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10 QUESTIONS TO A LAWYER ABOUT SECURITY MEASURES

The civil legislation of Kazakhstan provides for various methods allowing to secure performance of obligations. The types of measures allowing to secure performance of obligations most commonly used in practice are pledge, guarantee and surety.

Below is general information in the form of 10 questions and answers relating to security measures.

- What are the methods of securing obligations?
- What is default interest?
- What types of pledge are stipulated by legislation?
- May a claim/property arising and coming in the future be pledged?
- What are the content and form of a pledge agreement?
- Does the right of pledge to the pledged property preserve when transferring the right (title) to the pledged property to another person?
- What are the distinctive features of the pledge of monetary funds coming to a bank account?
- When is it required to register pledge?
- What is the difference between guarantee and surety?
- What are the distinctive features of an earnest payment, retention, guarantee deposit and security payment?

1. What are the methods of securing obligations?

According to the Civil Code of Kazakhstan, performance of obligations may be secured by:

- default interest;
- pledge;
- retention of the debtor's property;
- surety;
- guarantee;
- earnest payment;
- guarantee deposit;

- security payment; and
- other methods stipulated by the Kazakhstan legislation or a contract.

2. What is default interest?

Default interest (fine, penalty) is an amount of money determined by legislation or a contract, which a debtor must pay to a creditor in case of a failure to perform or improper performance of obligations.

A default interest agreement must be made in writing, regardless of the form of the main obligation. Failure to comply with the written form entails nullity of the default interest agreement.

The law also grants the right to the creditor to claim for payment of the default interest determined by legislation (lawful default interest), regardless of whether an obligation to pay such was stipulated by agreement of the parties (contract). The amount of the lawful default interest may also be increased by agreement of the parties, unless this is prohibited by legislation. By default, the lawful default interest is calculated on the basis of the base rate of National Bank of Kazakhstan (*14.50% as of 3 June 2024*) on the date of performance of a monetary obligation or its relevant part. The lawful default interest for using someone's monetary funds is charged until the date of paying such money to a creditor.

The default interest amount is determined by a fixed amount of money or percentage of the amount of an outstanding or improperly performed obligation. If so requested by the debtor, the court may reduce the default interest in case the default interest to be paid is extremely high as compared with the losses of the creditor in light of degree of the obligation performance by the debtor and the interests of the debtor and the creditor.

3. What types of pledge are stipulated by legislation?

Any property, including things and property rights (claims) may serve as collateral, except for the things removed from circulation, claims inseparably associated with the debtor's identity, specifically, claims for alimony, compensation for harm caused to life or health, and other rights prohibited for assignment to other persons by legislative acts.

The Civil Code of Kazakhstan provides for the following types of pledge:

- mortgage – type of pledge, according to which the pledged property remains in possession and use of a pledger or a third party (*property to be mortgaged may be represented by enterprises, structures, buildings, constructions, apartments in an apartment house, transport vehicles, space objects, stock-in-trade, etc.*);
- possessory pledge – type of pledge, according to which the pledged property is transferred by the pledger into possession of the pledge holder;
- pledge of rights, for example, property rights, which may be alienated, specifically, rights to lease enterprises, structures, buildings, constructions, right to a share in the property of a business partnership, debt claims, copyright, and rights to inventions;
- pledge of securities; and

- pledge of monetary funds in case of complying with the conditions restricting the ability to use the pledged money by such person (transfer for storage to a bank safe, safe box, separate storage premises).

4. May a claim/property arising and coming in the future be pledged?

The law-maker provides for a possibility of establishing pledge over claims, which will arise in the future, and over property coming into ownership of economic management in the future, provided that the parties agree upon the amount of pledge securing such claims. In practice, such construction is complicated by the necessity to enter into a doble-stage agreement. Thus, the first agreement is entered into with respect to pledge of claims/property arising and coming in the future, while the second one is entered into for the coming assets (rights of claim), which must be registered to create the "first priority" claim for the pledged property.

5. What are the content and form of a pledge agreement?

A pledge agreement must contain information on collateral, substance, amount or maximum amount and term of performance of an obligation secured by pledge. A pledge agreement must be entered into in writing.

In case of pledge of immovable property and property deemed equal to it, an agreement must contain its evaluation. We do not exclude that other categories of assets may also require evaluation in light of certain legislative rules. Evaluation of the collateral must be expressed in tenge or be specified as an equivalent of a foreign currency (in case the secured obligation is in a foreign currency) in tenge at the market currency exchange rate as of the date of entering into the agreement. Movable property and/or separate categories of movable property (including mechanical equipment and inventory stock) serving as collateral may have common description of collateral without the requirement on specific description of the pledge security and without evaluation of collateral.

