of property ownership
In economic terms, property defines human relations on assignment and economic usage of all wealth. At the same time, the legal definition of property shows how the property communications which have developed in practice are enshrined and fixed in rules and regulations of the law, established by the state.

According to world practice, among various forms of property, private property appears as "the starting mechanism" of any market economy, the basic tool for the effective organization of business. In our country, as a result of an intensive privatization programme that took place at the beginning of 90's, the private sector share became dominating almost in every sector of our economy. Thus, by the end of 1998 the share of the private sector was: 87% in the industry, 97% in trade, 57% in construction, and 55% in transport. The share of the small-scale and medium-scale sector in GDP reached 46% in 2008. For the period January to October of 2009 the level of investments development into fixed capital due to all financing sources increased by 31,7% compared with the same period of the previous year. For the reporting period 28,3 billion soms was invested into fixed capital.[1] Therefore, special attention was paid to private property issues in this project.

The present review and analysis was made with the use of IBC quarterly research into the condition of the investment climate in our Republic, based on 10 basic and 20 other questions concerning the planning of investment in the Kyrgyz Republic. Questions on such topics as «The right to purchase, possession of the land and real chattels », and «Access to information on property rights and their restrictions» were evaluated by the investors and local businessmen as the most important.[2]

The preliminary questionnaire also confirmed the choice of the experts in selection of the basic directions of research – revealing protection problems of the private property in the field of tenure (buildings, facilities) and the land.

[1] Review of socio-economic development of the Kyrgyz Republic for January – October, 2009

[2] IBC surveys, 2005-2009

Considering the experience of earlier investigations, it is possible to confirm evidence of protection problems of private property in the Republic. We did not raise the issue of lack of confidence in security of property rights ahead of the surveys.

II . METHODOLOGY OF SURVEY. CASES.

The goals of the research were the gathering of information from groups of respondents, some statistical data, building the informational base of the IBC, and study of legal practice.

Sources of information:

- Legal bodies – IBC members;
- Legal bodies - members of other business associations;
- Workers of courts and judicial executors;
- Independent lawyers, experts;
- The data of National Statistical Committee of KR;
- The data of IBC quarterly researches;
- The data of some court orders.

Research problems:

- To define those kinds of the property which require greater protection;
- To establish the presence or absence of the existence of problems on property right protection;
- To reveal institutional problems with and obstacles to property right protection.

Using the survey method, the IBC attempted to identify those improvements in property right protection that businesses believe to be most important.

With this purpose, the IBC held two surveys among its members.

The first survey helped identify types of property that appear to be in the greatest need of protection, as well as the reasons for the current low level of protection of proprietors' rights in these areas.

According to the survey participants,

Types of property that are in the greatest need of protection are:

- Immovable property;
- Intellectual property;
- Securities.

Problems of property rights protection are related primarily to the:

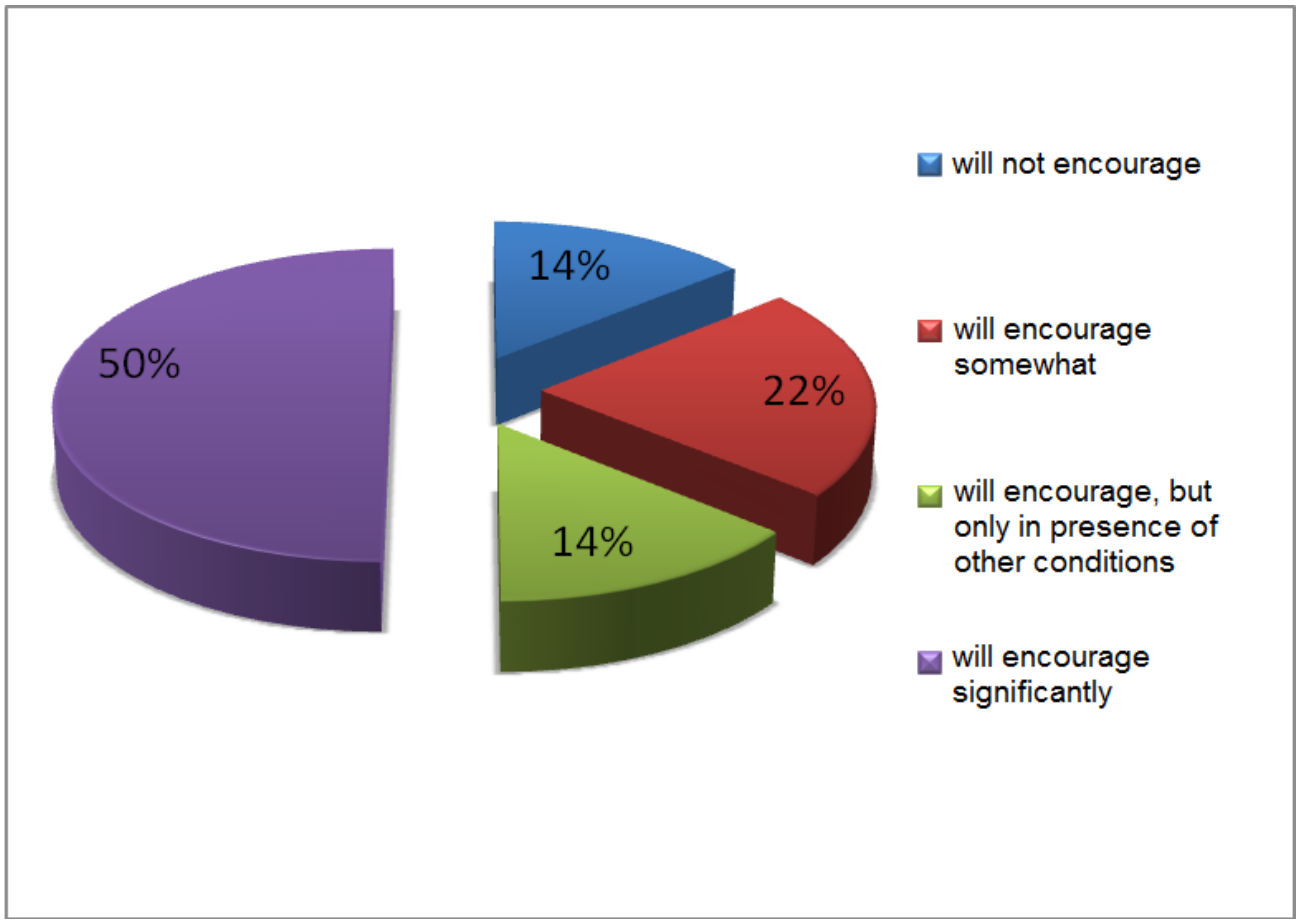
- Quality of legal provisions that regulate the legal status of property objects;
- Methods of property withdrawal; and
- Poor enforcement of legislation.

