



Right Moves
Effective Solutions

Financing Agribusiness in Kazakhstan: Key Legal Challenges

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Applicable Legal Framework

- 1) The Commercial Code, No. 375-V 3PK dated 29 October 2015 (the “**Commercial Code**”).
- 2) The Law “On state regulation of development of the agribusiness and rural territories” No. 66-III 3PK dated 8 July 2005.
- 3) The Law “On Grain” No. 143-II dated 19 January 2001 (the “**Grain Law**”).
- 4) The Law “On development of cotton industry” No. 298-III 3PK dated 21 July 2007 (the “**Cotton Law**”).
- 5) Law of the Republic of Kazakhstan dated 29 October 2015 no. 372-V “On Agricultural Cooperatives”
- 6) The Rules for the Issue, Circulation and Redemption of Grain Receipts, the Requirements for Sample Grain Receipts and Forms of Grain Receipts and the Rules for Production, Acquisition, Storage and Destruction of the Grain Receipt Forms dated 9 July 2015, No. 4-1/620 (the '**Rules**').

GRAIN SECTOR v CURRENT STATUS

Kazakhstan is among the world's top 10 exporters of wheat which is by far the country's most important agricultural commodity, well-known for its modernization of harvesting techniques.

Kazakhstan has inherited the Soviet system of grain storage infrastructure where the grain is mainly stored in large, centralised storage and trading facilities, the elevators. After privatization and a series of re-sales, ownership and management of elevators ended up mostly in the hands of large grain producers. Storing and handling of their own grain is the top priority for them, while delivering storage services to other producers and traders is just an additional source of income.

Some elevators try to make their own arbitrage gains from grain trading using the grain stocks that are the property of their customers. The elevator management may sell a portion of stored grain on attractive terms and then return it after the next harvest, when the prices are relatively low. This is illegal to do, because the grain receipt system implies that holders can withdraw their grain at any time. As long as holders do not withdraw massively, the elevator's grain deals will not be noticed. But once elevator stocks are depleted, the management may fail to find other sources quickly in case a farmer's grain is to be returned. Grain owners may thus see themselves unable to withdraw their grain.

Experienced farmers or traders thus keep black lists of elevators that are active in illegal trading practices. A recent report said that there were unsupplied grain receipts worth 180 thousand tons of grain between 2008 and 2010.

THE CONCEPT OF GRAIN AND GRAIN RECEIPT

Grain means fruits of grass family, pulse crops and the olive cultures, used for the nutritional, seed, fodder and technical purposes (see section 4 of article 1 of the Grain Law).

Grain receipt - double warehouse certificate, issued by grain collection stations (the “Silo”) in confirmation of the acceptance of grain from the owner of the grain for storage (see section 10-1 of article 1 of the Grain Law).

A grain receipt, by definition, is the letter of guarantee, which contains more than 10 quantitative and qualitative characteristics of the product, as well as information about the seller and the buyer. Forms are issued by the banknote factory of the National Bank of Kazakhstan and, as securities they have several degrees of protection.

Grain receipts are composed of two parts - the **warehouse certificate** and **pledge warrant** - which can be further separated and handled individually (see section 2 of article 39 of the Grain Law).

USE OF GRAIN RECEIPTS

Grain receipts are issued by grain collection stations for some amount of grain production within three days after receiving the goods for storage. At the same time, at the request of the seller, the entire volume of production can be divided into parts, and each part will be given a separate grain receipt (see article 39-1 of the Grain Law and section 4 of the Rules).

The owner of grain receipt is the owner of the grain stored at the elevator, and a sale of receipt by him automatically transfers the rights for production to the buyer. The sale is made by endorsement, i.e. affixing the endorsement on the folio verso of a valuable security. The number of resale transactions is not limited (see article 40-1 of the Grain Law).

Current holder of grain receipt can present a document to the elevator, where they will be obliged to release the appropriate amount of grain products for him (see articles 14 and 41 of the Grain Law).

WAREHOUSE CERTIFICATE AND PLEDGE WARRANT RIGHTS

The holder of a warehouse certificate can dispose of the stored grain by endorsement of the warehouse certificate, however, it cannot demand the delivery of grain by the Silo until the full discharge of its obligations secured by the separated pledge warrant (see section 2 of article 40 of the Grain Law).

The holder of a pledge warrant is entitled to:

- 1) demand fulfillment of the obligation secured by the pledge warrant and payment of interest on such obligation, as indicated in the pledge warrant; and
- 2) transfer pledge warrant and associated rights to third parties by the way of endorsement (see section 3 of article 40 of the Grain Law).

TWO OPTIONS OF PLEDGE OF GRAIN

The law allows a **pledge of grain** to be perfected:

- 1) either by **endorsement** of the pledge warrant; OR
- 2) by executing of the **pledge of grain receipts** agreement (see section 15 of the Rules).

Once the pledge warrant is endorsed, it shall be separated from the warehouse certificate.

*We (GRATA) usually recommend our clients to use both options in one time, just to be on the safe side (i.e. endorse the pledge warrant and in addition to execute the pledge of grain receipts agreement). Our interpretation of the law also suggest that there is a third option – executing of **pledge of grain** agreement.*

RELIABILITY OF THE GRAIN RECEIPTS

Grain collection companies in Kazakhstan are obliged:

- 1) either to participate in the system for guarantee of obligations under grain receipts (i.e. in this case it shall conclude participation agreement with the so-called special fund for guarantee of grain receipt obligations (the “**Fund**”)), so that in case a silo cannot meet its obligations under the grain receipt (because of the loss or deterioration of the stored grain) the Fund pays in cash amount of not less than 80% market price of the grain which has been lost/deteriorated, for such silo (see article 16 of the Grain Law); OR
- 2) procure liability insurances in amount of not less than 80% market price of the grain which has been lost/deteriorated (see article 16 of the Grain Law).

Important Note: draft law as of March 2016 is in the Parliament that shall introduce electronic grain receipts (instead of paper grain receipts) and solve issue of unsupplied grain receipts.

Investment Preferences

In accordance with article 283 of the Commercial Code, local companies (i.e. it can be existing Kazakh company) that operate in eligible areas (including agribusiness) are entitled to the following benefits (on the basis of the so-called investment contract):

- 1) an exemption from customs duties on imported equipment and components, and raw materials required for investment projects (the exemption can be granted for up to five years) and an exemption from VAT for import;
- 2) state in-kind grants (land plots, buildings, equipment, machinery, etc.), which are granted for gratuitous use for the duration of the contract. Total amount of such state in-kind grant shall not exceed 30% of the total investment in fixed assets of such local company.

Projects in eligible areas (including agribusiness) with investment exceeding approximately USD 12.3 million are considered to be so-called “priority investment projects”. Newly created local companies that have entered into investment contracts relating to priority investment projects are entitled to the following benefits (in addition to those two listed above):

- 3) tax exemptions (corporate income tax - 0% for 10 years, land-tax-0% for 10 years, property tax-0% for 8 years);
- 4) an investment subsidy of compensation by the Government of up to 30% of the costs relating to construction, assembly and acquisition of equipment; and
- 5) stability of tax law and labor laws (see article 289 of the Commercial Code).



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