An agreement on pledge of movable property being pledged may have a common description of the property being pledged without the necessity to specify the amount of an obligation secured by pledge and specific description of the pledge security and without evaluation of the property being pledged.

The agreement must contain an indication to a party possessing the collateral and whether it is possible to use it. Failure to comply with these conditions entails nullity of the pledge agreement.

6. Does the right of pledge to the pledged property preserve when transferring the right (title) to the pledged property to another person?

According to the general rules of the civil legislation, in case of transfer of the right of ownership to the pledged property or the right of economic management from a pledger to another person as a result of fee-paid or free-of-charge alienation of such property or under the procedure for universal legal succession, the right of pledge remains in force.

Unless an agreement with a pledge holder provides for otherwise, a legal successor of the pledger falls into the place of the pledger and bears all obligations of the pledger.

7. What are the distinctive features of the pledge of monetary funds coming to a bank account?

The law-maker provides for the possibility of pledging monetary funds coming to a bank account of a pledger. The monetary funds pledge agreement (also spread as a bank account pledge agreement) is entered into in writing and provides a pledge holder with the right of pledge of funds coming to a bank account of a pledger. In practice, there may also be a bank account direct debiting agreement entered into according to a similar scenario, which gives the right to the creditor to conduct direct debiting (non-acceptance writing-off) of funds coming to a bank account of a borrower. Such pledge structures are more often used when securing major pledges (credit lines) extended by banks, financial organizations and institutions.

8. When is it required to register pledge?

Registration of pledge may be mandatory and voluntary, depending on the type of pledged obligations/assets (property). Subject to mandatory state registration is the pledge of immovable property. The types of pledge not subject to mandatory registration may be registered following the desire of the participants of the very security measure (pledge agreement). A registered pledge agreement allows filing the first priority claims of a creditor to a debtor in case of a failure to perform obligations or default. In case of a registered right, the creditor may count on satisfaction of its claims in accordance with the registered order of priority after satisfying the higher priority claims in accordance with the imperative rules of legislation (*debts for salary payments, social contributions, tax debts, etc.*).

9. What is the difference between guarantee and surety?

The key difference between guarantee and surety is in the scope of liability of a guarantor and a grantor to a creditor of a debtor.

According to a *guarantee*, a guarantor assumes an obligation to a creditor of another person (debtor) to be liable for the performance of obligations of such person in full or in part jointly and severally with the debtor. The persons that jointly gave a guarantee are jointly and severally liable to a creditor, unless otherwise established by a guarantee agreement. In other words, a creditor may apply to both debtor and the guarantor for the performance of obligations and with respect to both partially performed and non-performed obligations. A guarantee agreement may also be entered into to secure an obligation, which will arise in the future.

According to a *surety*, a grantor assumes an obligation to a creditor of another person (debtor) to be **vicariously** liable for the performance of an obligation of such person in full or in part. In case of vicarious liability, a creditor may apply for the performance of obligations to a debtor first, and then to a grantor with respect to an outstanding part.

10. What are the distinctive features of an earnest payment, retention, guarantee deposit and security payment?

Earnest payment is an amount of money given by one of the parties to a contemplated transaction on account of payments due from it to the other party and to secure execution and performance of the contract or performance of any other obligation. In case an obligation terminates prior to the moment a party started performing it by agreement of the parties or dues to a failure to perform occurring through no fault of the parties, an earnest payment must be returned. In case the obligation performance failure occurred because of the party giving the earnest payment, the earnest payment must remain with the other party or, if the other party is liable (which received the earnest payment), it must pay twice the amount of the earnest payment.

The distinctive feature of *retention* is that a thing is in possession of a creditor. Thus, in case of a debtor's failure to timely perform an obligation on payment for a thing or compensation to a creditor for the costs and other losses associated with such thing, the creditor holding the thing, which must be transferred to the debtor or a person to be designated by the debtor, may retain it until a relevant obligation is performed. According to the general rule, the creditor may also retain a thing in its possession regardless of the fact that such thing came into the creditor's possession after the rights to the thing were transferred to a third party.

A *guarantee deposit* is an amount of money transferred by a payer of the guarantee deposit to a guarantee deposit recipient to secure the performance of an obligation on execution of a contract in case of a tender or performance of any other obligation.

Security payment is a security of a payment obligation (including on compensation for losses or payment of default interest) in case of a contract violation in the form of transfer by one of the parties of a certain amount of money into ownership of the other party.

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