Among the factors that cause difficulties in property rights protection, some of the survey participants named special legal treatment that applies to certain categories of owners. This is explained not only by the fact that the IBC has a broad representation of international businesses investing in the economy of the Kyrgyz Republic, but also by the fact that in land relations the status of a foreign entity has an excessively broad scope of application. Criteria under which a person qualifies as foreign may have quite erratic legal consequences for businesses (thus, for example, changed status of an owner of 20% of shares in a joint stock company may turn such a company into a "foreign entity" for the purposes of the Land Code – quite unexpectedly for the entity itself). Given the restrictions that apply to foreign entities with respect to property, this situation naturally raises concerns of businesses.

The research written by the IBC covers these problems and analyses some of the legislative gaps that invite violations of property rights.

The second survey built upon the results of the first one; its purpose was to verify some of the conclusions drawn in the research and to find out what businesses think about the influence of the existing legal status of a foreign entity upon the overall investment climate in the country.

The survey has shown that business practitioners directly relate increased attractiveness of the national market for investment to the possible lifting of restrictions that apply to foreign entities in the field of property.



Among the conditions that might encourage investment the survey participants named:

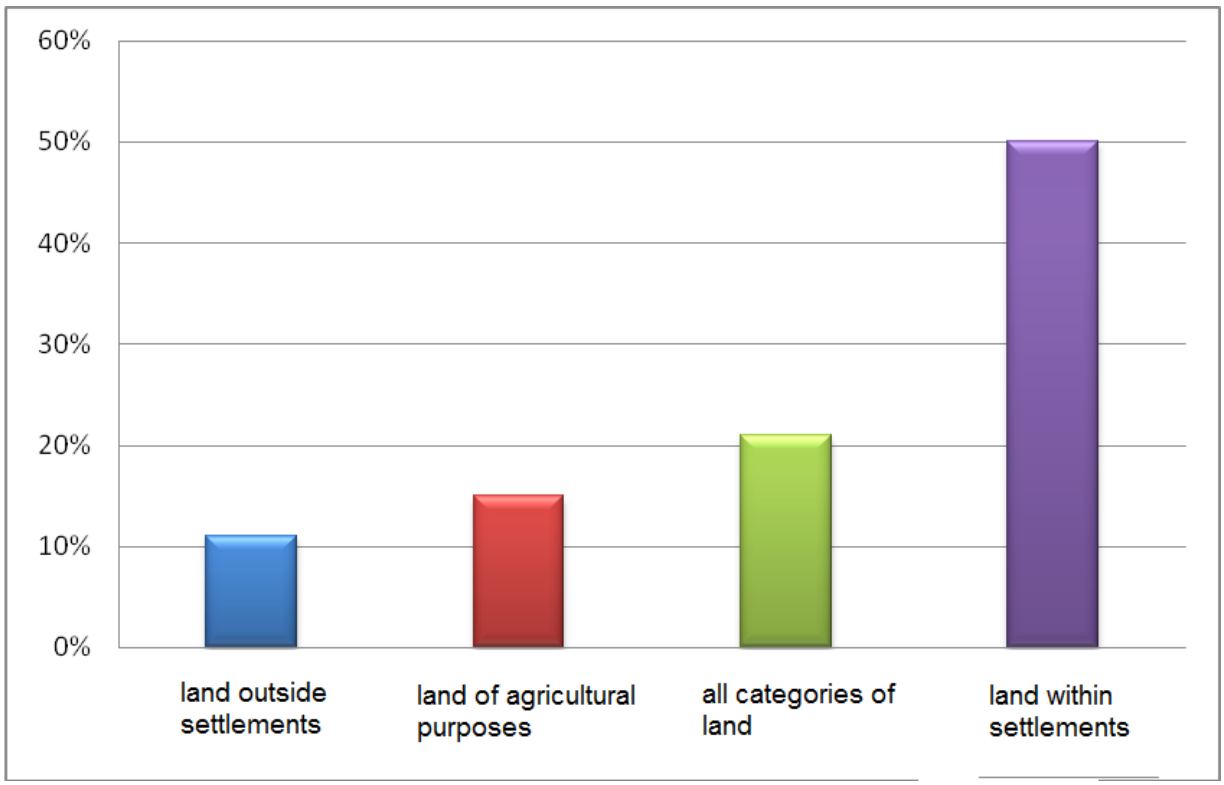
- effectiveness of laws,
- working guarantees of private property inviolability (low raider risk, independence of the judicial system), and
- development programs.

It can be reasonably concluded that many problems of property right protection are related to the special legal status of certain categories of persons, including foreign persons.

Comment by a survey participant:

> *The possibility of obtaining property rights to land of certain categories could provide foreign entities with broader guarantees and exclude many risks in doing business within the Kyrgyz Republic. This would make foreign investors more comfortable about their future and increase their interest capital investment. Respectively, this would foster full-scale development of various sectors of the economy, and would help resolve many social problems that currently exist in the country.*

The survey results about which categories of lands to which, in the participants' opinion, foreign and domestic persons should have equal rights are noteworthy.
Invited to select from three categories of land, as many as 27 % of the participants mentioned the need to give equal rights to foreign and domestic persons with respect to <u>all</u> types of land (naturally, with the exception of lands of defense purposes and suchlike lands.)



The result shows that for the most part businesses focuses on land within settlements, but businesses' interest in land as object of property is generally high, as well.

Interestingly, 100% of the representatives of the banking and service area believe that equal rights to land within settlements are most important. Representatives of consulting and mining companies have the broadest range of responses: their votes spread equally between all types of land.

Another set of questions in the second survey of the IBC has to do with ***practical*** influence that public legal regulation of private legal relations may have upon business participants.
As many as 93% of the respondents believe that the tax service's current power to unconditionally extract money from them as a third party is a factor that negatively affects business.

Concern of the businesses about possible interference of public authorities is natural. Such interference may impede the regular course of commercial activities and add to the usual commercial risks additional hazards not related to company performance.

Below is an example offered by a survey participant in his comment:

> *Example: a taxpayer and a third party on a contractual basis resolve that, upon discretion of the third party, debt may be repaid in cash, within the established term, or in works (services) of a seasonal character – in this case, the third party has longer term to perform the obligation. In this case the third party to which Article 74 of the Tax Code applies may suffer from a lost profit – which is subject to other provisions of the existing legislation of the Kyrgyz Republic.*

Banks are particularly concerned that interference by public authorities' in their activities undermines the banks' credibility with their customers.

One of the elements of property right protection is the judicial system. The issue of credibility of the national judicial system is the subject of other studies. A lot of censures from the direction of businessmen cause terms of consideration of judicial disputes which take longer than the timeframe assigned by the civil-procedural legislation.

One of the indicative examples of judicial system activity is the court decision which, unfortunately, is not the only thing in judicial practice.

Ex: Citizen N has an uninhabited premise on the property right. In some years he gets notified that the other citizen claims the right for the property for some part of his uninhabited premise, confirmed with some law constitutive documents, however, the basis of delivery was not the court decision, but the certificate of assignation given by the judicial executor. Despite that fact that the property right of citizen N is obvious and lawful, under the current legislation its protection right is confined by the period of limitation.

However, as many as 93% of the survey participants believe that the possibility of having their contractual disputes settled by foreign courts or arbitration courts is a major contribution to their rights' protection; this demonstrates that owners feel more comfortable when the variety of methods for their property protection is as broad as possible.

II. In addition to the surveys, the IBC also used feedback mechanisms.

Businesses were invited to consider the recommendations of the research on property protection developed by the IBC.

III. RECOMMENDATIONS

1. A definition of "withdrawal of land for the needs of the state" should be included into the law (the Land Code) together with an exhaustive list of grounds on which such withdrawal may become possible.

2. Provisions that allow withdrawal of land plots for public and municipal needs must be excluded from the Civil Code and the Land Code.

3. Provisions allowing the Tax Service to interfere with private legal relations of commercial parties and to execute payments from accounts of third parties must be excluded from the Tax Code (Article 75).

4. A foreign legal entity, according to the Land Code of the Kyrgyz Republic, should be defined by one or more of the following criteria:
a)established and registered in accordance with the legislation of a foreign state;
b) fully owned by one or more foreign individuals or legal entities;
c) controlled by one or more foreign individuals or legal entities based on a written contract, the right to sell majority of voting shares, the right to appoint majority of members of the executive or supervisory body;

5. Equalize foreign persons and persons of the Kyrgyz Republic in their rights to land plots located within settlements; develop a more acceptable mechanism for the sale of agricultural land plots by foreign banks in case of foreclosure against such land plots;

6. Under Article 47 of the Land Code, a mechanism for settlement of disputes between land plot owners should be developed.

7. Objects of unfinished construction:The legal status of "objects of unfinished construction" must be defined; the necessary procedures that make an unfinished construction object a full-fledged object of civil relations must be developed.

8. The requirement according to which foreign persons must obtain permits of the special committee to purchase apartments and residential houses should be lifted.

9. It is necessary to establish mechanisms that would make decisions of foreign courts enforceable in the Kyrgyz Republic.

IV. REVIEW OF LEGISLATION IN THE PROPERTY RIGHTS AREA.

1. FOREWORD

An owner is legally in the position to own and use an object and to dispose of it, as long as this right is not restricted by law or by rights of any third parties.

This well-known formula is the starting point for discussion of numerous legal and economic aspects of exercise of owner rights.

Owners may exercise their property rights only when the state, allowing this right, obliges the parties acting vis-à-vis the owners to refrain from any infringement of the property rights, while the parties (including the state itself and its bureaucratic system) act respectively.

Property rights may not be protected if legislation substitutes the notion of private property with a surrogate that actually may not qualify as such.TH

There must be no opportunity to adopt a law that limits the principal institute of property rights to the extent where this right becomes virtually non-existent.

A legal treatment, being a system of legal rules that define the status of property as an object of civil relations, represents the entirety of all norms and provisions that apply to both static and dynamic aspects of property existence in its legal environment.

Since property is a basic component required for development of economic relations, and due protection of owners is the necessary precondition of market development, this document will focus on legal aspects of property rights protection and on legal treatment of property, as set forth by the national legislation.

Both proper recognition of participants' civil rights and due protection of these rights are required for normal civil turnover. Generally speaking, protection of rights provides the remedy against illegitimate infringements and restrictions, prevents such infringements and restrictions, and assures reimbursement of damage in cases where they could not be prevented or warded off.

The discussion below shows that the current legal system of the country at times makes it difficult to distinguish between legitimate and illegitimate restrictions of rights. In such cases, means and purposes of protection acquire rather specific features, as reflected in the recommendations that follow the discussion.

This Memorandum touches upon some theoretical aspects of the power of eminent domain, and upon the lack of guarantees that could have balanced this power out. Further on, the Memorandum covers the issues of normative regulation and demonstrates that the discussed deficiencies can have rather serious financial consequences.

Discussing protection of property rights, one inevitably deals with regulation of various types of property. On the one hand, protection of property rights is a relatively independent area; on the other hand, in every specific case it will be closely related to the legal status of the property in question.

This study covers primarily legal regulation of immovable property. It should be emphasized that the status of foreign persons has not been the specific focus of the study. Discussing legal treatment from the general to the specific, one inevitably touches upon the problem of foreign owners' special status; however, the legal situation described below directly affects the domestic participants of commercial relations, as well.

Therefore, the study focuses on the issues that most of the active participants of commercial relations face in the course their practical work in this country.

Apparently, discussion of property rights protection could be of particular interest in the framework of (1) intellectual property rights, and (2) securities market. Both areas have quite specific features and face serious problems that require a separate study.

2. CONSTITUTION: LEGAL TREATMENT OF PROPERTY. GROUNDS FOR DEVIATION FROM THE REGULAR TREATMENT OF PROPERTY. PUBLIC LEGAL REGULATION

Constitution of the Kyrgyz Republic (hereinafter – the Constitution) contains three principal provisions based on which the legislator should further develop the legal environment for property and proprietors.

Article 2 of the Constitution provides:

1. No person can be deprived of his/her property arbitrarily; confiscation against the will of the owner is allowed only by decision of a court.
2. In exceptional cases, property may be alienated for the state's needs stipulated by the law, with prior fair compensation.
3. Land and other natural resources may also be private, communal, or other type of property.

Limits of and procedures for execution of property rights to land and natural resources by owners, and guarantees for protection of these rights, are set forth by law.

Noticeably, Paragraph 2 of Article 2 of the Constitution providing for property alienation for the state's needs contains no provisions about termination of property right against the owner's will.

Therefore, property alienation in the interests of the state is possible either with consent of the owner, or based on a respective court decision, and it can be said that situations where neither is required must be extremely rare.

Based on the provisions above, we can suggest the following model of withdrawal of property right.

Property right may be withdrawn:

1. with consent of the owner;

2. without consent of the owner based on a respective court decision (confiscation of property);

3. in exceptional cases, as set forth by law, for the state's needs, on condition of prior fair compensation.

In effect, the third option may be executed on either voluntary or involuntary basis, and the mechanism of alienation will involve either owner consent, or a court procedure.

The wording "on condition of prior fair compensation" is typical of the practice known in the international practice as expropriation. In the legal system of the Kyrgyz Republic the term of either requisition or nationalization applies in this case. There are differences between these two special legal treatments, but here focus the feature typical of them both: property in these cases is withdrawn without owner's consent, legally, and based on compensation.

These two treatments qualify as exceptional.

The question whether this third option of property withdrawal may include any possibilities other than requisition and nationalization.

We wish we could answer with a definite "no".

However, legal regulation of property right to land requires special attention.

The Constitution provides for the possibility to include in law norms that set forth limits and procedures according to which an owner of land or of other natural resources should exercise their property rights.

Without getting into the theory of possible limits of property, one can represent the property right by the so-called civil law triad: in a simplified form, property right is understood as the right to use, own, and dispose of property.

Therefore, the legal status of a land owner can be represented by the following:

A land owner may be subject to:

1. Limits and procedures that apply to ownership;
2. Limits and procedures that apply to use; and
3. Limits and procedure that apply to disposal

The Constitution does not provide for any simplified methods to terminate any property right.

Considering the problem of non-judicial termination of property right without owner consent, we must understand that public authorities may infringe or derogate from property rights of private persons both illegally and legally.

Since public authorities may legally infringe interests of private owners or holders of other property rights, special measures are required for protection of owners. Termination of property rights of private persons by nationalization, as considered above, is legal. In this situation the owner must comply with the law, and may demand full compensation of losses, including the non-received income and the value of the property lost. This clearly follows from Articles 286 and 288 of the Civil Code of the Kyrgyz Republic (hereinafter – the Civil Code).

The unreasonable expansion of legitimate activities that may infringe owner rights, and the resulting possibility to use public legal mechanisms of property confiscation, raises concerns.

PUBLIC MECHANISMS OF PROPERTY WITHDRAWAL

Public legal relations are characterized by inequality of parties. One party to such relations is usually the state (or its agency/official) that has the command function and acts as the bearer of public power/authority.

In this respect, a number of provisions in the Civil Code and the Land Code of the Kyrgyz Republic (hereinafter – the Land Code) are of particular interest, as they can potentially broaden the scope of right-infringing activities that the public authorities may legally perform.

The language of the Constitution and Laws is compared in the Table below.

Constitution of the Kyrgyz Republic	Laws
In exceptional cases, property may be alienated for the state's needs stipulated by the law, with prior fair compensation.	**Civil Code** Article 233-17 1. A land plot can be withdrawn from its owner for state or public needs by means of redemption. 2. The respective authorized agency takes the decision to withdraw a land plot for state and public needs. 3. Procedure of withdrawal (redemption) of a land plot for state and public needs is subject to the Land Code of the Kyrgyz Republic. **Land Code** Article 66. Grounds for Non-Judicial Withdrawal of a Land Plot 1. Withdrawal of a land plot shall be allowed in the event of: 2) withdrawal (redemption) of the land plot for state and public needs in accordance with provisions of this Chapter; 3) failure to use a land plot or part of the land plot allocated for agricultural production within three years; 7) resolution of the state agency on subsoil to terminate (cancel) the right to use subsoil in cases set forth in the Law of the Kyrgyz Republic "On Subsoil". Article 20. The Government of the Kyrgyz Republic has the power to: set forth the procedure for withdrawal (redemption) of a land plot for state and municipal needs.

<u>The following can be concluded.</u>

1. The Constitution provides for exceptional cases where property can be alienated in the interests of the state, and refers to law as the basis of such alienation. The respective law – the Civil Code – contains Articles 286 (Requisition) and 288 (Nationalization) that contain an exhaustive list of cases where withdrawal of property from its owner is possible. In both cases it is only possible on the basis of a specially adopted law.

2. In addition to these two cases, legislation provides for other possibilities of property withdrawal. These provisions apply to land plots. It is hard to say whether such cases can be considered exceptional, or fall under regular treatment of property right to land and other natural resources.

3. Court procedure in case of owner's disagreement with withdrawal or conditions thereof can be viewed as a legal remedy against the state powers.

4. In cases where agricultural land plots are withdrawn, and in cases where the State Agency on Subsoil withdraws land plots by termination (cancellation) of right to use the subsoil this legal remedy is absent.

5. The Constitution only mentions the possibility to alienate property for the **state** needs. Possibility of alienation for **public** needs is provided by the Civil Code and the Land Code. Moreover, the Land Code (Article 20) empowers the Government of the Kyrgyz Republic to set forth the procedure of withdrawal (redemption) of a land plot for state and **municipal** needs.

What are these public needs and how are they defined? What is their scope and magnitude, and who represents them?

Clearly, the state is meant to function for the good of the society. Since the state performs functions required by the society, withdrawal of property by decision of a local community or another suchlike decision should not be possible.

Evidently, this provision broadens the existing possibilities to alienate property for the state needs and must be excluded.

Moreover, the law should contain a clear definition of "state needs". Otherwise the Constitution provides for exceptional cases when alienation of property for state needs is possible and refers to a law, while the law, instead of defining such cases, broadens their scope, adds public and municipal needs, and authorizes the Government to set forth the procedure of withdrawal.

Withdrawal of particularly valuable lands (Article 70) is regulated in the same fashion (Article 70). Withdrawal of particularly valuable agricultural and non-agricultural lands is only allowed in exceptional cases upon decision of the Government of the Kyrgyz Republic.

What are these exceptional cases, and why the respective decisions should be based on a Government's resolution, and not on law (provided that the lands, as stated above, are particularly valuable)?

Overabundance of cross-references in the area where the state should particularly well protect its citizens' interests is surprising.

It appears that for basic compliance with the constitutional provisions the law must define the grounds on which property can be withdrawn for state needs; the law should also include the procedure of property alienation for these purposes.

Another example of legislation allowing public norms interfere with private relations are Articles 74 and 75 of the Tax Code of the Kyrgyz Republic (hereinafter – the Tax Code) that regulate forced recovery of tax debts.

Article 75 of the Tax Code allows the Tax Service to file a court claim to enforce tax collection from property of the taxpayer. As far as a taxpayer (debtor) is concerned, the article complies with the constitutional requirements.

However, there exists a provision regarding third parties.

When filing a court claim, the tax authority may send to a third party, such as the taxpayer's debtor, employer, bank, or another institution, a notification with a demand to cease payments to or on behalf of the taxpayer who has a tax debt.

Should the third party fail to perform accordingly until a respective court decision is taken, the amount equivalent to the payment, but not exceeding the tax due, can be executed from this third party. This amount is executed based on the respective court decision.

Why does the Tax Service have the power to interfere with relations of two subjects of **private** legal relations? Since payments are executed based on a court decision, one may argue that no direct violation of property right (such as withdrawal without owner consent) takes place.

However, the court must base its decision on this very law; therefore, it is assumed that property (money) may be withdrawn from a person that has failed to comply with the requirements of the tax service, **but in these given relations does not act as a taxpayer**. This

constitutes an evident violation of such fundamental principles of the civil law as equality, autonomy of will, and independence of property of participants of legal relations, inviolability of property, freedom of agreement, impossibility of arbitrary interference into private affairs, unrestricted execution of civil rights, restoration of breached rights, and judicial remedies thereof.

Article 74 of the Tax Code contains a still more intriguing legal scheme.

> Should funds of a taxpayer be insufficient or absent, the tax authority may, within the limits of the tax amount due and recognized by the taxpayer, execute cash payments from accounts of third parties.
>
> Amounts may be executed from accounts of third parties if the third party has documentally proven debt to the taxpayer, as confirmed by a reconciliation report between the taxpayer and the third party, without recourse.

Again, a participant of civil relations recognizes its debt to another participant of these relations, but makes no respective payment.

What should a creditor do in this situation?

The creditor should file a court claim. It is hardly plausible that the legislator has deliberately made a provision under which a bank, on demand of a creditor, would without recourse transfer money from the debtor's account, once the creditor produces a reconciliation report. Remarkably, however, the state, represented by its Tax Service, is authorized to act in this fashion.

3. IMMOVABLE PROPERTY. LAND PLOT. OWNER STATUS. LAW CONFLICTS

Immovable property has special status among all objects of proprietary rights. Due to its high value and objective durability, immovable property pays a significant role in economic development of a nation.

This Section covers legal regulation of land and other immovable property, which is particularly important due to the importance of the object of regulation, and clearly illustrates the situation with protection of property rights in the country.

Civil Code of the Kyrgyz Republic, in addition to other grounds on which property right to immovables arises, provides for property right arising in case of buildings, structures, and other newly created immovable property (Articles 251, 252 of the Civil Code).

It must be noted, however, that immovable property must be "created" by legal means.

If a new object of immovable property is created, the following three key elements are required for recognition of rights to this newly created object.

1. A land plot for construction must be allocated legally. It means that the authorized agency must provide it to the holder of construction right, specifying the scope of rights provided (ownership right or right to use), without any violations.

2. The land must be used in compliance with the legislation. Clearly, this requirement is closely related to the previous one, as it is critical that the land plot is not only allocated on legal grounds, but also used for the designated purposes. In other words, if land is allocated for construction of an industrial object, building a high-rise residential house on it will constitute a violation of law.

3. Immovable property must be built in compliance with the established technical norms and standards and in presence of all necessary permits obtained from authorized state agencies.

The immovable property built in violation of any of the above requirements will qualify as unsanctioned construction. The person who has performed unsanctioned construction obtains neither property right to it, nor the right of disposal (that is, the right to sell, donate, lease, or perform other transactions).

Another important feature of legal regulation of creation and protection of rights to immovable property is that legislation of the Kyrgyz Republic links creation, transfer, and termination of rights to and encumbrances of property to registration of rights to immovable property. The legal basis of registration of rights to immovable property is the Law "On State Registration of Rights to Immovable Property and Transactions Therewith".

4. REGULATION OF LAND RELATIONS: EXISTING DEVIATIONS FROM THE REGULAR TREATMENT OF PROPERTY AND THEIR REASONABILITY

The system of legal regulation of land plots, the approaches and principles of civil legislation and land legislation reflect the special status that land has both as a natural object and as an object of legal regulation.

The Land Code declares that land relations in the Kyrgyz Republic are regulated, among other documents, by the Civil Code; however, at the same time the Land Code contains a provision according to which its provisions shall govern in case of any conflict with land law provisions contained in other legislation.

Thus, the Land Code recognizes the possibility of a law conflict, yet reserves for itself the "last say" in regulation of land relations. This arrangement is further supported by the Law "On Normative Legal Acts of the Kyrgyz Republic", according to which in case of a conflict between normative legal acts of equal legal force, provided that neither of them contradicts a legal act of higher status, provisions of the act that specifically regulates this field of legal relations shall govern (Articles 6 and 32). Since the Civil Code and the Land Code are legal acts of the same status, but the Land Code regulates specifically land relations, norms contained in the Land Code shall thus govern.

These features are closely linked to and follow from the constitutional provisions described in Section 1 of this Memorandum and related to the limits of ownership rights to land plots; land legislation broadly uses these possibilities.

Thus, pastures in the Kyrgyz Republic may only be owned by the state. If idle pastures are available, foreign individuals and legal entities may obtain the right to use these lands based on international and intergovernmental agreements ratified by the *Jogorku Kenesh* (Parliament) of the Kyrgyz Republic. This example illustrates particular inequality between the state and the foreign persons, which is typical of land legislation of the Kyrgyz Republic

in general (Article 3 of the Law "On Pastures", Article 4 of the Land Code).

This is a direct deviation from the general treatment of property. There exist indirect approaches, too.

Thus, the Civil Code provides that the Kyrgyz Republic is a participant of civil legal relations and may act as a party to civil legal relations with individuals and legal entities on a parity basis.

Norms that apply to participation of legal entities in civil legal relations also apply to the Kyrgyz Republic as participant of such relations, unless otherwise follows from a law or from specific features of the Kyrgyz Republic as a participant (Article 168 of the Civil Code).

The Land Code actively elaborates on this provision and establishes features of the state as participant of commercial relations.

Thus, a land plot being used by the state or by a municipality may not be withdrawn for repayment of its user's debts, including cases of the user's bankruptcy, with the exception of foreclosure against buildings and structures owned by the user (Article 23 of the Land Code).

The Law "On Management of Agricultural Lands" (hereinafter – the Law on Management) provides that, in case of transactions with land that qualifies as agricultural, rural residents of the Kyrgyz Republic shall have the preemptive right. This provision is puzzling, and not only from the viewpoint of its reasonability – although its inclusion in the legislation could have represented a virtuous yet questionable attempt to protect the rights of rural residents (Article 17 of the Law on Management).

The current situation makes this provision unviable for a number of reasons.

First, the question is bound to arise, how a seller can make sure that all rural residents have a chance to use their preemptive right as guaranteed by law. Does the seller have to send a personal notification to each rural resident, or is an public announcement sufficient? Another logical question is, what kind of media (printed media, television, etc.) must be used for such announcements, how frequently these announcements must be repeated, how long the seller must wait till prospective buyers react, etc.

In the process of negotiations a seller must know whether a prospective buyer is a rural resident. Here another question arises, namely, who qualifies as a rural resident. The Law on Management contains a formula "citizen of the Kyrgyz Republic permanently residing in the rural area for a period of 2 years or more", but it remains unclear, who qualifies as a rural resident for the purposes of Article 17, whether such citizen must actually live in the rural area, or whether it is enough just to be officially registered there, whether any time limits apply, etc.

Second, it is only logical to assume that, if the state establishes such rules, it is obligation of the state to assure compliance with the rules.

How can the state, represented by its authorized agencies, perform that? Does it have to track how the seller "notifies" prospective buyers? Finally, how is it possible to make sure that all rural residents of the Kyrgyz Republic have chosen not to use their preemptive right, and the seller, having duly complied with this provision, may finally sell the land to other persons?

5. IMMOVABLE PROPERTY AND LAND PLOTS: CONFLICTS OF LEGALIZATION

Below is a discussion of the Kyrgyz legislation regulating rights to land and buildings and structures in cases where scope of these rights is different.

According to the legislation of the Kyrgyz Republic, an owner of a land plot does not automatically become the owner of the immovable property constructed on the land plot.

This approach results in specific character of legal regulation of rights to land and immovable objects on it.

Thus, according to the Land Code, if the right of ownership of a building or a structure, or of a part thereof, is transferred, reassigned, or mortgaged to another person, this person obtains the rights to the land plot linked to this building or structure, in the same scope and under the same conditions that applied to the previous owner of the building or structure, unless otherwise provided by agreement between the parties (Article 44 of the Land Code).

Suppose a pledgeholder is a foreign person. [3]The Land Code prohibits land ownership by foreign persons. In these situations foreign persons obtain the right of land use. The question is, who they obtain this land from. Having sold the land in question or having handed it over to the pledgeholder against the non-repaid debt, the previous owner no longer has property right. There is an opinion that local authorities should be the effective owner in such cases; however, there is no legal ground for this.

Enforcement of some other provisions of the Land Code also appears questionable.

Article 47 of the Land Code provides that, in case a right to a land plot is terminated, the owner decides what should happen to the buildings and structures on the land plot in question. At the first sight, this provision appears to protect the rights of the building owner and not to cause problems.

What happens in reality.

Suppose an owner loses the right to land as a result of failure to make allocation to the Social Fund, or in under similar conditions. The state confiscates the land plot and, most likely, has clear plans about its further use. Ideally, neither the state, nor the previous owner needs the building, and the owner agrees to have it turned down without any compensation.

However, if the owner is unwilling to turn down the building unwanted by the state, or claims compensation for the objects construction of which could have cost more than the land plot itself, a problem is bound to arise.

This issue is regulated relatively clearly in the description of consequences of land plot withdrawal for state or public needs. Article 68 of the Land Code provides that redemption price of a land plot must include the market value of the right to land and of the buildings and structures located on the land, and the damages inflicted to the land owner/user by termination of the right to land plot, including the damages connected with early termination of his obligations to third parties.

[3] The influence of "foreign person" to the property rights protection was examined more detail in section III

Naturally, a dispute about further destiny of the owned objects may be settled by court - but the court should base its decision on law. What is the basis of a fair court decision in this case?

In our opinion, it would be wise to consider the possibility of lifting the restrictions that may vary depending on the status of the right holder (Kyrgyz or foreign) and on the object of legal relations (land or another object).

In our opinion, the norms that provide for rural residents' preemptive right to purchase land must be eliminated. In our understanding, this provision is aimed at protection of rural residents' rights and prevention of mass purchase of land for further non-agricultural use. However, it is important to take into account that a person unwilling to use land for its designated purpose, i.e., for agricultural production, will not purchase such land. Use of agricultural land for non-agricultural purpose is impossible, because it will constitute violation of the land legislation. The existing legal environment thus only creates additional problems to persons who already own land.

Another pressing issue is the need to lift the restrictions that apply to transactions with agricultural land, including the restriction on pledge of land (with banks only). If an individual needs funding, for example, for purchase of agricultural equipment, but has no right to pledge land to any person other than a bank, the question is, who actually needs this land, ownership of which is costly, since land is subject to taxation. Banks, in their turn, are not always interested to issue credits secured by land – for the very reasons described above.

6. INVESTMENTS: DIRECT AND INDIRECT REGULATION

Legal regulation of property right of foreign persons: restrictions constituting conflict of laws. Mechanisms of property right transfer.

Because of gaps in the legislation, participants of civil relations lack the due protection. Before analyzing the extent to whih property rights of foreign persons are protected in the Kyrgyz Republic, we will reiterate several well-known legal provisions.

The situation with individuals (nationals of the Kyrgyz Republic and foreign nationals) is clear and requires no further discussion here.

Legal entities registered according to the legislation of the Kyrgyz Republic (the Civil Code, Law “On State Registration of Legal Entities, Branches (Representation Offices)” qualify as legal entities of the Kyrgyz Republic.

At the same time, the Land Code of the Kyrgyz Republic contains a definition of a foreign entity.

A foreign person is a foreign legal entity, a foreign national, or a stateless person acting as a party in land relations.

A foreign legal entity is a legal entity that has one of the following features:
a) established and registered in accordance with the legislation of a foreign nation;
b) fully owned by one or more foreign individuals or legal entities;
c) controlled or managed by one or more foreign individuals or legal entities based on a written contract, on the right to sell majority of voting shares, in the right to appoint majority of members of the executive or supervisory body;
d) registered in the Kyrgyz Republic and having not less than 20 % of the authorized fund owned by foreign nationals, stateless persons or legal entities mentioned herein;
e) established on the basis of an international treaty or agreement.

It must be noted that definition of a “foreign person” contained in the Land Code creates a “vicious circle”, as virtually any legal entity can qualify as foreign under it.

Now consider the property issues.

According to Article 5 of the Land Code, foreign persons can obtain property right to land plots within settlements in one case only: if such persons issue mortgage-based loans for construction of residential premises. Land outside settlements can only be used for a limited time.

Foreign banks and specialized financial and crediting institutions can obtain property right to agricultural land plots in cases of foreclosure against such land plots.

Property right is termless by definition. The termless character of the property right is set forth by the Civil Code of the Kyrgyz Republic (Article 222).

However, the Law on Management of Agricultural Land "modifies" this provision in a peculiar way.

The restriction that applies to land ownership by foreign persons results in the following

situation.

Land is known to be the most attractive collateral. Naturally, creditors prefer obligations secured by land.

However, due to the reasons discussed above, most banks active in the Kyrgyz Republic qualify as foreign persons; therefore, the mechanism for protection of pledgeholder rights – foreclosure against pledged land – can not be used in their case.

Trying not to hinder further economic development of the country, and having found no other, more adequate legal mechanism, drafters of the Law "On Management of Agricultural Land" have introduced a novelty called "temporary property right". The same principle has been used in a number of provisions of the Land Code. According to it, foreign banks and specialized financial institutions obtain property right to an agricultural land plot for the period of one year in cases of foreclosure against the land plot.

The bizarre legal construct of a "temporary property right" represented the legislator's attempt to soothe the situation with banks, because prior to introduction of this norm the situation remained completely unregulated. However, this solution is only a palliative, as the question is bound to arise, what a bank should do if one year proves not enough to find a solvent buyer of the land. According to the legislation, the bank must get rid of the land within one year. If a buyer is there, the problem is solved, but what happens, if not?

Moreover, banks will face yet another problem, and that is the preemptive right of rural residents to purchase land.

Does the state have funds to purchase land from banks at a price that will be sufficient to cover the principal and interest on the loan, as well as the costs of land maintenance incurred by the bank and the land tax paid by it?

Normative documents that regulate rights of foreign persons to houses and apartments purchased by them also raise questions.

Foreign persons may not own land in the Kyrgyz Republic, but this restriction does not apply to ownership of non-residential objects located on land plots.

Another conflict becomes evident here. Kyrgyz individuals and legal entities are in the position to sell to foreign persons buildings or other structures they own. These immovables become property of the foreign person and are registered respectively. But what happens to the land on which the immovables are located? What happens to the property right that the earlier owner loses? All that a foreign person may obtain is the right of temporary use. In other words, an owner loses its property right, while the next owner does not exist. The result is a land plot without an owner.

There is an opinion that reassignment of the property right to local authorities of the respective area solves the problem. However, the first question is, on which grounds such reassignment should take place. Second, even if the property right is reassigned, further allocation of the land plot for ownership or use must be subject to primary market rules, that is, it should be tender-based. Therefore, a foreign entity that has already purchased immovable property must also participate in a tender for the land on which the property is located.

The problem does not end here. If a foreign person later chooses to sell the immovable object to a Kyrgyz person, the rights to land obtained by the Kyrgyz person as a result of such transaction will be limited to those of the foreign person.

Foreign persons are allowed to purchase individual residential houses and apartments in residential buildings, but they have to obtain a permit of the Committee for Alienation of Residential Houses and Apartments of Residential Stock to Foreign Individuals and Legal Entities, as regulated by Resolution of the Government #82 of 15 February 1999.

According to Article 46 of the Land Code, a land plot attached to a building with several apartments and/or non- residential premises (a multi-apartment house) may be indivisible and shall belong on the basis of the common shared ownership to the owners of apartments and/or non-residential premises.

So, on the one hand, the Land Code provides that a foreign person purchasing an apartment in

an apartment house automatically obtains the right of common shared ownership of the land plot attached to the house; on the other hand, the very Land Code prohibits such ownership.

Most likely, the provision that prohibits ownership of land by foreign persons will govern. In this case, there should exist a legally binding procedure of registration by the State Agency for Registration of Rights to Immovable Property under the Government of the Kyrgyz Republic (hereinafter - the *Gosregister).* The importance of such registration should not be underestimated, as creation and termination of rights to immovable property in the Kyrgyz Republic is linked to the respective records in the Unified Registry of Rights to Immovable

Property kept by the *Gosregister*. Absence of legal regulation means absence of any legal protection.

Given the current definition of a foreign legal entity, the scope of persons to whom various restrictions of property rights apply is extremely broad. It must be noted that exactly these persons have proven to be most active and sustainable in business. The largest Kyrgyz banks and other financial and crediting institutions are known to have foreign interest.

The existing situation is not attractive for investment in the national economy, because the principal mechanism that guarantees and protects the respective rights – the land ownership – can not function.

It will be appropriate to cite a provision of the Law of the Kyrgyz Republic “On Investment in the Kyrgyz Republic”:

The Kyrgyz Republic applies to economic activities of foreign investors who invest within the territory of the Kyrgyz Republic the domestic treatment that applies to individuals and legal entities of the Kyrgyz Republic.

The features of legal regulation discussed above graphically illustrate the favorability of legal treatment that foreign investors have in this country.

Evidently, the legislation has something of a "double layer" when it gets to regulation of investor rights. On the one hand, domestic treatment of investors’ economic activities is declared. On the other hand, legislation contains requirements that, in our opinion, are not just unreasonable and incapable of protection of the state, its citizens, or its natural resources

against possible infringement by foreign persons, but are also legally unfair. Moreover, the examples above illustrate the conflict of laws that is of hindrance to all participants of civil relations, including domestic participants. As we have mentioned earlier in this document, conflict of laws is one of the primary reasons for the lacking protection of owners.

7. UNFINISHED CONSTRUCTION: INVESTMENT RISKS

The problem discussed below is rather specific, yet it is a good illustration of the overall insufficiency of legal regulation in the important area directly related to protection of investors' property rights in case of unfinished construction (which includes participatory share in construction in progress, as well as purchase of an unfinished construction object) – an option that can be profitable and attractive for many investors.

A prospective investor has to realistically assess investment risks when considering capital investment in unfinished construction.

Section II of this document touches upon one of the critical issues in this area: legal recognition of newly created property. Clearly, physical existence of an object is not equal to its legal existence. Property right can only be protected if the property is "legalized" subject to the established legal norms. Unfortunately, the wording of these critical norms is sometimes dubious.

In this case, the most important issues are mandatory registration of a participatory share agreement or purchase and sale agreement, and registration of rights to the unfinished construction object with the *Gosregister*.

We have already mentioned the principal importance of these issues, as the legislation of the Kyrgyz Republic directly links creation of rights to immovable property and validity of transactions therewith to their registration with the *Gosregister*.

The principal questions that are not resolved by the existing legislation are, first, whether the objects of unfinished construction qualify as immovable objects, and, second, who qualifies as an owner of an unfinished construction object until it is put into operation.

According to Article 252 of the Civil Code, ownership right to newly constructed buildings, structures, and other newly created immovable property arises at the moment of registration, which means that only the fact of registration makes an object of unfinished construction qualify as immovable property.

According to the Law on State Registration, rights subject to registration in the Unified State Registry are the rights to a unit of immovable property that may be represented by a land plot, a building, a structure, an apartment, or by other immovable property with established boundaries according to the legislation of the Kyrgyz Republic

An object of unfinished construction is property represented by undismountable (complex) assemblage of capital constructions attached to land, which can not be moved without causing incommensurable detriment to its designated purpose. In other words, an object of unfinished construction does not have the features of immovable property.

Judicial practice has no consistency here.

Considering disputes that involve rights to immovable property, including objects of unfinished construction, some courts decide that the unfinished construction objects qualify as immovable property and compel the *Gosregister* to register transactions with it and the respective rights (see, for example, Resolution of the Court of Arbitration of Chui Oblast of 5 November 2002 on the claim of special administrator of *Severnaya* mobile mechanical department against the Alamudun office of the *Gosregister*, case # Ч07-357/С6пр02).

Other courts recognize objects of unfinished construction as immovable property if such objects are registered with the *Gosregister*: thus, Ruling of the Supreme Court of Arbitration of the Kyrgyz Republic of 14 December 2001[4] provides that, based on Article 252 of the Civil Code, right to newly created property subject to state registration arises from the moment of such registration. However, disputable objects of unfinished construction are represented both by property and by funds invested into construction.

The issue of ownership of unfinished construction objects and the moment when such ownership begins lacks sufficient regulation.

Thus, the Practical Guide approved by Order of the Gosregister #107 of 27 June (hereinafter – the Practical Guide) provides that property right to an object of unfinished construction is

registered based on the documents proving property right to a land plot, a construction permit, and documents containing description of the object of unfinished construction. Since the entitling documents are a construction permit and a description of the object, rather than an agreement of participatory share that regulates relations between the interest holder and the contractor, it can be assumed that it is the property rights of the contractor that must be registered.

Article 251 of the Civil Code names, among other, such grounds for obtaining property right as a transaction that involves alienation of the respective property, and full payment of the due share contribution.

If payments made in the process of participatory construction qualify as accumulation of interest-holders' contributions, the question about ownership and, respectively, about rights subject to registration with the *Gosregister*, should be resolved in favour of the contractor, because the interest-holder who fails to contribute its full share does not meet the requirements and therefore does not obtain property rights to property in question, as provided by Article 251 of the Civil Code.

Based on the above, it can be reasonably assumed that an object of unfinished construction currently is unlikely to qualify as immovable property, and that the owner of such an object should be the contractor.

Due to the lack of clarity with the legal status of unfinished construction objects yet another question is bound to arise: whether the owner is in the position to alienate the object.

Since the legislation does not provide for the possibility of registration of rights and transactions with immovable property before the object physically comes into existence, an agreement of its purchase and sale can not be registered with the *Gosregister*. The discussion above shows that property rights to an object of unfinished construction is regulated on the basis of the documents that prove property right to the attached land plot, the construction permit, and the documents that contain description of the unfinished construction object.

[4] The suit of Kyrgyz National State Holding Company "Interenergoholding" about revision as inspectorate by the decision of Bishkek Arbitration court from June, 29th, 2000 on case N Б-01-397/2000-С1 under the suit of joint-stock commercial "Dos-Kredobank" to the collective enterprise to the construction firm "Alga", the Limited Liability company "Smile", to Joint Kyrgyz-Kazakh enterprise "Rising" and Joint-stock company "Chuistroy" about debt collecting, case N Б-01-397/2000-С1

Therefore, a buyer can not register the object in its name, since the buyer has none of the above documents (except when a land plot is being sold together with the object on it, which is not considered here).

Therefore, the situation of the buyer is the same as that of a participatory construction participant: neither has adequate legal protection. In fact, the situation is such that the question whether purchase and sale of an unfinished construction object is possible should be answered with a “no”, and owners of such objects have no chance to dispose of the objects at their discretion.

8. JUDICIAL SYSTEM: ENFORCEMENT OF FOREIGN COURT DECISIONS

Evidently, true protection of property rights, especially given the uneasy legal environment, is highly dependent on efficiency of the judicial system. Speaking of protection of investors' property rights, it is necessary to touch upon one aspect of foreign investor rights' protection: enforceability of decisions of foreign courts within the territory of the Kyrgyz Republic.

Foreign investors include into their agreements provisions about international arbitration in case of possible disputes.

Formally, the Kyrgyz Republic has the necessary legal environment for inclusion of both arbitration and forum-selection clauses into agreements.

Recognition and enforcement of decisions of foreign courts and foreign arbitration courts by courts of the Kyrgyz Republic is provided by the Code of Civil Procedure of the Kyrgyz Republic (hereinafter - the CCP), according to which decisions of foreign courts are recognized and enforced in the Kyrgyz Republic if it is provided by laws of the Kyrgyz Republic or international treaties to which the Kyrgyz Republic is a party, or on a parity basis (Article 380 of the CCP).

Decisions of foreign courts are understood as decisions on civil cases, including decisions on business disputes and other disputes related to entrepreneurial and other economic activities, and verdicts related to reimbursement of damage caused by crime (Article 430 of the CCP). With respect to foreign third-party courts (arbitration courts), the legislation applies the same norms as apply to enforcement of decisions of foreign courts.

According to Article 380 of the CCP, a law, an international treaty, or parity is required for recognition and enforcement of court decisions.

Therefore, the following is necessary for enforcement of a foreign court decision:

1. A special law containing a norm of direct application that allows to enforce a decision of a foreign court. There is no such law in the Kyrgyz Republic. All respective norms of the national legislation are reference norms, and not direct application norms. Article 380 of the CCP refers to law, Article 430 of the CCP refers to Article 380 of the CCP, Article 96 of the Law of the Kyrgyz Republic "On Enforcement Proceedings and Status of Court Marshals in the Kyrgyz Republic" refers to international treaties and legislation of the Kyrgyz Republic.

2. An international treaty. The Kyrgyz Republic has joined the Convention on Legal Assistance in Civil, Family and Criminal Matters (Minsk, 22 January 1993) and the Convention on Legal Aid and Assistance in Civil, Family and Criminal Matters (Kishinev, 7 October 2002). According to these two agreements, enforcement of a decision of a foreign court/arbitration court within the territory of the Kyrgyz Republic is possible upon recognition of the respective decision by a competent Kyrgyz court. Enforcement of court decisions related to business disputes is subject to special regulation (as signed in Kiev on 20 March 1992) and to adopted in its furtherance Agreement on Mutual Enforcement of Decisions of Arbitration, Economic, and Business Courts within the Territory of the Commonwealth of Independent States (signed in Moscow on 6 March 1998).

According to Article 3 of the above Agreement, a decision of a competent court of an Agreement Party must be unconditionally enforced within the territory of another Agreement Party

Therefore, enforcement of decisions made by courts of the CIS nations has solid legal basis. To enforce decisions of courts of other nations, bilateral agreements are required. So far, the Kyrgyz Republic has not entered into any such agreements.

3. Enforcement of competent court decisions on a parity basis.

Courts of the Kyrgyz Republic have to decide whether a petition to recognize and enforce a decision of a foreign court can be satisfied in the absence of a respective international agreement, and make sure that courts of the foreign nation recognize court decisions on the parity basis, or that no negative decisions have been taken so far by thtis nation with respect to recognition of decisions of Kyrgyz courts. Practically, this means that courts of the Kyrgyz Republic, when considering such petitions, have to check whether decisions of Kyrgyz courts have been recognized in the respective country, or whether legislation of this country does not allow such situations.

Elaborating further, one can say that, to develop positive practice of enforcement, somebody would have to take the risk of using a forum selection clause, obtaining a foreign court decision, and petitioning a Kyrgyz court respectively. In other words, a precedent has to be created.

All of the above makes it clear that a foreign party (not being a party to the Agreement on Procedure of Settlement of Disputes Related to Business Activities) that includes a forum selection clause into an agreement with a Kyrgyz party faces the risk of having its petition denied.

In other words, recognition and enforcement of foreign court decisions (with the exception of courts of the CIS countries) is questionable.

Therefore, it is important that nations whose businesses actively enter the market of the Kyrgyz Republic and require proper legal protection sign the respective treaties with the Kyrgyz Republic.

9. CONCLUSIONS

The current legislation contains provisions that restrict owners' rights or cause conflicts of law, thus preventing proper execution of owners' rights.

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